

## **THE IMPACT OF THE FIRST YEAR OF COVID-19 PANDEMIC ON ROMANIA'S ECONOMIC GROWTH**

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### **Abstract**

*In Romania, the first case of Covid-19 was reported on February 26, 2020 and since then, nothing has been the same. The government implemented a range of measures to delay the spread of the virus, which severely impacted the economic activity. At the end of 2020, we had a very clear perspective of the total number of Covid-19 cases and the total number of deaths caused by the virus, but in this research, I want to highlight the impact of the first year of the pandemic on Romania's economic growth.*

**Keywords:** *Covid-19 pandemic, Romania, Gross Domestic Product*

**JEL classification:** *E32, F43*

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### **1. Introduction**

The COVID-19 pandemic and its implications for the world economy is a topic of great interest among economists worldwide (Bagchi, Chatterjee, Ghosh, 2020, Ahmed, 2020). Researchers have analyzed the unprecedented impact of the virus on the US economy (Thorbecke, 2020), India's economy (Dev, Sengupta, 2020), Turkey's economy (Açikgöz, Günay, 2020) and the examples can go on. In Romania, it was analyzed the impact of the COVID-19 pandemic on the labour market (Radulescu, Ladaru, Burlacu, Constantin, Ioanăș, Petre, 2021), on the agricultural sector (Istudor, Popescu, Begalli, Ignat, Petrescu, Petre, 2021) etc. In the present paper, the main objective is to highlight the impact of the first year of the pandemic on Romania's economic growth. To

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achieve this goal, I have performed an analysis of the evolution of Romania's GDP growth, GDP's demand-side components and GDP's supply-side components for the period 2015 – 2020. Regarding the methodology used, I have elaborated a quantitative research, collecting information and data from national and international statistics and from specialized literature. For a better understanding of the analyzed phenomenon, I have made a comparative analysis of Romania's economic performance compared to those of other EU countries.

The first hypothesis of the research: After the first year of the pandemic, amongst GDP's demand-side components, private consumption contributed to the greatest extent to the contraction of Romania's GDP.

The second hypothesis of the research: After the first year of the pandemic, amongst GDP's supply-side components, the most affected types of services were trade, transport, hotels and restaurants.

## **2. Romania's real GDP contraction in the context of the European Union**

After 9 years of economic growth, Romania registered at the end of the first year of the COVID-19 pandemic, an economic decrease of 3.9%. As can be seen in Table 1, the 2nd quarter of the year 2020 was the most affected, as Romanian authorities declared a two months state of emergency (March 16, 2020 - May 14, 2020) to fight the coronavirus pandemic. During this period of time, the right to leave home was restricted, schools were closed and education moved online; restaurants, coffee shops and hotels were shut down, many other companies being affected. After the cessation of the state of emergency, the Romanian economy registered a slight recovery in the following quarters, the recovery being limited by the uncertainty regarding the evolution of the pandemic. The resumption of the economic activity was not achieved at full capacity, against the background of lower aggregate demand and the maintenance of restrictions.

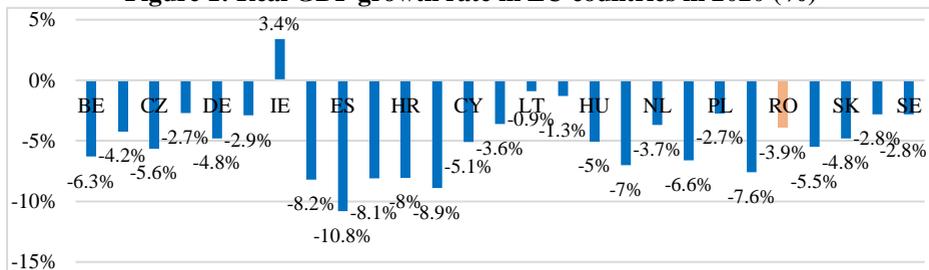
**Table 1: Romania's real GDP in 2020. The percentage changes compared to the corresponding period of the previous year**

