The evolution of the major macroeconomic indicators in the Romanian economy for 2020 - 2024

1. Macroeconomic developments in 2020

According to the data published by Eurostat, the Romanian economy registered a decrease of 5% in the volume of activity according to the gross series and 4.5% according to the seasonally adjusted series in the first 9 months of 2020, compared to the same period in 2019. The statistical data place Romania among some of the European countries with the smallest decreases in the January- September 2020 interval. Only a few relevant states such as Ireland (the only one registering growth), Poland, Sweden, Bulgaria, and the Netherlands had a better performance, demonstrating that the governmental policies had a favourable effect in mitigating the COVID-19 shock crisis.

Romania was affected by two negative factors, one the one hand - the COVID crisis and on the other, the unfavourable climate conditions leading to a 29% decrease in gross value added in agriculture in the 3rd trimester, compared to the same period of the previous year and a 23.2% decrease in the first nine months of 2020. Even so, the 5% decrease is half of the economic downturn registered in developed economies such as Spain (-11.6%), Great Britain (-11.2%), Italy (-9.8%) and France (-9.6%).

A significant positive signal comes from the gross investments in economy (gross fixed capital formation – GFCF) registering an increase of 4.4% during the first nine months and having the most remarkable positive contribution to the GDP dynamics: 1.1 pp. Governmental capital expenses stimulated investments, some of which have been in construction, which also registered a consistent growth in this period, of 12.7% as gross value added. Construction works were followed by information and communication, with a 10.6% increase.

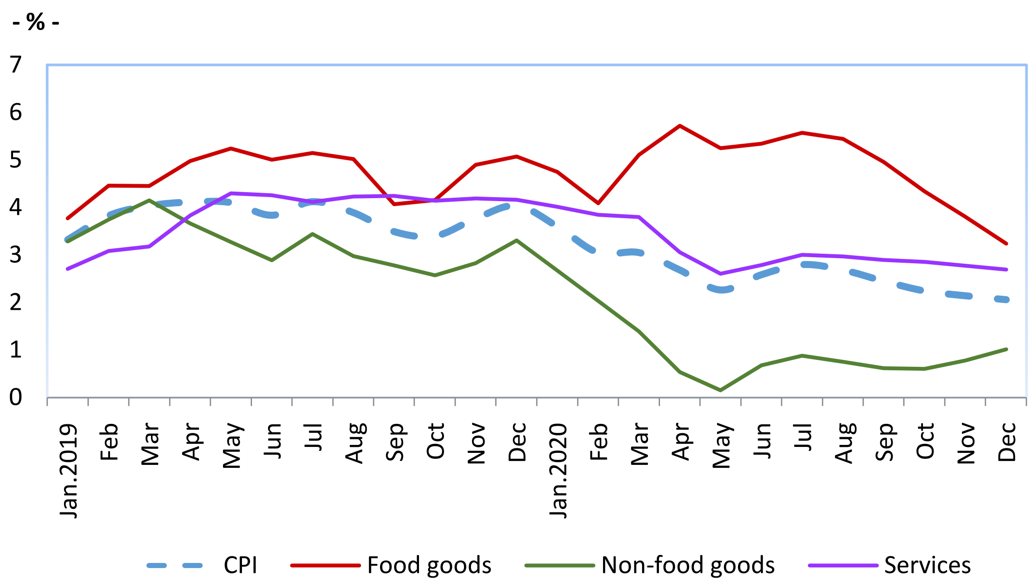
At the opposite end, determined by the peak of the crisis in the 2nd trimester, there were the activities registering decreases between January and September 2020 (gross value added), such as the cultural and leisure activities (-25.4%), industry (-11.2%), trade, transport, hotels and restaurants (-4.7%). The volume of exports of goods and services also registered a reduction (-12.1%), in connection with the developments in industry, as a consequence of demand being blocked on the external markets. There was also a more cushioned decrease in the volume of goods and services imports (-7.5%), partially sustained by the internal demand in investments.

