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Presentation at the conference "Romania Facing Major Fiscal Decisions. Balance and Perspectives for the Future"

AAFBR Annual Conference

Bucharest 2025

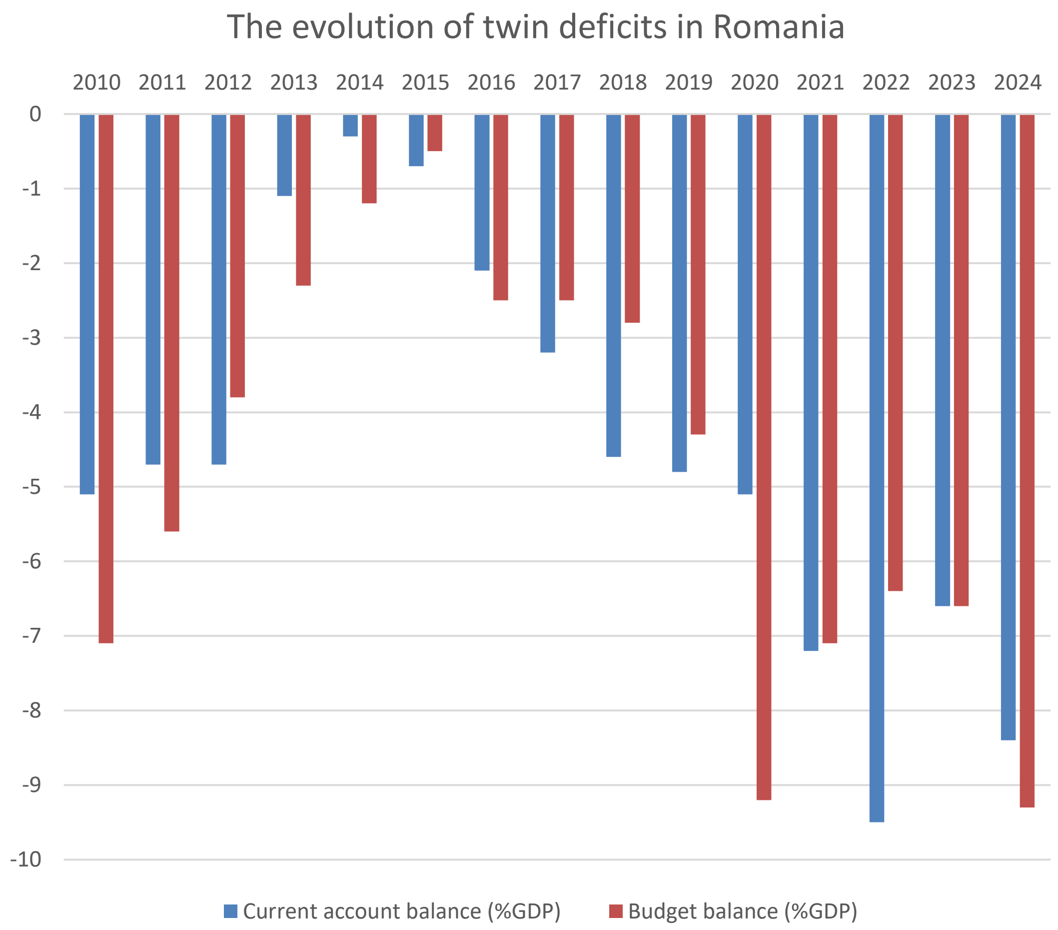
General framework – the main challenges facing Romania

- **A divided society** (political risk).

- **Tense social situation** (cost-of-living crisis and large disparities between regions and citizens).

- **Major imbalances in public finances and the external account** (significant financial and economic risk).

