



NATIONAL COMMISSION FOR STRATEGY AND PROGNOSIS

The evolution of the main macroeconomic indicators in the Romanian economy for 2020 – 2021

1. Macroeconomic developments over the first nine months of 2020

According to the data published by the National Statistics Institute (NIS), the Romanian economy registered a decrease of 4.6% in the volume of activity over the first nine months of the current year, compared to the same period of the previous year. The quarterly evolution of GDP in 2020 was highly influenced by the crisis in the healthcare system.

The first quarter started with favourable developments in many sectors (construction, services for enterprises, communications, etc.) and the economic activity was only to a small extent influenced by the lockdown adopted starting the second half of March. As a consequence, the economic growth in the first quarter was positive, GDP registering an increase of 2.4% compared to the first quarter of 2019. The effects of the pandemic caused by the Sars-Cov 2 virus were strongly felt during the second quarter, after which the economy was set on a positive upward quarterly path.

The state of emergency came with administrative measures leading to lockdown in certain sectors, especially in services, the cultural and leisure sectors as well as in the hospitality sector, leading to significant contractions. Also, teleworking, free movement limitations, physical distancing measures - led to the decrease in the volume of activity for certain service categories (services for enterprises transport etc.). Tourism and transports were the most affected by the lockdown imposed by authorities nationally and globally. The industrial sector was also affected as a consequence of diminished external demand. The sectors which continued their positive evolutions in this period were the ones in construction, IT, as well as public administration - the latter as a consequence of the measures adopted by the government in the context of intensifying activity in the healthcare sector. All of the above mentioned, led to a significant decrease in GDP in the second quarter of 2020, compared to the same quarter of the previous year.

Overall in the first half of 2020, GDP registered a decrease of 4.5% in volume according to the gross series and 3.9% according to the seasonally adjusted series, as consequence of the contraction in gross value added in the industry (-14.1%, with a contribution of -3 percentage points) and in agriculture (-6,7% with a contribution of -0,1 percentage points). The service sector declined moderately in this period, by 1.5% compared to the same period of the previous year, representing, thus, a contribution of -1.0pp. The services sector contracted moderately over this period, by 1.5% compared to the same period of the previous year, with a contribution of -1.0 pp. Within the services sector, there are also positive evolutions - in



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information and communications, with an increase of 12.4% and a contribution of 0.7 pp and public administration with 1.6% (and a contribution of 0.2 pp). The steepest decline was registered by the entertainment and recreational services, -26.3%, with a significant contribution to the GDP dynamics (-1pp).

The crisis in healthcare extended into the third quarter which meant to continue keeping the state of alert. The restrictive measures eased but the recovery of activity was gradual and limited (especially where social distancing measures were required). The third quarter meant a recovery process visible at the level of each sector, except agriculture - which registered a significant contraction of over 25%, caused by the prolonged drought this year. The negative impact in the agricultural sector reduced the magnitude of the economic recovery. The statistical results indicate a decrease of 6% in GDP compared to the same quarter in 2019, compared to only - 3.5%, had agriculture not been taken into account.

The sector whose activity continued at an upward and steady pace, including during the pandemic, was construction, which meant a contribution to real GDP growth of at least 0.5 percentage points over the first 9 months, following an increase by 15.6% in the gross value added in the first half compared to the corresponding period in 2019, and by at least 8.8 % in the third quarter.

On the demand side, private consumption registered a decrease of 5.3% compared to the first semester of 2019 (-3.5 pp), with an unfavourable influence in the services provided to the population area (-21.9%). Moreover, the measures required by the crisis in healthcare led to additional spending in the health and social sectors in order limit the spread of COVID-19 virus, which led to an increase by 11.6% in general government effective collective consumption over the first semester of 2020, its contribution being significant (+ 1.2 pp).

