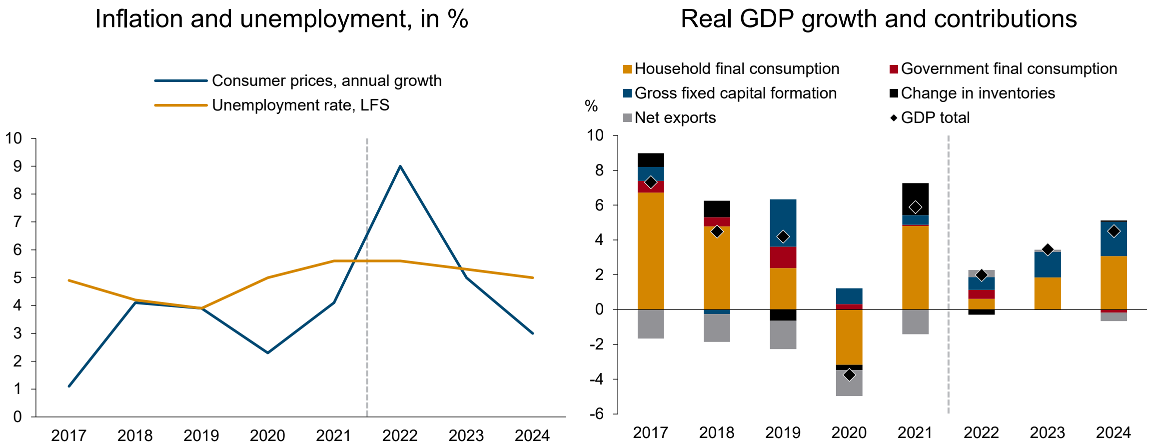
ROMANIA: On the bumpy road to readjustment

GÁBOR HUNYA

Romania's energy and trade dependence on Russia and Ukraine is relatively modest, but still the energy price shocks and supply-chain disruptions have set back its economic performance. GDP will grow by no more than 2% in 2022, despite the generous inflows of EU funds. Inflation will rise to 9% on average, which will depress household demand. Currency devaluation will be modest, due to the central bank's interventions on the currency market.

Figure 4.17 / Romania: Main macroeconomic indicators



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

Romania's economic growth in 2021 was 5.9% – below the wiiw forecast. GDP expanded rapidly in the first half of the year, mainly on account of base effects; but that was followed by stagnation in the second half. Fiscal consolidation curtailed demand and investment, while the external balance saw a deterioration. Soaring energy prices and supply-chain bottlenecks depressed the economy months before the Russian attack on Ukraine. Thus, the huge challenges presented by the war came on top of pre-existing woes.

The international price shock hit Romanian producers and consumers back in September 2021. For household consumers, this only added to the energy price increases that came in the wake of price liberalisation at the beginning of the year. To put people out of their misery, the retail price of electricity and gas supplied to households and smaller business consumers was capped in October. Higher caps have since been introduced, to run from April 2022 until the end of the year. This move is to be funded from taxes levied on the extra profits of the electricity companies.

Inflation has been on the rise since Q3 2021 and will reach about 9% on average in 2022. The central bank has made modest upward adjustments to the policy rate, which currently stands at 3%, but may rise to 4% in the course of the year. Despite negative real interest rates, financial conditions have tightened, and consumer lending weakened in Q1 2022. The national currency has been pretty stable, losing only 1% against the euro between the start of the year and early April, and it displayed only a minor reaction to the outbreak of the war. The central bank is following a policy of managed flotation, making interventions when it considers it necessary to keep the exchange rate stable. As a result, euroisation has been on the decline in recent years. (This policy stands in contrast to that of countries such as Hungary, which follows pure inflation targeting.)

Romania's trade dependence on those countries involved in the war is generally fairly small, though it is relatively significant in specific industries. In 2021, 1.3% of Romania's exports went to Russia and 0.8% to Ukraine. Romania supplied mainly finished or processed products to these markets. The dependence is stronger on the import side: 2.3% of the country's imports originated in Russia and 1.2% in Ukraine. Romania's energy dependence on Russia increased in 2021, when it got access to abundant gas deliveries through TurkStream. In 2021, the country's overall dependence on energy imports stood at 45% – 69% for oil and 28% for natural gas. Its gas dependence is much lower than the EU average and could in future be substituted by local production: the Black Sea Oil & Gas consortium (owned by Carlyle International Energy Partners and the European Bank for Reconstruction and Development) could commence extraction operations in 2022, while Romgaz (in partnership with OMV Petrom) could also be ready in a few years' time. The implementation of major new investments and the start of extraction will depend on the government undertaking to reduce the excessive offshore tax, which has so far delayed exploitation by some four years.

