Romania: slower growth, higher inflation

Valentin Tataru, Chief Economist

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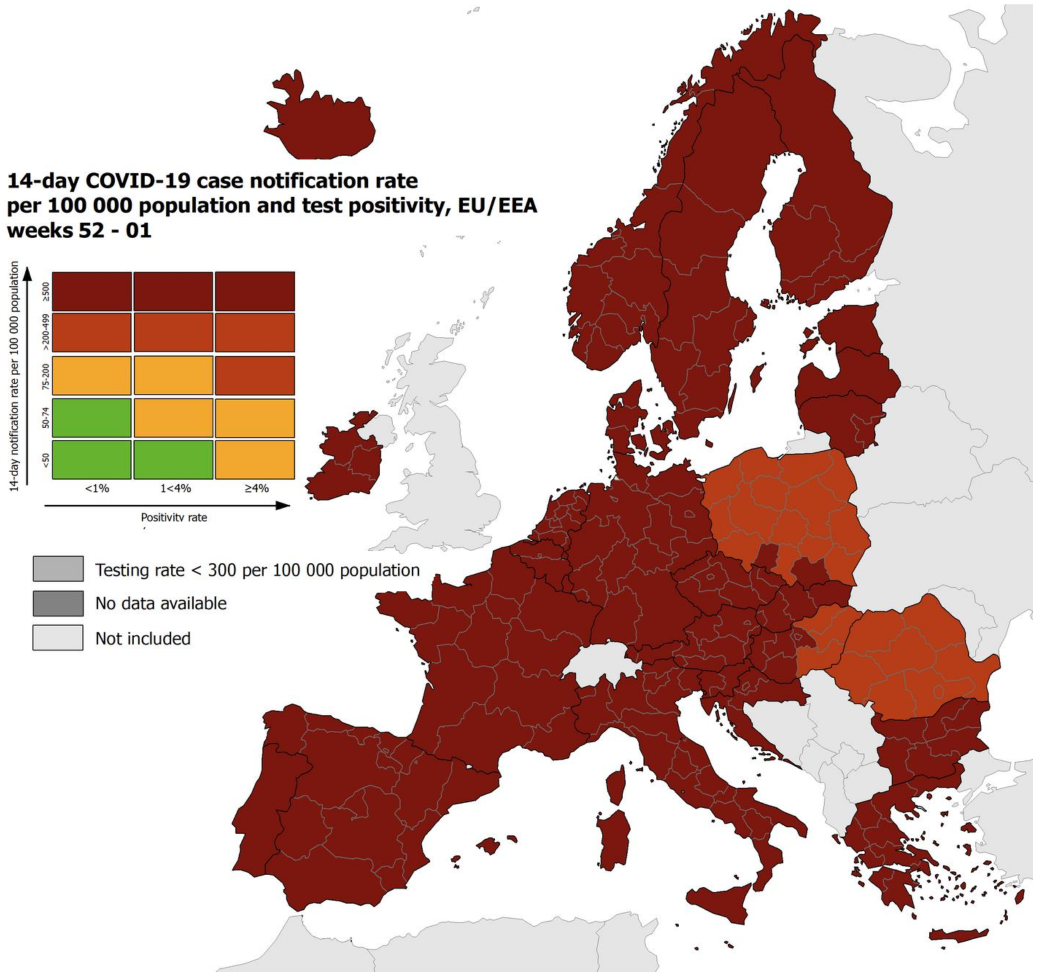
think.ing.com

Data sources: Eurostat, European Commission, National Statistics Institute, National Bank of Romania, Brugel, Ministry of Finance, CompNet, EIB, ECB, OECD, WEF, Reuters, Bloomberg, ING

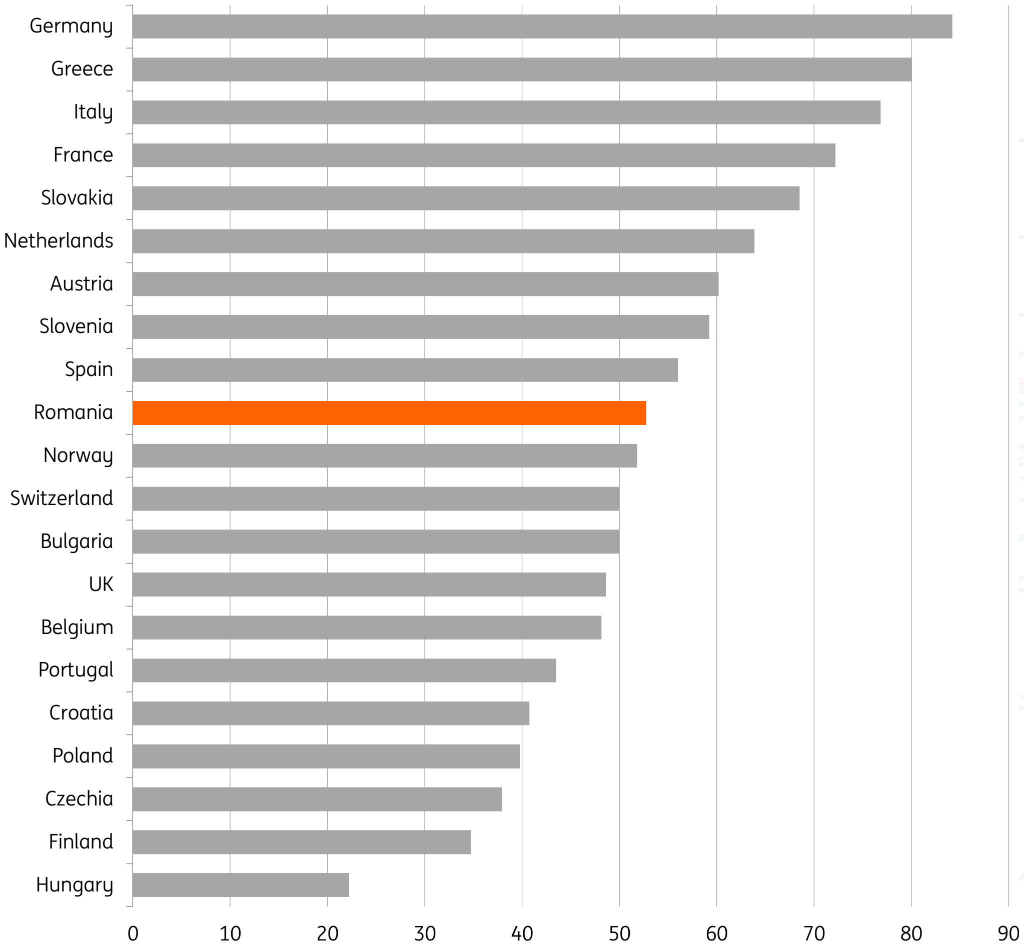
Embracing for the 5th wave

Infections per 100k (as of 13 January)



Source: ecdc.eu

Restrictiveness index (100=maximum)



