

# Romania

## Systematic Country Diagnostic (SCD)

2023 Update

September 2022

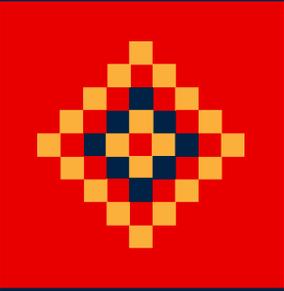
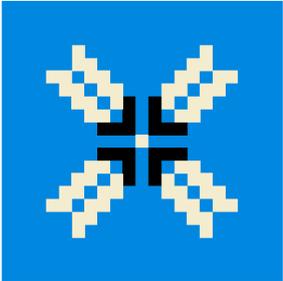


## A. Context for a Systematic Country Diagnostic (SCD)

## B. Romania's SCD Update 2022:

### CONTENTS

- 1** Where does Romania stand today, and what emerging trends will shape its outcomes?
- 2** What is holding back Romania: constraints to growth and prosperity?
- 3** What are Romania's priorities for inclusive, strong, and sustainable growth



# Why the SCD Update for Romania?



## Systematic Country Diagnostic:

1

**Is a major analytical diagnostic of the World Bank Group (WBG)**

- Independent view of technical staff
- Based on analysis of data and existing studies by WBG, external partners, and independent research.

2

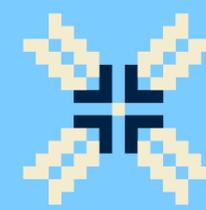
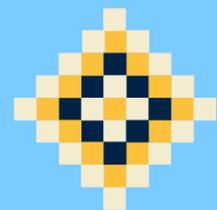
**Identifies a set of constraints and priorities for sustainable reduction in poverty and increase in shared prosperity.**

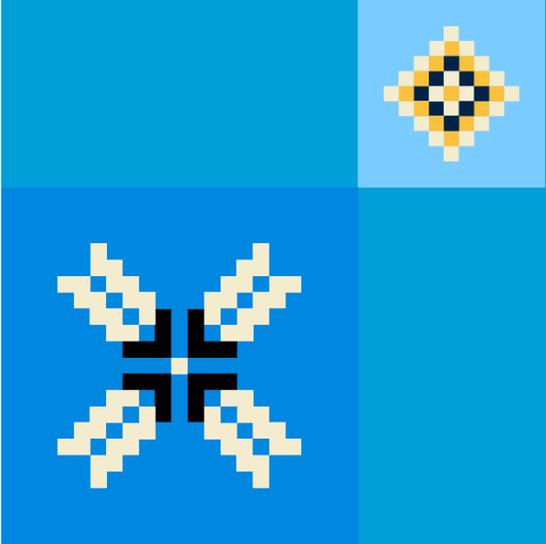
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**Informs strategic engagement of the WBG with Romania.**

Country Partnership Framework 2024-2029 focuses on:

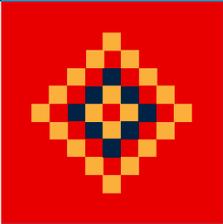
- Diagnostics of the SCD
- WBG comparative advantage
- Government priorities.





B

# Romania's SCD Update



1

# Where does Romania stand today, and what emerging trends will shape its outcomes?

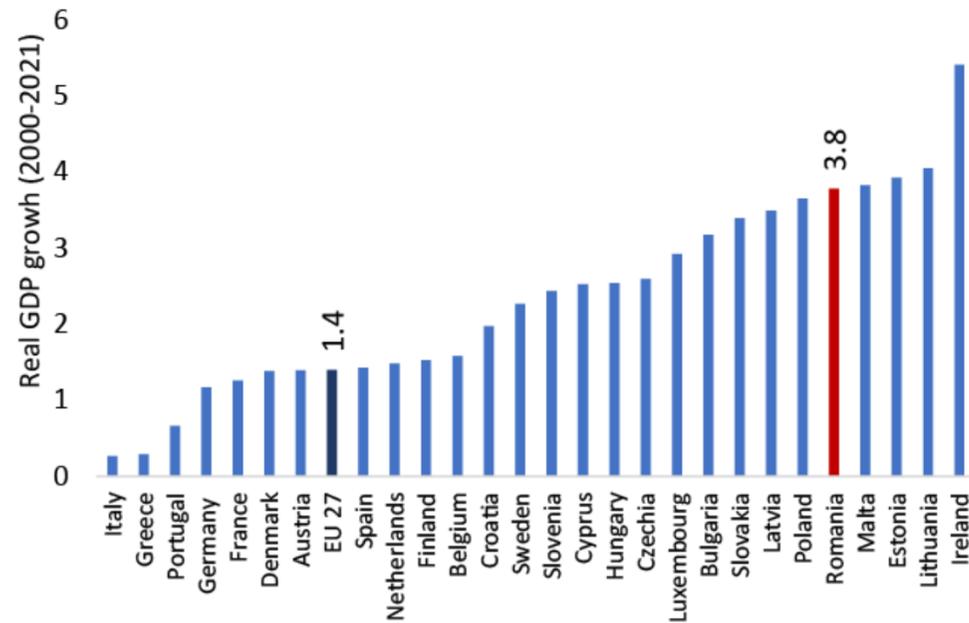


# 1 Where does Romania stand today?

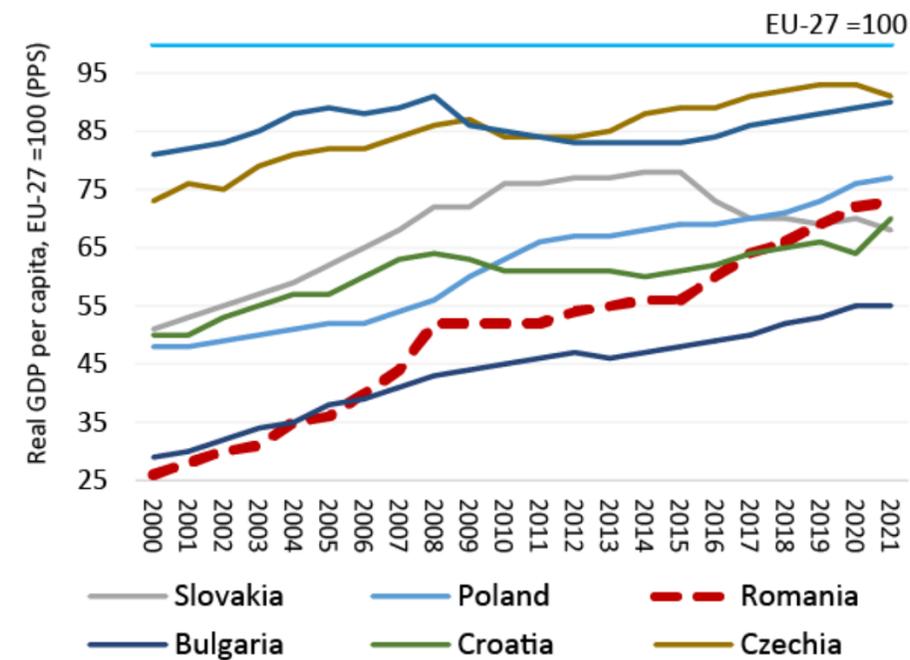


## High but volatile growth

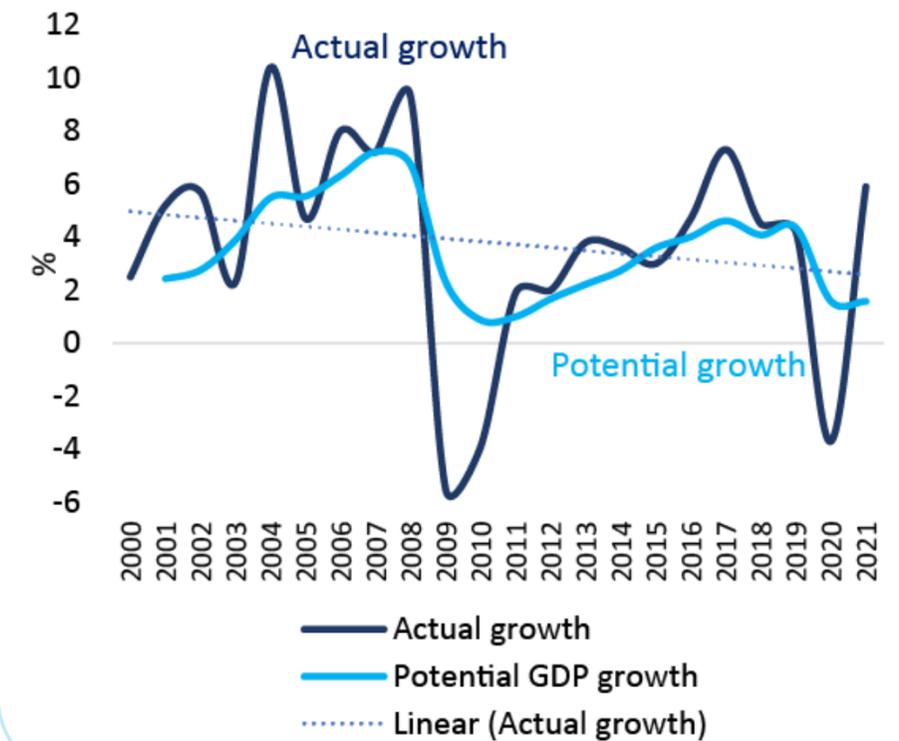
Romania's economic growth has been among the highest in the EU in the last two decades...



...supporting an impressive convergence with the EU (though still some way to go)...



...but growth has been volatile and potential growth has also declined



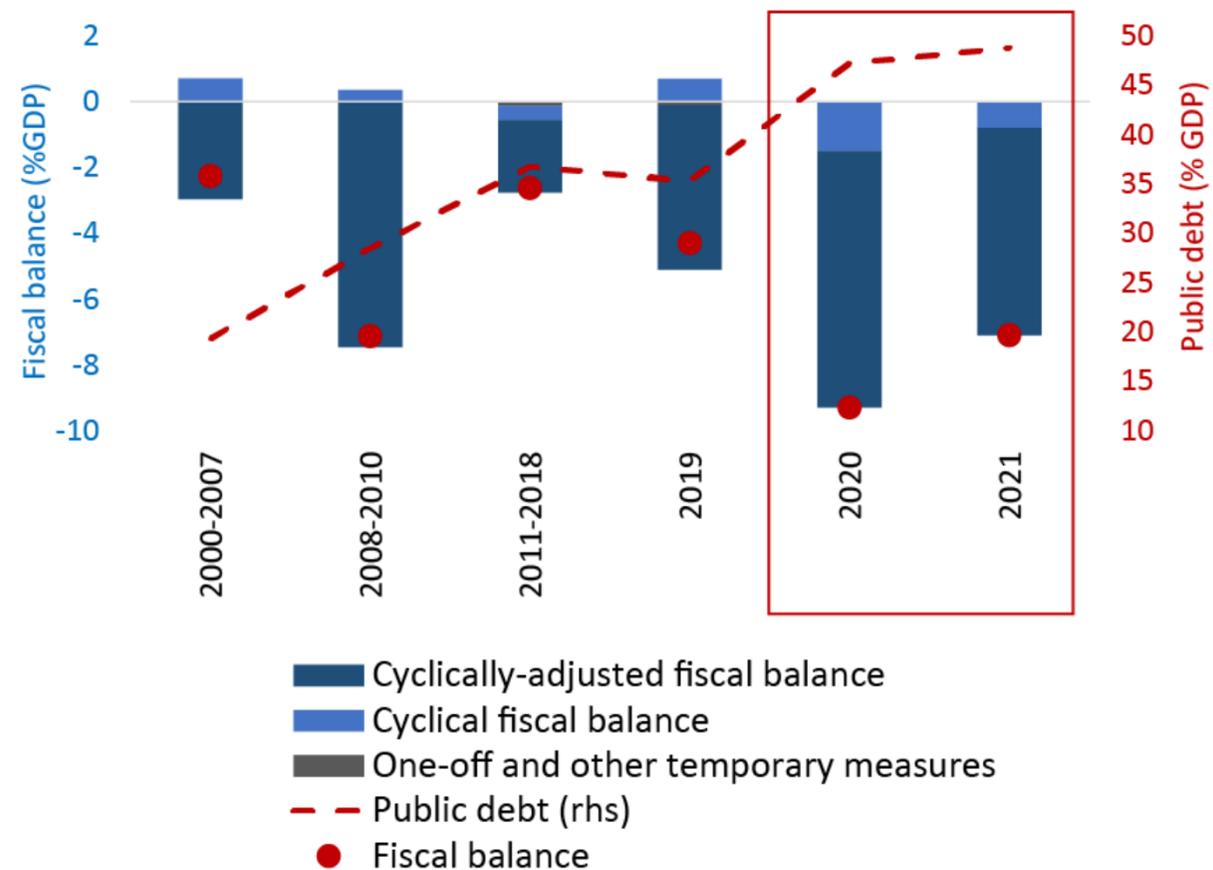
Source: Eurostat, AMECO, World Bank calculations

