2.26. ROMANIA

Economic growth in Romania eased further in 2019. Real GDP growth declined from a post-crisis peak of 7.1% in 2017 to 4.4% in 2018 and is expected to have moderated to 3.9% in 2019. Private consumption remained the main growth driver, the result of a tight labour market and high wage increases, particularly in the public sector. Investment is expected to have made a significant contribution to growth in 2019 supported mainly by construction. Net exports' contribution to GDP growth turned more negative in 2019 with both imports and exports declining. More sluggish external demand was the main culprit behind the fall in export growth and also led to a decline in industrial production.

Real GDP growth is forecast to remain robust at 3.8% in 2020 and 3.5% in 2021. The significant fiscal stimulus planned in 2020 and 2021 is expected to give a new boost to private consumption while also stimulating imports. Investment is expected to remain strong in 2020, supported by construction and greater use of EU investment funds. The reversal in early 2020 of measures introduced in December 2018 concerning the taxation of the banking and energy sectors is expected to favour private investment. The contribution of net exports is expected to remain negative over the forecast horizon, leading to a worsening of the already high current account deficit.

Risks to the growth forecast are tilted to the downside. The fiscal policy stance will be a key determinant of the evolution of economic growth in 2020 and 2021. A continuation of expansionary fiscal policies aggravating existing macroeconomic imbalances could affect investors’ confidence and lead to higher funding costs. Conversely, the start of much needed fiscal consolidation would contribute to the unwinding of the accumulated imbalances but would also result in somewhat lower economic growth over the forecast horizon. More legislative unpredictability or rapidly deteriorating fiscal deficit could also affect the business environment in Romania and have a detrimental effect on investment decisions.

After a 4.1% peak in 2018, HICP inflation declined slightly and averaged 3.9 % in 2019. The decline in headline inflation in the second half of 2019 was mainly due to decreasing food and energy prices. The annual average rate of inflation is forecast to decline to 3.4% in 2020 and 3.3% in 2021. Core inflation remained high in 2019, growing at an annual 3.8%, but is expected to decrease in 2020 and 2021.

Graph 2.26: **Romania - Real GDP growth and contributions**