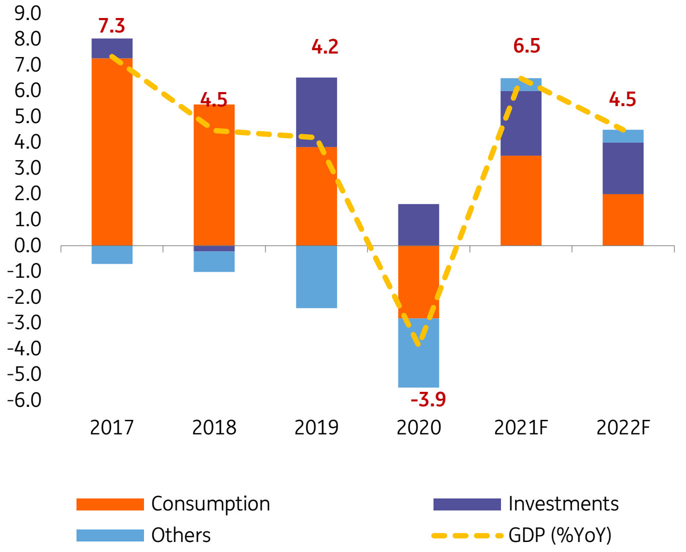
Source: ourworldindata.org

Jan 12, 2022

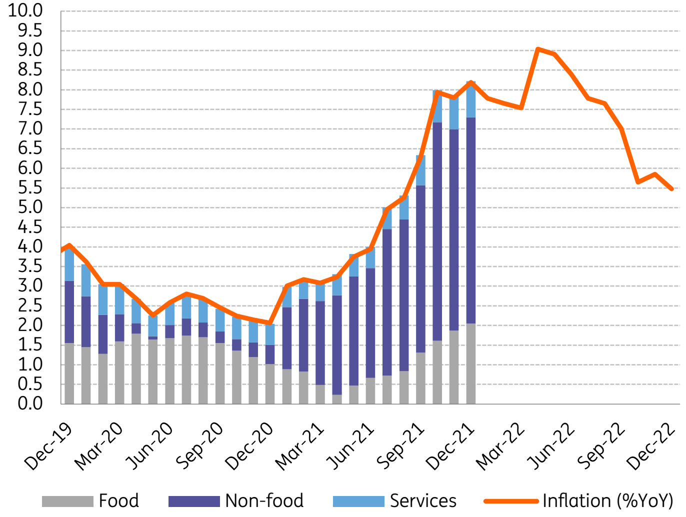
Portugal	90.01%
Spain	81.56%
Belgium	75.90%
Finland	75.09%
Italy	74.88%
France	74.87%
Austria	73.17%
Norway	72.29%
Germany	71.71%
United Kingdom	70.09%
Cyprus	69.14%
Greece	68.82%
Lithuania	68.66%
Switzerland	67.37%
Hungary	62.75%
Czechia	62.67%
Estonia	62.05%
Slovenia	57.67%
Poland	56.54%
Croatia	53.30%
Romania	41.30%
Bulgaria	28.34%

Macro outlook: good recovery, but Omicron can inhibit the momentum

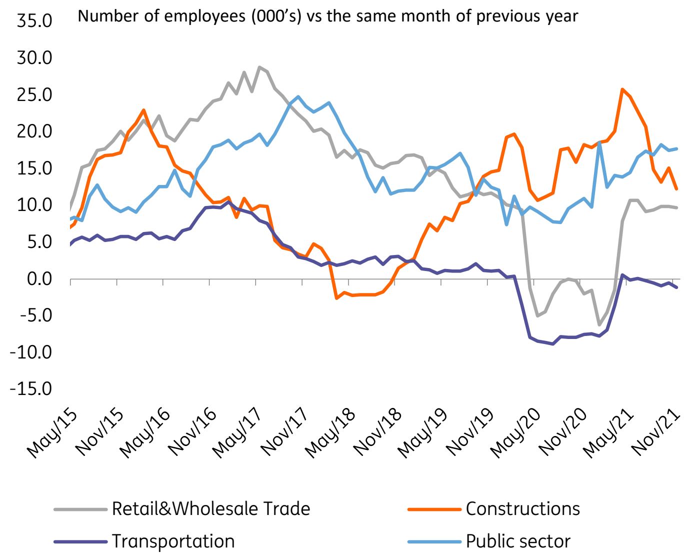
GDP: strong growth, driven by both consumption and investments



Inflation: energy and 2nd round effects will push inflation above 8.0%



Labour market: close but not yet to pre-pandemic levels



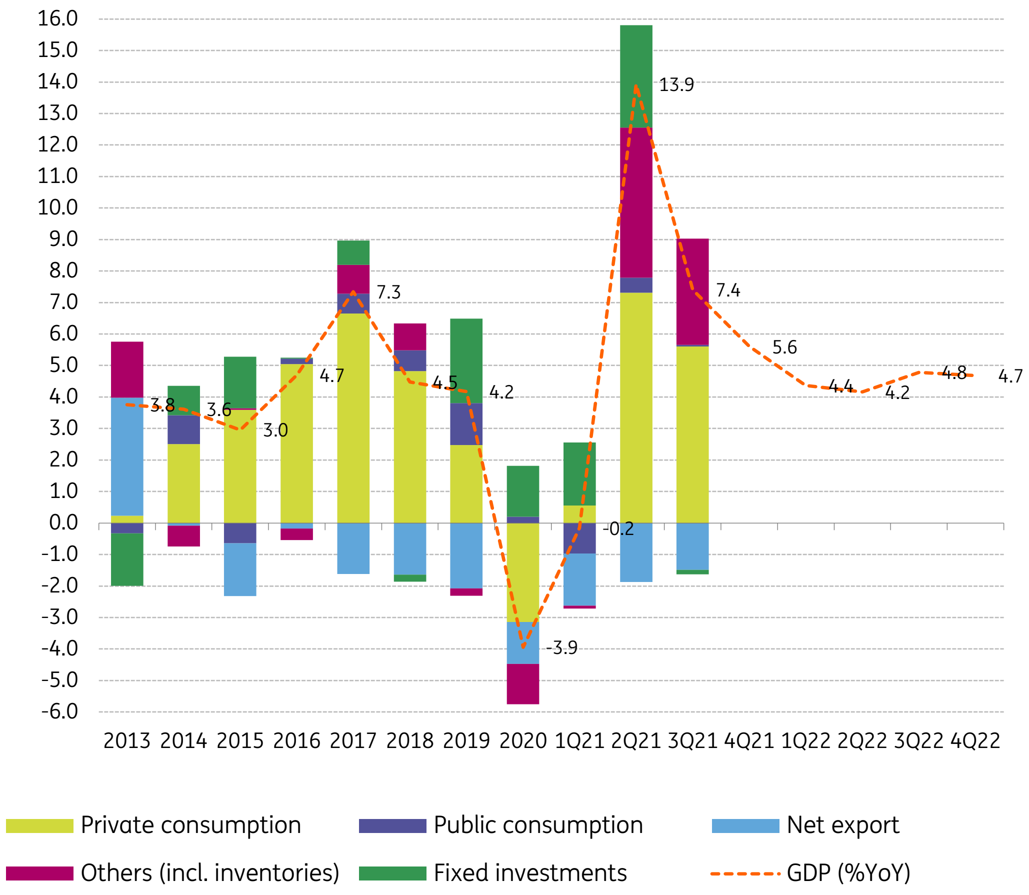
- We remain confident on Romania's growth prospects: **consumption** is resilient and **investments** are set to reach record levels (>7% off GDP) due to large public infrastructure works
- Funds from EU's **Recovery and Resilience Facility** can boost growth by approx. 0.8-1.0pp each year
- Watch out for Omicron variant and political instability

- **Inflation** can touch 9.0% in 2Q22, stay within 7.0%-8.5% in 3Q22 and dip below 6.0% in 4Q22
- We believe that NBR will increase the key rate to at least 3.00% by mid-2022. Risks are to the upside
- **EUR/RON** should remain below 5.00 for most of 2022 and only marginally above it in 2023

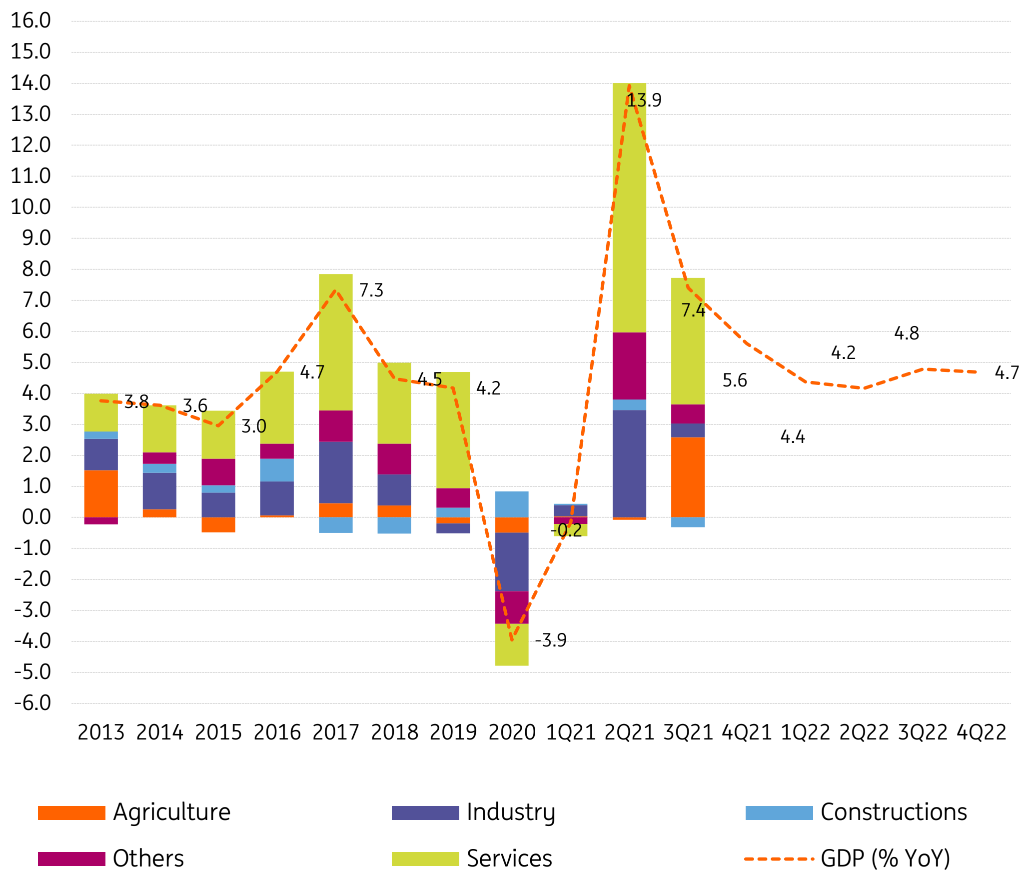
- The labor market was remarkably resilient throughout the crisis
- The number of employees reached an all-time high in 4Q21, pointing to a very tight labor market
- Average wage advances should only marginally exceed the inflation rate over the next couple of years