# 1 Where does Romania stand today?



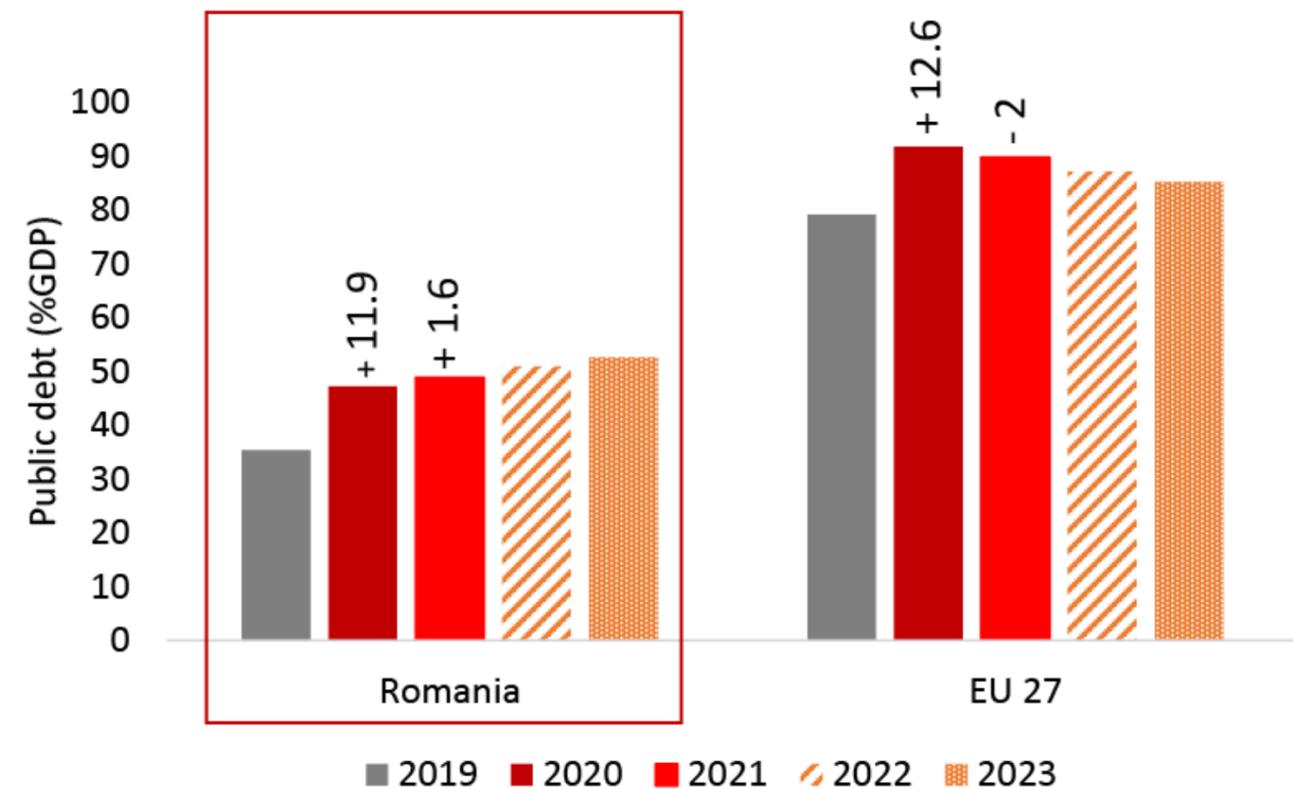
## Large fiscal deficits and public debt

Fiscal deficits –already high before the pandemic –widened as government moved to limit the impact of the pandemic on output, employment



Source: AMECO

During COVID-19, Public debt stock rose by 12% of GDP as financing needs increased, and will remain elevated in the medium term



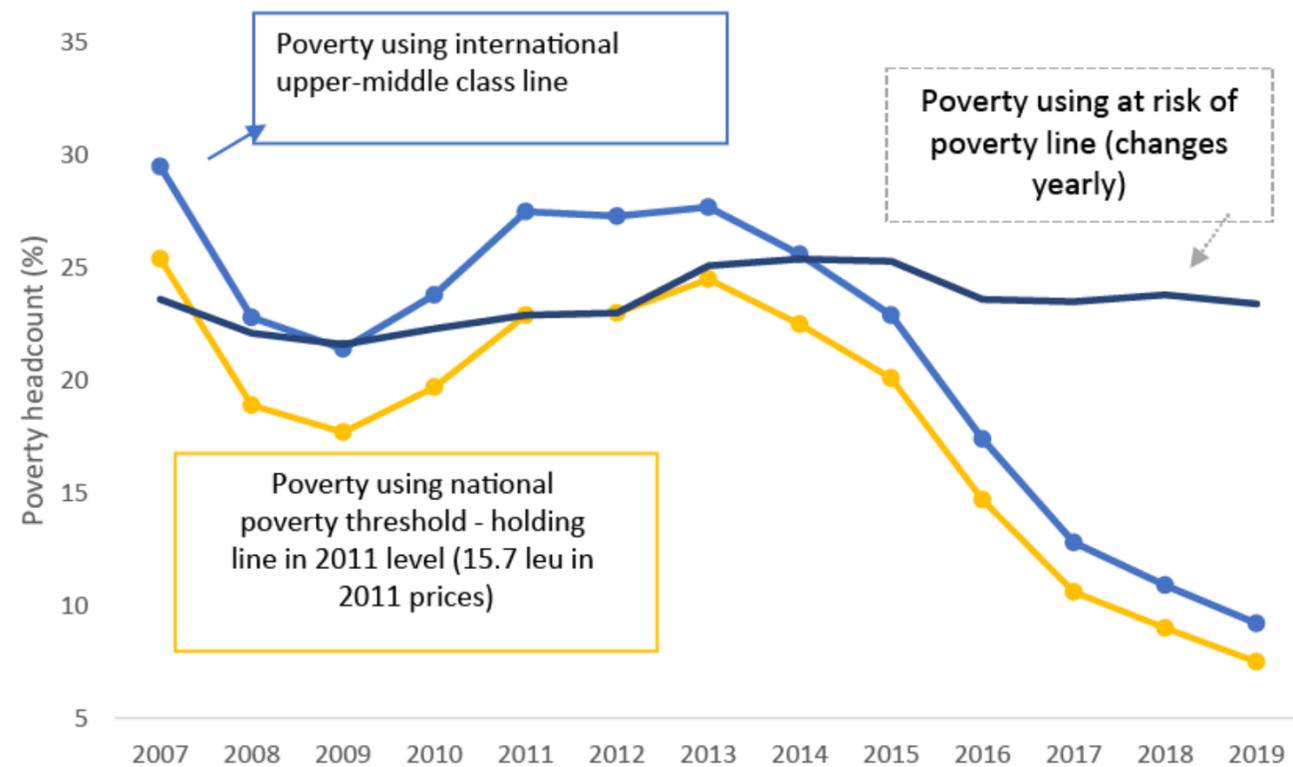
Source: AMECO

# 1 Where does Romania stand today?



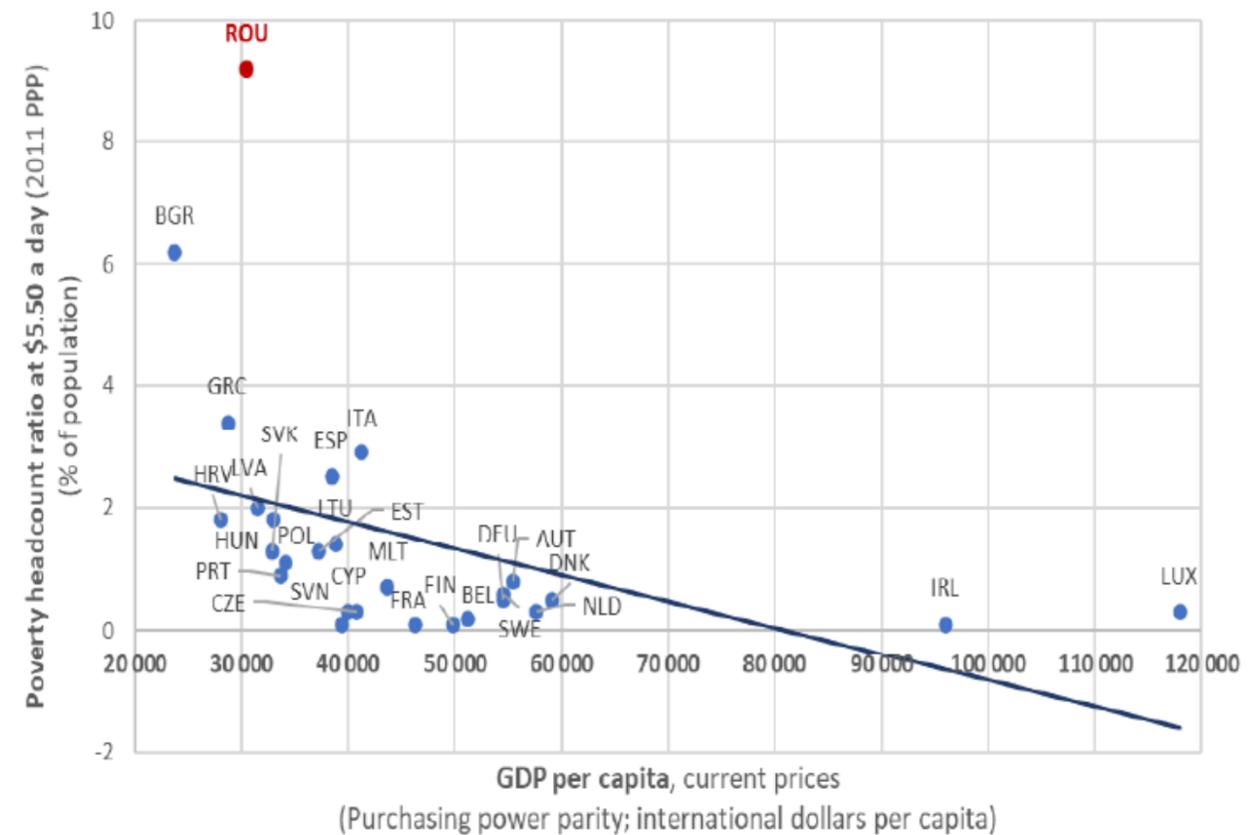
## Highest poverty rate in the EU

Significant progress has been made in reducing poverty and inequality over the past decade.



Source: World Bank staff calculation using EU SILC 2008-2020

But in 2020, Romania still has the highest poverty rate in the EU based on the international poverty line of \$5.5 a day at 2011 revised Purchasing Power Parity.

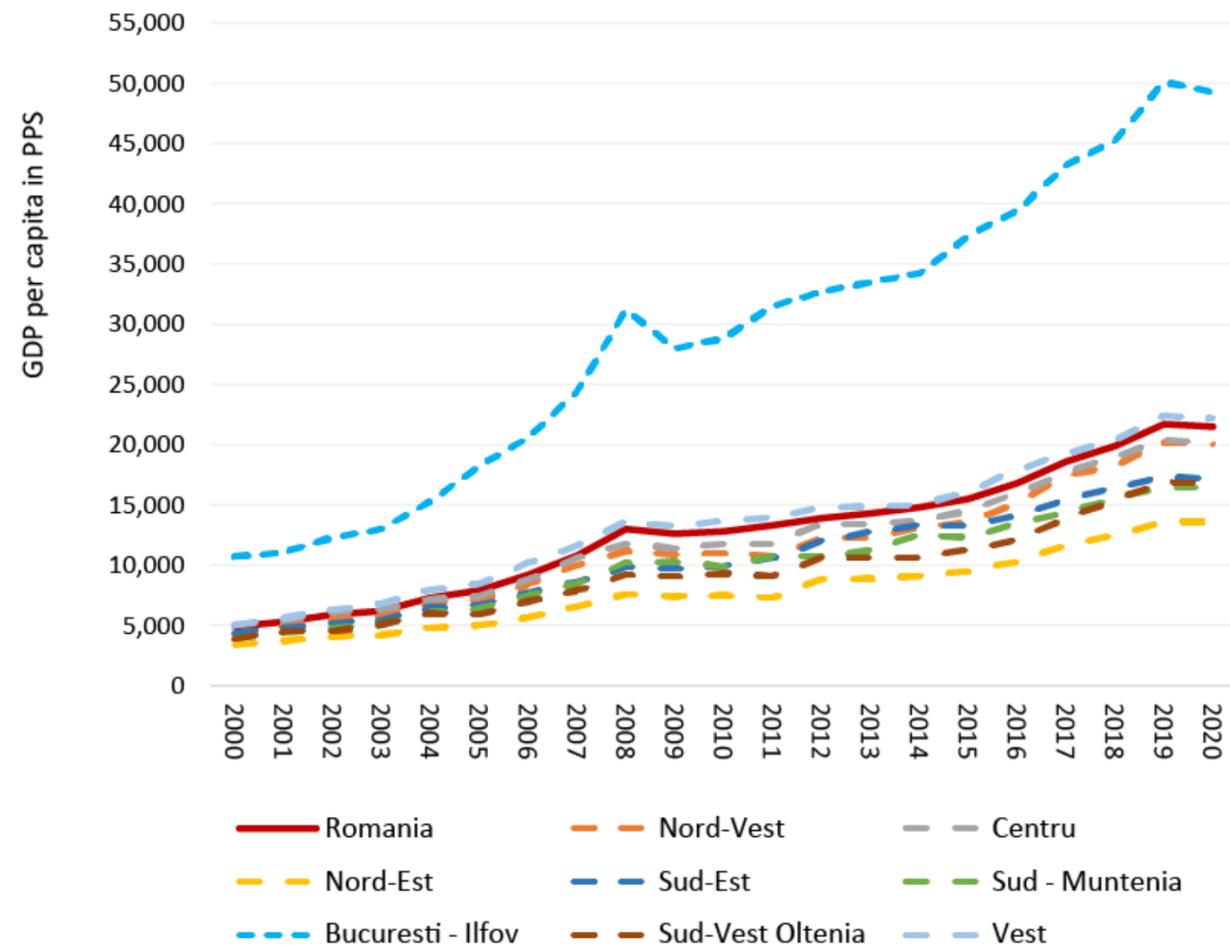


Source: World Bank Development Indicators and latest household survey (EU SILC 2020).