Sustainability of public finances



- Romania has a very large, structural deficit (ESA: 8.65% of GDP in 2024; for 2025, the European Commission forecasts the deficit at 8.6% of GDP) – by far the highest in the EU;

- **A credibility problem** due to repeated failure to meet commitments: see low sovereign rating (BBB-) and borrowing costs…

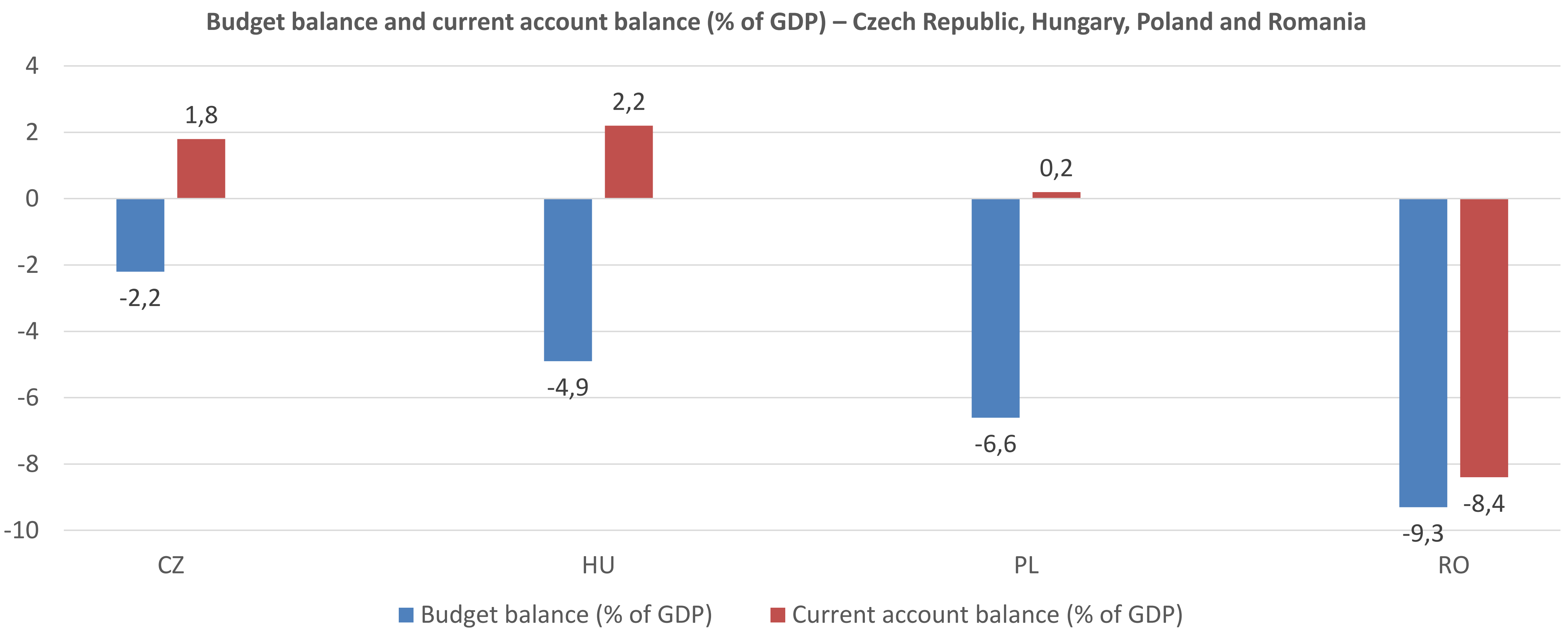
- **We will pay a premium to regain trust / restore financial credibility… through a robust package of measures;**

- **Twin deficits:** large current account deficit mainly caused by the budget deficit;

- **Why large budget deficit and low GDP growth?** – our production is embedded in European production chains (external demand).