GDP growth: still robust, but decelerating growth

Investments continue to consolidate but so are the external imbalances

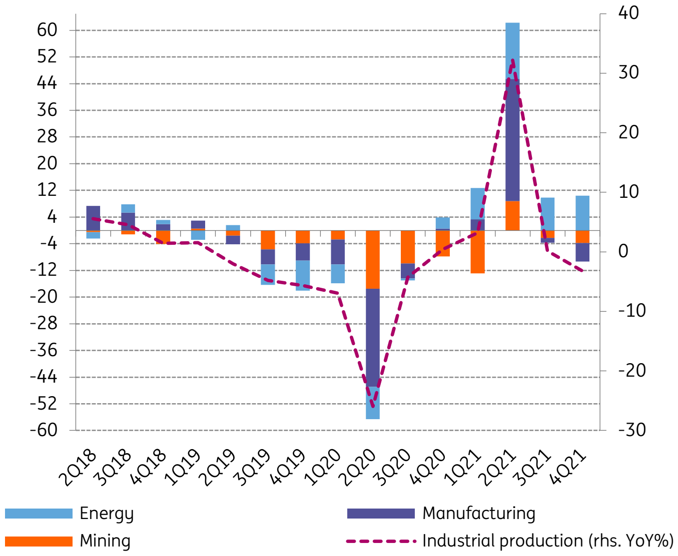


Supply side: pent-up demand driving services

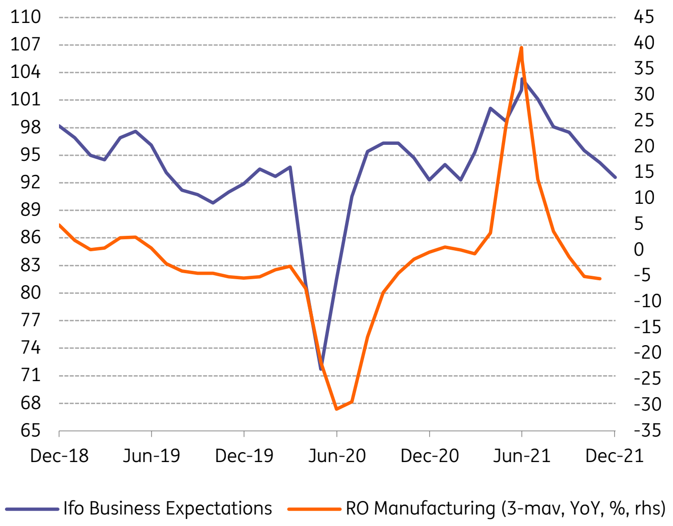


Industrial production flattening

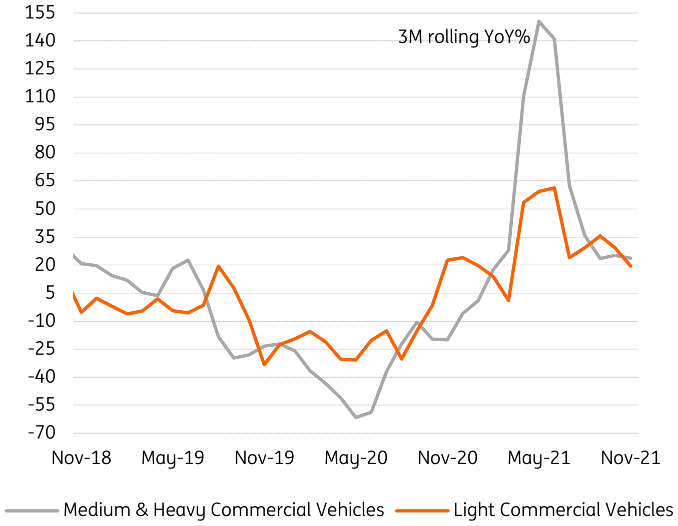
Still lower than pre-covid



External demand not helping either



Vehicle registration still looks growth-supportive



Resuming the contraction

The growth in the energy sector is largely misleading as it is mainly caused by the higher prices

Not what it used to be

German demand used to power local industry but the recovery was rather short-lived

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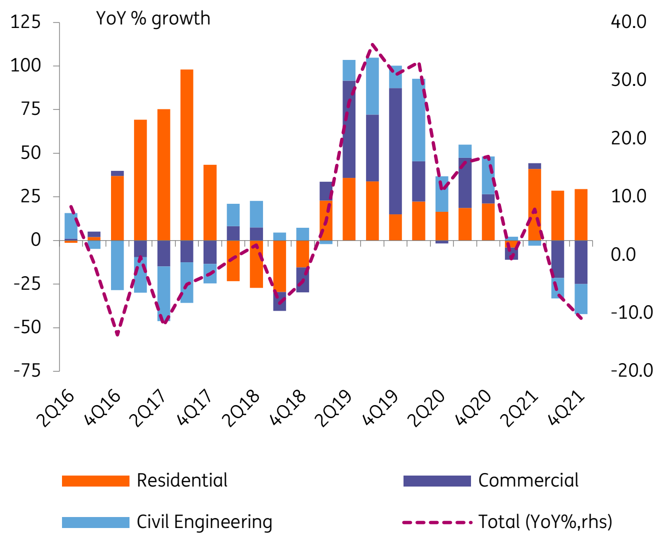
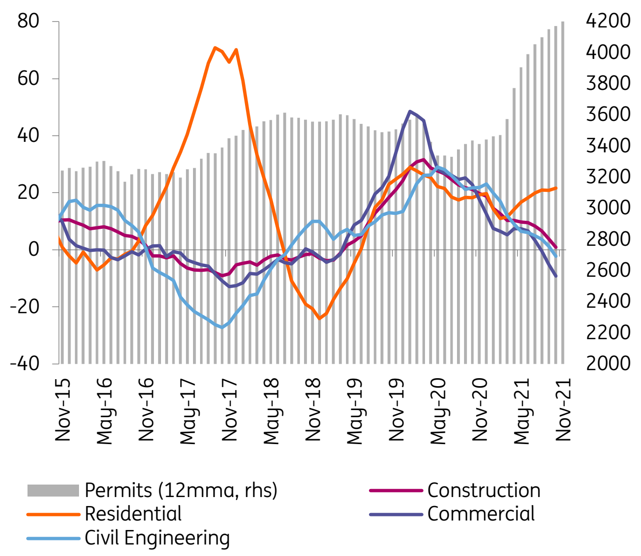
Constructions –normalising growth in 2021

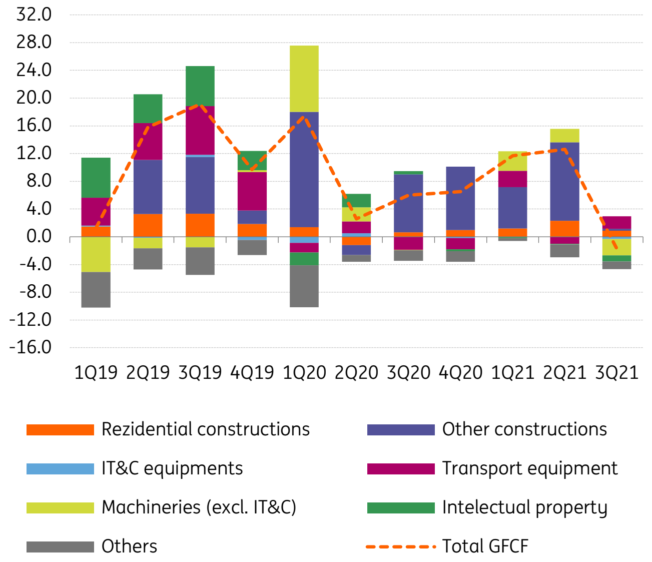
Slowing down to more sustainable levels



New building permits stay strong



Total investments in the economy



More normal growth pace

After a couple of years of high double-digit advance, 2021 marked a normalisation of the growth pace

