S&P upgrades Romania’s outlook from negative to stable citing abatement of short-term fiscal risks

Standard and Poor's Global Ratings (S&P) affirmed on Friday Romania's long- and short-term foreign and local currency sovereign credit ratings at 'BBB-/A-3', and also revised its outlook on Romania from negative to stable, the Finance Ministry announced.

This is the agency's first upward revision of Romania's outlook since November 2013.

"We revised the outlook to stable because we believe Romania's short-term fiscal risks have abated. The government, led by the Liberal party that assumed office after the December general election, has rolled back costly pension hikes that had previously been legislated. It has also charted a consolidation course that we consider will ensure that Romania's government and external debt stocks remain moderate through 2024," reads the rating agency's statement.

Standard & Poor's expects Romania's output to expand by 5% in 2021 and remain steady in 2022-2023, based on a recovery in private consumption and an uptick in investments, especially within the public sphere. The latter will be supported by the government's multiyear infrastructure plan, under which public spending is to increase by 15% in 2021. This will boost the investment-to-GDP ratio to a historical high of 5.5%, the agency notes.

The rating agency points out that the government's successfully executing its investment ambitions will depend on its ability to absorb the plentiful EU funds designated for Romania, and that in order to access the EU funds, Romania will need to design eligible projects and implement the accompanying reform agenda.

"Our economic forecast remains sensitive to the still-evolving situation regarding the pandemic, and to possible delays in vaccination roll-out. In particular, success in administering immunization programs, both domestically and abroad, will determine the extent to which Romania's economy can reopen," the S&P analysts note.

The rating agency expects Romania's government deficit to be 7% of GDP this year.

"We project that the government deficit will stand at 7% of GDP in 2021, with fiscal policy gradually adapting in a bid to assist the near-term economic recovery. We also forecast that the fiscal deficit will gradually reduce to 3% of GDP in 2024 supported by the government's medium-term consolidation ambitions and the recovering economy. We believe this will halt the erosion of Romania's government balance sheet and we see its net general government debt to GDP stabilizing at around 50% of GDP by 2023," S&P predicts.

According to the cited source, Romania's recently instated government has taken action to defuse near-term fiscal risks by rolling back previous costly pension legislation, which is seen as key to achieving budgetary stability. "Importantly, government has defused near-term fiscal risks by rolling back, through emergency ordinance, legislation passed by the previous administration that would have hiked pensions. We understand that the PNL-led government aims to present legislation that more clearly charts the fiscal framework regarding future wage and pension increases, by the end of this year," S&P writes.

The agency goes on to note that thus far, the government's consolidation efforts have primarily focused on the expenditure side of the budget, and the government is now expected to broaden its budgetary rebalancing efforts to include revenue-side measures. "In our view, such efforts are key to improving Romania's dismal revenue generation performance and closing the largest value-added tax gap in the EU," S&P states.

In the rating agency's view, risks from Romania's still-elevated twin deficits are mitigated by the prospect of sizable EU funds deployment, the government's stated reform ambitions, and a return to economic growth (as Romania is one of the key beneficiaries of the structural funds designated under the EU's upcoming Multiannual Framework, alongside the newly created EU Recovery and Resilience Fund). S&P forecasts that Romania's GDP growth will average 5% in 2021-2022.

The agency's affirming Romania's sovereign rating is also supported by the country's robust access to financing from international capital markets, the Finance Ministry stressed.

"Standard & Poor's decision is proof of the international recognition for Romania's efforts to ensure fiscal and budgetary consolidation and confirms that the measures adopted were the right ones our country needed and which our external partners were expecting. We also note the agency's positive estimates on Romania's medium-term economic growth potential," Finance Minister Alexandru Nazare remarked.

The Finance Ministry pledges to continue both the steps for the implementation of measures aimed at mitigating the negative effects of the Covid-19 pandemic and at economic recovery, as well as the prudent fiscal-budgetary policy capable of ensuring that Romania meets the committed targets. "This signal encourages us and shows us that we are on the right track, but this does not mean that we have already arrived there, efforts must be continued," the Finance Minister states.

The reforms planned by the current government would ensure the creation of a more robust fiscal framework, limiting the risks of reversal of the fiscal consolidation policies, which will lead to the improvement of Romania's sovereign rating, the Finance Ministry's release concludes.