PIRAEUS BANK

SEE Economic Review

ECONOMIC ANALYSIS & MARKETS DIVISION

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Executive Summary: **Macroeconomic Balance Index Redux**

Our readers will surely remember the Macroeconomic Balance Index (MBI) that we publish every year immediately following our annual forecast round. The aim of this index was, and still is, to provide a concise and comprehensive assessment of the imbalances (both internal and external) of each economy in our sample and, based on these imbalances, to provide a macroeconomic scorecard. In doing so, we are fully aware of the limitations of our approach. However, we are confident that our results provide an interesting and informative assessment of the macroeconomic situation in each of the economies we follow.

In its original format (first published in the March 2010 issue of this Review), the MBI was calculated using 4 variables. GDP growth was used as the cornerstone variable that reflected the increase in the overall output of each economy; the fiscal deficit and inflation rate were included as indicators of internal imbalances, while the current account deficit was our external imbalances indicator. The main criterion for the selection of these variables was simplicity and ease of computation. Nevertheless, when we revisited the issue of calculating the MBI this year, we had to admit that our index looked incomplete. Based on the experience we have accumulated in recent years, we have decided to augment our MBI with a number of additional macro-variables, so as to provide a more complete picture of the relative strengths and weaknesses of each economy. As a result, our revamped MBI is based on GDP growth, public debt and deficit, inflation, current account balance, private sector loans and deposits growth, unemployment and Real Effective Exchange Rate (REER) changes.

In order to provide some historical perspective for the new index, we provide estimates of the index from 2008 onwards. When calculating the index for the years up to 2011, we use historical values for the underlying components. For 2012, we follow a more forward-looking approach and employ our forecasts for these variables.

Based on these forecasts, our estimates for the 2012 MBI provide a bifurcated picture: Bulgaria and Romania clearly stand out as the best performers with virtually no difference between them. Similarly, in the runners-up group, Albania, Cyprus and Serbia have roughly equal scores.

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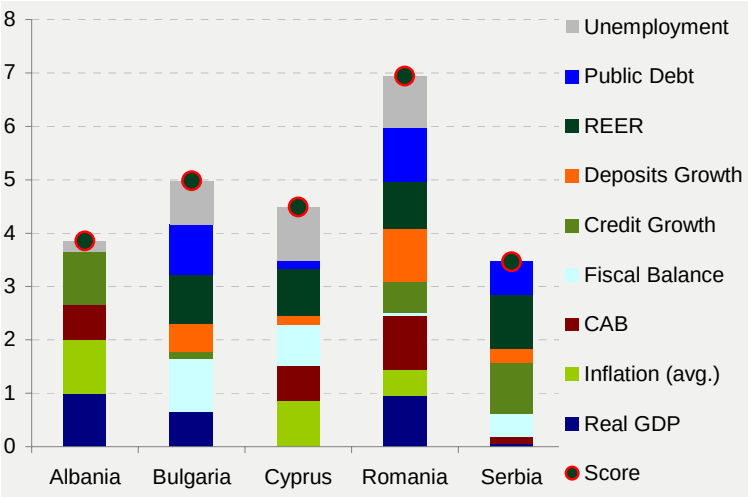
1. Macroeconomic Balance Index

Following our forecasts for 2012, presented in the previous SEE Economic Review, we have attempted to produce a unified score for each of the five SEE countries that we analyze. In doing this, we recognize that there are many limitations to the methodology we are employing; however, we are confident that our results paint an interesting and informative picture of the macroeconomic situation in all of the countries studied.

This attempt would be incomplete without a historical perspective. It is essential to include in this perspective each year since 2008, when the effects of the financial crisis began to manifest themselves throughout Southeastern Europe. Since 2009, plummeting credit growth rates and increasing fiscal imbalances have characterized the region and, therefore, we feel that the inclusion of data from 2008 to 2011 provides our analysis with the necessary perspective to complete this exercise. For 2012, we have used our projections to create a forward-looking assessment of the five countries, which, of course, is highly dependent on the uncertainties surrounding the entire European continent and especially the eurozone.

Starting with 2008, in Chart I we can observe the relative rankings of the five countries in the final year of a period of relatively high growth rates, coupled with current account imbalances and a mixed fiscal situation. Credit was growing at very high rates, and inflation was high in Bulgaria and Serbia and lower in the other three countries. Romania appears to be the outlier among the countries with an exceptionally high score (in fact, the second highest of all the countries over the whole five-year period studied) as it scores very highly on all the variables except one: fiscal balance (a clear sign of things to come).

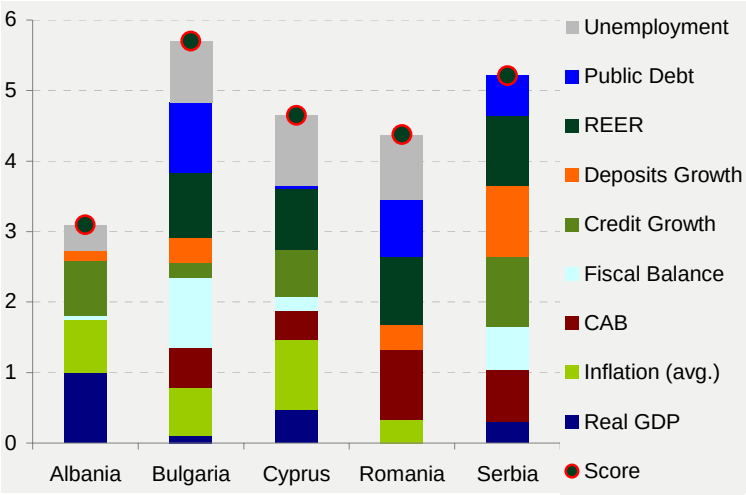
Chart I: Macroeconomic Balance Index - 2008



Source: Piraeus Bank Research

In 2009 (Chart II), at the height of the financial crisis, the figures suddenly exhibit dramatic swings. Real GDP growth turns negative everywhere but in Albania, fiscal balances deteriorate, unemployment increases and, of course, credit growth rates are substantially reduced. This new macroeconomic environment is worse for all the countries studied. However, given the cross-sectional rather than longitudinal nature of this study, we can only comment on the relative changes in rank from 2008 to 2009. In that respect, changes were quite evident in 2009 as the former front-runner (Romania) is now second from last, while Serbia has jumped to second place. Bulgaria, the country that exhibited the most stable behaviour throughout the years studied, captures first place, with high scores in almost all the variables with the notable exception of GDP growth. Serbia's change in the rankings is mainly a product of the significant changes in its current account balance and its deposits' growth rate.

