

ROMANIA

20

WEAKENED BY POLITICAL INSTABILITY

Recent political tensions are once again drawing attention to Romania. The next government's priority will be to further consolidate public finances; otherwise, the public debt-to-GDP ratio will continue to deteriorate. In addition, Romania appears to be the Central European country most adversely affected by the energy shock, although the situation is still manageable. Economic growth has been sluggish since 2024 and is not expected to improve in 2026. Inflation has now exceeded 10%, but it is expected to ease from September as the effects of the VAT rate hike subside. Monetary authorities are expected to adopt a cautious approach in the short term. By 2027, the Neptun Deep gas project in the Black Sea is set to be a major asset that should help reduce public and external account deficits.

STAGNANT GROWTH

Since 2024, Romanian growth has been below 1%, constrained by political uncertainties and, since last summer, by budgetary austerity measures. In Q1 2026, Romania's GDP contracted by 1.1% y/y (0% q/q) following a contraction of -1.4% in Q4 2025 (-1.9% q/q). Consumption, which is one of the key pillars of the economy, has contracted for the first time since 2021. The rebound in investment has not been sufficient to offset this decline. In terms of foreign trade, both exports and imports have increased at similar rate, but their growth has slowed. Economic indicators do not point to any improvement in Q2. Retail sales and consumer confidence continue to deteriorate. Likewise, confidence in the industrial and services sectors remains low.

For the remainder of 2026, the outlook is bleaker due to the combined effect of political tensions in the country and the conflict in the Middle East. A rebound in consumption is unlikely, as inflation is rising faster than wages, which is eroding households' purchasing power.

One positive aspect is that investment opportunities are becoming more promising due to the availability of European Union funds. In particular, the recovery and resilience funds, a significant portion of which remains unallocated (EUR 8.4 bn, or 2.2% of GDP), will be used to finance various public investment projects. However, it is anticipated that the economy should regain momentum by 2027, as consumer spending picks up and global demand improves.

DOUBLE-DIGIT INFLATION

Romania currently has the highest inflation rate in Central Europe. This situation can largely be attributed to the VAT rate increase of 2 pp (to 21%) implemented in August last year as part of the Romanian government's austerity measures. Furthermore, the surge in fuel prices in Q2, driven by the ongoing conflict in the Middle East, is further intensifying inflationary pressures. The price of diesel has even slightly exceeded the 2022 level, reaching EUR 1.84 per litre in June (compared to the peak of EUR 1.72 per litre in 2022). According to the Consumer Price Index (CPI), inflation has already crossed into double digits, recorded at 10.4% y/y in June. This increase is primarily fuelled by rising costs in the « energy » segment and services. However, the inflation rate remains lower than in 2022 (see Chart 1).

In the short term, the potential for a peace agreement between the United States and Iran offers some respite for oil prices and, therefore, for inflation, even though, according to our scenario, oil prices may hover around USD 80/85 per barrel in the short term before gradually decreasing. However, a rebound in inflation cannot be ruled out in the short term, as the rise in transport costs and the prices of certain raw materials could have a knock-on effect on the prices of all goods.

Economic forecasts

	2022	2023	2024	2025	2026e	2027e
Real GDP growth, %	4.2	2.3	0.9	0.7	0.1	2.6
Inflation, CPI, year average, %	13.7	10.5	5.6	7.3	7.9	4.6
General gov. balance / GDP (%)	-6.5	-6.6	-9.3	-7.9	-6.5	-5.7
General gov. debt / GDP (%)	48.1	49.3	54.8	59.3	61.5	63.0
Current account balance / GDP, %	-9.6	-6.7	-8.2	-7.9	-8.0	-7.5
External debt / GDP, %	54.7	56.9	57.5	60.2	62.1	64.9
Forex reserves, EUR bn	52.3	66.0	70.5	77.0	85.0	92.0
Forex reserves, in months of imports	5.3	6.9	7.1	7.5	8.0	8.2

TABLE 1

e: ESTIMATES & FORECASTS

SOURCE: BNP PARIBAS ECONOMIC RESEARCH

Inflation driven by energy and services

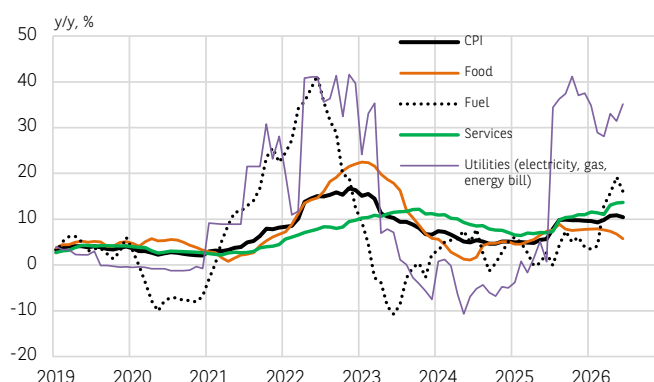


CHART 1

SOURCE: NATIONAL INSTITUTE OF STATISTICS, BNP PARIBAS

Moreover, the impact of the VAT rate increase is expected to diminish starting in September. Our projections indicate that inflation will average 4.6% next year. The central bank's target of 2.5% ± 1 pp is not expected to be achieved before 2029.

Monetary policy remains cautious. The central bank has maintained its key rate at 6.5% since August 2024, following two rate cuts earlier that year. In the short term, it is likely that the current stance will persist. While inflationary risks and downward pressure on the Romanian currency suggest a need for tightening, the slowdown in economic activity calls for a cautious approach.