As to private consumption, a decrease of 4.8% was registered over the first nine months (with a contribution of -3.1 pp), the services provided to the population having the most negative impact (-20.2%). Still, it is worth highlighting that the rebound in retail, starting the second half of 2020, depended directly on the merchandise purchase component, which registered a real dynamic of 1.1% over the first nine months. At the same time, the measures required by the health crisis determined additional health and social expenditure for the containment of the virus, which led to an increase of 11.7% in the collective consumption of the public administration over the first nine months of 2020 (with a positive contribution of 1 pp).

Annual inflation continued on a downward trajectory manifested starting the first part of the year, reaching a minimum of 2.06% in December. The decrease in the inflation rate was due to a contraction in the internal demand, whose effects were partially mitigated by a depreciation of the national currency of 1.88%, on average, against the euro.

The downturn in the inflation rate over the last months of the year was determined by the decrease in the prices of fruit and vegetables in the context of a growing supply, and also by a base effect registered for some food-goods. The development was partially mitigated by the tobacco and fuel price increases in December.

Chart 1. The evolution of the annual inflation rate



Source: NCSP calculations based on NIS data

On average, inflation registered a moderate level of 2.63% in 2020, with above the average increases for food-goods (4.8%) and service tariffs (3.1%), while non-food goods prices increased by only 1.01%.

International trade registered a steep decline in the context of the coronavirus pandemic that affected the global economy overall. According to the most recent data published by NIS, during the first 11 months of 2020, Romania's exports registered an 11.0% decrease compared to the same period of the previous year and amounted to EUR 57.1 billion.

By sectors, the machinery and transport equipment export was 8.8% lower than during the first 11 months of 2019 and the EUR 27.6 billion value was almost half the amount of the external markets exports (48.4%). The manufacturing industry products had a 30.4% share in exports, although they registered significant decreases compared to the same period in 2019.

The imports of goods registered a value of EUR 73.5 billion over the first 11 months of 2019, 7.7% less compared to the same period of the previous year. This development in international purchases proves that easing the containment measures led to a moderate rebound in the demand of goods, as imports dynamics started to recover the loss registered over the first half of 2020.

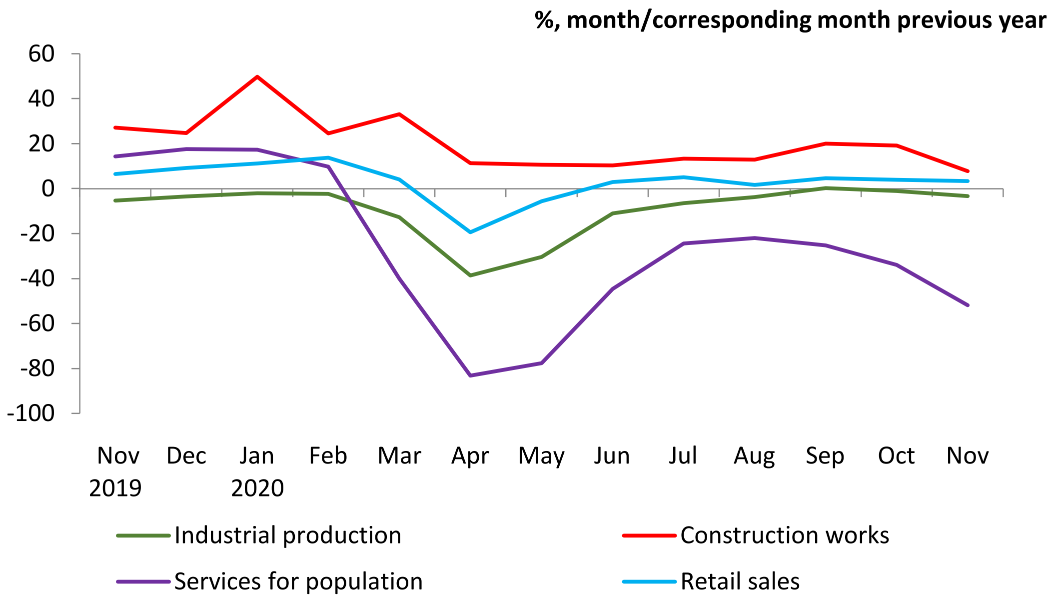
Romania's trade balance registered a FOB-CIF deficit of EUR 16.4 billion over the first 11 months of 2020, 72.3% of which was generated by the internal trade exchanges. The machinery and transport equipment sector covered 2.6 % of the total deficit, with a surplus of EUR 426.1 million. The negative balance of the international trade registered in the petrochemicals (pharmaceutical products, fertilisers, plastic materials, etc.) was of EUR 8.0 billion and represented almost half of the total registered loss.