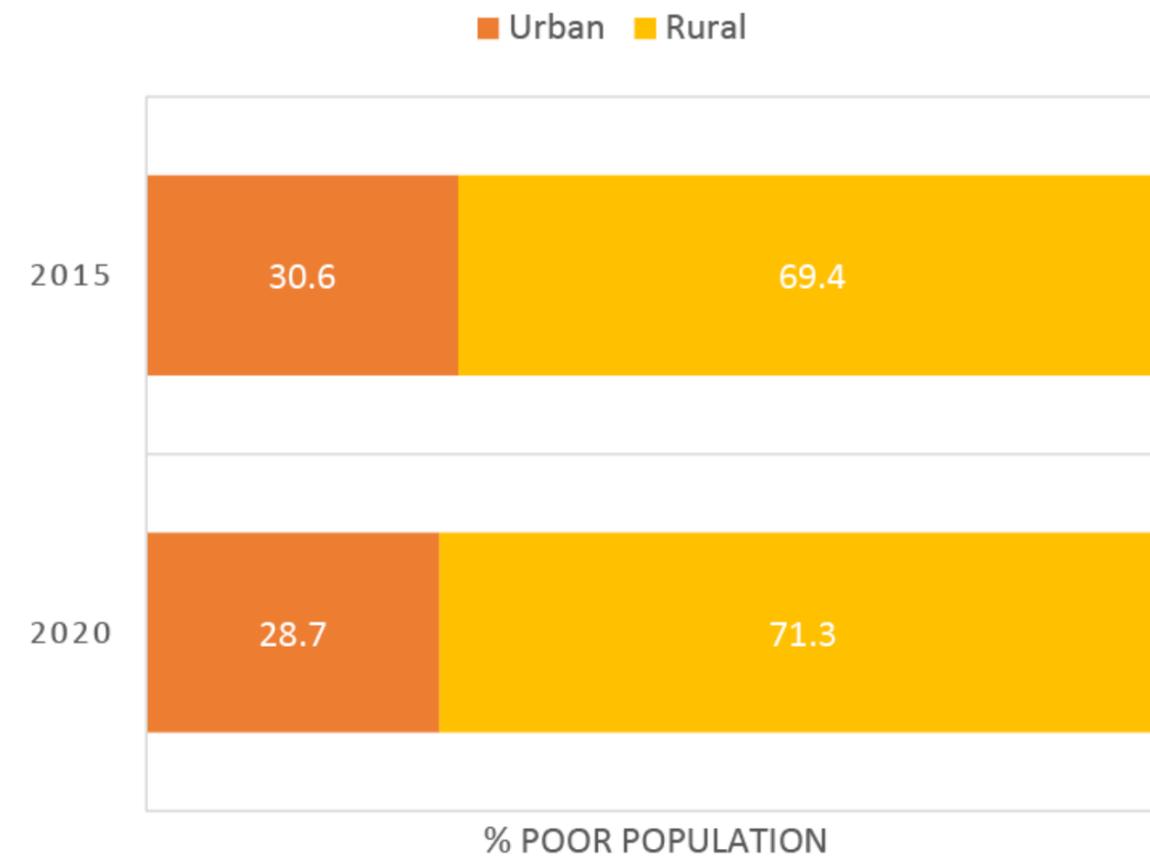
## A “tale of two Romanias”: urban vs. rural

**Bucharest-Ilfov has by far the highest income per person**



Source: Eurostat

**Out of every 10 poor Romanians, 7 live in rural areas.**



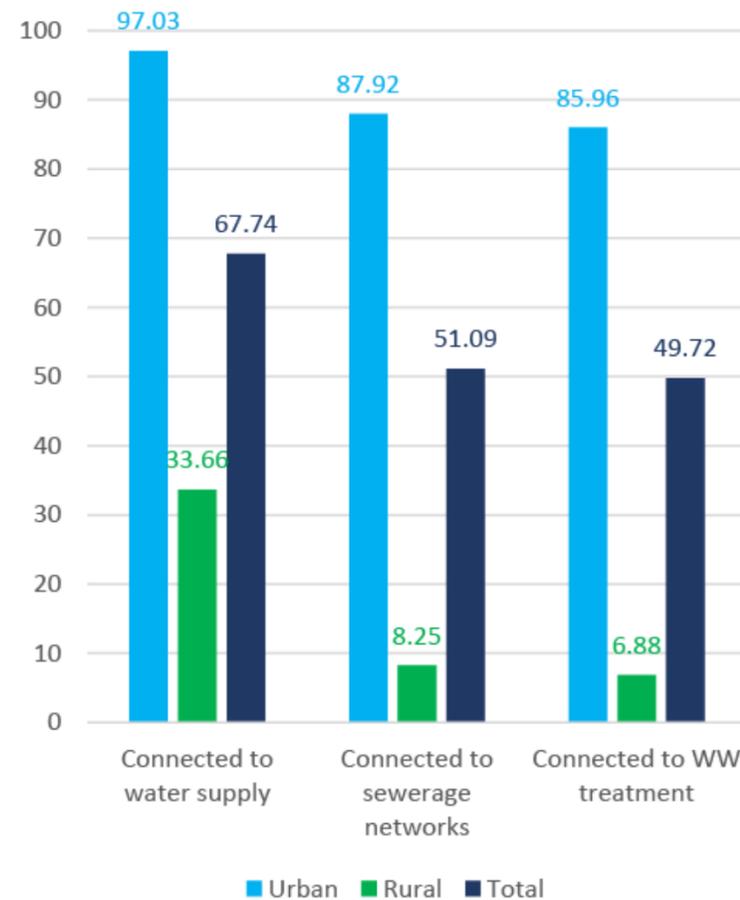
Source: World Bank calculations based on EU-SILC 2020 and 2015..

# 1 Where does Romania stand today?



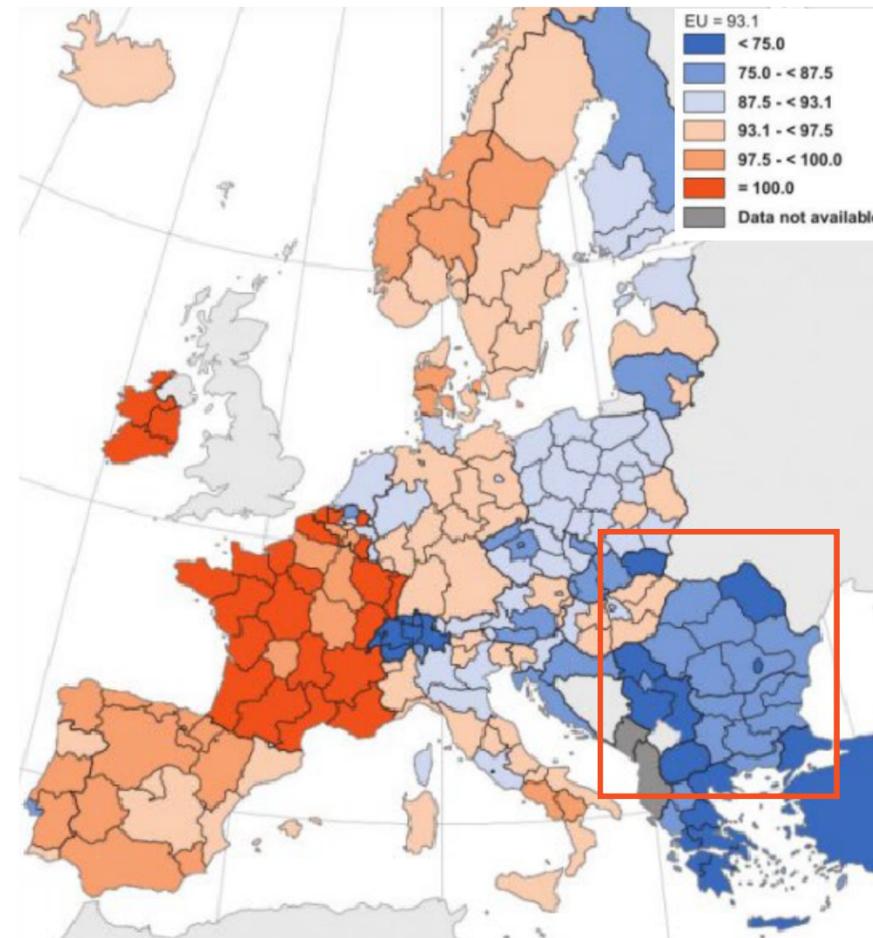
## Low and unequal access to public services

Romania is the only EU country without universal access to water. The urban-rural divide is also sharp.



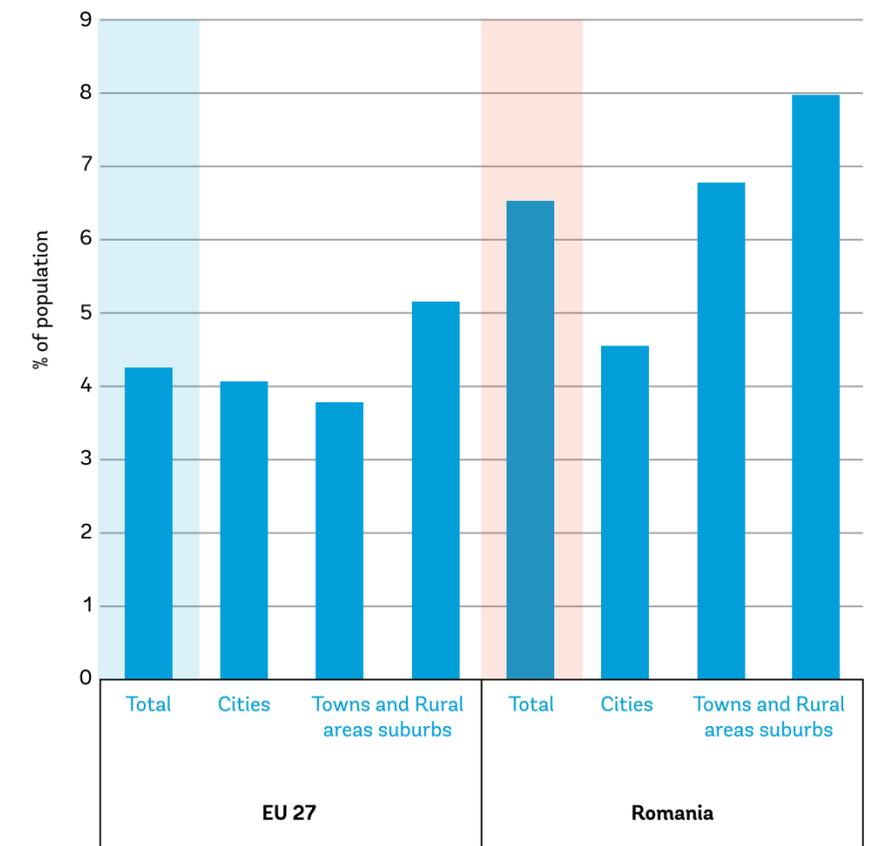
Source: INS, 2017

Participation rates in early child education remain below EU average, especially in the North-East.



Source: Eurostat, 2020.

Self-reported unmet needs in medical examination are more severe in Romania than the EU average, especially in rural areas.

