# Romania

B3

**Sensitive**
risk for enterprises

## Macroeconomic imbalances remain a concern

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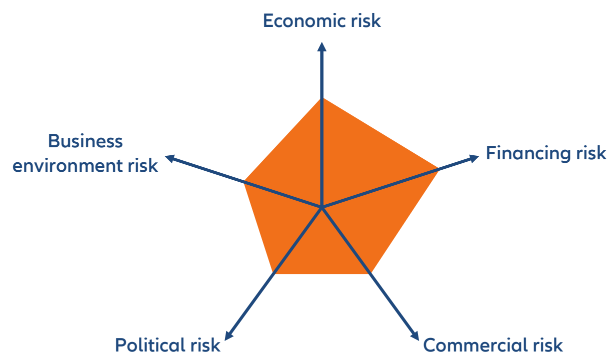
|---|---|
| **GDP** | USD351.0 (World ranking 43) |
| **Population** | 19.1mn (World ranking 65) |
| **Form of state** | Republic |
| **Head of government** | Marcel Ciolacu (Prime Minister) |
| **Next elections** | 2025, Presidential |




## Strengths & weaknesses

- EU membership and good international relations
- Competitive industrial sector
- Low unemployment
- Adequate business environment

- Government instability
- Lack of structural reforms in key economic sectors
- Weak public finances
- Large annual current account deficits, with modest coverage through net FDI inflows
- High external debt burden

## Economic overview

### Moderate growth and sticky inflation

Romania has been a strong performer among emerging economies, though periods of economic overheating have caused concern at times. Average annual real GDP growth was +3.7% over the past 20 years, well above the respective average of the Central and Eastern European EU member states. The global Covid-19 crisis affected the Romanian economy markedly in 2020 (-3.7% contraction), but it rebounded strongly with a +5.7% output increase in 2021. However, Romania's economic prospects have significantly deteriorated since the war in Ukraine. This is due to the country's (pre-war) energy import-dependence on Russia and the impact of EU sanctions against Russia on the domestic economy (for example increased inflation and potential energy shortages). In 2022, economic activity in Romania still held up better than initially expected, thanks to robust consumer spending, investment and external demand. Statistical base effects also helped to achieve growth of +4.1% annually. However, the impact of surging inflation, rising interest rates, weakening external demand and deteriorating business confidence took full effect thereafter. As both domestic and external demand slowed down, real GDP grew by just +2.1% in 2023. In 2024, growth reached an average of +1.4% in the first half of the year, but fell into recession at -0.3% in Q3, ending with an overall growth of +0.8% for the full year. Going forward, growth is forecast to pick up gradually to +3.1% in 2025 and 3.6% in 2026, supported by resilient public spending and investment as well as strengthening consumer spending on the back of rising real disposable income, the fading impact of past interest rate hikes and some monetary easing.

Monetary policy by the National Bank of Romania (NBR, the central bank) is officially based on inflation targeting (2.5% ± 1pp) but has been loose for a long time. The real interest rate was negative from end-2017 to October 2023, i.e., the key policy interest rate was below the inflation rate, even when the latter was above the target range for most of 2018-2019 amid rapid double-digit wage growth, and again since mid-2021 amid rising energy prices. The latter drove consumer price inflation into double digits from early 2022 until mid-2023. The NBR hiked its policy rate moderately from 1.25% in September 2021 to 7.00% in January 2023. Romania then began a rate-cutting cycle in July 2024, gradually lowering the policy rate, which currently stands at 6.5%. It has also frequently intervened in foreign exchange (FX) markets to prevent excessive currency volatility – not surprising as the official exchange rate regime is that of a managed float – thereby maintaining the exchange rate of the RON stable against the EUR. We expect it to continue to do so as long it has sufficient FX reserves. Meanwhile, inflation is forecast to remain stickier than in neighboring countries on the back of hikes in food prices, strong wage growth and loose fiscal policies. Inflation remained at 5.6% in 2024 but will fall gradually to 4.5% in 2025 and 3.4% in 2026. .

### Worrisome public and external finances

Romania's public finances will continue to deteriorate and have become a cause for concern. Strong pro-cyclical fiscal stimulus already widened the annual fiscal deficit to -4.3% of GDP in 2019. That ratio rose sharply to -9.3% in 2020 and -7.2% in 2021 because of Covid-19-related fiscal stimulus and loan guarantees and subsidies for SMEs, as well as lower nominal GDP. Further large annual fiscal shortfalls of more than -6% of GDP were posted in 2022-2023, this time due partly to lower fiscal revenues as well as higher spending needs in the wake of the crisis sparked by the war in Ukraine. Despite some planned fiscal consolidation, the annual deficits are forecast to remain high at more than -5% of GDP in 2024-2026. Meanwhile, the public debt-to-GDP ratio increased from 35% of GDP in 2019 to 49% in 2023 and is forecast to exceed 50% in 2024-2026. While this still appears moderate compared to other EU countries, the trend dynamics are a reason to worry.

Romania's external finances are another cause for concern. The annual current account deficit widened steadily from -0.3% of GDP in 2014 to -9.3% in 2022 and has remained high at over -7% in 2023-2024. Crucially, only some 30% of the combined shortfall in the last two years was financed through net foreign direct investment (FDI) inflows, well below the comfortable level of 75% and down from a recent high of 168% in 2016. Looking ahead, we expect exports and imports to grow at similar rates in 2025-2026 so annual current account deficits should remain large at above -6% of GDP in this period. The net FDI coverage of the deficits is likely to remain below 50% as capital flows to (weaker) emerging markets will remain muted amid ongoing global economic headwinds. Combined with the projected high fiscal deficits, this could raise external financing needs to critical levels. Moreover, the downtrend in the external-debt-to-GDP ratio from 77% of GDP in 2011 to 47% in 2019 has reversed; the ratio came in at 57% in 2020 and should remain above 50% in the next few years. Meanwhile, the NBR's FX reserves have increased again from temporary lows in 2022, although the aforementioned exchange-rate interventions cause some volatility in the level. At USD70bn in August 2024, reserves covered about five months of imports, which is considered an adequate ratio. In other terms, however, they do not cover all external debt payments falling due in the next 12 months (well below the benchmark "comfort" level of 125%).

### Above average business environment but high political uncertainties

The business environment is generally adequate though spots of weaknesses remain. The World Bank Institute's annual Worldwide Governance Indicators surveys suggest that the regulatory and legal frameworks are generally business-friendly while weaknesses remain with regard to perceived corruption. The Heritage Foundation's Index of Economic Freedom survey 2024 assigns Romania rank 51 out more than 180 economies, reflecting strong scores with regard to property rights, tax burden, trade freedom and investment freedom. However, weaknesses remain in the areas of government integrity and financial freedom. In our proprietary Environmental Sustainability Index, Romania ranks 54th out of 210 economies, reflecting strong scores for energy use and CO2 emissions per GDP, and water stress. Yet, there are still weaknesses in renewable-electricity output and the recycling rate, as well as its exposure to climate events and its readiness to protect itself against such events.

Overall systemic political risk is moderate. Romania is a democracy with good international relations. It is a member of the EU and NATO and an OECD accession candidate. But political uncertainty has reached high levels, significantly impacting prospects for fiscal consolidation. In December 2024, the Constitutional Court annulled the presidential election amid allegations of foreign interference, prompting new presidential elections in spring 2025. A new pro-European coalition government of four parties has been formed, though its stability remains uncertain.