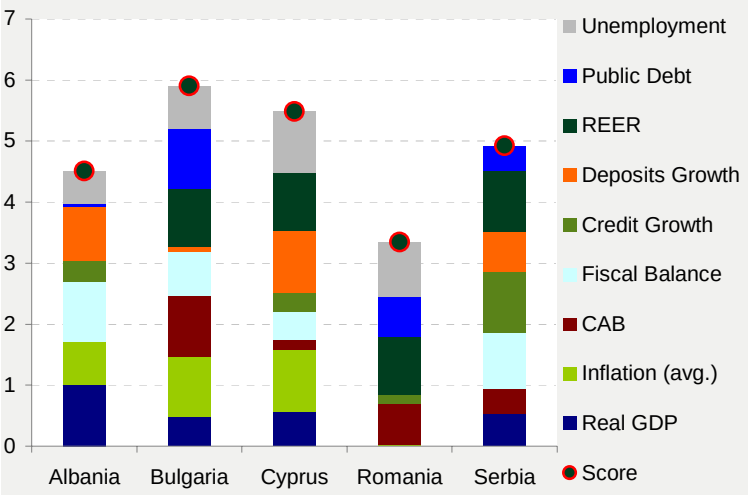
Chart II: Macroeconomic Balance Index - 2009



Source: Piraeus Bank Research

In 2010 (Chart III), the effects of the 2008 – 2009 financial crisis continued to be felt throughout the region. However, a lot of the indicators studied showed significant improvements in several of the five countries. Bulgaria exhibited the strongest performance and the other countries moved by no more than one position at the most. Bulgaria's stellar performance was mainly a result of its fiscal variables, where a prudent fiscal policy went a long way towards counterbalancing many of the effects of the crisis.

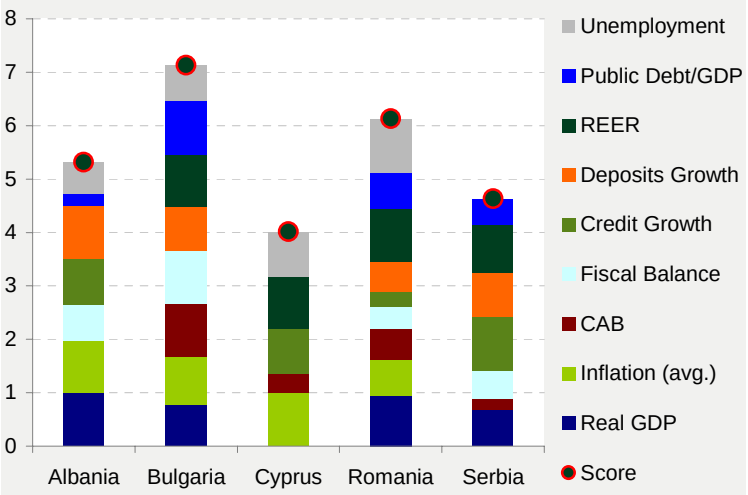
Chart III: Macroeconomic Balance Index - 2010



Source: Piraeus Bank Research

The eurozone crisis is in full swing by 2011, and the picture that emerges is clear as we observe in Chart IV. Bulgaria, other than its very low credit growth, exhibits an above-average performance in all the variables studied and thus scores very highly (the highest score for any of the countries over the whole five-year period studied). Romania, in the wake of its painful adjustment during 2010, is now on the road to recovery and its relative rankings have improved in almost all the variables. Cyprus, on the other hand, has a surprisingly low score, being more affected by the eurozone crisis (as it is the only one of the five countries that is a eurozone member) and by the explosion in the power plant at Vassillikos. Albania has climbed to third place and is now rather close to Romania, exhibiting a benign inflation picture and solid credit and deposits growth. Finally, Serbia has a mixed performance with both high inflation and a high current account deficit, while results are better for the other variables.

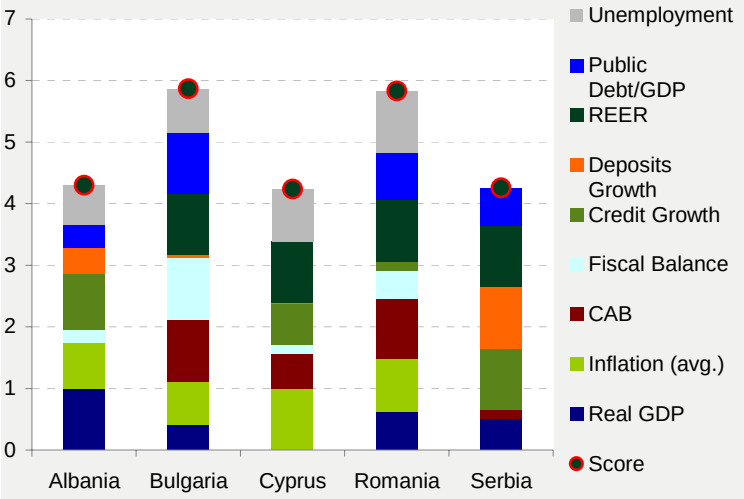
Chart IV: Macroeconomic Balance Index - 2011



Source: Piraeus Bank Research

Our outlook for 2012 has not changed since our last forecasts were made at the beginning of the year. Using certain IMF forecasts and our own calculations, we have arrived at a set of numbers that we feel accurately convey our current view on the countries studied. The picture that emerges follows the trends observed (Chart V), especially during the 2010 – 2011 period, but shows a distinct grouping of the five countries into two groups. The clear leaders, with minimal differences between them are Bulgaria and Romania.

Chart V: Macroeconomic Balance Index - 2012



Source: Piraeus Bank Research

Bulgaria's solid fiscal performance in previous years is expected to continue in 2012, with a very low fiscal deficit and the lowest public debt of the five countries. Its current account balance, while, we believe, becoming negative again in 2012, will still be the best of the countries studied. Its relatively low credit and deposits growth are the only variables where Bulgaria's ranking is well below average. Our prediction of a slowdown in GDP growth is also a factor that makes Bulgaria's overall score lower than it was for 2011, while still maintaining first place in our rankings.

Romania's resurgence in 2011 will continue in 2012. Although both Romania's and Bulgaria's scores have decreased since 2011, they remain the clear leaders in the field. We expect a slight improvement in Romania's ranking in terms of fiscal finances and a much greater positive change in the rankings related to inflation and current account balance. The unemployment situation is expected to remain stable (lowest unemployment of the five countries) while credit and deposits are expected to grow at rather low rates.

Albania is ranked third, and although its score has declined by one point since 2011, we still feel that there is much promise in the economic fundamentals of the country. Growth is expected to continue in 2012 (and, in fact, to be the strongest of the five countries' growth) and public debt will remain below the 60% threshold. We see the unemployment situation improving during 2012 while the other structural imbalances (current account,

fiscal) will still be present.

Serbia is a close fourth, as its scores have changed very little since 2011. Specifically, small improvements in some variables (public debt, deposits growth) are counterbalanced by negative moves in others (GDP growth, current account balance and fiscal balance).

Cyprus has seen its fortunes change dramatically between 2010 and 2011. We do not expect any major shifts in its relative ranking for 2012, leaving it in last place. Positive developments are expected in both fiscal and current account balances both in absolute numbers and relative to the other four countries. In all the other variables, however, Cyprus' scores are almost identical to those of 2011, and therefore these small improvements do not translate to a change in the rankings.

Table 1: Macroeconomic Balance Index Total Scores

	2008	2009	2010	2011	2012
Albania	3.9	3.1	4.5	5.3	4.3
Bulgaria	5.0	5.7	5.9	7.1	5.9
Cyprus	4.5	4.6	5.5	4.0	4.2
Romania	6.9	4.4	3.4	6.1	5.8
Serbia	3.5	5.2	4.9	4.6	4.3

Source: Piraeus Bank Research

Conclusion

It is never easy to rank countries, even those in the same region, with such different economic characteristics. The geography, population, industrial and political history of the five countries we are covering are very different, and an all-encompassing index risks neglecting these differences to arrive at a single score. This is, however, an issue with most rankings of this type, and we felt that we should not have shied away from the task.

We feel that some interesting conclusions can be drawn from this comparative analysis. Looking at the changes in rankings from year to year, it is obvious that imbalances in certain areas, and especially in fiscal and current account balances, inevitably affect all of the other variables and lead to a deterioration in a country's score.

