INTERNATIONAL MONETARY FUND

IMF Country Report No. 13/307

ROMANIA

REQUEST FOR A STAND-BY ARRANGEMENT

October 2013

In the context of the request for a Stand-By Arrangement, the following documents have been released and are included in this package:

- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on September 27, 2013, following discussions that ended on July 31, 2013, with the officials of Romania on economic developments and policies underpinning the IMF Stand-By Arrangement. Based on information available at the time of these discussions, the staff report was completed on September 12, 2013.
- A **Staff Supplement** of September 12, 2013 on the assessment of risks to the Fund and the Fund's liquidity position.
- A **Staff Supplement** of September 24, 2013 updating information on recent developments.
- A **Press Release** including a statement by the Chair of the Executive Board.
- A **Statement by the Executive Director** for Romania.

The documents listed below have been or will be separately released.

Letter of Intent sent to the IMF by the authorities of Romania*
Memorandum of Economic and Financial Policies by the authorities of Romania*
Technical Memorandum of Understanding*

*Also included in Staff Report

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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ROMANIA

REQUEST FOR A STAND-BY ARRANGEMENT

September 12, 2013

KEY ISSUES

Stand-by Arrangement: Romania successfully completed in June 2013 a 27-month Stand-By Arrangement (SBA), including a three-month extension, equivalent to SDR 3,090.6 million (€3.4 billion, 300 percent of quota). The authorities have requested a successor 24-month SBA with proposed access of SDR 1,751.34 million (about €2 billion, 170 percent of quota). The first tranche of SDR 194.7 million would be made available upon program approval. The authorities intend to treat the SBA as precautionary and have also requested support from the European Union (€2 billion), while €1 billion remains available under a World Bank policy loan.

Program objectives: Since the 2008 global financial crisis, Romania has made significant progress in reducing macroeconomic imbalances and rebuilding fiscal and financial buffers. However, Romania remains vulnerable to external shocks, in particular uncertainties in the euro area as well as global volatility in capital flows to emerging markets. The new SBA would provide a valuable policy anchor and support Romania's comprehensive economic program for 2013–15 to maintain sound macroeconomic policies and financial sector stability and continue structural reforms to enhance growth prospects.

Program conditionality: Romania's cumulative access, net of scheduled repurchases, would be exceptional given its outstanding credit to the GRA arising from purchases under the 2009–11 SBA. The program calls for continued gradual fiscal adjustment and allows for short-term measures in support of domestic demand. Structural reforms build on the previous program with a focus on arrears reduction. Conditionality is front-loaded via a number of macro-critical structural benchmarks. An Ex Post Evaluation is envisaged for around end-2013 and an update of the Safeguards Assessment by the time of the first review.

Staff views: Staff supports the authorities' request for a new SBA. A precautionary Fund-supported program would foster policy discipline and provide a reserve buffer, while helping to catalyze support for difficult structural reforms and put Romania on a firm path toward exiting from Fund support.

Approved By
Poul M. Thomsen and Vivek Arora

Discussions were held in Bucharest during July 17–31, 2013. The mission met with Prime Minister Ponta, President Basescu, Deputy Prime Minister and Minister of Public Finance Chitoiu, other members of the government, National Bank of Romania Governor Isarescu and his staff, other senior officials, and representatives of political parties, labor and business organizations, and financial institutions. The staff team comprised A. Schaechter (head), J. Ralyea, C. Saborowski, A. Tuladhar, J. McCoy (research assistant; all EUR); J. Bersch (SPR); F. Eich (FAD); and H. Hesse (MCM). G. Tolosa and G. Babici (Resident Representative office) assisted the mission. Discussions were held jointly with staff from the European Commission. S. Matei (Senior Advisor to the Executive Director) and World Bank staff attended some of the meetings; European Central Bank staff participated as an observer.

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INTRODUCTION

1. **Following the severe downturn during the 2008–09 crisis, Romania has made significant progress in restoring macroeconomic stability.** Large external and fiscal imbalances have been reduced to more sustainable levels under two consecutive IMF Stand-By Arrangements (SBAs) (Text Figure 1 and Box 1), supported by the European Union and the World Bank. Since 2010, Romania has maintained continued market access and has begun to rebuild fiscal, capital, and reserve buffers even as it has started to make large repayments to the Fund.

2. **The economic recovery is fragile and vulnerability to external shocks remains high.** Romania's growth outlook for 2013 is better than that for many regional peers, but its real GDP has yet to return to pre-crisis levels. At the same time, financial and external vulnerabilities persist given high external debt rollover needs. The banking system remains heavily dependent on parent funding, exposing it to spillover risks from the euro area, and is vulnerable to currency depreciation given substantial foreign currency lending. New sources of external risk have emerged as capital flows to emerging economies have recently become more volatile.

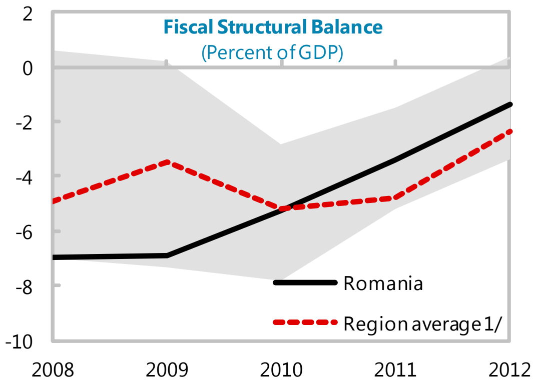
3. **Against this backdrop, the authorities have requested a new precautionary SBA.** The key objectives of a new program are to provide a buffer against possible external shocks, while assisting Romania in preserving the hard-won macroeconomic stability and catalyzing difficult structural reforms that were initiated under the previous program. In particular, the program seeks to: (i) safeguard sound public finances underpinned by a stronger institutional fiscal framework; (ii) continue monetary and financial sector policies that restore buffers shielding the economy against external shocks; and (iii) reduce bottlenecks to the country's growth potential and competitiveness through structural reforms. The program aims to preserve investor confidence by ensuring policy discipline and stability.

4. **The program also allows for targeted measures in support of domestic demand.** As households, banks and corporations continue to deleverage, domestic consumption and investment demand remain weak. The program combines long-term institutional responses with targeted short-term measures such as the extension of the mortgage guarantee scheme with the view to put the economic recovery on a firmer footing.

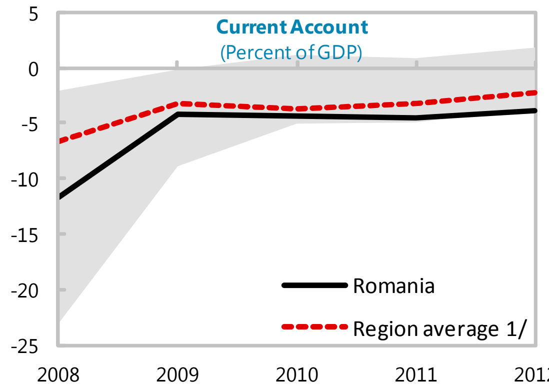
5. **The program has strong political backing.** After a tumultuous period that saw three changes in government last year, the political environment has improved. The governing coalition led by the Socialist Democratic Party (PSD) with the support of the National Liberal Party (PNL) and the Conservative Party (PC) has a comfortable majority. Both Prime Minister Ponta and President Basescu have underlined their support for a follow-up arrangement and political tensions generally eased after the parliamentary election in December 2012.

Text Figure 1. Romania, 2006–2012

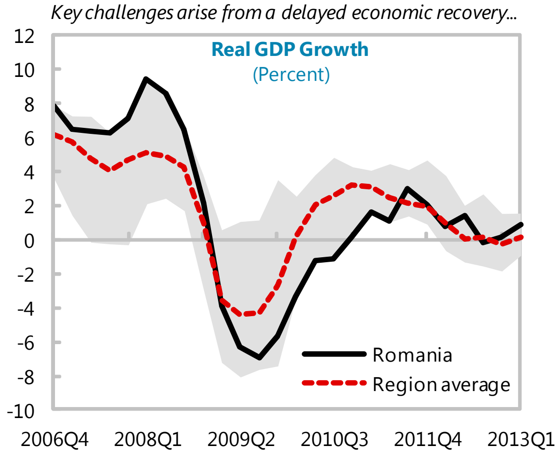
Romania has implemented a relatively large fiscal adjustment...



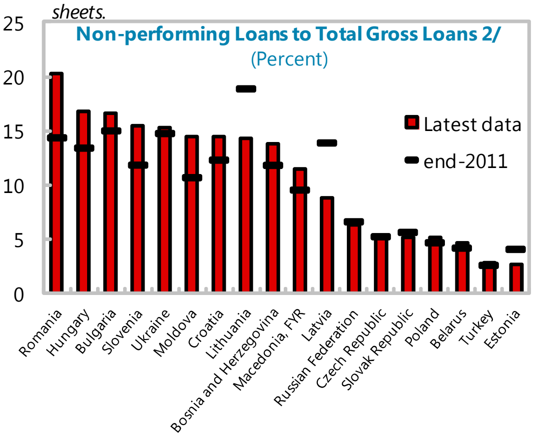
...while the current acount deficit has also reversed significantly.



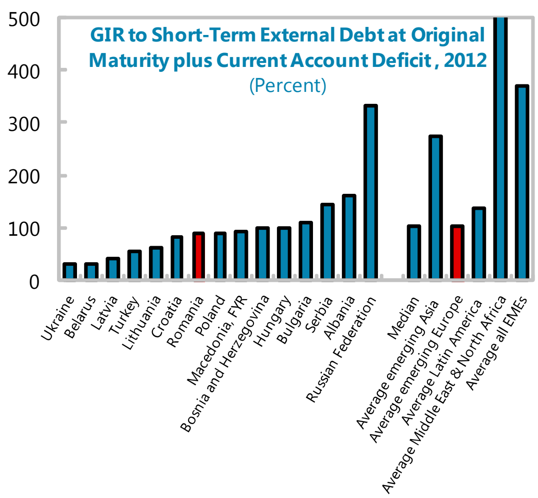
Key challenges arise from a delayed economic recovery...



...and rising NPLs, which are weighing on bank balance sheets.



Vulnerability to short-term external financing shocks remains.



Structural and governance reforms will be critical in order to attract investment and improve Romania's growth potential.

Sources: Transparency International; World Bank; World Economic Forum; IMF Financial Soundness Indicators datase; and WEO.

1/ Region average weighted by GDP includes Bulgaria, Czech Republic, Hungary, and Poland. Shaded regions show range between the minimum and maximum values in the region.

2/ NPL definitions differ across countries. Data are from the IMF Financial Soundness Indicators database.

3/ Out of 183 countries, except for competitiveness where 139 countries were ranked.

6. **Nonetheless, implementation of structural reforms continues to face pockets of resistance.** The period up to the EU parliamentary elections (summer 2014) and the next Presidential election (end-2014) provides a window of opportunity for reforms. However, political risks remain. In particular, vested interests could lead to attempts to delay some overdue structural reforms, in particular those linked to SOEs. These reforms, which include the energy and transportation sectors and are supported by other multilateral donors (WB, EBRD, EC), are macro-critical given that they could spur economy-wide investment and growth and facilitate the development of underutilized energy resources. Failure to implement the reforms could exacerbate existing bottlenecks and lead to a permanently lower growth trajectory. The authorities plan to push the reform agenda forward with greater involvement in program implementation from the highest levels of government and adopting successful measures from the prior programs. For example, to address financial and operating difficulties in SOEs the authorities have indicated a willingness to consider more readily the use of insolvency procedures.

RECENT ECONOMIC DEVELOPMENTS

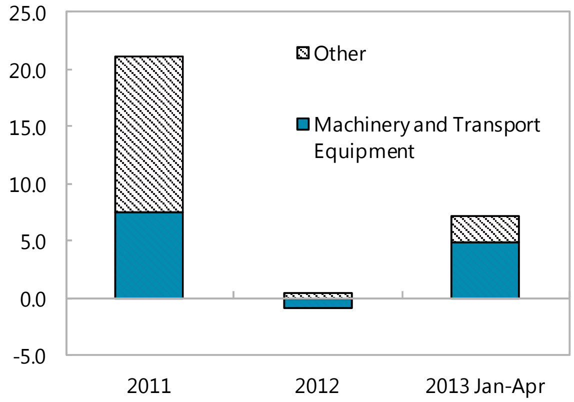
7. **GDP growth has picked up after the recovery slowed in 2012** (Figure 1). Real GDP grew 0.6 percent qoq in 2013:Q1 (2.2 percent yoy) as weak domestic demand was more than offset by increased exports of machinery and transportation equipment and greater demand for Romanian goods from non-European countries. At the same time, a fall in investment and a relatively mild winter contributed to a decline in imports, in particular of energy. This follows a slowdown in real GDP growth in 2012 to 0.7 percent from 2.2 percent in 2011. The unemployment rate, which averaged 7 percent in 2012, is lower than others in the region but has yet to come down significantly from its elevated post-crisis level. Total employees are still only 91 percent of levels achieved in the summer of 2008 (Figure 3).

8. **Inflation has begun to ease** (Figure 4). Headline inflation peaked at 6 percent in January 2013, pulled upward by increases in food prices and administered price hikes, particularly for electricity and tobacco products, and reversing base effects. Since then, annual inflation has come down to 4.4 percent in July as the effects of the shocks partly dissipate. Annual core inflation has fallen from 3.3 percent at end-2012, to 2.5 percent by end-July 2013.[1]

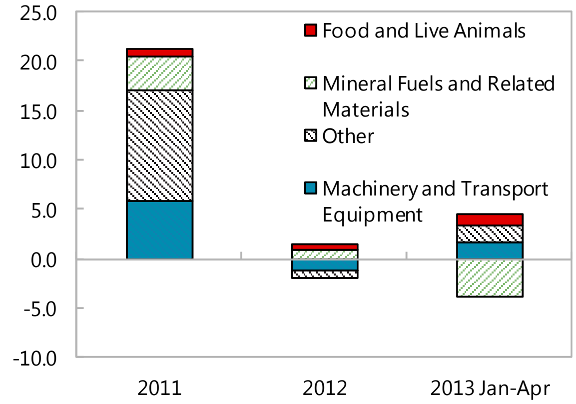
9. **The current account recorded a small surplus in the first half of 2013, while reliance on portfolio financing has increased**. A smaller trade deficit and a continuing surplus in the services balance were the main drivers of the turnaround in the current account from a deficit of 3.9 percent of GDP in 2012 to a small surplus. Though public sector capital inflows from international bond placements and non-residents' investments in local government securities were strong, FDI remained weak and the private sector faced net capital outflows (Figure 2).

[1] Food items comprise over 40 percent of the core index.

Contributions to Export Growth
(Percent)



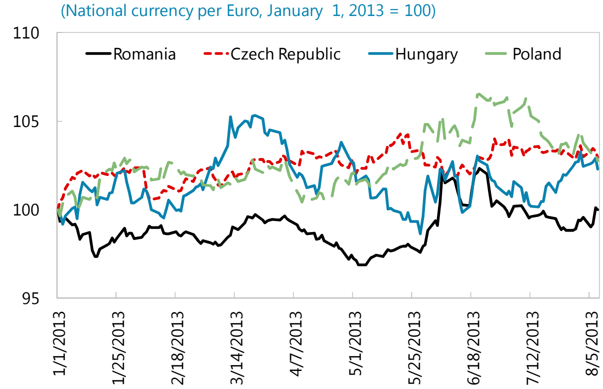
Contributions to Import Growth
(Percent)



Source: Haver.

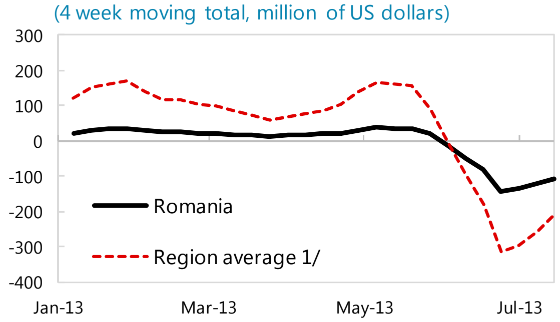
10. **Overall market conditions are favorable, though volatile.** Positive market sentiment following the December general election and inclusion of Romania in emerging market bond indices boosted the exchange rate earlier this year. More recently though, against the backdrop of expectations of global monetary tightening, portfolio inflows have waned, though less than in other emerging economies, and the leu has retraced most of its gains early in the year (Figures 4 and 7). At the same time, the CDS and EMBIG spreads for sovereign debt remain well below levels of a year ago. Favorable market conditions have enabled the central bank to sustain international reserves at €35.7 billion as of end-August, while making substantial repayments to the Fund.

Exchange Rate
(National currency per Euro, January 1, 2013 = 100)



Sources: Bloomberg

Bond Flows: ETFs/Mutual Funds
(4 week moving total, million of US dollars)



Source: Haver Analytics.
1/ Region average weighted by GDP; includes Bulgaria, Czech Republic, Hungary, and Poland.

Romania: CDS Spreads
(Percentage points)

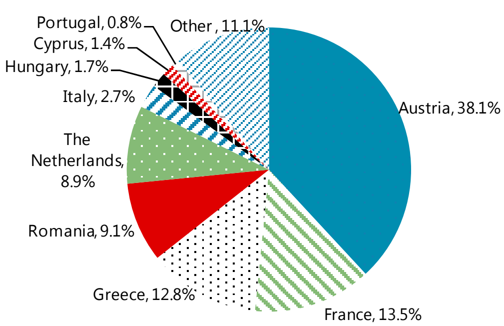
Source: Bloomberg.

11. **The Romanian banking sector maintains reassuring capital buffers and provisions but faces increased pressures on asset quality** (Figure 6). Non-performing loans (NPLs) rose decisively

to 20.3 percent of total loans at end-June 2013 (compared to 14.3 percent at end-2011)—one of the highest ratios in the region—primarily reflecting the weak economic environment, previously weak credit standards, and difficulties in removing NPLs from bank balance sheets. However, provisions (with a prudential filter) were sufficient to cover a comfortable 88.3 percent of NPLs while the International Financial Reporting Standards (IFRS) provisioning ratio stood at 62.8 percent at end-June.[2] Prospects for bank profitability remain challenging, notwithstanding the small profit recorded in the first half of 2013. The capitalization of the banking sector remained strong at 14.7 percent at end-June 2013 albeit with some differences between banks.[3]

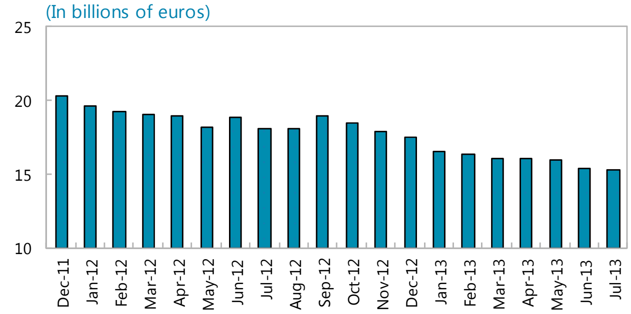
12. **Vulnerabilities to external shocks persist amid an accelerated pace of foreign bank deleveraging**. Spillovers from the Cyprus crisis have been contained, and the resolution of one Cypriot bank subsidiary is still pending. With system-wide deposit growth of 9 percent since end-2011, overall liquidity conditions have improved but remain uneven across banks. The pace of foreign-owned bank deleveraging has accelerated in line with regional developments and has remained orderly so far with a parent funding decline of 26 percent since end-2011. Likely drivers of this retrenchment include parent bank weakness and changes in funding strategies at the group level toward greater reliance on domestic deposits for subsidiaries. Other factors such as tightened lending standards, weak economic activity, and fragile private balance sheets, have also acted as a drag on private credit growth, which turned negative in 2013 (Box 2). Risks from parent funding retrenchment remain elevated and could put further pressure on credit growth going forward. Finally, the latest NBR banking sector stress test illustrates that in a severe adverse scenario involving a substantial depreciation and recession in 2014–2015, the banking system would be overall resilient but a number of banks would need to raise additional capital.

Bank Ownership Structure (percent of total gross assets)



Sources: National Bank of Romania

Romania: Parent Bank Funding
(In billions of euros)



Sources: National Bank of Romania and IMF staff calculations.

[2] Including all provisions and not only those for NPL's 90 days past due, the total provisioning ratio was 102.4 percent and the IFRS provisioning ratio stood at 77.2 percent at end-June.

[3] One small bank has a solvency ratio less than the minimum 10 percent but above 8 percent. The bank is under intensive supervision.

OUTLOOK AND RISKS

13. **The baseline scenario envisages a gradual recovery in 2013 and 2014.**

- ***Growth*** is expected to accelerate in 2013 to 2 percent driven by a return to a more normal agriculture harvest following last year's drought and increased exports, particularly to non-EU countries. The flash estimate of 0.3 percent for real GDP growth in 2013:Q2 (1.3 percent yoy) is in line with this projection. The recovery is expected to continue in 2014, with real GDP advancing by 2.2 percent, with domestic demand growth supported by greater absorption of EU funds and positive nominal private sector credit growth, while an anticipated improvement in the external environment supports continued export growth. The output gap is projected to close over the medium term, as employment and investment recover.

Romania: Macroeconomic Outlook, Baseline

(Percent)

	2010	2011	2012	2013	2014	2015
Real GDP growth	-1.1	2.2	0.7	2.0	2.2	2.5
CPI inflation, average	6.1	5.8	3.3	4.5	2.8	2.9
CPI inflation, eop	8.0	3.1	5.0	3.3	3.0	2.9
Current account balance (percent of GDP)	-4.4	-4.5	-3.9	-2.0	-2.5	-2.7
Fiscal balance (percent of GDP, cash)	-6.4	-4.3	-2.6	-2.3	-2.0	-1.8
Gross international reserves (bn euros)	36.0	37.3	35.4	34.1	31.6	30.5

Source: Romanian authorities; and IMF staff projections.

- ***Inflation*** is expected to decline further during the second half of 2013 to 3.3 percent by year-end, within the NBR's target band of 2.5±1 percent. This is mainly on account of the reversal of base effects as well as expectations that a more normal harvest than last year will hold down food prices. Headline inflation is projected to continue easing in 2014 and 2015, as lower inflation expectations become more entrenched.
- ***External position***. The current account deficit is projected to narrow to 2 percent of GDP in 2013 as domestic demand remains weak and imports grow more slowly than exports. In 2014–15 the current account deficit is expected to widen slightly to 2½–2¾ percent of GDP as domestic demand starts to recover. Capital inflows are expected to hold up, with FDI picking up from recent lows and continued portfolio inflows. With sizable repayments to the Fund, gross international reserves are projected to decline to €30.5 billion (five months of imports) by end-2015. Under the baseline scenario, no financing gaps are envisaged.

14. **Risks are tilted toward the downside.** A more protracted recession or renewed financial tensions in the euro area could hamper exports, spark a further retrenchment of foreign investment and accelerate bank deleveraging. A deeper than expected slowdown in emerging markets would also negatively impact exports and growth. Moreover, monetary policy tightening in advanced economies could trigger capital account outflows as investors further reassess portfolio risks and

returns. Any of these developments would put pressure on the exchange rate, which would feed back to bank and private sector balance sheets, given the large volume of foreign-currency lending. In addition, renewed political uncertainty in the run-up to elections in 2014, in particular the presidential elections, could weigh on investor and consumer sentiment. However, the possibility that the recent diversification of export markets could become more permanent or the autumn harvest might replicate the strong performance of the summer harvest provide upside potential for growth.

Romania: Macroeconomic Outlook, Adverse Scenario

(Percent)

	2010	2011	2012	2013	2014	2015
Real GDP growth	-1.1	2.2	0.7	1.5	0.3	2.3
CPI inflation, average	6.1	5.8	3.3	4.5	2.8	2.9
CPI inflation, eop	8.0	3.1	5.0	3.3	3.0	2.9
Current account balance (% of GDP)	-4.4	-4.5	-3.9	-2.3	-3.6	-3.8
Fiscal balance (% of GDP, cash)	-6.4	-4.3	-3.0	-2.4	-2.4	-2.2
Gross international reserves (bn euros)	36.0	37.3	35.4	34.4	30.7	28.2

Source: Romanian authorities; and IMF staff projections.

15. **Under the adverse scenario, the euro zone slips back into deeper recession undermining investor confidence in the region.** Over the period 2013–15 Romania's exports to the euro zone, its main trading partner, foreign direct investment and rollover rates on external liabilities of Romania's banks and private sector would be lower than in the baseline scenario (Tables 5 and 6). This would also weaken domestic demand and widen the current account deficit in 2013–15, reducing economic growth by a cumulative 2½ percentage points. Lower net inflows would require additional external financing of €5 billion, which would be covered by disbursements from the Fund, the EU and the World Bank, and a limited drawdown of international reserves. Under this scenario, additional fiscal measures for 2013 will likely be needed to meet program targets. For 2014, automatic stabilizers could be allowed to play, provided financing remains available and the ESA deficit ceiling of 3 percent of GDP is respected. In addition, with the policy rate at a historic low, there is room to tighten liquidity conditions in an effort to limit capital outflows.

PROGRAM POLICIES

16. **The proposed new Fund-supported program would provide a policy anchor and reserve buffer, while catalyzing broader support for macro-critical structural reforms.** The authorities consider that a follow-up precautionary arrangement would help Romania to lock in the recent gains on macroeconomic and financial sector stability, complete fiscal policy adjustment underpinned by stronger institutions, and garner support for politically difficult structural reforms. The program would also guard against adverse economic shocks in the euro area and volatile global

capital flows to emerging economies, while preserving market access and limiting risk premiums. Progressing with structural reforms, particularly in the energy and transportation sector, will be crucial to remove bottlenecks in the economy and reduce fiscal pressures that could otherwise crowd out much needed spending for other priority areas. To achieve these goals, the program would seek to (Box 3):

- Continue the fiscal adjustment process while strengthening the fiscal institutional framework to preserve sound public finances.
- Maintain prudent monetary policy in line with the NBR's inflation target and strengthen reserve buffers; reinforce financial sector policies to protect against shocks and strengthen bank balance sheets to support the economic recovery.
- Build on the structural reform measures initiated under the previous program and follow through on their implementation in the areas of energy, transportation and SOE reforms to boost investment, competitiveness and potential growth.

17. **Key structural policy areas would include the following:** (i) durable reduction of arrears; (ii) energy price deregulation; (iii) SOE reform; (iv) improved public financial management including medium term budgetary planning; and (v) reduction of NPLs.

A. Fiscal Policy: Strengthening the Institutional Framework

18. **Securing the fiscal position and strengthening the fiscal institutional framework are program priorities.** The authorities aim to gradually reach their medium-term budgetary objective (MTO) of a structural deficit of 1 percent of GDP (in ESA terms) in 2015. This implies fiscal adjustment of around ½ percent annually in 2013–14. Key measures include a windfall levy on energy deregulation, agriculture tax, and rationalization of capital expenditures. To help underpin the required adjustment effort and contain fiscal risks, the authorities aim to strengthen fiscal institutions, better control of spending at all levels of the public sector to avoid future arrears, reform the health care system to make it more efficient and sustainable, and improve management of public debt and contingent liabilities (in particular, regarding state guarantees).

19. **Within the fiscal stance, fiscal policy aims to support weak domestic demand.** The program seeks to strengthen the capacity to prioritize investment projects generally and EU co-financed projects in particular. Given lags in reimbursement, the government will provide bridge financing through net lending of EU projects from the treasury (within a ceiling) and the program allows for adjustment of the deficit target, up to a cap, should co-financing exceed the amount budgeted. To address the rising tax arrears of small and medium-size enterprises (SMEs), the tax administrator will consider granting payment terms in installments. Moreover, the program raises the ceiling of government guarantees, in line with sustainability considerations. To do so it accommodates the continuation of the mortgage guarantee lending program, though with revised modalities (¶36), and fully implements the underused SME lending guarantee fund.

20. **In 2013, the fiscal deficit cash target of 2.3 percent of GDP will be preserved.** This is consistent with an ESA deficit target of 2.4 percent of GDP and includes capital expenditure under PNDI amounting to 0.2 percent of GDP.[4] Following a 1.1 percent of GDP cash deficit in the first half of the year, which was in line with projections, the mid-term budget rectification includes measures to achieve the annual target. Revenues underperformed so far, reflecting bank losses and a less-tax rich economic recovery (i.e., declining imports and rising VAT export refunds). These were compensated by lower than expected social transfers and spending on EU corrections (see text table). Fiscal buffers increased beyond the targeted 4 months of gross financing needs. Going forward, the revised budget allocates additional spending to mitigate the impact of gas and energy price liberalization through raising the Guaranteed Minimum Income (GMI) and family allowances as well as increasing the eligibility thresholds, consistent with the authorities' social assistance reform program to consolidate benefits and improve means testing. At the same time, the authorities lowered the VAT on bread and the production chain temporarily to 9 percent from 24 percent, effective September 1. Offsetting measures and savings include higher excises on alcohol, and luxury cars and goods, lower allocations for EU funds corrections and cuts in domestically-financed capital spending.