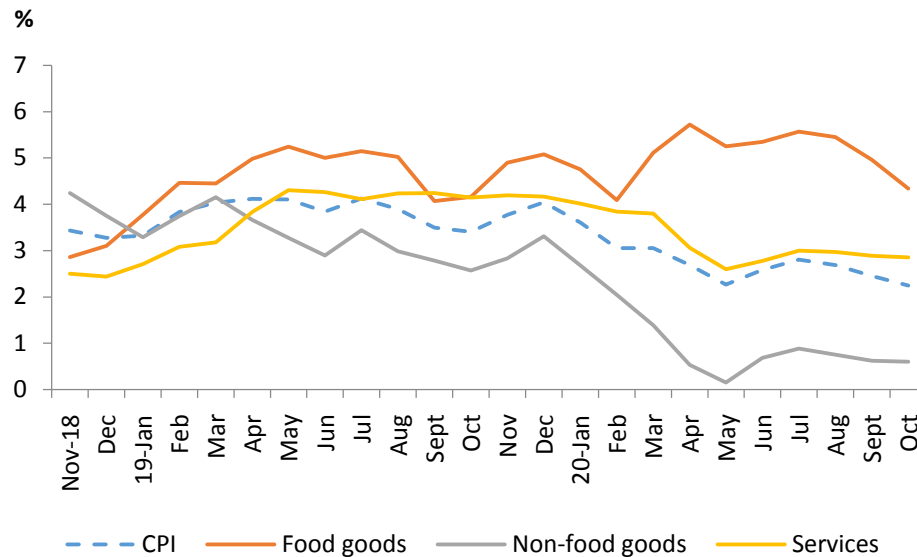
Investment in infrastructure and the residential sector in the first half of the year led to an increase by 6.1% in gross fixed capital formation compared to the first half of 2019, with a positive contribution of 1.2 pp to GDP growth. At the same time, change in inventories registered a negative contribution of 1 pp. The net export also had a negative contribution (-2.2 pp), as a result of the 15% reduction in the exports of goods and services, while the imports of goods and services registered a milder decrease of 9.6%.

Annual inflation continued on a downward trajectory manifested starting the first part of the year and reaching a minimum of 2.24% in October. 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 compared to the euro. The downturn in the inflation rate over the previous months was determined by the decrease in the prices of fruit and vegetables in the context of a growing supply, as well as by the relatively constant prices of fuels.



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Figure 1: The evolution of the annual inflation rate



Source: NCSP calculation based on NIS data

On average, inflation registered a moderate level over the first 10 months at 2.74% with above the average increases for food-goods (5.06%) and service tariffs (3.18%), while non-food goods prices increased by only 1.03%.

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 the National Statistics Institute, over the first nine months of 2020, Romanian exports amounted to EUR 44.8 billion, registering a decrease of 13.6% compared to the same period of the previous year. The structure of the exports was dominated by the delivery of the transport equipment and machinery (47.5%), nonetheless their value diminished by 13.5% compared to the first 9 months of 2019. Also, important shares were registered by other manufactured goods exports (30.8%), group consisting of manufactured merchandise classified mainly according to the raw material (iron, steel, rubber, metal, woodwork, etc.)

The imports of goods registered a value of EUR 57.9 billion over the first 9 months of 2020, registering a decrease of 9.5%, a dynamic clearly below to the export's one. The evolution of international purchases shows that although the lockdown measures have been eased, the demand for goods remains low. The structure of the import of goods was dominated, as was the case with export, by transport equipment and machinery (36.6%) and other manufactured products (30.2%).



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Romania's trade balance registered a FOB-CIF deficit of EUR 13.1 billion over the first 9 months of 2020, almost EUR 1 billion higher than the deficit registered over the same period in 2019. The machinery and transport equipment sector covered only 0.8% of the total deficit, with a surplus of only EUR 101.4 million. The negative balance of the international trade registered in the petrochemicals (pharmaceutical products, fertilisers, plastic materials, etc.) was of EUR 6.5 billion and represented 49.3% of the total registered loss.

The third quarter was characterized by a consistent recovery in trade, following the severe decline in the second. Romanian export increased by 40.7% compared to the previous quarter, reaching 95.7% of the value of exports registered over the second quarter of 2019. In September there was only a 0.5% decrease, compared to the exports in September 2019. A similar situation was registered with imports, with a decrease of 3.2% compared to the third semester of 2019. In September the annual dynamics of imports turned positive, registering an increase of 4.4% compared to the same month in 2019.

The recovery in external demand led to an important recovery in industrial production. On average, the volume of industrial production decreased, over the first three quarters, by 12.1% in annual terms, with clothing and footwear manufacturing and capital goods industry (manufacture of motor vehicles, machinery and equipment and manufacture of electrical equipment) remaining the most vulnerable branches during the pandemic. Correlated with the evolution in the exports of goods, the volume of output in September reached the same level it had in September 2019, with the most important uptake in the manufacture of road vehicles (+9.1%), due to the recovery in demand of the main external trade partners, and the textile industry (+ 6.5%). Moreover, it must be noted 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 17.6% in construction works volume over the first 9 months. By construction objects, positive evolutions for all components have been registered over the first three quarters, the highest ones for engineering construction (+19.5%), branch mainly supported by public investment, while according to structural elements the increases were of 56.5% for capital repair works and 39.8% for current maintenance and repairs.