Those sectors worst affected by the war are the metallurgical, automotive and furniture industries. Car manufacturer Dacia is the largest exporter – both overall and to Russia. This Renault subsidiary has lost markets and is also missing components that should have been delivered from Russia. Since Renault is withdrawing from Russia, the value chains will have to be completely reorganised. The furniture industry is facing reduced deliveries of wood from Ukraine and the loss of markets in Russia. Bottlenecks have also appeared in other economic branches: construction work has been hampered by the lack of steel and cement, usually supplied from Ukraine. Russian-owned companies face additional problems. The accounts of TMK-Artrom – one of the largest industrial pipe producers in Romania and Europe, and until recently owned by a Russian oligarch – have been frozen. The high cost of energy has led to production being cut in another Russian-owned company, Alro, a big aluminium producer and Romania's single largest consumer of electricity. Moreover, this company may also be hit by sanctions on Russian multinationals owned by oligarchs.

The repercussions of the war in neighbouring Ukraine have affected the workforce. When production was curtailed in the Dacia factories, workers voiced their discontent over falling wages. The authorities expect up to 30,000 employees of larger companies to be affected by redundancy. They will be eligible to receive 75% of their gross wages from the state budget (up to 75% of the gross average wage) – just like those workers affected by the pandemic. A modest increase in unemployment is to be expected, alongside a drop in household demand. Two further consequences are that the wage-price spiral that evolved at the start of 2022 will come to an end, and the 100,000 non-EU workers who are expected may not arrive – or else may come from Ukraine, rather than Asia.

Romania is one of the main transit countries for refugees from Ukraine and for aid deliveries to the war zones. Of the 515,000 or more Ukrainian citizens who had entered the country up to the end of March, some 79,000 had decided to stay in Romania. Local and international organisations are taking care of the refugees, and some of them have joined the local labour force, finding employment in the service sector. Romania is sending aid to Ukraine, including military equipment, along with other NATO countries. Important support is also being given to neighbouring Moldova, which has shouldered a disproportionately large burden of refugees and is enduring severe supply-chain bottlenecks. Commercial consignments of Moldovan exports have been redirected from the seaport of Odesa in Ukraine to Constanța in Romania. The Romanian government has started to eliminate those bottlenecks in the connecting infrastructure that have been hindering rapid access to the port.

Economic growth will slow to 2% at best in 2022. Real wages will stagnate and household consumption will be sluggish in an inflationary environment of 9% on average. The government will temporarily suspend fiscal consolidation. A social and economic support package to compensate for the effects of soaring inflation will come into force on 1 May. The package is worth 1.2% of GDP, and half of its costs will be financed from EU funds. It will provide income support to about half of the population and will benefit a wide range of small and medium-sized businesses and other companies. Gross fixed capital formation will again expand in 2022, according to the government's ambitious investment plans, which will mainly be financed by EU funds. Romania has already received 13% of the NextGenerationEU funds, and further instalments are due on top of the funds it will receive from the multiannual financial framework. As a side-effect of the war, services exports will receive a boost from the diversion of international trade routes from Ukraine and Moldova to Romanian harbours and transit routes. In agriculture, crop yields could be boosted to replace some of Ukraine's lost exports. The impact of further sanctions on Russia – above all, the European oil and gas import embargo – is the most severe downside risk to growth and is an upside risk for inflation. There could be a significant negative impact from falling demand for Romanian products on shrinking EU markets.

Next year may witness higher growth and lower inflation under a 'new normal'. The economy will continue along the road of bumpy adjustment to elevated energy prices and the loss of Russian and Ukrainian suppliers and markets. Increased energy self-sufficiency – based on offshore gas fields, reopened coal mines and new solar park investments – will render the country less vulnerable. Romania may attract foreign investments that leave Russia and Ukraine, and could benefit from the potential reconstruction of war-torn areas.