Public works to keep the flag up

Governments commitment to boosting public investments should act as a backstop for the construction sector

Construction driven

Constructions (mostly non-residential) have kept total investments in green in 2021

Services sector getting used to the Covid-19 waves

Transports

- Usually a leading indicator, it points to a continued recovery into 2022

IT

- Thriving sector - turnover up 25% in year-to-date, as companies boost digitalisation and make work-from-home schemes permanent

Engineering

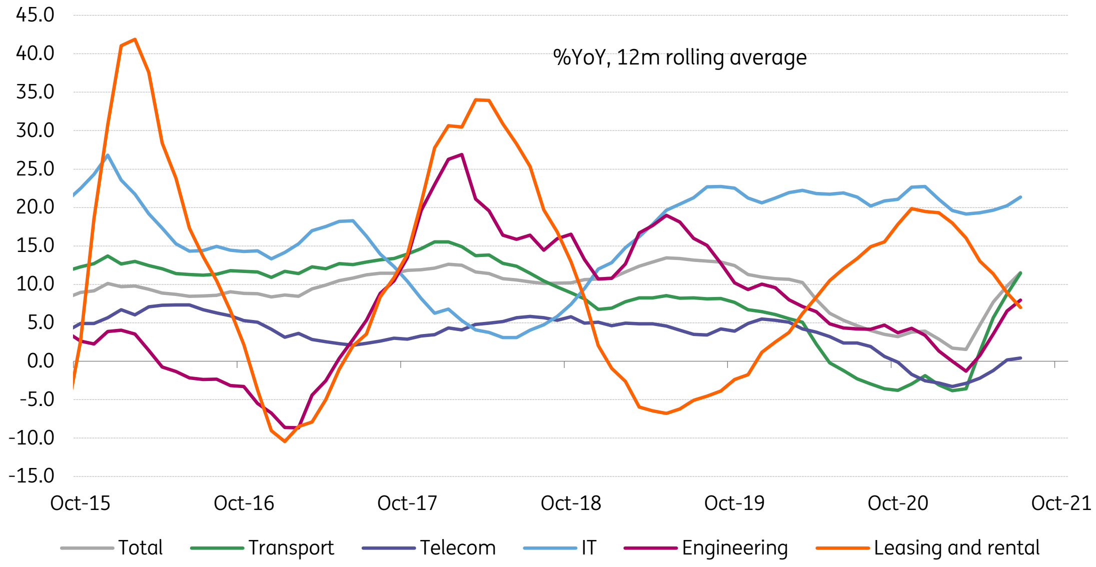
- +16% year-to-date. Normally a good indicator of future investments. Likely to corelate better with public works rather than private investments.

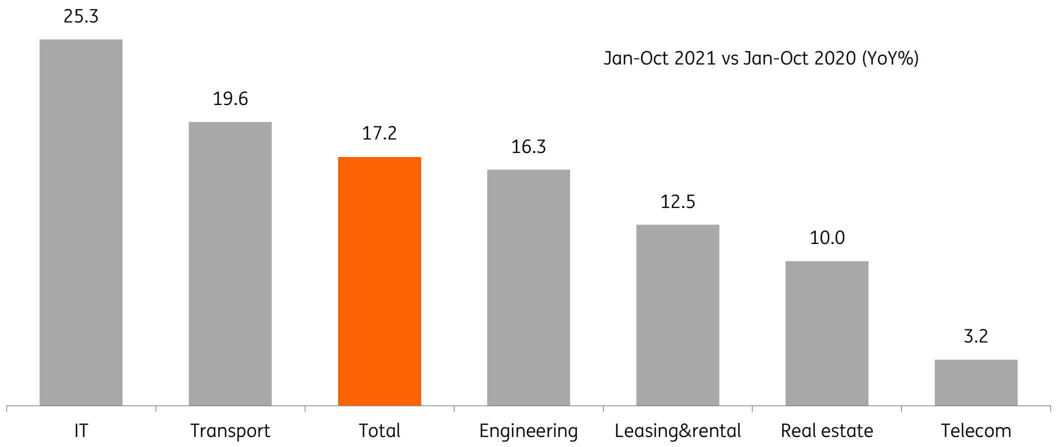
Telecom

- +3% year-to-date, less sensitive to economic cycles

Leasing & rental:

- Cycle-sensitive, it doesn't indicate a prolonged slowdown





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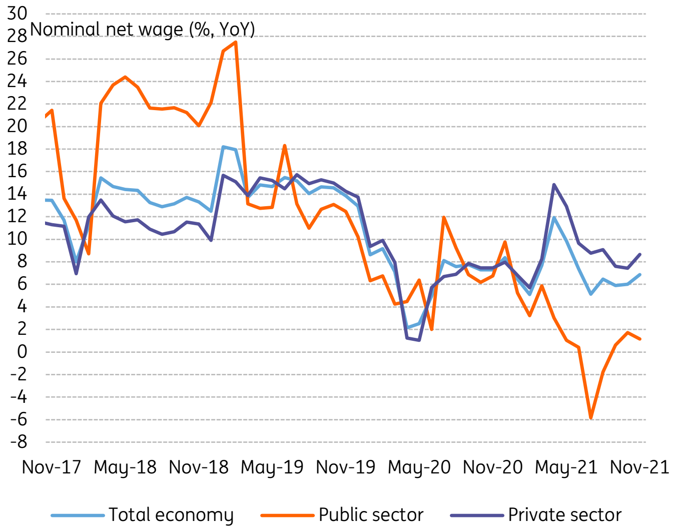
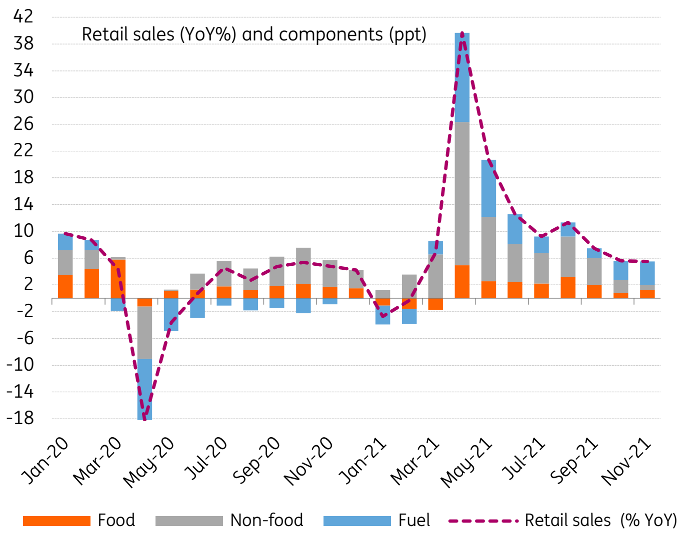
Consumer sector

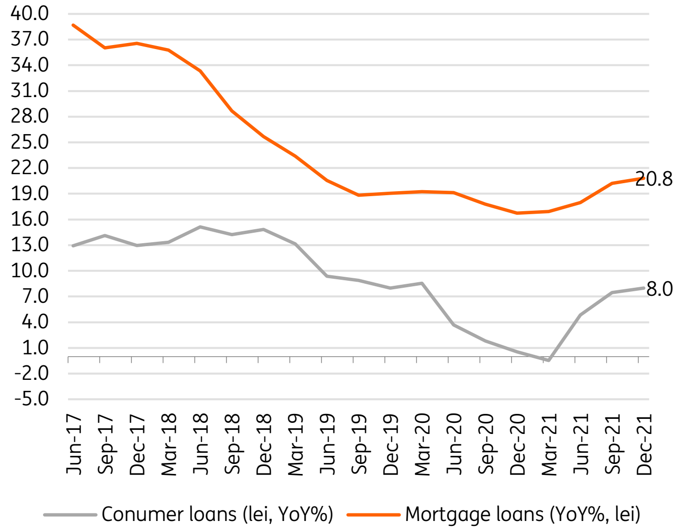
Wage rise only marginally above inflation, if at all



