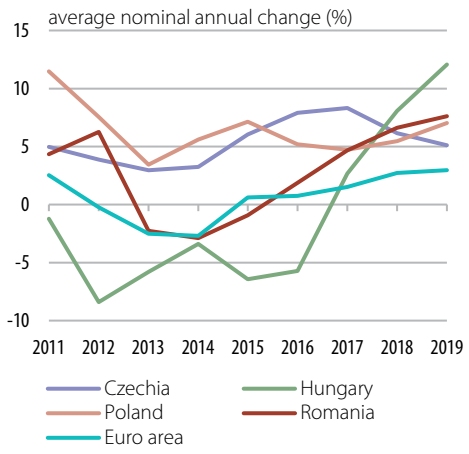
Box 9. Credit to the private sector and liquidity in the economy[1]



Source: NCBs

Chart A
Credit to the private sector

In 2019, the dynamics and composition of private sector credit – relevant from the perspective of monetary transmission, as well as of convergence with the particulars of the euro area and of countries in the region – had the following characteristics:

1. The growth rate of credit to the private sector remained in the vicinity of the record high for the past seven years reached at end-2018.

Against this background, the average dynamics of credit to the private sector climbed further in 2019, from 6.6 percent in 2018 to a 10-year peak of 7.6 percent – the second highest level in the region for the second consecutive year (Chart A)[2]. Beyond the influence of other factors, incidental ones included[3], these developments reflected the step-up in lending, especially in domestic currency[4], and particularly to non-financial corporations (Chart B), amid the stimulative effects exerted on credit demand and supply by: (i) the overall decline in lending rates on new business, resulting from their relatively steeper downward adjustment after the advance in the first months of the year (Chart C), (ii) the uptrend in confidence of both firms and consumers, (iii) the faster growth of households' disposable income, particularly on account of wage earnings[5], (iv) the consolidation of bank asset quality[6], and (v) the further decline in the loan-to-deposit ratio in the banking system, which reached 72.8 percent in December 2019, i.e. the lowest value in the past 14 years.

Opposite influences came from the persistence of structural weaknesses in the corporate sector[7], as well as from the relative tightening of credit standards on consumer and housing loans in 2019 Q1, partly attributable to the new prudential measures taken by the NBR[8], and of those applicable to corporate loans in the latter part of the year under review. To these added the risks and uncertainties generated

1 For a clearer picture, changes in dynamics were analysed, as a rule, in the form of indicators calculated as an average of annual growth rates expressed in nominal terms.

2 In real terms, the annual dynamics of private sector credit regained momentum versus 2018, for the first time in three years (to 3.6 percent from 1.9 percent, annual averages), and peaked at a 10-year high as well.

3 The weaker influence of credit institutions' NPL sales, as well as the statistical effect associated with two entities ceasing their activity at end-2017, which countered that of incorporating a new credit institution in the credit institutions' consolidated balance sheet in March 2018.

4 The average annual dynamics of the flow of leu-denominated credit, adjusted by the volume of renegotiated loans, climbed to 8.1 percent in 2019 from 5.2 percent a year earlier.

5 The average annual dynamics of the average net wage economy-wide picked up to a new post-crisis high of 15.0 percent in 2019 from 13.1 percent in the previous year.

6 The NPL ratio fell from 4.95 percent in December 2018 to 4.08 percent in December 2019.

7 The large share of firms with equity below the regulatory threshold, loose financial discipline, the features of the insolvency general framework.

8 NBR Regulation No. 6/2018 amending and supplementing NBR Regulation No. 17/2012 on certain lending conditions, which capped the level of indebtedness for households.

by the initial version of the tax on credit institutions' financial assets[9] introduced on 1 January 2019, but also by some legislative initiatives – in various stages of the legislative process – regarding the banking sector[10]. The moderation of price dynamics[11] and of the activity on the residential real estate market was probably relevant as well.