Table 4.17 / Romania: Selected economic indicators

	2018	2019	2020	2021 1)	2022	2023	2024
						Forecast	
Population, th pers., average	19,474	19,372	19,258	19,250	19,200	19,100	19,000
Gross domestic product, RON bn, nom.	951.7	1,059.0	1,058.9	1,181.9	1,330	1,440	1,570
annual change in % (real)	4.5	4.2	-3.7	5.9	2.0	3.5	4.5
GDP/capita (EUR at PPP)	19,900	21,670	21,500	23,540	.	.	.
Consumption of households, RON bn, nom.	599.4	655.8	637.3	726.1	.	.	.
annual change in % (real)	7.6	3.8	-5.1	8.0	1.0	3.0	5.0
Gross fixed capital form., RON bn, nom.	200.4	239.4	252.5	285.0	.	.	.
annual change in % (real)	-1.1	12.9	4.1	2.3	3.0	6.0	8.0
Gross industrial production 2)							
annual change in % (real)	3.5	-2.3	-9.2	7.1	1.0	4.0	5.0
Gross agricultural production							
annual change in % (real)	7.2	-3.8	-15.4	16.9	.	.	.
Construction industry 2)							
annual change in % (real)	-4.1	27.6	15.9	-0.6	.	.	.
Employed persons, LFS, th, average 3)	8,689	8,680	8,521	7,756	7,780	7,780	7,780
annual change in %	0.2	-0.1	-1.8	0.7	0.3	0.0	0.0
Unemployed persons, LFS, th, average 3)	380	353	452	459	460	440	410
Unemployment rate, LFS, in %, average 3)	4.2	3.9	5.0	5.6	5.6	5.3	5.0
Reg. unemployment rate, in %, eop	3.3	3.0	3.4	2.7	.	.	.
Average monthly gross wages, RON 4)	4,357	4,853	5,213	5,583	6,100	6,600	7,000
annual change in % (real, gross)	8.0	7.3	4.7	1.9	0.0	3.0	3.0
Average monthly net wages, RON	2,642	2,986	3,217	3,445	3,800	4,100	4,300
annual change in % (real, net)	8.0	8.8	4.9	1.9	0.0	3.0	3.0
Consumer prices (HICP), % p.a.	4.1	3.9	2.3	4.1	9.0	5.0	3.0
Producer prices in industry, % p.a.	5.1	3.8	0.0	14.9	20.0	3.0	3.0
General governm. budget, EU def., % of GDP							
Revenues	32.0	31.9	32.7	34.0	33.0	34.0	34.0
Expenditures	34.9	36.3	42.0	41.0	40.0	39.0	38.0
Net lending (+) / net borrowing (-)	-2.9	-4.4	-9.3	-7.0	-7.0	-5.0	-4.0
General gov. gross debt, EU def., % of GDP	34.7	35.3	47.2	49.0	51.0	51.0	50.0
Stock of loans of non-fin. private sector, % p.a.	7.9	7.0	5.0	14.3	.	.	.
Non-performing loans (NPL), in %, eop	5.0	4.1	3.8	3.4	.	.	.
Central bank policy rate, % p.a., eop 5)	2.50	2.50	1.50	1.75	3.50	3.00	2.00
Current account, EUR m	-9,497	-10,906	-10,893	-16,723	-18,700	-17,600	-18,200
Current account, % of GDP	-4.6	-4.9	-5.0	-7.0	-7.0	-6.2	-5.9
Exports of goods, BOP, EUR m	61,814	63,056	57,532	70,170	74,400	79,600	84,400
annual change in %	8.1	2.0	-8.8	22.0	6.0	7.0	6.0
Imports of goods, BOP, EUR m	77,153	80,900	76,476	93,324	101,700	107,800	114,300
annual change in %	10.3	4.9	-5.5	22.0	9.0	6.0	6.0
Exports of services, BOP, EUR m	23,791	27,058	23,764	27,909	30,700	33,200	35,900
annual change in %	9.5	13.7	-12.2	17.4	10.0	8.0	8.0
Imports of services, BOP, EUR m	15,431	18,408	14,321	18,343	19,300	20,800	22,500
annual change in %	13.9	19.3	-22.2	28.1	5.0	8.0	8.0
FDI liabilities, EUR m	6,205	6,574	3,056	8,813	.	.	.
FDI assets, EUR m	1,259	1,721	112	1,508	.	.	.
Gross reserves of CB excl. gold, EUR m	33,065	32,927	37,379	40,475	.	.	.
Gross external debt, EUR m	99,841	109,783	126,750	134,617	150,000	160,000	170,000
Gross external debt, % of GDP	48.8	49.2	57.9	56.1	56.4	56.1	55.2
Average exchange rate RON/EUR	4.6540	4.7453	4.8383	4.9215	5.00	5.05	5.10

1) Preliminary and wiiw estimates. - 2) Enterprises with 4 and more employees. - 3) From 2021 the new LFS methodology is applied in line with the Integrated European Social Statistics Regulation (IESS). - 4) Average gross wages include the employers' social security contribution. - 5) One-week repo rate.

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