

## Romania: harsh realities

The reality of the Covid-19 crisis will bite severely into the real economy. We see GDP contracting by 6.6% in 2020, with a second quarter to forget, followed by a less pronounced “V-shaped” recovery than previously expected



Source: Shutterstock

In these turbulent times, economic forecasts have become even less of an exact science than they were before. In all fairness, we are facing an unprecedented situation, with a sudden large-scale shutdown of almost all economic sectors, for reasons that go beyond - in fact have nothing to do with - economics. Nevertheless, faced with the avalanche of revisions to macroeconomic indicators, one cannot help but recall Ezra Solomon's words that “the only function of economic forecasting is to make astrology look respectable”.

### Growth

So far, the socio-economic developments that Romania is experiencing seem to fit the general picture of most countries at a similar stage of the pandemic: from general warnings to schools closing, factories closings and increasingly tough travel restrictions. And while we still don't have much data to assess the economic impact, the first estimates we're getting from confidence surveys and economic actors converge on the same conclusion: in the course of only a few weeks

we will experience a contraction that normally would have taken a few bad years to materialise. Considering that a [-4.0% contraction in Germany](#) has just become the most optimistic scenario, and that France is losing roughly the equivalent of [3 percentage points of GDP per month](#) of lockdown, Romania's position is unlikely to look any better.

While the specialised literature on this topic is not lacking (few examples [here](#), [here](#), or [here](#)), the magnitude and rapidity of current developments is unprecedented. For the purpose of our forecast, we assumed a neutral impact of otherwise volatile factors like agriculture, net taxes or statistical discrepancies. In general, we consider the agriculture, pharma and IT&C sectors as being the ones less impacted by the current crisis.

We believe that GDP contraction will begin in 1Q20 and estimate a -1.3% drop vs 4Q19 (+1.7% vs 1Q19), despite the probably strong first two months. The bulk of the current anti-pandemic measures will be visible in 2Q20, where we see a -19.7% contraction vs 1Q20 (-19.1% vs 2Q19), with the main drags coming from industry and trade. This assumes a gradual re-opening of the economy starting in late May and, by the end of June, we expect the conditions to restart growth engines to be met, prompting a third quarter advance by +17.0% vs the second one. It might seem a sharp rebound but it comes from a low base. The year-on-year dynamics will remain deeply negative at -5.9%. Benefiting from a relatively low base as well, we see the fourth quarter expanding by 4.4% compared to the previous one, while still contracting by 3.2% vs 4Q19. This will create quite a strong carry-over effect for 2021, when we see GDP accelerating by 7.1%.

## Fiscal impact

An even more erratic indicator for 2020 is – in our view – the year-end fiscal gap which we think could land anywhere between 7 and 9% of GDP. It depends not only on the already difficult to predict GDP dynamics, but also on how revenues will perform in this unprecedented situation. Under other circumstances, we would have assumed the budget sensitivity to GDP growth to be around 0.3 as per the European Commission's latest data, but applied to the current unique context of a widespread economic freeze, we tend to believe that this metric is somewhat underestimated. We are therefore pinpointing a -7.9% budget deficit for 2020, acknowledging that there are many unknowns at this stage.

## FX, rates and inflation

After the latest [decision from the National Bank of Romania](#) taken at an emergency meeting, one might have imagined that the NBR's policy would gradually become less FX-focused. We are rather doubtful about that and do not share the current market views of more aggressive rate cuts from the NBR. However, to the extent the (lack of) FX pressures will allow, we believe that the key rate could reach 1.50% by the end of the year, with the same  $\pm 0.5$ pp corridor around the key rate. Also, we believe that reserve requirements for hard currency and RON will be cut by at least 2 percentage points each. We maintain our year-end forecast for the EUR/RON at 4.8800 and inflation at 2.5%. All in all, we believe that the NBR is able to keep things under control due to its still large FX reserves, but pressures for something to give in will remain.

Closing this piece on a similar note as we started, we take the opportunity to recall JK Galbraith's words: "In economics, hope and faith coexist with great scientific pretension and also a deep desire for respectability".

## Author

**Valentin Tataru**

Chief Economist, Romania

[valentin.tataru@ing.com](mailto:valentin.tataru@ing.com)

## Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies).* The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit [www.ing.com](http://www.ing.com).