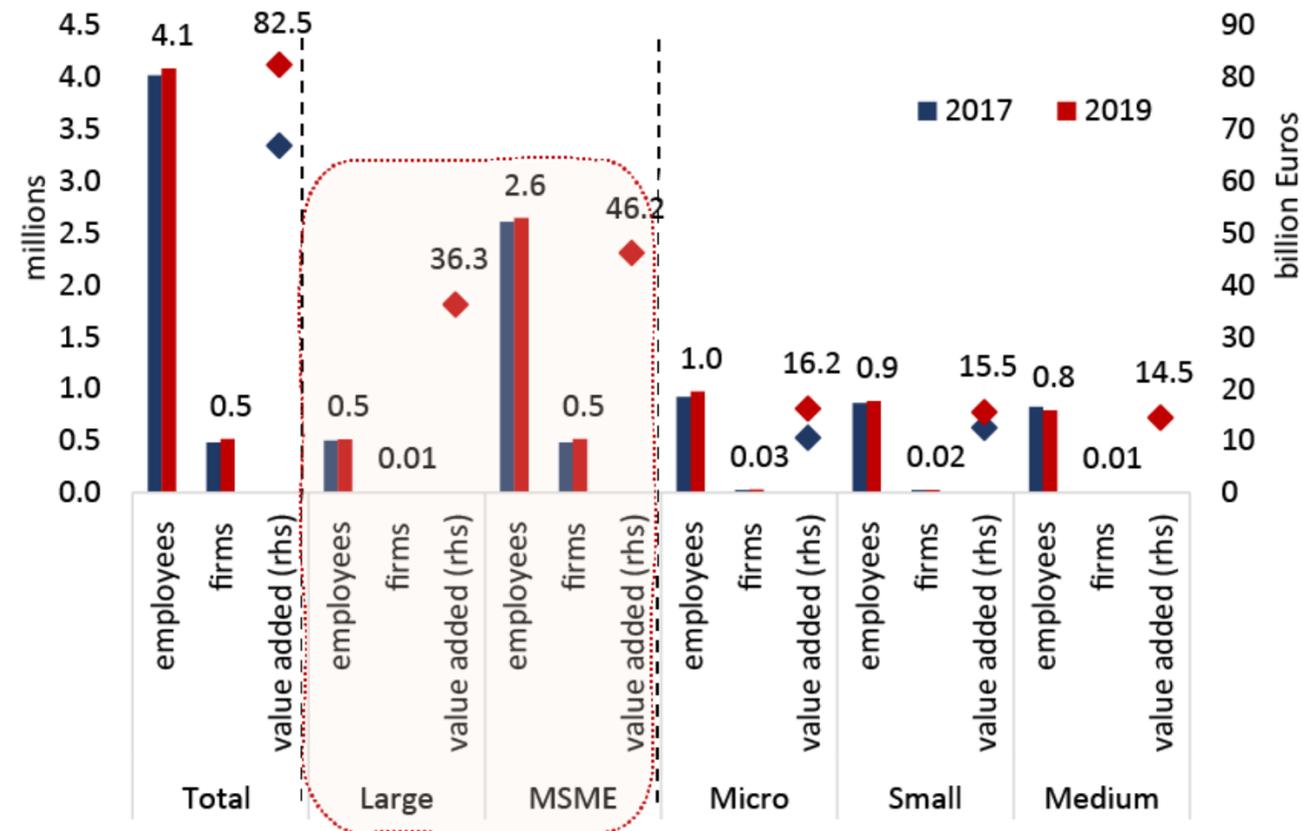


# 1 Where does Romania stand today?



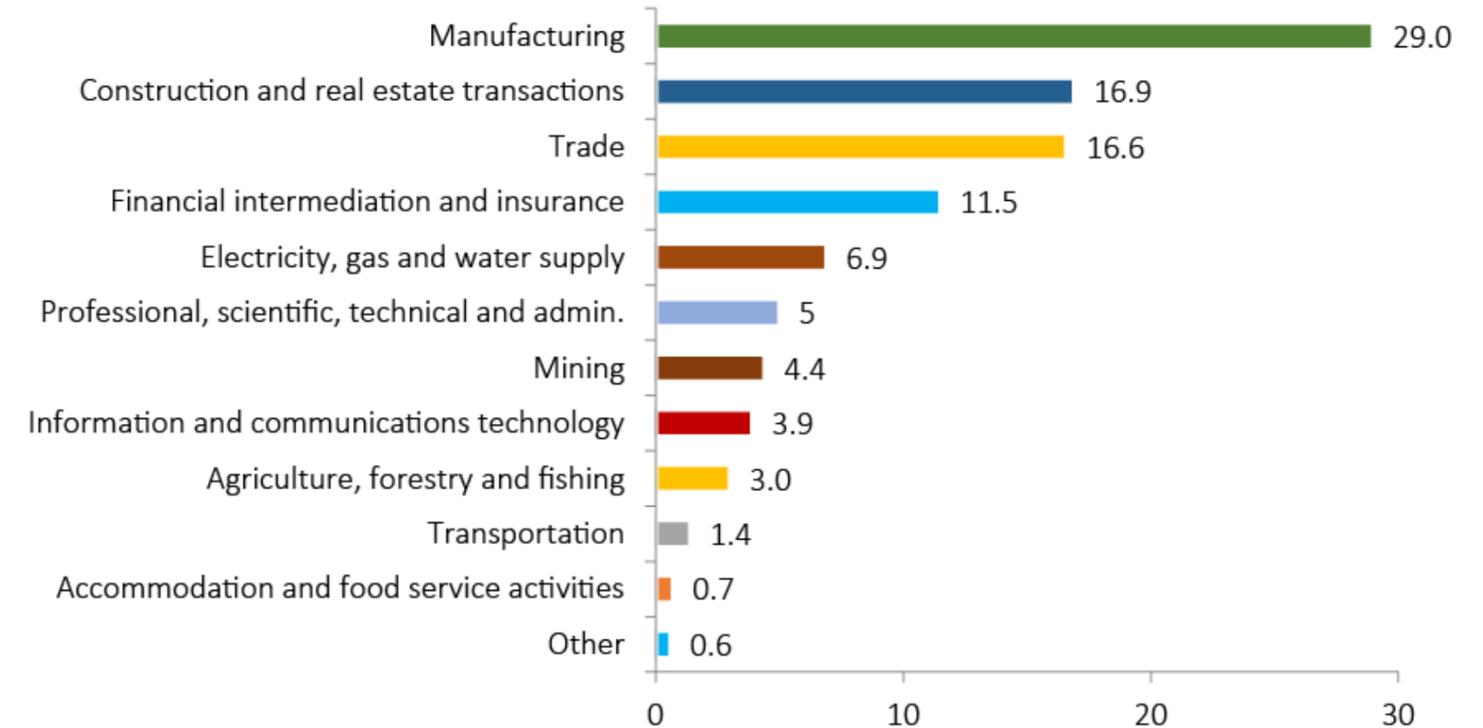
## Private sector dominated by small firms in established sectors

### Private sector continues to be dominated by Micro, Small, and Medium Enterprises (MSMEs)



### With most of the Foreign Direct Investment (FDI) stock concentrated in 'low innovation' activities..

FDI stock by main economic activity (% total), 2019



Source: Eurostat

Source: National Bank of Romania



Emerging risks and new opportunities for Romania's sustainable and inclusive growth in the medium- and long-term.

## 1 COVID-19 pandemic

- Widening deficits and rising debt
- Disproportionated - and lasting - adverse effects on poor and vulnerable households (income decline, access to education and health, etc.)

## 2 War in Ukraine

- Energy security considerations
- Negative economic impact (e.g. rising food and energy prices), especially on the poorest and most vulnerable
- Inflows of Forcibly Displaced Persons

## 3 Digitalization

- Opportunity to boost productivity, and transform jobs and skills
- Risks of shifting demand and skills, and deepening existing inequality between regions, and across population groups

## 4 Green transition

- Widening deficits and rising debt
- EU-wide commitment to reduce emissions and put growth on more environmentally sustainable path

## 5 EU funds

- Unprecedented amount of funding available for Romania to support post-pandemic recovery, green and digital transitions, and support convergence with the EU
- Requirement of strong institutional capacity to absorb and use the funds efficiently

**These complex challenges are also interrelated**

2

# What is holding back Romania: constraints to growth and prosperity?

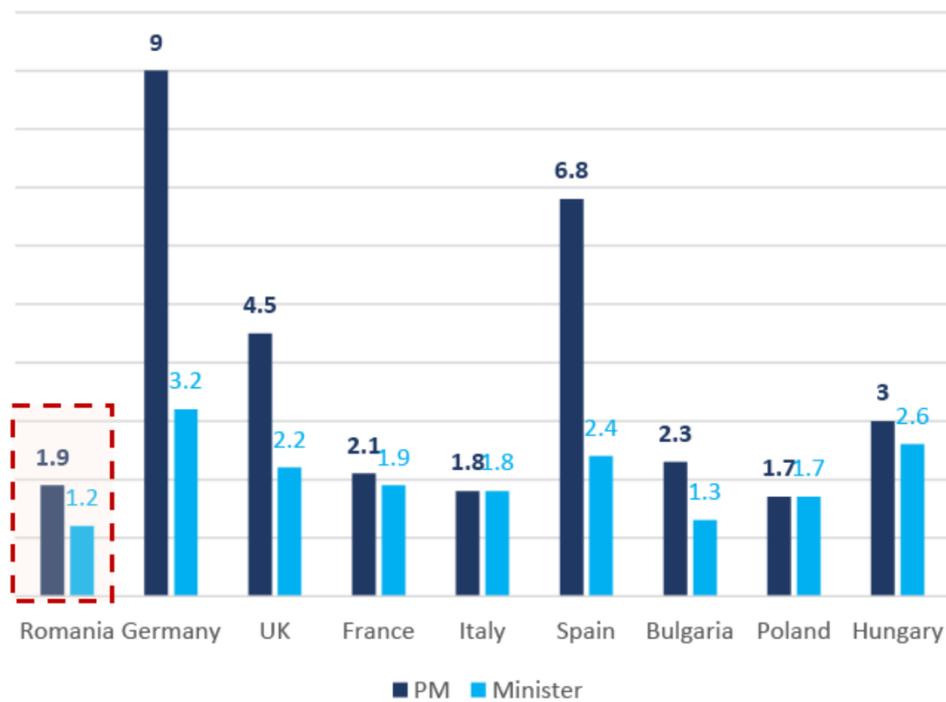




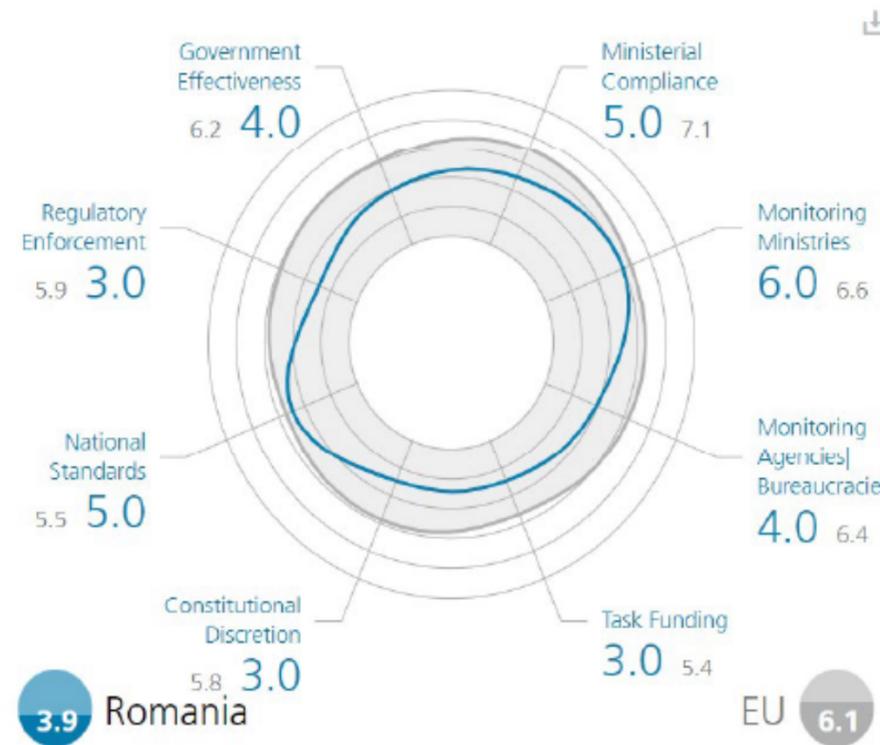
## Weak institutions, low administrative capacity, and lack of long-term commitments

**High political volatility leads to constant changes in priorities and discontinuity in reforms**

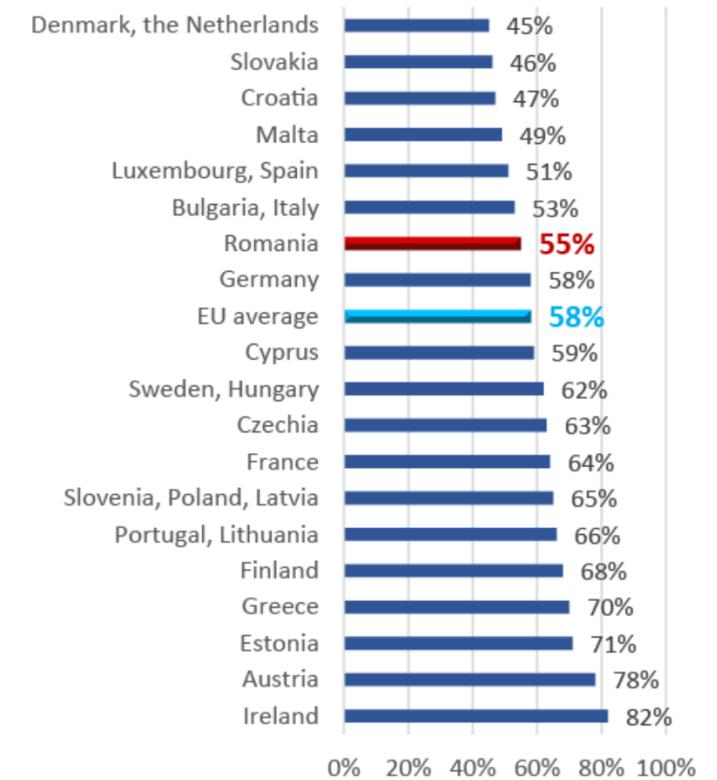
1990-2021 – Average term for Prime Ministers and Cabinets



**Romania falls well below the EU average for efficiency and effectiveness of policy implementation**



**Lack of capacity to utilize effectively resources, including European funding, remains a key challenge for Romania**



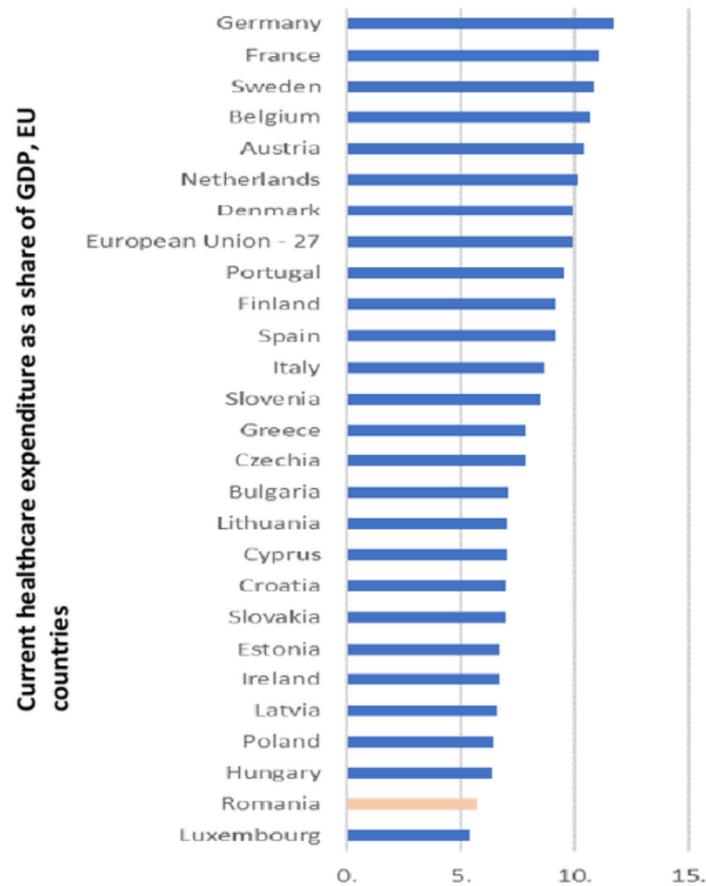
Source: National School of Political and Administrative Studies, July 2017, "Chronic Government Instability"