Romania: Fiscal Performance, January to June 2013
(In billions of lei)

	Proj.	Actual	Diff
Total revenue	102.9	97.5	-5.3
Current revenue	98.0	94.5	-3.5
Tax revenue	88.2	85.3	-2.9
Nontax revenue	9.9	9.2	-0.7
Capital revenue	0.3	0.3	0.0
Grants	4.5	3.1	-1.4
Total expenditure	109.2	104.2	-5.0
Current	101.7	97.3	-4.3
EU Funds, post-accession	8.3	5.2	-3.1
Capital	7.4	7.2	-0.2
Reserve fund	0.1	0.0	-0.1
Net lending	0.0	-0.3	-0.3
Deficit/Surplus (authorities' definition)	-6.3	-6.6	-0.4
Deficit/Surplus including PNDI	-6.9	-6.6	0.2

Source: Romanian authorities; and IMF staff estimates.

21. **In 2014, the government targets a deficit of 2.0 percent of GDP (in cash and ESA terms).** The authorities have taken a first step in widening the tax base for healthcare contributions effective in 2014, by including rental income (prior action). Additional measures will be needed though, for example to offset the impact of court decisions on restoring public wages for certain groups and compensatory benefits to protect the poorest households from energy price liberalization. In addition to a tight spending envelope, the authorities are contemplating revenue measures, including on property taxes and social security contributions.

22. **In order to lock in the benefits of recent adjustment efforts, the authorities are moving ahead with structural fiscal reforms.** The measures include:

- **Fiscal Compact:** In compliance with the EU fiscal governance requirements, the authorities will revise the Fiscal Responsibility Law to integrate structural fiscal targets and corrective actions in case of deviations.

[4] Until mid-2013, the authorities reported spending for PNDI (National Program for Infrastructure Development) outside their deficit but it was included in the fiscal target under the previous SBA. All unexecuted contracts for PNDI projects have since been cancelled and spending reallocated on budget.

- **Public financial management** (MEFP ¶8): The authorities are committed to (i) contain arrears; (ii) improve the fiscal reporting system; and (iii) better manage fiscal risks. To meet the first objective, the authorities will implement a commitment control system, covering the central and local governments. As a first step the authorities defined commitments (prior action). Until the system is fully implemented by mid-2014, the authorities are taking additional measures. These include quarterly publication of detailed reports of arrears and corrective measures; an audit by the Court of Accounts on the disputed invoices presented by local governments; and enhanced supervision of those local governments that received transfers to cover arrears. Once the commitment control system is in place, arrears targets should be reduced further and eventually eliminated. Regarding the consolidated fiscal reporting system, the authorities are finalizing its design, with Fund support. A transition to GFSM 2001 for the 2014 budget is also planned. Finally, the authorities will prepare an annual report on fiscal risks and request an IMF fiscal transparency assessment and plan to strengthen debt management, including through a project supported by the European Union and the World Bank.

- **EU funds absorption and public investment planning:** A key priority of the government is to improve budgetary planning and project prioritization to increase absorption of EU funds. Measures over the next six months, supported by the World Bank, include (i) staffing the Public Investment Evaluation and Monitoring Unit at the MoPF; (ii) preparing a list of investment projects based on predefined prioritization criteria; and (iii) updating the investment database along with the three-year budgetary allocation (MEFP ¶9). From 2014, no new public investment project will be approved without first vetting eligibility for EU funds financing. Budgetary planning and monitoring will be further improved to accommodate higher co-financing and needed financial corrections. The World Bank will also assist in capacity building for evaluating fiscal commitments in PPP projects.

- **Public administration and Unified Wage Law:** With public sector employment now considerably lower than in the past, the authorities have recently substituted the 1 for 7 replacement rule with a 1 for 1 rule while eliminating the vacancies. Public employment is being shifted away from central to local governments with a net reduction of 2,000 positions in 2013. To ensure a more efficient and equitable public sector, the authorities will develop staffing plans, with the assistance of the World Bank, for each line ministry in line with their functional reviews and strategies (MEFP ¶10). They will also seek to implement the Unified Public Wage Law—introducing a wage grid— from 2014 within the available budgetary envelope.

- **Tax administration:** A comprehensive reform of the tax administration (ANAF) remains an important policy goal so as to raise revenue collection and efficiency (MEFP¶11). ANAF is shifting resources towards its anti-fraud unit and is progressing, with Fund support, in making its High Net-Wealth Individual taxpayer unit operational. ANAF also seeks to improve taxpayer services, through a "one-stop" shop and by providing unambiguous tax law interpretation to taxpayers, step up efforts to streamline the VAT reimbursement procedures and ensure that SMEs in distress are granted payment terms in installments to clear tax arrears.

- **Tax policy** will be geared toward further improving tax buoyancy and efficiency (MEFP ¶12). For the 2014 budget, the property tax base will be revised. Preparations for a new oil and gas taxation, and royalty regime have started with the new regime becoming effective no later than 2015. The authorities are assessing how the high labor tax wedge can be reduced while widening the base of the social contribution system. The authorities will also analyze the efficiency of measures taken to tackle tax evasion, including the recent temporary reduction in the VAT rate for bread.

23. **For the healthcare system, the authorities seek comprehensive reforms to make it financially sustainable, raise its efficiency, and improve health outcomes.** Romania's public healthcare system relies heavily on transfers from the central government budget and faces significant financial imbalances and increasing spending pressures from an ageing population. To make the system sustainable, the authorities are considering mandatory taxes on different sources of income to supplement existing health contributions, consistent with a basic health package, and a voluntary contribution for supplementary health insurance. The basic health package will be defined within the existing envelope this fall. The government has prepared and published its action plan. The authorities plan to revise the list of services that can be contracted with primary care providers, as part of the 2014 health care framework agreement, to increase the share of spending on primary and ambulatory services. The authorities also continue to monitor public hospital budgets to ensure that they are consistent with the expenditure programmed in the general government budget, and will collect and analyze the cost of service provision across hospitals with the aim of developing benchmarks in the future. A number of other measures to improve the system efficiency are being taken (MEFP ¶15). Design of the healthcare reforms is being done in consultation with the World Bank and European Commission.

B. Structural Reforms: Increasing Investment and Growth

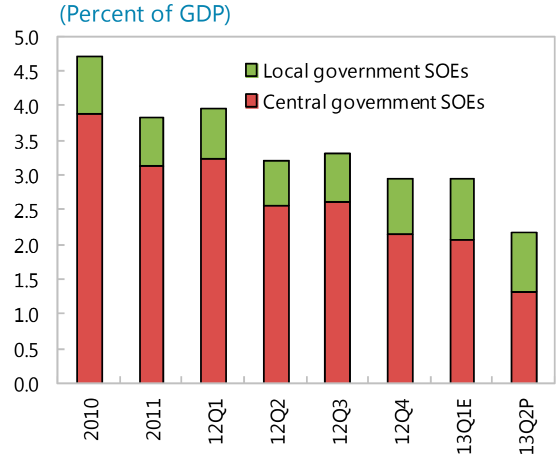
Energy and Transportation Sector

24. **Enhancing growth prospects by fostering investment and improving service delivery in the energy and transportation sectors is a key program objective.** Reforms in these sectors are macro-critical given that energy and transportation pricing is not fully market determined, and the sectors are dominated by inefficient SOEs that incur significant losses, face conflicting objectives, and accumulate arrears. SOEs control more than half of the energy sector and one third of the transportation sector. In addition, the World Bank estimates that the energy sector[5] alone will require €30–35 billion in investment over the next decade. Moreover, the authorities have committed to undertake a number of measures to improve the business environment and facilitate access to finance for small and medium-size enterprises (SMEs) during the program period.

[5] Eight SOEs generated over 90 percent of Romania's electricity and one produces almost half the domestic gas.

25. **Under the program, the authorities will pursue a three-pronged approach.** It is composed of strengthened measures to reduce arrears of central-government owned enterprises, further efforts to enhance SOE governance and transparency, and reforms to improve pricing and efficiency in the energy and transportation sectors. The approach builds on reforms initiated under the previous program but puts even greater emphasis on overall arrears reduction, focuses explicitly on achieving efficiency gains in the three SOEs (and their subsidiaries) with the highest operating losses, and concentrates on achieving greater private sector involvement in a small group of energy companies. Progress will be monitored with program conditionality in all three areas. Implementation of the approach will allow Romania to better leverage its favorable geographical position and spur growth.

SOE Arrears
(Percent of GDP)



Sources: Romanian authorities; and IMF staff estimates.

26. **The first leg of the approach will focus on the reduction of SOE arrears, which remain considerable despite recent efforts to reduce them.** Total SOE arrears (including central and local government SOEs) were reduced from 4.7 percent of GDP in 2010 to an estimated 2.2 percent of GDP at end-June 2013. The authorities have committed under the new program to further lower the arrears of the SOEs owned by the central government to a de minimis level.[6] Progress will be monitored through a quarterly indicative target (MEFP ¶38).[7] Measures to reduce arrears include placing enterprises into insolvency or liquidation procedures, SOE restructuring, and financial schemes such as debt-for-equity swaps of arrears between and among SOEs and the central government.

27. **The second pillar of the approach is composed of measures to enhance SOE service delivery through greater transparency, and improved governance and oversight.** The authorities reaffirmed their commitment that all new bilateral contracts of electricity producers will be made transparently and non-discriminatorily on the competitive market, consistent with conditions in the World Bank's Development Policy Loan. The authorities also plan to publish annual reports on SOE performance in accordance with the detailed stipulations specified in the government ordinance on SOE corporate governance (ordinance 109/2011) (MEFP ¶40). Moreover, the government plans to appoint, in accordance with ordinance 109/2011, a professional supervisory board for the state-owned hydro-electricity generator (Hidroelectrica) by end-

[6] Given the strict definition for SOE arrears under the program of any outstanding payment that is past the due date, i.e., there is no grace period, a stock of less than 0.2 percent of GDP will be considered a de minimis level.

[7] As of June 30, 2013, there were 233 central-government owned enterprises, excluding the 15 SOEs under insolvency or liquidation procedures.

November 2013. In the meantime, the government committed to empower the current interim board appointed upon Hidroelectrica's exit from insolvency to take decisions.

28. **More broadly, the authorities plan to strengthen the legal foundation and implementation of the existing SOE corporate governance framework.** They will seek passage of the draft SOE corporate governance law in parliament by end-September. In addition, given observed weaknesses about the process for appointing professional boards and management in SOEs over the last year, the authorities will undertake and publish an assessment of how the provisions of ordinance 109/2011 have been implemented. The results of the assessment will also inform the development of government-wide guidelines for implementation of the SOE corporate governance law, which will also draw on guidelines prepared, with World Bank assistance, by the Ministry of Transportation and Infrastructure (MEFP ¶39). Complementing these measures, the authorities plan, with support from the World Bank, to improve the monitoring function of the directorate in the Ministry of Public Finance that oversees central- and local-government owned enterprises.

29. **The third part would be to continue to improve the pricing framework and efficiency of the energy and transportation sectors.** The energy regulator (ANRE) implemented the July 2013 steps of the energy price liberalization roadmaps as planned and committed to implement the remainder of electricity and gas price road maps and to apply the pass-through mechanism for electricity and gas purchases by the supply companies (see text table). However, ANRE officials signaled that they would consider postponing implementation of the gas price roadmap as provided for in the energy legislation if market conditions deteriorated. The authorities also continue to work with the World Bank on measures to protect vulnerable consumers (see ¶18).

30. **The authorities also plan to launch initial public offerings (IPO) in five key state-owned energy companies (Box 4 and MEFP ¶41)**. In preparation for the IPO in Romgaz, the authorities committed to clarify the tax treatment in Romania for securities issued in a foreign jurisdiction (prior action). They also will restart the process for the IPO in Hidroelectrica by submitting requests to the Court of Appeal to formally withdraw the government's and Hidroelectrica's appeals of a court ruling against the initial decision to hold the IPO. They will authorize, through a General Shareholder's Meeting of Hidroelectrica, the current interim board to take decisions while it seeks to appoint a professional board in accordance with the SOE Corporate Governance ordinance (prior action). This will allow the government to issue a new decision on the IPO that observes all the legal requirements.

Romania: Energy Price Liberalization Roadmaps (abriged)

	Electricity 1/			Gas 2/		
	Non-household	Household	Status	Non-household	Household	Status
	(percent sourced from competitive market)			(estimated percent increase in regulated price)		
1/1/2013	30	…	Implemented	…	…	
4/1/2013	45	…	Implemented	5	…	Implemented
7/1/2013	65	10	Implemented	5	8	Implemented
9/1/2013	85	…		…	…	
10/1/2013	…	…		3	2	
1/1/2014	100	20		4	2	
4/1/2014	…	…		5	2	
7/1/2014	…	30		5	3	
1/10/2014	…	…		4	3	

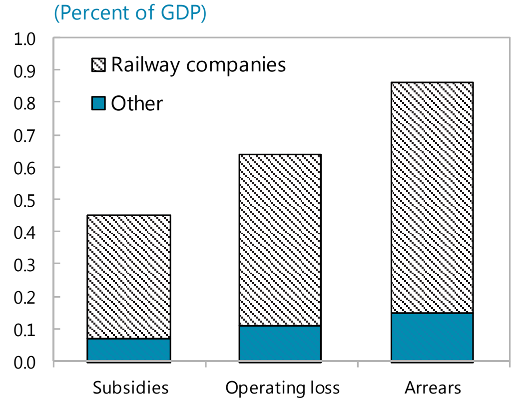
Source: Romanian authorities and IMF staff

1/ The electricity roadmap specifies a timeline for electricity suppliers to progressively increase the share of electricity sourced from the competitive market. Non-household electricity is to be fully sourced from the competitive market by January 1, 2014, and household electricity by December 31, 2017.

2/ The gas roadmap contains a calendar of price increases to raise the price of domestically produced gas up to international levels and the corresponding estimated increase in the regulated end-user price. Non-household prices are to be raised to international levels by October 1, 2014, and household prices by October 1, 2018.

31. **Reforms in the transportation sector will focus on improving the operational and financial performance of the state-owned railway companies.** Three inefficient state-owned companies dominate the Romanian rail network[8] and, along with their subsidiaries, are among the SOEs with the largest arrears and the largest annual operating deficits (see text figure). To increase the probability that these firms will become financially viable, a quarterly indicative target on the cumulative operating balances of these companies, including their subsidiaries, will complement the indicative target on SOE arrears. The authorities took an initial step toward improving the situation when they initialed a sale-purchase agreement (SPA) for the majority sale of CFR Marfa to the winning strategic investor as a prior action for the completion of the previous program. Subsequently, the authorities passed a government decision approving the terms of the SPA in July and published it on August 14, 2013. The decision calls for the parties to sign the SPA and to close the deal (exchange payment for shares) within 60 days of publication of the decision, provided the conditions precedent in the SPA

The 5 SOEs with the Largest Subsidies, Operating Losses, and Arrears for 2012 1/
(Percent of GDP)



Sources: Romanian authorities; and IMF staff estimates.

1/ Excludes companies under insolvency procedures or in liquidation.

[8] CFR Infrastructura administers and maintains the rail network; CFR Calatori provides passenger service; and CFR Marfa provides freight service.

are satisfied. If the deal is not closed, the authorities committed to sell a majority of Marfa to a new strategic investor. The authorities also plan to review both the scope of the rail network and the adequacy of budget support for rail maintenance and the rail passenger public service obligation, with support from the World Bank's advisory services. Moreover, a number of specific measures to improve the performance of CFR Infrastructura, including implementation of conditionality tied to a loan from the European Reconstruction and Development Bank (EBRD) and CFR Calatori (MEFP ¶42) have been identified.

Labor Markets

32. **The authorities continue to monitor the functioning of the new labor market legislation and are taking steps to help young Romanians enter the job market** (MEFP ¶45). The new Labor Code has helped employment growth, with fixed-term contracts growing from 6 percent of total active contracts at end-June 2011 to 9 percent at end-June 2013. The authorities continue to monitor implementation of the Social Dialogue Law and remain committed to ensure that the new legislation respects core ILO Conventions and that any amendments will be undertaken in consultation with all stakeholders through the normal legislative process. In view of the high youth unemployment in Romania, the authorities have started to amend current legislation to help young Romanians enter the labor market under the new National Job Plan. Moreover, an Apprenticeship Law that introduces a dual apprenticeship model and a law facilitating professional training stages for higher-education graduates have been adopted and are expected to be finalized over the coming months.

C. Financial Sector Priorities: Dealing with NPLs and Contingency Planning

33. **Financial sector policies need to safeguard against shocks and strengthen bank balance sheets to support the economic recovery.** To achieve these objectives, the program seeks to address the banks' sizable NPL debt overhang, finalize the operational preparedness for bank resolution powers, further strengthen financial sector supervision, and develop longer-term funding instruments, including covered bonds. Measures also need to ensure that the supply side does not continue to constrain credit should demand pick up as the economy recovers. Continued close cooperation with host supervisors will be important.

34. **The authorities are taking steps to address the high NPL overhang.** The approach is multi-pronged (MEFP ¶27-28). First, following a letter from the NBR to the banking system,[9] the NBR will continue to urge banks, within the IFRS framework, to remove fully-provisioned NPLs (especially for unsecured consumer loans) from their balance sheets in a timely manner. Second, to provide incentives for write-offs while maintaining a prudent provisioning stance on collateral treatment, the NBR will not consider additional collateral deductions unless banks make significant progress on removal of NPLs related to unsecured (consumer) loans. Third, the insolvency code is being

[9] The NBR letter clarified that under the IFRS framework banks do not necessarily have to exhaust all legal means to remove fully-provisioned NPLs from their balance sheets.

amended to accelerate and improve the long and inefficient bankruptcy proceedings. And fourth, to foster the development of a viable distressed debt market, possible discrepancies in the fiscal code and IFRS accounting rules on the treatment of NPLs sold to domestic debt management companies will be resolved in line with the outcome of the pending EC infringement case. A planned IMF TA mission in the autumn will examine accounting issues related to NPL write-offs and will serve as critical input for the program.

35. **Intensive supervision of the banking system and close monitoring of parent bank deleveraging will continue.** The NBR is conducting regular top-down and bottom-up solvency stress tests as well as top-down liquidity stress tests of the banking industry, with input from the Fund on stress scenarios. Moreover, it has just completed another collateral audit, allowing to strengthen banks' collateral evaluations where needed. A relatively small amount of additional provisions, compared to last year's collateral audit, is expected. The NBR will also examine in detail banks' loan restructuring practices as well as the adequacy of IT systems to deal with impaired assets, after which a NPL resolution action plan will be agreed with the IFIs (MEFP ¶25–26).

36. **The authorities are committed to finalize all relevant legislation related to the bank resolution framework by end-2013, in line with the Capital Requirements Directive IV.** This not only includes the new EU state aid rules for the bank stabilization measures but also the finalization of the corporate governance principles of the Deposit Guarantee Fund (DGF), as well as amendment of the internal procedures for bridge bank powers (MEFP ¶23).[10]

37. **Developing long-term funding instruments and reducing foreign-currency denominated lending should reduce bank balance sheet risk while alleviating credit supply constraints.** With parent funding currently the predominant long-term funding source, the majority of the long-term loan stock, in particular mortgages, is denominated in foreign currency. A few banks are already shifting toward RON mortgage lending, and complementary reforms should follow. In particular, covered bonds are a promising funding alternative and the authorities are committed to approving the relevant draft legislation by year end. Furthermore, the government guarantee scheme (Prima Casa) will be extended and limited to RON-denominated loans only, balancing the goals of supporting credit supply while lowering the exchange rate risk (99 percent of loans under the scheme have been extended in foreign currency, mostly to unhedged households) (MEFP ¶30). Maintaining higher reserve requirements on foreign currency deposits than on RON deposits is another tool to incentivize lending in lei. To address difficulties of viable SMEs to access credit, the authorities will reform the underused SME guarantee fund (see ¶19).

38. **The corporate governance of the new Financial Supervision Authority (FSA) should be swiftly brought into compliance with best international practices**.[11] The authorities will amend the legislation and institutional arrangements especially in regard to the size of the managing and

[10] Under the previous program, the authorities had significantly strengthened their bank resolution framework and contingency planning, including establishing a bridge bank and purchase and assumption powers.

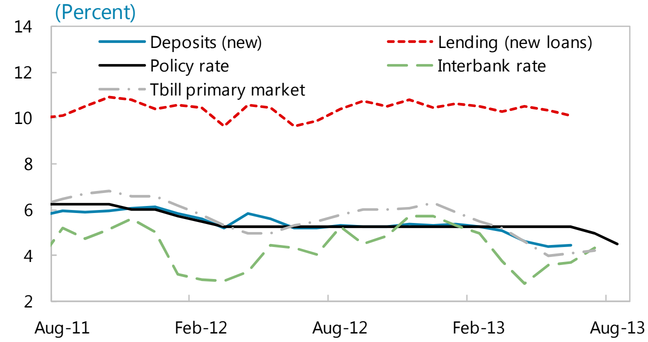
[11] The FSA is the unified regulator for pensions, insurance, and securities in Romania.

council boards, minimum required professional qualifications of FSA board members, statutory protection of the supervisory staff and institution, and avoidance of conflicts of interest (MEFP ¶31). Transparency and public disclosure of fees and commissions will also be enhanced.

D. Monetary and Exchange Rate Policies: Anchoring Expectations

39. **The central bank remains committed to reducing inflation to within its target band.** Headline inflation is expected to enter the band of 2.5±1 percentage point by September and remain within thereafter. The current end-year inflation target band will be converted to a continuous target from 2014 forward. Under the program, progress towards achieving the inflation target will be monitored through an inflation consultation clause with consultation bands drawn symmetrically around the projected path of headline CPI inflation.

Interest Rates on RON Instruments
(Percent)



Sources: NBR; and Haver.

40. **The current monetary policy rate is appropriate.** The authorities resumed the easing cycle in July and August, lowering the policy rate by a cumulative 75 basis points to 4.5 percent amid rapidly declining headline inflation, stable and low core inflation as well as the still large output gap, a tepid economic recovery and negative credit growth. Following the recent narrowing of the interest rate corridor around the policy rate, the interest rates for the NBR lending and deposit facilities now stand at 7.5 and 1.5 percent, respectively. Staff cautioned the authorities to monitor inflation developments following these easing steps and to reduce the policy rate further only if inflation declines as rapidly as expected in the coming months, inflation expectations remain firmly anchored, and market conditions permit. Staff also stressed that minimizing the divergence between interbank rates and the policy rate, through open market operations, is important to strengthen the interest rate transmission mechanism and ensure a good functioning of money markets. Ratios for minimum required reserves are expected to remain unchanged in the coming months.

41. **The program supports exchange rate flexibility while also seeking a gradual build-up of international reserves to guard against external shocks.** Most standard reserve metrics assess the current level of reserves as broadly adequate. Over the program period, substantial repayments to the Fund and a first repayment to the EC will weigh on reserves (See text table in ¶44). The program's performance criterion on Net International Reserves (NIR) targets coverage of short-term financial liabilities of around 95 percent. This will allow the NBR to continue effectively servicing peak repayments to the Fund while achieving full short-term debt coverage in subsequent years. The real exchange rate remains broadly in line with fundamentals according to the latest estimates. The NBR should hence continue allowing the exchange rate to adjust with market conditions and limit interventions in support of the leu to smoothing disorderly exchange rate volatility.

PROGRAM MODALITIES

A. Access and Phasing

42. **Romania is not expected to face actual balance of payments financing needs in 2013–15, though financing risks remain.** Under staff's assumptions, continued portfolio inflows, and renewed private sector capital inflows, including FDI, should fully cover the current account deficit. The general government is expected to fully rollover its external payments. The authorities have indicated that they will treat the SBA as precautionary. However, Romania remains vulnerable to adverse developments in international financial markets, which could produce a scenario whereby the authorities might temporarily need to draw on the proposed SBA (¶14). In staff's view, access of 170 percent of quota (SDR 1,751.34 million; about €2 billion) under a 24-month SBA together with precautionary resources under the EU's balance of payments facility (€2 billion) and a World Bank Development Policy Loan (DPL DDO, €1 billion) should provide a sufficient financing cushion against unforeseen shocks.

43. **Staff assesses that Romania meets the four criteria for exceptional access (Box 5) and considers that SBA terms are appropriate.** Given Romania's cumulative use of Fund resources, the new program entails exceptional access. Program resources would be made available at 37.8 percent of quota in 2013, 75.6 percent of quota in 2014, and 56.6 percent of quota in 2015. Disbursements will be in broadly equal installments (Table 10).

B. Program Conditionality and Monitoring

44. **The attached Letter of Intent (LOI) and MEFP describe the authorities' objectives and policies under the economic program to be supported by the Fund.** Quantitative performance criteria and indicative targets have been established for the first year and targets set for the first two reviews (Table 1). In addition, macro-critical structural benchmarks have been agreed and five prior actions have been set for program approval (Table 2). They relate to the program priorities of (i) creating institutional solutions to control government arrears; (ii) fostering investment planning and absorption of EU funds; (iii) strengthening health care financing; (iv) advancing private sector involvement in the energy sector; and (v) raising the energy sector's efficiency.

45. **The program will be monitored initially through quarterly reviews.** To firmly put the authorities on an exit path from IMF-supported programs, three quarterly reviews are envisaged followed by two semi-annual reviews, when outstanding Fund credit is expected to have fallen substantially below 300 percent of quota. Semi-annual reviews would be combined with quarterly performance criteria and quarterly missions that would facilitate implementing the authorities' economic program.

C. Capacity to Repay the Fund and Risks to the Program

46. **Romania's capacity to repay the Fund is expected to remain strong.** Fund credit outstanding has begun to decline from 40.7 percent of gross reserves in 2012. Scheduled payments will peak in 2014 at a manageable 14.4 percent of gross reserves, or 7.7 percent of exports of goods and services (Table 11). While this exposure is large, servicing risks are mitigated by the relatively low level of public debt. General government indebtedness (including guarantees) is expected to remain under 39 percent of GDP, with general government external debt peaking at around 25 percent of GDP in 2013. Total external debt was 75.1 percent of GDP in 2012 and is projected to decline over the medium term. Romania's broad political commitment to the SBA program and its excellent track record servicing external obligations, also provide comfort that it will fulfill its financial obligations to the Fund in a timely manner. An Ex Post Evaluation is envisaged for around end-2013 and an update of the Safeguards Assessment by the time of the first review.

Repurchases from IMF and Principal Repayments to the EC

(In millions of euros)

	2012	2013	2014	2015	2016	2017
IMF	1,570	4,639	4,426	1,400	109	-
BOP	1,445	3,680	3,439	1,245	109	-
Budget	125	959	987	155	-	-
EC	-	-	-	1,500	-	1,150

Source: Romanian National Authorities.

STAFF APPRAISAL

47. **Macroeconomic rebalancing and financial stability have been the hallmarks of success under the previous program.** Despite a sluggish economic recovery and period of high political uncertainty, the authorities held steadfast to their fiscal adjustment path, contained inflation pressures, and preserved banking system stability.

48. **Nevertheless, Romania remains vulnerable to shocks.** Its rebalancing process is not yet complete: the fiscal deficit has yet to reach the medium-term budgetary objective (MTO); bank balance sheet repair needs to accelerate as NPLs continue to rise, and the non-financial private sector continues to deleverage. At the same time, the economy, balance of payments, and financial sector are exposed to external shocks, such as global liquidity tightening. Gross financing requirements are sizeable, growth in Romania's main trading partners remains weak while its domestic demand is tepid, and banks continue to rely on parent funding.

49. **Setbacks to the structural reform agenda have hampered long-term growth prospects.** Critical progress was made in some areas, such as moving toward market-based pricing of energy and reducing the stock of arrears. In other areas, progress was slow, such as in increasing private

sector involvement in the energy and transportation sectors, which inhibited much-needed capital investment and delayed efficiency enhancing reforms. In areas where important legislative initiatives were approved, such as reforms of corporate governance for SOEs, implementation has disappointed.

50. **The new economic program must therefore stand on three pillars.** It aims to preserve the macroeconomic gains, provide a reserve buffer, and foster growth-oriented structural reforms. As under the previous program, moving the structural reform agenda forward will be the most challenging part given strong vested interests. A Fund-supported program can help catalyze the support for such reforms.

- **Fiscal policy:** The authorities' commitment to continue the fiscal adjustment process, underpinned by the requirements under the EU governance framework, and undertake further tax and spending reforms, including on health care, is welcome. At the same time, with Romania having exited the EDP, pressures for populist measures are on the rise that would unwind earlier difficult reforms or create new risks (e.g., PPPs without proper capacity to assess risks). These pressures need to be resisted. Moreover, internal strife needs to be overcome that have hampered institutional reforms, for example in the area of investment planning. Bold, concerted efforts are needed to improve the absorption of EU structural funds. Institutional reforms to permanently address government arrears should be expedited to safeguard the achievements made thus far.

- **Monetary policy:** The NBR needs to continue striking the right balance between anchoring inflation expectations and supporting the economic recovery. An area of further policy improvement is keeping the interbank rate more closely aligned with the policy rate to enhance policy credibility and the signaling role of the policy rate.