The current account deficit registered a value of EUR 9763 million in the first 11 months of 2020, EUR 108 million less than in the same interval of the previous year. The increase in the current account deficit was due to the trade balance deterioration, as the decline in the imports was not as steep as the one in exports. These developments led to a EUR 1.1 billion increase in the goods deficit, which means a 7% increase. The developments of the balance trade were mostly mitigated by an increasing surplus in services.

Once the external demand started rebounding starting the 3rd trimester, industrial production also registered significant recovery. On average, the volume of industrial production decreased, over the first 11 months, by 10.2% in annual terms, with clothing and footwear manufacturing and capital goods industry (manufacture of motor vehicles, machinery and equipment) remaining the most vulnerable branches during the pandemic. Moreover, it is worth noting that the evolution of the chemical industry and pharmaceutical products maintained their upward trend in the context of the health crisis.

The performance in the construction sector is remarkable, with an advance of 16.7% in construction works volume over the first 11 months. By construction objects, positive evolutions for all components have been registered over this period, the highest ones for residential buildings (+18.8%), closely followed by engineering construction (+18.4%), branch mainly supported by public investment, while according to structural elements the increases were of 50.0% for capital repair works and 29.9% for current maintenance and repairs.

Chart 2. Monthly dynamics of the main sector indicators



Source: NCSP calculations based on NIS data

The turnover in services for enterprises increased, on average, by 3.4% over the first 11 months in nominal terms, the last three months being characterized by a recovery from the contraction manifested during the emergency state, with the maximum value registered in November, and an annual dynamics of 7.6%. Computer and IT services, which have a high added value, contributed significantly to cushion the economic decline, registering an increase of 23.3% during the first 11 months. Moreover, other support corporate services managed to continue the upward trend in the complicated context of the pandemic and economic activity decline, such as professional and scientific activities, post and courier services, and cleaning activities. The transport sector remains affected, especially the air transport component that registered a 70% decrease in activity over the first 11 months.

The most affected economic activities since the pandemic have continued to be hotels and restaurants, along with other services for the population. In the first 11 months, the volume of turnover for market services rendered to the population decreased by 35.6%, mainly due to the drop in the activity of travel agencies by 42.8%, while hotels and restaurants reduced their activity by 32%. The last two months have been marked by the resumption of contractions in the volume of activity in these areas, caused by the intensification of the physical distance measures imposed with the emergence of the second wave of the pandemic. The negative impact was visible especially for the gambling sector and that of travel agencies, the decreases in the annual dynamics being in November of 77.3% and 62.5% respectively.

Retail trade is the economic activity for which the recovering was the most obvious. The most recent available data have showed the re-entry into positive territory of the annual dynamics since June, but also their maintaining in this area. The food products sales in shops recorded an increase of 5.3% in the first 11 months, being exceeded by the non-food products (+5.8%) which had a substantial recovery in the last period, with double-digit increases. Fuel sales continued to place below the previous year volume of sales, this evolution being driven by the limiting mobility of population measures. Turnover declined by 8.7% for this category.

The measures adopted by the Government in order to support affected companies and employees had an mitigation effect of the negative impact of the Covid crises both on the number of employees and the average gross earnings per economy. Thus, the average number of employees reached 4931 thousand persons in the first 11 months, which means a 1% decrease as compared to the similar period of the previous year. It should be noted that the mitigation of the shock to the average number of employees is due to government measures on technical unemployment. Correspondingly, after an increase in the ILO unemployment rate in the first part of the year, according to monthly data, it stabilized during the summer, reaching 4.9% in the first 11 months (443.7 thousand people).

