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Romania booms

After experiencing 5% annual GDP growth over the past three years, the Romanian economy continues to flourish in 2004 as well. First quarter 2004 GDP growth was 6.1%, fuelled by private consumption that rose by 8.1%. This upswing is reflected in booming sales in the retail sector, new car sales and private home construction. In March real wages in industry were almost 12% higher than a year before; this was not unjustified as labour productivity was 17% higher. Meanwhile, manufacturing production increased at a higher rate than a year before: a trend attributable to the progress achieved in privatization, restructuring and new investments.

The 7.3% increase in fixed capital formation in the first quarter of 2004 is remarkable, as is the decline in stocks. The business confidence survey for the next three months confirms an optimistic investment climate. The government, however, wants to stimulate investments even more by planning corporate tax cuts for 2005. The Ministry of Public Finance is considering reducing the profit tax to 19% as of 2005 to support the competitiveness of Romania as a business location. In 2004 the fiscal deficit may rise to 2.7% of GDP owing to increased spending on expenditures on new motorways and other construction projects. This overheating, however, may entail costs as domestic interest rates are more than 10% in real terms. Over the past twelve months the National Bank has repeatedly increased the reference interest rate in an attempt to curtail the demand for credit; it has also instructed commercial banks to keep a closer eye on their clients' creditworthiness. As a result, household borrowing has stagnated over the past few months at a level lower than the November 2003 peak, thus allowing the National Bank to reduce the intervention interest rate by 0.5 percentage points to 20.75% per year in early June.

The foreign trade deficit (goods and services) increased to EUR 600 million, a rise of 50% compared to the first quarter last year. The current account deficit, however, was significantly smaller, EUR 269 million, owing to a new high in terms of private transfers. Remittances from persons working abroad generate more inflows than FDI. We expect the current account deficit per GDP for the year as a whole to surpass 6%, and its financing could entail a certain degree of risk. It is unlikely, however, that a crisis or the recent agreement with the IMF will trigger restrictive policies in the short run. The international rating of the country is improving; external debts are relatively low and the government sees imports as being essential to greater modernization. In view of the accelerated growth in the first quarter and given that the increasing current account deficit has not triggered off a series of restrictive measures, the wiiw has revised its GDP growth forecast upwards to 5%. But following the current election year, we expect that incomes policy will become more restrictive.

Expanding foreign trade activity proceeded in tandem with a slow, but positive shift in the commodity structure. In the first four months of 2004, FOB exports totalled EUR 5.82 billion, up 17% compared to the same period in 2003. Two thirds of the exports went to the EU-15. Exports of machines (and metals) increased more rapidly than those of traditional commodities such as clothing and footwear. Structural shifts are the result of recent FDI in the car and machinery components sectors and an outcome of the export-oriented restructuring of the large Galati steel mill following its privatization. CIF imports in the first four months reached EUR 7.46 billion, up 19.2% year-on-year. The commodity structure reflects a growing demand for investment goods and means of transport.

Consumer price inflation does not appear to have been affected much by the boom in demand. CPI is tending downwards to a one-digit level by the end of the year. High international energy prices, however, may trickle through later in the year, thus stopping the downward inflationary trend. Demand-pulled effects can also not be excluded in the latter part of the year. We expect a stricter inflation target for 2005 to support the planned denomination of the ROL.

Privatization has achieved some progress over the past ten months. The final terms and conditions of the largest deals, such as the sale of the Brasov tractor plant and the national oil company PETROM, are still under negotiation with the companies that won the tenders prior to the new owners taking over. When the Austrian OMV has paid more than EUR 600 million for PETROM and once revenue from the privatization of the BCR bank starts to flow in, FDI will increase to EUR 2 billion in 2004.

The remaining 72 loss-making state-owned enterprises are located mainly in coal mining, energy production and district heating. The government decided to cancel the debts and penalties that 31 companies owed to the state budget so as to make them more attractive to investors. Previously relief actions of this kind were restricted to companies that were being sold for privatization purposes, whereas today they are also applied to state-owned companies in current operation with no imminent prospects of being privatized. Such measures run counter to the principle of free competition and hardly heighten the country's image as a 'functioning market economy'. None the less, it seems that the Commission will accord Romania this status, honouring the progress towards privatization and paving the country's path towards EU accession in 2007. Having closed two chapters in June 2004, Romania still has to finalize six chapters by the end of the year or early 2005.

Both national and presidential elections are due in November 2004. Although it may appreciate the rapid economic growth achieved under the present social-democratic minority government (PSD), supported by the Hungarian Democratic Alliance (UDMR), the electorate is also frustrated by widespread corruption. The results of the local elections in June 2004 revealed a PSD on the decline and the socio-liberal opposition grouping

(PNL-PD alliance) on the rise. The overall loser was the nationalistic Greater Romania Party (PRM), which secured only about 5% of the votes. It seems that thanks to the opposition, the outcome of the upcoming parliamentary elections will be much closer than previously expected. The PSD, however, will likely emerge as the strongest party and provide the next President. If it needs to join forces in the next government with a current opposition party, an unstable ‘great coalition’ would emerge which may be incapable of agreeing on EU-conforming reforms.