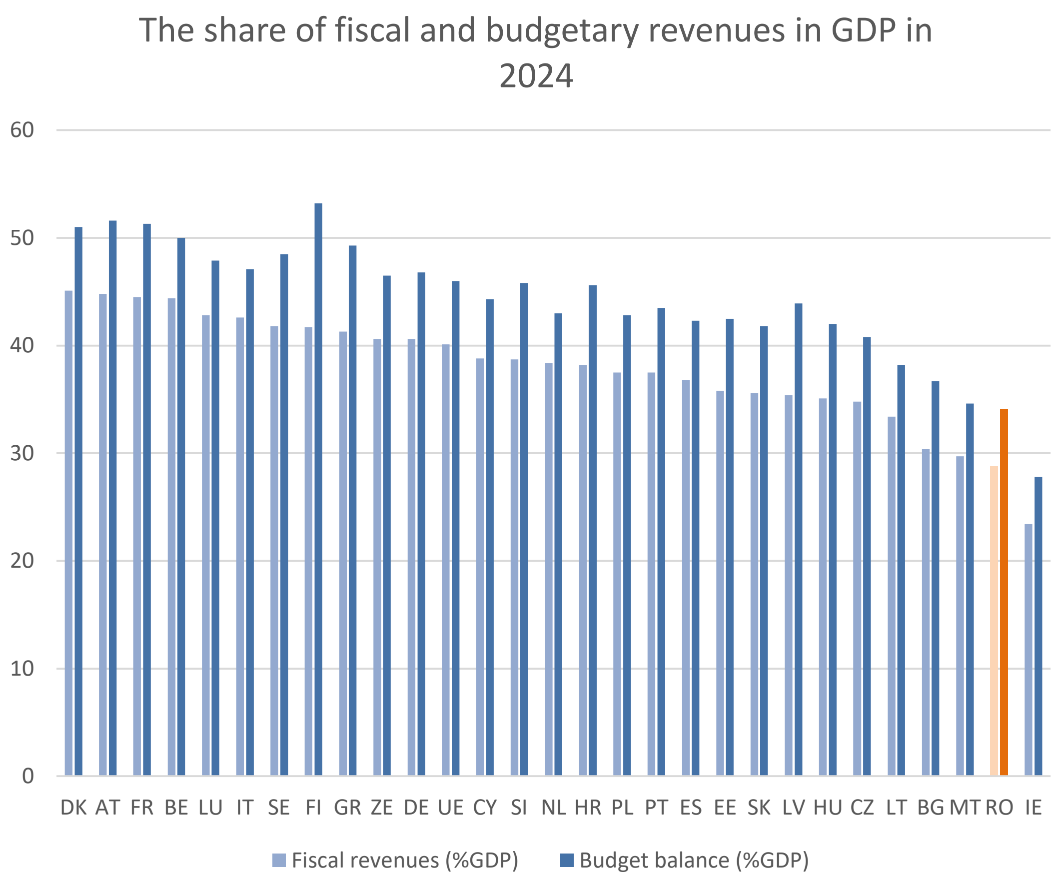
Souce: AMECO

Sustainability of public finances



Souce: AMECO

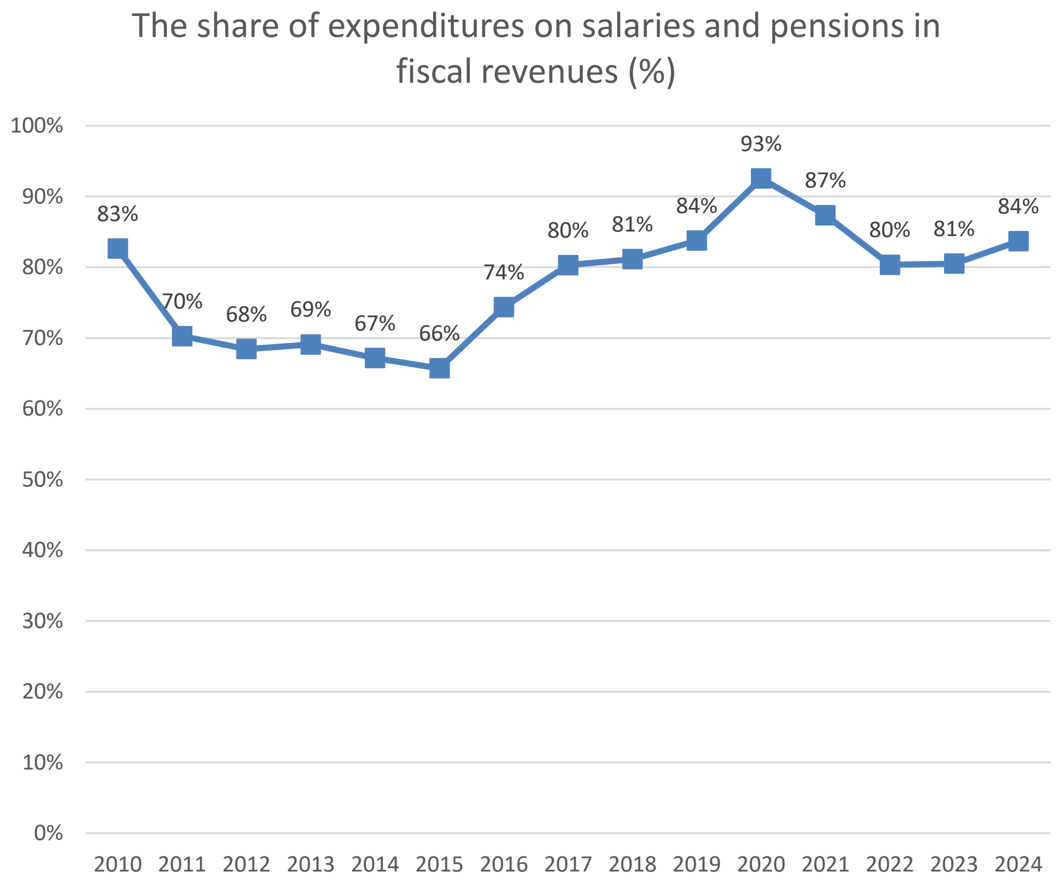
What structural adjustments are needed in the 2025-2027 period?



Source: AMECO

- Deficit correction: from around 8.65-9% in 2024 to 3% of GDP by 2031; with a reduction of over 2% of GDP by the end of 2026
- **The correction: not a classic balance of payments adjustment through strong depreciation and drastic cuts in the budget deficit…**
- **What is needed** is a sharp fiscal correction through **reduced domestic absorption… which leads to a distributional conflict (who bears the cost?)**
- **Expenditures cuts and tax increases will affect GDP growth, but they are unavoidable**
- Limiting the pain – fine-tuning is difficult under current condition…
- In two years (by 2026), we must bring the deficit below 6.5%, according to the Medium-Term Budgetary Framework (PNSB), market expectations, and rating agencies: **a credible/robust adjustment package of 2-3% of GDP through both revenues and expenditures**
- **Perceptions matter tremendously**

The risk of maintaining a high structural deficit in the current geopolitical and economic context