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LIMITED CORRECTION OF FINANCIAL MARKETS DESPITE THE POLITICAL CRISIS

The political context deteriorated in May with the collapse of the government that had been in place for less than a year. Tensions within the governing coalition ultimately resulted in one of the four parties exiting, leading to a vote of no confidence on 5th May. Prior to that, the government managed to survive several votes of confidence since it came to power. The immediate challenge is to quickly form and approve a new government, otherwise the country would be heading towards snap elections.

At the onset of the conflict in the Middle East, the Romanian currency (leu), which operates within a managed float framework against the euro, exhibited minimal fluctuations compared to other currencies in the region, due to several interventions by the central bank. However, downward pressures increased at the end of April amid the political crisis, intensifying further in early May with the collapse of the government. The leu peaked at 5.27 against the euro in early May, then stabilised slightly below that level (5.25 leu to 1 euro, compared to 5.1 before the political crisis). Between 29 April and 10 July, the currency depreciated by 2.8% against the euro and by 5.3% against the dollar. The political crisis has so far had minimal impact on the 5-year bond yield, which has only risen by 0.7 point since late April. Similarly, the impact of geopolitical tensions has been minimal. The stock market has maintained its upward trajectory (+15.6% since the beginning of the conflict).

The repercussions on the financial markets have so far been limited. However, political uncertainties are impacting both household confidence and that of business leaders. The longer the resolution of the crisis is delayed, the longer it will take for economic activity to resume.

PUBLIC FINANCES TO KEEP AN EYE ON

In 2025, the austerity measures introduced by the government helped contain the budget deficit at 7.9% of GDP, thereby preventing a downgrade of the sovereign rating by external agencies and a freeze on European funds. However, further adjustment measures are essential in the short term. Otherwise, government debt as a percentage of GDP will continue to rise. According to our forecasts, this ratio is expected to exceed the 60% of GDP threshold in 2026. The target set last year aims to bring the deficit down to 6% of GDP in 2026, but achieving this goal will be challenging due to the ongoing political crisis and sluggish growth. Short-term uncertainties persist regarding the policies that will be implemented by the incoming government. While the budget consolidation process should remain intact, there might be a slight easing of austerity measures.

In response to the energy shock, the government has prioritised several targeted measures enacted by decree, designed to prevent an increase in public spending. These measures include a cap on the commercial margins of fuel distribution chains, a reduction in excise duties on diesel for three months, and a so-called « solidarity » tax on the exceptional profits of companies in the oil sector. The authorities have recently announced the end of the reduction in excise duties on diesel.

The government's financing needs are high (13.5% of GDP in 2026), but they are being met without major difficulties. Several unsuccessful auctions of last March can be largely attributed to the uncertainty stemming from the conflict in the Middle East. By early June, 43% of the financing needs for 2026 had already been secured. The increase in financing costs on the bond markets remains moderate.

Romania: A moderate energy trade deficit

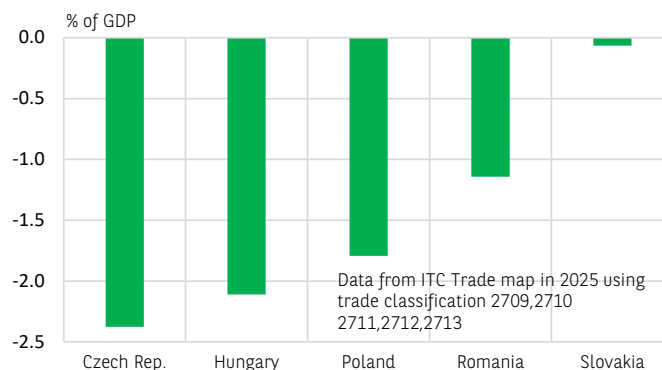


CHART 2

SOURCE: ITC, BNP PARIBAS

However, debt servicing has increased since 2020 due to increased borrowing and given that the bond rate is the highest in the region, standing at 6.75% at the end of June for the 5-year bond rate. The interest burden now stands at 2.8% of GDP (8.3% of budget revenues).

NEPTUN DEEP, A SIGNIFICANT ASSET

Romania appears to be the country most exposed in the region to the energy shock due to its significant macroeconomic imbalances. Last year, both the budget deficit and the current account deficit reached 7.9% of GDP, indicating limited fiscal flexibility for the government. Moreover, the increase in the energy bill is expected to weigh on the current account deficit. However, the country can withstand this shock, as its energy dependence is considerably lower than that of other countries in the region (see Chart 2). Indeed, most of Romania's gas needs are met through domestic production. Our estimates suggest that the impact of the energy shock on the trade balance would be -0.3% of GDP, assuming an average 25% increase in oil prices and a 13.5% increase in gas prices in 2026. The current account deficit is expected to be largely offset by capital inflows. Moreover, foreign exchange reserves are comfortable at EUR 77 bn as of May 2026, equivalent to 8 months of imports, and provide a safety net. However, these reserves have decreased by EUR 2.9 bn since January.

By 2027, the Neptun Deep offshore gas exploitation project, located in the Black Sea, is anticipated to provide a significant financial benefit for Romania. Once operating at full capacity, Romania is expected to generate around 8 bn cubic meters (bcm) of gas per year. The country already produces gas that covers around 90% of its consumption needs (approximately 10 bcm). Romania is on track to become a net exporter of gas, which will strengthen its position as a key partner in supplying Europe and improve its external accounts. Moreover, the royalties and various taxes derived from gas exploitation will help strengthen its public finances.

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