Retail sales by main components



Lending growth - stock (incl. repayments, NPLs)



Real wage growth remains positive…

…but inflation will erode most of the wage gains in 2022 and 2023. The tight labour supply will keep the upward pressure on wages

It's more than just base effects

With pent-up demand exhausted, retail sales are flattening, but a contraction looks unlikely

Lending activity moderates

2021 has been a very good year for consumer and mortgage loans, as interest rates reached new lows. We expect moderation to follow

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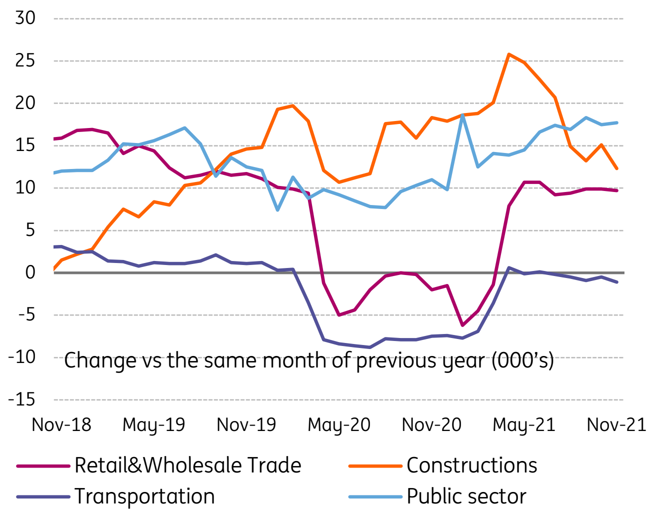
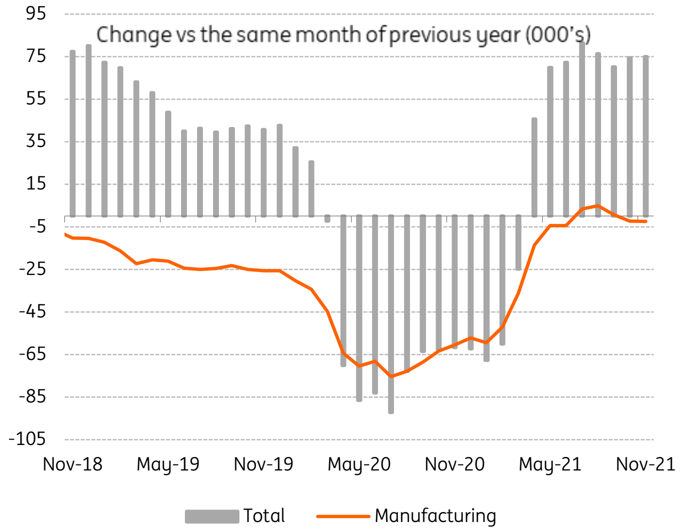
Labour market: remarkably resilient

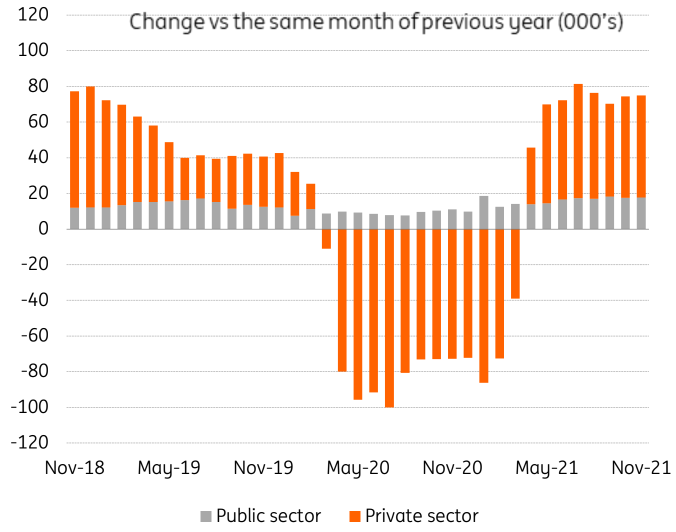
Monthly net job creation - selected sectors



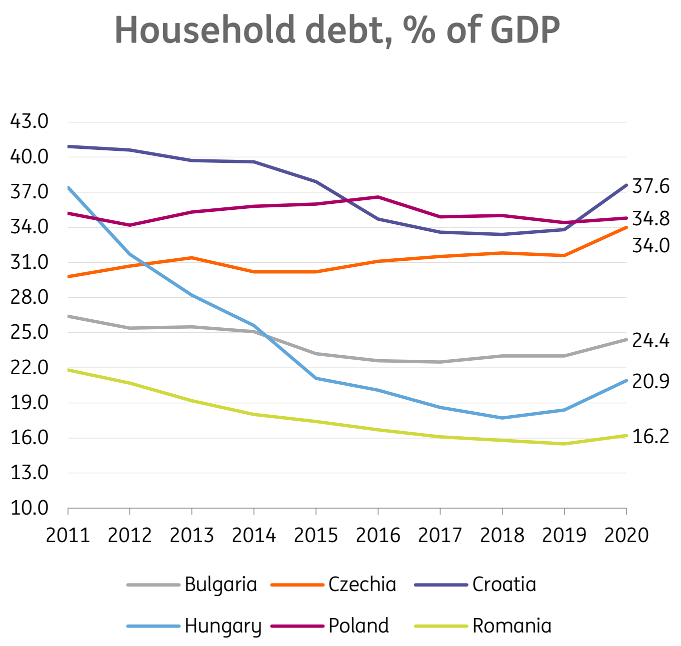
Manufacturing job creation expands for the first time since 2018

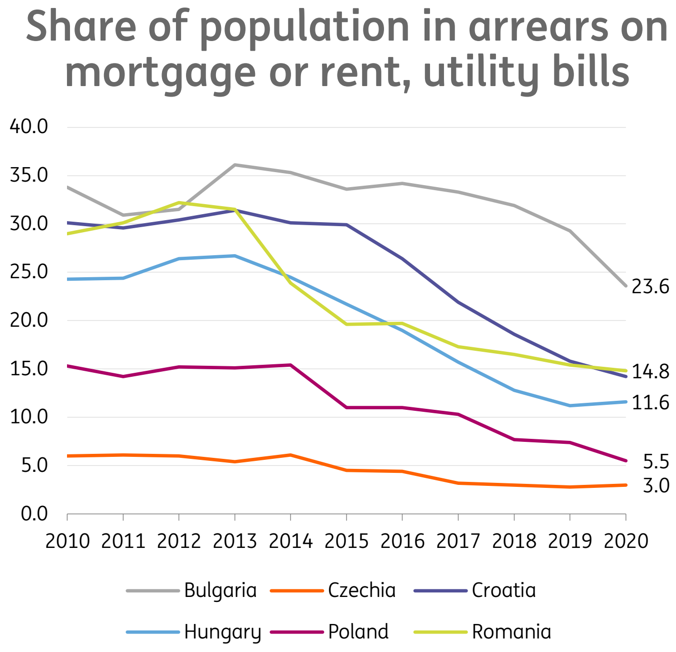


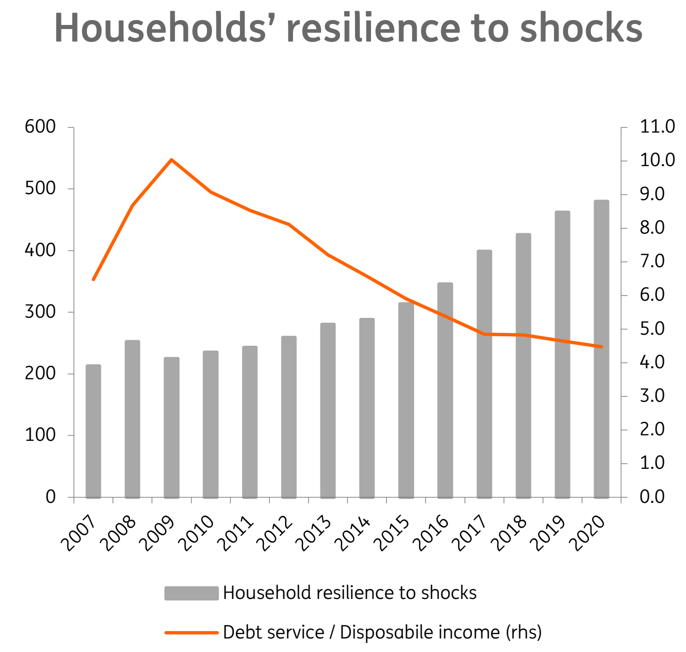
Number of workers in the public sector is still rising

