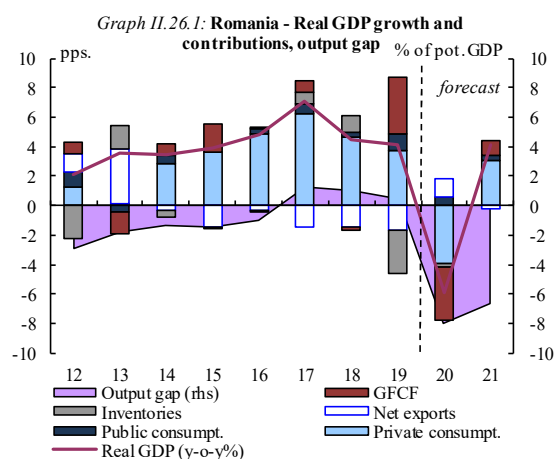


26. ROMANIA

Real GDP is projected to decline sharply in 2020, after several years of robust growth. Private consumption, the main driver of growth in recent years, is expected to be impacted severely by the lockdown measures. Uncertainty is expected to hurt investment decisions, while net exports are projected to contribute positively to growth. Unemployment is set to increase while inflation is forecast to ease due to the drop in oil prices. In 2021, real GDP is projected to rebound, though not to pre-crisis levels. The budget deficit is projected to increase significantly as the fiscal measures required to fight the COVID-19 crisis come on top of past fiscal slippages.

Sharp output drop followed by a moderate recovery

At the onset of the COVID-19 crisis Romania's economy was growing at an annual rate of around 4%, mainly driven by private consumption. However, signs of macro-economic imbalances had already emerged, notably in the form of high and growing current account and fiscal deficits.



Romania declared a state of emergency on 16 March and subsequently extended it until mid-May. Containment measures are expected to significantly affect services and manufacturing. To counter the negative impact of the crisis, the government adopted measures aimed at supporting consumers and businesses, such as loan guarantees for SMEs, temporary moratoriums on loan servicing, and technical unemployment schemes.

Real GDP is projected to contract by 6% in 2020 and rebound by 4¼% in 2021. Private consumption, which is expected to be significantly affected by lockdown measures in 2020, should increase gradually as these are lifted and contribute positively to growth in 2021. After a very strong performance in 2019, investment is projected to drop significantly in 2020, as businesses react to the very uncertain environment by postponing or

cancelling investment projects. Public investment activity, meanwhile, is projected to be subdued. In 2021, investment is expected to recover only partially amid persistent uncertainty.

Exports are also set to contract in 2020, reflecting the economic contraction in Romania's main trading partners and supply chain disruptions. They should resume growth in 2021 as global economic activity gradually picks up. Imports are also set to decline, as domestic demand drops and as production in other countries is affected by lockdowns and supply chain disruptions. Overall, the contribution of net exports to growth in 2020 is set to turn positive and result in a lower current account deficit. However, this positive evolution is expected to start reversing in 2021.

From a record low of 3.9% in 2019, the unemployment rate is projected to increase to 6½% in 2020 as some firms will inevitably close as a result of the COVID-19 crisis, although policy measures are expected to limit job losses. Nominal wages are projected to increase only moderately in 2020 after several years of double-digit growth and remain relatively subdued in 2021.

Inflation is projected to fall to 2.5% in 2020 mainly due to the sharp fall in oil prices. Core inflation is projected to ease somewhat but remain above 3% in 2020 and 2021. In response to the COVID-19 crisis, the National Bank of Romania cut its key monetary policy rate from 2.5% to 2% and started purchasing RON-denominated government securities on the secondary market in order to support the financing of the real economy and the public sector.

Downside risks to the growth forecast

The current projections are subject to a particularly high degree of uncertainty. Beyond the uncertainty that affects all countries related to the evolution of the health crisis, global growth and international

trade, for Romania it will be important how the authorities balance the need for support measures with concerns about the medium-term trajectory of public finances which pre-dated the COVID-19 crisis.

Public deficit set to increase

In 2019, the general government deficit rose to 4.3% of GDP from 2.9% in 2018. The increase was driven by higher current expenditure, in particular on public wages. Additionally, public investment rebounded from the very low levels of previous years.