Source: The Sustainable Governance Indicator 2020, Bertelsmann Stiftung relies on a combination of expert qualitative assessments and quantitative data drawn from official sources



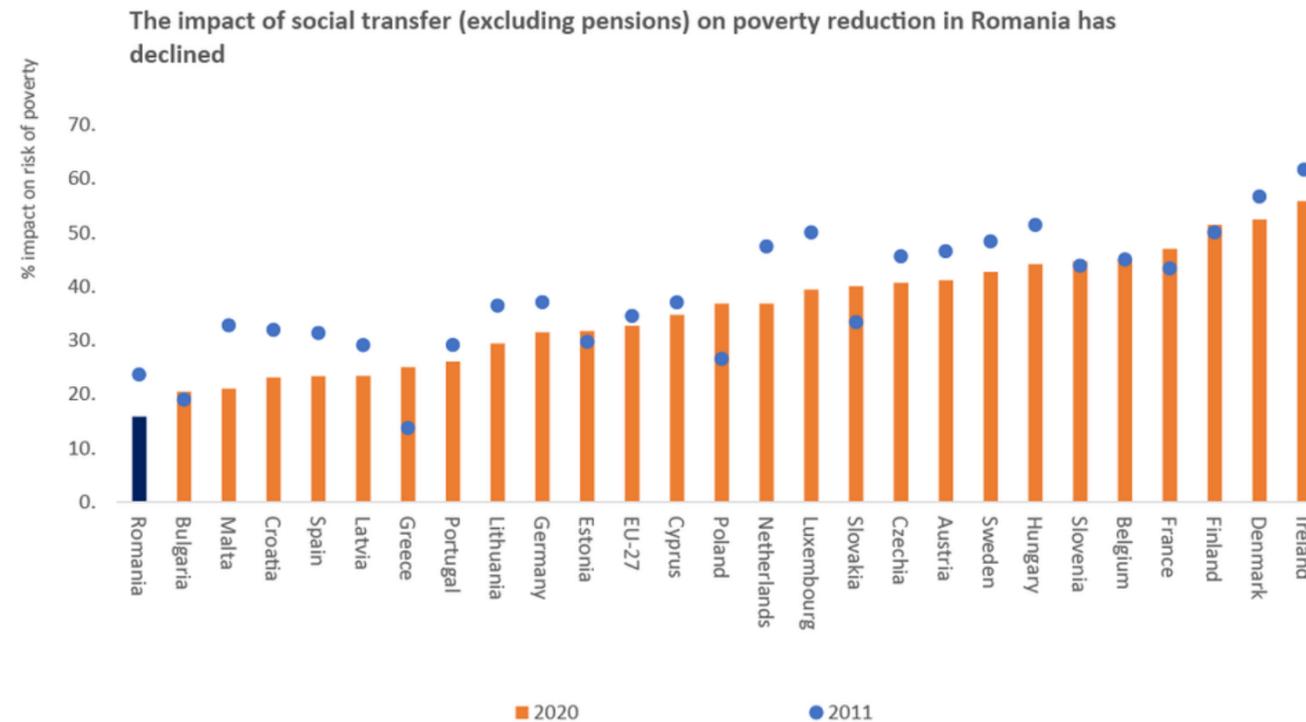
Insufficient and inefficient spending on human capital development, and low provision of public services

**Expenditure on human capital and social services is one of the lowest in the EU**



Source Eurostat 2019

**Insufficient spending and low generosity of social assistance programs led to Romania having the lowest impact of social transfers on poverty reduction in the EU**

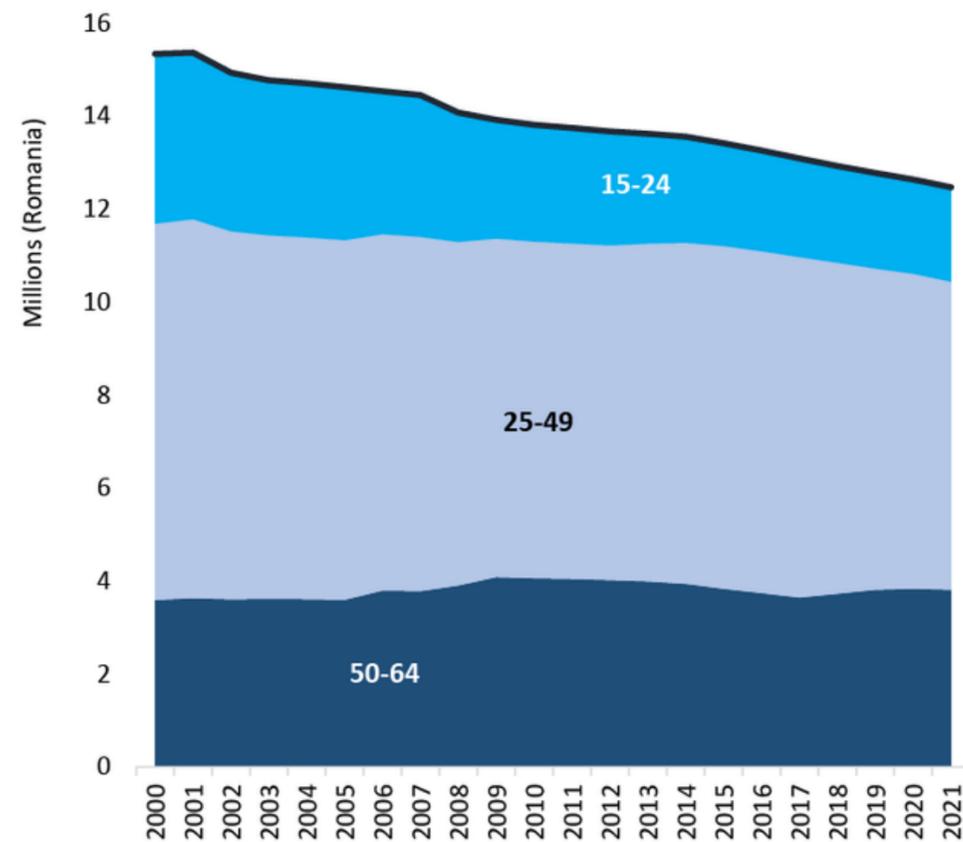


Source: Eurostat, 2021.



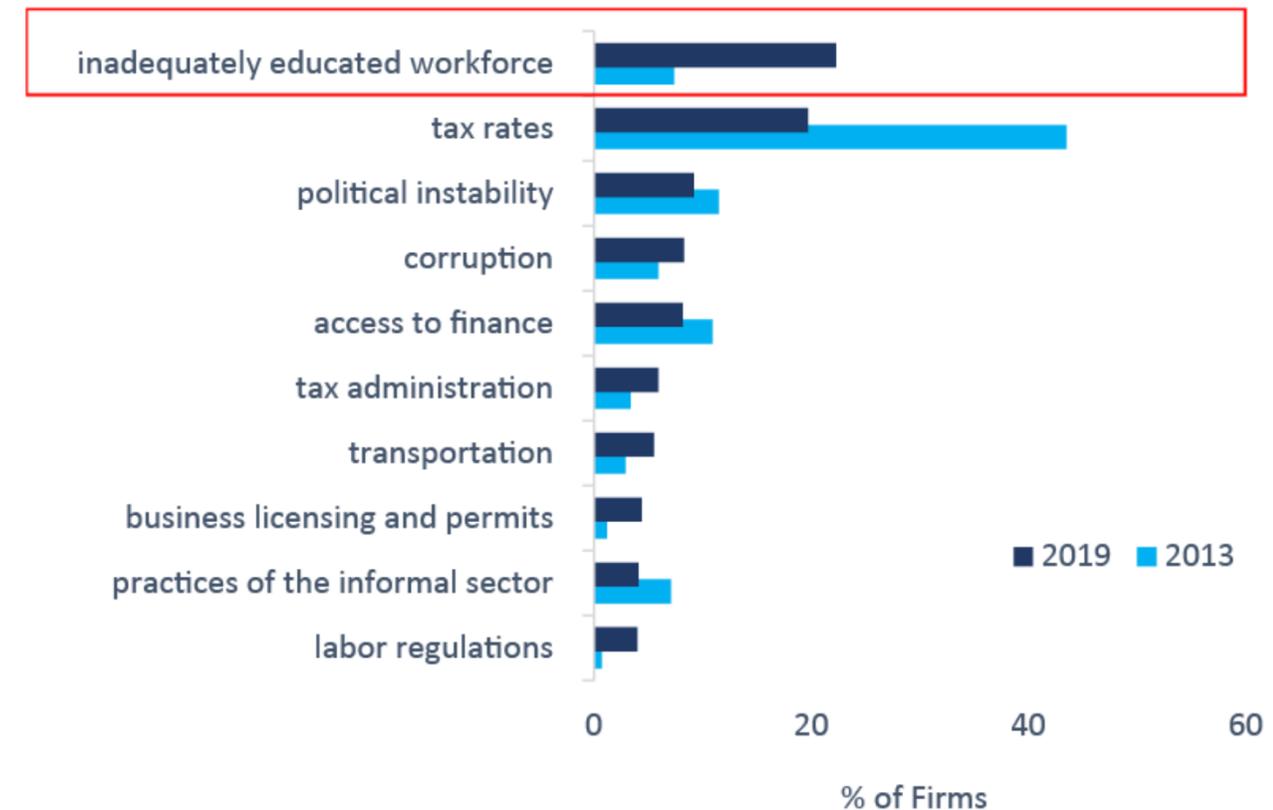
## Labor shortages and skills mismatches

Romania's working-age population (especially youth) is declining. In addition, Romania has one of the highest share of emigrants in the population among EU countries.