Moreover, although a ranking could include a multitude of variables, we feel that the variables chosen present a balanced macroeconomic picture that is useful for any further analysis. In this turbulent period, the inclusion of current account, fiscal, growth, banking, consumer prices, real effective exchange rates and unemployment data offers an opportunity to assess various economic forces that shape the environment of each country. We estimate that a proliferation of indicators would only serve to increase the correlations among them and not the richness of the analysis.

Appendix

The scores for each country were calculated using nine indicators. Specifically, the indicators used were:

1. Real GDP growth, y-o-y %
2. Inflation (average)
3. Current Account Balance, % of GDP
4. Fiscal Balance, % of GDP
5. Credit growth
6. Deposits growth
7. Real Effective Exchange Rate
8. Public Debt, % of GDP
9. Unemployment Rate

The data for each country were collected from national sources and the International Monetary Fund. For 2012, we used our own projections, as well as those of the International Monetary Fund. Since the indicators varied widely in the range of values that were observed, all the data were normalized so that a uniform picture could be obtained. Based on the normalized figures, the difference between each figure and the minimum observed for the year was divided by the difference between the minimum and the maximum figures for that particular indicator in that year. That resulted in a score between 0 and 1 for every country in every variable. In the case of variables where a high figure represents a negative development for an economy, the scores were subtracted from 1 giving the highest score to the country with the lowest value.

Scores were added up for each country in each year and the charts presented in the text were created. Although the possible scores range from 0 to 9, we can observe that 3.1 (Albania, 2009) was the lowest score given and 7.1 (Bulgaria, 2011) was the highest. All of the other scores fell within that range 4-point range and in some cases, e.g. for 2012, we observed very similar scores within certain groups of countries.

2. Table of Forecasts

Table of Economic Forecasts								
	Real GDP (% YoY)		Inflation		Fiscal Balance (% GDP)		Current Account Balance (% GDP)	
	2011	2012	2011	2012	2011	2012	2011	2012
Albania	3.1	2.7	3.5	3.2	-2.8	-3.7	-12.0	-9.7
Bulgaria	2.1	0.7	4.2	3.3	-2.1	-1.3	0.9	-1.5
Cyprus	0.5	-0.7	3.3	2.4	-6.0	-4.0	-7.2	-5.0
Romania	2.1	1.4	5.8	2.8	-4.1	-3.0	-4.2	-1.7
Serbia	1.6	1.0	11.2	5.4	-3.9	-4.4	-8.9	-8.5

Source: Piraeus Bank Research

3. Conjunctural Analysis

3.1 Albania

Albanian economy remains weak- although there was a pick up in economic activity in 2011Q3

The Albanian economy remains weak, although there was a significant pick up in economic activity in 2011Q4. The annual growth of real GDP in 2011Q4 accelerated to 3.8% from a revised 2.8% in 2011Q3 although this was lower than the corresponding quarter in 2010 where growth stood at 5.5%. This unexpected rise is mainly due to an acceleration in the transfers sector and a return to growth in the construction sector. Specifically, the transport sector increased by 15.4% YoY in 2011Q4 from 19.5% in 2011Q3 and 30.1% in the same quarter in 2010. The construction sector returned to growth in 2011Q4, recording an increase of 1.2% YoY after contracting by 0.8% in 2011Q3 and by 9.4% in the corresponding quarter in the previous year. The industrial sector - the main growth driver of real GDP in the last year – contracted in 2011Q4 from a one-off recovery noted in the previous quarter to 8.9% YoY and from an increase by 22.8% over the same period last year. The agricultural sector showed signs of a marginal slowdown as in 2011Q4 it increased by 1,9% YoY compared to 2,8% in 2011Q3 and 2,3% in the corresponding quarter in 2010. In quarterly terms, real GDP (seasonally adjusted) increased by 0.1% in 2011Q4 from 2.4% in the previous quarter, while in annual terms economic activity in 2011 accelerated to 3.1% YoY from 3.3% in 2010.

Moderation in aggregate demand and private consumption is expected

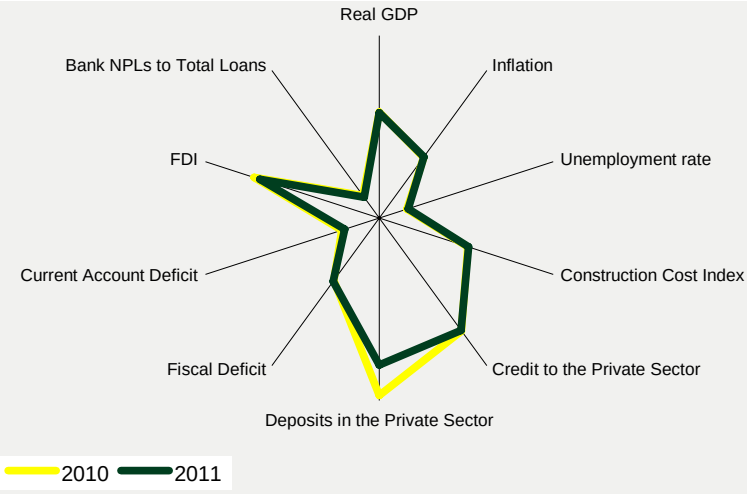
Based on the available leading economic indicators, we note that retail sales in 2011Q4 contracted for yet another quarter by 5.6% YoY from 6.9% in 2011Q2, while all sub-indices show signs of moderation, signalling a decrease in aggregate demand and private consumption. In the labour market, in 2011, the unemployment rate fell marginally to 13.3% from 13.7% in 2010 as economic activity picked up in the last quarter, while the construction cost index in 2011 increased marginally to 0.5% YoY from 0.3% in 2010. The Economic Sentiment Indicator in the final quarter of 2011 subsided to 83.5 from 91.4 in the previous quarter due to a moderation in the construction and services confidence indices, while it is worth noting that the consumers' confidence index in 2011Q4 increased and thus contributed positively to the general index. The economic sentiment index is, however, well bellow the level of 100 that separates positive and negative future expectations, signalling that consumers and businesses expect a deterioration in economic activity.

Inflationary pressures have been eliminated in the last three months

Inflation has been following a downward trend since the first half of last year, as inflationary pressures originating from the supply side have significantly moderated. Specifically, in 2011, the rate of inflation decreased marginally to 3.5% from 3.6% in 2010 as rises in food prices have remained at low levels:

4.7% YoY from 4.8% over the same period. It is noteworthy that inflationary pressures have been basically eliminated in the last three months, as in February inflation reached an all-time low of 0.6% from 1.6% in January and 4.5% for the corresponding month the previous year mainly due to a continuing negative output gap. Food prices in February contracted for the first time since August 2007 by 1.2% YoY from an increase of 1.4% in January and 6.9% in the same month in 2010. In monthly terms, the consumer price index increased by 1.3% in February from 0.7% in the previous month, while food prices increased at a faster rate in February of 2.2% YoY from 1.4% in January. Following the downward trend of inflationary pressures and the expectation of a more prudent fiscal policy, the Central Bank of Albania (CBA) has decided to cut the key interest rate to the historic low of 4.25% in its March monetary policy meeting after a cut by 25bp in January, as it estimated the current level of the key interest rate provides the appropriate conditions to fuel economic activity.