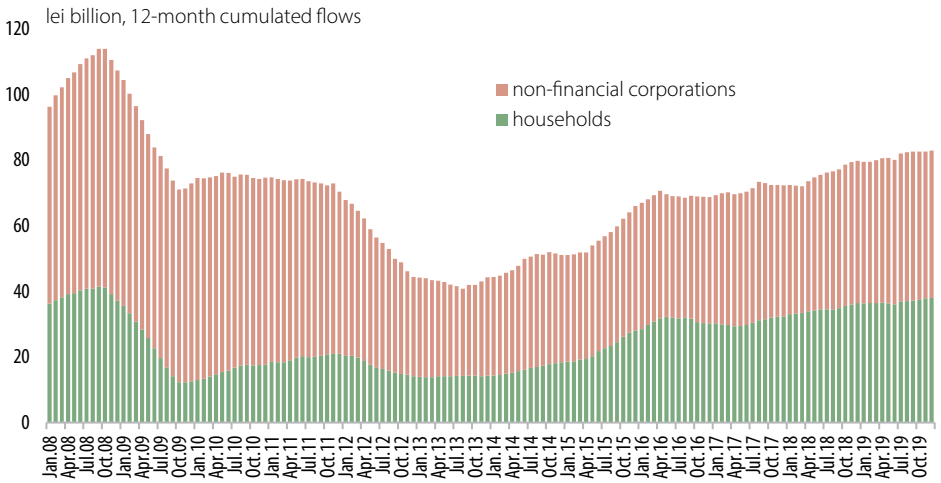


Chart B
New loans to households and non-financial corporations

The share of private sector credit in GDP continued to narrow slightly in 2019, to 25.2 percent, from 26.4 percent a year earlier, with decreases being also recorded in the economies in the region, except for Hungary, and in the euro area, after the previous years had seen mixed developments.

2. The share of the leu-denominated component in credit to the private sector continued to rise, reaching 67.6 percent[12] in December 2019 from 66.0 percent at end-2018.

Nevertheless, the share widened at a slower pace during the reported year as well, amid a renewed reduction in the positive spread between the robust, albeit decelerating increase in domestic currency credit[13] and the contraction in the foreign currency component. The latter moderated however to a much lower extent than in 2018 (to -1.1 percent at end-2019 from -1.4 percent in December 2018, based on stocks expressed in euro)[14], even though the dynamics of this component turned positive for a short while for the first time in seven years, on account of developments in credit to non-financial corporations, probably associated with foreign trade, but also with the interest rate differential.

9 The set-up of the tax, stipulated in GEO No. 114/2018, was then revised at end-Q1 (according to GEO No. 19/2019, approved by the Government on 29 March).

10 These legislative initiatives sought to: (i) cap interest rates on household loans, (ii) limit the amount that the transferee may collect from a debtor with a consumer status to double the price paid by the transferee to the transferor, (iii) remove the enforceability of loan contracts, and (iv) amend Law No. 77/2016 on debt discharge by defining the term "unforeseeability"; however, they were afterwards ruled as unconstitutional.

11 The average annual growth of house prices slowed to 3.4 percent in 2019 against 5.6 percent in the previous year.

12 A new post-1996 high.

13 9.3 percent in December 2019 versus 13.5 percent at the end of the prior year.

14 The statistical effect of the EUR/RON exchange rate acted, however, in the opposite direction.

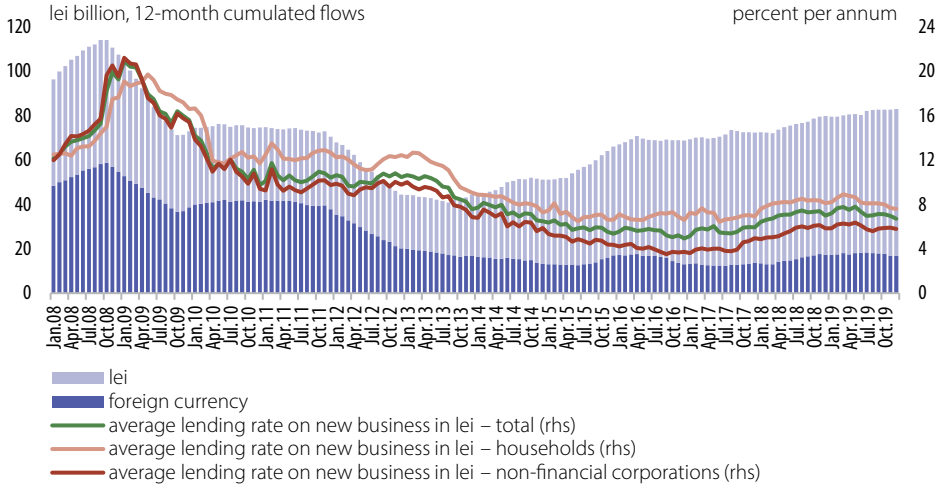


Chart C
New loans to the private sector and the average lending rate on new business in lei

In terms of flow as well, leu-denominated credit consolidated its majority share in total new credit to the private sector (79.6 percent during the year as a whole versus 78.3 percent in 2018) – Chart C, given the step-up in its growth rate alongside the marked decline in the dynamics of the foreign currency component[15]. At a sectoral level, the relative weight of leu-denominated credit continued to rise visibly for households, to a more than 17-year peak of 76.0 percent at end-2019 against 71.9 percent in December 2018[16], but diminished slightly for non-financial corporations (to 58.3 percent in December 2019 from 59.5 percent at the end of the previous year), thus seeing its uptrend manifest since 2012 come to a halt.