Source: Eurostat

Skills is the top constraint to private sector growth, and has been intensifying

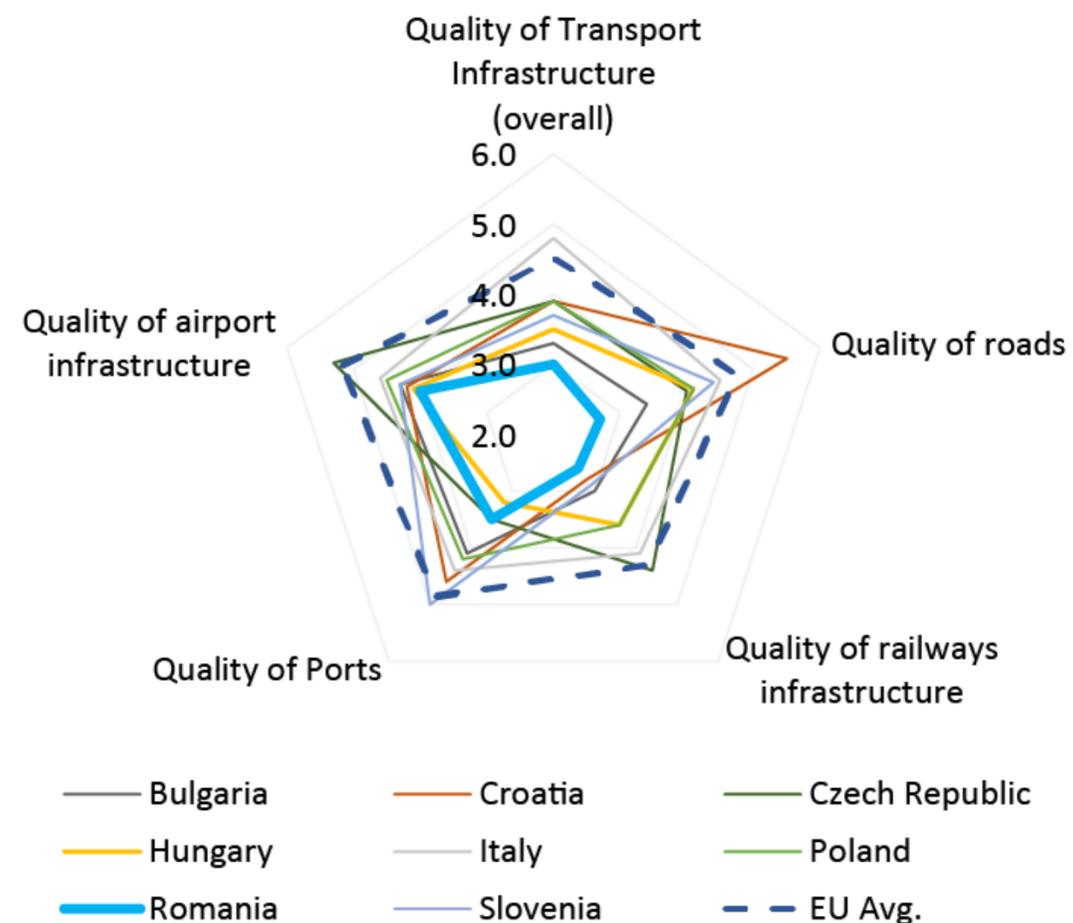


Source: World Bank Enterprise Survey 2019  
Source: World Bank 2021

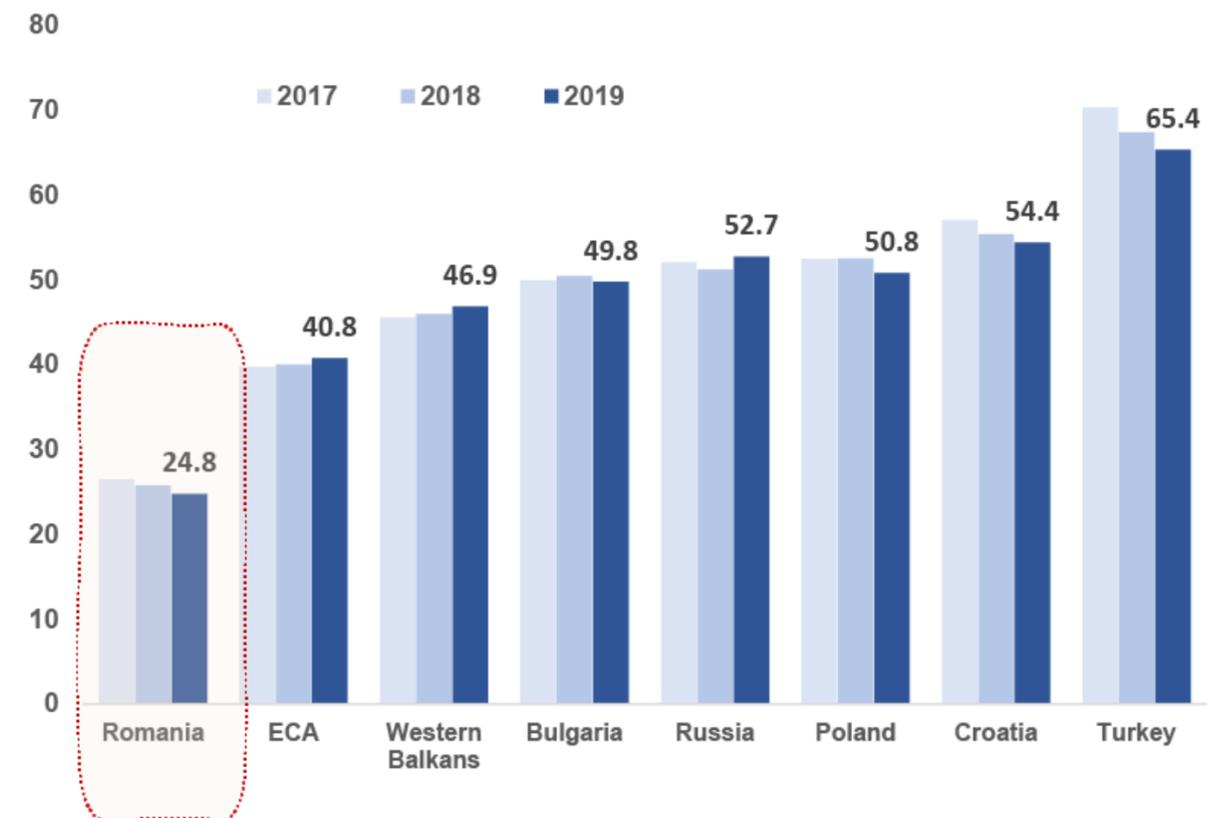


## Low connectivity and shallow financial sector impeding private sector development

**Romania's infrastructure (particularly transport) conditions overall are the lowest in the EU**



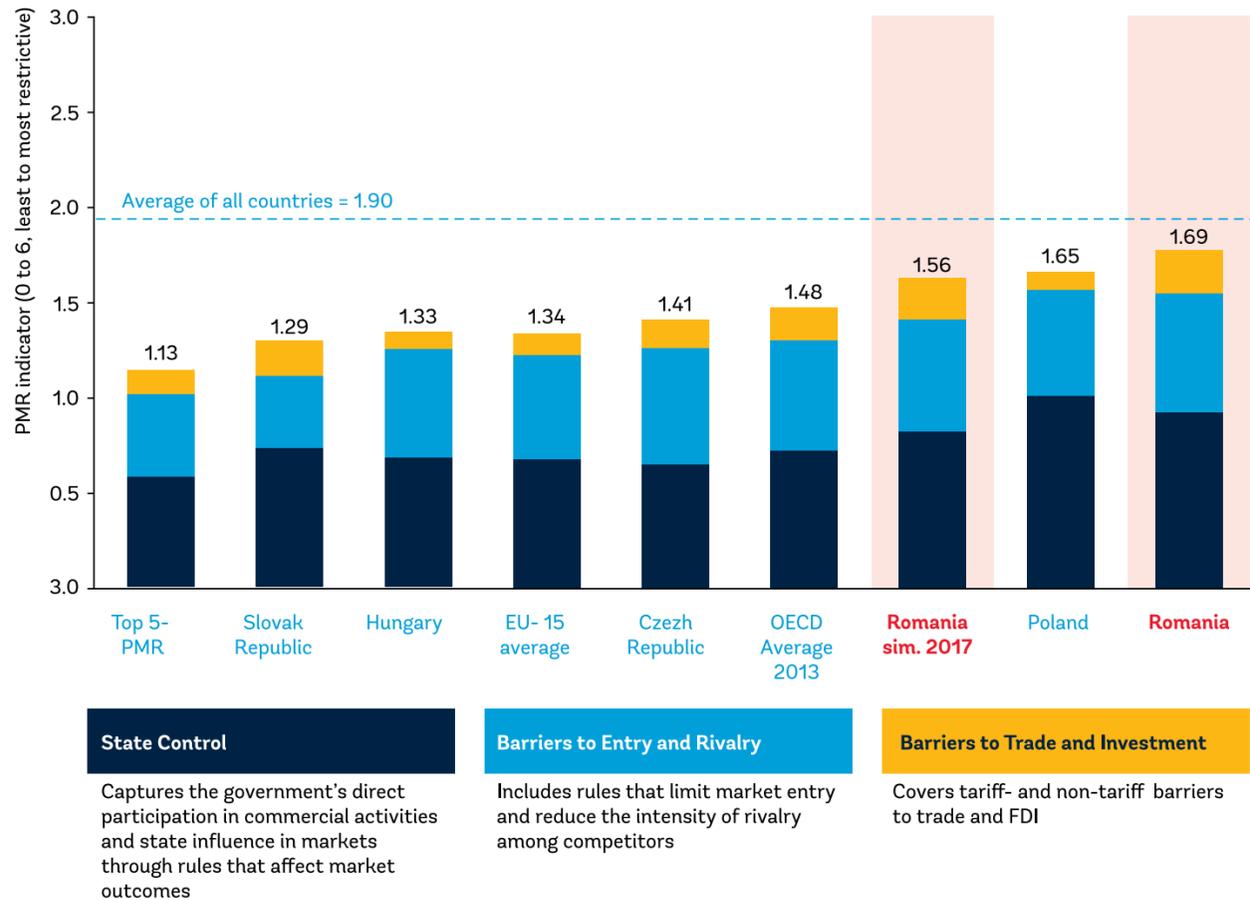
**The financial sector (particularly financial intermediation) remains shallow. Financial inclusion in Romania is a tale of “two Romanias” –with significant urban/ rural disparities.**



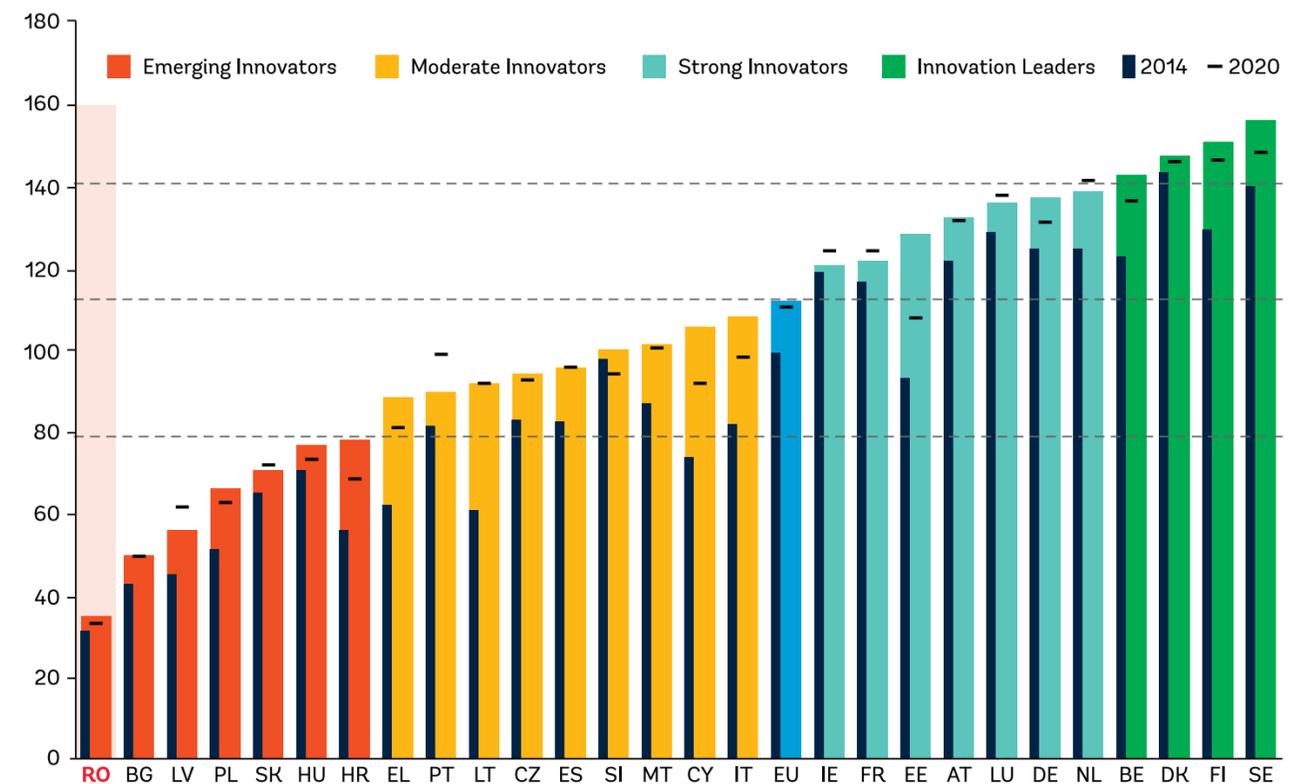


## Unpredictable business environment and limited innovation

**Impediments to competition in Romania are associated with state control of the economy and barriers to entry and rivalry, especially in services**



**Romania's economy is limited in its innovative capacity, ranking at the bottom of the EU innovation scoreboard**



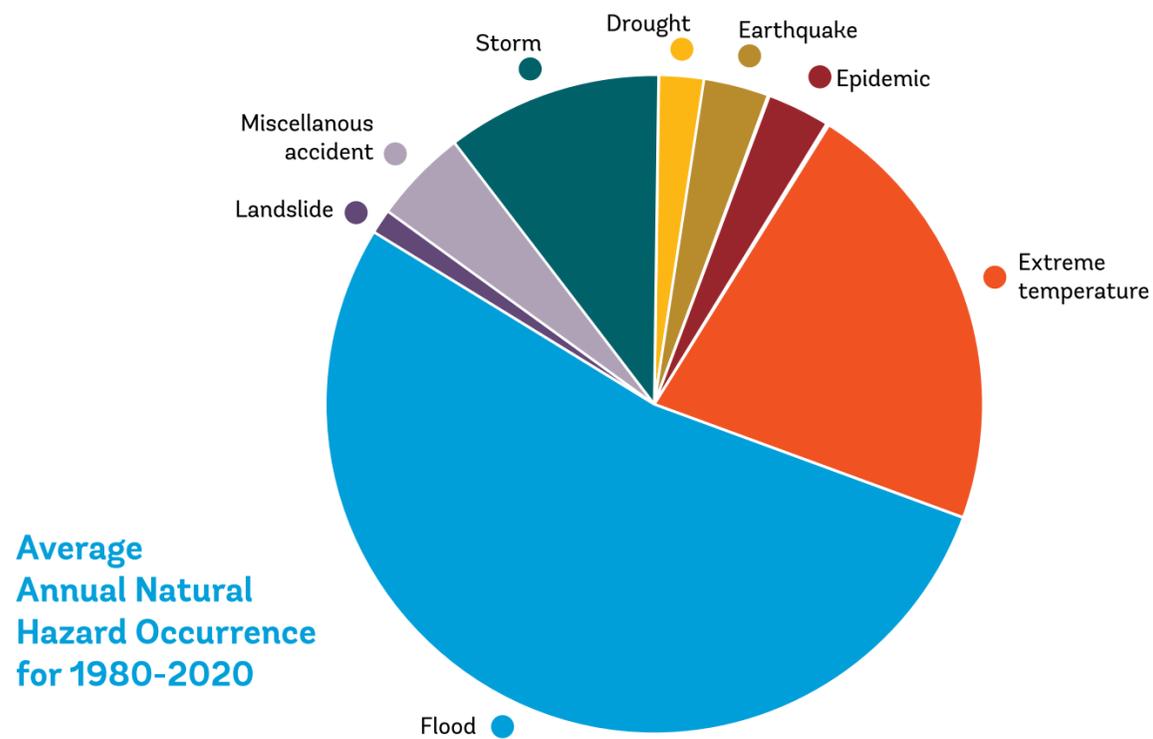
Source: Markets and People: Romania Country Economic Memorandum. International Development in Focus. Using OECD Product Market Regulation (PMR) indicator, as in lootty et al. (2020)