- **Financial sector policy:** While the banking system is well-capitalized and well-provisioned, more tangible progress is needed from the authorities' multi-pronged strategy to reducing NPLs and maintaining adequate prudential provisioning. For example, a proper implementation process for the amended insolvency code is needed to make bankruptcy proceedings more efficient, while banks need to aggressively write-down fully provisioned NPLs at an earlier juncture. Moreover, agreement on the long delayed covered bond legislation would allow creating new sources of bank long-term funding. The FSA also needs to be urgently reformed to adhere to best international practices especially with regard to its governance structure.

- **Structural reforms:** Determined implementation of macro-critical reforms to improve service quality in the transportation and energy sectors is needed to enhance growth prospects. Given the frequent delays in the reform pace in these two sectors in the past, the program asks for front-loaded measures and puts greater emphasis on SOE arrears reduction. Backtracking remains a risk, also in areas such as cross-subsidization of less efficient producers and interference in the day-to-day operations of SOEs with professional boards and management. In addition, strong efforts should be made to bring the process for the majority sale of CFR Marfa to completion.

51. **Political backing for an IMF/EC arrangement is broad-based, but diverging priorities in the coalition will likely test the government's resolve**. In principle, with the election calendar free until EU parliamentary elections in mid-2014, an opportunity exists to make headway on the reform agenda. Moreover, the ruling coalition, which has a comfortable majority, and the President support a new SBA. However, after a relatively calm period, political tension appears to be growing again as evidenced by recent public statements by the Prime Minister and the President over economic policies. In addition, as the structural reform measures deepen, vested interests will test the authorities' resolve. Active engagement in program implementation will likely be required at the highest levels to manage these pressures.

52. **Staff supports the authorities' request for a new SBA given that the economic program is balanced and Romania faces potential external shocks.** The economic program to be supported by the SBA maintains sound macroeconomic policies and financial sector stability, further builds fiscal and financial buffers, and continues structural reforms to enhance growth prospects. Fund support for the program can serve as an anchor for keeping fiscal policy and structural reforms on course as pressures are rising to ease some of the earlier reforms as well as providing an additional buffer against external shocks. Moreover, the authorities' performance under the two previous SBAs provides confidence in Romania's institutional and political capacity to implement sound policies.

Box 1. Romania 2009–11 and 2011–13 Stand-By Arrangements

2009–11 Stand-By Arrangement:

- 24-month arrangement; access: 1,111 percent of quota.
- The Fund-supported program was designed to cushion the effects of a sharp drop in capital inflows while addressing Romania's external and fiscal imbalances and strengthening the financial sector.
- Main objectives: (i) substantially lower the fiscal imbalances, accompanied by structural reforms, in order to restore market confidence and improve fiscal and external sustainability; (ii) strengthen the bank resolution framework to provide an enhanced safety net for banks to weather the economic downturn; (iii) lower inflation to and maintain it within the NBR's target range; and (iv) secure sizeable external financing to restore market confidence and cushion the adjustment process.
- The central program objectives were achieved because of strong ownership together with large and front-loaded financing, flexible program design, and appropriate reform prioritization. Market confidence was quickly restored, with a successful return to private financial markets; strong fiscal adjustment and substantial fiscal structural reforms were achieved; international reserves buffers quickly built; and the banking system weathered the crisis well.[1]

2011–13 Stand-By Arrangement:

- 27-month arrangement (including a three-month extension); access: 300 percent of quota and treated as precautionary.
- The Fund-supported program was designed to provide precautionary support against possible future economic shocks, while assisting Romania in continuing its adjustment.
- Key objectives (building on the achievements of the 2009–11 SBA): (i) continue the fiscal adjustment process while addressing problems of revenue and expenditure efficiency, and arrears; (ii) boost growth potential through structural reforms and improved flexibility of the economy; and (iii) continue fostering confidence and facilitate improved private capital flows, by improving policy stability and the business climate.

  The objective of continuing the fiscal adjustment process was achieved, setting the stage for Romania to exit the EU Excessive Deficit Procedure. Macroeconomic stability and policy credibility ensured a ratings upgrade and continued market access. Labor market reforms to increase flexibility were implemented. Progress was made in SOE monitoring and arrears reduction and energy price liberalization was initiated but the SOE reform agenda remains incomplete, and the reform process has not yet borne fruit through higher investment and growth.

[1] Romania—Ex Post Evaluation of Exceptional Access Under the 2009 Stand-By Arrangement (EBS/12/23).

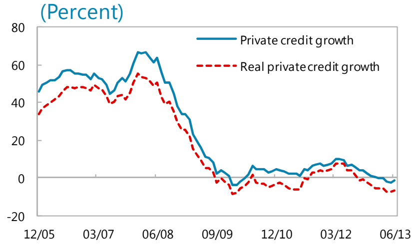
Box 2. What is Holding Back Credit Growth in Romania?

Credit growth has been sluggish in Romania. Weak parent banks and changes in parent funding strategies have been important factors. Other supply side factors, such as weak domestic bank balance sheets and tighter lending and supervisory standards, alongside tepid credit demand have also held back bank lending.

Private credit growth has been slow since the crisis and has turned negative recently. Credit to the private sector declined by 2 percent in real terms (15 percent increase in nominal terms) between 2008:Q3 and 2011:Q4 and has subsequently fallen at a faster pace of 7 percent (0.5 percent increase, nominal) through June 2013.

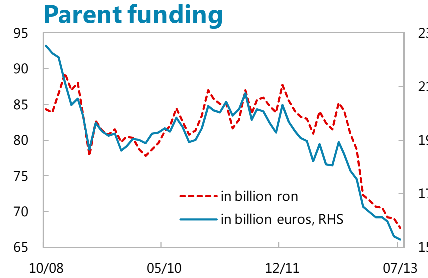
This recent credit decline coincides with lower parent bank funding. Until late 2011, the tepid credit growth partly reflected a shift in banks' asset composition away from private lending towards marketable securities. Although parent funding declined by 10 percent in euro terms during this period, capital injections and solid deposit growth of 27 percent supported a 23 percent increase in total gross assets of the banking sector. From mid-2012, however, bank assets started to fall as domestic liability growth no longer offset foreign funding, which declined by 24¾ percent between 2011:Q4 and July 2013.

Credit Growth
(Percent)



Source: Haver.

Parent funding

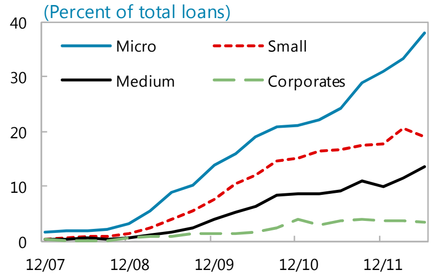


Source: National Bank of Romania.

Other supply factors also played an important role in constraining credit growth. Low growth prospects, including because of delays in implementing structural reforms, reduced lending appetite and as the crisis progressed, tighter lending standards and supervisory requirements, and weaker bank balance sheets due to the growing stock of NPLs compounded the drag on credit supply.

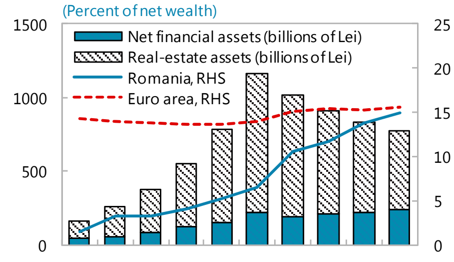
Credit demand has also fallen. Although interest rates declined gradually from their crisis level highs, private sector balance sheets have come under stress from the significant household and corporate debt overhang and falling collateral values. On the corporate side, small and medium sized enterprises (SMEs) continue to face difficulty servicing the high debt burden, as evidenced by their high NPL ratios. Meanwhile, the household ratio of liabilities to net wealth more than doubled between 2007 and 2011 as the value of real estate assets declined. Household deposits have increased, but a substantial currency mismatch remains between assets and liabilities.

NPLs by Company Size
(Percent of total loans)



Source: National Bank of Romania.

Household Liabilities
(Percent of net wealth)



Source: National Bank of Romania.

Box 3. Program Objectives, Policy Areas and Key Measures

OBJECTIVES:	1. Safeguard sound public finances underpinned by stronger fiscal institutions.		2. Continue monetary/financial sector policies that restore buffers against external shocks.		3. Reduce bottlenecks to potential growth and competitiveness through structural reforms.	
KEY POLICY AREAS:	Durable elimination of arrears.	Better public financial management, incl. medium-term planning.	NPL reduction		Energy price deregulation.	SOE reforms.
KEY MEASURES	1. Commitment control system (SB). 2. Improved monitoring and transparency of arrears (PC/SB). 3. Fiscal reporting (SB). 4. Arrears target (PC/IT).	1. Investment project prioritization (SB). 2. Net lending for EU projects (IT). 3. Healthcare reforms (SB). 4. Annual fiscal adjustment, ceiling on guarantees (PC). 5. Fiscal Compact. 6. Tax policy and administrative reform. 7. Unified Public Wage Law.	1. Removal of fully provisioned NPLs. 2. Insolvency code. 3. Prudential provisioning. 4. Capital market development and regulations. 5. SME and mortgage guarantees.	Other measures 1. Bank resolution powers of DGF. 2. Intensive supervision. 3. Inflation consultation band around inflation (IT). 4. NIR floor (PC).	1. Implementing energy price liberalization roadmap (SB). 2. Improve social safety net program.	1. SOE arrears and operating balance (IT). 2. Improve monitoring and transparency (SB). 3. Increased private ownership and restructuring in key energy and transport companies (SB).

Box 4. Romania: Initial Public Offerings

The authorities also plan to launch initial public offerings (IPO) in five key state-owned energy companies (MEFP ¶41):

- Nuclearelectrica (generates about 20 percent of Romania's electricity from nuclear power)—launch an IPO for 10 percent of the government's shares by end-September 2013;
- Romgaz (produces about 45 percent of Romania's natural gas)—launch an IPO for 15 percent of the government's shares by end-October 2013;
- Electrica (electricity distribution, supply, and service company)—launch an IPO for the majority of the government's shares by end-May 2014;
- Oltenia (produces about 30 percent of Romania's electricity from coal-fired generators)—launch an IPO for 15 percent of the government's shares by end-June 2014; and
- Hidroelectrica (generates about 25 percent of Romania's electricity from hydro power)—launch an IPO for 10 percent of the government's shares by end-June 2014.

Box 5. Romania: Exceptional Access Criteria

Staff's evaluation is that Romania continues to meet the four exceptional access criteria. Proposed access under the new SBA would equal about €2 billion (SDR 1,751.34 million, 170 percent of quota). However, the overall access by Romania to the Fund's general resources (net of scheduled purchases) exceeds normal access, requiring evaluation under the exceptional access framework. In staff's view, Romania meets these criteria:

- ***Criterion 1***—*The member is experiencing or has the potential to experience exceptional balance of payments pressures on the current account or the capital account resulting in a need for Fund financing that cannot be met within the normal limits.*

  Romania does not face actual balance of payments pressures. However, it is exposed to risks of economic and financial disruptions, particularly in Europe and from greater global volatility of capital flows. The realization of a stress scenario could give rise to a need for Fund financing, which would result, given outstanding GRA credit, in a need for Fund financing that cannot be met within the normal access limits.

- ***Criterion 2***—*A rigorous and systematic analysis indicates that there is a high probability that the member's public debt is sustainable in the medium term. However, in instances where there are significant uncertainties that make it difficult to state categorically that there is a high probability that the debt is sustainable over this period, exceptional access would be justified if there is a high risk of international systemic spillovers.*

  Public debt is low (38.2 percent of GDP, including guarantees) and is not expected to pose a risk under the program or within the medium term. Continued fiscal adjustment would ensure debt sustainability with a high probability. Barring unexpected events, potential contingent liabilities of the government would also be limited. SOE debt stands at 6.3 percent of GDP (including SOEs under insolvency procedures or in liquidation). The 2010 pension reform has also helped mitigate the impact of demographic pressures on fiscal sustainability. Despite remaining vulnerabilities to the banking system, including due to a large share of foreign currency denominated loans, and high rollover needs, downside risks materializing are not expected to render public debt unsustainable over the medium term. Banks are generally well capitalized and their short-term external liabilities are below 4 percent of GDP. Total external debt has risen to 75.1 percent of GDP in 2012 and is expected to decline. Starting from 2013, repayments to the Fund, a manageable current account deficit, and higher economic growth would gradually reduce the external debt over the medium term. Overall, Romania's public debt, including contingent liabilities, is assessed as sustainable in the medium term with a high probability.

Box 5. Romania: Exceptional Access Criteria (concluded)

- ***Criterion 3****—The member has prospects of gaining or regaining access to private capital markets within the timeframe when Fund resources are outstanding.*

  Romania has maintained access to private capital markets, which is expected to continue going forward under normal market conditions. The authorities have indicated that they will treat the SBA as precautionary. Experience with the previous precautionary SBA shows that it strengthened market confidence in Romania's economic policies. Even under an adverse scenario (as described in ¶ 14), Romania is expected to continue having market access, but with lower rollover rates. In 2010–11, Romania was able to return to external markets in the midst of turbulence in Europe. With better fundamentals now, the prospect should be good that it can remain in the market, even if at higher rates. In 2012 Romania sold $2.25 billion in U.S. dollar denominated bonds, €2.25 billion in Eurobonds in addition to domestic issuances of Euro-denominated instruments totaling €763 million. The authorities continued to tap international markets in 2013, selling $1.5 billion in 10-year U.S. dollar-denominated bonds at a yield of 4.5 percent in February and slightly more than €1.4 billion in three-year euro-denominated bonds with an average yield of less than 3 percent thus far on the local market.

- ***Criterion 4****—The policy program of the member provides a reasonably strong prospect of success, including not only the member's adjustment plans but also its institutional and political capacity to deliver that adjustment.*

  Romania's adherence to the recent Fund-supported program has been good overall despite the need for significant fiscal adjustment and difficult structural reforms. The two delays in completing the second and third reviews in the 2009 SBA and the seventh and eighth reviews of the 2011 SBA were due to political reasons. Quantitative performance criteria were met through much of the program, but the political instability that led to three changes in government in 2012 and included two elections and a failed referendum to impeach the President, took its toll on the program towards the end. Several targets were missed, albeit narrowly, and the structural reform agenda, which had advanced slowly through most of the program, stalled. The final combined reviews were thus postponed by three months in order for the new government to undertake corrective actions to meet program commitments, which the authorities have since successfully completed.

  Going forward, tensions have eased after the December 2012 elections and a new program has political backing within the coalition, which has a comfortable majority, and from the President. With politically difficult issues in the forefront of the reform agenda going forward, the authorities see a new program as an important catalyst for broader support in advancing those efforts. The authorities' performance during the recent program lends confidence in their institutional and political capacity to continue to implement sound policies. On the fiscal front a much more gradual pace of planned adjustment, following the sharp reduction in the structural budget deficit in the past three years, suggests good prospects of success.

Table 1. Romania: Quantitative Program Targets

	2012	2013			2014	
	Dec	June	Sept	Dec	March	June
	Actual	Prelim.	Prog.	Prog.	Indicative	Indicative
I. Quantitative Performance Criteria						
1. Floor on the change in net international reserves (mln euros) 1/	16,344	3,922	3,922	3,922	250	0
2. Floor on the general government overall balance (mln lei) 2/	-17,430	-6,629	-9,181	-14,700	-4,000	-6,200
3. Ceiling on the stock of central government and social security arrears (bn lei)	0.027	0.04	0.02	0.02	0.02	0.02
4. Ceiling on general government guarantees issued since end-2008 (face value, bn lei)	9.8	10.9	16.0	16.0	18.0	18.0
II. Continuous Performance Criterion						
5. Nonaccumulation of external debt arrears	0	0	0	0	0	0
III. Inflation Consultation						
6. 12-month rate of inflation in consumer prices						
Outer band (upper limit)	...	...	5.1	5.3	4.6	5.0
Inner band (upper limit)	...	...	4.1	4.3	3.6	4.0
Actual/*Center point*	5.0	5.4	*3.1*	*3.3*	*2.6*	*3.0*
Inner band (lower limit)	...	...	2.1	2.3	1.6	2.0
Outer band (lower limit)	...	...	1.1	1.3	0.6	1.0
IV. Indicative Target						
7. Ceiling on general government current primary spending (excl. EU funds and social assistance, mln lei) 2/	134,330	70,412	106,300	147,509	36,700	74,400
8. Floor on operating balance (earnings before interest and tax, net of subsidies and one-off adjustments to income due to financial or accounting operations) of key SOEs (as defined in paragraph 22 of the TMU (bn. lei)) 2/	-3.3	-1.0	-1.6	-2.3	-0.5	-0.8
9. Ceiling on outstanding payments past due of all central-government owned enterprises (as defined in TMU, bn lei)	12.6	8.2	7.5	5.6	4.7	3.7
10. Ceiling on stock of local government arrears (bn lei)	0.84	0.14	0.30	0.30	0.30	0.30
11. Ceiling on stock of net Treasury loans for EU-funded projects (mln lei) 2/	...	1,546	3,000	3,000	3,000	3,000

1/ The end-December 2012 figure is a stock. Reported at program exchange rates and gold price.
2/ Cumulative figure during calendar year (e.g. September 2013 figure is cumulative from January 1, 2013).

Table 2. Romania: Proposed Conditionality		
	Measure	Target Date
Prior Actions		
1.	Approve a government ordinance to provide standard definitions of commitments for the commitment control system.	
2.	Approve a government ordinance defining the prioritization criteria for public investment projects.	
3.	Approve a government ordinance to broaden the social contributions base by applying a mandatory tax (health contribution) on rental income of individuals, to be implemented from January 1, 2014.	
4.	Authorize, through a General Shareholder's Meeting of Hidroelectrica, the current interim board to take decisions in accordance with law 31/1990, while it seeks to appoint a professional board in accordance with the SOE Corporate Governance ordinance.	
5.	Clarify the tax treatment of securities bought in Romgaz traded on the foreign stock exchange and adopt, if needed, the necessary legal basis.	
Structural benchmarks		
1.	Start publishing monthly arrears reports and corrective measures being taken by the central and local governments, by unit, on a quarterly basis.	End-September 2013
2.	Prepare the basic health package within the existing spending envelope which will also define the scope of the private sector in the health care system in the future.	End-September 2013
3.	Prepare medium-term financial projections that properly identify the fiscal implications of EU-funded projects, including co-financing needs, financial corrections and non-eligible spending.	Mid-October 2013
4.	Approve, by government memorandum, a list of significant priority projects, based on the prioritization criteria, to help prepare for the 2014 budget.	Mid-October 2013
5.	Launch an initial public offering of 15 percent of the government's shares in Romgaz.	Mid-November 2013
6.	Appoint a professional board in Hidroelectrica in accordance with the provisions of Ordinance 109/2011.	End-November 2013
7.	Approve Covered Bond legislation.	End-December 2013
8.	Fully operationalize the commitment control system, supported by necessary legal and procedural changes and cover expenditures of the MoPF and at least one additional unit at both the central and local government levels.	End-January 2014
9.	Launch an initial public offering of a majority of the government's shares in Electrica, after the planned capital increase.	End-May 2014
10.	Fully operationalise the commitment control system for all general government entities.	End-June 2014
11.	Launch an initial public offering of 15 percent of the government's shares in Oltenia, prior to the planned capital increase.	End-June 2014
12.	Launch an initial public offering of 10 percent of the government's shares in Hidroelectrica, after the planned capital increase.	End-June 2014
13.	Roll out the consolidated fiscal reporting system to all government entities.	End-June 2014
14.	Resolve possible discrepancies in the fiscal code and IFRS accounting rules on the treatment of NPLs sold to domestic debt management companies in line with the outcome of the pending EC infringement case.	End-December 2014
15.	Prepare and publish consolidated general government accrual based financial statements and ESA95 based reports from the system (the first sets of reports will be for the year ending 2014), and reconcile with each other and with cash-based budget execution reports.	End-June 2015

Table 3. Romania: Selected Economic and Social Indicators, 2009–14

	2009	2010	2011 Est.	2012 Est.	2013 Proj.	2014 Proj.
Output and prices			(Annual percentage change)			
Real GDP	-6.6	-1.1	2.2	0.7	2.0	2.2
Contributions to GDP growth						
Domestic demand	-13.5	-1.1	2.6	1.5	0.4	2.2
Net exports	7.0	0.0	-0.5	-0.8	1.6	0.0
Consumer price index (CPI, average)	5.6	6.1	5.8	3.3	4.5	2.8
Consumer price index (CPI, end of period)	4.7	8.0	3.1	5.0	3.3	3.0
Core price index (HICP, end of period)	2.3	4.2	2.4	3.0	2.0	2.0
Producer price index (average)	2.5	4.4	7.1	5.4	...	...
Unemployment rate (average)	6.9	7.3	7.4	7.0	7.1	7.1
Nominal wages	8.4	2.5	4.9	5.0	5.3	4.0
Saving and Investment			(In percent of GDP)			
Gross domestic investment	25.4	25.6	26.9	27.0	26.1	26.2
Gross national savings	21.2	21.2	22.4	23.1	24.1	23.7
General government finances 1/						
Revenue	31.2	32.2	32.6	32.9	33.4	33.1
Expenditure	38.5	38.6	36.9	35.4	35.8	35.1
Fiscal balance	-7.3	-6.4	-4.3	-2.5	-2.3	-2.0
External financing	2.6	2.8	2.7	3.3	1.1	0.9
Domestic financing	4.6	3.6	1.5	-0.8	1.3	1.1
Privatization proceeds 2/	0.1	0.1	0.0	0.0	...	...
Fiscal balance (including PNDI)	-7.3	-6.4	-4.3	-2.6	-2.3	-2.0
Primary balance	-6.1	-5.0	-2.7	-0.7	-0.5	-0.2
Structural fiscal balance 3/	-6.8	-5.1	-3.0	-1.7	-1.3	-0.9
Gross public debt (direct debt only)	21.7	28.1	32.3	35.8	35.9	36.0
Gross public debt (including guarantees)	23.8	31.1	34.4	38.1	38.1	38.1
Money and credit			(Annual percentage change)			
Broad money (M3)	9.0	6.9	6.6	2.7	6.6	5.5
Credit to private sector	0.9	4.7	6.6	1.3	-1.1	2.7
Interest rates, eop 4/			(In percent)			
Euribor, six-months	4.5	1.2	1.6	0.3	0.3	...
NBR policy rate	8.0	6.25	6.0	5.25	4.50	...
NBR lending rate (Lombard)	12.0	10.25	10.0	9.25	7.50	...
Interbank offer rate (1 week)	10.7	3.6	6.0	5.8	2.3	...
Balance of payments			(In percent of GDP)			
Current account balance	-4.2	-4.4	-4.5	-3.9	-2.0	-2.5
Merchandise trade balance	-5.8	-6.1	-5.6	-5.6	-3.9	-4.2
Capital and financial account balance	-2.5	1.0	1.6	2.5	4.6	3.8
Foreign direct investment balance	3.0	1.8	1.4	1.3	1.0	1.5
International investment position	-62.3	-62.6	-64.2	-64.9	-65.1	-67.3
Gross official reserves	26.1	28.9	28.4	26.9	24.3	21.8
Gross external debt	68.7	74.3	75.2	75.1	71.3	70.4
Exchange rates 4/						
Lei per euro (end of period)	4.2	4.3	4.3	4.4	4.4	...
Lei per euro (average)	4.2	4.2	4.2	4.5	4.4	...
Real effective exchange rate						
CPI based (percentage change)	-7.5	1.9	2.8	-2.7	2.6	...
GDP deflator based (percentage change)	-8.7	1.9	2.6	-4.1	...	...
Memorandum Items:						
Nominal GDP (in bn RON)	501.1	523.7	556.7	587.5	626.2	661.3
Potential output growth	1.3	1.2	1.2	1.1	1.3	1.6
Potential output gap	-1.2	-2.5	-1.3	-2.9	-2.3	-1.8

Social and Other Indicators

GDP per capita (current EUR, 2012): 6,179; **GDP per capita, PPP** (current international $, 2011): 15,163

People at risk of poverty or social exclusion: 40.3% (2011)

Sources: Romanian authorities; IMF staff estimates and projections; and World Development Indicators database.

1/ General government finances refer to cash data.

2/ Excludes receipts from planned privatizations under the program.

3/ Fiscal balance (cash basis) adjusted for the automatic effects of the business cycle.

4/ For 2013: Latest available data

Table 4. Romania: Medium-Term Macroeconomic Framework, Current Policies, 2009–18

	2009	2010	2011 Est.	2012 Est.	2013 Proj.	2014 Proj.	2015 Proj.	2016 Proj.	2017 Proj.	2018 Proj.
GDP and prices (annual percent change)										
Real GDP	-6.6	-1.1	2.2	0.7	2.0	2.2	2.5	2.9	3.4	3.5
Real domestic demand	-12.0	-1.1	2.5	1.4	0.4	2.1	2.7	3.2	3.6	3.9
Consumption	-7.4	-1.3	0.9	1.2	0.9	1.9	2.5	3.0	3.4	3.5
Investment	-28.1	-1.8	7.3	4.9	0.5	3.0	3.5	3.7	4.1	5.1
Exports	-6.4	13.2	10.3	-3.0	6.6	6.4	7.6	7.5	8.6	8.4
Imports	-20.5	11.1	10.0	-0.9	2.3	6.0	7.5	7.7	8.6	8.9
Consumer price index (CPI, average) 2/	5.6	6.1	5.8	3.3	4.5	2.8	2.9	2.7	2.6	2.5
Consumer price index (CPI, end of period) 2/	4.7	8.0	3.1	5.0	3.3	3.0	2.9	2.7	2.6	2.5
Saving and investment (in percent of GDP)										
Gross national saving	21.2	21.2	22.4	23.1	24.1	23.7	23.7	23.6	23.5	23.6
Government	-2.0	0.8	3.4	3.9	3.8	3.9	4.2	4.6	4.7	4.7
Private	23.2	20.3	19.0	19.2	20.3	19.8	19.5	18.9	18.8	18.8
Gross domestic investment	25.4	25.6	26.9	27.0	26.1	26.2	26.4	26.5	26.6	26.9
Government	5.2	7.2	7.7	6.5	6.2	5.9	6.0	6.4	6.5	6.6
Private	20.1	18.3	19.2	20.6	19.9	20.3	20.4	20.0	20.1	20.4
General government (in percent of GDP)										
Revenue	31.2	32.2	32.6	32.9	33.4	33.1	33.1	33.0	32.8	32.6
Tax revenue	27.2	26.5	28.0	28.2	28.2	27.6	27.4	27.3	27.2	27.1
Non-tax revenue	2.9	3.8	3.3	3.1	3.0	3.2	3.2	3.1	3.1	3.1
Grants	1.0	1.8	1.2	1.4	2.0	2.2	2.4	2.5	2.4	2.2
Expenditure	38.5	38.6	36.9	35.4	35.8	35.1	34.8	34.9	34.6	34.4
Fiscal balance	-7.3	-6.4	-4.3	-2.5	-2.3	-2.0	-1.8	-1.8	-1.8	-1.8
Fiscal balance (including PNDI)	-7.3	-6.4	-4.3	-2.6	-2.3	-2.0	-1.8	-1.8	-1.8	-1.8
Structural fiscal balance 1/	-6.8	-5.1	-3.0	-1.7	-1.2	-0.9	-1.2	-1.5	-1.8	-2.0
Gross general government debt (direct debt only)	21.7	28.1	32.3	35.8	35.9	36.0	35.2	35.0	34.8	34.6
Gross general government debt (including guarantees)	23.8	31.1	34.4	38.1	38.1	38.1	37.1	36.9	36.5	36.2
Monetary aggregates (annual percent change)										
Broad money (M3)	9.0	6.9	6.6	2.7	6.6	5.5	5.8	6.7	6.7	6.7
Credit to private sector	0.9	4.7	6.6	1.3	-1.1	2.7	5.8	7.0	7.0	7.3
Balance of payments (in percent of GDP)										
Current account	-4.2	-4.4	-4.5	-3.9	-2.0	-2.5	-2.7	-2.9	-3.1	-3.4
Trade balance	-5.8	-6.1	-5.6	-5.6	-3.9	-4.2	-4.2	-4.3	-4.4	-4.6
Services balance	-0.2	0.3	0.3	0.4	1.4	1.3	1.3	1.3	1.3	1.3
Income balance	-1.6	-1.5	-1.7	-1.3	-1.4	-1.4	-1.5	-1.5	-1.6	-1.6
Transfers balance	3.5	2.9	2.5	2.5	2.0	1.9	1.7	1.6	1.5	1.4
Capital and financial account balance	-2.5	1.0	1.6	2.5	4.6	3.8	2.9	4.4	4.6	4.4
Foreign direct investment, balance	3.0	1.8	1.4	1.3	1.0	1.5	1.6	1.7	1.8	1.8
Memorandum items:										
Gross international reserves (in billions of euros)	30.9	36.0	37.3	35.4	34.1	31.6	30.5	32.8	35.4	37.2
Gross international reserves (in months of next year's imports)	7.2	7.2	7.5	7.1	6.5	5.6	5.1	5.0	5.0	5.0
International investment position (in percent of GDP)	-62.3	-62.6	-64.2	-64.9	-65.1	-67.3	-66.1	-64.4	-62.8	-61.5
External debt (in percent of GDP)	68.7	74.3	75.2	75.1	71.3	70.4	67.6	65.0	62.9	60.0
Short-term external debt (in percent of GDP)	13.2	15.7	17.4	15.4	15.2	15.1	14.4	13.6	12.7	11.9
Terms of trade (merchandise, percent change)	1.1	1.0	2.7	3.2	-0.1	-1.1	0.1	0.0	0.0	0.1
Nominal GDP (in millions of lei)	501,139	523,693	556,708	587,499	626,200	661,269	700,706	742,244	788,530	838,045
Output gap (percent of potential GDP)	-1.2	-3.5	-2.5	-2.9	-2.3	-1.8	-1.3	-0.8	0.0	0.6
Potential GDP (percent change)	1.3	1.2	1.2	1.1	1.3	1.6	2.0	2.4	2.6	2.9

Sources: Romanian authorities; and IMF staff estimates and projections.

