

The results presented in this bulletin are based on the GEA Economic Conjuncture Questionnaire 3/2005, applied on a representative sample of 170 industrial companies. The variations registered in the structure of respondents on criteria of industrial sector, turnover and number of employees have been insignificant as compared to the previous bulletins.

The questionnaire was delivered during 4-18 of July 2005. The interpretation of the material was done by a GEA team led by of Liviu Voinea and Laura Simionescu.

We wish to thank Mr. Daniel Daianu and Mr. Florin Citu for their suggestions and comments. We would also like to thank our colleagues Dragos Pislaru, Silvia Toma, Iulia Serb and Diana Spiridon for the logistical support.

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GEA INDUSTRIAL CONFIDENCE INDEX

GEA index = $(P+C-S)/3$

where **P** represents the expectations regarding the evolution of production, **C** – the current volume of orders and **S** – the current volume of stocks.

P, C and S are calculated as a conjunctural balance (the difference between positive and negative evolutions) reported to the total number of respondent companies.

It is a standard methodology recommended by OECD and used by Eurostat.

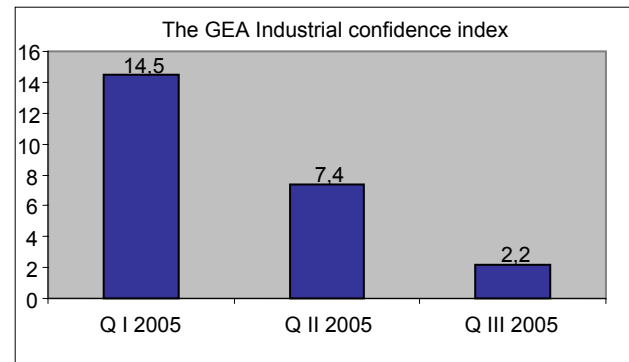
The contribution of GEA stands in its application on a representative sample of industrial companies and especially in the quarterly public announcement of the results and their interpretation.

The values of this index should be regarded as an indicative level, as they are the results of a survey.

The GEA index should not be regarded as statistical data, but as indicative measure regarding the confidence managers have towards the evolution of Romanian industry.

GEA Industrial Confidence Index for Q3 2005 = 2,2

(on a scale from -100 to +100).



The GEA index points at a significant drop in industrial confidence in Q III, compared to the previous quarter. It also shows a descending trend registered from the beginning of the year.

Still, the level of industrial confidence remains slightly positive (above 0 value)¹.

This drop in industrial confidence matches the decline of industrial confidence within the European Union, both at the level of EU-15 and EU-25, from - 4 at the beginning of the year to - 9 in May (the latest available Eurostat data).

The similarity of trends registered in Romania and the EU may point at a greater resemblance of the industrial production structures, and thus represent a sign of convergence.

On the other hand, the similarity of trends could be only a consequence of the acknowledged dependence of Romanian industrial production (especially of the export oriented sectors) on EU demand.

Also, the industrial production and orders from the euro zone display a descending trend.

As regarding Romania, the BNR Conjecture Bulletin 7/2005 suggests a slowing down in the industrial production rhythm.

Among the three components of the industrial confidence index calculated for Romania, the level of orders brought a significant negative contribution, as it experienced a strong decline as compared to the previous quarters (also refer to the next section of the Bulletin).

Amidst the causes which could have lead to this unfavourable evolution, there could be mentioned:

- the accelerated increase in the prices of utilities;
- the increase in the price of fuel;
- the continuous appreciation of the RON exchange rate in rapport to the Euro;
- the uncertainty regarding the date of Romania's accession to EU;
- the frequent changes in fiscal legislation;
- the short term effects of floods².

This is the third quarterly index and we can now proceed to making preliminary observations regarding the degree of concordance between the GEA index and the evolution of industrial production.

Of course, the GEA index is more complex, as it also includes orders and stocks, but a justly calculated confidence index (which is a form of estimating) should be, at least at the tendency level, confirmed by the statistical data registered ex-post.

The closest approximation for these statistical data is the industrial production.

In the following graph, it can easily be noticed that the tendency reflected by the GEA index was later to be found in the industrial production.

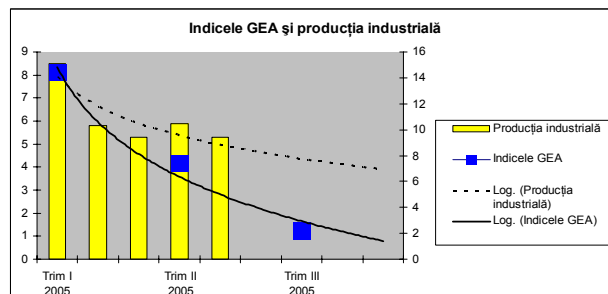
The GEA industrial confidence index is thus confirmed by reality.