	Q1_2020	Q2_2020	Q3_2020	Q4_2020	Year 2020
Real GDP	+2.4%	-10.5%	-6%	-1.7%	-3.9%

Source: The National Institute of Statistics, 2020b

The Romanian population anticipated that in this context there will be an economic decline, generated by bankruptcies and rising unemployment (Rus, Sandu, TaseŃe, 2020). However, Romania's real GDP contraction was much lower than the European Commission's forecasts which estimated a 6% decline (European Economic Forecast, Spring 2020), or those of the International Monetary Fund, which estimated a 5% decline in real GDP (International Monetary Fund, 2020). Compared to the other European Union countries, at the end of 2020 Romania was on the 11th place in terms of real GDP contraction (Fig.1) by 2.6 percentage points below the Euro area countries decrease (-6.5%) and by 2.2 percentage points below the EU-27 countries decrease (-6.1%) (Eurostat, 2021c).

**Figure 1: Real GDP growth rate in EU countries in 2020 (%)**



Source: Eurostat, 2021c

However, the fiscal-budgetary measures adopted by the Romanian government, to combat the effects of the COVID-19 pandemic, generated in 2020 a budget deficit of 9.2% of GDP (Eurostat, 2021a), ranking 6th in the EU on a par with France. Approximately 46.3 billion lei (4.45% of GDP) were funneled in the economic environment through fiscal facilities, investments and exceptional expenditures allocated to combat the effects of the COVID-19 pandemic (Ministry of Finance, 2020).

### **3. Romania GDP growth and demand-side components**

In the last 7 years before the outbreak of the COVID-19 pandemic, the Romanian real GDP grew on average by a rate of 4.44%, a growth that was well above the EU-28 countries of 1.78%, calculated in the same interval (Eurostat, 2021c). As can be seen in Fig.2, this increase was mainly due to private consumption, which since 2015 has remained at very high levels. The increase

in private consumption was stimulated by the increase in the minimum wage, which grew during the analyzed period by 112% (CONTEXPERT, 2021). However, the increase in private consumption was tempered in 2018 and 2019, by record high prices hikes, Romania registering in these two years the highest inflation rate in the EU (Eurostat, 2021b).

**Figure 2.: Romania GDP growth and demand-side components (2015-2020)**



Source: The National Institute of Statistics, 2015-2020a, 2021c

Once Romania entered the state of emergency, on March 16, private consumption was severely affected. At the end of 2020 it registered a 5% decrease compared to the previous year, contributing to a 3.5% real GDP contraction. The year 2020 was marked by an adjustment in population demand, which led to both structural changes and lower dynamics. The 2nd quarter of the year 2020 was the most affected in terms of private consumption, followed by a slight improvement by the end of the year. A small impulse in the increase of private consumption also came from the increase of pensions. The pension point increased in September 2020 from 1,265 lei to 1,442 lei (The National House of Public Pension, 2021) and the increase of the minimum wage which increased in January 2020 from 2.080 lei to 2.230 lei (Ministry of Labour and Social Protection, 2021). Being a regularly collected amount, most of this extra money, went to consumption.

Net exports also had a negative influence on Romania's economic growth, contributing to a 1.6% real GDP contraction. This was the consequence of the 9.9% reduction in exports of goods and services correlated with a lower contraction in imports of goods and services, respectively 6.6%. International trade marked a significant decline in 2020, in the conditions of the pandemic,

which impacted Romania's trade balance, thus the trade deficit increased by 6.3% in 2020 compared to 2019 (The National Institute of Statistics, 2015-2020b).