Albania – Economic Indicators (closer to centre=deterioration)



Source: Piraeus Bank Research, National Sources

Fiscal deficit in 2011 moderated

The opposition's boycott of parliament and related political polarization has come to an end, raising expectations that the reforms needed to converge towards the EU prerequisites and to improve economic growth and fiscal prudence will be implemented. This political polarization, however, has led to the rejection of the country's EU candidacy member status by the EU. Further, according to preliminary data from the Ministry of Finance, the 2011 budget deficit amounted to 2.8% of the expected annual GDP compared to 3.1% in 2010. Budget revenues are estimated to have increased by 5.3% YoY in 2011 covering approximately 96.3% of the total, while public expenditure increased by 3.6% YoY covering 96.2% of the year's target. Nevertheless, the main challenges the government has to face remain the ratio of interest payments to revenues and government debt

relative to the size of the economy.

Current account deficit marginally widened in 2011

In the external sector, the current account deficit marginally widened to 12.0% of the expected annual GDP in 2011 from 11.4% in 2010, due to a worsening of the trade deficit. Specifically, the deficit in the trade balance increased to 23.5% of GDP in 2011 from 23.2% in the previous year. Further, we observe moderation in most of the balance of payments' sectors, as the services surplus in 2011 was 1.4% of GDP from 2.5% in 2010 and the transfers' surplus decreasesd to 9.8% from 10.3% over the same period. However, in 2011, the income balance was a surplus of 0.3% of GDP after a deficit of 1.0% for the previous year, while the current account deficit has been relatively well financed by net FDIs in 2011. Net FDIs decreased to 3.5% of GDP in the last year from 4.3% in 2010.

Local financial system is stable - while liquidity is improving amidst the cut in interest rates

In the banking sector, total credit in the private sector in 2011 was 10.4% YoY from 10.6% in 2010, as firms' lending accelerated to 15.4% YoY compared to 14.7% over the same period, while household loans in 2011 contracted by 0.2% YoY from a growth of 1.5% the previous year. Growth of total deposits in the private sector slowed-down in 2011 to 12.2% YoY from 18.8% in 2010. Further, the local financial system is stable, while liquidity is improving amidst the cut in interest rates. NPLs (substandard, doubtful and loss loans) ratio increased in 2011Q4 to 18.94% from 18.03% in 2011Q3 and 13.6% in the same quarter of the previous year, while provisions deteriorated accordingly to 10.8% in 2011Q4 from 8.2% in 2010Q4.

Albania Economic Indicators

	2009	2010	2011	Q1 2011	Q2 2011	Q3 2011	Q4 2011
			% YoY				
GDP	3.6	3.3	3.1	4.8	1.1	2.8	3.8
Inflation	2.3	3.6	3.5	4.0	4.1	3.2	2.5
Unemployment rate	13.0	13.7	13.3	13.5	13.3	13.3	13.3
Construction Cost Index	0.0	0.3	0.5	0.5	0.2	0.5	0.7
Credit to the Private Sector	11.7	10.6	10.4	11.5	11.6	14.0	10.4
Deposits in the Private Sector	6.8	18.8	12.2	15.8	16.7	14.0	12.2
EUR/ALL Spot Rate	123.7	137.9	138.6	138.6	140.7	141.4	140.6
			% of GDP				
Fiscal Balance	-0.1	-3.1	-2.8	-0.9	-2.0	-2.4	-2.8
Current Account Balance	-15.2	-11.4	-12.0	-2.3	-5.8	-8.5	-12.0
FDI	7.8	8.8	7.5	0.8	3.1	4.7	7.5

Albania Banking Indicators

	2006	2007	2008	2009	2010	2011
Bank NPLs to Total Loans	3.1	3.4	6.6	10.5	13.9	14.4
Bank Provisions to NPLs	56.3	47.2	42.8	51.3	52.7	56.8
Return on Assets	1.4	1.6	0.9	0.4	0.7	0.3
Return on Equity	20.2	20.7	11.4	4.6	7.6	2.9
Financial Leverage	14.4	12.9	12.7	11.5	10.9	9.7
Bank Capital to Assets (%)	6.8	7.6	8.6	9.6	8.5	9.1
Bank Regulatory Capital to Risk-Weighted Assets (%)	18.1	17.1	17.2	16.2	15.4	14.8

Source: Piraeus Bank Research, National Sources, IMF

3.2 Bulgaria

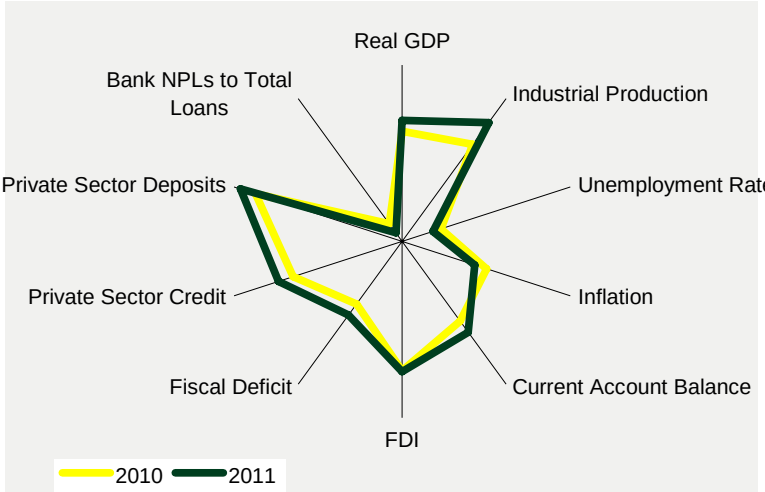
Growth remains resilient as opposed to the EU trends

Economic recovery in 2011Q4 has slowed to a standstill, though growth remains resilient unlike in most European countries. Real GDP (seasonally adjusted) in 2011Q4 slowed down to 1.6% YoY, remaining flat compared to the growth in the previous quarter and from 3.9% in 2010Q4. Exports were the main growth driver in 2011Q4 as net exports increased by 8.1% YoY after contracting by 3.6% in 2011Q3 and increasing by 4.3% in the same quarter last year. A drop in investments was observed – for the eleventh consecutive quarter - of 9.7% YoY in 2011Q4 from 7.4% YoY in 2011Q3 and 6.5% in 2010Q4, while final consumption remained at low levels: 0.5% from 0.9% and 1.8% over the same period. In quarterly terms, real GDP in 2011Q4 increased by 0.3% from 0.2% in the previous quarter, while for the year real GDP accelerated to 2.1% YoY in 2011 from 0.6% in 2010.

Consumers are very cautious in terms of household spending

Industrial production in 2011 increased by 5.8% YoY from 2.0% in 2010, while manufacturing production rose by 2.5% YoY from 3.9% over the same period. At the consumer front, retail trade continued to contract over the last year by 1.4% YoY from 1.8% in 2010, as consumers have been very cautious in terms of household spending due to the uncertainty over the debt crisis in the Euro-area. We must note however that there is a firm medium-term growth prospect, assuming that the absorption of the EU funds will improve in the future, while we do not expect the delay in the decision on the country's entry to the Schengen treaty to affect investor confidence.

