The World Bank in Romania

# Country Snapshot

*An overview of the World Bank's work in Romania*

**April 2018**

| ROMANIA | 2017 |
|---|---|
| Population, million | 19.6 |
| GDP, current US$ billion | 206.9 |
| GDP per capita, current US$ | 10,563 |
| Life Expectancy at birth, years (2015) | 75.0 |

## At a Glance

- Romania's economy experienced 7% growth in 2017, the second fastest growth in the European Union. But, the country still faces the twin challenges of promoting inclusion and consolidating the sustainability of its growth model by focusing on better quality investments, higher productivity, and exports.
- A new government was formed in January 2018, providing an opportunity to create the stability needed to deepen reforms and ensure sustainable economic growth.
- The World Bank continues to engage in a strong partnership with Romania, and maintains a large portfolio of lending, advisory services, and technical assistance in areas such as government reforms, strategy formulation and budgetary reforms, the deinstitutionalization of children, education, transport, and the financial sector.
- The Bank's lending portfolio and analytical work focus on supporting key structural reforms in education, health, social protection, the environment, and the judiciary, all of which are critical to fully unlocking Romania's development potential.

## Country Context

Romania held parliamentary elections in December 2016. A governing coalition composed of the Social Democratic Party (PSD) and the Liberal-Democratic Alliance (ALDE) appointed a cabinet on January 29, 2018, following the resignation of a short-lived cabinet that governed from June 2017 to January 2018.

The new Government's priorities for 2018–20 include improved absorption of European Union (EU) funds and a focus on securing investments in infrastructure and health care, reforming the pension system, and simplifying tax administration. The Government's program reconfirms Romania's roadmap for achieving the Europe 2020 objectives for smart, sustainable, and inclusive growth.

Anti-corruption activities continued to move forward and Romania's record in combating corrupt practices is informing similar regional efforts. The credibility of the country's National Anti-Corruption Directorate (DNA) was bolstered by its indictment of several high-profile figures in recent years, with strong public support demonstrated by the anti-corruption protests that have recently taken place against political attempts to weaken the independence of the judiciary.

Romania has one of the highest poverty rates in the EU. The share of Romanians at risk of poverty, after social transfers, increased from 21.6% in 2010 to 25.3% in 2016. However, the share of the population at risk decreased from 41.5% in 2010 to 38.8% in 2016.

## The World Bank and Romania

Since joining the International Bank for Reconstruction and Development (IBRD) in 1972, Romania has received US$13.6 billion in commitments for over 117 IBRD loans, guarantees, and grants covering a broad range of sectors.

Under the Country Partnership Strategy (CPS) FY 2014–18, the World Bank supports Romania's efforts to accelerate structural reforms. The overarching long-term objective of the CPS is to support the country's convergence with the EU through robust, sustainable, and equitable growth and enhanced competitiveness.

The Bank engages in Romania through the full range of its instruments: development policy lending, investment lending, Advisory Services and Analytics (ASA), and especially Reimbursable Advisory Services (RAS). Engagement over FY14–18 aims at advancing poverty reduction and promoting shared prosperity through three pillars:

- creating a 21st-century Government,
- advancing growth and private sector job creation,
- promoting social inclusion.

## Key Engagement

The Romania program consists of a portfolio of five projects and two trust funds and a program of 34 ASA tasks, of which 16 are RAS. The active lending portfolio amounts to US$858.92 million in net commitments (US$750.45 million undisbursed), supplemented by one recipient-executed trust fund of over US$3.07 million (US$0.64 million undisbursed).

ASAs address themes of major interest, ranging from partnerships for marginalized Roma to improving fiscal effectiveness. The ongoing 14 RAS activities amount to over US$40 million and support the General Secretariat of the Government, the Ministry of Education, the National Authority for the Protection of Child Rights and Adoption, the National Agency for Public Procurement, the Romanian Agency for Quality Assurance in Higher Education, the Ministry of Public Finance, the Municipality of Constanta, Bucharest District 5 City Hall, and the Municipality of Brasov. Since 2010, 58 RAS agreements totaling US$95.71 million have been signed.

### WORLD BANK PORTFOLIO

No. of Projects: 5

IBRD Lending: 5 Loans ($858.92 Million)

Other TFs: 1 Grant ($3.07 Million)

ASA: 34 activities, of which 14 RAS under implementation ($40.68 million) and 2 RAS under preparation.

The Bank's RAS program, launched in 2010, has diagnosed structural bottlenecks to growth and made recommendations for capacity building, many of which were implemented in 2012–15 under the Memorandum of Understanding (MoU) supporting the implementation of EU Structural and Cohesion Funds in Romania and the modernization of public administration.

In January 2016, the World Bank and the Government of Romania signed an MoU, effective until 2023, that provides a framework for continued World Bank support to Romania's efforts to advance structural reforms, improve public administration, and achieve faster EU convergence.

After the successful experience of the past five years, the new MoU includes an extension of advisory services to the entire ESIF 2014–20, including, for the first time in Europe, access to the European Agricultural Fund for Rural Development and the European Maritime and Fisheries Fund.

## Recent Economic Developments

Romania's economy grew by 7% in 2017, the second fastest growth in the EU. Growth was led by private consumption (up 8.8% year-on-year [y-o-y]), fueled by tax cuts, hikes in minimum and public sector wages, and increases in pensions. Investment also showed signs of recovery, growing at 5.4% y-o-y. On the production side, the main drivers were information and communications technology (up 10.9% y-o-y), industry (up 8% y-o-y), and agriculture (up 18.3% y-o-y), the latter benefiting from good weather conditions.