2. Macroeconomic outlook 2020 – 2024

The international context points out the persistence of risks related to recovery perspective, even though a number of vaccines with high efficacy in testing have been developed. The short term perspective is uncertain mainly in the context of arising new outbreaks and possibility of escalating the geopolitical tensions. A number of euro zone states have been forced to impose new periods of quarantine, which could affect the external demand, private consumption and investments. If tourism continues to be affected, the growth perspectives may suffer, mainly in the states that rely on this branch. Delays in production, purchase and distributions of the vaccine, its possible efficacy below expectations or the continuation of restrictions related to pandemic may delay the economy's recovery.

Even if pandemic is kept under control, the damages caused in 2020 may be more pronounced as expected. Consumers and business environment may behave more restrictively, with influence on spending and investments. Access to credit in the context of low level of interest rate could help companies in difficulty survive, and those more dynamic to increase productivity. However, high levels of indebtedness put additional pressure on economic activity and may create turmoil on financial markets.

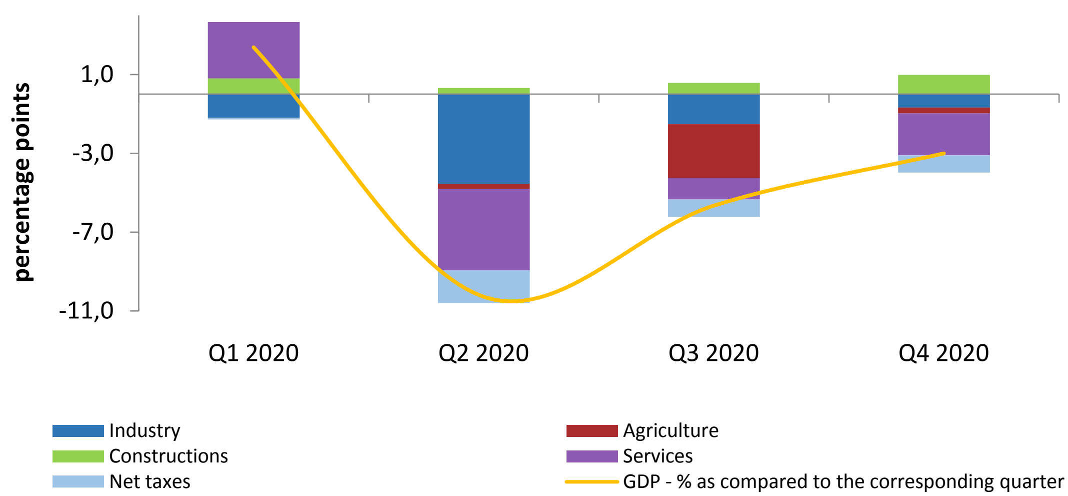
On the other hand, there are also prerequisites for an economic growth beyond expectations supported by an efficient management of the pandemic and the streamlining vaccination process, the accelerating adoption of the digital services or technologies introduced during pandemic.

The forecasting process continues to be marked of severe uncertainties regarding the evolution of macroeconomic indicators. Compared to the previous forecast, the latest developments required contrary revisions, ultimately leading to a negative adjustment of the gross domestic product forecast.

The second wave of pandemic and the continuation of physical distancing measures in the fourth quarter had a negative impact on economy for **the year 2020** which was wider than initially estimated on certain sectors, such as services rendered to the population or cars sales, which imposed a sharper reduction of 0.3 percentage points of the gross value added for services. To these are added the larger decreases in production reported by the NIS for agriculture, the current forecast of gross value added being in this case lower by 0.7 percentage points. At the same time, the results in construction were positively reassessed for 2020, with a plus of 1.1 percentage points.