Table RO

Romania: Selected Economic Indicators

	1999	2000	2001	2002	2003 [1]	2003	2004	2004	2005
						1st quarter		forecast	
Population, th pers., mid-year	22458.0	22435.2	22408.4	21794.8	21733.6	.	.	.	.
Gross domestic product, ROL bn, nom.	545730	803773	1167687	1512617	1890778	327703	405355	2233000	2540000
annual change in % (real)	-1.2	2.1	5.7	5.0	4.9	4.4	6.1	5	4.5
GDP/capita (EUR at exchange rate)	1491	1795	2002	2221	2316	.	.	.	.
GDP/capita (EUR at PPP - wiiw)	4980	5230	5700	6360	6730	.	.	.	.
Gross industrial production									
annual change in % (real)	-2.4	7.1	8.4	6.0	3.1	3.5	5.8	6	4
Construction output total									
annual change in % (real)	-0.2	2.8	9.0	10.0	6.2	5.3	6.9	.	.
Actual final consump.of househ., ROL bn, nom.	453308	634590	917186	1151356	1451166	265187	336356	.	.
annual change in % (real)	-1.1	0.2	6.8	3.1	7.1	3.8	8.4	.	.
Gross fixed capital formation, ROL bn, nom.	96630	151947	241154	322383	425917	53616	67815	.	.
annual change in % (real)	-4.8	5.5	10.2	8.2	9.2	6.8	7.3	8	7
LFS - employed persons, th, avg. [2]	10775.6	10763.8	10696.9	9234.3	9222.5	8806.6	.	.	.
annual change in %	-0.6	-0.1	-0.6	-13.7	-0.1	-0.1	.	.	.
Reg. employees in industry, th pers., avg.	1991.0	1873.0	1901.0	1891.0	1855.0	.	.	.	.
annual change in %	-12.4	-5.9	1.5	-0.5	-1.9	-1.9	-2.4	.	.
LFS - unemployed persons, average [2]	789.9	821.2	750.0	845.3	692.0	778.8	.	.	.
LFS - unemployment rate in %, average [2]	6.8	7.1	6.6	8.4	7.0	8.1	.	8	7
Reg. unemployment rate in %, end of period	11.8	10.5	8.8	8.4	7.2	8.6	7.7	7	7
Average gross monthly wages, ROL	1957731	2876645	4282622	5452097	6741152	6304419	7852024	.	.
annual change in % (real, net)	-3.8	4.6	4.9	2.2	8.8	9.6	9.0	.	.
Consumer prices, % p.a.	45.8	45.7	34.5	22.5	15.3	16.7	13.6	11	8
Producer prices in industry, % p.a.	44.5	53.4	41.0	24.7	19.5	22.0	17.9	15	10
General governm.budget, EU-def., % GDP [3]									
Revenues	.	.	36.4	34.9	.	.	.	.	.
Expenditures	.	.	39.9	36.9	.	.	.	.	.
Deficit (-) / surplus (+), % GDP	.	-4.4	-3.5	-2.0	-2.0	.	.	-3	-3
Public debt, EU-def., % of GDP [3]	24.0	23.9	23.2	23.3	21.8	.	.	23.5	23.5
Discount rate, % p.a., end of period [4]	35.0	35.0	35.0	20.4	20.4	18.4	21.3	.	.
Current account, EUR mn [5]	-1352	-1494	-2488	-1623	-2920	-149	-269	-3500	-3500
Current account in % of GDP	-4.0	-3.7	-5.5	-3.4	-5.8	-1.6	-2.7	-6.4	-6.0
Gross reserves of NB excl. gold, EUR mn	1520.0	2654.8	4445.3	5876.8	6373.6	5802.2	6725.1	.	.
Gross external debt, EUR mn [6]	8734.3	11043.5	13507.1	14648.3	15382.8	14391.4	15809.0	.	.
FDI inflow, EUR mn [5]	980	1147	1294	1212	1381	389	414	.	.
FDI outflow, EUR mn [5]	15	-14	-18	18	36	13	7	.	.
Exports of goods, BOP, EUR mn [5]	7986	11273	12722	14675	15614	3778	4329	18000	20000
annual growth rate in %	8.3	41.2	12.9	15.4	6.4	14.3	14.6	15	10
Imports of goods, BOP, EUR mn [5]	9168	13140	16045	17427	19569	4191	4933	23000	26000
annual growth rate in %	-5.6	43.3	22.1	8.6	12.3	9.1	17.7	17	13
Exports of services, BOP, EUR mn [5]	1286	1910	2273	2468	2656	587	613	.	.
annual growth rate in %	18.1	48.5	19.0	8.6	7.6	17.6	4.4	.	.
Imports of services, BOP, EUR mn [5]	1658	2170	2402	2463	2630	570	609	.	.
annual growth rate in %	2.0	30.9	10.7	2.5	6.8	9.2	6.8	.	.
Average exchange rate ROL/USD	15332.9	21692.7	29060.9	33055.5	33200.1	33155.4	32430.0	.	.
Average exchange rate ROL/EUR (ECU)	16295.6	19955.8	26026.9	31255.3	37555.9	35619.9	40573.7	41000	43500
Purchasing power parity ROL/USD, wiiw	4464.1	6349.2	8437.8	10175.4	11853.6	.	.	.	.
Purchasing power parity ROL/EUR, wiiw	4877.9	6845.7	9138.1	10914.1	12928.7	.	.	.	.

Notes: 1) Preliminary. - 2) From 2002 break in methodology and according to census March 2002. - 3) According to ESA 95, excessive deficit procedure. - 4) Reference rate of NB from February 2002. - 5) Up to 1999 wiiw calculated from USD. - 6) Medium- and long-term.

Source: wiiw Database incorporating national statistics; AMECO; wiiw forecasts.