ROMANIA: Modest slowdown, moderate recovery

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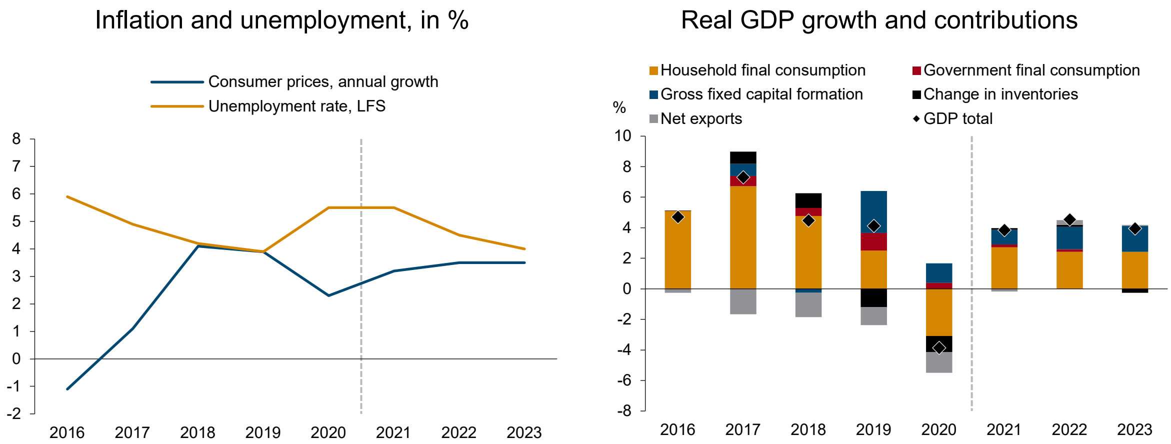
The Romanian economy weathered the 2020 COVID-19 storm better than many others in the EU. Restrictions were less severe than elsewhere during the winter, and so the full-year contraction of GDP remained below 4%. The recovery in 2021 will not be fast (+3.8%), owing to protracted lockdowns and austerity measures in the government budget. Huge inflows of EU funds could boost investment in the coming years.

Figure 4.17 / Romania: Main macroeconomic indicators



Source: wiiw Annual Database incorporating national and Eurostat statistics, own calculation. Forecasts by wiiw.

The second wave of the COVID-19 pandemic in Romania was milder and restrictions were less severe than in many other European countries. Restaurants, hotels and shops were allowed to remain open, with some restrictions, and a curfew was applied only between 11 pm and 5 am. Foreign tourists were absent, but domestic winter tourism was only one-third lower than in the previous year. As a result, real GDP grew by 5.3% on a quarterly basis in the fourth quarter of 2020 and the downturn was only 3.9% for the whole year. A decline in household consumption was responsible for most of the economic contraction. Net exports also made a negative contribution to GDP growth, although no more than had been the case in the previous three years. The structure of the Romanian economy – specifically, its relatively limited reliance on foreign trade and tourism – also mitigated the economic impact of the pandemic. Government consumption was up by 2.3%, and gross fixed capital formation by 5.6%, moderating the economic decline.

Industrial production shrank by 9% in 2020, mainly on account of sluggish foreign demand. Production of motor vehicles was 16% lower than in the previous year, while that of non-metallic minerals, electrical machinery and computers remained flat. Only the production of chemicals and pharmaceuticals expanded, benefiting from orders in the health sector. The food industry contracted by 3%, on account of falling agricultural output (-20%), despite elevated domestic demand for food. Rising food prices and imports balanced the market. Had agriculture not suffered from adverse weather conditions, the GDP contraction last year could have been about 1 percentage point smaller.

Retail sales declined only in April and May 2020; otherwise, they were in positive territory on an annual basis (including in January 2021). Sales of goods did not decline in 2020, but household services fell by 36% in the wake of the restrictions. Services to the business sector were up by 4.2%, among which information technology services expanded by as much as 25%. Construction was another booming economic sector, expanding by 16% in 2020. All segments of construction, including roads and dwellings, grew by double-digit rates. A mild winter and an abundant labour force allowed increased investment from rising personal incomes and from EU funds.

Inflation slowed to 2.3% in 2020, although food prices rose by twice as much. Consumer prices got an upward push in January 2021, when electricity prices were liberalised and customers failed to take advantage of a competitive retail market. This one-time effect may subside during the year, but higher international oil prices and rising consumer demand are likely to increase inflation to about 3.2% in 2021.