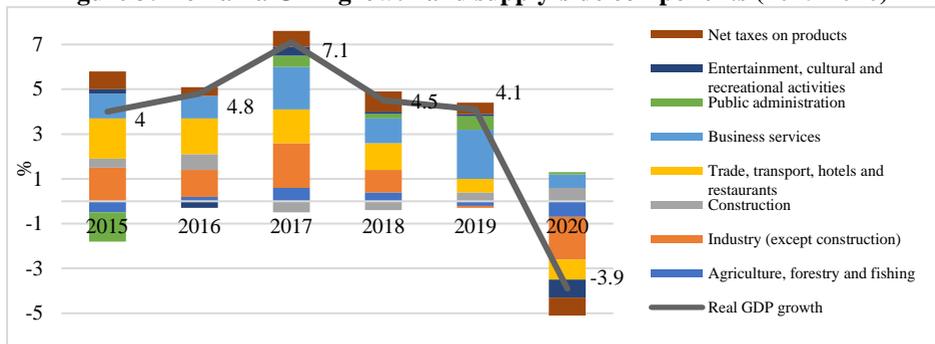
As in 2019, in 2020, important shares in the structure of exports and imports were held by cars and transport equipment (48.6% for export and 37.1% for import) and other manufactured products (30.3% for export and 30.2% for import) (The National Institute of Statistics, 2021b). 60% of Romania's exports of goods are insured from imports, as the domestic companies import various components which are assembled and then exported. The 2020 low external demand caused a contraction in industrial production by 9.2%, the most vulnerable branches, in the context of the pandemic, being those of light industry and the manufacture of motor vehicles, machinery and equipment. (The National Commission for Strategy and Prognosis, 2021).

On the other hand, gross fixed capital formation increased by 6.8% compared to 2019, being supported by both the development of the residential sector and infrastructure investments. This development resulted in a contribution of 1.5% to real GDP growth. For the year 2021 and the following years, gross fixed capital formation will be the engine of economic growth, as a result of the impact of European funds allocated through the National Recovery and Resilience Plan (PNRR) (33.5 billion euros), and through the Multiannual Financial Framework 2021-2027 (46.4 billion euros). However, increasing the absorption capacity is absolutely essential to take use of the allocations of European funds. At the end of 2020, Romania registered an absorption rate of only 50.31% for the programs financed from the European Structural and Investment Funds (ESF) (Ministry of Investments and European Projects, 2021).

#### **4. Romania GDP growth and supply-side components**

On the *supply side* (Fig.3), due to the pandemic, services were some of the most affected sectors of activity. Thus, as a result of the administrative measures adopted in the context of the pandemic, the activity of certain categories of services was closed, or was carried out in compliance with certain restrictions. Physical distance measures forced the cessation of the activity of hotels and restaurants, which also have the largest share in services for the population. As for the restaurants, they remained closed to the indoor spaces. Some initiatives by entrepreneurs to adapt to the conditions imposed, such as home delivery, have to a small extent offset the decline in activity.

**Figure 3: Romania GDP growth and supply-side components (2015-2020)**



Source: National Institute of Statistics, 2015-2020a, 2021c

The most affected categories of services were "trade, transport, hotels and restaurants", which had a contribution of 0.9% to the decrease of GDP and "entertainment, cultural and recreational activities", with a contribution of 0,8% to the decrease of GDP. Currently, HoReCa taxpayers can access the state aid scheme which involves providing financial support to tourism enterprises, accommodation structures, food structures and travel agencies whose activity has been affected in the context of the COVID-19 pandemic. Through this measure, taxpayers would receive compensation for the decrease in turnover in 2020, but are obliged to maintain the activity for 12 months and respectively 24 months (if the value of the grant exceeds 200,000 euros). This measure is beneficial, but the delay in the release of funds could make it even more difficult for some players in this industry. Hotel industry and HoReCa, losses in the first year of the pandemic amounted to approximately 7 billion euros, the biggest losses since its establishment.

Industry, which contributes 18% to Romania's GDP, was another area affected by the reduced global demand and disrupted supply chains. In 2020, it contributed to the decrease of real GDP by 1.9%, the largest decrease being registered in the manufacturing industry. Along with the automotive industry, the textile industry was in great distress in 2020. The textile companies that have remained on the market, and which depend on big names in international fashion, have worked at a maximum of 50% of their capacity, some have started to develop their own brands and even produce sanitary materials in order to survive. With the exception of the tobacco industry, all other industries suffered

significant losses during the state of emergency, especially in April 2020 (The National Institute of Statistics, 2020a).