Inflation is on an upward trend, driven by the pickup in private consumption. Annual headline inflation increased to 4.7% in February 2018, above the upper limit of the National Bank of Romania (NBR) target band. In response, the NBR board increased the policy rate by 25 percentage points (to 2.25%) in two consecutive meetings in early 2018.

This came amid robust private sector credit growth (up 5.6% as of December 2017) and concerns over the perspective of the fiscal stance. The current account deficit deteriorated to 3.4% of GDP at end-2017, reflecting the strong growth of imports.

The labor market strengthened further on the back of strong economic growth and fiscal relaxation. Real wages increased by 8.1% y-o-y as of December 2018 and unemployment fell to 4.6%, a 25-year low. Nonetheless, the low employment rate of 63.4% in the fourth quarter of 2017 reflects persistent structural rigidities in the labor market.

Fiscal policy remained pro-cyclical in 2017. The budget execution posted a deficit of 2.9% of GDP in 2017. The deficit reflects a 14% increase in public expenditure and a lower-than-expected revenue collection (up 12.5%), particularly from the value added tax (VAT) (up 3.6%).

The increase in current spending was driven by a 22% hike in the compensation of employees and a 15.5% increase in current spending, while public investment spending contracted by 9.5%.

## Economic Outlook

Growth is expected to remain solid in 2018, fueled by additional fiscal relaxation measures. GDP will likely expand by roughly 5.1% in 2018, driven by the fiscal stimulus and aided by a resurgent EU. Continued growth in consumption is expected to widen the current account deficit to 4.3% in 2018.

Coupled with a positive output gap and increased import prices, aggregate demand will drive inflation upward. The NBR projects annual inflation to reach 3.5% at end-2018, above the upper limit of the NBR target band.

In the absence of corrective measures, the fiscal deficit is projected to reach 3.3% of GDP in 2018, which would place Romania on a trajectory toward re-entering the Excessive Deficit Procedure of the EU. However, the Government has stated that, as in 2017, it would be ready to promote adjustment measures should the deficit threaten the 3% ceiling.

The widening of the fiscal deficit would push public debt up to 46.8% of GDP at end-2020 from 44.5% in 2017. Nevertheless, public debt remains one of the lowest in the EU.

Continued strong private consumption growth, aided by a lower VAT rate and a continued growth in real wages, partly supported by minimum wage increases, should boost real incomes and lead to further declines in poverty incidence. The US$5.50 per day (2011 purchasing power parity) poverty rate is projected to decline to 22.6% in 2018, 21.7% in 2019, and 20.9% in 2020.

This is consistent with the rate trend for those at risk of poverty or social exclusion (AROPE) for Romania based on the EU's Statistics on Income and Living Conditions (SILC), indicating that severe material deprivation has decreased significantly. However, income inequality has increased, partially due to the diminishing redistributive effect of the tax and transfer systems.

## Project Spotlight

### Building a Greener and Cleaner Environment in Romania

Manure collection platform in Targsoru Vechi commune

Since 2007, the World Bank has supported Romania's nationwide efforts to combat nutrient pollution.

Agricultural production in Romania is concentrated in small farms under 5 hectares in size, the majority of which keep animals in the vicinity of the household without adequate collection and storage facilities for animal waste.

Such environmentally unfriendly practices lead to the pollution of groundwater and pose a general health hazard for Romania's rural population, such as the incidence of blue baby disease, which can lead to infant death.

The Integrated Nutrient Pollution Control Project (INPCP) supports the country's efforts to reduce the discharge of nutrients (nitrogen and phosphorus) into water bodies and helps Romania comply with the provisions of the EU Nitrates Directive on a national scale. The project is currently the only intervention in Romania that finances direct investments in rural communities.

To date, INPCP has financed 82 platforms for the management and storage of animal waste in 77 rural communities around the country. These platforms have been equipped with new tractors, bins, and other essential tools needed to improve livestock manure management and prevent nitrates and other dangerous minerals from contaminating soil and water supplies. The project also financed several sewerage networks and wastewater treatment plants, and the first pilot biogas installation in the city of Seini, Maramures County. The project has provided training and technical assistance to beneficiary communities and strengthened the institutional capacity of the relevant government institutions responsible for regulating, implementing, monitoring, and reporting on the requirements of the EU Nitrates and Water Framework Directives.

In 2016, a €48 million additional financing was approved to scale up investments in addressing nutrient pollution. Approximately 30,000 small farms are expected to benefit from support for manure collection and composting facilities, manure management, biogas production from animal waste, and sewage and wastewater treatment in about 100 highly vulnerable communes. The project aims to enhance public awareness about nitrate pollution and capture citizen feedback on implementation challenges and experiences to inform broader national efforts to reduce nutrient pollution.

The "Country Snapshot" is a bi-annual update, highlighting the country's recent developments, economic outlook and major overview of the World Bank's partnership with the country. You can find the latest updates at http://www.worldbank.org/romania

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**CONTACTS**

**Bucharest**
**40 21 201 03 11**
**UTI Building, 6th floor, 31, Vasile Lascar St. Sector 2, Bucharest, Romania.**


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