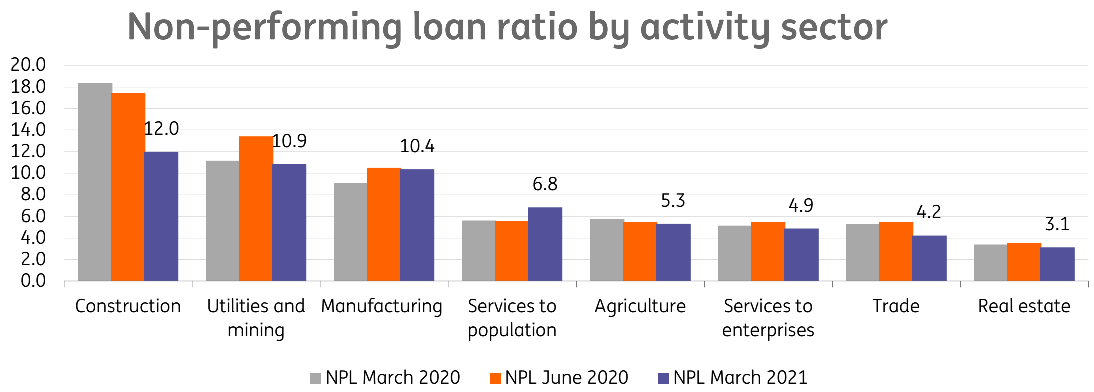


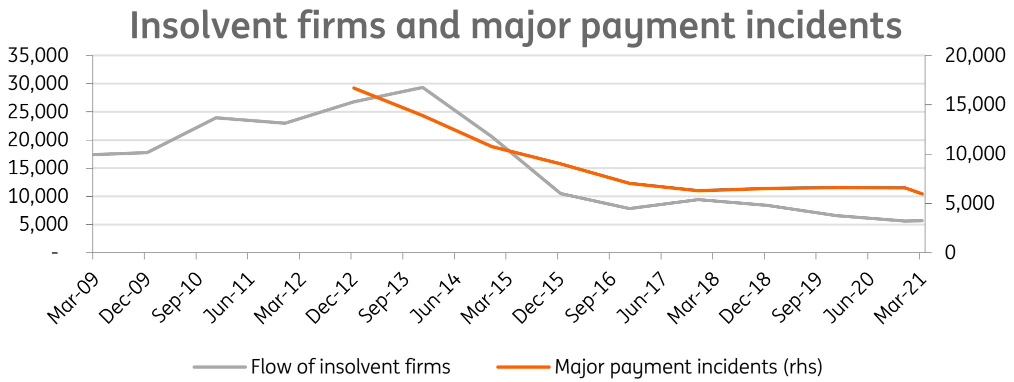
Household's balance sheet continue to improve



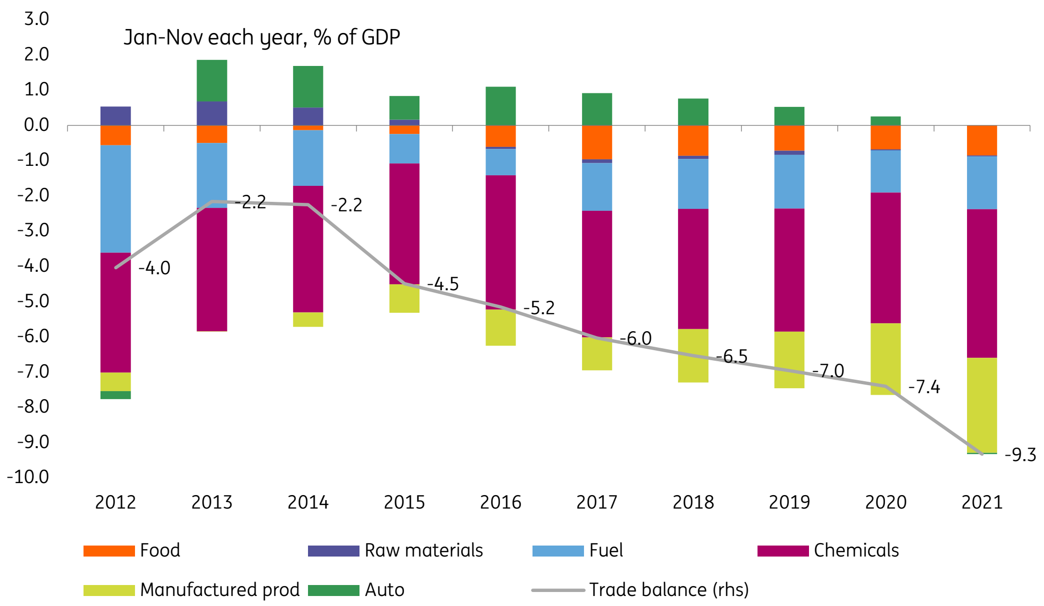


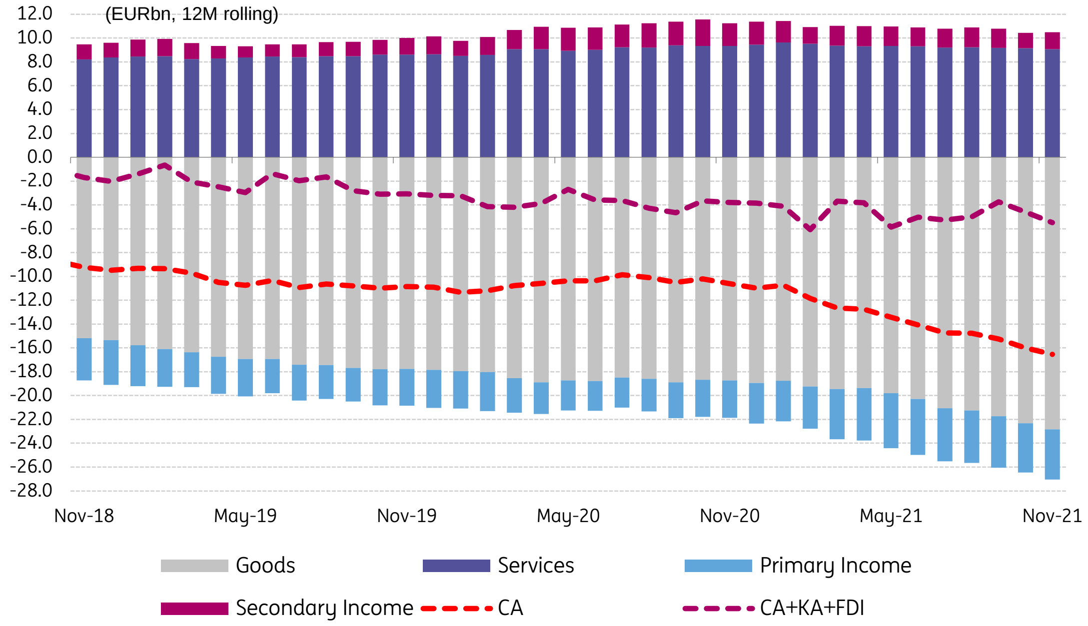






Deteriorating external picture





Trade deficit still widening

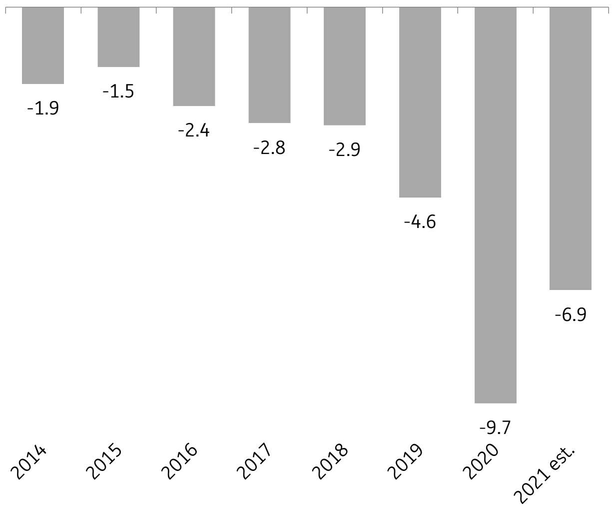
- The surplus on the auto sector has been shrinking constantly, to the point of becoming irrelevant.
- Rebalancing of the trade picture is not taking place. Reliance on imports seems to be have deeper structural fundamentals