3. The share of household credit in total credit saw its increase come to a near-halt, staying around 53 percent, slightly above the euro area level, but trailing behind Czechia and especially Poland.

These developments occurred in a context in which the robust dynamics of household credit moderated slightly in 2019, for the first time in seven years (to 7.8 percent from 9.4 percent in 2018), while the growth rate of credit to non-financial corporations gained considerable traction and reached 7.0 percent (versus 3.3 percent in 2018), the highest reading for the 2013-2019 period. The step-up in corporate loans was due to a favourable statistical effect[17], but especially to the strong rebound in the dynamics of new loans in lei, overlapping the further swift, albeit decelerating, pace of increase of foreign currency loans. Looking at the breakdown by business sector, the most sizeable increase in the flow of credit was seen in agriculture, probably also on account of short-term secured loans. As for services and industry, growth rates were moderately positive, the two sectors further accounting however for more than 80 percent of the volume of new business to non-financial corporations; by contrast, the flow of loans to construction companies witnessed a contraction, after the previous year's

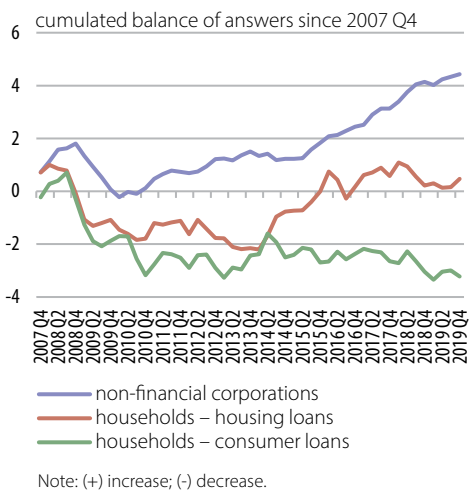
15 Nevertheless, the dynamics of the flow of foreign currency credit adjusted by the volume of renegotiated loans continued to exceed slightly those of the flow of leu-denominated credit.

16 As new business to households was further almost entirely accounted for by domestic currency loans.

17 Associated with the removal from the aggregate monetary balance sheet of two credit institutions that had ceased their activity in December 2017.

substantial rise, an evolution difficult to reconcile however with the strong pick-up in the activity of this sector during 2019.

Chart D
Demand for loans

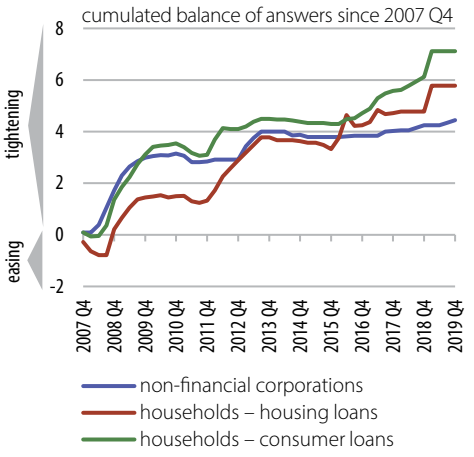


Note: (+) increase; (-) decrease.

The maturity breakdown of the stock of loans to non-financial corporations shows that the markedly stronger momentum came particularly from medium- and long-term credit, in correlation with the step-up in investment, whereas short-term credit – used for working capital financing – witnessed slower growth, especially in the latter part of the year. Looking at household credit, the moderation of the dynamics was ascribable to both major types of credit, i.e. consumer and housing loans respectively (see Section 4 below).

The successive issues of the NBR's *Bank Lending Survey* pointed, in fact, to non-financial corporations' further keener demand for loans, as well as to a relative steadiness in the demand for housing loans, accompanied by a rather fluctuating evolution of consumer credit, probably associated with changes in the relevant interest rates, which went up in the first months of the year, before posting a steeper downward adjustment (Chart D). Banks' credit standards on household loans witnessed a tightening in the first quarter (Chart E), probably amid the new prudential measures taken by the NBR[18], and afterwards were kept unchanged, while standards on loans to non-financial corporations were moderately tightened in the second part of the year.

4. The majority share of housing loans in total credit to households widened again only marginally (56.7 percent in December 2019).



Note: (+) increase; (-) decrease.