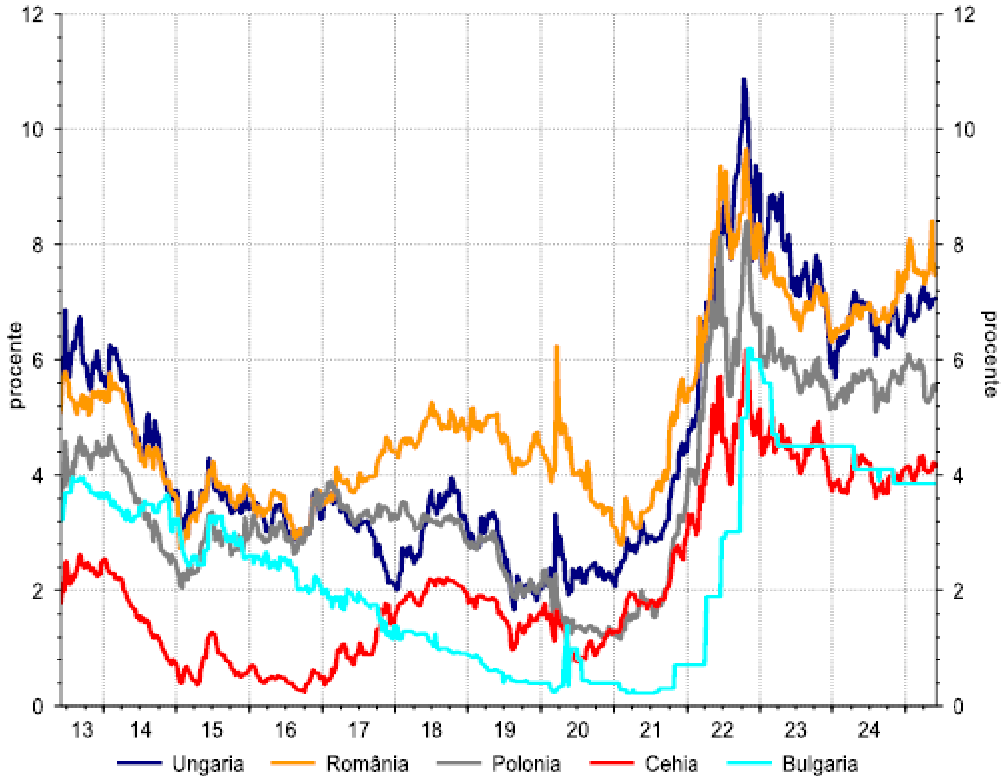


Source: AMECO

- **Better collection and unclear spending cuts: a non-starter in the adjustment package**
- Spending cuts need to be permanent
- **Improved revenue collection will help in the coming years**
- Investments should be protected as much as possible — the lesson from the financial crisis in the EU: between 2008 and 2009, total investments in the EU dropped on average from 22% to 17% of GDP
- Prioritized investments (NRRP); NRRP's revision?

Downgraded credit rating in the absence of swift and credible measures – effects

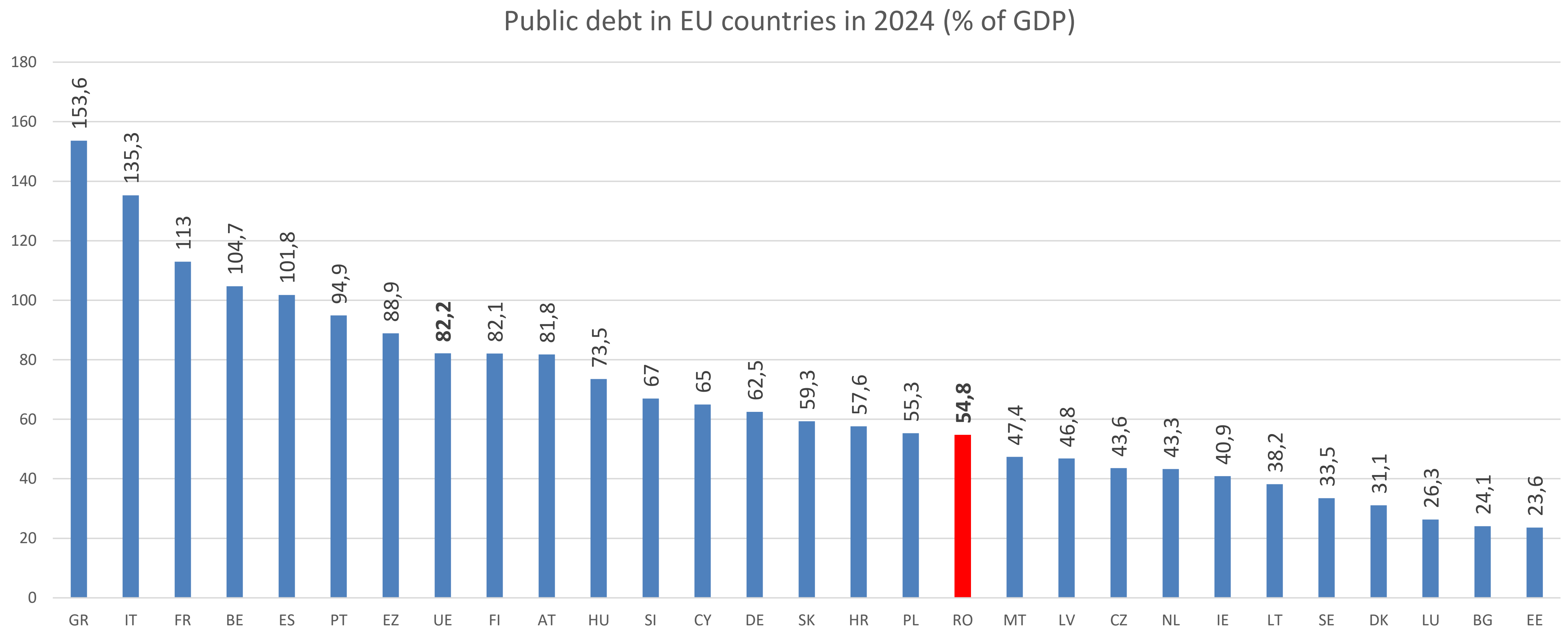
The evolution of 10-year government bond yields