Current account deficit to remain a (big) headache

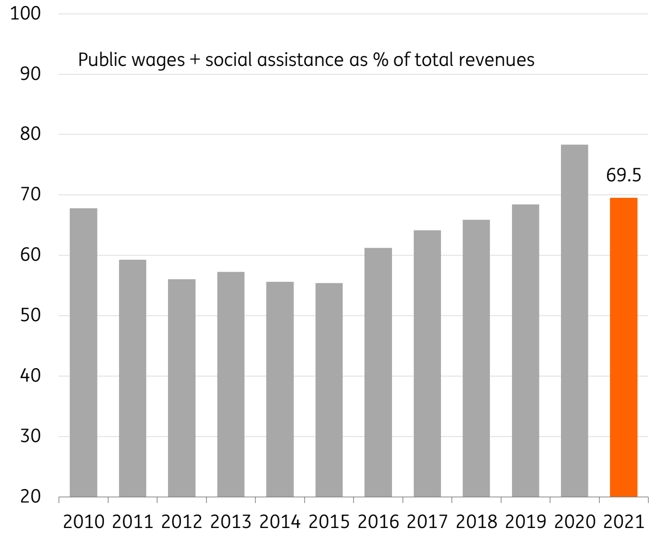
- In the absence of meaningful FDIs, financing the external shortfall remains largely reliant on FX borrowing
- A current account widening during a year of economic contraction is not often heard of
- NGEU funds will alleviate the short to medium-term pressure

Budget deficit: fiscal consolidation not taking off

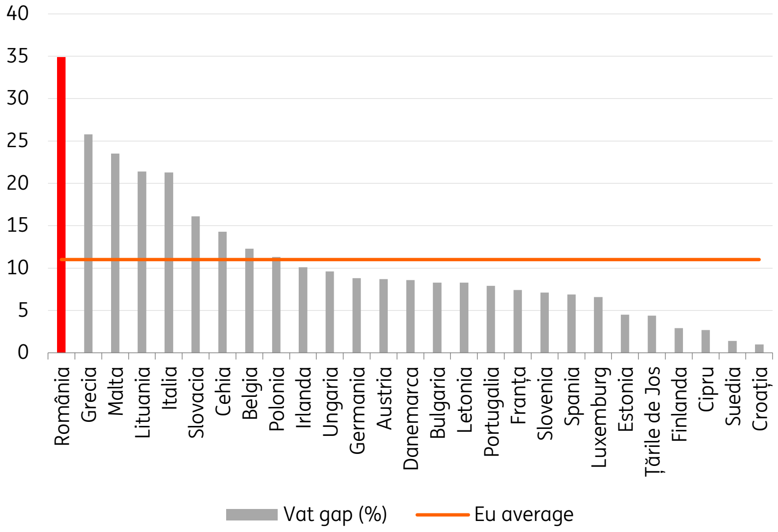
Budget deficit each year (% of GDP)



Rigid spending seizing most resources



Largest VAT gap in Europe



Not as bad…

…as expected. However, the better than expected revenues are being used to increase the nominal deficit

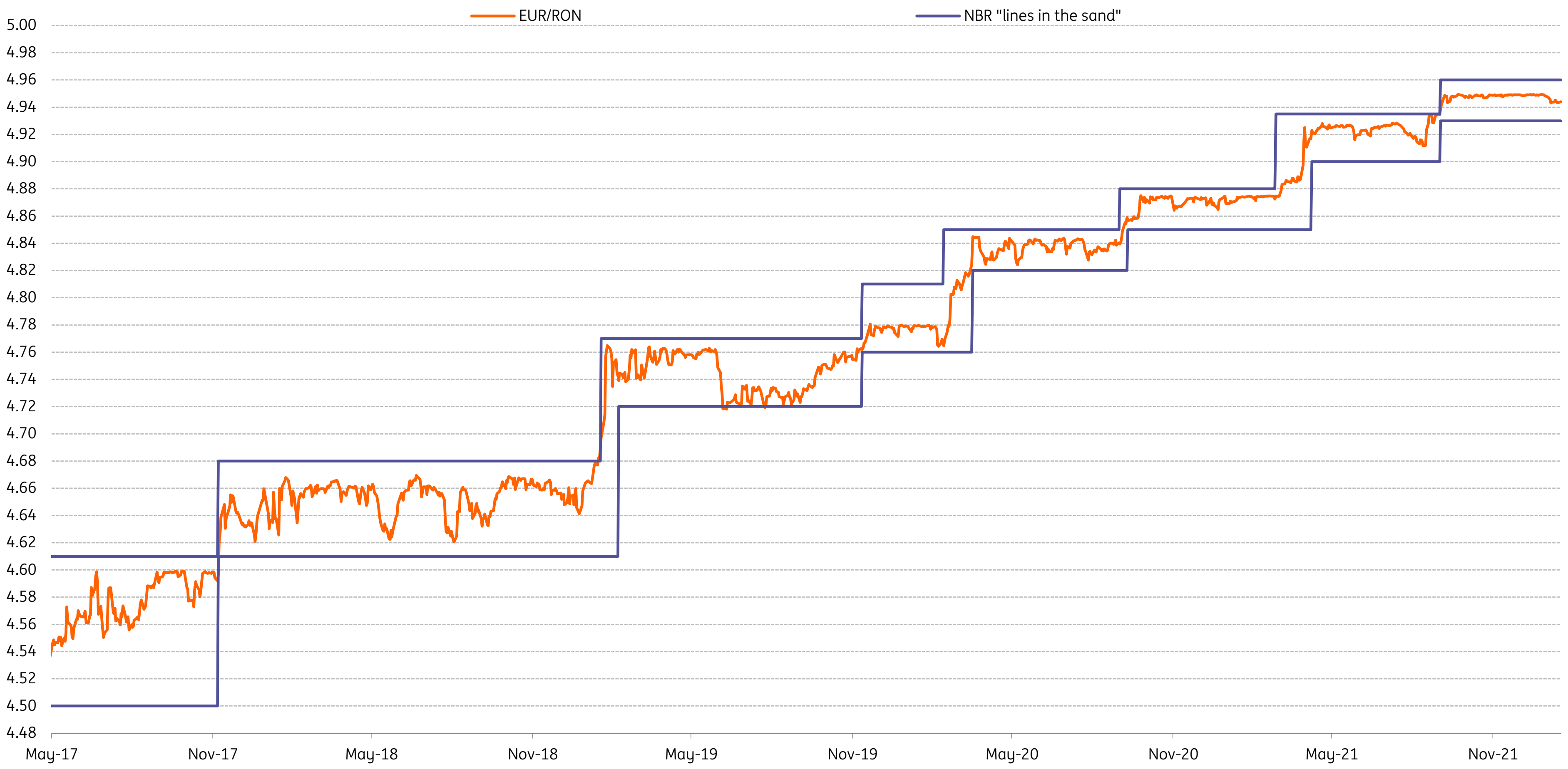
Growth to save the day

With a tighter grip on expenses for the next few years, rapid growth could help dilute the large share of rigid spending

Untacked tax evasion

Low compliance rate, WB program for ANAF declared off-track, large share of self-produced consumption in GDP

EUR/RON: central bank remains hands-on



Ratings: don't take it for granted

Rating drivers/sensitivities, factors that could lead to an upgrade or downgrade

Rating agency	Upgrade factors	Downgrade factors
Moody's Baa3 sta	For outlook back to stable: • Government is successful in halting and – over the medium-term – reversing the structural deterioration in **public finances** In the medium-term: • Structural **fiscal consolidation** supported by higher tax collection and a lower share in current expenditure • Steady reduction in the structural **current-account deficit** and increased coverage by non-debt generating flows, together with a rebalancing towards **higher investment expenditure**	• Continued structural deterioration in **fiscal strength** while **external imbalances** remain at an elevated level, reflecting the medium-term absence of a determined and effective policy response to structural challenges, thus weakening the assessment of **institutional and governance strength**
S&P BBB- sta	• Reforms that strengthen **institutional arrangements** (ie, leading to a more-robust fiscal framework and limiting the potential for costly policy reversal while also revitalising foreign investor interest in Romania's real economy and thus making the sovereign less externally fragile)	• Efforts to rebalance budget endanger the consolidation of its **fiscal and external finances** • **Financing for twin deficits** is oriented toward debt-creating foreign flows (eg, due to inability to absorb EU funding sources and restore FDI flows)
Fitch BBB- neg	• **Fiscal**: Confidence that general government debt/GDP will stabilise over the medium-term (eg, due to effective implementation of expenditure-control reforms and credible plans for revenue raising measures) • **External**: A reduction in external vulnerabilities, for example via a sustained improvement in external debt ratios	• **Fiscal**: Weaker confidence in the implementation of a credible medium-term consolidation strategy that would lead, for example, to a faster-than-projected increase in public debt • **External**: Sustained deterioration in balance of payments (eg, reflecting stronger widening in the CAD and/or failure to attract non-debt financing flows) that undermines external and macroeconomic stability