The otherwise tight labour market felt the impact of the recession: employment fell and unemployment expanded, mostly in industry. Companies in other economic activities relied more on short-time work schemes and thus kept up employment levels. Although demand will recover in 2021, not all companies currently surviving on government support will be able to recover, and so unemployment may increase further.

The current-account deficit reached 5% of GDP last year, mostly because of the expanding trade deficit in goods. The decline in industrial production was matched by a 10% contraction in merchandise exports. Imports declined by only 5%, mainly on account of fuels, while food imports increased. The balance of services improved compared with the previous year. The negative tourism balance diminished, and the trade surplus in telecommunications and other business services increased. Remittances declined by 13%, mainly those of short-term migrants whose mobility was hindered by the pandemic. FDI slumped by 63%, and the remaining inflows targeted mainly existing enterprises. The number of new projects was small and chiefly confined to services with low capital intensity and real-estate investments. Portfolio investments expanded more than fivefold, mainly on account of government bond placements. Public debt soared from 35% to 46% of GDP, which is still relatively low by international comparison. A depletion of international reserves was also necessary to bring the balance of payments into equilibrium.

Fiscal policy has been lax over the last three years; the extra spending in 2020 came on top of the earlier procyclical loosening. The general government deficit of almost 10% of GDP did not cause problems in the current international environment, but the government is committed to keeping the deficit under control. The 2021 budget law seems realistic, free from the excesses that characterised the previous few years. The public deficit is planned to reach 7.16% of GDP (based on an optimistic 4.3% increase in GDP). The deficit will be cut by curtailing increases in public-sector wages, pensions and other social benefits. Bonuses and other benefits in the public sector will be maintained at 2020 levels, and holiday-related bonuses and vouchers waived. Social security expenditures will increase only by the rate of inflation. Moderate fiscal austerity is planned to continue in subsequent years, bringing down the deficit further, to 5.8% of GDP in 2022 and 4.4% in 2023.

The economy will embark on a growth track in 2021, but expectations are moderated by the current new wave of infections. After months of large-scale opening, the third wave saw secondary schools and indoor restaurants close again in the second week of March. Interruptions in international supply chains – as was the case early this year, when car assembly plants had to restrict production owing to the short supply of chips – may further moderate the recovery.

The government intends to concentrate resources on health care and investments, but keep salaries under tight control in 2021. It will continue to support short-time work and will delay tax payments until the middle of the year. Deferred taxes may become due in the second half of the year, bringing a wave of bankruptcies and an increase in unemployment. Monetary policy will stay moderately lax, with marginally negative real interest rates. After a small cut in the policy rate to 1.25% in January 2021, an increase may follow towards the end of the year if inflation continues to rise. The external balance might not improve as imports could rise more strongly than exports. A current-account deficit of 5% of GDP is rare among EU member states, but related financial inflows can support further economic growth.

Abundant resources from the EU will be at Romania’s disposal this year and next. Only 47% of the ESIF 2014-2020 had been spent by the end of 2020; the rest will be available for three more years. In addition, the disbursement of the EU Recovery and Resilience Facility, of which Romania is entitled to some EUR 30bn (13% of GDP), may start in the second half of 2021. The European Commission has already approved the modification of the Operational Programme ‘Competitiveness’, redirecting EUR 550m of funding to cushion the adverse effects of the coronavirus crisis. Financial support will be given to more than 120,000 SMEs and to initiatives for digitalisation and e-education. The government also agreed a EUR 4.1bn soft loan from the EU SURE programme, to be disbursed in tranches over an 18-month period ending in March 2022. Further EU funds will finance investment activities, making gross fixed capital formation a permanent source of economic recovery. Although absorption capacity and the efficiency of spending remain problematic, the centre-right coalition government installed late last year has the prerogatives and intentions that are needed to improve public governance.