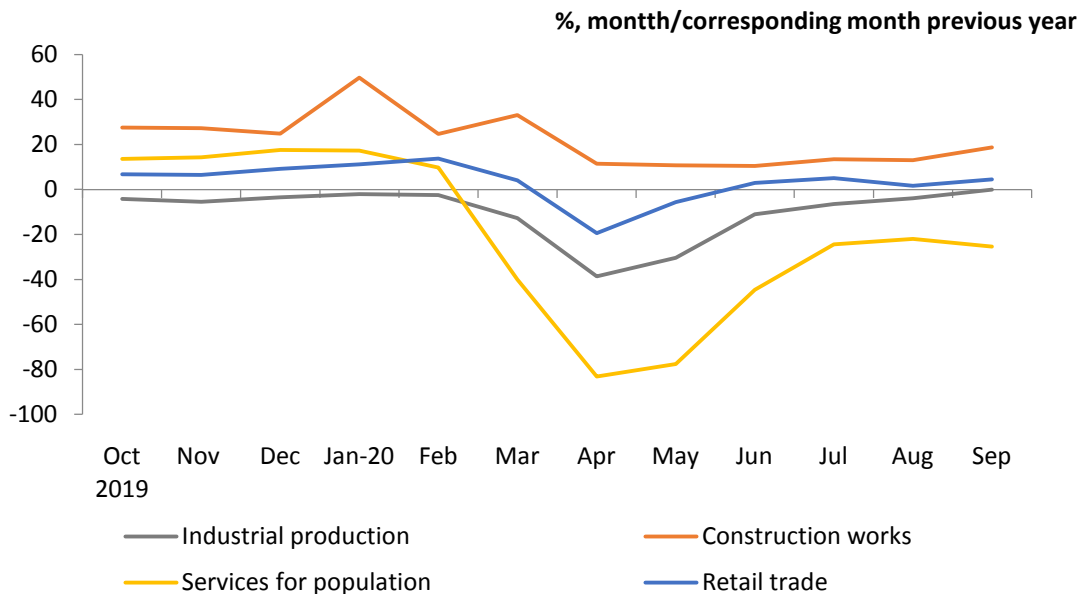
The turnover in corporate services increased, on average, by 2.9% over the first 9 months in nominal terms, the third quarter being characterized by a recovery from the contraction manifested during the emergency state (+13.3% compared to the previous quarter). Computer and IT services, which have a high added value, contributed significantly to cushion the economic decline, registering an increase of 24% during the first 9 months. Moreover, other support corporate services managed to continue the upward trend in the difficult context of the pandemic and economic activity decline, such as professional and scientific activities, post



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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 9 months.

Figure 2: Monthly dynamics of the main sector indicators



Source: NCSP calculation based on NIS data

The most affected economic activities since the pandemic outbreak continue to be the hotels and restaurants, as well as other services provided to the population. Over the first three quarters, the volume of the turnover for the market services provided to the population decreased by 32.9%, especially as a consequence of the decline in the tourism agencies' activity by 49.1%, while hotels and restaurants diminished their activity by 30%.

Retail trade is the economic activity for which the recovery is the most obvious. The most recently available data showed positive recovery both of the dynamics of food-goods sales in shops (+ 5.8% over the first 9 months) as well as of the dynamics of non-food goods sales (+3.9%). The change in consumers behaviour and economic operators must be noted, who rapidly refocused towards online sales (+41.4% over the first 9 months), compensating therefore for the non-food goods, traditionally purchased in stores.

2. International context

The first signs of recovery since May, once economic activity has resumed and restrictions have been relaxed both at European and global level, as well as the experience gained by states in managing the pandemic, represent a favorable signal supporting the upward adjustment of the



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autumn forecasts released by the main international organizations regarding the evolution of the European and the global economy.

Thus, the Organization for Economic Cooperation and Development (OECD) has estimated in September 2020 a contraction of 7.9% for the euro area (compared to the expected decreases of -9.1% and -10.5% in the two June scenarios, respectively without and with the second wave of the pandemic). In the case of the European states, compared to the June OECD estimates in the single-wave scenario of the pandemic, the estimates of the economy contraction in 2020 are improved, the most pronounced adjustment being in the case of the French economy (almost 2 pp). For the German economy, there is an upward adjustment of 1.2 pp, as in the case of the euro area economy (for which a contraction in GDP of 7.9% is estimated). At the same time, for the US economy, the revision of OECD estimates of about 3.5 p.p. leads to a 3.8% drop in GDP this year.