Two remarks still have to be made.

Firstly, we have at our disposal too few monthly statistical observations and calculations of the GEA quarterly index to be able to compare beyond any

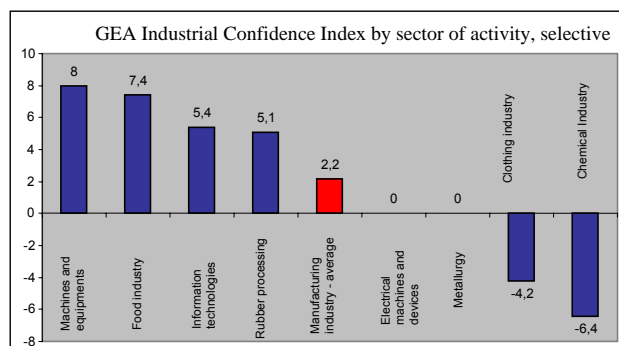
doubt the evolution of industrial production along with the evolution of the GEA index.

Secondly, if we exclude the rise in industrial production registered in January, we can notice that the rest of the months had a more balanced evolution and thus, in this case, we are dealing with a less drastic trend.



Note: industrial production – monthly series, cumulated variation since the beginning of the year, as compared to the same period of the previous year (source: The National Institute for Statistics).

As regarding the index's evolution on industrial sectors, the previous quarter's trends are confirmed, for the majority of sectors.

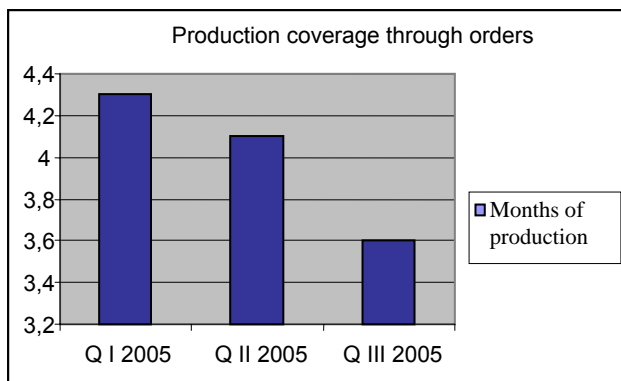


Thus, the machines and equipments industry, the rubber processing industry, the food industry and the information technologies industry preserve their position above the manufacturing industry's average, while the metallurgy sector remains at the same neutral level, and the clothing industry registers a negative index, which denotes the high degree of pessimism (also confirmed by the unfavourable evolution in foreign trade).

The sectors which have reached values below the manufacturing industry average are: the electrical machines and devices industry (for the first time in the index's history) and the chemical industry.

LEVEL OF ORDERS

The current level of orders covers 3.6 months of production considering the manufacturing industry on the whole, dropping from the 4.1 months registered in the previous quarter.



The number of firms for which orders cover a year of production has continued to drop (from 16,5% in the first quarter and 11,2% in the second quarter to 9,3% during quarter three).

The number of firms for which orders cover a month of production at maximum has remained constant (38,5% in quarter III as compared to 38,8% in quarter II).

The standard deviation has also fallen from 4,4 to 3,8 – indicating a reducing variation in the situations occurring at the level of the entire industry.

The drop in orders is also a conclusion of the BNR Conjecture Bulletin 7/2005, which reveals an over five fold reduction in the conjectural balance of the answers to the question regarding the level of orders (the lowest level of the last 12 months).

In the BNR Bulletin, the fall in orders is considered to be a factor which will lead to limitation of the industrial production growth pace, affirmation concordant with the results of the GEA Bulletin 3/2005.

The drop in orders occurs in Romania in the same industrial sectors in which, according to Eurostat, there is a significant reduction in orders at the level of EU-25: machines and equipments, electrical machines and devices, metallurgy and, especially, the clothing industry.

Thus, it could be stated that the external conjecture has contributed to this unfavourable evolution.

Another possible explanation would be that orders are dropping due to the fact that the industry is passing through a restructuring period, which, once over, will help boost orders once again, but for a different production structure.

It remains to be seen which of this hypothesis will be confirmed in the following quarters.

