Fiscal Council of Romania

We badly need to repair the public finances[*]

The Fiscal Council's 2025 Report opens with an introduction that takes as its starting point the exceptional nature of both the domestic and international circumstances. Last year marked the beginning of a major fiscal adjustment. In May 2026, the Bolojan government fell following a vote of no confidence, triggering a prolonged political crisis. The domestic political situation is complicating the fiscal consolidation process against an increasingly unfavourable international backdrop.

For several years, Romania had been living well beyond its means as a result of misguided fiscal/budget policies, and it was only a matter of time before it had to face a very harsh reality: the imminence of a large-scale fiscal adjustment. It is worth recalling that, even before the pandemic year of 2020, Romania was the only EU country subject to the Excessive Deficit Procedure. In 2020, the budget deficit exceeded 9% of GDP, admittedly also as a consequence of the partial shutdown of the economy. The Romanian economy has also been displaying an acute twin-deficit syndrome – a large budget deficit coupled with a large current account deficit, more than 55% of which is financed through borrowing. This situation pushed public debt above 60% of GDP in 2026, compared with 35% of GDP in 2019, with approximately half of the debt being external.

Fitch and Moody's have maintained Romania's sovereign credit rating recently, in view of the remarkable budget deficit correction achieved over the past two years. The budget deficit, which reached 9.3% of GDP in 2024, declined to 7.9% of GDP (ESA methodology) in 2025 and is projected to stand at around 6% of GDP in 2026. Budget execution over the first seven months of the year, showing a deficit of 2.34% of GDP – around 1.7 percentage points of GDP lower than in the corresponding period of 2025 – indicates that fiscal adjustment is continuing firmly. The reduction in the budget deficit was achieved through a freeze on public-sector wages and pensions (reducing their share in GDP) and increases in certain taxes, primarily VAT and excise duties. This combination of measures was unavoidable, as other means of rapid adjustment which were aired in public debate – drastic expenditure cuts or a massive and rapid increase in tax revenues – were not realistic. This is also what the Fiscal Council has argued in its analyses. Both rating agencies, however, pointed to political instability/fragility as a factor that could jeopardise Romania's sovereign rating, since their assessments also take into account the outlook for the budget consolidation process.

[*] This text is the *Introduction* to the Fiscal Council's 2025 Report.

The budget deficit adjustment entails an economic and social cost that cannot be avoided. In an increasingly unforgiving world, there are no free gifts, and even assistance comes at a price that can become overburdening. A budget deficit adjustment of more than 3 percentage points of GDP over 2025–2026 could not have taken place without someone bearing the effects of the measures; these effects concern both citizens' purchasing power and the business environment. It is worth noting that economic growth in 2024 was only 0.9%, despite public investment amounting to almost 7% of GDP (capital expenditure and European funds). In 2025, economic growth was only 0.7%, which is hardly surprising given the scale of the budget deficit adjustment.

In 2026, even if not all the funds available under the NRRP are absorbed (as is also the case with the unitary pay law), European funds will provide substantial support to the economy at a time when the impact of fiscal adjustment is severe; this year, Romania may experience a mild recession.

The break-up of the governing coalition in May this year threw the political landscape into turmoil and raised questions about the institutional capacity to continue the budget consolidation process and implement necessary reforms – including the reform of the unitary public-sector pay system.

Political instability can be seen in other EU countries too, but Romania alone faces such a severe combination of internal and external imbalances, a very low level of tax revenues (including social security contributions) and, not least, a relatively low credibility in economic policy. As Romania is not a member of the euro area, it is also exposed to exchange-rate risk. Romania's major advantage, however, is that it belongs to the EU and benefits from substantial European funds, as well as from support should it find itself in serious difficulty (as happened in the aftermath of the global financial crisis). But such support is subject to strict conditionality.

The unitary public-sector pay law has strained political dialogue and reached an impasse, hopefully only a temporary one. The loss of EUR 770 million represents a cost to the budget, but cannot, in itself, cause fiscal slippage. Romania urgently needs the reform of the unitary public-sector pay system, as it would correct inequities and ensure predictability in the evolution of public-sector wages, preventing the kind of sharp increases that put public finances at risk. It is regrettable that this legislation was not discussed in due time. In the months ahead, efforts should be made to reach a consensus on this reform, so that it can be incorporated into the 2027 draft budget, while taking into account the constraints arising from the need to continue budget deficit correction. The reform of the unitary public-sector pay system must not be abandoned; it would support Romania's sovereign rating and strengthen the credibility of economic policy.

For 2027, projected public expenditure on wages and pensions should not grow faster than nominal GDP, and any indexation should be prudent. In 2027, economic growth could be around 2%, while inflation could fall below 4% by the end of the year, provided that no further major shocks occur.

The rectification of the 2026 budget and the preparation of the 2027 budget require the formation of a fully empowered government as soon as possible. Both the domestic and international circumstances call for such a government.

In 2027, budget consolidation must continue, with the aim of bringing its deficit down to around 5.5% of GDP. This will not be easy, but it can happen, especially if tax revenue collection improves substantially. An inadequate tax regime, permissive legislation, and vested interests seeking to preserve privileges have fostered a culture of impunity, fraud against the public budget, and resistance to reforms. There has also been a systematic neglect of the need to raise tax revenues; in Romania, these revenues (including social security contributions) amounted to around 29% of GDP in 2025, compared with an EU average of over 40% of GDP.

The development of defence capabilities in Europe, including Romania, will place increasing pressure on public budgets. The devastating consequences of climate change must also be taken into account, as they erode national wealth and alter economic flows and resource allocation. Geopolitics and geoeconomics increasingly dominate international relations. The technological race driven by AI (artificial intelligence) is generating an enormous appetite for energy and resources, which will tighten financial conditions internationally; a global crowding-out effect is likely to emerge. There is also a trend towards deregulation of the financial industry which, together with the rapid development of AI, may amplify systemic risks. Domestic financial markets will also be affected by these developments, further complicating the budget consolidation process and the objective of bringing its deficit down to 3% of GDP by around 2030.

Romania must achieve a primary budget surplus that should enable public debt to stabilise. Without low and readily financeable deficits, there can be no serious discussion of joining the euro area.

The increasingly adverse international environment, the war between Russia and Ukraine, the war in the Middle East, hybrid attacks (including those targeting Romania), trade conflicts, and the erosion of rules governing relations among states call for greater responsibility at home and require public governance to operate in a state of permanent crisis management.

We must tap the efficiency reserves that exist in the public sector, make the best possible use of European funds (the NRRP comes to an end this year), take full advantage of the SAFE programme, effectively combat tax evasion and aggressive tax optimisation, as well as corruption, and carry out necessary reforms in the public sector. We must also make intelligent use of our energy resources and raw materials. If we will advance in these areas, we will facilitate a further reduction in the budget deficit (and the current account deficit), the stabilisation of public debt, a more competitive economy, and a greater capacity to absorb adverse shocks.

Repairing the public budget is like a battle for heavy water!

Professor Daniel DĂIANU, Fellow of the Romanian Academy