Once the threat of the pandemic spread narrowed faster than expected at the beginning of the year, the improvement in confidence will support a significant increase in activity in 2021, estimated at 5.1% in the euro area. However, the persistence or recurrence of the health crisis and the undertaken lockdown measures can reduce, by 2-3 percentage points, the global growth in 2021, leading to a prolonged period of low investment.

Regarding the recent estimates of the International Monetary Fund (IMF) in October 2020, a contraction of 4.4% in the global economy is expected in 2020 compared to the estimate of -4.9% of the summer forecast, with a more pronounced decline in advanced economies (-5.8%), and for the euro area economy the economic contraction is estimated at 8.3%, with an adjustment of 2 percentage points compared to the summer forecast. With the exception of Spain (-12.8%), estimations regarding the economic contraction for the main European economies have been improved as follows: Germany - 6.0%, France -9.8%, Italy -10.6%. The IMF estimations for Romania indicate a contraction of 4.8% in 2020 followed by economic growth of 4.6% the following year.

In the autumn forecast (November 2020), the European Commission estimates a decrease in the European economy of 7.4% in 2020 (compared to -8.3% in the summer forecast) and that of the euro area by 7.8%. In 2021, the European economy is expected to recover, growing by 4.1% and 4.2% in the euro area respectively, with large differences between economic developments in the Member States.

For the Romanian economy, the EC estimates a contraction of 5.2% this year (with an adjustment of 0.8 pp compared to the summer forecast), followed by an increase of 3.3% in 2021. In the structure, a gradual recovery of private consumption is expected, in line with the relaxation of physical distancing measures by 2021, as well as of investments. The contribution of net exports to growth over the forecast horizon is expected to remain negative.



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3. 2020 – 2021 outlook

Compared to the situation existing at the time of elaboration of the summer forecast, in August 2020, certain hypotheses have been modified:

- Continuing the state of alert in the fourth quarter (until the availability of the large-scale vaccine) to ensure the protection of public health, with a direct economic impact on services provided to the population and private consumption;
- Slower recovery of gross value added in industry, in correlation with external demand and in line with the agricultural outcomes (households industry, self-consumption);
- The sharp reduction of agricultural production, especially in the vegetal sector, with a partial recovery in 2021, the scenario presented being a prudent one;
- Higher performance in construction, with a positive influence on investments.

The current scenario was based on a health crisis worsening in the in the last quarter of the year and an intensification of restrictive measures in areas involving high human interaction (closing restaurants and shops after a certain hour, restricting traffic at night, tele-working activity where is possible etc.) and even local quarantine.

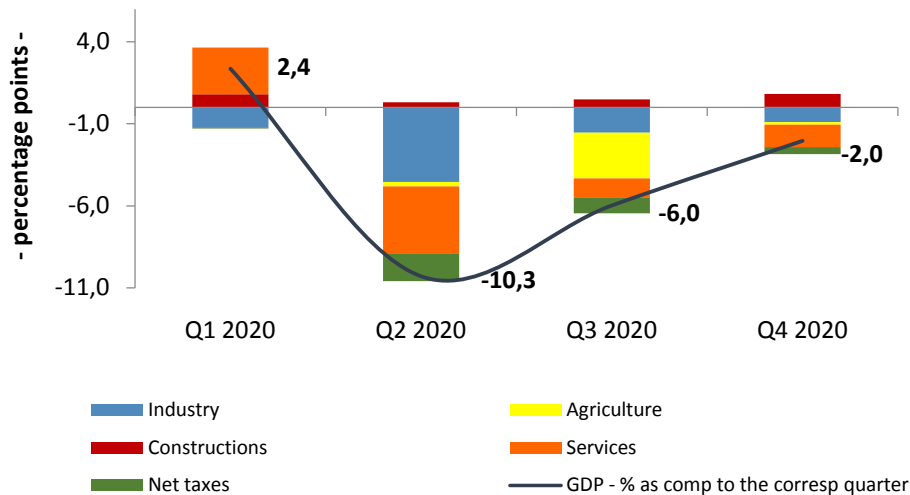
In these circumstances, it has been estimated that the most affected activities remain those in the services sector, such as hotels and restaurants, gambling or air transport. Positive developments are expected to continue in construction, IT services and health, the latter as a result of constant government action to address the health crisis as effectively as possible. Moreover, industry, which has shown signs of recovery beyond expectations starting with the third quarter, will continue the recovery process, which will make the reduction of activity (compared to the fourth quarter of 2019) to be more attenuated. Agriculture, although affected by the drought this year, will have a low negative impact in the fourth quarter, with a modest share in GDP (around 2%).