Source: DESI 2020



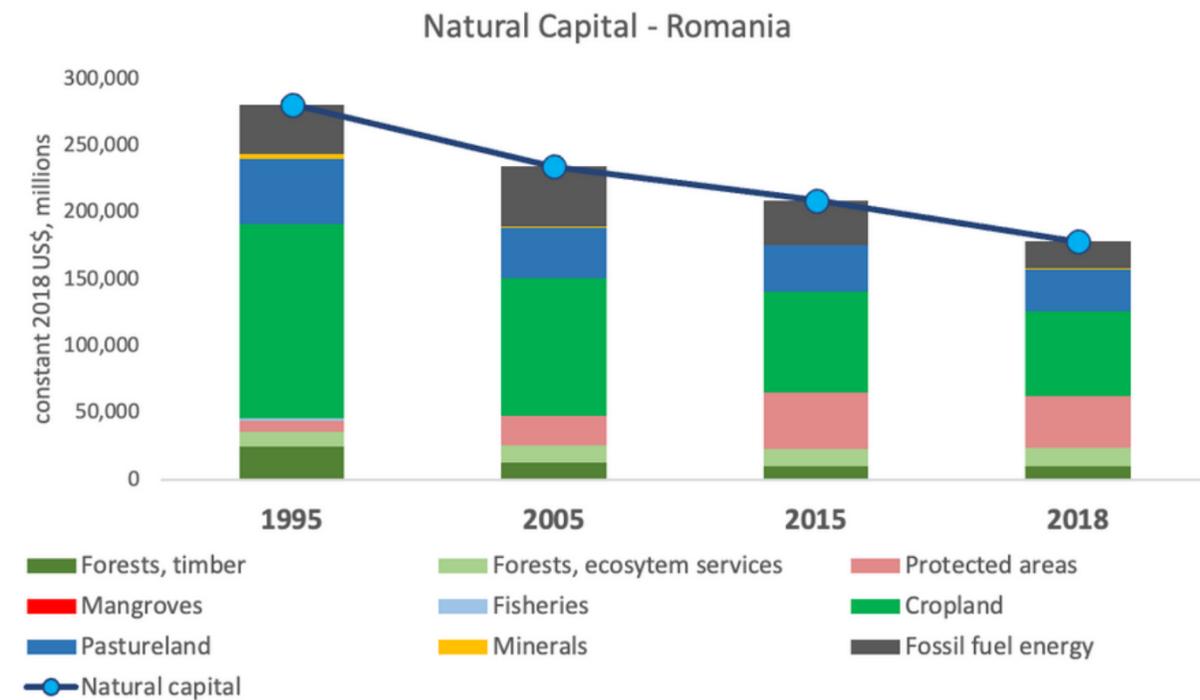
## Vulnerability to natural disasters and untapped opportunity to be more environmentally friendly

Romania is vulnerable to natural hazards (some of which are intensifying with climate change), with vulnerable populations disproportionately affected, but its readiness to adapt relatively low



Source: World Bank

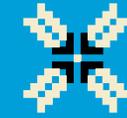
The declining natural capital and European Green Deal commitments necessitate climate mitigation action



Source: World Bank Changing Wealth of Nations (2021)

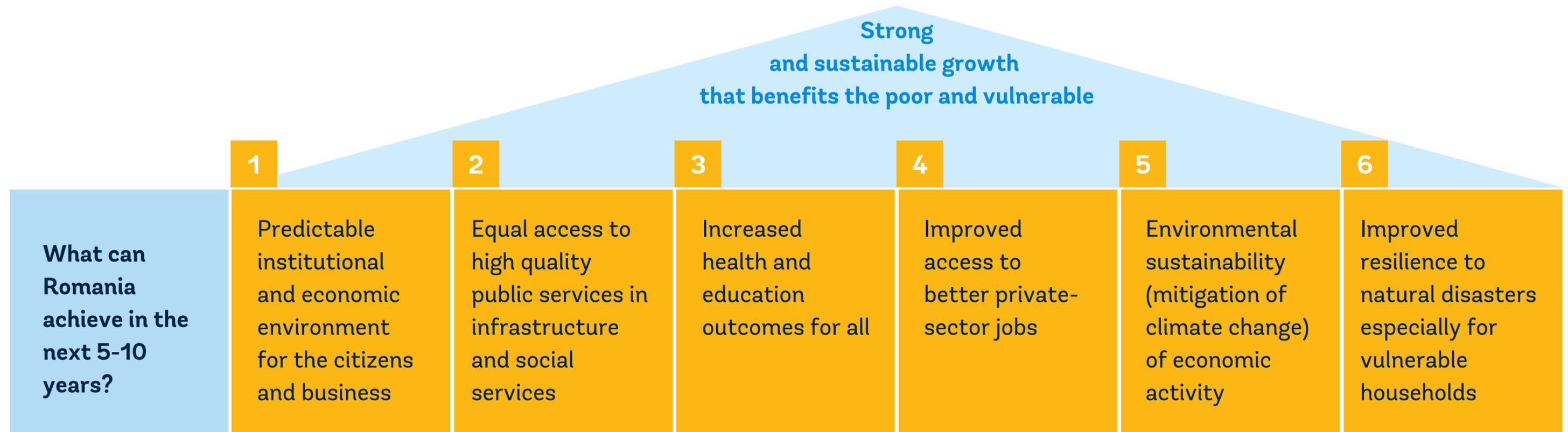
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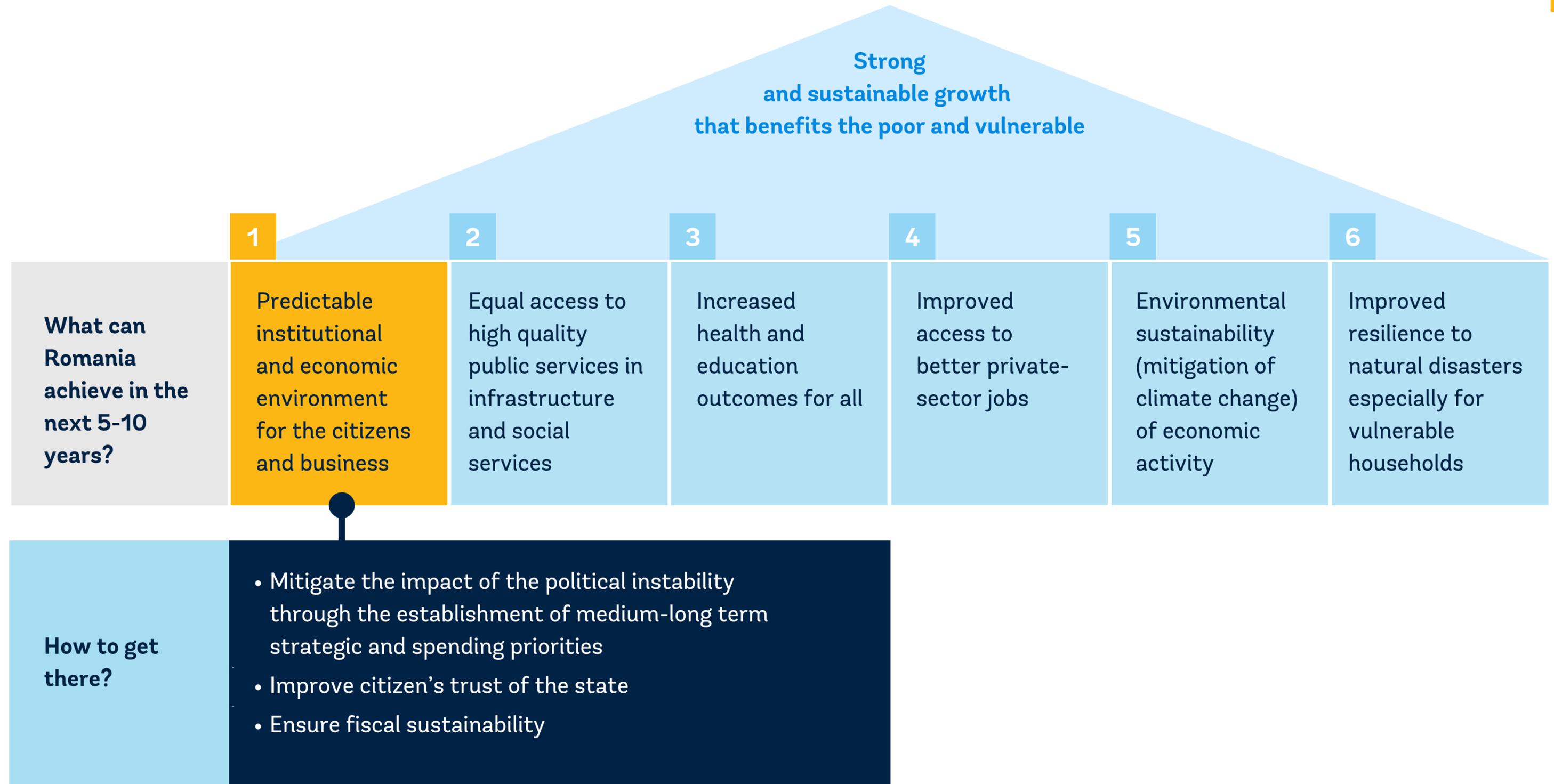
# What are Romania's priorities for inclusive, strong, and sustainable growth?

