We're lowering our Romanian growth forecasts

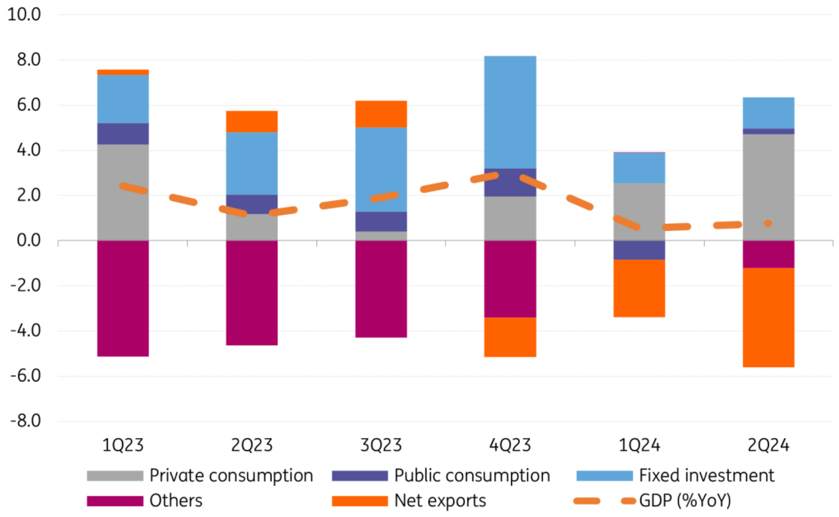
While private consumption and investments were again strong positive drivers for the second quarter's 0.8% annual growth, the Romanian economy is performing poorly at not letting the benefits of strong activity dissipate externally through imports. This is weighing visibly on growth. We are revising our 2024 growth forecast lower from 2.0% to 1.3%

Restoration work on the Palace of the University of Bucharest

Today's data for the second quarter of 2024 reconfirms the first reading's negative surprise. Private consumption annual growth picked up visibly, broadly in line with what retail sales data had already been signalling. Its overall positive contribution to growth was a solid 4.9pp to the total of 0.8% GDP growth. And as far as investment growth is concerned, it's still at robust levels, but it's slowing, contributing to GDP growth by 1.4pp.

But here's the stinger: net exports wiped out most of the gains, subtracting a whopping 4.4pp. The strong internal demand boosted imports, subtracting 3.0pp from growth, while weak external demand led exports to subtract the remaining 1.4pp.

Net exports' negative growth contribution is increasing



Source: NSI, ING

It's clear that strong private consumption momentum and loose fiscal policy are generating a stimulus that is spreading primarily outside the local economy to the benefit of the country's trading partners. While there is also a rapid investment boom, consisting of multiple large-scale projects with tight deadlines, this is also showing up in higher imports as the local supply side cannot match the demand.

Moreover, the fact that almost all of last year's trade balance gains were lost as a result of the strong response of consumers to their wage increases shows that Romania's structural supply-demand imbalances still have a long way to go before they can improve. The leu's overvaluation, indeed useful in the fight against inflation, is also weighing on the trade situation.

In the first six months of the year, the economy has advanced by only 0.7%. The reconfirmation of the first half's growth picture has led us to revise our 2024 GDP growth projection from 2.0% to 1.3%, which still needs fairly robust growth rates over the next two quarters. We don't see room for major structural improvements in either the dissipation of the strong internal demand through imports or in higher external demand from key trading peers.

Given all this, the chances of one more rate cut from the NBR in the fourth quarter have increased. However, while weak GDP growth can indeed be an argument for less monetary policy restrictiveness, the strong credit activity still requires policymakers' caution.

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