Table 4.17 / Romania: Selected economic indicators

	2017	2018	2019	2020 [1]	2021	2022 Forecast	2023
Population, th pers., average	19,589	19,474	19,372	19,300	19,200	19,000	19,000
Gross domestic product, RON bn, nom.	857.9	951.7	1,058.2	1,053.9	1,140	1,240	1,340
annual change in % (real)	7.3	4.5	4.1	-3.9	3.8	4.5	4.0
GDP/capita (EUR at PPP)	18,630	19,830	21,690	21,220	.	.	.
Consumption of households, RON bn, nom.	536.7	599.4	654.8	636.5	.	.	.
annual change in % (real)	10.9	7.6	4.0	-5.0	4.5	4.0	4.0
Gross fixed capital form., RON bn, nom.	192.2	200.4	239.4	257.2	.	.	.
annual change in % (real)	3.5	-1.1	13.0	5.6	4.0	6.0	7.0
Gross industrial production [2]							
annual change in % (real)	7.9	3.5	-2.3	-9.2	6.0	7.0	5.0
Gross agricultural production							
annual change in % (real)	12.5	7.2	-3.8	-20.1	.	.	.
Construction industry [2]							
annual change in % (real)	-5.5	-4.1	27.6	15.9	.	.	.
Employed persons, LFS, th, average	8,671	8,689	8,680	8,550	8,590	8,620	8,620
annual change in %	2.6	0.2	-0.1	-1.5	0.5	0.3	0.0
Unemployed persons, LFS, th, average	449	380	353	440	500	410	360
Unemployment rate, LFS, in %, average	4.9	4.2	3.9	5.5	5.5	4.5	4.0
Reg. unemployment rate, in %, eop	4.0	3.3	3.0	3.4	.	.	.
Average monthly gross wages, RON [3]	3,223	4,357	4,853	5,162	5,500	5,900	6,400
annual change in % (real, gross)	13.2	8.0	7.3	3.6	3.0	4.0	5.0
Average monthly net wages, RON	2,338	2,642	2,986	3,186	0	0	0
annual change in % (real, net)	12.8	8.0	8.9	4.0	3.0	4.0	5.0
Consumer prices (HICP), % p.a.	1.1	4.1	3.9	2.3	3.2	3.5	3.5
Producer prices in industry, % p.a.	3.5	5.1	3.8	0.0	3.0	2.0	3.0
General governm.budget, EU-def., % of GDP							
Revenues	30.8	31.9	31.8	35.0	33.0	33.0	33.0
Expenditures	33.5	34.9	36.2	44.7	40.0	38.0	37.0
Net lending (+) / net borrowing (-)	-2.6	-2.9	-4.4	-9.7	-7.0	-5.0	-4.0
General gov.gross debt, EU def., % of GDP	35.1	34.7	35.3	46.0	49.0	50.0	50.0
Stock of loans of non-fin.private sector, % p.a.	5.3	7.9	7.0	5.0	.	.	.
Non-performing loans (NPL), in %, eop	6.4	5.0	4.1	3.8	.	.	.
Central bank policy rate, % p.a., eop [4]	1.75	2.50	2.50	1.50	1.25	1.50	1.75
Current account, EUR m	-5,239	-8,961	-10,481	-10,981	-11,600	-11,300	-10,100
Current account, % of GDP	-2.8	-4.4	-4.7	-5.0	-5.0	-4.6	-3.9
Exports of goods, BOP, EUR m	57,162	61,814	63,086	57,579	61,600	65,300	69,500
annual change in %	9.6	8.1	2.1	-8.7	7.0	6.0	6.5
Imports of goods, BOP, EUR m	69,365	76,617	80,510	76,377	82,500	86,600	90,900
annual change in %	12.8	10.5	5.1	-5.1	8.0	5.0	5.0
Exports of services, BOP, EUR m	21,730	23,791	27,057	23,436	25,500	28,100	30,900
annual change in %	15.1	9.5	13.7	-13.4	9.0	10.0	10.0
Imports of services, BOP, EUR m	13,544	15,431	18,404	13,802	15,500	16,700	18,000
annual change in %	23.1	13.9	19.3	-25.0	12.0	8.0	8.0
FDI liabilities, EUR m	5,225	6,205	6,571	2,166	.	.	.
FDI assets, EUR m	348	1,259	1,723	419	.	.	.
Gross reserves of CB excl. gold, EUR m	33,494	33,065	32,927	37,379	.	.	.
Gross external debt, EUR m	97,446	99,841	109,783	125,453	130,000	135,000	140,000
Gross external debt, % of GDP	51.9	48.8	49.2	57.6	56.4	55.0	54.3
Average exchange rate RON/EUR	4.5688	4.6540	4.7453	4.8383	4.95	5.05	5.20

1) Preliminary and wiiw estimates. - 2) Enterprises with 4 and more employees. - 3) From 2018 the employers' social security contribution was transferred to the employees; real growth 2018 refers to net wages. - 4) One-week repo rate.

Source: wiiw Databases incorporating Eurostat and national statistics. Forecasts by wiiw.