The general government deficit is forecast to increase to around 9¼% of GDP in 2020. The pre-existing expansionary trend largely driven by pension increases is set to be reinforced by the impact of the COVID-19 crisis. Expenditure on old-age pensions is set to rise considerably, driven by the full-year effect of the 15% pension increase that came into effect in September 2019 and a

further increase of 40% scheduled for September 2020. COVID-19 related measures in the 2020 budget amendment amount to 1.3 pp of GDP of additional spending, out of which 0.4 pp of GDP financed by EU transfers. They include in particular the technical unemployment benefit and emergency spending. Tax revenues are set to be negatively affected by the recession.

The general government deficit is set to further increase in 2021 to around 11½% of GDP under a no-policy-change assumption, despite a projected recovery in tax revenues and phasing out of pandemic-relief related expenditures. This is due to the full-year effect of the 40% increase in pensions in September 2020, an additional upward pension recalculation scheduled for September 2021, and the doubling of child allowance payments.

The debt-to-GDP ratio is forecast to rise from 35.2% in 2019 to around 54¾% in 2022.

Table II.26.1:

Main features of country forecast - ROMANIA

	2018		Annual percentage change							
	bn RON	Curr. prices	% GDP	00-15	2016	2017	2018	2019	2020	2021
GDP	952.4		100.0	3.7	4.8	7.1	4.4	4.1	-6.0	4.2
Private Consumption	604.6		63.5	5.3	7.9	10.0	7.3	5.9	-6.2	4.9
Public Consumption	159.6		16.8	-0.5	2.2	4.2	2.1	6.4	3.4	1.4
Gross fixed capital formation	199.7		21.0	6.7	-0.2	3.6	-1.2	18.2	-15.0	5.0
of which: equipment	75.5		7.9	5.6	-8.9	-9.9	4.3	17.8	-22.1	7.2
Exports (goods and services)	396.1		41.6	8.7	16.0	7.6	6.2	4.6	-12.8	9.9
Imports (goods and services)	424.6		44.6	11.2	16.5	10.8	9.1	8.0	-14.4	9.8
GNI (GDP deflator)	932.8		97.9	3.7	4.5	7.5	4.4	5.0	-5.9	4.0
Contribution to GDP growth:										
Domestic demand				5.5	5.1	7.7	4.7	8.7	-6.9	4.4
Inventories				-0.1	0.0	0.8	1.2	-2.9	-0.3	0.0
Net exports				-1.6	-0.3	-1.4	-1.4	-1.7	1.2	-0.3
Employment				-1.5	-1.1	2.4	0.2	-0.1	-2.5	0.6
Unemployment rate (a)				7.1	5.9	4.9	4.2	3.9	6.5	5.4
Compensation of employees / head				16.6	15.0	14.8	13.4	8.9	2.6	4.8
Unit labour costs whole economy				10.8	8.5	9.8	8.8	4.5	6.4	1.3
Real unit labour cost				-2.0	5.9	4.9	2.4	-2.2	4.0	-1.2
Saving rate of households (b)				-9.0	-9.3	-7.3	-2.3	-2.5	6.9	9.5
GDP deflator				13.1	2.5	4.7	6.3	6.9	2.3	2.5
Harmonised index of consumer prices				10.9	-1.1	1.1	4.1	3.9	2.5	3.1
Terms of trade goods				2.5	-1.7	-2.4	1.3	1.0	-0.5	0.5
Trade balance (goods) (c)				-10.4	-5.5	-6.5	-7.3	-7.8	-6.6	-6.6
Current-account balance (c)				-5.9	-2.0	-3.4	-4.4	-4.6	-3.3	-3.4
Net lending (+) or borrowing (-) vis-a-vis ROW (c)				-4.9	0.5	-1.8	-3.2	-3.1	-1.7	-1.7
General government balance (c)				-3.3	-2.6	-2.6	-2.9	-4.3	-9.2	-11.4
Cyclically-adjusted budget balance (d)				-3.4	-2.3	-3.0	-3.3	-4.4	-6.7	-9.2
Structural budget balance (d)				-	-1.9	-3.0	-2.9	-4.3	-6.7	-9.2
General government gross debt (c)				25.2	37.3	35.1	34.7	35.2	46.2	54.7

(a) as % of total labour force. (b) gross saving divided by adjusted gross disposable income. (c) as a % of GDP. (d) as a % of potential GDP.