Source: Moody's, S&P, Fitch, ING

Forecasts

	2021	2022	2023
GDP (%)	6.5	4.5	4.5
Inflation (avg, %)	5.0	7.0	4.0
Unemployment (ye, %)	5.2	4.8	4.6
Avg. wage growth (%)	7.0	7.0	6.0
NBR key rate (ye, %)	1.75	3.00	3.00
10Y Yield (ye,%)	5,50	5,40	5,20
Budget deficit (ye, %)	-7.1	-5.8	-4.3
EUR/RON (ye)	4.95	5.00	5.05

think.ing.com/forecasts

Romania

	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021F	2022F	2023F
Activity													
Real GDP (%YoY)	1.9	2.0	3.8	3.6	3.0	4.7	7.3	4.5	4.2	-3.9	6.5	4.5	4.5
Private consumption (%YoY)	1.5	1.8	0.5	4.6	5.8	8.2	9.8	10.1	6.0	-3.8	7.0	4.0	4.5
Government consumption (%YoY)	-1.2	7.4	-1.6	6.1	-3.8	0.0	4.4	3.3	6.0	2.0	1.9	2.0	2.0
Investment (%YoY)	6.1	3.1	-5.9	3.8	7.0	-0.1	3.5	2.5	-2.6	6.8	8.0	8.0	9.0
Industrial production (%YoY)	8.1	3.0	7.7	6.4	2.7	3.1	8.7	4.4	-3.2	-9.5	6.5	3.0	3.0
Unemployment rate (year-end, %)	7.1	6.9	7.0	6.8	6.8	5.9	5.0	4.2	3.9	5.0	5.2	4.8	4.6
Nominal GDP (RONbn)	559	592	635	670	712	764	858	952	1058	1055	1190	1310	1410
Nominal GDP (€bn)	132	133	144	151	160	170	188	205	223	218	241	264	282
Nominal GDP (US$bn)	185	171	191	199	176	187	214	241	250	251	282	295	316
GDP per capita (US$)	9200	8600	9600	10000	8900	9500	11000	12500	13000	13000	14700	15500	16800
Gross domestic saving (% of GDP)	22.3	21.8	24.8	24.2	24.5	22.4	21.0	19.4	19.1	20.1	21.8	21.8	21.8
Prices													
CPI (average, %YoY)	5.8	3.3	4.0	1.1	-0.6	-1.6	1.3	4.6	3.8	2.9	5.0	7.0	4.0
CPI (year-end, %YoY)	3.1	5.0	1.6	0.8	-0.9	-0.5	3.3	3.3	4.0	2.1	8.0	5.3	3.5
Wage rates (nominal, %YoY)	5.0	5.0	5.0	5.3	8.4	13.0	14.2	13.1	14.9	6.7	7.0	7.0	6.0
Fiscal balance (% of GDP)													
Consolidated government balance	-5.4	-3.7	-2.1	-1.2	-0.6	-2.6	-2.6	-2.9	-4.4	-9.8	-7.1	-5.8	-4.3
Consolidated primary balance	-3.8	-1.9	-0.3	0.5	1.0	-1.1	-1.4	-1.8	-3.2	-8.6	-6.8	-5.4	-4.0
Total public debt	34.0	37.1	37.6	39.2	37.8	37.4	35.1	34.7	35.3	47.3	52.0	53.2	54.5
External balance													
Exports (€bn)	45.3	45.0	49.6	52.5	54.6	57.4	62.6	67.4	68.7	56.8	74.0	81.0	86.0
Imports (€bn)	54.9	54.6	55.3	58.6	63.0	67.4	75.6	82.8	86.2	80.5	95.0	104.0	110.0
Trade balance (€bn)	-9.7	-9.6	-5.8	-6.1	-8.4	-10.0	-13.0	-15.4	-17.6	-19.3	-21.0	-23.0	-24.0
Trade balance (% of GDP)	-7.3	-7.2	-4.0	-4.0	-5.2	-5.9	-6.9	-7.5	-7.9	-8.7	-8.6	-8.6	-8.4
Current account balance (€bn)	-6.6	-6.4	-1.5	-1.0	-2.0	-3.6	-6.0	-9.2	-10.2	-11.3	-15.8	-16.0	-15.8
Current account balance (% of GDP)	-5.0	-4.8	-1.1	-0.7	-1.2	-2.1	-3.2	-4.5	-4.6	-5.1	-6.5	-6.0	-5.5
Net FDI (€bn)	1,8	2,1	2,9	2,7	2,9	4,8	4,8	4,9	4,8	2,9	5,2	3,2	3,3
Net FDI (% of GDP)	1,4	1,6	2,0	1,8	1,8	2,8	2,6	2,4	2,2	1,3	2,1	1,2	1,2
Current account balance plus FDI (% of GDP)	-3,6	-3,2	0,9	1,1	0,6	0,7	-0,6	-2,1	-2,4	-3,7	-4,4	-4,8	-4,4
Foreign exchange reserves ex gold (€bn)	33.2	31.2	32.5	32.2	32.2	34.2	33.5	33.1	32.9	37.4	40.3	42.1	43.8
Import cover (months of merchandise imports)	7.2	6.9	7.1	6.6	6.1	6.1	5.3	4.8	4.6	5.9	5.1	4.9	4.8
Debt indicators													
Gross external debt (€bn)	99.9	100.9	98.1	94.7	92.1	92.9	97.4	99.8	109.8	126.8	135.0	138.0	140.0
Gross external debt (% of GDP)	75	72	69	63	57	54	51	48	48	58	55	52	49
Gross external debt (% of exports)	221	224	198	180	169	162	156	148	160	223	182	170	163
Lending to corporates/households (% of GDP)	39.2	39.5	37.9	34.3	31.7	30.5	28.9	27.2	26.7	25.5	25.7	25.9	26.5
Interest & exchange rates													
Central bank key rate (year-end, %)	6.25	6.00	5.25	4.00	2.75	1.75	1.75	1.75	2.50	1.50	1.75	3.00	3.00
Broad money supply (average, %YoY)	6.2	6.2	7.9	4.1	6.8	7.8	11.4	11.1	9.3	13.7	16.0	9.0	9.0
3m interest rate (Robor average, %)	5.82	5.34	4.22	2.54	1.40	0.89	1.15	2.80	3.15	2.38	1.79	3.20	3.25
3m interest rate spread over Euribor (ppt)	4.4	4.8	4.0	2.3	1.4	1.2	1.5	3.1	3.5	2.8	2.3	3.7	3.7
5yr yield (average, %)	7.2	6.3	4.8	3.3	1.9	1.5	1.9	3.7	3.7	3.5	3.50	5.00	4.80
10yr yield (average, %)	7.4	6.7	5.3	4.6	3.5	3.3	3.9	4.7	4.8	4.2	3.90	5.50	5.30
USD/RON exchange rate (year-end)	3.32	3.36	3.27	3.70	4.15	4.32	3.88	4.07	4.26	3,97	4,27	4,55	4,39
USD/RON exchange rate (average)	3.03	3.45	3.32	3.37	4.04	4.08	4.01	3.94	4.24	4,24	4,21	4,44	4,48
EUR/RON exchange rate (year-end)	4.32	4.43	4.48	4.48	4.52	4.54	4.66	4.66	4.78	4,87	4,95	5,00	5,05
EUR/RON exchange rate (average)	4.24	4.46	4.42	4.44	4.45	4.49	4.57	4.65	4.75	4,84	4,93	4,97	5,02

Source: National sources, ING estimates

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