Source: Refinitiv Datastream

- Rapidly rising costs, **snowball effect** on debt
- Capital flight
- Triggering of a full-blown financial crisis
- The National Bank of Romania is not a magician
- We will need financial assistance similar to that required during a deep crisis (as in 2009-2010)

Fiscal policy must support monetary policy by eliminating fiscal dominance



Source: AMECO

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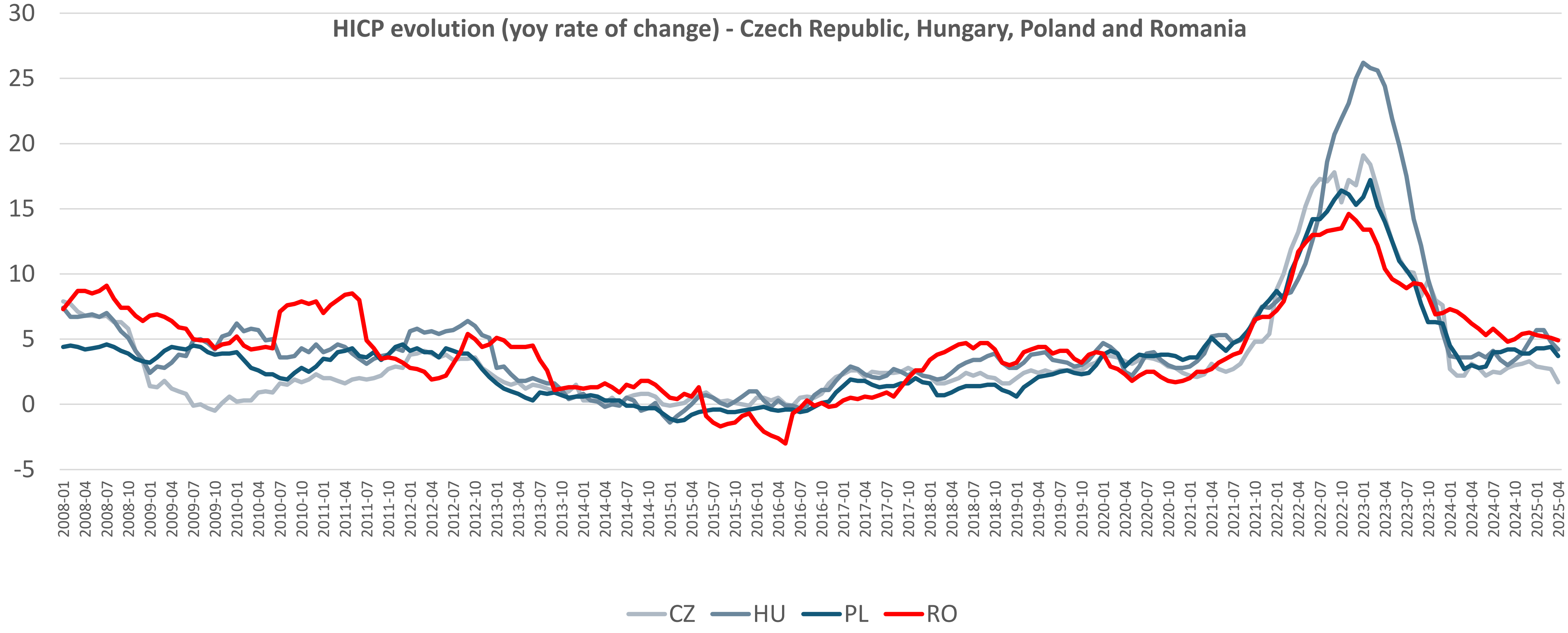