Bulgaria – Economic Indicators (closer to centre=deterioration)



Source: Piraeus Bank Research National Sources

Inflation in 2011 accelerated due to an increase in domestic demand and low base effect

Inflation in 2011 accelerated to 4.2% from 2.4% in 2010, mainly due to an increase in domestic demand, a low base effect from the previous year and a rise in food prices. Specifically, food prices increased by 6.9% YoY in 2011 compared to a decrease of 0.4% in 2010. However, inflationary pressures in the last 8 months remain limited as international food and commodity prices continue to decrease. Inflation in February increased at a slower rate of 2.0% from 2.3% in January and 5.2% in January 2010, while food prices increased by 1.7% YoY from 0.3% and 4.0% over the same period. In monthly terms, the consumer price index increased by 0.9% in February from 0.2% in January. Further, on the supply side, the producer price index increased to 8.6% YoY in 2011 from 7.2% in 2010 signalling that the pass-through effect in inflation will lead to a future deceleration.

Fiscal deficit in 2011 was significantly corrected

The country's strong track record of fiscal consolidation in 2011 led to an impressive correction in the fiscal deficit since the 2008 financial crisis, which at the same time moves the country out of the EU's excessive deficit procedure. The fiscal deficit in 2011 decreased to 2.1% of the expected annual GDP, compared to 3.9% in 2010, as public expenditure slowed down to 34.9% of GDP in 2011 from 36.9% the previous year. The government has committed to a further budget consolidation by freezing wages, reforming the pension system, and increasing the retirement age and extending the working period in the current year. Total revenues in 2011 remained almost flat at 33.8% of GDP in 2011 from 33.9% in 2010, while in 2011 there was a better absorption of EU funds at 1.0% of GDP, compared to 0.9% in the previous year. The fiscal deficit in the first month of the current year shows signs of improvement as it reached 0.4% of GDP compared to 0.6% in January 2011 due to an increase in total revenues. Further, the fiscal reserve account in the central bank in 2011 contracted by 16.9% YoY from 21.6% in 2010.

Current account balance remained in 2011 on a surplus –as most of the year

In 2011, the current account balance remained in surplus –for most of the year - feeding from the low aggregate demand and private consumption in the country. Specifically, the current account surplus reached 0.9% of the expected annual GDP from a deficit of 1.0% in 2010, as the trade deficit shrank to 5.1% of GDP from 7.7% over the same period. Further, the current transfers' surplus increased to 4.4% of GDP in 2011 from 4.2% in the previous year, while the services balance remained flat over the same period. Further, we must emphasize the improvement in the net FDI's after a period of an almost trivial performance in 2010 and the first half of 2011. Net FDI's reached 3.1% of GDP in 2011 from 2.9% in 2010, hence financing comfortably the current account balance. This improvement represents an increase in investor confidence. Moreover, the currency board remains adequately supported as foreign exchange reserves in December covered 109.5% of the country's short-term debt.

The local banking system preserves the appropriate liquidity

The local banking system remains well-capitalized and it also preserves the appropriate liquidity to weather the storm. Although, the deleveraging of parent-banks, mainly in Greece, continues, the Bulgarian subsidiaries are adequately supervised. Lending in the private sector increased by 3.4% YoY in 2011 from 1.2% in 2010, while credit in non-financial corporations increased by 5.7% YoY from 2.4% over the same period. Lending to households continued to contract in 2011, by 0.8% YoY which is the same rate as in 2010, while private sector deposits increased at a faster rate by 9.0% YoY from 6.8% over the same period.

Bulgaria Economic Indicators

	2009	2010	2011	Q1 2011	Q2 2011	Q3 2011	Q4 2011
		% YoY					
GDP (sa)	-5.6	0.6	2.1	3.2	2.2	1.6	1.6
Final Consumption	-7.7	0.4	0.6	0.6	0.4	0.9	0.5
Investment	-15.2	-19.9	-7.4	-5.5	-6.9	-7.4	-9.7
Exports of G&S	-11.1	14.7	12.8	21.5	13.2	5.4	12.6
Imports of G&S	-21.0	2.2	8.7	13.6	8.1	9.0	4.5
Industrial Production	-18.3	2.0	5.8	12.0	7.1	3.9	1.3
Unemployment Rate	9.1	9.2	10.4	10.7	9.7	9.4	10.4
Inflation	2.8	2.4	4.2	5.1	4.8	3.9	3.1
		% of GDP					
Current Account Balance	-8.9	-1.0	0.9	-0.2	-0.2	2.8	0.9
FDI	7.0	3.4	3.5	-0.1	0.2	1.1	3.5
External Debt	108.3	102.8	91.9	94.8	94.6	94.0	91.9
Cash Deficit(-)/Surplus(+)	-0.9	-4.0	-2.1	-1.0	-0.8	-1.1	-2.1
Base Interest Rate	2.40	0.20	0.20	0.18	0.21	0.18	0.21
EUR/BGN				1.95583			
USD/BGN	1.36	1.47	1.51	1.38	1.35	1.45	1.51

Bulgaria Banking Indicators

		% YoY					
Private Sector	3.6	1.2	3.4	1.6	2.3	2.5	3.4
Firms	2.3	2.4	5.7	3.0	4.1	4.1	5.7
Households & NPISHs	5.8	-0.8	-0.4	-0.7	-0.6	-0.2	-0.4
Private Sector Deposits	10.9	6.8	9.0	6.5	8.4	11.6	9.0
		% of GDP					
Domestic credit	69.6	70.9	71.5	68.4	68.5	69.6	71.5
Claims on government sector	-5.9	-3.2	-0.7	-1.2	-1.7	-1.3	-0.7
Claims on non-government sector	75.5	74.1	72.1	69.5	70.2	70.9	72.1
Claims on households and NPISHs	28.0	26.9	25.1	25.1	25.2	25.2	25.1
		2006	**2007**	**2008**	**2009**	**2010**	**2011**
Bank NPLs to Total Loans		2.2	2.1	2.5	6.4	11.9	13.5
Bank Provisions to NPLs		109.9	100.4	109.0	81.0	74.1	71.2
Return on Assets		2.2	2.4	2.1	1.1	0.9	0.9
Return on Equity		25.0	24.8	23.1	10.2	7.9	7.9
Financial Leverage		11.4	10.3	11.0	9.3	8.8	8.8
Bank Capital to Assets (%)		7.3	7.7	8.5	10.8	10.5	10.6
Bank Regulatory Capital to Risk-Weighted Assets (%)		14.5	13.8	14.9	17.0	17.5	17.7

Source: Piraeus Bank Research, National Sources, IMF

3.3 Cyprus

Economic activity in 2011Q4 plummeted as real GDP dwindled

Economic activity in 2011Q4 fell as real GDP dwindled by 0.7% YoY from a revised contraction of 0.3% in 2011Q3 and a growth of 2.5% in the same quarter of 2010. This is the second quarter in which real GDP decreased since the previous global financial turmoil in 2009/10 as investments and final consumption declined. Specifically, investments plummeted for a third consecutive quarter, by 28.1% YoY in 2011Q4 from 16.1% in 2011Q3 and a respective decline of 13.8% in 2010Q4, while final consumption decreased by 3.3% YoY in 2011Q4 from 0.1% the previous quarter and an increase of 1.4% in 2010Q4. Exports' growth slowed further in 2011Q4 to 0.1% from 3.2% in 2011Q3 and 10.6% in the same quarter of 2010, while imports continued to decline by 14.1% YoY in 2011Q4 from 3.5% in the previous quarter and an increase of 13.4% in 2010Q4. In quarterly terms, real GDP declined by 0.1% in 2011Q4 after a respective decrease of 0.8% in the previous quarter. For the year, economic activity fell to 0.5% YoY in 2011 from 1.1% in 2010 mainly due to the reduction in investments.