Another economic sector strongly affected by the COVID-19 pandemic was agriculture, with a negative contribution to real GDP growth of 0.7%. Strongly dependent on the HoReCa industry and the food industry, farmers suffered significant losses in 2020. The health crisis also overlapped with an extreme drought in some areas of the country, one of the worst in 50 years. Cereal production in Romania reached 18,968 million tons in 2020, down 37.6% compared to 2019. Wheat production and corn grain production decreased by 37.7% compared to the previous year, sunflower production decreased by 43% and rapeseed production decreased by 8.8%.

At the opposite end of the spectrum, there were areas that defied the pandemic and registered positive evolutions. One of the sectors that grew at a steady pace since the beginning of the year is construction. In 2020, the volume of construction works increased compared to 2019 by 15.9%, contributing to the real GDP growth by 0.6%. By analyzing construction objects, we noticed that the activity in engineering constructions increased the most (by 18.5% compared to 2019), correlated with the similar advance registered by public investments. Residential buildings come second, with an annual increase of 17.8%; a performance that is in line with the trend of recent years, non-residential buildings (warehouses, industrial halls, etc.) registered an increase of almost 11% (The National Institute of Statistics, 2021a).

Also, within the services there were areas with positive developments. The “information and communications” branch supported the real GDP growth by 0.6%, and the “public administration” supported the real GDP growth by 0.1% as a result of the measures taken by the government during the crisis, but also due to the intensification of the activity in the sanitary field.

## **5. Conclusions**

Both hypotheses from which we started the research were verified. Analyzing the demand-side components, we have observed that private consumption and net exports contributed to the contraction of Romania's real GDP growth rate, while gross fixed capital formation increased compared to the previous year, due to the development of the residential sector and investments in infrastructure. Analyzing the supply-side components, in the context of the physical distancing measures adopted by the government, the most affected services were trade, transport, hotels and restaurants, alongside entertainment,

cultural and recreational activities. Construction had a positive evolution, while industry and agriculture made a negative contribution to real GDP growth.

The fiscal-budgetary policy adopted by the Romanian government managed to alleviate the shock of the COVID-19 crisis and contributed to limiting the country's economic decline to -3.9% of the GDP. The challenge was for these measures to meet the significant short-term difficulties and support the economy in the medium term while finding a way to adjust the budget deficit. Government support has been found both in mitigating the costs of companies in industrial activities and services as well as in the positive influence of public consumption on GDP. At the end of 2020, public consumption generated a contribution of 0.6% to real GDP growth.

The forecasts are optimistic as International Monetary Fund experts estimate a growth of 6% for the Romanian economy in 2021 and a moderation of up to 4.8% in 2022. Thus, they place Romania on the 2nd place in the top of European economies with the highest growth in 2021, after Spain (International Monetary Fund, 2021). This increase is based on the return of services to the level recorded before the pandemic, on maintaining the upward trend in construction, and also on an agricultural production unaffected by unfavorable climatic conditions.

Investments will remain robust over the entire forecast horizon, supported by the construction sector, as the real estate segment still offers attractive long-term investment opportunities, especially for investors that can cope with lower liquidity. A major opportunity which Romania should take advantage of relates to EU funds: the coronavirus aid package plus the normal allocation for the 2021-2027 period for Romania, which is around 80 billion euros. Additional investments in transport infrastructure would lead to major improvements, and would unlock a significant and sustainable GDP growth.

The magnitude of Romania's economic recovery will depend on the evolution of the pandemic and the government's response policies to the health crisis. Moreover, the increase of international prices for raw materials can cause inflationary pressures with a negative impact on economic growth. Romania's macroeconomic objective must be to recover the economic downturn from 2020, creating the premises for sustainable economic growth.

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