Chart E
Credit standards

The advance in housing loans stuck to two-digit readings in 2019, albeit moderating visibly (10.4 percent from 12.8 percent in the previous year), on account of the slower growth of the leu-denominated component. This remained however particularly brisk (20.5 percent versus 30.9 percent in 2018), amid the further sizeable increase in new business without state guarantees, on one hand, and the renewed contraction in the flow of loans extended under the "First Home" programme[19], on the other hand.

Leu-denominated housing loans thus saw their large share in total household credit widen again (to 40.6 percent in December 2019 against 36.6 percent at the end of the previous year) and came to account for 71.6 percent of total credit for this purpose (66.3 percent in December 2018).

[18] NBR Regulation No. 6/2018 amending and supplementing NBR Regulation No. 17/2012 on certain lending conditions, which capped the level of indebtedness for households.

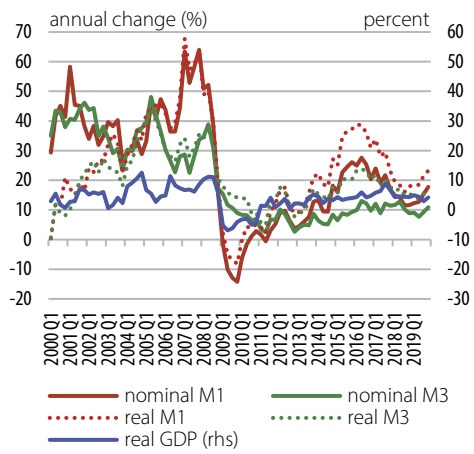
[19] In a context in which the guarantee ceiling earmarked for this programme was however kept at lei 2 billion. The assessments are based on CCR data referring to loans granted with state guarantee associated with the "First Home" programme.

Running at much lower levels, the annual rate of change of consumer credit and other loans witnessed, by contrast, only a minor decline (to 4.6 percent from 5.5 percent in 2018), despite an unfavourable statistical effect[20], as new business in domestic currency hit new historical highs in terms of both annual average and monthly values. This was supported by the faster dynamics of disposable income, especially on the back of wage earnings, as well as by the overall decrease in related interest rates, also ascribable to the keen competition on this segment of the banking market.

Looking at other countries in the region and at the euro area, in 2019 the share of housing loans in total credit to households in Romania equalled that in Poland and exceeded more visibly that in Hungary, while remaining well below those in Czechia and the euro area.

As for liquidity in the economy, the most important developments were:

1. The relatively constant degree of monetisation of the economy for the third consecutive year.



Source: NIS, NBR

Chart F
Broad money and GDP

The pace of increase of broad money (M3) was, however, brisk in 2019, returning in December to double-digit readings, i.e. 10.9 percent, implicitly above the value recorded at the end of the previous year, amid the considerable easing of the budget execution and the higher dynamics of EU fund inflows. The average annual dynamics of broad money also remained robust, although moderating slightly[21] – to 9.3 percent from 11.2 percent in 2018 (Chart F).

From the perspective of M3 counterparts (Chart G), monetary expansion was mainly prompted, for the second consecutive year, by credit to the private sector and – only to a slightly lesser extent – by net foreign assets of the banking system, whose contribution rose substantially after the previous year's marked decline. Net credit to central government also continued to act as a source of money creation in 2019, albeit of a much lower magnitude, including against the prior year, given a much more visible weakening of the expansionary effects exerted by central government deposits compared with the strengthening of those stemming from the increase in credit institutions' government security investments. Conversely, an unusually strong contractionary impact came from the significant step-up in the rate of change of long-term financial liabilities, mainly on the back of capital accounts[22].

20 Associated with the inclusion of a new credit institution in the aggregate monetary balance sheet in March 2018.

21 In real terms, the annual M3 dynamics declined at a considerably slower pace (5.2 percent versus 6.3 percent in 2018, as annual averages).

22 Their marked increase was associated with the application, starting 1 January 2019, of the maximum value of the capital conservation buffer (2.5 percent of the total risk exposure amount, as against 1.875 percent in the previous year), following the end of the transition period for its implementation.