1/ Actual fiscal balance adjusted for the automatic effects of the business cycle.
2/ Projections are based on HICP weights.

Table 5. Romania: Balance of Payments, 2009–15
(In billions of euros, unless otherwise indicated)

	2009	2010	2011	2012	2013		2014		2015	
				Est.	Proj.	Scen.	Proj.	Scen.	Proj.	Scen.
Current account balance	-4.9	-5.5	-5.9	-5.2	-2.7	-3.2	-3.6	-5.1	-4.1	-5.7
Merchandise trade balance	-6.9	-7.6	-7.4	-7.4	-5.5	-5.9	-6.1	-7.1	-6.4	-7.5
Exports (f.o.b.)	29.1	37.4	45.3	45.1	46.9	46.4	49.4	44.9	52.6	47.8
Imports (f.o.b.)	36.0	44.9	52.7	52.4	52.4	52.2	55.4	52.0	59.0	55.3
Services balance	-0.3	0.4	0.3	0.5	1.9	1.8	1.9	1.5	2.0	1.6
Exports of non-factor services	7.1	6.6	7.3	7.6	9.3	9.2	9.8	8.9	10.4	9.5
Imports of non-factor services	7.4	6.2	6.9	7.1	7.4	7.4	7.9	7.4	8.4	7.9
Income balance	-1.9	-1.9	-2.2	-1.7	-2.0	-2.0	-2.1	-2.1	-2.3	-2.3
Receipts	1.2	0.9	1.3	1.4	1.1	1.1	1.0	1.0	0.9	0.9
Payments	3.1	2.8	3.5	3.0	3.1	3.0	3.1	3.0	3.3	3.2
Current transfer balance	4.1	3.6	3.3	3.4	2.7	2.7	2.7	2.6	2.6	2.5
Capital and financial account balance	-2.9	1.2	2.0	3.3	6.4	6.1	5.5	3.6	4.4	2.9
Capital account balance	0.6	0.2	0.7	1.9	1.9	1.9	1.9	1.9	1.9	1.9
Foreign direct investment balance	3.6	2.2	1.8	1.7	1.4	1.4	2.1	1.8	2.4	2.1
Portfolio investment balance	0.5	0.9	1.6	3.6	4.4	4.4	1.2	1.2	-0.3	-0.3
Other investment balance	-7.6	-2.1	-2.1	-3.9	-1.3	-1.6	0.3	-1.3	0.3	-0.8
General government	-2.0	0.1	-0.4	-0.5	-0.1	-0.1	-0.3	-0.3	-0.6	-0.6
Domestic banks	-4.5	1.0	-0.2	-2.4	-1.2	-1.4	0.3	-0.7	0.5	-0.1
Other private sector	-1.0	-3.2	-1.5	-1.0	0.0	-0.2	0.3	-0.3	0.5	0.0
Errors and omissions	-1.0	-0.2	0.4	1.0	-0.4	-0.4	0.0	0.0	0.0	0.0
Multilateral financing	2.1	3.7	3.5	1.0	...	0.7	...	1.3	...	1.0
European Commission	1.5	2.2	1.4	0.0	...	0.4	...	0.9	...	0.7
World Bank	0.3	0.0	0.7	0.0	...	0.2	...	0.4	...	0.3
EIB/EBRD/IFC	0.3	1.5	1.4	1.0	...	...	...	...	...	...
Overall balance	-6.7	-0.8	0.0	0.1	3.3	2.5	1.9	-1.5	0.3	-2.8
Financing	6.7	0.8	0.0	-0.1	-3.3	-2.5	-1.9	1.5	-0.3	2.8
Gross international reserves (increase: -)	-1.1	-3.5	-0.9	1.5	1.3	1.0	2.5	3.7	1.1	2.5
Use of Fund credit, net	6.8	4.3	0.9	-1.6	-4.6	-4.2	-4.4	-3.5	-1.4	-0.7
Purchases 1/	6.8	4.3	0.9	0.0	0.0	0.4	0.0	0.9	0.0	0.7
Repurchases	0.0	0.0	0.0	-1.6	-4.6	-4.6	-4.4	-4.4	-1.4	-1.4
Other liabilities, net	1.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:					(In percent of GDP)					
Current account balance	-4.2	-4.4	-4.5	-3.9	-2.0	-2.3	-2.5	-3.6	-2.7	-3.8
Foreign direct investment balance	3.0	1.8	1.4	1.3	1.0	1.0	1.5	1.3	1.6	1.4
Merchandise trade balance	-5.8	-6.1	-5.6	-5.6	-3.9	-4.2	-4.2	-5.0	-4.2	-5.0
Exports	24.6	30.0	34.5	34.2	33.4	33.2	34.1	31.6	34.4	32.0
Imports	30.4	36.1	40.1	39.8	37.3	37.4	38.3	36.6	38.5	37.0
Gross external financing requirement	29.5	25.9	29.1	32.8	28.0	28.4	27.6	29.2	23.9	25.4
					(Annual percent change)					
Terms of trade (merchandise)	1.1	1.0	2.7	3.2	-0.1	-0.1	-1.1	-1.1	0.1	0.1
Export volume	-6.4	13.2	10.3	-3.0	6.6	5.4	6.4	-2.0	7.6	7.6
Import volume	-20.5	11.1	10.0	-0.9	2.3	2.0	6.0	-0.4	7.5	7.5
Export prices	4.7	6.8	8.9	2.6	-2.5	-2.5	-1.2	-1.2	-1.1	-1.1
Import prices	3.3	5.7	6.5	0.4	-2.4	-2.4	-0.1	-0.1	-1.2	-1.2
					(In billions of euros)					
Gross international reserves 2/	30.9	36.0	37.3	35.4	34.1	34.4	31.6	30.7	30.5	28.2
Excluding Fund credit	24.1	24.7	25.3	24.5	28.1	28.4	30.1	29.2	30.4	28.0

Sources: Romanian authorities; and IMF staff estimates and projections.
1/ Includes IMF disbursement to the Treasury of €0.9 billion in 2009 and €1.2 billion in 2010.
2/ Operational definition. Reflects the allocation of SDR 908.8 million that was made available in two tranches in August and September 2009.

Table 6. Romania: Gross Financing Requirements, 2012–15
(In billions of euros, unless otherwise indicated)

	2012	2013						2014						2015	
		Q1	Q2	Q3	Q4	Year		Q1	Q2	Q3	Q4	Year		Year	
				Proj	Proj	Proj.	Scen.	Proj	Proj	Proj	Proj	Proj.	Scen.	Proj.	Scen.
I. Total financing requirements	**43.4**	**8.0**	**7.8**	**7.2**	**10.0**	**33.0**	**33.5**	**7.3**	**8.2**	**7.7**	**9.3**	**32.5**	**33.9**	**34.7**	**35.9**
I.A. Current account deficit	5.2	-0.3	-0.4	1.4	2.0	2.7	3.2	1.2	0.5	0.9	1.0	3.6	5.1	4.1	5.7
I.B. Short-term debt	25.8	5.5	4.7	4.1	4.9	19.2	19.2	4.2	4.6	4.6	5.5	19.0	18.9	19.8	19.4
Public sector	7.5	2.0	1.8	0.9	0.9	5.6	5.6	0.9	0.7	0.9	0.9	3.4	3.4	3.6	3.6
Banks	14.2	2.6	2.1	1.9	2.7	9.2	9.2	2.1	3.1	2.3	3.1	10.7	10.6	11.0	10.6
Corporates	4.2	1.0	0.8	1.3	1.3	4.4	4.4	1.1	0.8	1.5	1.5	4.9	4.9	5.2	5.2
I.C. Maturing medium- and long-term debt	12.0	2.7	3.6	2.1	3.3	11.6	11.6	2.0	3.1	2.2	3.0	10.4	10.4	11.4	11.4
Public sector	2.8	0.4	0.8	0.6	1.0	2.8	2.8	0.5	0.9	0.6	0.6	2.5	2.5	3.7	3.7
Banks	4.9	1.6	2.0	0.7	0.5	4.8	4.8	0.6	1.1	0.9	0.9	3.5	3.5	3.3	3.3
Corporates	4.3	0.7	0.8	0.8	1.7	4.0	4.0	0.9	1.1	0.8	1.5	4.4	4.4	4.4	4.4
I.D. Other net capital outflows 1/	0.5	0.1	-0.1	-0.3	-0.3	-0.6	-0.6	-0.1	-0.1	-0.1	-0.2	-0.5	-0.5	-0.6	-0.6
II. Total financing sources	**41.6**	**10.3**	**9.3**	**7.1**	**9.9**	**36.7**	**36.4**	**7.5**	**7.9**	**9.3**	**9.8**	**34.4**	**32.4**	**36.5**	**34.6**
II.A. Foreign direct investment, net	1.7	0.2	0.4	0.5	0.4	1.4	1.4	0.2	0.5	0.7	0.7	2.1	1.8	2.4	2.1
II.B. Capital account inflows	1.9	0.3	0.7	0.5	0.5	1.9	1.9	0.2	0.4	0.5	0.8	1.9	1.9	1.9	1.9
II.C. Short-term debt	23.3	4.9	5.4	4.5	5.5	20.3	20.3	4.4	4.7	4.8	5.6	19.5	19.2	20.0	19.5
Public sector	6.7	1.9	1.8	0.9	0.9	5.5	5.5	0.9	0.7	0.9	0.9	3.4	3.4	3.6	3.6
Banks	11.9	1.9	2.7	2.1	3.1	9.9	9.9	2.3	3.1	2.4	3.1	10.9	10.6	11.0	10.6
Corporates	4.6	1.1	0.8	1.5	1.5	4.9	4.9	1.2	0.9	1.5	1.6	5.2	5.2	5.3	5.3
II.D. Medium- and long-term debt	14.7	4.9	2.9	1.7	3.6	13.1	12.8	2.7	2.3	3.2	2.6	10.9	9.5	12.2	11.0
Public sector	6.6	3.7	1.4	0.4	1.5	7.0	7.0	1.3	0.1	1.6	0.2	3.2	3.2	3.5	3.5
Banks	5.1	0.9	1.0	0.6	0.5	3.0	3.0	0.6	1.1	0.8	0.9	3.3	2.8	3.6	3.1
Corporates	3.0	0.3	0.5	0.7	1.6	3.1	2.8	0.9	1.1	0.8	1.5	4.3	3.5	5.1	4.4
Errors and omissions	1.0	-0.4	0.1	0.0	0.0	-0.4	-0.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
III. Increase in gross international reserves	-1.5	1.0	0.4	-1.2	-1.4	-1.3	-1.0	-1.2	-1.8	0.7	-0.2	-2.5	-3.7	-1.1	-2.5
IV. Financing gap	**-0.6**	**-0.9**	**-1.2**	**-1.2**	**-1.4**	**-4.6**	**-3.5**	**-1.4**	**-1.5**	**-0.9**	**-0.6**	**-4.4**	**-2.2**	**-2.9**	**-1.2**
V. Program financing	**-0.6**	**-0.9**	**-1.2**	**-1.2**	**-1.4**	**-4.6**	**-3.5**	**-1.4**	**-1.5**	**-0.9**	**-0.6**	**-4.4**	**-2.2**	**-2.9**	**-1.2**
IMF	-1.6	-0.9	-1.2	-1.2	-1.4	-4.6	-4.2	-1.4	-1.5	-0.9	-0.6	-4.4	-3.5	-1.4	-0.7
Purchases	0.0	0.0	0.0	0.0	0.0	0.0	0.4	0.0	0.0	0.0	0.0	0.0	0.9	0.0	0.7
Repurchases	-1.6	-0.9	-1.2	-1.2	-1.4	-4.6	-4.6	-1.4	-1.5	-0.9	-0.6	-4.4	-4.4	-1.4	-1.4
European Commission	0.0	0.0	0.0	0.0	0.0	0.0	0.4	0.0	0.0	0.0	0.0	0.0	0.9	-1.5	-0.8
Disbursements	0.0	0.0	0.0	0.0	0.0	0.0	0.4	0.0	0.0	0.0	0.0	0.0	0.9	0.0	0.7
Principal repayments	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	-1.5	-1.5
Others	1.0	...	...	...	...	...	0.2	...	...	...	...	...	0.4	...	0.3
World Bank	0.0	...	...	...	...	...	0.2	...	...	...	...	...	0.4	...	0.3
EIB/EBRD/IFC	1.0	...	...	...	...	...	...	...	...	...	...	...	...	...	...
Memorandum items:															
Rollover rates for amortizing debt ST (in percent)															
Public sector	90	97	101	100	100	99	99	100	100	100	100	100	100	101	101
Banks	84	73	131	115	115	107	107	105	100	105	100	102	100	100	100
Corporates	111	117	101	110	115	111	111	110	105	105	105	106	106	102	102
Rollover rates for amortizing debt MLT (in percent)															
Public sector	238	940	172	62	155	252	252	270	14	279	29	126	126	95	95
Banks	104	60	49	90	90	63	62	90	95	95	100	95	80	110	95
Corporates	69	49	60	90	90	77	70	95	100	100	100	99	80	115	100
Rollover rates for total amortizing debt (in percent)															
Public sector	130	236	123	85	129	150	150	157	50	171	72	111	111	98	98
Banks	89	68	91	108	111	92	92	102	99	102	100	100	95	102	99
Corporates	90	88	80	103	101	95	92	103	102	103	102	103	94	108	101
Gross international reserves 2/	35.4	36.4	35.4	...	...	34.1	34.4	...	...	...	...	31.6	30.7	30.5	28.2
Coverage of gross international reserves															
- Months of imports of GFNS (next year)	7.1	6.9	6.7	...	...	6.5	6.9	...	...	...	...	6.3	6.2	5.1	5.0
- Short-term external debt (in percent)	97.0	100.0	97.3	...	...	93.7	94.5	...	...	...	...	97.4	95.3	94.8	88.2

Sources: Romanian authorities; and IMF staff estimates and projections.
1/ Includes includes portfolio equity, financial derivatives and other investments, assets position.
2/ Operational definition.

Table 7. Romania: General Government Operations, 2009–15
(In percent of GDP)

	2009	2010	2011	2012	2013 Prog.	2014 Proj.	2015 Proj.
Revenue	31.2	32.2	32.6	32.9	33.4	33.1	33.1
Taxes	27.2	26.5	28.0	28.2	28.2	27.6	27.4
Corporate income tax	2.7	2.1	2.0	2.0	1.9	1.9	1.9
Personal income tax	3.7	3.4	3.5	3.6	3.7	3.7	3.7
VAT	6.8	7.5	8.6	8.6	8.5	8.2	8.2
Excises	3.1	3.3	3.4	3.4	3.5	3.5	3.5
Customs duties	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Social security contributions	9.5	8.7	9.1	8.8	8.7	8.7	8.6
Other taxes	1.2	1.3	1.2	1.7	1.8	1.4	1.3
Nontax revenue	2.9	3.8	3.3	3.1	3.0	3.2	3.2
Capital revenue	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Grants, including EU disbursements	1.0	1.8	1.2	1.4	2.0	2.2	2.4
Expenditure	38.5	38.6	36.9	35.4	35.8	35.1	34.8
Current expenditure	34.6	35.0	32.8	32.2	32.9	33.2	33.0
Compensation of employees	9.3	8.2	6.9	6.9	7.4	7.2	7.1
Goods and services	5.6	5.6	5.7	5.9	6.3	6.0	6.0
Interest	1.2	1.4	1.6	1.8	1.8	1.8	1.8
Subsidies	1.4	1.3	1.2	1.0	0.8	0.9	0.8
Transfers	16.6	18.2	17.1	16.3	16.4	17.1	17.0
Pensions	8.0	8.0	8.5	8.2	7.9	8.0	8.0
Other social transfers	4.8	5.1	3.7	3.2	3.2	3.1	3.0
Other transfers 1/	3.4	4.5	4.3	4.4	4.8	5.5	5.6
Other spending	0.5	0.6	0.6	0.5	0.5	0.4	0.4
Projects with external credits	0.4	0.3	0.4	0.3	0.2	0.2	0.2
Capital expenditure 2/	4.4	3.7	4.1	3.3	2.8	1.8	1.8
Reserve fund	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net lending and expense refunds	-0.5	-0.1	-0.1	-0.1	0.0	0.0	0.0
Fiscal balance	-7.3	-6.4	-4.3	-2.5	-2.3	-2.0	-1.8
Primary balance	-6.1	-5.0	-2.7	-0.7	-0.5	-0.2	0.0
Fiscal balance including PNDI 3/	-7.3	-6.4	-4.3	-2.6	-2.3	-2.0	-1.8
Idem including EU receivables	…	…	…	-3.0	…	…	…
Financing	7.3	6.4	4.3	2.5	2.3	2.0	1.8
External borrowing (net)	2.6	2.8	2.7	3.3	1.1	0.9	0.2
Domestic borrowing (net)	5.8	4.0	2.2	0.9	1.3	1.1	1.0
Use of deposits	-1.2	-0.4	-0.7	-1.7	0.0	0.0	0.6
Privatization proceeds	0.1	0.1	0.0	0.0	0.0	0.0	0.0
Financial liabilities							
Gross general government debt 4/	23.8	31.1	34.4	38.1	38.1	38.1	37.1
Gross general government debt excl. guarantees	21.7	28.1	32.3	35.8	35.9	36.0	35.2
External	10.0	12.9	15.3	17.3	17.3	17.3	16.5
Domestic	11.7	15.2	16.9	18.5	18.6	18.8	18.7
Memorandum items:							
Total capital spending (excluding PNDI)	5.2	7.2	7.7	6.5	6.2	5.9	6.0
Fiscal balance (ESA95 basis) 5/	-9.0	-6.8	-5.5	-2.9	-2.4	-2.0	-1.8
Structural balance (ESA95 basis) 5/	-9.7	-6.1	-3.9	-2.6	-1.6	-1.2	-1.0
Gross general government debt (ESA95 basis)	23.6	30.5	34.7	37.8	38.6	38.5	38.5
Output gap 6/	-1.2	-3.5	-2.5	-2.9	-2.3	-1.8	-1.3
Cyclically adjusted balance	-6.8	-5.1	-3.3	-1.5	-1.5	-1.4	-1.3
Structural fiscal balance	-6.8	-5.1	-3.0	-1.7	-1.2	-0.9	-1.2
Gross general government debt (authorities definition) 7/	29.4	37.1	40.1	41.0	…	…	…
Nominal GDP (in billions of lei)	501.1	523.7	556.7	587.5	626.2	661.3	700.7

Sources: Ministry of Public Finance; Eurostat; and IMF staff estimates and projections.
1/ Includes EU-financed capital projects.
2/ Does not include all capital spending.
3/ National Program for Infrastructure Development (PNDI).
4/ Total consolidated public debt, including government debt, local government debt, and guarantees.
5/ European Commission estimate.
6/ Percentage deviation of actual from potential GDP.
7/ Includes guarantees and intra-governmental debt.

Table 7. Romania: General Government Operations, 2009–15 (concluded)
(In millions of lei)

	2009	2010	2011	2012	2013 Prog.	2014 Proj	2015 Proj
Revenue	156,373	168,635	181,567	193,148	209,406	218,672	231,784
Taxes	136,350	138,667	155,710	165,702	176,896	182,538	191,714
Corporate income tax	13,466	10,969	11,030	11,826	12,135	12,815	13,579
Personal income tax	18,551	17,957	19,461	20,956	23,159	24,260	25,707
VAT	34,322	39,246	47,917	50,516	53,175	54,114	57,341
Excises	15,646	17,312	19,105	20,260	21,843	23,282	24,671
Customs duties	656	574	674	707	742	792	853
Social security contributions	47,829	45,704	50,637	51,658	54,428	57,709	60,601
Other taxes	5,879	6,905	6,885	9,778	11,413	9,567	8,962
Nontax revenue	14,487	19,796	18,217	18,328	19,039	21,005	22,258
Interest Revenue	864	595	718	279	182	314	333
Capital revenue	546	685	766	653	687	726	769
Grants	5,057	9,494	6,874	8,422	12,785	14,403	17,044
o/w EU pre-accession funds	2,959	4,054	765	443	631	2	176
Financial operations and other	-67	-6	0	43	0	0	0
Expenditure	192,782	202,256	205,277	207,921	224,106	231,897	244,159
Current expenditure	173,445	183,243	182,709	189,274	206,166	219,775	231,320
Compensation of employees	46,676	42,839	38,496	40,799	46,153	47,383	49,757
Goods and services	28,028	29,541	31,643	34,444	39,744	39,925	42,307
Interest	6,063	7,275	8,883	10,710	11,373	12,218	12,591
Subsidies	7,215	6,735	6,407	6,122	5,230	5,803	5,821
Transfers	83,407	95,060	95,172	95,585	102,583	112,846	119,149
Pensions	39,851	42,107	47,469	48,051	49,511	53,076	55,858
Other social transfers	24,101	26,505	20,539	18,997	19,865	20,428	21,020
Other transfers 1/	16,931	23,514	24,049	25,569	30,341	36,395	39,248
Other spending	2,523	2,933	3,115	2,968	2,866	2,947	3,023
Projects with external credits	2,056	1,794	2,108	1,614	1,083	1,600	1,695
Capital expenditure 2/	21,828	19,441	23,056	19,305	17,734	12,015	12,732
Reserve fund	0	0	0	0	207	107	107
Net lending and expense refunds	-2,490	-428	-488	-657	0	0	0
Fiscal balance	-36,409	-33,621	-23,710	-14,774	-14,700	-13,225	-12,375
Primary balance	-30,346	-26,346	-14,827	-4,064	-3,327	-1,007	216
Fiscal balance including PNDI 3/	-36,409	-33,621	-23,837	-14,984	-14,700	-13,225	-12,375
Idem including EU receivables		...	...	-17,431	...	...	...
Financing	36,409	33,621	23,710	14,774	14,700	13,225	12,375
External borrowing (net)	13,144	14,807	15,250	19,271	6,674	5,939	1,657
Domestic borrowing (net)	29,129	20,841	12,377	5,305	7,976	7,237	6,707
Use of deposits	-6,129	-2,161	-3,827	-9,916	0	0	3,960
Privatization proceeds	291	289	0	5	50	50	50
Financial liabilities							
Gross general government debt 4/	119,195	163,022	191,423	224,040	238,690	251,865	260,230
Gross general government debt excl. guarantees	108,528	147,261	179,639	210,254	224,904	238,079	246,444
External	49,993	67,717	85,382	101,476	108,149	114,088	115,745
Domestic	58,535	79,544	94,257	108,778	116,755	123,992	130,699
Memorandum item:							
Gross general government debt (authorities definition) 5/	147,329	194,459	223,268	240,843	...	...	...

Sources: Ministry of Public Finance; Eurostat; and IMF staff estimates and projections.
1/ Includes EU-financed capital projects.
2/ Does not include all capital spending.
3/ National Program for Infrastructure Projects (PNDI).
4/ Total consolidated public debt, including government debt, local government debt, and guarantees.
5/ Includes guarantees and intra-governmental debt.

Table 8. Romania: Monetary Survey, 2009–14

(In millions of lei, unless otherwise indicated; end of period)

	Dec-09	Dec-10	Dec-11	Dec-12	2013				Dec-14
					Q1	Q2	Q3 Proj.	Q4 Proj.	Proj.
					I. Banking System				
Net foreign assets	**17,684**	**19,086**	**15,740**	**30,203**	**43,264**	**44,895**	**44,657**	**49,474**	**55,662**
In millions of euros	4,182	4,454	3,644	6,820	9,799	10,069	10,207	10,872	12,164
o/w commercial banks	-19,708	-21,086	-21,846	-18,594	-16,963	-16,779	-16,575	-17,776	-18,155
Net domestic assets	**171,946**	**183,687**	**200,468**	**191,815**	**182,052**	**182,887**	**187,570**	**187,197**	**194,026**
General government credit, net	26,748	43,140	52,596	49,599	41,131	38,350	42,963	47,576	52,812
Private sector credit	199,887	209,294	223,037	225,836	223,943	224,159	223,700	223,242	229,335
Other	-54,688	-68,747	-75,165	-83,621	-83,021	-79,622	-79,093	-83,621	-88,121
Broad Money (M3)	**189,630**	**202,773**	**216,208**	**222,018**	**225,317**	**227,782**	**232,227**	**236,671**	**249,688**
Money market instruments	1,617	3,201	4,149	188	206	202	202	201	212
Intermediate money (M2)	188,013	199,572	212,059	221,830	225,111	227,580	232,025	236,470	249,476
Narrow money (M1)	79,361	81,592	85,834	89,020	88,787	93,138	92,760	93,406	98,543
Currency in circulation	23,968	26,794	30,610	31,477	31,693	33,261	32,866	32,471	34,257
Overnight deposits	55,394	54,799	55,224	57,543	57,094	59,877	59,895	60,935	64,286
					II. National Bank of Romania				
Net foreign assets	**101,015**	**109,433**	**110,106**	**112,552**	**118,161**	**119,710**	**121,492**	**130,361**	**138,733**
In millions of euros	23,891	25,540	25,489	25,414	26,761	26,848	26,782	28,648	30,319
Net domestic assets	**-49,354**	**-54,330**	**-48,541**	**-55,244**	**-61,906**	**-64,309**	**-64,233**	**-71,244**	**-76,364**
General government credit, net	-13,626	-12,795	-13,564	-24,973	-27,886	-32,065	-29,230	-32,572	-33,048
Credit to banks, net	-23,848	-26,148	-19,529	-14,443	-20,493	-23,268	-23,722	-25,176	-27,561
Other	-11,880	-15,387	-15,448	-15,828	-13,527	-8,975	-11,280	-13,495	-15,755
Reserve money	**51,662**	**55,103**	**61,565**	**57,308**	**56,255**	**55,401**	**57,259**	**59,118**	**62,369**
					(Annual percent change)				
Broad money (M3)	9.0	6.9	6.6	2.7	4.2	5.0	5.1	6.6	5.5
NFA contribution	2.6	0.7	-1.7	6.7	9.2	11.3	7.5	8.7	2.6
NDA contribution	6.4	6.2	8.3	-4.0	-5.0	-6.3	-2.4	-2.1	2.9
Reserve money	2.4	6.7	11.7	-6.9	5.2	-5.6	-4.6	3.2	5.5
NFA contribution	-18.4	16.3	1.2	4.0	3.3	12.1	2.2	31.1	14.2
NDA contribution	20.8	-9.6	10.5	-10.9	1.9	-17.6	-6.8	-27.9	-8.7
Domestic credit, real	5.6	3.2	5.9	-4.8	-6.7	-10.7	-7.4	-4.8	1.2
Private sector, real	-3.6	-3.0	3.3	-3.5	-5.2	-6.3	-6.0	-4.3	-0.3
Public sector, real	268.9	49.4	18.2	-10.1	-14.2	-29.9	-18.7	-7.1	7.8
Broad money (M3), in real terms	4.0	-1.0	3.4	-2.2	-1.0	-0.3	1.9	3.2	2.4
Private credit, nominal	0.9	4.7	6.6	1.3	-0.2	-1.3	-3.1	-1.1	2.7
Memorandum items:									
CPI inflation, eop	4.7	8.0	3.1	5.0	5.3	5.4	5.3	3.3	3.0
Inflation target	2.5 - 4.5	2.5 - 4.5	2.0 - 4.0	2.0 - 4.0	1.5 - 3.5	1.5 - 3.5	1.5 - 3.5	1.5 - 3.5	1.5 - 3.5
Interest rates (percent)									
Policy interest rate	8.00	6.25	6.0	5.25	5.25	5.25	...	...	...
Interbank offer rate, 1 week	10.7	3.6	6.0	5.9	4.7	4.0	...	...	
Corporate loans 1/	15.4	9.4	9.7	9.8	9.3	...	...	...	...
Household time deposits 1/	9.9	7.6	6.6	5.6	5.5	...	...	...	...
Share of foreign currency private deposits	39.3	36.1	33.6	36.7	36.8	...	...	...	...
Share of foreign currency private loans	60.1	63.0	63.4	62.5	62.4	...	...	...	...
M2 velocity	2.67	2.62	2.63	2.81	4.00	4.00	3.47	2.65	2.65
Money multiplier (M3/reserve money)	3.67	3.68	3.51	3.87	4.01	4.11	4.06	4.00	4.00

Sources: National Bank of Romania; and IMF staff estimates and projections.