Leading indicators point to a further decrease of GDP

The available leading indicators signal a further decrease in economic activity. Specifically industrial production in 2011 shrunk significantly by 7.4% YoY after a decrease of 0.7% in 2010 as the limited electric power in the country confined production. On the demand side, retail sales growth rose marginally by 3.2% YoY in 2011 from 2.9% in 2010, while on the positive side growth in tourism arrivals accelerated significantly in 2011 by 10.1% YoY, up from 1.5% in 2010.

Headline inflation picked up in the previous year

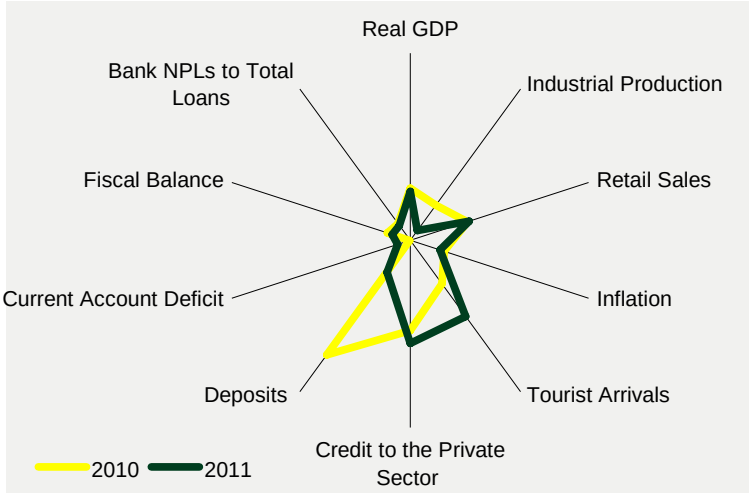
Headline inflation rose in 2011 to 3.3% from 2.4% in 2010 as food prices increased significantly in 2011. Specifically, food prices in 2011 increased by 4.1% YoY compared to 0.2% in 2010. According to the latest data, headline inflation in February increased to 3.1%, the same as in January as food prices increased at the slower rate of 3.5% YoY from 4.8% over the same period. In monthly terms, the consumer price index increased by 0.4% in February after contracting by 1.5% the previous month. On the supply side, the producer's price index in January increased at the faster rate of 8.0% YoY from 6.5% in December increasing the possible passing-through effect in inflation.

Greek debt restructuring will further burden the 2012 Budget

On the fiscal front, the budget deficit continues to rapidly widen as in 2011 it reached 6.01% of the expected annual GDP from 4.91% in 2010, due to a fall in public revenues and an increase in expenditures. The destruction of the Vasillikos power plant in July brought the economy to a halt, and the underlying structural inadequacies, while Greek debt is being restructured, are expected to further burden the 2012 budget. The government, however, decided to increase

VAT to 17% from 15%, a move that is expected to increase revenues in the current year. Further, based on the inadequate fiscal consolidation and uncertainty about the domestic fiscal and banking sector due to the EU debt crisis, Moody's and Fitch Ratings have downgraded the country's sovereign debt rating in the last two months.

Cyprus – Economic Indicators (closer to centre=deterioration)



Source: Piraeus Bank Research, National Sources

External imbalances worsened in the first nine months

External imbalances continued to worsen in the first nine months of 2011 as the current account deficit widened to 7.9% of the expected annual GDP from 6.3% in the same period in 2010, due to a worsening of the income surplus to 9.2% of GDP from 10.8% over the same period. Trade balance posted a deficit of 18.1% of GDP in Jan-Sep from 19.2% in Jan-Sep 2010, while the transfers deficit and services surplus remained unchanged over the same period at 0.7% of GDP and 14.3% respectively. The financing of the current account surplus improved, as net FDIs reached 5.4% of GDP in Jan-Sep from negative figures for the same period in 2010.

The Cypriot banking sector must tackle a number of challenges

The Cypriot banking sector must tackle a number of challenges that have surfaced in the last year, mainly due to the larger-than-expected write-downs of its exposure to Greek government bonds and impending losses on its loans to the Greek private sector. Further, lending in the private sector increased to 12.0% YoY in 2011 from 9.3% in 2010 as credit expansion in firms spiked at 39.5% YoY from 20.2% over the same period. However, household lending fell to 5.4% YoY in 2011 from 10.0% in the previous year, while private sector deposits contracted for the first time by 1.6% YoY in 2011 after seeing growth of 20.2% in 2010.

Cyprus Economic Indicators

	2009	2010	2011	Q1 2011	Q2 2011	Q3 2011	Q4 2011
			% YoY				
GDP	-1.9	1.1	0.5	1.5	1.4	-0.3	-0.7
Final Consumption	-4.6	1.2	-0.9	0.8	-1.1	-0.1	-3.3
Gross Capital Formation	-16.2	4.9	-13.8	-2.5	-9.6	-16.1	-28.1
Exports	-10.7	3.7	3.6	4.9	6.6	3.2	0.1
Imports	-18.6	4.9	-5.0	1.7	-3.1	-3.5	-14.1
Industrial Production	-7.5	-0.7	-7.4	-3.0	-3.6	-12.2	-10.5
Retail Sales	-5.6	2.9	3.2	3.5	7.2	2.5	0.0
Inflation	0.3	2.4	3.3	2.8	3.8	3.0	3.6
Tourist Arrivals	-10.9	1.5	10.1	0.3	14.1	11.2	5.7
Credit to the Private Sector	9.7	9.3	12.0	9.4	9.3	13.9	12.0
Deposits	3.8	20.2	-1.6	12.8	6.3	4.1	-1.6
Residents Deposits	3.3	11.0	-3.8	6.6	-1.7	-0.2	-3.8
Rest of the world deposits	4.3	28.5	-3.2	16.3	16.4	6.9	-3.2
			% of GDP				
Current Account Balance	-10.7	-9.9	--	-3.7	-6.2	-8.0	--
Direct Ivestment	13.2	0.4	--	8.2	6.1	5.6	--
Fiscal Deficit(-)/Surplus(+)	-6.1	-4.9	-6.0	-3.4	-3.6	-3.5	-3.3

Cyprus Banking Indicators

	2008	2009	2010	2011
Bank NPLs to Total Loans	3.6	4.5	5.6	6.1
Bank Provisions to NPLs	67.9	57.6	49.0	47.0
Return on Assets	1.0	0.8	0.6	0.8
Return on Equity	14.5	14.0	11.0	12.2
Financial Leverage	14.5	17.5	18.3	15.3
Bank Capital to Assets (%)	6.9	4.9	5.9	6.7
Bank Regulatory Capital to Risk-Weighted Assets (%)	11.0	12.1	12.5	13.3

Source: Piraeus Bank Research, National Sources, IMF

3.4 Romania

Economic growth in 2011 picked up – compared to the rest of the EU

Economic growth in 2011Q4 continued at a strong rate, especially when compared to the rest of the EU. Specifically, real GDP (seasonally adjusted) increased to 2.2% YoY from 3.4% in 2011Q3 and a contraction of 0.7% in the corresponding quarter of 2010. The low base effect from last year and the favourable agricultural production boosted real GDP, while final consumption and investments increased for the second consecutive quarter after 11 recessionary ones. Specifically, final consumption in 2011Q4 increased by 2.8% YoY, the same as in the previous quarter and -0.7% in 2010Q4 as aggregate demand showed signs of improvement. Accordingly, investments rose by 9.8% YoY in 2011Q4 compared to 11.2% in 2011Q3 and 6.2% in 2010Q4 signalling an improvement in investor confidence in the country as the Stand-By Arrangement with the IMF and the EU is being implemented successfully. Net exports continue to improve for yet another quarter – being the main growth driver of economic activity - in 2011Q4. Net exports recorded an increase in 2011Q4 of 10.1% YoY from 18.1% in 2011Q3 and 7.6% in the same quarter of 2010. In quarterly terms, real GDP in 2011Q4 contracted by 0.2% after an increase of 1.1% in the previous quarter, while for the year real GDP grew by 2.1% YoY in 2011 from -1.8% in 2010, driven by the recovery in final consumption, investments and the improvement of net exports.