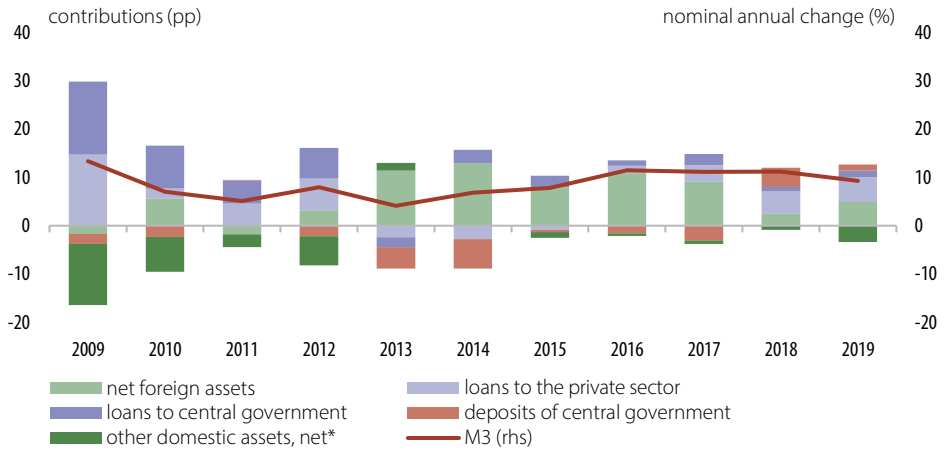


Chart G
M3 and its counterparts

*) long-term financial liabilities, capital accounts, other assets and other liabilities

2. The faster growth of the majority share held by narrow money (M1) in M3, which widened to 65.5 percent in December 2019 from 61.7 percent at end-2018 – Chart H.

While the share of M1 in M3 increased in most countries in the region (except for Czechia), it saw a more pronounced rise in Romania, hitting a record high for more than 25 years and thus almost bridging the M3 structural gap vis-à-vis the euro area. This was due to the renewed growth in the divergence between the rising dynamics of the M1 monetary aggregate and the decelerating rate of change of time deposits with a maturity of up to two years, which re-entered negative territory at year-end.

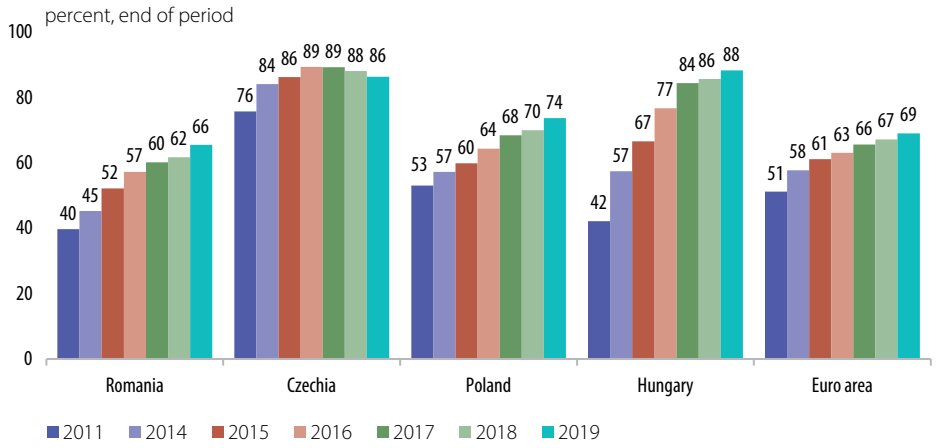


Chart H
Share of M1 in M3, international comparison

Source: NCBs

Amid relatively steady dynamics of currency in circulation, the sizeable added momentum of the most liquid M3 component came from the renewed step-up in the growth of ON deposits from non-financial corporations, along with the further

particularly brisk pace of increase of similar household deposits[23]. The evolutions reflected the keener demand for money for current transactions, in correlation with the solid growth of the economy and of private consumption, as well as with the considerably faster increase in household income, largely on account of wage-related income, amid the more strongly procyclical fiscal and income policy stance.

At the same time, the rate of increase of time deposits with a maturity of up to two years decelerated further, owing largely to developments in household deposits, but also to the protracted decline in the dynamics of non-financial corporations' deposits, associated *inter alia* with additional dividend payments by state-owned enterprises.

Against this backdrop, the share of ON deposits in M3 peaked at a post-April 1994 high of 48.0 percent in December 2019, while the relative weight of currency in circulation posted again a slight downward correction (17.5 percent at end-2019).

3. Protraction of the generally upward trend of the share of household deposits in total non-banking sector deposits (60.5 percent in December 2019 versus 60.3 percent at end-2018).

This was attributable to the further pick-up in the dynamics of households' bank deposits, to an annual average of 11.6 percent (from 10.9 percent in 2018), in correlation with the faster increase in disposable income.

The growth rate of non-financial corporations' deposits slowed, however, significantly (to 7.3 percent against 10.0 percent in the previous year), thus trailing – for the second consecutive year, this time more visibly – behind that of household deposits, probably under the influence of dividend payments to the public sector, as well as of the rising dynamics of wage costs.

[23] The share of non-financial corporations' ON deposits in M3 thus posted a new record high since 1993, while those from households reached a new historical peak.