1/ Rates for new local currency denominated transactions.

2/ For interest rates and shares of foreign currency loans and deposits, latest available data.

Table 9. Romania: Financial Soundness Indicators, 2008–13
(In percent)

	2008 Dec.	2009 Dec.	2010 Dec.	2011 Dec.	2012 Dec.	2013 Mar.	2013 Jun.
Core indicators							
Capital adequacy							
Capital to risk-weighted assets	13.8	14.7	15.0	14.9	14.9	15.0	14.7
Tier 1 capital to risk-weighted assets	11.8	13.4	14.2	13.9	13.8	13.9	13.6
Asset quality							
Nonperforming loans (1/) to total gross loans	2.8	7.9	11.9	14.3	18.2	19.1	20.3
Earnings and profitability							
Return on assets	1.6	0.2	-0.2	-0.2	-0.6	0.5	0.7
Return on equity(2/)	17.0	2.9	-1.7	-1.4	-5.9	5.1	6.0
Net interest income to operating income	44.8	44.1	60.6	61.9	62.3	58.0	59.2
Noninterest expense to operating income (cost to income)	55.7	63.9	64.9	68.2	58.7	55.4	57.3
Personnel expense to operating income	23.4	20.3	21.0	22.1	26.0	25.9	26.6
Liquidity							
Liquid assets (3/)to total assets	47.1	57.4	60.0	58.6	57.6	58.7	58.3
Liquid assets (3/) to short-term liabilities (4/)	230.5	132.0	142.2	138.8	147.7	153.3	155.2
Liquid assets (3/) to total attracted and borrowed sources	116.2	79.4	80.9	79.7	76.4	78.2	77.2
Foreign exchange risk							
Net open position in foreign exchange, in percent of capital	1.6	2.3	-1.4	-4.8	-1.8	-1.0	-1.1
Lending in foreign exchange, in percent of non-gov. credit	57.8	60.1	63.0	63.4	62.5	62.4	62.4
Foreign currency liabilities, in percent of total attracted and borrowed sources	43.7	42.8	43.5	43.1	46.3	46.9	47.5
Deposits in foreign exchange, in percent of non-gov. dom. deposits	34.8	38.8	36.0	33.5	36.4	36.5	36.2
Encouraged indicators							
Deposit-taking institutions							
Leverage ratio (5/)	8.1	7.6	8.1	7.9	8.0	8.2	8.0
Personnel expenses to noninterest expenses	41.9	31.8	32.3	32.3	44.3	46.8	46.4
Loan to Deposit (LTD) Ratio	122.0	112.8	117.9	119.1	114.5	111.5	110.9

Structural indicators:
Number of banks (March 2013): 41; Number of foreign-owned subsidiaries/branches (March 2013): 25 (9); Share of deposits/loans of 5 largest banks (March 2013): 61.4 percent (54.6 percent)

Source: National Bank of Romania.

1/ The NPLs represent un-adjusted exposures of loans and related interests overdue for more than 90 days and/or for which legal proceedings were initiated.

2/ Return on equity is calculated as Net profit/loss to average own capital.

3/ Liquid assets = balance sheet assets and off balance sheets items with residual maturity of up to 3 months.

4/ Short term liabilities =balance sheet liabilities and off balance sheet items with residual maturity of up to 3 months.

5/ Tier 1 capital to average assets.

Table 10. Romania: Schedule of Reviews and Purchases

Date	Amount of Purchase: Millions of SDRs	Amount of Purchase: Percent of Quota	Conditions
September 27, 2013	194.70	18.9	Approval of arrangement
December 20, 2013	194.70	18.9	First review and end-September 2013 performance criteria
March 28, 2014	194.70	18.9	Second review and end-December 2013 performance criteria
June 28, 2014	194.70	18.9	Third review and end-March 2014 performance criteria
September 28, 2014	194.70	18.9	End-June 2014 performance criteria
December 28, 2014	194.70	18.9	Fourth review and end-September 2014 performance criteria
March 28, 2015	194.70	18.9	End-December 2014 performance criteria
June 28, 2015	194.70	18.9	Fifth review and end-March 2015 performance criteria
September 22, 2015	193.74	18.8	End-June 2015 performance criteria
Total	1,751.34	170.0	

Source: IMF staff estimates.

Table 11. Romania: Indicators of Fund Credit, 2013–18 1/

(In millions of SDR)

	2013	2014	2015	2016	2017	2018
Existing Fund Credit						
Stock 2/	5,210.0	1,328.9	96.1	0.0	0.0	0.0
Obligations 3/	1,729.9	3,921.4	1,241.5	97.1	0.8	0.8
Repurchase	1,711.6	3,881.1	1,232.8	96.1	0.0	0.0
Charges	18.2	40.3	8.8	1.0	0.8	0.8
Prospective Fund Credit under Stand-By Arrangement						
Disbursement	389.4	778.8	583.1	0.0	0.0	0.0
Stock 2/	389.4	1,168.2	1,751.3	1,727.0	1,386.3	680.6
Obligations 3/	2.2	10.0	17.4	43.3	358.7	719.0
Repurchase	0.0	0.0	0.0	24.3	340.7	705.7
Charges	2.2	10.0	17.4	18.9	18.0	13.4
Stock of existing and prospective Fund credit						
In millions of SDR	5,599	2,497	1,847	1,727	1,386	681
In percent of quota	544	242	179	168	135	66
In percent of GDP	4.6	2.0	1.4	1.2	0.9	0.4
In percent of exports of goods and services	11.5	4.9	3.4	2.9	2.2	1.0
In percent of gross reserves	18.9	9.1	6.9	6.0	4.5	2.1
Obligations to the Fund from existing and prospective Fund arrangements						
In millions of SDR	1,759	3,967	1,259	140	359	720
In percent of quota	170.8	385.0	122.2	13.6	34.9	69.9
In percent of GDP	1.4	3.1	0.9	0.1	0.2	0.4
In percent of exports of goods and services	3.6	7.7	2.3	0.2	0.6	1.0
In percent of gross reserves	5.9	14.4	4.7	0.5	1.2	2.2

Source: IMF staff estimates.

1/ Using IMF actual disbursements, SDR interest rate as well as exchange rate of SDR/US$ and US$/€ of August 22, 2013.

2/ End of period.

3/ Repayment schedule based on repurchase obligations.

Table 12. Romania: Public Sector Debt Sustainability Framework, 2008-2018

(In percent of GDP, unless otherwise indicated)

	Actual					Projections						
	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	**Debt-stabilizing primary balance 9/**
1 **Baseline: Public sector debt 1/**	13.6	23.8	31.1	34.4	38.1	**38.1**	**38.1**	**37.1**	**36.9**	**36.5**	**36.2**	**-0.4**
o/w foreign-currency denominated	8.6	15.3	20.0	20.5	22.6	21.8	20.7	19.2	18.0	16.8	15.6	
2 Change in public sector debt	0.9	10.1	7.3	3.3	3.7	0.0	0.0	-0.9	-0.3	-0.4	-0.3	
3 Identified debt-creating flows (4+7+12)	3.6	8.0	6.8	3.2	0.8	0.0	0.0	-0.4	-0.3	-0.4	-0.3	
4 Primary deficit	4.1	6.1	5.0	2.7	0.7	0.5	0.2	0.0	0.1	-0.1	0.0	
5 Revenue and grants	32.2	31.2	32.2	32.6	32.9	33.4	33.1	33.1	33.0	32.8	32.6	
6 Primary (noninterest) expenditure	36.3	37.3	37.2	35.3	33.6	34.0	33.2	33.0	33.2	32.7	32.5	
7 Automatic debt dynamics 2/	-0.6	1.9	1.7	0.5	0.1	-0.5	-0.2	-0.3	-0.4	-0.3	-0.3	
8 Contribution from interest rate/growth differential 3/	-1.7	1.6	0.4	-0.3	0.0	-0.5	-0.2	-0.3	-0.4	-0.3	-0.3	
9 Of which contribution from real interest rate	-1.0	0.7	0.1	0.4	0.3	0.2	0.6	0.6	0.6	0.9	0.9	
10 Of which contribution from real GDP growth	-0.8	0.9	0.3	-0.6	-0.2	-0.7	-0.8	-0.9	-1.0	-1.2	-1.2	
11 Contribution from exchange rate depreciation 4/	1.2	0.3	1.3	0.8	0.1	...	...	...	...	...	...	
12 Other identified debt-creating flows	0.1	0.1	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
13 Privatization receipts (negative)	0.1	0.1	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
14 Recognition of implicit or contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
15 Other (specify, e.g. bank recapitalization)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
16 Residual, including asset changes (2-3) 5/	-2.7	2.1	0.6	0.1	2.9	0.0	0.0	-0.6	0.0	0.0	0.0	
Public sector debt-to-revenue ratio 1/	42.4	76.2	96.7	105.4	116.0	114.0	115.2	112.3	111.6	111.4	111.1	
Gross financing need 6/	6.7	18.4	13.9	13.0	11.6	11.2	10.7	10.1	7.8	7.4	7.1	
in billions of U.S. dollars	13.6	30.2	22.8	23.8	19.6	20.6	20.2	20.3	16.5	16.8	17.3	
Scenario with key variables at their historical averages 7/						**38.1**	**37.7**	**36.7**	**36.4**	**36.1**	**35.9**	**-2.7**
Scenario with no policy change (constant primary balance) in 2013-2018						**38.1**	**38.4**	**38.1**	**38.2**	**38.4**	**38.6**	**-0.4**
Key Macroeconomic and Fiscal Assumptions Underlying Baseline												
Real GDP growth (in percent)	7.3	-6.6	-1.1	2.2	0.7	2.0	2.2	2.5	2.9	3.4	3.5	
Average nominal interest rate on public debt (in percent) 8/	7.1	8.6	6.1	5.4	5.6	5.1	5.1	5.0	4.8	5.4	5.5	
Average real interest rate (nominal rate minus change in GDP deflator, in percent)	-8.2	4.4	0.4	1.4	0.8	0.6	1.7	1.7	1.9	2.6	2.8	
Nominal appreciation (increase in US dollar value of local currency, in percent)	-13.3	-3.5	-8.4	-4.0	-0.5	...	...	...	...	...	...	
Inflation rate (GDP deflator, in percent)	15.3	4.2	5.7	4.1	4.8	4.5	3.4	3.3	2.9	2.7	2.7	
Growth of real primary spending (deflated by GDP deflator, in percent)	12.4	-4.0	-1.2	-3.2	-4.1	3.2	-0.1	2.0	3.3	2.1	2.9	
Primary deficit	4.1	6.1	5.0	2.7	0.7	0.5	0.2	0.0	0.1	-0.1	0.0	

1/ Coverage: general government gross debt, including guarantees.

2/ Derived as [(r - p(1+g) - g + ae(1+r)]/(1+g+p+gp)) times previous period debt ratio, with r = interest rate; p = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

3/ The real interest rate contribution is derived from the denominator in footnote 2/ as r - π (1+g) and the real growth contribution as -g.

4/ The exchange rate contribution is derived from the numerator in footnote 2/ as ae(1+r).

5/ For projections, this line includes exchange rate changes.

6/ Defined as public sector deficit, plus amortization of medium and long-term public sector debt, plus short-term debt at end of previous period.

7/ The key variables include real GDP growth; real interest rate; and primary balance in percent of GDP.

8/ Derived as nominal interest expenditure divided by previous period debt stock.

9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Table 13. Romania: External Debt Sustainability Framework, 2008-2018

(In percent of GDP, unless otherwise indicated)

	Actual							Projections						
	2008	2009	2010	2011	2012			2013	2014	2015	2016	2017	2018	Debt-stabilizing non-interest current account 6/
1 **Baseline: External debt**	51.8	68.7	74.3	75.2	75.1			**71.3**	**70.4**	**67.6**	**65.0**	**62.9**	**60.0**	**-5.9**
2 Change in external debt	4.7	16.9	5.7	0.8	-0.1			-3.7	-1.0	-2.8	-2.6	-2.1	-2.9	
3 Identified external debt-creating flows (4+8+9)	0.4	10.2	-1.5	-2.1	-0.4			-3.6	-1.3	-0.4	-1.5	-2.2	-1.9	
4 Current account deficit, excluding interest payments	9.2	1.8	2.0	1.8	1.4			0.1	0.7	1.2	1.5	1.8	2.2	
5 Deficit in balance of goods and services	13.2	6.1	5.8	5.4	5.2			2.5	2.9	2.9	3.0	3.0	3.2	
6 Exports	30.4	30.6	35.4	40.0	40.0			40.1	40.8	41.2	41.4	42.0	42.5	
7 Imports	43.6	36.6	41.1	45.4	45.1			42.6	43.7	44.0	44.4	45.0	45.7	
8 Net non-debt creating capital inflows (negative)	-6.0	-3.4	-2.5	-2.6	-4.0			-4.1	-2.3	-1.4	-2.5	-3.3	-3.2	
9 Automatic debt dynamics 1/	-2.8	11.8	-1.0	-1.2	2.2			0.4	0.2	-0.2	-0.4	-0.8	-0.8	
10 Contribution from nominal interest rate	2.3	2.4	2.4	2.7	2.5			1.8	1.7	1.5	1.4	1.3	1.2	
11 Contribution from real GDP growth	-3.1	4.0	0.8	-1.5	-0.5			-1.4	-1.5	-1.7	-1.9	-2.1	-2.1	
12 Contribution from price and exchange rate changes 2/	-2.0	5.4	-4.1	-2.4	0.3			...	...	...	...	...	...	
13 Residual, incl. change in gross foreign assets (2-3) 3/	4.3	6.7	7.1	2.9	0.3			-0.2	0.3	-2.4	-1.1	0.2	-1.0	
External debt-to-exports ratio (in percent)	170.3	224.7	210.2	187.9	187.8			178.0	172.3	164.1	157.0	149.9	141.2	
Gross external financing need (in billions of Euros) 4/	46.2	34.9	32.2	38.2	43.2			39.2	39.9	36.6	36.9	37.8	38.9	
in percent of GDP	33.1	29.5	25.9	29.1	32.8			28.0	27.6	23.9	22.7	21.8	21.0	
Scenario with key variables at their historical averages 5/								**71.3**	**68.4**	**64.3**	**61.6**	**60.0**	**57.5**	**-8.6**
Key Macroeconomic Assumptions Underlying Baseline						10-Year Historical Average	10-Year Standard Deviation							
Real GDP growth (in percent)	7.3	-6.6	-1.1	2.2	0.7	3.5	4.7	2.0	2.2	2.5	2.9	3.4	3.5	
GDP deflator in Euros (change in percent)	4.5	-9.4	6.4	3.4	-0.4	7.3	10.1	4.3	1.1	3.0	3.1	3.3	3.3	
Nominal external interest rate (in percent)	5.5	3.9	3.7	3.9	3.3	4.5	0.8	2.6	2.5	2.3	2.2	2.2	2.1	
Growth of exports (Euro terms, in percent)	16.6	-14.9	21.7	19.4	0.3	12.5	11.8	6.7	5.3	6.5	6.6	8.4	8.3	
Growth of imports (Euro terms, in percent)	13.2	-28.9	18.1	16.5	-0.1	13.0	16.8	0.3	6.1	6.3	6.9	8.4	8.7	
Current account balance, excluding interest payments	-9.2	-1.8	-2.0	-1.8	-1.4	-5.5	3.7	-0.1	-0.7	-1.2	-1.5	-1.8	-2.2	
Net non-debt creating capital inflows	6.0	3.4	2.5	2.6	4.0	5.3	2.2	4.1	2.3	1.4	2.5	3.3	3.2	

1/ Derived as [r - g - r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock, with r = nominal effective interest rate on external debt; r = change in domestic GDP deflator in Euro terms, g = real GDP growth rate, e = nominal appreciation (increase in Euro value of domestic currency), and a = share of domestic-currency denominated debt in total external debt.

2/ The contribution from price and exchange rate changes is defined as [-r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock. r increases with an appreciating domestic currency (e > 0) and rising inflation (based on GDP deflator).

3/ For projection, line includes the impact of price and exchange rate changes.

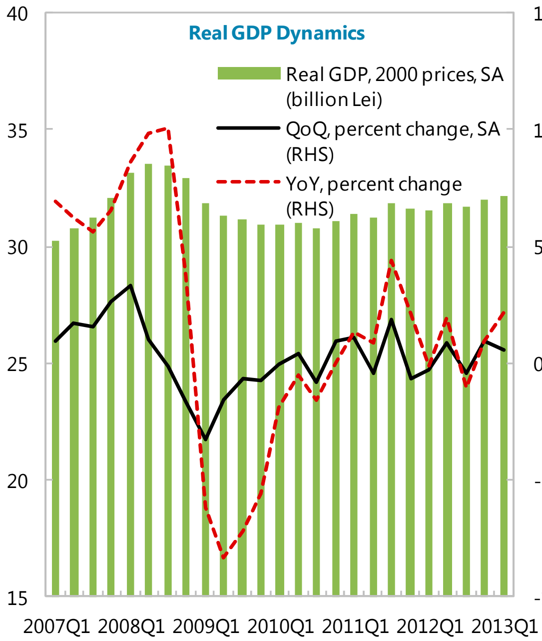
4/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

5/ The key variables include real GDP growth; nominal interest rate; Euro deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.

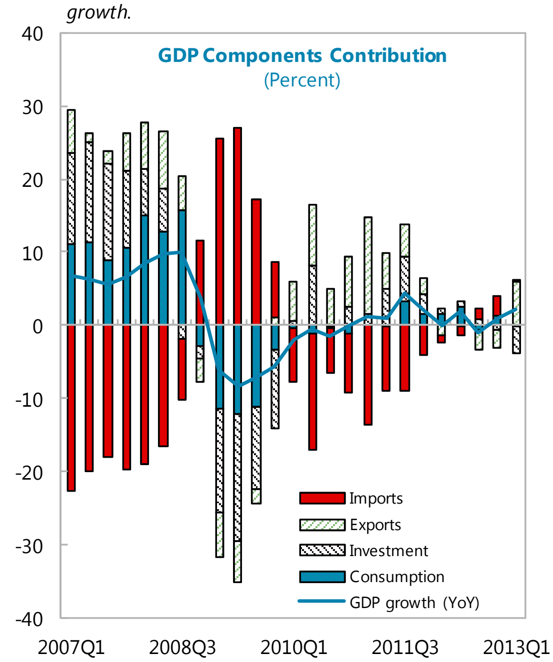
6/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, Euro deflator growth, and non-debt inflows in percent of GDP) remain at their levels of the last projection year.

Figure 1. Romania: Real Sector, 2007–13

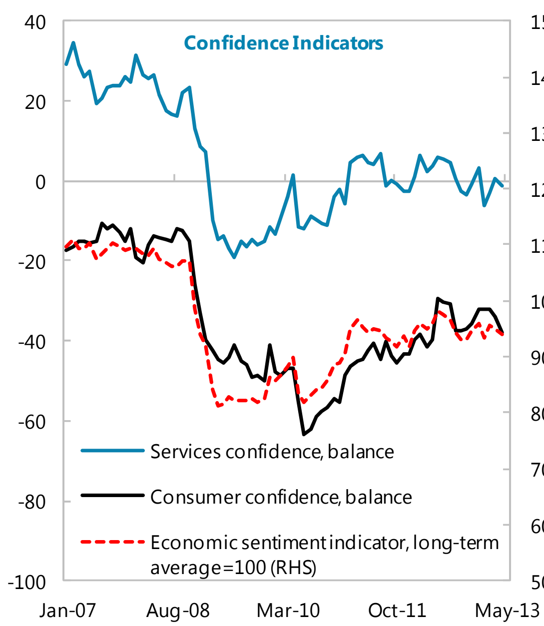
Real GDP has yet to return to pre-crisis levels...



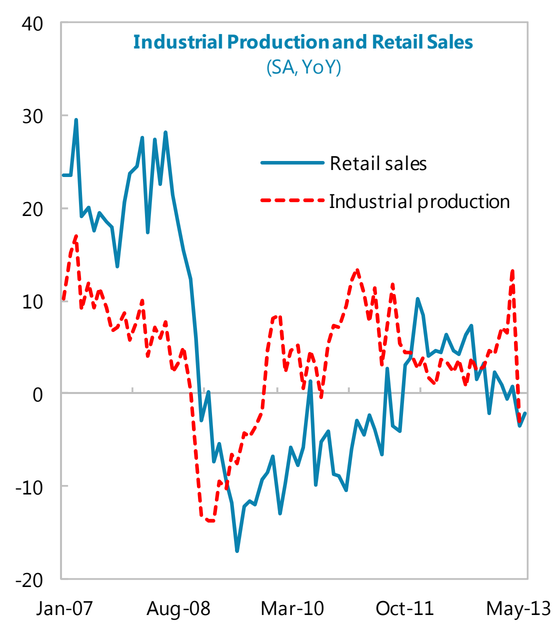
...as weak internal and external demand dampen growth.



Flat confidence indicators suggest a wait and see attitude by consumers...

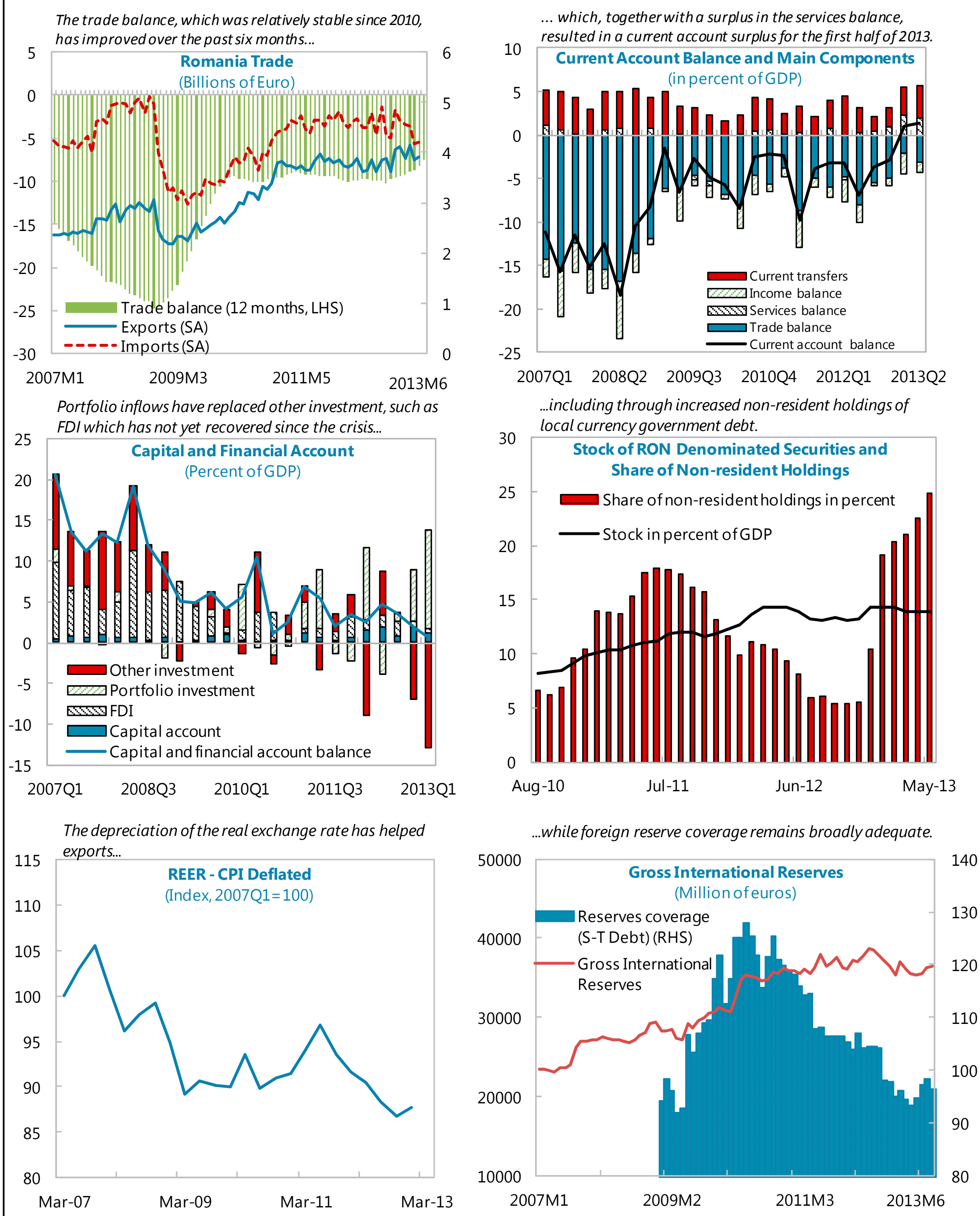


...though the recent pick up in IP suggests the economy may be slowly gaining speed.



Source: Haver.

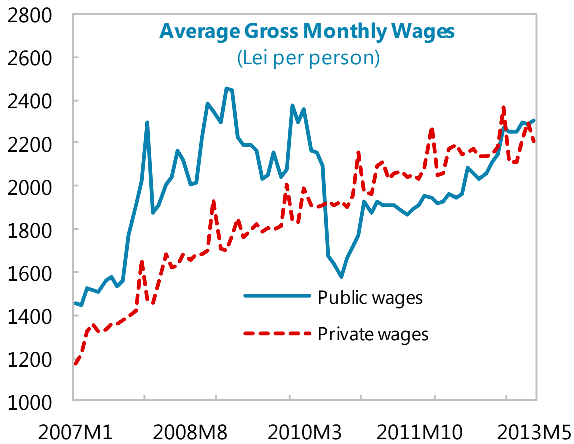
Figure 2. Romania: External Sector, 2007–13



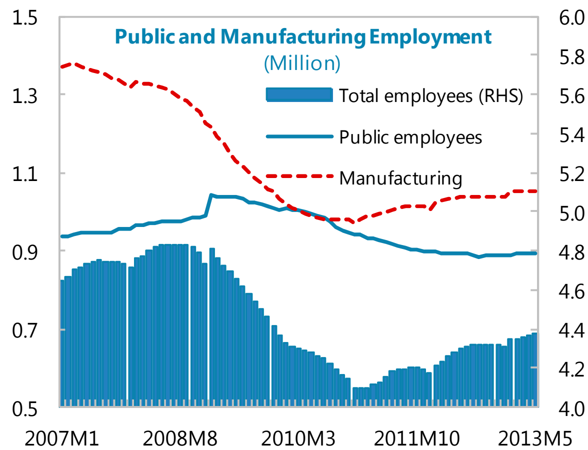
Sources: Haver; and National Bank of Romania.

Figure 3. Romania: Labor Market, 2007–13

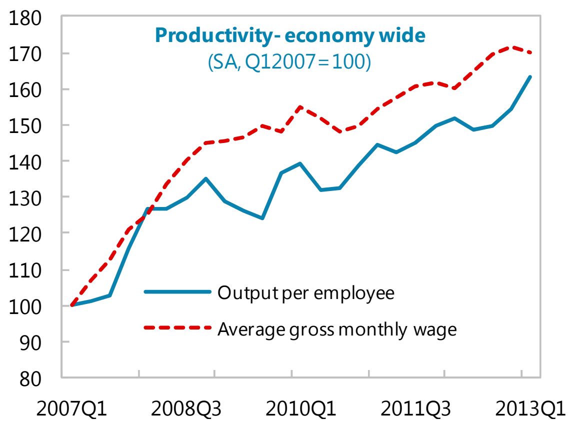
Public salaries, which were cut during the crisis, have been restored...



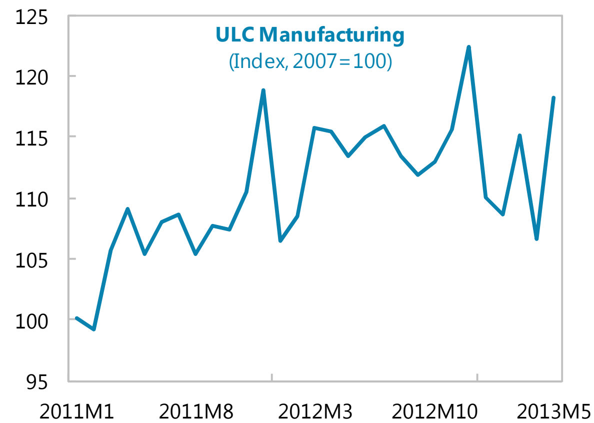
...while, public employment remains well below pre-crisis levels.