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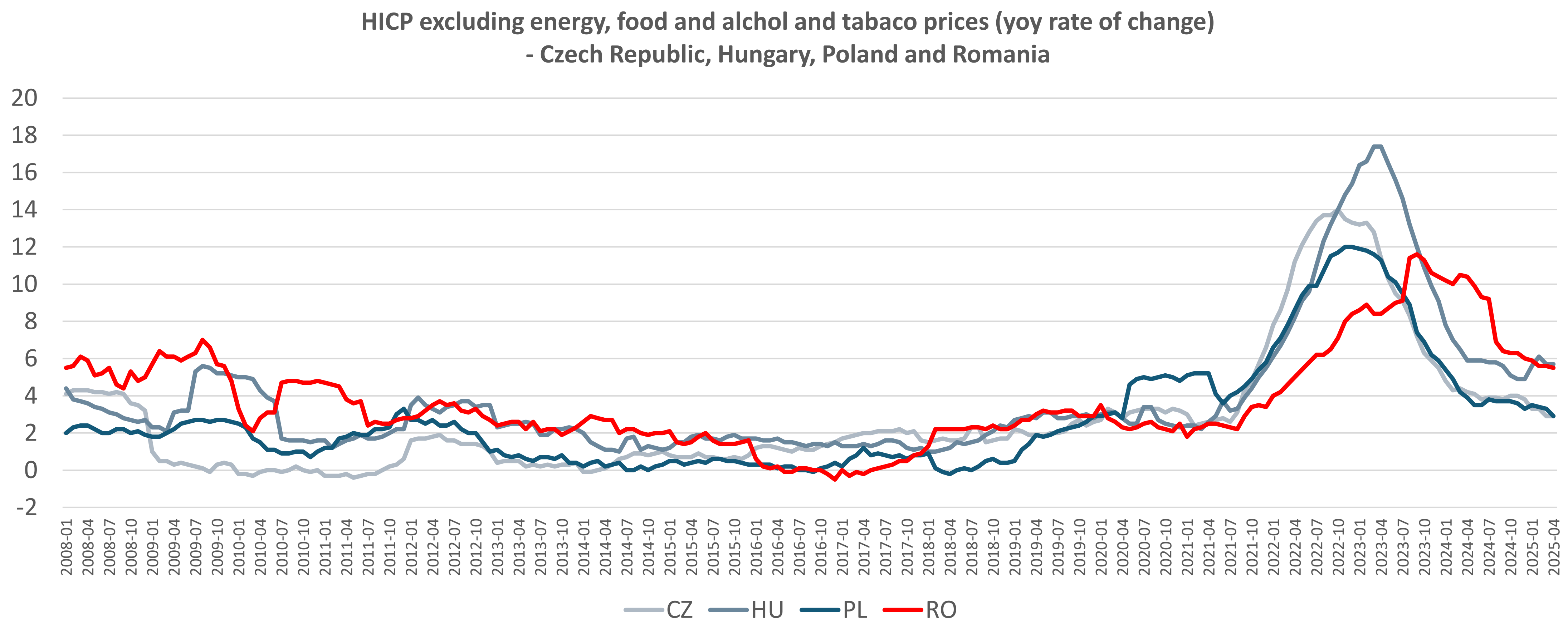