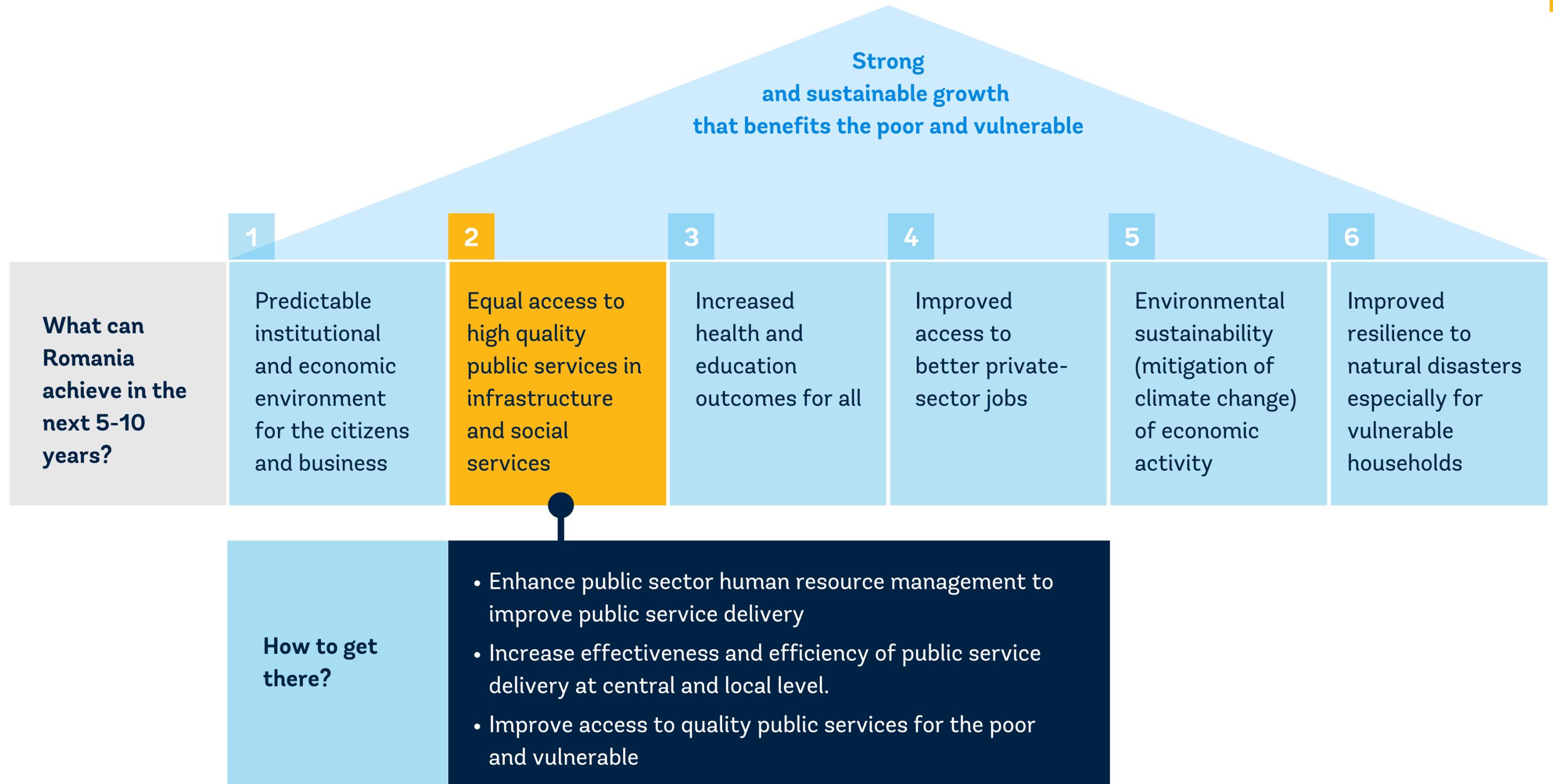


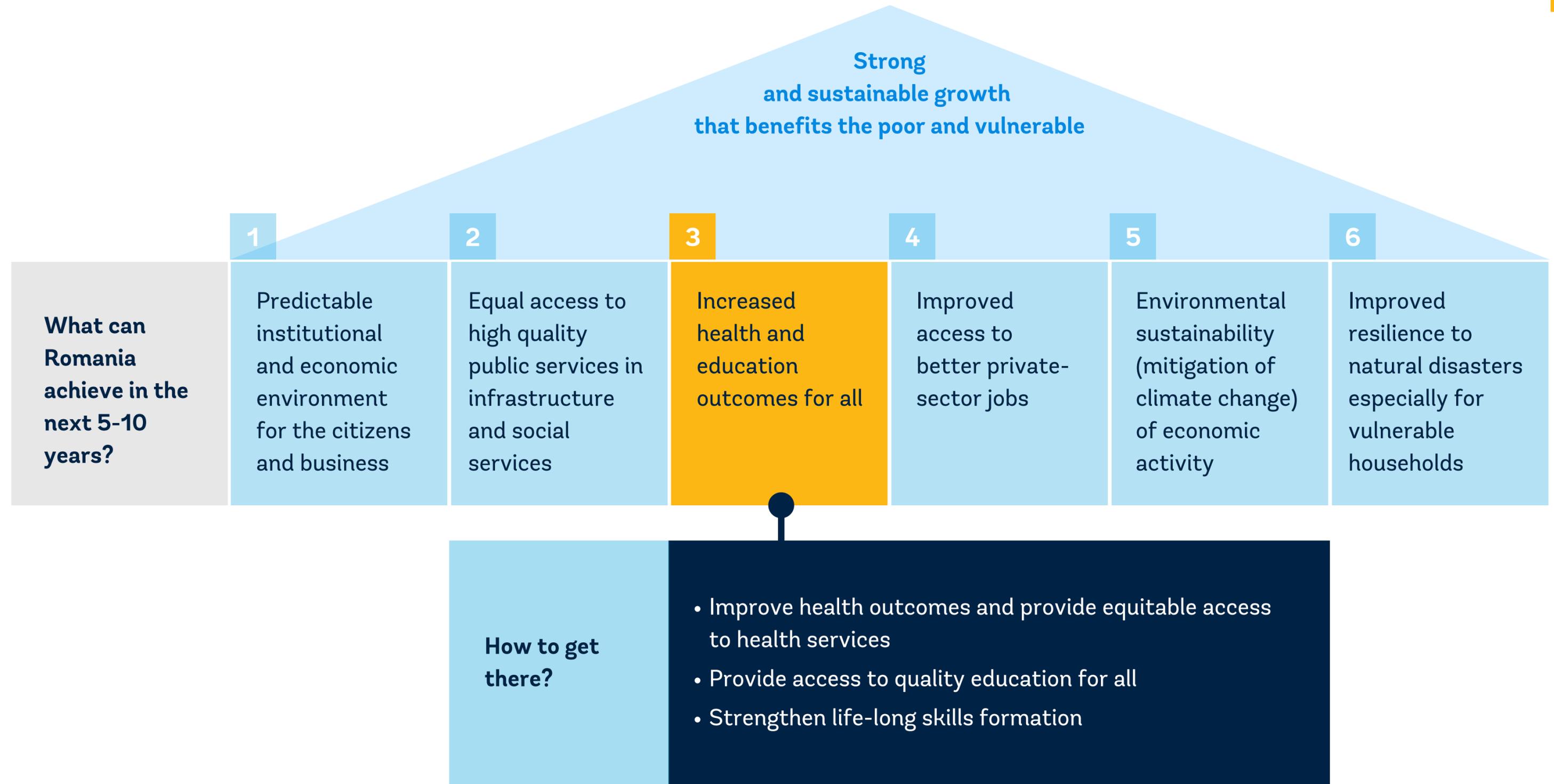


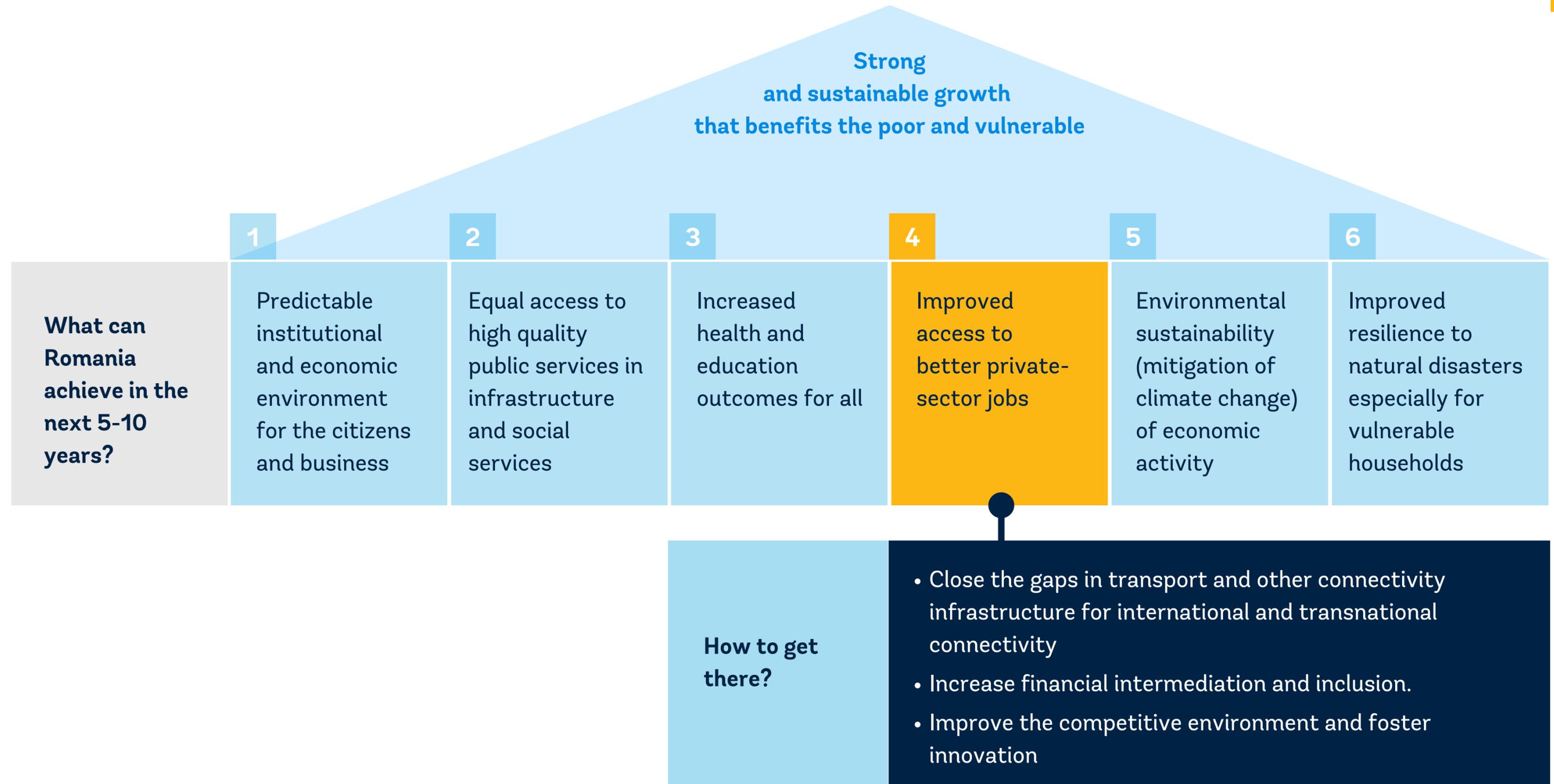
To address the constraints holding Romania back, 6 pathways are identified:

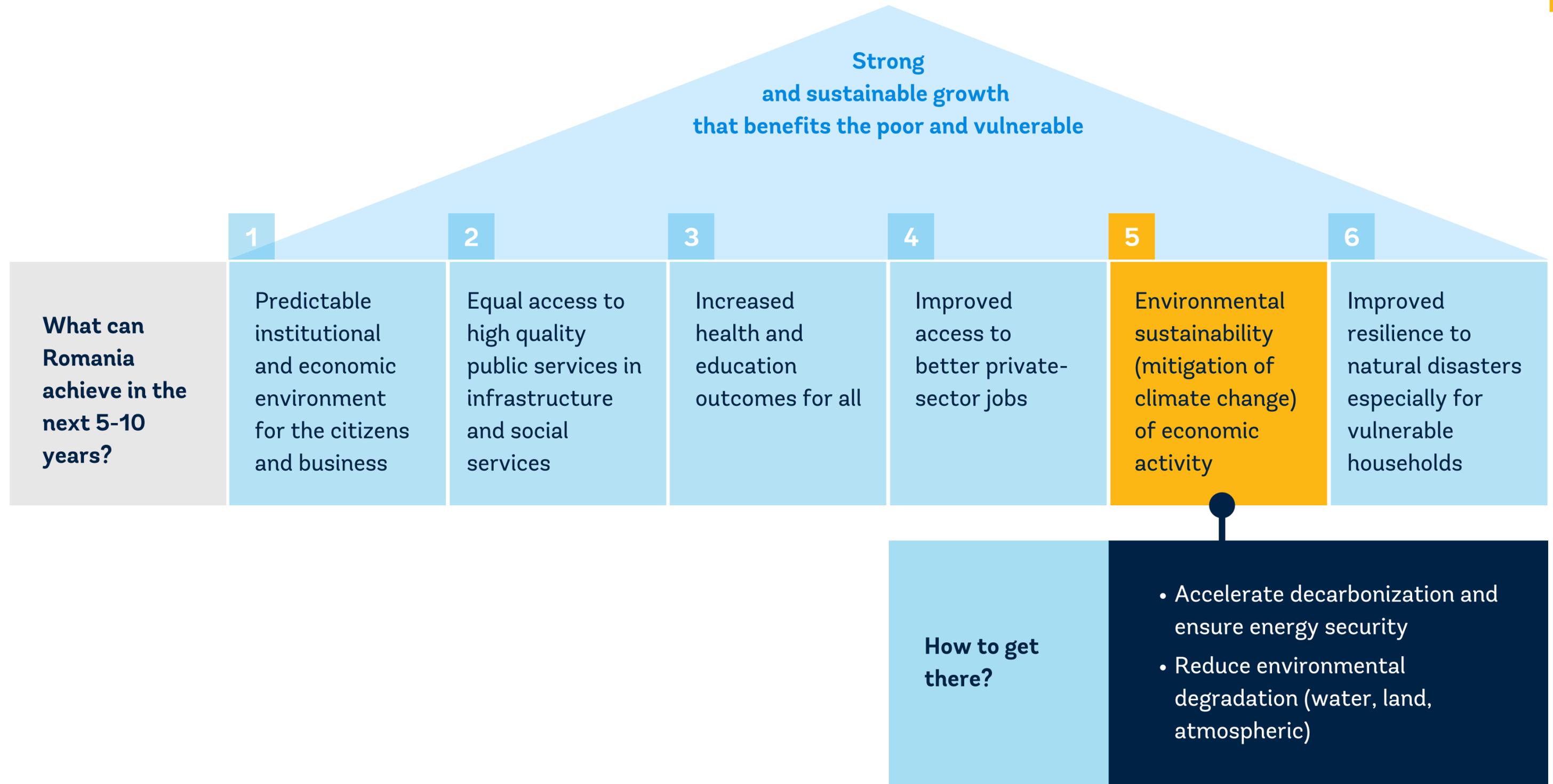


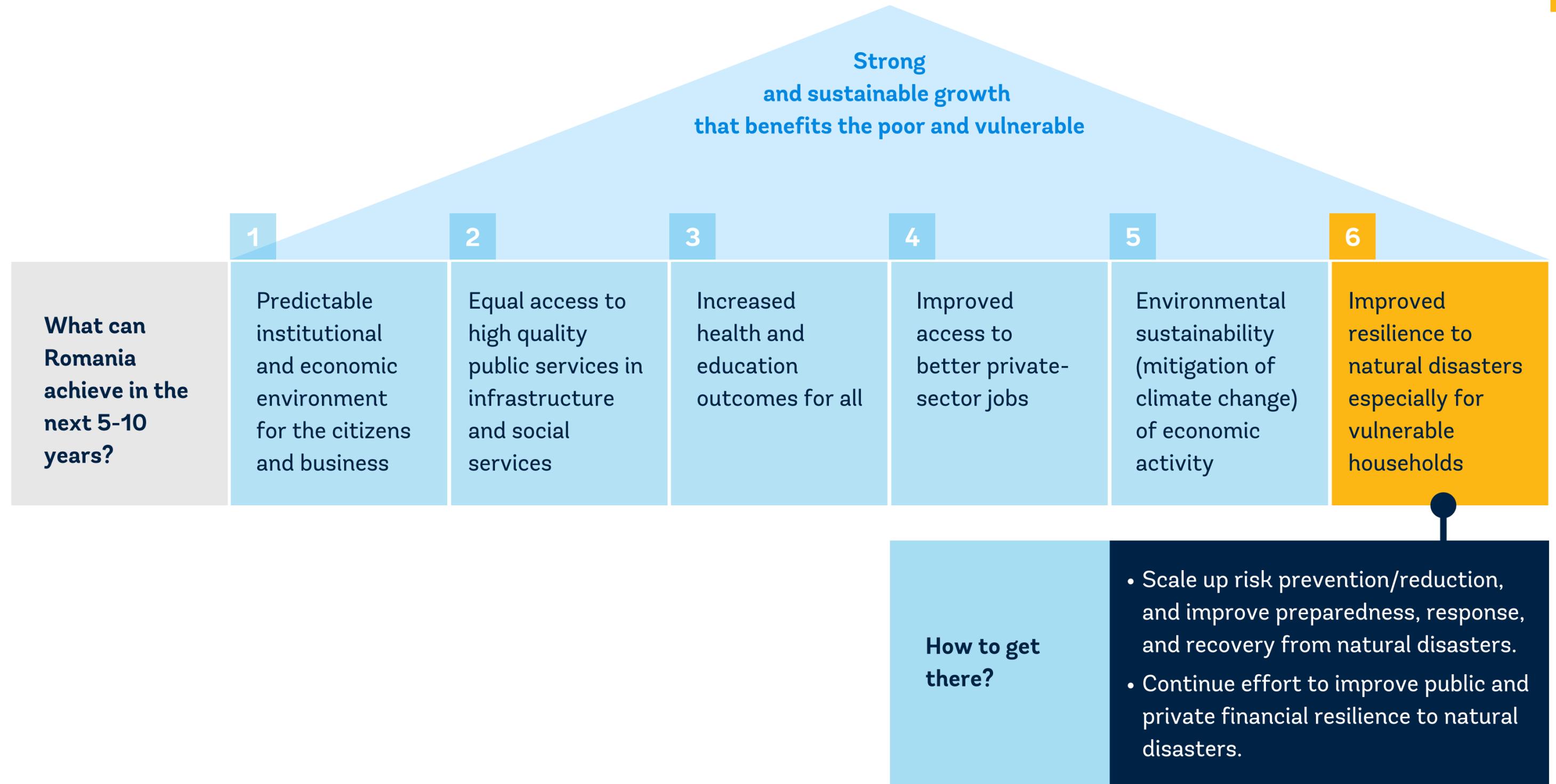












# Next steps

▶ Online consultation SCD	September 8 – October 9, 2022
▶ Face-to-face consultation SCD	September 19 – October 6, 2022
▶ Publication SCD	2023
▶ Online consultation SCD	mid-2023 – 2024