Leading indicators show signs of improvement

Annual growth in idustrial production improved in 2011 to 6.2% YoY from 5.6% in 2010, as manufacturing production picked up and economic activity recovered. On the demand side though, along with the rise in aggregate demand, retail sales increased in the last months of 2011 for the first time since May 2010, but this was not enough to reverse the contraction in the sector. Specifically, retail trade in 2011 contracted by 3.4% YoY from 5.8% in 2010.

NBR decided to further relax its monetary policy since January

Inflationary pressures moderated in 2011 as inflation slowed-down to 5.8% from 6.1% in the previous year, due to a decrease in food prices and subdued domestic demand. In February, inflation stood at 2.6% from 2.7% in January and 7.6% for the same period last year, while in monthly terms the consumer price index increased by 0.6% in February from 0.4% in the previous month. Food prices in February contracted by 0.4% YoY after an increase of 0.1% the previous month. The indices for core inflation also point to a deceleration in prices in the following months, while NBR has decided to further relax its monetary policy since January by 75bps at 5.25% in order to continue its support of the local economy and the RON.

Authorities decided to treat the SBA disbursements as precautionary

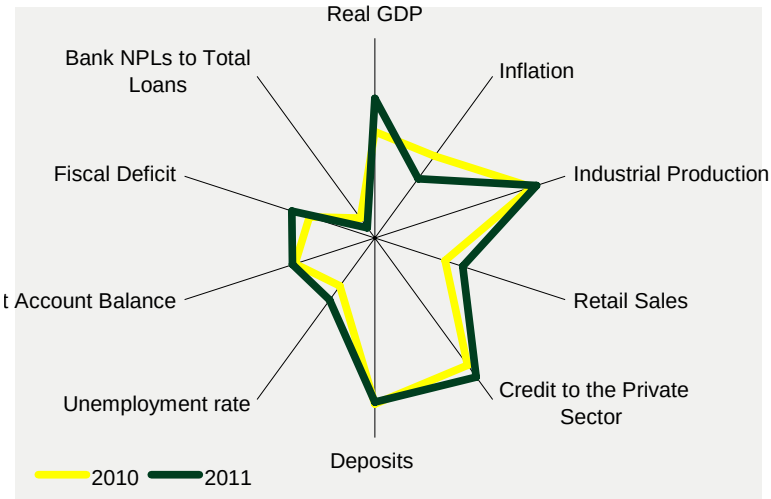
The fiscal deficit in 2011 declined significantly to 4.4% of the expected annual GDP from 6.5% in 2010, as public expenditure decreased to 37.8% of GDP in 2011 from 39.3% in the previous year. On the other hand, budget revenues improved to 33.4% of GDP in 2011 from 32.8% in 2010. The IMF made available the fourth tranche of the precautionary SBA of EUR 500mn (of a

total of EUR 2.0bn since March 2011) in March, though the authorities have decided to keep it as a precaution, and only draw on the funding in case of need. However, it is noted that risks have now risen significantly due to the financial turbulence in the Euro area, while further reforms and privatizations should proceed.

External imbalances marginally deteriorate

External imbalances seem to have marginally declined as the current account deficit in 2011 fell to 4.3% of the expected annual GDP from 4.5% in 2010, due to a narrowing of the trade deficit to 3.8% of GDP in 2011 from 4.7% in the previous year. Income deficit decreased to 1.8% of GDP in 2011 compared to 1.6% in 2010, a trend also exhibited by the transfers' surplus of 2.8% from 2.9% over the same period. Net FDIs rose marginally in the last few months of 2011, reaching 1.5% of GDP in 2011 from 1.8% in the previous year.

Romania – Economic Indicators (closer to centre=deterioration)



Source: Piraeus Bank Research, National Sources

NPLs ratio deteriorates in 2011

In the banking sector, foreign exchange exposure risks remain elevated as the level of eurization of credit is very high in the country. Additionally, the NPLs ratio continued to deteriorate (according to NBR methodology) in 2011 to 23.3% from 20.8% in 2010.

Romania Economic Indicators							
	2009	2010	2011	Q1 2011	Q2 2011	Q3 2011	Q4 2011
			% YoY				
GDP (nsa)	-6.6	-1.7	2.5	1.7	1.4	4.4	1.9
Consumer Prices	3.3	2.4	5.8	7.5	8.2	4.2	3.4
Industrial Production	-6.4	5.6	6.2	9.6	6.3	6.1	3.2
Retail Sales	-9.7	-5.8	-3.4	-5.7	-6.6	-3.6	2.6
Credit to the Private Sector	0.9	4.7	6.6	2.3	1.3	6.5	6.6
Credit in Local Currency	-4.7	-3.0	5.6	-2.4	0.9	3.5	5.6
Credit in Foreign Currency	5.0	9.8	7.1	5.4	1.6	8.3	7.1
Deposits	10.8	5.8	5.6	2.6	2.5	6.6	5.6
Unemployment rate	6.3	7.6	5.4	6.5	5.1	4.9	5.0
			% of GDP				
Current Account Balance	-3.9	-4.5	-4.2	-0.7	-2.5	-3.7	-4.2
Fiscal Surplus (+) /Deficit (-)	-7.3	-6.4	-4.1	-0.9	-1.9	-2.4	-4.1
EUR/RON Spot Rate	4.237	4.281	4.326	4.122	4.236	4.359	4.326

Romania Banking Indicators						
	2006	2007	2008	2009	2010	2011
Bank NPLs to Total Loans	1.8	2.6	2.8	7.9	11.9	13.4
Bank Provisions to NPLs	51.4	61.6	60.3	50.6	55.0	58.6
Return on Assets	1.3	1.0	1.6	0.2	-0.1	0.1
Return on Equity	10.2	9.4	17.0	2.9	-1.0	0.6
Financial Leverage	7.8	9.4	10.6	14.5	10.0	6.0
Bank Capital to Assets (%)	12.9	10.7	9.0	8.6	8.9	7.8
Bank Regulatory Capital to Risk Weighted Assets (%)	18.1	13.8	13.8	14.7	14.7	14.2