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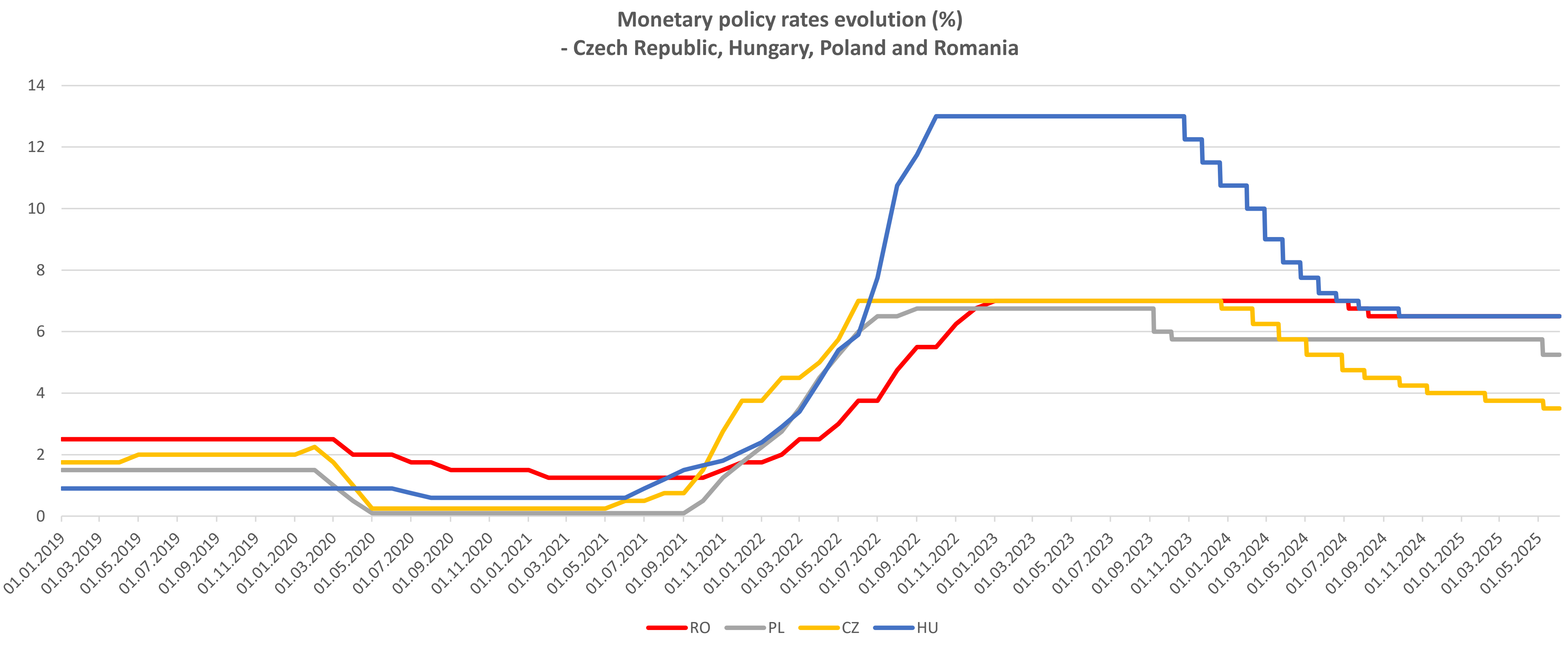

Source: AMECO

The problem of European funds

- Dependence on European funds: what will happen when the Multiannual Financial Framework (MFF) and the Recovery and Resilience Plan are significantly reduced? **The risk of falling into a "low investment equilibrium" — lower GDP growth, reduced potential GDP, economic stagnation? (middle income trap)**
- **A different economic model?** Competitive domestic production… investments
- The need for fiscal space: defense spending, other adverse shocks.

Absolutely necessary to reassure external creditors and ensure sound governance

- **Budget revision by June 30 + announcement of the Prime Minister**

- **Thank you for your attention!**