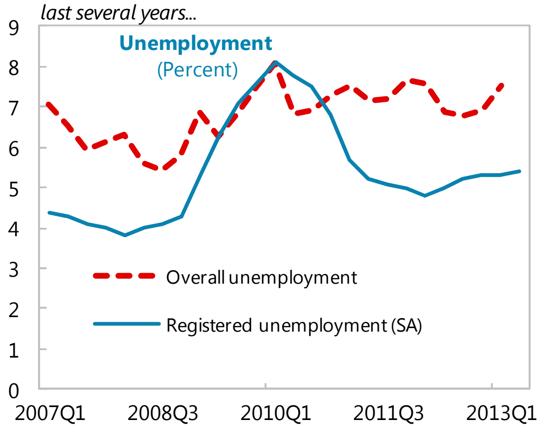
Economy-wide productivity gains have mirrored wage increases since end-2008...



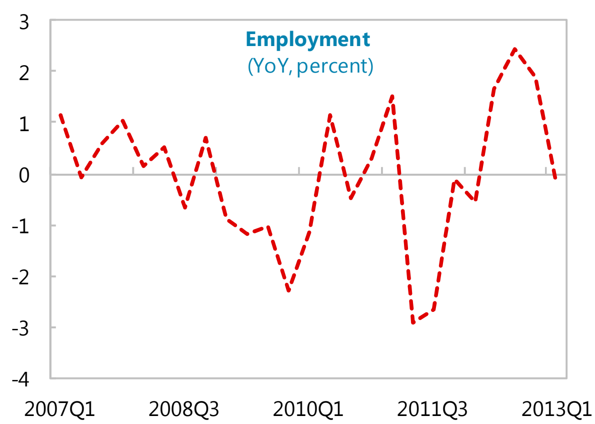
...but unit labor costs in the manufacturing sector increased somewhat in 2012.



Overall unemployment remains little changed over the last several years...



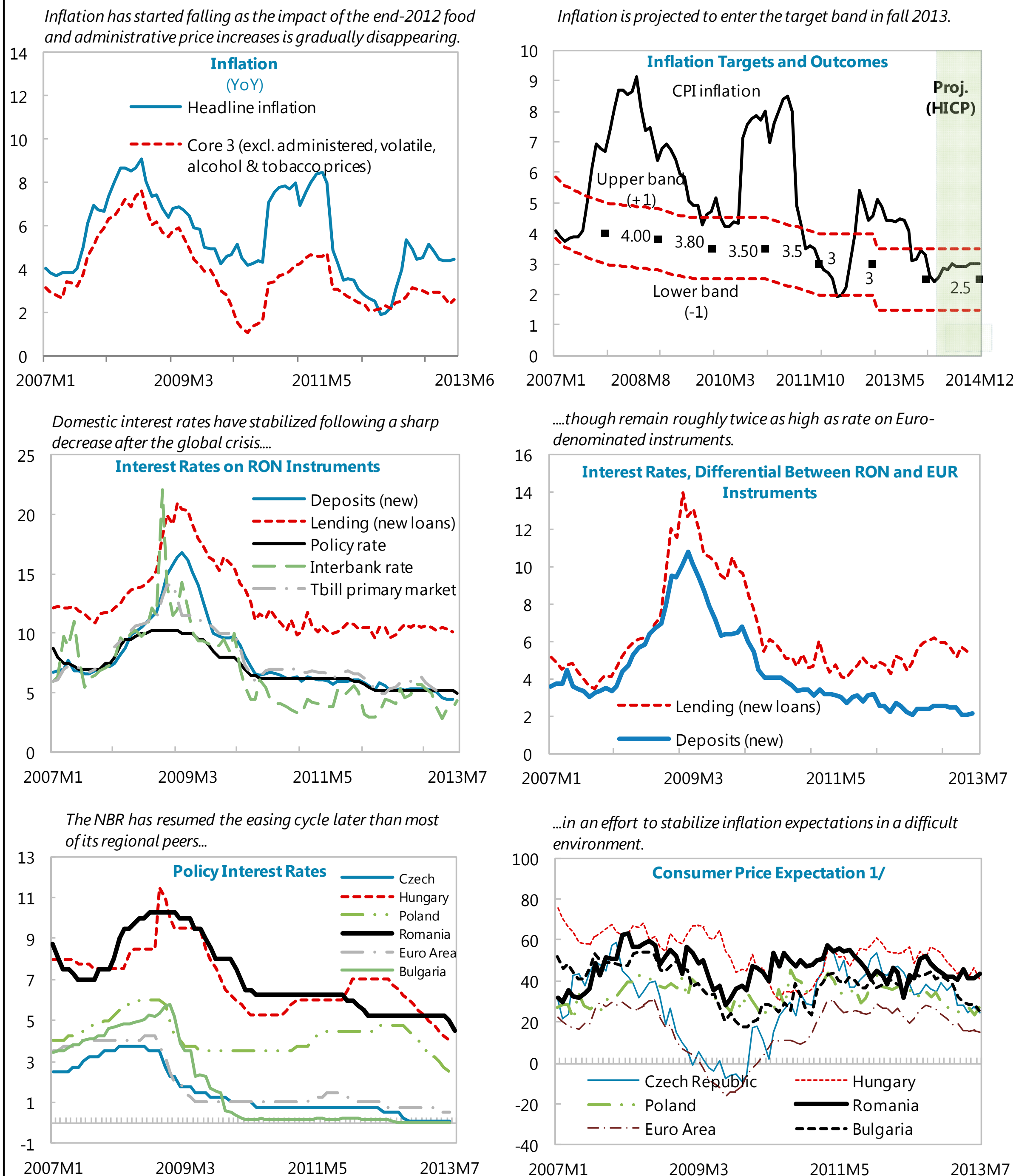
...and employment does not show a clear recovery trend.



Sources: Eurostat; and Haver.

Figure 4. Romania: Monetary Sector, 2007–13

(Percent)

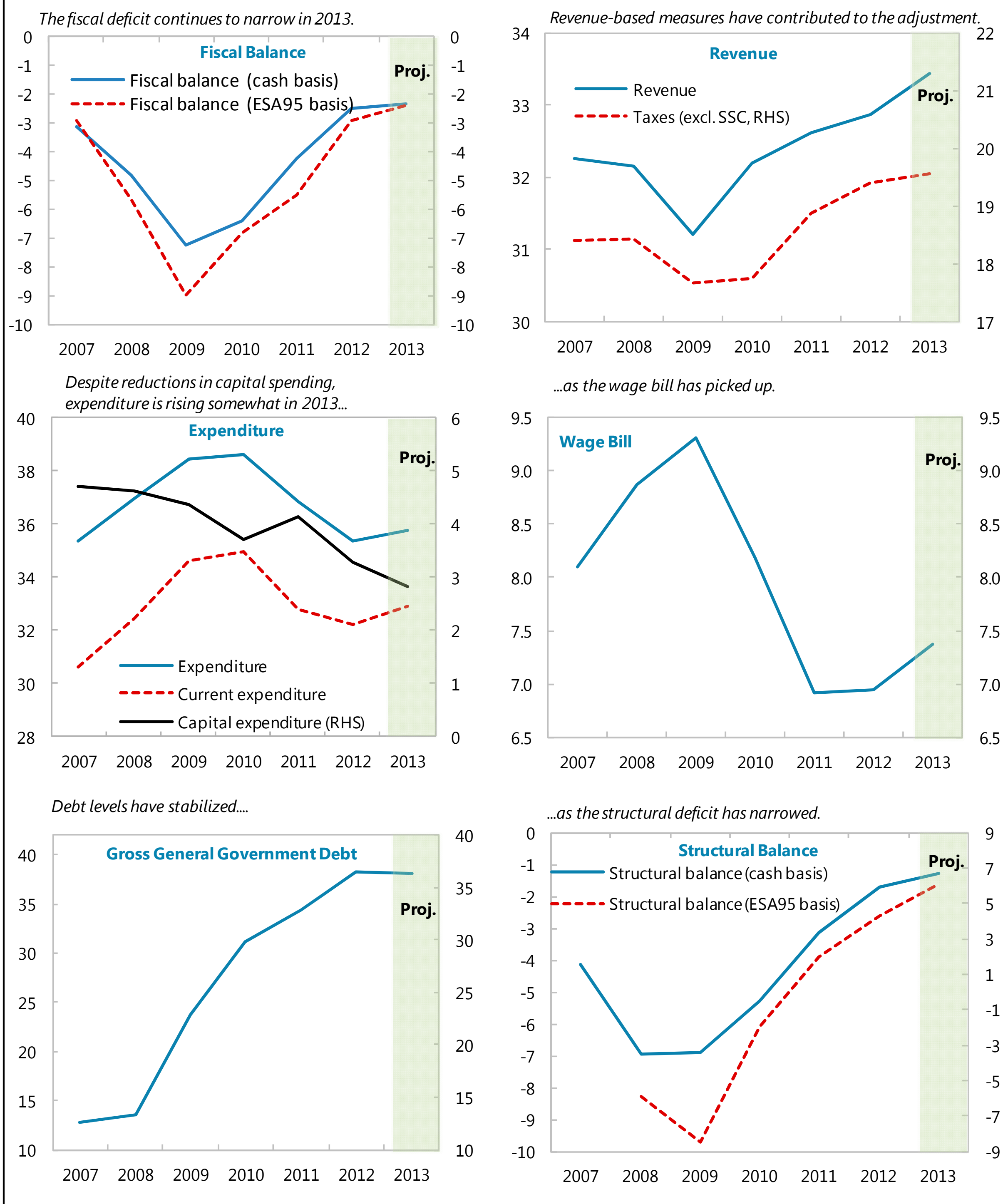


Sources: Haver; National Bank of Romania; Consensus Forecast; and IMF staff estimates.

1/ Value equals percent of respondents reporting an increase minus the percent of respondents reporting a decrease.

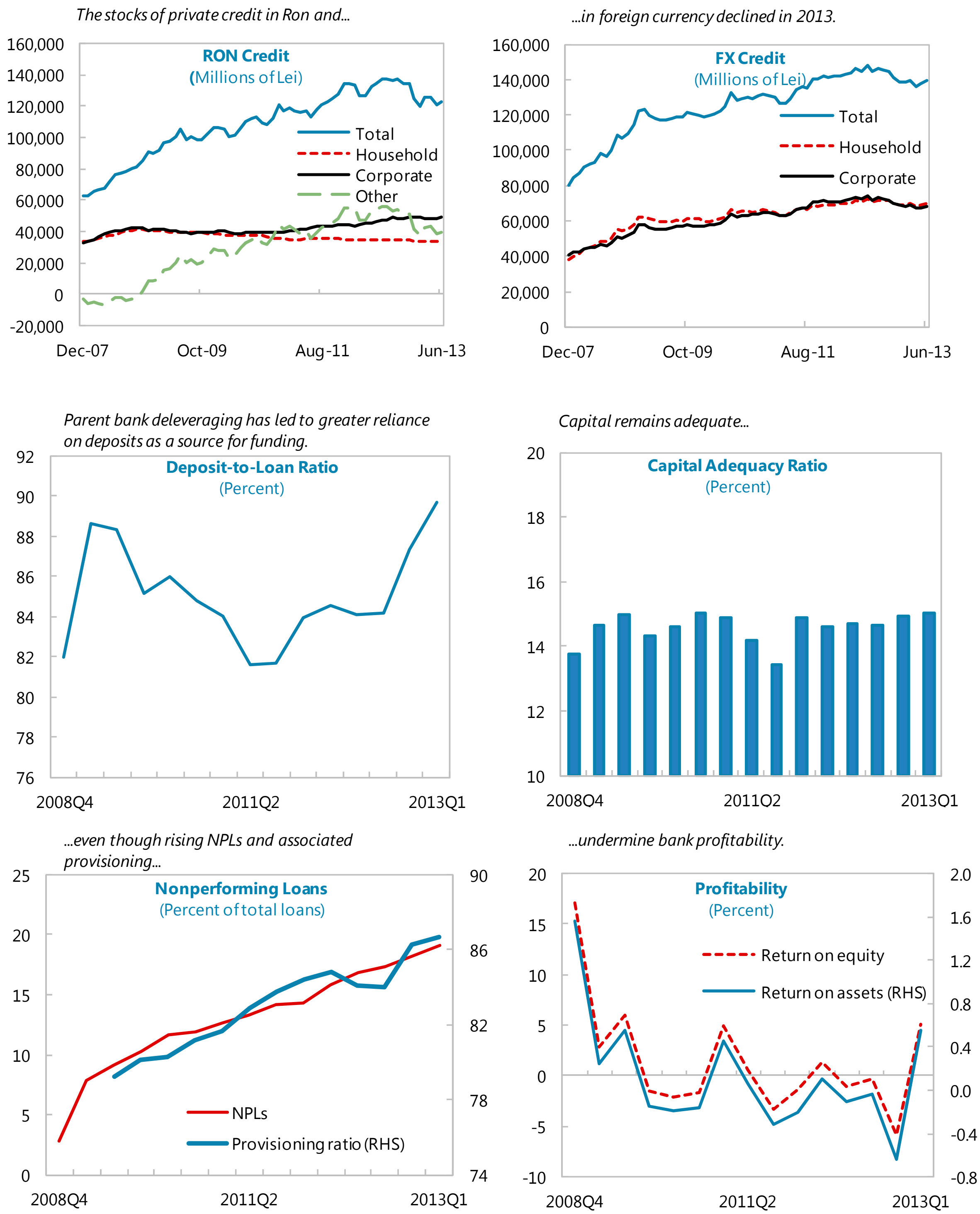
Figure 5. Romania: Fiscal Operations, 2007–13

(Percent of GDP)



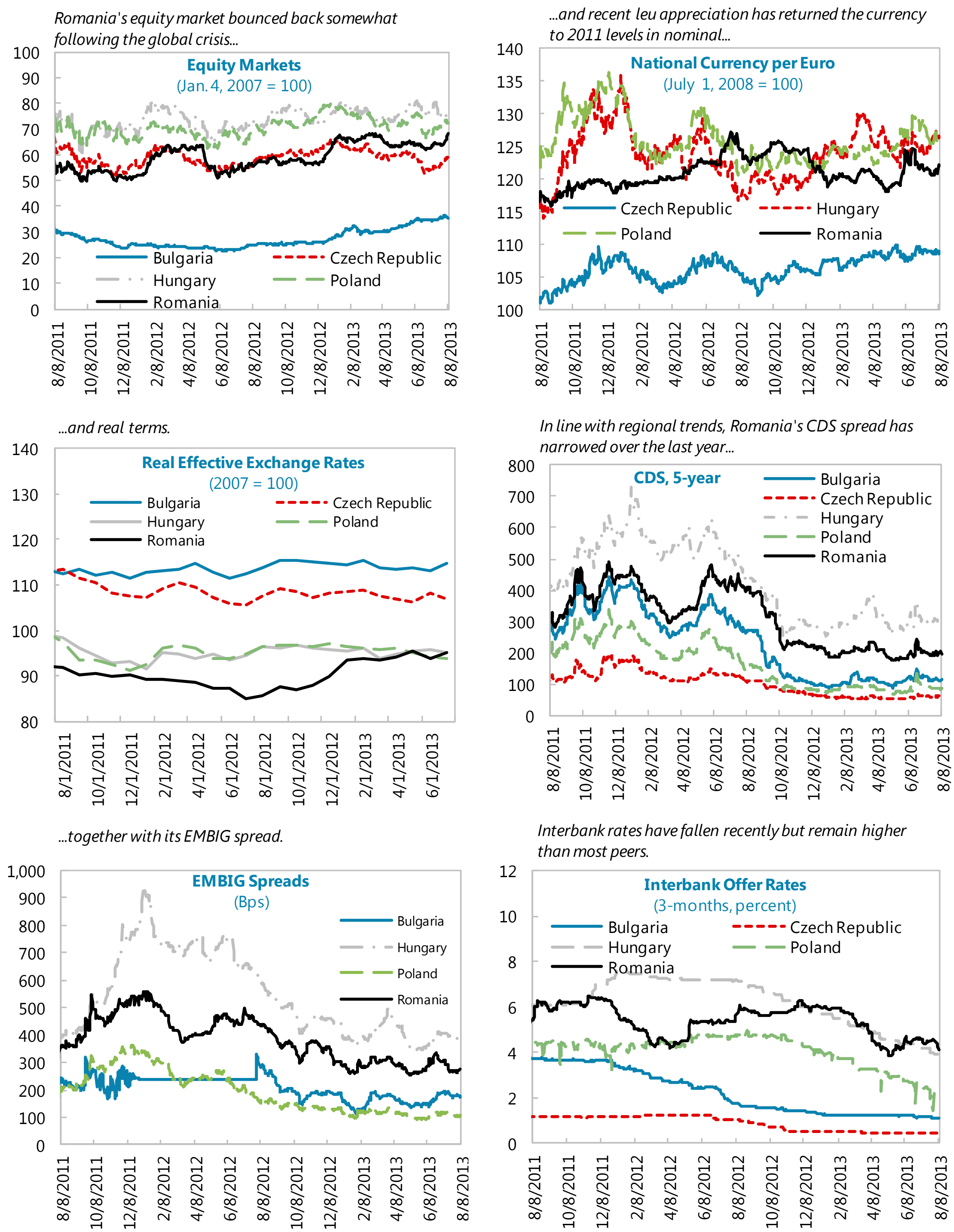
Sources: Romanian authorities; and IMF staff estimates and projections.

Figure 6. Romania: Financial Sector, 2007–13



Sources: Dxtime; and National Bank of Romania.

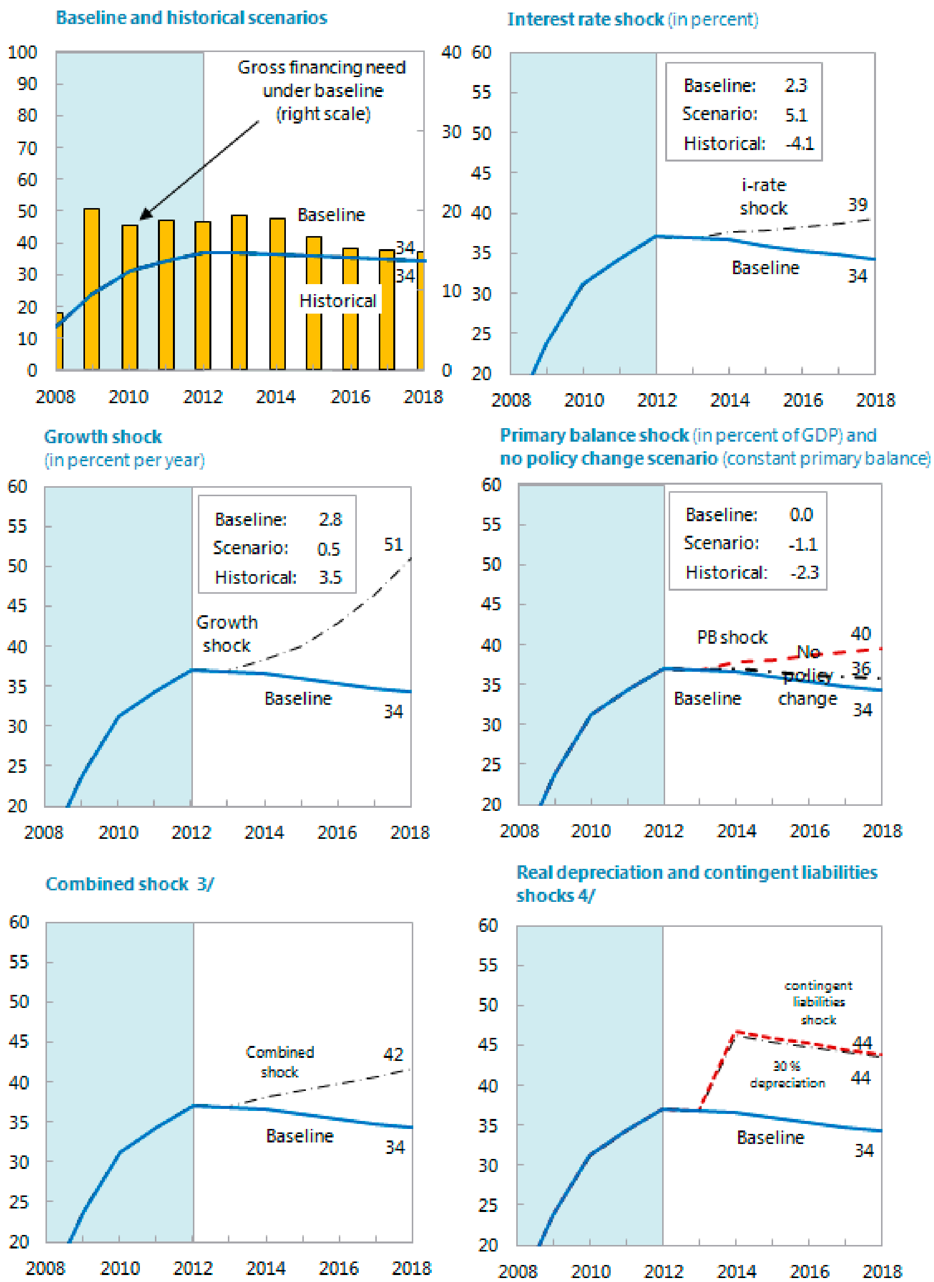
Figure 7. Romania: Financial Developments, 2011-13



Sources: Bloomberg; and Haver.

Figure 8. Romania: Public Debt Sustainability: Bound Tests 1/ 2/

(Public debt in percent of GDP)



Sources: International Monetary Fund, country desk data, and staff estimates.

1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.

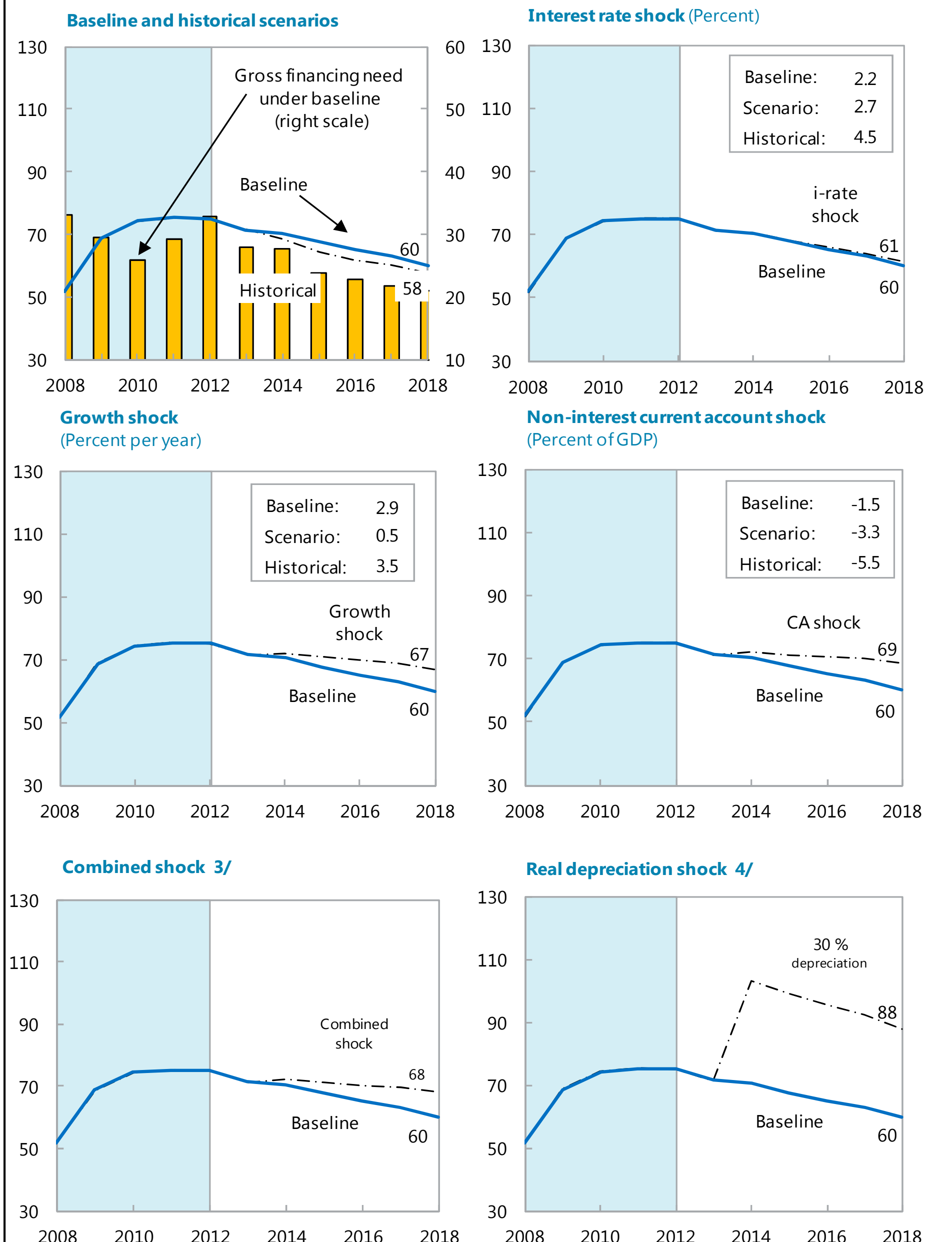
2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.

3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and primary balance.

4/ One-time real depreciation of 30 percent and 10 percent of GDP shock to contingent liabilities occur in 2013 with real depreciation defined as nominal depreciation (measured by percentage fall in dollar value of local currency) minus domestic inflation (based on GDP deflator).

Figure 9. Romania: External Debt Sustainability: Bound Tests 1/ 2/

(External debt in percent of GDP)



Sources: International Monetary Fund, Country desk data, and staff estimates.

1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.

2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.

3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.

4/ One-time real depreciation of 30 percent occurs in 2013.

Appendix I. Romania: Letter of Intent

Bucharest, September 12, 2013

Mme. Christine Lagarde
Managing Director
International Monetary Fund
Washington, DC 20431
U.S.A.

Dear Mme. Lagarde:

1. Under two consecutive economic programs supported by the International Monetary Fund (IMF), the European Union (EU), and the World Bank (WB) we have made significant progress in reducing macroeconomic imbalances and rebuilding fiscal and financial buffers. However, structural reforms in key areas are ongoing and Romania remains vulnerable to external shocks and turmoil in international capital markets. We therefore request approval of a new 24-month Stand-By Arrangement (SBA) totaling SDR 1,751.34 million (about €2 billion, 170 percent of quota), which we intend to treat as precautionary. The new SBA will support our comprehensive economic program for 2013–15 to maintain sound macroeconomic policies and financial sector stability, and continue structural reforms in an environment of significant external uncertainties. In conjunction with precautionary financial assistance of €2 billion under the EU's balance of payments facility and €1 billion under a Development Policy Loan (DPL DDO) provided by the WB, this arrangement will signal the international community's continued support for our policies and provide a buffer against external shocks.

2. The program will be monitored through quantitative performance criteria and indicative targets, structural benchmarks and consultation clauses, during quarterly reviews in the first year and semi-annual reviews afterwards. Table 1 in the attached Memorandum of Economic and Financial Policies (MEFP) sets out specific quarterly targets that are to be observed under the SBA for the general government overall balance, the change in arrears for the central government and social security, CPI inflation, and net international reserves, as well as for the issuance of new government guarantees on behalf of the nonfinancial private sector and public enterprises. In addition, there will be indicative targets on the current primary expenditure of the general government, net of disbursements of pre- and post-accession EU structural funds, arrears of state-owned enterprises

(SOEs) under the control of the central government, the operating balance of key SOEs, local government arrears, and net lending to beneficiaries of EU-funded projects. Table 2 attached to the MEFP sets out proposed prior actions for approval of the SBA and structural benchmarks under the SBA. The first review of the program will take place by December 20, 2013 and the second review by March 28, 2014.

3. We believe that the policies and measures set forth in the attached MEFP are adequate to achieve the objectives of our economic program. We also remain committed to preserving the achievements of the preceding two programs and adhering to previously made commitments. We stand ready to take additional measures as appropriate to ensure achievement of these objectives. We will consult with the IMF and European Commission (EC) before modifying measures contained in this Letter and the attached MEFP or adopting new measures that would deviate from the goals of the program, and will provide the IMF and the EC with the necessary information for program monitoring.

4. We recognize the importance of completing a safeguards assessment by the first review under the SBA. The National Bank of Romania will provide the information required to complete the assessment by the first review and will receive as safeguards mission from the IMF as necessary.

5. We authorize the IMF and the EC to publish the Letter of Intent and its attachments, and the related staff reports. This letter is being copied to Mr. Olli Rehn.

Sincerely,

/s/	/s/	/s/
Daniel Chiţoiu	Mugur Isărescu	Liviu Voinea
Deputy Prime Minister and Minister of Public Finance	Governor of the National Bank of Romania	Minister Delegate for Budget

Attachment I. Romania: Memorandum of Economic and Financial Policies

Recent Economic Developments and Outlook

1. Economic growth picked up in early 2013 with real GDP growth of 0.6 percent (qoq) in 2013:Q1 driven by a sharp turnaround in net exports while domestic demand remained weak. Exports were supported by a pick-up in sales of machinery and transportation equipment and greater external demand including from non-EU countries. At the same time, a fall in investment and a relatively mild winter contributed to a decline in imports, in particular of energy. Inflation has begun to ease as expected after headline inflation peaked at 6 percent in January 2013 on the back of volatile food prices and administered price hikes. As the effects of these shocks dissipated, inflation came down to around 4.4 percent in July. Annual core inflation has also fallen from 3.3 percent at end-2012 to 2.5 percent at the end of July. In June 2013, we also exited the EU Excessive Deficit Procedure.