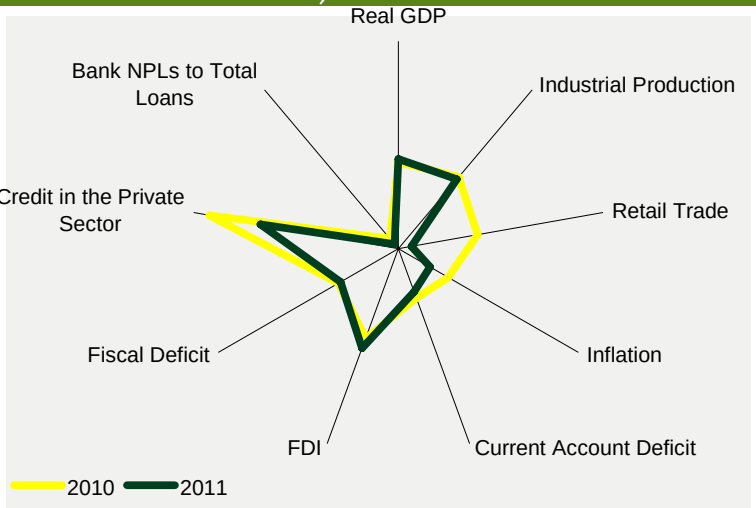
Source: Piraeus Bank Research, National Sources, IMF

3.5 Serbia

Economic activity in 2011Q4 moderated

Growth in economic activity in 2011Q4 slowed down to 0.4% YoY from 0.7% in 2011Q3 and 1.7% in the same quarter last year. Hence, in 2011, real GDP accelerated to 1.6% YoY compared to 0.9% for the previous year. This indicates signs of recovery, though it is expected that economic activity will subside as the country is strongly linked to the European debt crisis. The main growth drivers in 2011Q4 were the electricity and gas, mining, telecom and construction sectors, while the wholesale and retail sectors contracted. According to the leading economic indicators, growth will slow in the following months, as in 2011, industrial production increased at a slower rate of 1.9% YoY, pushed by exports from 3.1% in 2010, while retail trade contracted by 14.5% as domestic demand remains subdued after an increase of 1.3% in 2010. However, the recent approval of Serbia's EU candidate status is expected to attract additional FDIs and prompt the government to make a firmer commitment to reforms, which will lead to growth. Based on that, the international rating agency Moody's affirmed the country's sovereign rating at BB/B, with stable outlook emphasizing however the economic pressure arising from Europe, as Serbia is heavy dependent on external financing.

Serbia – Economic Indicators (closer to centre=deterioration)



Source: Piraeus Bank Research, National Sources

Inflationary pressures in 2011 doubled due to low base effect

Inflation in 2011 almost doubled to 11.2% from 6.2% in 2010, due to a spike in food prices in the first half of the last year and a low base effect from 2010. However, inflationary pressures in the last six months are subdued, as inflation values are in single digits. Specifically, inflation in February rose to 4.9% from 5.6% in January and 12.6% in February 2011, while in monthly terms the consumer price index increased by 0.8% in January from 0.1% the previous month. Food prices in February increased by 1.5% YoY from 3.4% in

January and 17.2% in the same month in 2011. This fall in prices has led the National Bank of Serbia (NBS) to relax its monetary policy rate since January by 25bps to 9.5%. The NBS has noted that inflation will enter its tolerance band in 2012H1, hence any further cut to the key policy rate will depend on the future economic and fiscal prospects in the domestic economy and the Euro-area.

Fiscal deficit widened in 2011 due to a moderation of revenues

The fiscal deficit in 2011 widened to 3.9% of the expected annual GDP compared to 3.4% in 2010, mainly due to a decrease in budget revenues. Specifically, total revenues in 2011 reached 22.2% of GDP from 23.8% in 2010, as tax revenues fell in 2011. On the other hand, public expenditure in 2011 reached 26.1% of GDP from 2.2% the previous year. In 2012, the fiscal deficit in the period Jan-Feb reached 1.2% of GDP compared to 0.6% recorded in the previous year. The fiscal deficit target for 2012 has been set at 4.25% of GDP; however, it might widen further as growth prospects are poor, although the country has committed to an increase in budget revenues and a cut on goods and services spending. Further, the IMF decided to freeze the SBA with the country until the second half of the current year due to a disagreement over the 2012 Budget targets. Specifically, the IMF estimates that the scheduled bond auctions will derail public debt from the 45% of GDP target. The new government, which will be elected on May 6th, however, is expected to pursue the necessary fiscal consolidation and structural reforms set by the SBA. At the same time, public debt reached 45.1% of GDP in 2011 from 42.9% in 2010, while in February public debt reached 44.5% of GDP according to the National Methodology and 41.9% according to the EU Methodology/EU Maastricht criteria.

Net FDIs in 2011 showed significant improvement

In the external sector, the current account balance widened in 2011 to 8.9% of the expected annual GDP from 7.4% in 2010, mainly due to an improvement in the services surplus to 0.5% of GDP in 2011 compared to 0.02% in 2010, as well as a decrease in the trade deficit to 16.5% from 16.7% over the same period. Further, the transfers' surplus deteriorated to 9.4% of GDP in 2011 from 11.6% in the previous year, while the income deficit remained the same compared to 2010 to 2.3 of GDP. Net FDIs showed a significant improvement in 2011 reaching 5.5% of GDP, as opposed to 3.0% in 2010, and financed comfortably the current account deficit. Moreover, we note that the level of the country's foreign exchange reserves remains satisfactory, although in February and March there were large outflows recorded due to the NBS' intervention in the interbank market. The RSD against the EUR stagnated in March, while excessive volatility of the exchange rate was noted over the past two months.

NPLs ratio in December peaked in 2011

Regarding the banking sector, the share of NPLs to the total assets of the sector in December was 19.2% up from 18.8% in September. However, the banking sector remains well-capitalized and stable as the capital adequacy ratio in December stands at a high 19.7%.

Serbia Economic Indicators

	2009	2010	2011	Q1 2011	Q2 2011	Q3 2011	Q4 2011
			% YoY				
GDP	-3.5	0.9	1.6	3.7	2.5	0.7	0.4
Industrial Production	-12.6	2.6	1.9	5.7	3.8	-1.8	0.4
Retail Trade	-11.8	-0.6	-16.8	-10.2	-19.4	-20.0	-16.4
Inflation	8.2	6.2	11.2	12.6	13.6	10.6	7.9
			% of GDP				
Current Account Balance	-7.1	-7.4	-8.9	-2.2	-4.1	-6.2	-8.9
FDI	4.6	3.0	5.5	0.9	1.7	3.8	5.5
Cash Deficit(-)/Surplus(+)	-3.3	-3.4	-3.9	-0.8	-2.0	-2.9	-3.9
Base Interest Rate	9.5	11.5	9.75	12.25	12.0	11.25	9.75
EUR/RSD	95.89	105.50	104.64	103.60	102.46	101.17	104.64

Serbia Banking Indicators

			% YoY				
Credit in the Private Sector	14.1	26.1	13.7	25.2	17.7	13.8	13.7
Other Enterprizes Credit	16.9	25.5	0.8	12.8	6.3	1.8	0.8
Households Credit	9.5	26.1	14.1	27.5	19.1	14.1	14.1
		2006	**2007**	**2008**	**2009**	**2010**	**2011**
Bank NPLs to Total Loans		--	--	11.3	15.5	16.9	18.6
Bank Provisions to NPLs		--	--	187.8	168.1	149.4	141.5
Return on Assets		1.7	1.7	2.1	1	1.1	1.4
Return on Equity		9.7	8.5	9.3	4.6	5.4	7.0
Financial Leverage		5.7	5.0	4.4	4.6	4.9	5.0
Bank Capital to Assets (%)		18.5	21.0	23.6	21.0	19.7	21.0
Bank Regulatory Capital to Risk-Weighted Assets (%)		24.7	27.9	21.9	21.3	19.9	19.7

Source: Piraeus Bank Research, National Sources, IMF