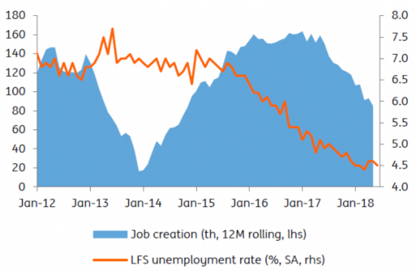
Romania: Labour market still hot

The unemployment rate in June came in near an all-time low, but labour market participation also remains low and underemployment is high. Hence, the market is not as hot as in other central and eastern European countries

June unemployment came in at 4.5% down 0.1 percentage point from the previous month and just 0.1 percentage point higher than the historical low reached in March this year. The labour market in Romania is in desperate need of reform in order to further support economic growth.

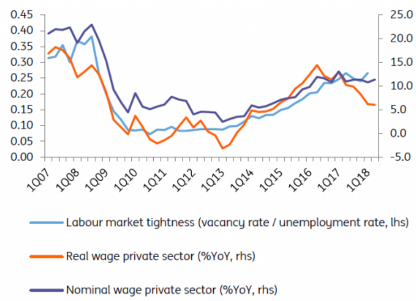
Reforms could address the obvious demand/supply mismatch as measured by the labour market tightness indicator. This is the ratio between the vacancy rate and the unemployment rate that keeps pressure on nominal wages and competitiveness in the private sector. Wage pressures are likely to intensify, as inflation bites into real incomes and higher wages in the public sector potentially lead to workforce migration from the private sector. Add to this a continuous decline in 12-month job creation and the outlook for growth remains somewhat subdued.

Fig 1 Jobless rate bottoming out, job creation slowing



Source: NIS, ING

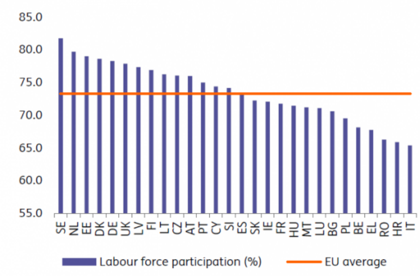
Fig 2 Inflation biting into wages despite tight job market



Source: NIS, ING

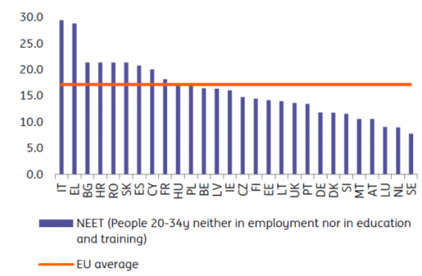
Reforms are also needed to target one of the lowest labour force participation rates (66.3% for 1Q18) in the EU, which can be attributed to a number of reasons ranging from low mobility, outdated skills and lack of proper retraining and reintegration into the labour force, lack of career advice and in some anecdotal cases, generous social benefits which can reduce the incentive to work. Romania has one of the largest percentages of young NEET people (neither in employment, education or training), which needs to be addressed. But these issues are not only about the labour market. They're also related to other factors such as social inclusion and the education system, which continues to score poorly in OECD surveys.

Fig 3 Low participation a backstop if addressed...



Source: Eurostat, ING

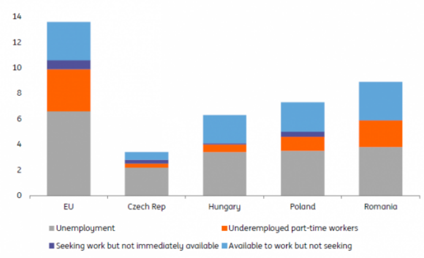
Fig 4 ... especially among the younger people



Source: Eurostat, ING

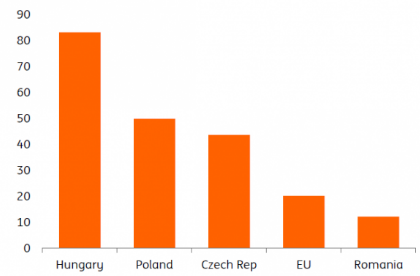
Contrary to anecdotal evidence, a European Commission survey reported that only a small percentage (12.2% of total surveyed) of Romanian companies in manufacturing have complained that labour is a factor limiting production. This may be because there is a significant share of the labour force which is either underemployed or available to work but not seeking a job. Still, the reported figure seems way out of the central and eastern European norm.

Fig 5 There are still some untapped resources



Source: Eurostat, ING

Fig 6 Labour as a factor limiting the production in manufacturing (% of total)



Source: EC, ING

To sum up, the labour market is turning into a hindrance for the growth outlook. Job creation is slowing down as the economy is running out of people to hire following a period of stagnant labour market reform. At the same time, the tight labour market, exacerbated by official wage policies, is likely to remain a risk to the inflation outlook.

Recent data, which points to an economy shifting into a lower gear and CPI topping out, needs to be considered by the central bank before it decides to hike rates further. In the meantime, a firmer Romanian leu and higher interest rates driven by tighter liquidity have led to a less accommodative monetary policy stance. This provides the central bank with more flexibility in case the economy slows down more than expected.

We expect the National Bank of Romania to keep its key rate on hold at 2.50% at the 6 August rate-setting meeting and expect it to leave the tightening cycle open for one more hike this year at one of the two remaining meetings, most likely on 3 October, provided that the economy does not decelerate further. A clear risk and uncertainty is related to fiscal policy and the NBR might want to wait for the budget revision plans to be announced before reassessing its outlook.

Author

Ciprian Dascalu
Chief Economist, Romania
+40 31 406 8990
ciprian.dascalu@ing.com