2. We expect annual growth of around 2 percent for 2013 driven by net exports and a return to a normal agriculture harvest following last year's drought. Inflation is projected to drop sharply and reenter the central bank's target band by September, largely due to favorable base effects. The current account deficit is expected to improve significantly to around 2 percent of GDP from 3.9 percent of GDP in 2012 as a pick-up in imports and a moderation in exports reverses the positive current account balance recorded in the first five months of the year. Risks to the economic outlook are broadly balanced. The agriculture harvest could be better than expected, but Romania remains vulnerable to adverse developments in international markets and low growth in the euro area. Prudent policy implementation will thus be crucial in maintaining confidence and securing policy buffers.

Fiscal Policy

3. In 2013, the fiscal deficit target of 2.3 percent of GDP (in cash terms, including PNDI) will be preserved, consistent with ESA deficit target of 2.4 percent of GDP. This would imply a reduction in the ESA structural deficit by at least 0.5 percent of GDP in line with the commitments under the EU's Stability and Growth Pact (SGP). In the first half of the year, the deficit reached 1.1 percent of GDP, in line with projections. However, revenues have underperformed primarily reflecting bank losses, declining imports and increase in VAT export refunds. The revenue shortfalls have been largely offset by lower than expected social transfers and spending on EU corrections. While reimbursable spending on EU funded projects remains low, spending on national cofinancing and net lending for

EU projects is in line with projections. Arrears have continued to decline at the local government level, but has started to rise again in the central government level.

4. Given the weak revenues and increasing spending pressures, we are undertaking several measures to achieve the deficit target. Public employment has been kept broadly stable as we have now removed the 1 for 7 rule and introduced a 1 for 1 rule while restructuring public administration. In June, we approved Government Emergency Ordinance 77/2013 eliminating the vacancies in public employment while maintaining a tight control on new hires and shifting employment from the central towards local governments. Nevertheless, current expenditures remain under pressure as agricultural subsidies have been frontloaded and goods and services spending has increased even as the implementation of the Payments Directive 7, shortening the settling of unpaid bills in the pharmaceutical sector, has been postponed from June to August. In addition, we have approved an Government Emergency Ordinance 42/2013 increasing the Guaranteed Minimum Income and family allowances, and increased eligibility thresholds and we also plan to simplify the asset test for these benefits to mitigate the impact of gas and energy price liberalization. Furthermore, we extended by three years the existing legislation to provide a top-up to unemployment benefits for some SOE layoffs and have so far provided the benefit to one large SOE. Spending commitments at the local government level is also on the rise as shown by increasing overdue bills. We are also reducing the VAT on bread and the production chain from September. To offset the revenue loss, we will increase excises on alcohol and luxury cars and goods. Unspent allocations for EU funds corrections will provide some savings while further cuts in domestically financed capital spending will also be needed. Moreover, all unexecuted contracts for PNDI projects have been cancelled while projects executed under the PNDI have been folded within the budget. An independent audit of the projects committed under the PNDI program will be conducted to ensure that they are properly executed and invoiced. In the event of lower than forecasted revenues, the government remains committed to achieving the annual deficit target.

5. For 2014, we will continue the gradual adjustment process and prepare a budget consistent with a headline deficit target of 2.0 percent of GDP in ESA terms, in line with our commitments under the SGP, and 2.0 percent of GDP in cash terms. Starting January 1, 2014, the second step of the planned increase of the Guaranteed Minimum Income will be implemented. We also plan to issue the regulation on the district heating program in September including the new asset test parameters and an additional benefit for the poorest households. To compensate for these measures, we will explore revenue measures, including on property taxes. We will also assess reforms in the social security contributions to widen the base.

6. In order to lock in the benefits of the adjustment efforts, we will undertake efforts to strengthen fiscal institutions. Key areas of reforms will include:

7. **Fiscal Compact and medium-term budget:** In compliance with the EU fiscal governance requirements, we will seek to improve the Fiscal Responsibility Law to integrate structural fiscal targets and corrective actions in case of deviations. We will seek to target a structural effort of ½ percent of GDP until a Medium-Term Budgetary Objective (MTO) of a structural general government deficit of 1 percent of GDP deficit is reached. Under this path, we expect to reach the MTO by 2015. We will also seek to shift to a medium-term budgetary framework.

8. **Public financial management:** We will seek to advance the reforms currently underway with the goal of improving the fiscal reporting system, preventing arrears, and better managing fiscal risks.

- To ensure that arrears are brought fully under control, especially at the local government level, we will publish monthly arrears reports and corrective measures being taken by the central and local governments, by unit, on a quarterly basis from end-September 2013 (structural benchmark). We will seek to maintain arrears for the central and local governments at a low level consistent with the targets under the program. The Court of Accounts shall submit a schedule of audits of the disputed invoices presented to the local governments (360 million lei) with the objective of preparing the first quarterly progress report on the status of the findings by mid-November 2013. We will evaluate the possibility of central government transfers to local government units to cover the unpaid bills that represent valid liabilities of the government as verified by the Central Harmonization Unit for Financial Management and Control Systems, which in turn will be used to cover the suppliers' tax payables. In such cases, the central government will undertake stricter control of the local government unit's total spending, consistent with Government Emergency Ordinance 46/2013.
- We have made progress in the implementation of the commitment control system. We have put in place a manual commitment control for new investments for local governments. We will approve a government ordinance to provide standard definitions of commitments (prior action) so that the commitment control system under development, supported by necessary legal and procedural changes, will be fully operational and cover expenditures of the MoPF and at least one additional unit at both the central and local government levels by end-January 2014 (structural benchmark) and fully operational for all general government entities by end-June 2014 (structural benchmark).

- The consolidated fiscal reporting system would be rolled out to all government entities by June 2014 (structural benchmark) and will run in parallel with the existing system until the end of 2014. Consolidated general government accrual based financial statements and ESA95 based reports will be prepared from the system and published from June 2015 (the first sets of reports will be for the year ended December 31, 2014), be reconciled with each other and with cash-based budget execution reports (structural benchmark).
- To improve fiscal transparency and ensure more consistency with ESA, we will request that the IMF undertake a fiscal transparency assessment. We will provide the fiscal data required to transition fully to GFSM 2001 for the 2014 budget.
- By end-2013, a report on fiscal risks will be published as part of the annual budget. This will commence with the 2014 budget. The report will take into account risks, including those related to contingent liabilities, the debt composition, the banking system, all PPPs, and all SOEs.

9. **EU funds absorption and public investment planning:** A key priority of the government is to improve budgetary planning and project prioritization to increase absorption of EU funds with a view to creating fiscal space and supporting economic growth.

- Improved prioritization of capital projects shifting funding away from domestic resources towards EU sources would help improve the fiscal deficit while increasing EU absorption. We will staff the Public Investment Evaluation Unit at the Ministry of Public Finance by end-September 2013 and make it functional with the support of the World Bank. This office will help strengthen quality control in the preparation, prioritization, appraisal and management of significant new public investment projects. We will approve a government ordinance defining the prioritization criteria for public investment projects (prior action). By mid-October 2013, we will approve, by government memorandum, a list of significant prioritized projects, based on the prioritization criteria, to help prepare for the 2014 budget (structural benchmark) and the 2014-2020 EU Financial Perspective. To the extent possible, we will seek to shift the projects that need cofinancing of local government projects onto EU funded projects. To this end, we will update and improve the database of prioritized investment projects for the central government and local government projects financed by the central government and the EU funds over the medium term and publish the list of projects included in the budget on the website together with their rolling three year budgetary allocations. From 2014, no new significant public investment project financed by the central administration will be approved without first vetting by the Public Investment Evaluation and

Monitoring Unit. We will prepare by mid-October 2013 an implementation mechanism to vet eligibility for EU funding as part of our medium-term budget planning.

- As the managing authorities seek to ramp up spending, better budgetary planning will be necessary to accommodate higher co-financing and needed financial corrections. We will prepare medium-term financial projections, by mid-October 2013, that properly identifies the fiscal implications of EU funded projects (structural benchmark) and allows proper monitoring of the spending on EU funded projects by managing authorities. To allow greater flexibility in financing of EU funded projects given lags in reimbursement, net lending of EU structural and cohesion fund projects will be provided within a ceiling on net lending of 3 billion lei (set as an indicative target). We will ensure that spending on non-eligible projects is limited to 2 billion RON. We will continue to implement fully the Priority Action Plan for the absorption of Structural and Cohesion Funds.
- Before contracting public-private partnerships (PPPs) and issuing guarantees for PPPs and concessions, the World Bank will assess MoPF capacity to (1) provide inputs to the PM/Line ministries unit to develop a methodology for identifying and evaluating fiscal commitment to PPPs, (2) assess the affordability of PPP fiscal commitment as an input to approval of any initiative, and (3) develop guidelines for incorporating PPP project in decision-making at the level of MoPF at various stages of PPP project life cycle (identification, preparation, bidding, implementation).

10. **Unified Wage Law and functional reviews:** We will ensure the sustainability of the public wage bill and implement a more efficient and equitable public sector. Towards this objective, we will seek to implement the Unified Public Wage Law within the available budgetary envelope. We commit not to introduce a stimulente regime in any government agency and we will amend Government Emergency Ordinance 74/2013 to remove the stimulente in ANAF. We have approved Government Emergency Ordinance 77/2013 that seeks to reorient public administration towards the local governments. Staffing plans for each of the line ministries will be developed in line with the functional reviews developed by the World Bank and the strategies of the line ministries prepared since. The Ministry of Public Finance will develop its own staffing plans based on ongoing modernization efforts in Treasury and the ANAF. A methodology for determining staffing levels in subnational governments will be developed while balancing local responsibilities with fiscal prudence. We will consult with the IFIs (IMF, EC and the World Bank) before making changes in the public employment policy and the Unified Wage Law.

11. **Tax administration:** We will continue our comprehensive reforms of the tax administration (ANAF) with a view to raising revenue collection and efficiency.

- As part of ANAF restructuring and modernization, the current 221 tax offices will be consolidated to eight regional directorates by September 2013 and 47 local tax offices by 2015. We are also reallocating around 1,700 staff away, mostly from support functions to prevention and inspection, and will increase resources in Bucharest Region to combat fraud. ANAF will take over the responsibilities of the Financial Guard by November 1, 2013, which will cease to exist, adding a further 1,100 staff to ANAF's disposal. The new positions will be directed to the new prevention and fighting tax evasion and tax customs fraud structure and will be filled following strict selection procedures. We will provide additional professional training to all staff involved in combating tax evasion. We ratified the loan agreement with the World Bank concerning a project to support the modernization of the tax administration.
- We continue to make progress on our High Net-Wealth Individual (HNWI) taxpayers initiative. We started 30 prior desk audits for HNWI following the tax procedure code in the first half of the year and re-launched our notification campaign by sending out letters on the risks of non-filing foreign income to 360 individuals. We have also published our program on ANAF's website. Voluntary compliance appears to be improving. We have improved the quality of our personal income tax audits more generally. We will strengthen our auditing further using the indirect proofs method, expanding the definition of un-sourced income and clarifying the taxability of dividend payments, which are currently often disguised as non-taxable loan repayments to businesses. To help us achieve these goals, we have undertaken training programs with the assistance of partner-country tax administration specialists and IMF technical assistance in April.
- We also aim to develop taxpayer services, for example, offered through ANAF's portal (considered as a "one stop shop") by June 30, 2014 and by ensuring that the interpretation of the tax law is unambiguous. To this end we will issue a common procedure with the MoFP and set up single channel dealing with all enquiries on tax law interpretation by December 31, 2014. Moreover, we will streamline the VAT reimbursement procedures based on a risk analysis, in order to significantly diminish the time allocated tax audits in this field and for decreasing the time needed for solving refund cases by June 2014 and will set up a central database that will allow us to manage and assess together with local authorities data regarding taxes and contributions owed to the general consolidated budget as well as information on properties. This will be an important source of information for taxpayers and should also raise compliance by December 31, 2014. Finally we will make all efforts to ensure SME in distress are granted payments terms in installments to clear tax arrears.

12. **Tax policy:** We aim to improve the efficiency and revenue-raising capacity of the tax system. In January 2013, we enacted measures to move VAT collection onto a cash accounting basis for companies with annual turnover below EUR 500,000. We will assess the performance of this new arrangement. We will initially on a temporary basis lower the VAT on bread and its production chain to 9 percent and have identified countervailing measures in excises to offset the budgetary impact, to be implemented from September 1, 2013. During 2014, we will assess the efficiency of these measures and decide whether they will be applied on a permanent basis. Before finalizing the 2014 budget we will revise the base for property taxes, which will vary depending on use of the property and not the legal status of the property owner. We have started the preparations for a strategy for a new oil and gas taxation and royalty regime by establishing an inter-ministerial working group. We will establish a new regime that takes effect from 2015 through 2024, if all stakeholders agree. We will receive IMF technical assistance for both work streams.

13. We will also analyze how revenue collection could be raised and the tax wedge reduced by widening the base of the social contribution system. We will implement measures for the 2015 budget based on the tax expenditure report. By mid-October 2013, we will prepare a reform package for health contributions in order to finance the public health system based on a mix of mandatory tax, consistent with the basic health package, and a voluntary contribution payable by individuals who wish to have a supplementary health insurance system. Towards this goal, we will approve a Government Ordinance (prior action), to broaden the social contributions base by applying a mandatory tax (health contribution) on rental income of individuals, to be implemented from January 1, 2014. We will also approve legislation to restructure the social security system to widen the base by reducing the differences that exist in the pension base for the different types of performing activity (i.e., salary remuneration, freelance activity, copyright, etc). We will consult with IMF/EC staff before undertaking any further changes of the tax system.

14. **Health care:** We are preparing a comprehensive reform of the healthcare system, which should make the system financially sustainability, raise the efficiency of healthcare spending and improve health outcomes.

- The reforms will strengthen the contributions base; streamline hospital services reducing the redundant capacity for inpatient services in line with the national health strategy and shifting the delivery of health services away from hospitals to ambulatory and primary health care providers; develop capacity in Health Technology Assessments and evidence-based protocols; and allocate more resources towards primary and secondary preventive care.

Rather than adopting a new framework law, we have decided to pursue a more gradual approach based on modifying existing legislation. This should allow individual initiatives to proceed at different speeds and to be completed without necessarily relying on the success of all other initiatives. In April we formulated a strategic action plan for this year. We published the agreed plan on the ministry's website as a statement of government policy agreed with the IFIs, we will meet all the deadlines set and, in particular, will prepare the basic health package within the existing spending envelope by end-September 2013, which will also define the scope of the private health insurance in the health care system in the future (structural benchmark). We will also prepare a comprehensive health strategy covering also the revenue side, together with the MOPF, including a timetable for implementing legislative changes and progress indicators.

15. Parallel to preparing and as part of a comprehensive health strategy, we will implement the following measures to address health sector financial imbalances and modernize its operations:

- To increase the share of spending on primary and ambulatory services in total health spending, we will revise by end-December 2013 the list of services, which can be contracted with primary care providers as part of the 2014 health care framework agreement. We will publish a revised list of compensated drugs by end-December 2013, to be approved by government ordinance, based on the methodology provided by a newly established unit conducting health technology assessments. The centralized procurement system for pharmaceuticals and medical devices for hospitals became operational in the first half of 2013. We will assess the system's performance at the end of 2013 and progress on the design of a centralized IT system.
- To avoid the future build-up of arrears in the hospital sector, we have shifted some financial resources from hospitals with limited competences to those in the network of regional emergency hospitals. This objective will be achieved through adjustments of the weighted-per case tariffs, while ensuring that arrears will not accumulate in hospitals with decreased funding. We amended the contracts of hospital managers in June 2013 so that they will be replaced automatically if the hospital has run arrears for three consecutive months.
- We will continue to monitor public hospital budgets to ensure that they are consistent with the expenditure programmed in the general government budget, will collect and analyze the cost of service provision across hospitals with the aim of developing benchmarks in the future, and have published online up-to-date financial statements of all public hospitals since October 2012. We signed a contract with the National Printing Office to produce 7½ million patient cards by end 2013 and the remainder for the eligible population by mid

2014. By September, we will decide on the mechanism for distribution of these cards. The electronic prescription system is now established, with 34m prescriptions produced by end of June 2013. To promote awareness and encourage the increased use of generic drugs, we will print from January 2014 the patient rights with respect to pharmacists' obligation to provide full information on available drugs on the printed prescription.

16. **Debt Management:** In line with our debt management strategy, we are improving our risk management and have reduced the share of short-term debt. We have sought to continue consolidating the fiscal buffers, to achieve our objective of four months of gross financing needs to protect against unforeseen external shocks. The net interest paid on these buffers represents a necessary cost for insurance against shocks. We are continuing our efforts to widen the investor base and improve outreach efforts. We are undertaking a project financed with European funds and implemented with support of the World Bank to strengthen the debt management department. We will ensure that increases in guarantees issued remains prudent, and will not issue guarantees for PPPs and concessions in 2013 and for bank lending with a view to repay tax liabilities.

Monetary and Exchange Rate Policy:

17. Monetary policy under the SBA will be guided by the NBR's inflation targeting framework. Progress towards achieving the official inflation target will be monitored through an inflation consultation clause with consultation bands drawn symmetrically around the projected path of headline CPI inflation (see TMU). The program also aims at maintaining adequate reserve coverage. Most standard reserve metrics assess our current level of reserves as broadly adequate. A performance criterion on Net International Reserves that is consistent with this goal will be established.

18. We remain committed to reducing inflation to within our medium-term target band of 2.5±1 percentage point by September and to keeping inflation in the target band from then on. Inflation has begun to ease to 4.4 percent in July 2013 after a food supply induced spike in the second half of 2012 and has continued to be very volatile reflecting the large share of food items (38 percent in CPI terms) and one-off effects of administrative price changes. For transparency and communication reasons we will continue to target headline inflation but also closely monitor core inflation as a measure of underlying inflation. We currently project headline inflation to reenter the target band in by September, mainly on account of the reversal of base effects and a significantly better harvest than in the previous year putting downward pressure on food prices. Core inflation was at 2.5 percent in July 2013.

19. We have lowered the policy rate by a cumulative 75 basis points to 4.5 percent in July and August as we expect headline inflation to continue its declining trend. Following the recent narrowing of the interest rate corridor around the policy rate, the interest rates for the NBR lending and deposit facilities stand at 7.5 and 1.5 percent, respectively. Anchoring inflation expectations and dealing with volatile international capital flows continues to require a prudent monetary policy stance supported by the consistent implementation of the macroeconomic policy mix. The current monetary policy stance appears broadly appropriate. We will closely monitor inflation developments following these easing steps and would consider gradually lowering the policy rate further only if inflation drops inside our target band as projected, inflation expectations remain firmly anchored, and market conditions permit. We will continue regular open market operations as needed to ensure adequate liquidity conditions in the banking system, while underpinning the good functioning of money markets and minimizing the divergence between interbank rates and the policy rate in order to strengthen interest rate transmission. Ratios for minimum required reserves are expected to remain unchanged in the coming months. Going forward, the NBR will preserve the wedge between minimum requirements for foreign and domestic currency liabilities. Moreover, any considered changes would be implemented gradually and take into account inflation expectations as well as liquidity and prudential considerations.

20. During the period of the SBA we will not, without Fund approval, introduce or intensify restrictions on the making of payments and transfers for current international transactions, nor introduce or modify any multiple currency practices or conclude any bilateral payment agreements that are inconsistent with Article VIII of the IMF's Articles of Agreement. Moreover, we will not introduce or intensify import restrictions for balance of payments reasons.

Financial Sector

21. The Romanian banking sector maintains reassuring capital buffers and provisioning but faces continues pressures on asset quality, and from foreign bank deleveraging, while also remaining vulnerable to external shocks. Annual credit growth to both corporates and households remains negative. Non-performing loans (NPLs) rose to 20.3 percent of total loans at end-June 2013 (compared to 14.3 percent at end-2011) reflecting the difficult economic environment, slow credit growth, deteriorating quality of loans, and difficulties in removing NPLs from bank balance sheets. However, provisions (with a prudential filter) were sufficient to cover a comfortable

88.3 percent of NPLs while the IFRS provisioning ratio stood at 62.8 percent at end-June.[1] The provisioning requirements along with the high cost base led to a loss in the banking system in 2012 but allowed for a small profit in the first half of 2013. In light of the still difficult economic environment, in particular as regards corporate and household balance sheets as well as low credit demand, prospects for bank profitability remain challenging. The capitalization of the banking sector remained strong at 14.7 percent at end-June 2013 albeit with some differences between banks. Overall, system household and corporate deposits have only increased by around 10 percent since end-2011. While the liquidity situation has improved for the banking system, funding conditions are still uneven among some banks. The pace of foreign-owned bank deleveraging has accelerated in line with regional developments but remains orderly so far with a parent funding decline of 26 percent since 2011. Risks from continuing parent funding retrenchment remain elevated and could be an impediment to the credit growth recovery should credit demand pick up sizably. The system-wide loan-to-deposit ratio stood at around 114 percent at end-June 2013, declining from 117 percent at end-2012 and at end -2011.

22. The NBR will continue to intensively supervise the banking system and take any necessary measures to ensure that banks maintain sufficient capital and liquidity, in light of the uncertain economic environment which could pose further challenges with respect to asset quality, profitability, and parent funding retrenchment for most banks. In that regard and in close coordination with the IMF and EC, the NBR will continue to regularly conduct top-down and bottom-up solvency stress tests as well as liquidity stress tests of the banking industry.

23. The NBR and Deposit Guarantee Fund (DGF) will continue to coordinate the implementation of operational preparedness plans and the arrangements for the acquired bank resolution powers according to their competencies. An amendment to the Government Emergency Ordinance no. 99/2006 will provide the NBR with more flexibility and powers to stabilize the financial system to protect depositors and maintain public confidence in the banking sector. After clarifying the new EU state aid rules for the bank stabilization measures, the amended Government Emergency Ordinance no. 99/2006 and Government Emergency Ordinance no. 39/ 1996 will be approved by end-2013 in line with the CRDIV implementation deadline. Based on the amended banking law, the NBR will amend the internal procedures for bridge-banks by end-2013. The details of the updated NBR contingency planning framework will be agreed with the IMF and EC staff. The NBR is preparing detailed contingency plans on an ongoing basis.

[1] Including all provisions and not only those for NPL's 90 days past due, the total provisioning ratio was 102.4 percent and the IFRS provisioning ratio stood at 77.2 percent at end June.

24. To avoid any perceived conflict of interest of its senior management, the DGF corporate governance principles will adhere to best international practices.

25. The NBR will continue to closely oversee bank practices to avoid evergreening so as to ensure that IFRS loan-loss provisioning and collateral valuations, as well as the assessment of credit risk of restructured loans, remain prudent and in line with good international practices. In particular, the NBR will examine in detail during onsite inspections all banks' loan restructuring practices as well as adequacy of IT systems to deal with impaired assets. A comprehensive report of the banks' loan restructuring practices and asset quality with granular information, migration matrices and a NPL vintage analysis will be shared with the IMF and EC by end-October 2013. The analysis on banks' IT adequacy will be finalized by end-2013 for a representative sample of banks. In consultation with the IMF and EC, an NPL resolution action plan will then be agreed. The NBR will ensure that following this year's collateral audit, banks with any estimated collateral gap will swiftly provide the additional provisioning.

26. The NBR will collect periodic and detailed supervisory data on restructured loans, including to SOEs, on a quarterly frequency by end September. To ensure transparency, the NBR will publish aggregate data.

27. Given the substantial NPL overhang, the authorities will remove, where possible, impediments to corporate and household out-of-court debt restructuring and NPL resolution. The NBR has clarified in a letter to the banking system that under the IFRS framework banks do not necessarily have to exhaust all legal means to remove fully-provisioned NPLs from their balance sheets. The NBR will hence urge banks within the IRFS framework to remove fully-provisioned NPLs (especially for unsecured consumer loans) from their balance sheets in a timely manner. To maintain a prudent provisioning stance on collateral treatment, the NBR will not consider additional collateral deductions unless significant progress on banks' NPL removal of unsecured (consumer) loans has been made. Any agreed further changes to the current regime will be agreed with the IMF and EC. As part of the prudential arrangements that would continue to apply in 2013, the prudential filter will remain in place in the current form, in line with evolving EU regulatory developments.

28. To foster the development of a viable distressed debt market, we will resolve possible discrepancies in the fiscal code and accounting rules on the treatment of NPLs sold to domestic debt management companies in line with the outcome of the pending EC infringement case structural benchmark, by end-December 2014. We will also conduct an impact study on the fiscal

costs from the tax deductibility of the sale of intra-group bank receivables (by end-December 2013) and of non-bank receivables (by end-August 2014).

29. To enable much needed longer term bank funding instruments, the authorities will swiftly approve the pending covered bond legislation by end-December 2013 as a Government Ordinance, while appropriate safeguards to preserve financial stability are implemented.

30. After the current Prima Casa program ends in September, a possible continuation will only apply to RON lending. This will help to develop the RON mortgage market and also contribute to RON denominated covered bonds in the future. In addition, we will make the SME guarantee fund more effective and operational especially as regards to the maturity, price, and rollovers of the guaranteed loans, as well as the implementation process for the guarantee execution.

31. We will ensure that the legislation and institutional arrangements for the FSA will be amended by end September to comply with international best practices. This regards notably to the size of the managing and council board (to a maximum of 9 overall), minimum required professional qualifications of FSA board members, statutory protection of supervisory staff and institution, and avoidance of conflicts of interest, in particular the connection of these members with members of Parliament and political parties. Senior management and board members will have to comply with the amended corporate governance principles. The FSA will also enhance transparency and public disclosure of all fees and commissions charged to the supervised entities.

32. Because preserving credit discipline among debtors contributes significantly towards enhancing financial stability, we will take all efforts to avoid the adoption of legislative initiatives which would undermine credit discipline. Furthermore, in order to avoid threats to financial stability, the authorities will consult extensively with all relevant stakeholders having in view also the impact assessment finalized by the NBR on the new provisions on abusive clauses in the law for the application of the civil procedure code. The authorities will ensure that court cases involving abusive clauses are dealt with by higher ranking courts or by a unique specialized court and will take all necessary measures to ensure a harmonized application of these provisions, such as training of judges.

33. To increase transparency and as corporate insolvencies are increasingly fuelling the still on-going deterioration in asset quality, the NBR together with the Romanian Banking Association will explore possibilities for setting up a database of shareholders of companies in insolvency as well as implement more effective data reporting of the Association of Insolvency Practitioners.

34. We will swiftly implement the World Bank recommendations on the ROSC, and following the comprehensive public consultation in September 2013 as well as with the IMF, EC and the World Bank, we will send the amended insolvency code draft to parliament by end-October 2013. All relevant stakeholders will be adequately consulted before the insolvency code amendment is passed in parliament.

Energy and transportation sector reforms

35. Comprehensive reform of the energy and transportation sectors is a central element of our goal to increase growth in Romania. We seek to foster investment and better service delivery in these sectors by bringing prices more in line with market forces and enhancing the operational and financial performance of the state-owned enterprises that dominate these sectors. These measures will also allow us to leverage Romania's favorable geographic location.

36. We undertook some important reforms related to state-owned enterprises (SOEs) and the energy and transportation sectors last year. For example, the cumulative arrears of central-government and local-government owned enterprises were reduced by 1 percent of GDP through voluntarily placing a few companies into the insolvency or liquidation process, debt swaps, and restructuring measures. Key reforms in the energy and transportation sectors include:

- ***Energy sector:*** We transposed the European Union's third energy directive into national law and promulgated a law to ensure the independence of the energy regulator (ANRE). ANRE started the implementation of the electricity price liberalization roadmap in September 2012 and continued the quarterly schedule in January, April, and July 2013. After an initial delay, ANRE started the implementation of the gas price liberalization road map and has raised the domestic gas producer price by almost 40 percent in accordance with the road map. The state-owned hydro-electric producer, Hidroelectrica, exited from the insolvency process on July 1, 2013. Under insolvency, the Legal Administrator cancelled or renegotiated below market bilateral contracts with the electricity released from contracts being sold at the OPCOM Power Exchange. The Administrator also cancelled hundreds of smaller contracts and investment projects deemed to be against the interest of Hidroelectrica.
- ***Transportation sector:*** We initialed a sale-purchase agreement for the sale a 51 percent stake in the state-owned freight company (Marfa) for RON 905 million and took a government decision approving the sale-purchase agreement. We also approved an arrears clearance scheme in June whereby CFR Marfa's arrears would be reduced by over 90 percent upon conclusion of the sale. To help improve the financial performance of the state-owned passenger rail company (Calatori), we changed the formula for calculation of the subsidy for

the public service obligations (PSO) and removed the international and inter-city trains from the PSO. We also closed the most unprofitable routes for passenger traffic.