INDUSTRIAL PRODUCTION PRICES

The forecasts made in the first two issues of the GEA Industrial Bulletin have been greatly confirmed by facts, especially those of quarter II.

The evolution of industrial production prices

| | GEA estimation | Statistical data |
|-----------------|----------------|-----------------------------|
| Quarter I 2005 | 0-1% | 1.8% |
| Quarter II 2005 | 3-5% | 3.7% (for April and May) |

In what concerns the expectations regarding the evolution of industrial production prices in quarter III, they are of moderate level, within the interval 0-1%.

PROFIT

The profit of industrial firms has continued to diminish, if compared to both the values of the same period of the previous year, as well as to those registered from the beginning of this year.

The rise of production costs, the appreciation of the exchange rate and the increasing competitive pressures had as a natural consequence the drop of the profit rate for the firms confronted with such problems.

Similar to the previous GEA bulletins, we can notice the managers' tendency to be optimistic about the profit expectations, even though the rest of their answers do not reflect the reasons for this optimism.

This apparent inconsistency between optimistic profit expectations and pessimistic answers to other questions, including the drop of the confidence index, inconsistency which is equally present in the previous GEA Bulletin, can be explained either psychologically (the respondents do not want to accept the logical consequence of the worsening business perspectives – namely the diminishing of

profit); either by means of hidden inflationist expectations (which may increase the prices of their products towards the end of the year).
But, both explanations should be seen as mere speculative interpretations of a statistical anomaly.

Anyway, it is worth noticing the fact that the conjectural balance of those who expect greater profit in quarter III is inferior to that registered in the previous quarter.

Profit evolution

| | Conjectural balance |
|---|---------------------|
| Profit gained in Q II 2005 in comparison to Q II 2004 | -20.8% |
| Profit gained in Q II 2005 in comparison to Q IV 2004 | -24.3% |
| Profit gained in Q III 2005 in comparison to Q II 2005 - estimation | +17.8% |

The sector with the highest profit reduction is the clothing industry (conjectural balance – 56,2).

Other export oriented industries achieved low performances in this regard, out of which the most eloquent examples are the machines and equipments industry (conjectural balance -52,4) and the electrical machines and devices industry (conjectural balance -26,6).

NUMBER OF EMPLOYEES

During quarter II 2005, the tendency to reduce the number of employees, forecasted by the

GEA Bulletin 2/2005, was confirmed. This tendency will continue to extend over quarter III.

The evolution in number of employees

| | Conjectural balance |
|---|---------------------|
| The number of employees in Q II 2005 in comparison to Q I 2005 | -15.7% |
| The number of employees in Q III 2005 in comparison to Q II 2005 – estimation | - 27.9% |

The BNR Conjecture Bulletin 7/2005 also remarks the continuing reduction in the number of employees, while the data put forward by the National Institute for Statistics for the International Monetary Fund within the new Data Dissemination Standard reflects a level of unemployment of 8,5% for quarter I 2005, which has risen in comparison to 2004 (8%).

Anyway, the tendency to proceed to personnel reduction is natural for industrial firms during summer, when temporary hiring in the service area increases.

¹ The interpretation of a positive, but dropping, value, is not considered managerial “pessimism”, but “the reduction of optimism”. We can refer to a negative feeling of the market when the index will fall below 0, should this thing happen.

² On medium and long term, rebuilding infrastructure may restore a higher degree of optimism.

METHODOLOGICAL NOTE

The used sample preserves the same characteristics as in the previous quarters. Over 80% of the respondents have answered at least one of the previous two conjecture bulletins.

The main industries in the sample continue to be: machines and equipments, electrical machines and devices, the chemical industry and the food industry. The structure of the respondent firms, on criteria of turnover and number of employees, has suffered insignificant changes.

Respondent firms by turnover, % out of total

| | Q I | Q II | Q III |
|-----------------------------|------|------|-------|
| Below 1.000.000 € | 22.3 | 21.2 | 21.4 |
| Between 1 and 10 million € | 47.1 | 51.8 | 50.7 |
| Between 10 and 50 million € | 22.4 | 21.2 | 22.1 |
| Over 50 million € | 8.2 | 5.8 | 5,8 |

Respondent firms by number of employees, % out of total

| | Q I | Q II | Q III |
|------------------------------|------|------|-------|
| Below 48 employees | 15.3 | 14.1 | 15.7 |
| Between 50 and 249 employees | 27.6 | 31.2 | 32.1 |
| Over 250 employees | 57.1 | 54.1 | 52.2 |

GROUP OF APPLIED ECONOMICS (GEA)

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