The evolution by sectors presented previously, as well as the sharper contraction in the agriculture, to which is added the slower recovery at international level, contributed to the negative revision of the gross domestic product, which is estimated to reach a value of 1040.8 billion lei in 2020 and an annual real dynamic of -4.4%.

Chart 3 Quarterly evolution of GDP and contribution of sectors to economic growth in 2020



Source: NIS and NCSP

The identified risks that may influence the estimation of economic growth in the current year, especially in the first half, are severe and interconnected, doubled by a high degree of uncertainty regarding the emergence of new outbreaks in the pandemic, vaccine implementation, speed of recovery of major trading partners, changes in consumer behavior etc. The risks on the economic dynamics are mainly of an external nature, the Romanian economy being closely dependent on the situation of trade with the euro zone at the level of some activities in industry with high added value.

For **the year 2021**, the macroeconomic objective is to largely recover the economic decline of 2020, creating the premises for sustainable economic growth. The forecast for 2021 predicts a gross domestic product advance of 4.3%.

The return to the positive zone is shifted towards the second quarter of 2021, and it is possible that in the first quarter of 2021 to have a slight economic contraction as well, compared to the first quarter of 2020.

Thus, it is expected that all activities will contribute positively to the economy advance in 2021. Constructions will continue their favorable evolutions in recent years, but at a slower pace, determined by the basic effect. Regarding the industry, strongly affected by the health crisis, a partial recovery is expected for the current year, reaching the level of 2019 being estimated in a conservative scenario for 2022. It is also prudent to estimate the evolution of the agriculture for which was forecasted an increase in production of only 14.7%, given that it would come after two years with successive reductions in production (-22.3% in 2020 and -2.2% in 2019). Under normal climate conditions, these estimates may be exceeded.

Table 1 Gross Domestic Product

- percentage change compared to the corresponding period -

	2020		2021
	9 months	Year	Year
GDP	**-5.0**	**-4.4**	**4.3**
Industry (GVA)	-11.2	-8.7	5.7
Agriculture (GVA)	-23.2	-21.9	14.8
Construction (GVA)	12.7	10.6	5.9
Services - total (GVA)	-1.8	-2.3	3.0
Private consumption	-4.8	-4.0	3.7
Government consumption	4.2	3.9	3.0
Gross fixed capital formation	4.4	3.8	6.5
Exports of goods and services	12.1	-10.6	8.1
Imports of goods and services	-7.5	-5.9	10.6

Source: NIS and NCSF

On the demand side, both private consumption and gross fixed capital formation will be the engines of economic growth in 2021, with contributions of 2.4 and 2.9 percentage points, respectively. Private consumption is expected to register a moderate dynamic, due to the lower growth, in real terms, of the wages.

For **the period 2022 - 2024**, the average annual growth rate is estimated at 4.9% with a peak in 2023 of 5%, the year in which a more consistent absorption of European funds is expected. On the demand side, gross fixed capital formation will be one of the main factors of economic growth, with an annual rate of 9%, the scenario taking into account the impact of European funds allocated through both the NRRP program and the multiannual financial framework. Net exports will continue to have a negative contribution, but the braking effect on the economic growth will gradually diminish. On the supply side, the most dynamic sector will be construction, for which an average annual rate of gross value added of 8.8% is expected, in line with the estimated growth in investment. Also, for the tertiary sector, an average annual advance of 4.6% is estimated, the emphasis being on the development of modern services (IT, business services etc.). For the industrial sector, the annual average growth rate is estimated at 4.5%, with the development mainly of branches with increased contribution of gross value added.

The current scenario is based on a prudent absorption of EU funds on the two axes, the financial framework for the 2014-2020 programming period and the Recovery and Resilience Fund, in line with the trend of previous years. A change in the degree of absorption may lead to changes in both directions in terms of gross fixed capital formation and, adjacent to, the labor market.

The economic model which the current estimates are based on makes the transition from an economic evolution focused on stimulating consumer demand to an increase driven by the increase of investments and aggregate supply, which implies the dynamic acceleration of gross fixed capital formation and a consumption pace that will be lower than economic growth.