At the same time, in a positive sense, the measures adopted by the Government in order to support the affected companies and employees will continue to have a mitigating effect on the negative impact both on the number of employees and on the average gross earnings per economy. Government support is also found in the government consumption positive influence on GDP, as well as in mitigating the costs of companies in industry and services, limiting the decline in supply by at least 1 percentage point for this year.



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Figure 3: GDP evolution and contribution to the economic growth by quarters 2020



Source: NIS and NCSP

All these influences led to an economic growth estimation of around -2% for the fourth quarter compared to the same period of the last year. As a consequence of these developments, the gross domestic product is estimated to decrease in 2020 by 4.2% (in real terms) compared to 2019.

Table 1 Revision of the GDP developments

	2020		2021	
	Summer forecast (%)	Autumn forecast (%)	Summer forecast (%)	Autumn forecast (%)
GROSS DOMESTIC PRODUCT	-3.8	-4.2	4.9	4.5
Private consumption expenditure	-2.2	-3.7	5.8	4.6
Government consumption expenditure	4.3	4.3	2.9	2.9
Gross fixed capital formation	-3.5	2.8	7.4	7.0
Export of goods and services	-10.3	-10.7	9.7	8.0
Import of goods and services	-7.7	-6.0	11.3	10.0
GVA Industry	-8.6	-9.1	7.8	6.1
GVA Construction	5.8	9.5	4.8	6.2
GVA Services - Total	-2.7	-2.0	4.0	3.5
- GVA trade, transport and storage, hotels and restaurants	-4.0	-3.9	5.7	4.6
- GVA Shows, culture and recreation activities, repair of households, goods and	-17.3	-28.0	22.5	24.5

Source: National Commission for Strategy and Prognosis



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The main support of economic activity this year, and in particular in the fourth quarter, is the construction sector, the increase in gross value added being estimated at 9.5%, with a contribution to real growth of 0.5 percentage points. Other annual increases are estimated in the IT sector (9.2%) and public administration (1.7%), their contributions to the real GDP dynamics amounting to 0.7 percentage points.

In contrast to these favorable developments are the reductions in the volume of activity in agriculture, industry and some categories of services. Agriculture is one of the most affected sectors, the estimation for 2020 predicting a 21.2% decrease in gross value added, and its contribution to real GDP growth being -0.9 percentage points. The gross value added in industry is estimated to decrease by 9.1%, contributing negatively by 2 percentage points to real GDP growth, noting that the influence of industry came from the decline in the second quarter, followed by a quarterly recovery in the second half of the year. Within the tertiary sector, in addition to those mentioned with positive developments, significant reductions are expected in the "shows, culture and recreation services", with gross value added estimated to be reduced by 28%.

On the demand side, for gross fixed capital formation an increase of 2.8% is estimated, a positive correction compared to the previous forecast, due to the favorable results in the first half when it remained at positive values in annual terms, but also to the continued growth of investments in the second half through the combined effort of absorbing European funds and supporting investments from public funds. This development is expected to translate into a contribution of 0.7 percentage points to real GDP growth. Government consumption will also have a positive impact, with an increase of 4.3%, as a result of the government measures undertaken to control and neutralize the effects of the pandemic. Regarding the private consumption, it is estimated to decrease by 3.7%, which means a negative contribution of 2.4 percentage points to real GDP growth. The contribution of net exports to GDP growth remains negative throughout the forecast horizon, with the trade deficit continuing to be the main determinant of the deterioration in the external balance.

For 2021, the macroeconomic objective is the recovery of the 2020 economic downturn, creating the premises for sustainable economic growth. The forecast for 2021 leads to an increase in gross domestic product of 4.5% in real terms.

Estimations of future developments are strongly related to the evolution of the health crisis. Currently, for 2021, the economy is expected to recover growth starting with the second quarter. For the year as a whole, the economy is expected to recover, and in those areas where significant contractions occurred in 2020 (industry, some categories of services, exports and imports), the declines will largely recover.



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Thus, for 2021 it is expected that all activities will contribute positively to the advancement of the economy (+ 4.5%). Construction will continue its favorable developments in recent years. As for the industry and services severely affected by the health crisis in 2020, these activities will be the main growth support in 2021.

Investments will play an important role in supporting economic growth with an increase of around 7% and a contribution of 1.9 percentage points, an important role in supporting them having the financial aid from the EU.

The current scenario is based, in line with previous years' trend, on a prudent absorption of EU funds in the first year on the two axes, the financial framework for the 2014-2020 programming period and the Recovery and Resilience Fund. A positive revision of the forecast is expected, depending on the implementation level of new investment projects.