Romania:
Post-crisis performance and current challenges

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GROWTH, CONVERGENCE AND SUSTAINABILITY
Romania’s economy is constantly growing

- Romania registered an impressive post-crisis performance
  - Average annual growth rate of 4.6 percent in the last five years

- The advance seen in recent years was primarily driven by consumption
  - High consumption rates were accompanied by strong imports
  - In spite of high export growth rates, this caused a significant current account deficit widening

- To preserve this growth trend, economic policies should focus on its sustainability
  - There is no substitute for a coherent mix of macroeconomic policies and structural reforms
After several consecutive years of economic growth, Romania’s GDP currently stands well above the pre-crisis level.

**Real GDP**

*annual change (%)*

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<td>lei billion, 2008 prices (s.a.)</td>
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f) forecast

*Source: NIS, National Commission for Strategy and Prognosis*
Romania’s economic growth was significantly above the EU average, chiefly due to consumer demand.

Economic growth in EU Member States in 2018

Contributions to economic growth in Romania

Source: Eurostat, NIS, NBR calculations
Worsening of external imbalance on the back of robust domestic absorption

Domestic absorption and external balance

Balance on trade in goods

Current account in EU Member States

Source: NIS, Eurostat, NBR, NBR calculations

*) according to BPM6, goods under processing trade arrangements are excluded
A durable economic growth is extremely important also from the perspective of euro adoption

- Romania has certainly come a long way in terms of economic convergence
  - Significant increase in per capita GDP as a share of the euro area average (based on PPS), from 31.3 percent in 2005 to 60.4 percent in 2018

- Practical experience has showed us that the Eurozone is not a “convergence club”
  - A high enough level of real convergence (in addition to compliance with the nominal convergence criteria) is needed when joining the euro area

- The level of convergence should increase in a sustainable manner
  - The pace of this process should be in line with the economic fundamentals
Significant progress in terms of real convergence, but the process is far from completion

GDP per capita (PPS) as a share of EA average, %

Source: EC
FINDING THE RIGHT BALANCE BETWEEN CONSUMPTION AND INVESTMENT
The concern for durable growth should prompt a switch to policies aimed at fostering investment

- A short-term focus on economic policies ought to be avoided, as it leads to suboptimal outcomes
  - The adequate approach is to ensure a rebalancing, not by discouraging consumption, but by stimulating investment

- Promoting investment is also a way to reduce development gaps between Romania’s regions
  - These imbalances can be mitigated, first and foremost, through investment in infrastructure (for instance, the construction of highways is essential for connecting Romania’s regions)
In 2017, the wealthiest region in Romania was almost four times richer than the poorest one.
LOOKING FOR A WAY OUT OF A LABOUR MARKET DILEMMA
The adequate path of the wage level in the Romanian economy is the subject of heated debate

- On the one hand, they cannot be considerably below those in other economies, as this would lead to a labour force drain
  - We are facing an emigration problem today, as a significant percentage of the population have left their homeland for other EU Member States

- On the other hand, if wages increase too much, attracting investment may become a problem
  - Wages need to go up, but they should remain compatible with preserving competitiveness

- The key is to increase wages at an adequate, sustainable pace and only by boosting productivity
Labour market tightening, with pay rises additionally fuelled by institutional factors, via the minimum wage and the budgetary sector wage
KEEPING THE EXTERNAL DEFICIT IN CHECK
Increase of ULC in recent years threatens competitiveness

Unit labour cost developments

annual change (%)

ULC measures – variation band
ULC measures – average value

*) data available only for unit wage costs in industry

Note: ULC measures include the annual dynamics of unit labour costs economy-wide (based on both the number of persons employed and the hours worked) and unit wage costs in industry. In case of unit wage costs in industry, starting January 2018 (until December 2018), the annual dynamics of the gross wage are adjusted for the effect of changing the way social contributions are levied and their overall level (from 16.5 percent and 22.75 percent for employees and employers respectively to 35 percent and 2.75 percent), as well as of the decline in income tax from 16 percent to 10 percent, so that the resulting values should reflect developments in unit labour costs.

Source: Eurostat, NIS, NBR estimates
To the extent to which the upward path of wage costs is too steep, it gets very difficult to preserve competitiveness

- If the Romanian companies are unable to gain market shares in the tough competition with rivals, the gap between imports and exports widens, causing the deepening of the trade deficit and hence of the current account deficit

- The latter is already at a level that raises concerns, also in terms of its financing by flows deemed stable (such as FDI and European funds), which have no longer fully covered it
Romania’s external imbalance is singular in the region in terms of its size.

![Current account balance: Romania](chart1.png)

### Current account balance: Romania

<table>
<thead>
<tr>
<th>Year</th>
<th>% of GDP</th>
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<tbody>
<tr>
<td>2005</td>
<td>-8.7</td>
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<tr>
<td>2006</td>
<td>-10.5</td>
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<tr>
<td>2007</td>
<td>-13.6</td>
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<tr>
<td>2008</td>
<td>-11.5</td>
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<tr>
<td>2009</td>
<td>-11</td>
</tr>
<tr>
<td>2010</td>
<td>-5.0</td>
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<tr>
<td>2011</td>
<td>-4.6</td>
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<tr>
<td>2012</td>
<td>4.8</td>
</tr>
<tr>
<td>2013</td>
<td>1.1</td>
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<tr>
<td>2014</td>
<td>-0.7</td>
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<td>2015</td>
<td>-1.2</td>
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<tr>
<td>2016</td>
<td>-2.1</td>
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<tr>
<td>2017</td>
<td>-3.2</td>
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<tr>
<td>2018</td>
<td>-4.5</td>
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![Current account balance: regional comparisons](chart2.png)

### Current account balance: regional comparisons

- **Czechia**
- **Hungary**
- **Poland**
- **Romania**

Source: NIS, NBR
However, Romania’s current account deficit has been mostly financed from stable capital inflows.

Source: NBR
Inflation targeters in the region record monetary policy rates and interbank rates below the inflation rate; in 2018, Romania posted the widest fiscal deficit and external imbalance

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<tr>
<td>Czechia</td>
<td>2.8</td>
<td>2.0</td>
<td>2.19</td>
<td>0.9</td>
<td>4.1</td>
<td>0.3</td>
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<tr>
<td>Hungary</td>
<td>3.9</td>
<td>0.9</td>
<td>0.20</td>
<td>-2.2</td>
<td>-1.1</td>
<td>0.4</td>
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<tr>
<td>Poland</td>
<td>2.2</td>
<td>1.5</td>
<td>1.72</td>
<td>-0.4</td>
<td>-1.0</td>
<td>-0.7</td>
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<tr>
<td>Romania</td>
<td>4.1</td>
<td>2.5</td>
<td>3.26</td>
<td>-3.0</td>
<td>-7.3</td>
<td>-4.5</td>
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Source: Ameco, Bloomberg, Eurostat, NCBs, national institutes of statistics
Conclusions

- It is essential to keep macroeconomic imbalances in check and to promote structural reforms so that the Romanian economy does not witness major vulnerabilities in a global environment marked by so many uncertainties.

- To make forecasts in such an environment is not an easy task, but one thing is sure: it takes a lot of economic policy wisdom to sail safely in waters that are not exactly tranquil.

  ✓ As Abraham Lincoln once said, “The best way to predict your future is to create it.”