37. Nonetheless, the reform effort remains unfinished. The corporate governance reforms are incomplete and the draft law on Corporate Governance in State-Owned Enterprises continues to languish in parliament. Planned initial public offerings in energy state-owned enterprises were delayed and, with only an interim board and management in place, Hidroelectrica risks losing the gains made under insolvency. In the railway sector, arrears accumulation remains a significant problem and the Marfa sale needs to be concluded. In addition, new challenges have arisen to the reform agenda. Pressure is building to delay implementation of the energy price liberalization roadmaps and the precarious financial state of high cost thermal electricity producers threatens to undermine the broader energy strategy.

38. Under the new program, we propose a three-pronged approach to decisively improve the financial position, operating efficiency, and overall transparency of SOEs and the pricing framework in the energy and transportation sectors. The first part is composed of strengthened measures to reduce state-owned enterprise arrears. This commitment would be reflected through an indicative quarterly target on the cumulative arrears of all central-government owned enterprises. This represents a substantial broadening of coverage of the SOE arrears target relative to the prior program. To ensure timely reporting for the target, all line ministries agree to ensure that all SOEs within their respective portfolios will file, in accordance with existing regulations, quarterly financial information with the MOPF by the 25th day following quarter end. Potential measures to reduce arrears include use of debt/equity swaps, including a measure to clear CFR Calatori's arrears with the state-owned rail network operator (CFR Infrastructura), placement of companies into the insolvency process or liquidation such as subsidiaries of CFR Calatori and CFR Infrastructura, and restructuring measures to improve financial performance. We also agree to place an indicative quarterly target on the operating performance of a the largest railway companies and their subsidiaries to ensure that arrears clearance measures are complemented by reforms that improve the viability of these companies (CFR Infrastructura, CFR Calatori, and CFR Marfa).

39. The second leg will continue measures to improve the governance, transparency, and monitoring of SOEs. We have taken note of observations made about the new boards appointed recently to energy SOEs. We will appoint a professional board in Hidroelectrica by end-November 2013 (structural benchmark) following the letter and spirit of the procedures specified in the SOE corporate governance Government Emergency Ordinance 109/2011. In the meantime, the current interim board appointed upon Hidroelectrica's exit from insolvency will continue to be in charge and

we will authorize through a General Shareholders Meeting the current interim board to take decisions in accordance with law 31/1990 (prior action). More broadly, we will undertake and publish an independent government-wide assessment of the implementation of the Government Emergency Ordinance (109/2011). Following the assessment, we will develop guidelines for its implementation across all ministries. We will also seek passage of the SOE corporate governance law in parliament by end-September 2013 which gives legal responsibility to the MOPF to supervise its proper implementation. The Fiscal Council plans a report on the operations and its fiscal implications in SOEs. Moreover, we will take steps, with support from the World Bank, to improve the monitoring function of the SOE oversight directorate in the Ministry of Public Finance.

40. We will continue measures to enhance the transparency of SOE operations. All new bilateral contracts of electricity producers will be made transparently and non-discriminatorily through the OPCOM power exchange and annual reports on SOE performance will be published in accordance with provisions of the SOE corporate governance Government Emergency Ordinance. Relatedly, line ministries will have all SOEs within their respective portfolios submit their 2013 budgets for approval by end-September 2013 and the 2014 budget one month after the approval of the state budget.

41. The third part would be to continue to improve the pricing framework and efficiency of the energy and transportation sectors. We are committed to implement the electricity and gas price road maps and the pass-through mechanism for electricity and gas purchases by the supply companies will continue to be applied. For electricity, complete deregulation of electricity prices for non-residential consumers will be achieved by January 1, 2014, and for households by December 31, 2017. For natural gas, we intend to implement the remainder of the roadmap to deregulate gas prices as planned to achieve complete price deregulation for non-residential consumers at the latest by December 31, 2015, and for residential consumers by December 31, 2018. We will continue to take steps to strengthen OPCOM as an electricity and gas trading platform. We also plan to sell the majority of the portfolio of companies under the Ministry of Economy and conclude the following five privatizations of state-owned energy companies during the program period, which will generate resources for the companies and the government and support development of the local capital markets. For majority privatizations, in which we seek strategic investors, we will do so with a view to attract new investment and provide professional expertise so as to enhance the viability of operations and service delivery. We commit not to break up and/or merge the companies or the assets of the companies slated for IPOs, except as provided for in the reorganization plan of Hidroelectrica or as specified below.

- **Nuclearelectrica (**nuclear energy producer): Launch an initial public offering (IPO) of 10 percent of the government's shares by end-September 2013.

- **Romgaz** (natural gas producer)**:** Launch an IPO of 15 percent of the government's shares by mid-November 2013 (structural benchmark). In advance, we will obtain approval of the Financial Supervision Authority (FSA) for use of global depository receipts and complete an environmental impact study. A decision to expand the size of Romgaz's board following the IPO has also been taken. As a prior action, we will clarify the tax treatment of securities bought in Romgaz traded on the foreign stock exchange and adopt, if needed, the necessary legal basis.
- **Electrica** (electricity distribution, supply, and service)**:** Launch an initial public offering of a majority of the government's shares, after the planned capital increase, by end-May 2014 (structural benchmark). In preparation, we will hire a transaction advisor for the IPO by mid-September 2013. Work is currently underway to determine what to do with five of Electrica's six regional service companies. At least three, but possibly all five may have to be separated from Electrica for eventual liquidation. Electrica's minority shareholdings in already privatized distribution companies could be a major area of uncertainty for the IPO and these share holdings will be taken out of Electrica prior to the IPO. We will also address the issue of non-payment by CFR for its electricity purchases from Electrica ahead of the IPO.
- **Oltenia** (thermoelectric generator)**:** In view of Oltenia's investment needs, we planned ahead of majority privatization an IPO of a 15 percent of the government's shares, prior to the planned capital increase, by end-October 2013 and hired a transaction advisor for this in May 2013. Subsequently, we decided to delay the IPO until end-June 2014 (structural benchmark) after the audited financial statements for 2013 are available and a study of the coal reserves is conducted.
- **Hidroelectrica** We planned an IPO of a 10 percent of the government's shares, after the planned capital increase, by end-October 2013. However, a court challenge to the government decision to conduct the IPO and the government's subsequent appeal of the court decision has delayed the process. The Ministry of Economy, the General Secretariat of the Government and Hidroelectrica submitted to the Court of Appeal the withdrawal of their respective appeals and asked for the Court to consider the withdrawal requests on an expedited basis. We will issue a new government decision for an IPO of 10 percent, in accordance with all required procedures. The government will sign a contract with the transaction advisor selected through a competitive process already in 2012 for the IPO which will be launched by end-June 2014 (structural benchmark), provided a Court decision is made by end-September, 2013.

42. In the transportation sector, we intend to work closely with the World Bank and European Bank for Reconstruction and Development to reform the rail sector with the goal of improving the financial and operational performance of railway SOEs and the quality of rail service. We plan to revisit the terms of the Multi-Annual Infrastructure Contract. At present, this contract is not in financial balance. The amounts paid to state-owned railway infrastructure company (CFR Infrastructura) are not consistent with the responsibilities it confers to maintain and operate the network. It will likely take a combination of efficiency improvements, network reductions, and possibly subsidy increases to bring this into balance. The World Bank is working on an assessment to help quantify what needs to be done. We also plan to facilitate improved payment of infrastructure access and electricity charges from the state-owned passenger rail company (CFR Calatori) and CFR Marfa through reforms of those enterprises and to settle of outstanding debts among the three main railway companies. Measures to improve the operating and financial performance of these companies could include:

- **CFR Marfa:** We will fulfill our obligations under the sale purchase agreement for the majority sale of CFR Marfa and close the transaction (exchange of payment for shares) by the mid-October 2013. In this context, merger control approval will be sought from the relevant regulatory authority. If the privatization process encounters insurmountable obstacles, we will reopen the tender for the majority privatization of Marfa abiding to a process that follows best international practices.
- **CFR Infrastructura and CFR Calatori:** We will allow the appointed boards of these companies to implement the approved administrative plans without interference. We will complete the procedure for appointing new management in CFR Infrastructura following the letter and spirit of the procedures specified in the SOE Corporate Governance ordinance (109/2011). We also intend to lease out an additional 1,500 kilometers of inoperable track, raise passenger tariff rates in September 2013, and further amend the formula for calculation of the PSO to give more weight to passenger-train kilometers travelled starting in January 2014. More broadly, we will continue to explore measures to rationalize the network, improve absorption of EU funds, strengthen the procurement process, and reduce costs. We will address the issue of non-payment by CFR Infrastructura to Electrica ahead of Electrica's IPO which would otherwise be undermined.

43. A high quality and extensive road network is a critical infrastructure component of a welcoming business environment for investment and a well functioning economy. To focus our efforts on increasing the absorption of EU funds in the 2014–2020 funding period, we will create an agency within the government dedicated to the development of highways eligible for EU funding.

The state-owned roads company also intends to minimize capital spending on existing projects in 2013, with a view to reducing arrears towards zero. The company will not lengthen the invoice certification procedures outside legal requirements.

Labor Markets

44. The new Labor Code has improved the functioning of the labor market. Fixed term contracts helped employment growth, growing from 6 percent of total active contracts at end-June 2011 to 9 percent at end-June 2013. We will continue to monitor implementation of the Social Dialogue Law and ensure that any amendments will be undertaken in consultation with all stakeholders through the normal legislative process. We will continue our cooperation with the International Labor Organization (ILO) to ensure that the new legislation respects core ILO Conventions.

45. In view of the high youth unemployment in Romania, we have started to amend current legislation to improve the transition of young Romanians towards the labor market under the new National Job Plan to boost youth employment towards 2013 and going forward. An action plan will be developed for the implementation of measures that could qualify for support under the Youth Employment Initiative, in line with the conclusions of the European Council of June 2013. The Apprenticeship Law that introduces a dual apprenticeship model has been adopted, and we expect the necessary secondary legislation to be finalized by end-September. A law facilitating acquiring professional experience for higher education graduates was adopted by government and will be sent for approval by the Parliament by end-October 2013.

Table 1. Romania: Quantitative Program Targets

	2012	2013			2014	
	Dec	June	Sept	Dec	March	June
	Actual	Prelim.	Prog.	Prog.	Indicative	Indicative
I. Quantitative Performance Criteria						
1. Floor on the change in net international reserves (mln euros) 1/	16,344	3,922	3,922	3,922	250	0
2. Floor on the general government overall balance (mln lei) 2/	-17,430	-6,629	-9,181	-14,700	-4,000	-6,200
3. Ceiling on the stock of central government and social security arrears (bn lei)	0.027	0.04	0.02	0.02	0.02	0.02
4. Ceiling on general government guarantees issued since end-2008 (face value, bn lei)	9.8	10.9	16.0	16.0	18.0	18.0
II. Continuous Performance Criterion						
5. Nonaccumulation of external debt arrears	0	0	0	0	0	0
III. Inflation Consultation						
6. 12-month rate of inflation in consumer prices						
Outer band (upper limit)	...	...	5.1	5.3	4.6	5.0
Inner band (upper limit)	...	...	4.1	4.3	3.6	4.0
Actual/*Center point*	5.0	5.4	*3.1*	*3.3*	*2.6*	*3.0*
Inner band (lower limit)	...	...	2.1	2.3	1.6	2.0
Outer band (lower limit)	...	...	1.1	1.3	0.6	1.0
IV. Indicative Target						
7. Ceiling on general government current primary spending (excl. EU funds and social assistance, mln lei) 2/	134,330	70,412	106,300	147,509	36,700	74,400
8. Floor on operating balance (earnings before interest and tax, net of subsidies and one-off adjustments to income due to financial or accounting operations) of key SOEs (as defined in paragraph 22 of the TMU (bn. lei)) 2/	-3.3	-1.0	-1.6	-2.3	-0.5	-0.8
9. Ceiling on outstanding payments past due of all central-government owned enterprises (as defined in TMU, bn lei)	12.6	8.2	7.5	5.6	4.7	3.7
10. Ceiling on stock of local government arrears (bn lei)	0.84	0.14	0.30	0.30	0.30	0.30
11. Ceiling on stock of net Treasury loans for EU-funded projects (mln lei) 2/	...	1,546	3,000	3,000	3,000	3,000

1/ The end-December 2012 figure is a stock. Reported at program exchange rates and gold price.
2/ Cumulative figure during calendar year (e.g. September 2013 figure is cumulative from January 1, 2013).

Table 2. Romania: Proposed Conditionality

	Measure	Target Date
Prior Actions		
1.	Approve a government ordinance to provide standard definitions of commitments for the commitment control system.	
2.	Approve a government ordinance defining the prioritization criteria for public investment projects.	
3.	Approve a government ordinance to broaden the social contributions base by applying a mandatory tax (health contribution) on rental income of individuals, to be implemented from January 1, 2014.	
4.	Authorize, through a General Shareholder's Meeting of Hidroelectrica, the current interim board to take decisions in accordance with law 31/1990, while it seeks to appoint a professional board in accordance with the SOE Corporate Governance ordinance.	
5.	Clarify the tax treatment of securities bought in Romgaz traded on the foreign stock exchange and adopt, if needed, the necessary legal basis.	
Structural benchmarks		
1.	Start publishing monthly arrears reports and corrective measures being taken by the central and local governments, by unit, on a quarterly basis.	End-September 2013
2.	Prepare the basic health package within the existing spending envelope which will also define the scope of the private sector in the health care system in the future.	End-September 2013
3.	Prepare medium-term financial projections that properly identify the fiscal implications of EU-funded projects, including co-financing needs, financial corrections and non-eligible spending.	Mid-October 2013
4.	Approve, by government memorandum, a list of significant priority projects, based on the prioritization criteria, to help prepare for the 2014 budget.	Mid-October 2013
5.	Launch an initial public offering of 15 percent of the government's shares in Romgaz.	Mid-November 2013
6.	Appoint a professional board in Hidroelectrica in accordance with the provisions of Ordinance 109/2011.	End-November 2013
7.	Approve Covered Bond legislation.	End-December 2013
8.	Fully operationalize the commitment control system, supported by necessary legal and procedural changes and cover expenditures of the MoPF and at least one additional unit at both the central and local government levels.	End-January 2014
9.	Launch an initial public offering of a majority of the government's shares in Electrica, after the planned capital increase.	End-May 2014
10.	Fully operationalise the commitment control system for all general government entities.	End-June 2014
11.	Launch an initial public offering of 15 percent of the government's shares in Oltenia, prior to the planned capital increase.	End-June 2014
12.	Launch an initial public offering of 10 percent of the government's shares in Hidroelectrica, after the planned capital increase.	End-June 2014
13.	Roll out the consolidated fiscal reporting system to all government entities.	End-June 2014
14.	Resolve possible discrepancies in the fiscal code and IFRS accounting rules on the treatment of NPLs sold to domestic debt management companies in line with the outcome of the pending EC infringement case.	End-December 2014
15.	Prepare and publish consolidated general government accrual based financial statements and ESA95 based reports from the system (the first sets of reports will be for the year ending 2014), and reconcile with each other and with cash-based budget execution reports.	End-June 2015

Attachment II. Romania: Technical Memorandum of Understanding

1. This Technical Memorandum of Understanding (TMU) defines the variables included in the quantitative performance criteria and indicative targets set out in the Memorandum of Economic and Financial Policies (MEFP), the key assumptions, the methods to be applied in assessing program performance, and the reporting requirements to ensure adequate monitoring of economic and financial developments. The quantitative performance criteria and indicative targets, and structural benchmarks for 2013 and 2014 are listed in Tables 1 and 2 of the MEFP, respectively.

2. For the purposes of the program, *the exchange rates* of the Romanian Leu (RON) to the euro is set at RON 4.4588 = €1, to the U.S. dollar at RON 3.4151 = $1, to the Japanese yen at RON 3.4480 = ¥100, and to the pound sterling at RON 5.2077 = £1, and *the gold price* is set at RON 132.1562 per gram as shown on the National Bank of Romania's (NBR's) website as of June 30, 2013. The exchange rates to other currencies, where applicable, will also be the ones shown on the NBR's website as of June 30, 2013.

3. For the purposes of the program, the *general government* includes the entities *as defined in the 2013 budget*. These are: the central government (state budget, self-financed state entities included in the budget, etc.), local governments, social security funds (pension, health, and unemployment), and the road fund company. This definition of general government also includes any new funds, or other special budgetary and extra budgetary programs that may be created during the program period to carry out operation of a fiscal nature as defined in the IMF's *Manual on Government Finance Statistics 2001*. The authorities will inform the IMF staff of the creation of any such new funds or programs immediately.

QUANTITATIVE PERFORMANCE CRITERIA, INDICATIVE TARGETS, INFLATION CONSULTATION BAND, AND CONTINUOUS PERFORMANCE CRITERIA

A. Floor on the Change in Net International Reserves

4. For program purposes, Net International Reserves (NIR) are defined as the NIR of the NBR minus Treasury liabilities to the International Monetary Fund.

5. NIR of the NBR are defined as the euro value of gross foreign assets of the NBR minus gross foreign liabilities of the NBR; and will be measured on the basis of the NBR's operational rather than accounting definitions. Non-euro denominated foreign assets and liabilities will be converted into euro at the program exchange rates and gold price.

6. Gross foreign assets of the NBR are defined to include the NBR's holdings of monetary gold, SDRs, the country's reserve position at the IMF, holdings of cash, securities and deposits abroad in convertible foreign currencies. Excluded from reserve assets are: (i) precious metals other than monetary gold; (ii) assets in nonconvertible currencies; (iii) illiquid assets; (iv) any assets that are pledged, collateralized, or otherwise encumbered, unless there is also a gross foreign liability associated with it; (v) claims on residents; and (vi) claims in foreign exchange arising from derivatives in foreign currencies vis-à-vis domestic currency (such as futures, forwards, swaps, and options).

7. Gross foreign liabilities of the NBR are defined as all foreign exchange liabilities to residents and nonresidents, including commitments to sell foreign exchange arising from derivatives (such as futures, forwards, swaps, and options), banks' foreign currency deposits against reserve requirements, and all credit outstanding from the IMF, but excluding government foreign currency deposits at the NBR.

Floor on Cumulative Change in NIR from the Beginning of 2013 and 2014 (in million euros)[1]

	2012	2013	2013			2014	
	December stock	June stock	June actual	September PC	December PC	March Indicative	June Indicative
Cumulative change in NIR	16,344	20,266	3,922	3,922	3,922	250	0
Memorandum Item: Gross Foreign Assets	34,152	35,381	1,229	40	-1,371	-1,161	-2,932

[1]PC = performance criterion; data for end-month. Flows are cumulative from the beginning of the same calendar year (e.g., June 2013 figure is cumulative from January 1, 2013). Current year stocks are obtained by adding the flows to the previous end-year stock.

8. The NIR targets will be adjusted (i) upward (downward) by the surplus (shortfall) in program disbursements relative to the baseline projection (Program disbursements are defined as external disbursements from official creditors (WB and the EC) that are usable for the financing of the overall central government budget); and (ii) downward by the full amount of the shortfall relative to the baseline of external bond placement by the MOPF.

External Program and MOPF Disbursements—Baseline Projections (in million euros)[1]

	2013			2014	
	June actual	September PC	December PC	March Indicative	June Indicative
Cumulative change under external program	0	0	0	0	0
Cumulative change in external MOPF bond placement	1,122	1,122	2,322	1,000	1,000

[1]Flows are cumulative from the beginning of the same calendar year (e.g., June 2013 figure is cumulative from January 1, 2013).

B. Consultation Mechanism on the 12-Month Rate of Inflation

9. The quarterly consultation bands around the 12-month projected rate of inflation in consumer prices (as measured by the headline consumer price index (CPI) published by the Romanian Statistical Institute), are specified below. Should the observed year-on-year rate of CPI inflation fall outside the outer bands specified below, the authorities will complete a consultation with the IMF on their proposed policy response before requesting further purchases under the program. In addition, the NBR will conduct discussions with IMF staff should the observed year-on-year rate of CPI inflation fall outside the inner bands specified for the end of each quarter in the table below.

Inflation Consultation Band

	2013			2014	
	June actual	Sept. target	Dec. target	March indicative	June indicative
Outer band (upper limit)		5.1	5.3	4.6	5.0
Inner band (upper limit)		4.1	4.3	3.6	4.0
Actual / *Center point*	5.4	*3.1*	*3.3*	*2.6*	*3.0*
Inner band (lower limit)		2.1	2.3	1.6	2.0
Outer band (lower limit)		1.1	1.3	0.6	1.0

C. Performance Criterion on General Government Balance

10. The budget deficit will be monitored quarterly through the cash balance of the general government in GFS 1986 classification. Consistent with the national methodology, revenues and spending for EU funds will be treated on an accrual basis. Any privatization receipts will be treated below the line item. The authorities will consult with IMF staff on corrective measures in the event of shortfalls in government revenue and financing. The 2014 budget will be prepared according to the GFSM 2001 methodology. The 2013 fiscal execution data will be presented in both GFSM 2001 and the methodology described above.

Cumulative Floor on General Government Balance[1]

	(In millions of lei)
End-June 2013 (actual)	-6,621
End-September 2013 (performance criterion)	-9,181
End-December 2013 (performance criterion)	-14,700
End-March 2014 (indicative)	-4,000
End-June 2014(indicative)	-6,200

[1] Cumulative figure during calendar year (e.g., June 2013 figure is cumulative from January 1, 2013).

11. The cumulative floor on the general government balance will be adjusted downward by the spending on national cofinancing of EU funded projects (excluding cofinancing from the top-up funds) exceeding 4,221 million RON at end-September 2013 and 5,886 million RON at end-December 2013, up to a limit of 600 million RON.

12. The Ministry of Public Finance (MOPF) will also provide monthly data to measure the deficit from below the line. The balance of the general government measured from below the line will include:

+ (i) net external financing, excluding valuation gains and losses;
+ (ii) change in net domestic credit from the financial system, excluding valuation gains and losses from deposits denominated in foreign currency and including adjustments for;
 + (a) received EU funds not yet spent (advance payments);
 + (b) claims of the government on EU funds;
 + (c) property fund obligations not yet paid;
+ (iii) change in the stock of issued government securities, net of valuation changes;
+ (iv) net changes in other financing;
 of which: (a) temporary financing for EU projects;
 (b) reimbursement payments from EU for the EU projects

The data on the beginning and ending balance of the Treasury account will also be provided.

13. If the difference between the general government deficit measured from above the line and from below the line is larger than lei 200 million each quarter during 2013 and 2014, the MOPF will consult with IMF staff.

D. Indicative Target on the Stock of Net Treasury Loans for EU- funded Projects

14. The Ministry of Public Finance may provide net loans from the Treasury for EU funded projects, defined as the temporary financing for EU structural and cohesion fund projects minus the reimbursements from EU for the EU structural and cohesion fund projects. The net stock outstanding at the end of each quarter cannot exceed 3 billion RON (indicative target).

E. Performance Criterion Limiting the Issuance of Government Guarantees to the Non-Financial Private Sector and Public Enterprises

15. The issuance of general government guarantees to the nonfinancial private sector and public enterprises will be limited during the program period. The ceilings are specified in the table below.

Ceiling on New General Government Guarantees Issued from end 2008 Until:	(In billions of lei)
End-June 2013 (actual)	10.9
End-September 2013 (performance criterion)	16
End-December 2013 (performance criterion)	16
End-March 2014 (indicative)	18
End-June 2014 (indicative)	18

F. Performance Criterion on the Stock of Domestic Arrears by the Central Government and Social Security System

16. The performance criterion established on the stock in domestic payments arrears of the central government and social security sector (as defined in ¶3 above) contemplates their elimination during the program period. The stock will be measured net of intergovernmental arrears, but both gross and net arrears will be reported by the government. In case of need, the government will take corrective measures to prevent the accumulation of new spending arrears. For the purpose of the program, arrears mean accounts payable past due date by 90 days (in line with ESA95 definitions for expenditures). The authorities will consult with IMF staff if new arrears are disputed following an audit by the Central Harmonisation Unit for Financial Management and Control Systems. As a memorandum item, arrears of central government hospitals will be reported separately.

Stock of Central Government and Social Security Arrears	(In billions of lei)
End-June 2013 (actual)	.035
End-September 2013 (performance criterion)	.02
End-December 2013 (performance criterion)	.02
End-March 2014 (indicative)	.02
End-June 2014 (indicative)	.02

G. Continuous Performance Criteria on Non-Accumulation of External Payments Arrears by the General Government

17. The general government will not accumulate external payment arrears during the program period. For the purposes of this performance criterion, an external payment arrear will be defined as a payment by the general government that has not been made within seven days of falling due. The performance criterion will apply on a continuous basis.

H. Indicative Target on General Government Current Primary Spending

18. The indicative target on current primary expenditure of the general government is defined as spending on personnel, goods and services excluding EU funds (specified under external grant category), subsidies, transfers to public entities, pensions (social security budget in social assistance category), state aid and other spending in other transfers category, Reserve Fund, and other expenditure as classified in the monthly reporting tables. Actual data (to which the target will be compared) should include payments related to arrears reduction plans and spending funded through the clawback tax.

Cumulative Change in General Government Current Primary Expenditures[1]	(In millions of lei)
End-June 2013 (actual)	70.412
End-September 2013 (performance criterion)	106.300
End-December 2013 (performance criterion)	147.509
End-March 2014 (indicative)	36.700
End-June 2014 (indicative)	74.400

[1] Cumulative figure during calendar year (e.g., June 2013 figure is cumulative from January 1, 2013).

I. Indicative Target on Local Government Arrears

19. The indicative target on the stock of domestic payments arrears of local governments contemplates no accumulation of new arrears and their reduction during the program period. In case of need, the government will take corrective measures to prevent the accumulation of new spending arrears. For the purpose of the program, arrears mean accounts payable past the due

date by 90 days (in line with ESA95 definitions for expenditures). As a memorandum item, arrears of local government hospitals will be reported separately on a quarterly basis.

Stock in Local Government Arrears	(In billions of lei)
End-June 2013 (actual)	.143
End-September 2013 (performance criterion)	.300
End-December 2013 (performance criterion)	.300
End-March 2014 (indicative)	.300
End-June 2014 (indicative)	.300

J. Absorption of EU Funds

20. The EU funds contribution mentioned in the MoU conditionality is to be measured taking into account the eligible expenditure from both the structural and cohesion funds (SCF) and the European Agricultural Fund for Rural Development (EAFRD).

K. Monitoring of Public Enterprises

21. Public enterprises are defined as all companies including research institutes, incorporated under Law 31/1990 (as amended) and *regii autonome,* organized under Law 15/1990 (as amended), with a cumulative public capital share of 50 percent or more, held directly or indirectly by the central or local governments.

22. A quarterly indicative target for the third and fourth quarters of 2013 is set on the aggregate operating balance net of subsidies and the effects of one-off financial or accounting operations, accumulated per calendar year, of the following public enterprises: C.N. Căi Ferate CFR S.A. and five of its subsidiaries (S.C. Interventii Feroviare S.A., Informaticã Feroviarã S.A., S.C. Sere şi Pepiniere S.A., S.C. Electrificare CFR S.A., and S.C. Întreţinere Mecanizata S.A.) S.N. de Transport Feroviar de Marfă "CFR Marfă" S.A. and its subsidiary (S.C. Întreţinere şi Reparaţii Locomotive şi Utilaje S.A.), and S.N. Transport Feroviar de Călători "CFR Călători" S.A. and its subsidiary (S.C. de reparaţii locomotive C.F.R. SCRL Braşov S.A.). The data shall be reported with operating results by firm. The targets will be as follows:

Floor on Cumulative Operating Balance[1]	(In billions of lei)
End-December 2012 (actual)	-3.3
End-June 2013 (preliminary)	-1.0
End-September 2013 (target)	-1.6
End-December 2013 (target)	-2.3
End-March 2014 (indicative)	-0.5
End-June 2014 (indicative)	-0.8

[1] Cumulative figure during calendar year (e.g., June 2013 figure is cumulative from January 1, 2013).

23. In case one of these enterprises is placed into insolvency procedures, which occurs when it is recorded in the trade registry that the enterprise was placed into insolvency or liquidation procedures, or its majority share is privatized, which occurs when payment is received from an entity, in which the government does not have a controlling interest, in exchange for the majority shares of the enterprise, the aggregate target listed above will not be adjusted by the original operating balance target for this firm. If any of the companies listed above is split into a new company, both companies will remain under monitoring. If some of the above companies are merged, the newly created companies will remain under monitoring.

24. A quarterly indicative target for the third and fourth quarters of 2013 is set on the stock of outstanding payments of public enterprises owned by the central government that were not made by the due date. The stock excludes outstanding payments past due of those public enterprises owned by the central government that are already under insolvency or liquidation procedures. The beginning date for measuring the stock is December 31, 2012. The data shall be reported at the firm level. The targets will be as follows:

Ceiling on Outstanding Payments Past Due	(In billions of lei)
End-December 2012 (actual)	12.6
End-June 2013 (preliminary)	8.2
End-September 2013 (target)	7.5
End-December 2013 (target)	5.6
End-March 2014 (indicative)	4.7
End-June 2014 (indicative)	3.7

The end-December 2013 target will be adjusted upward by 1.2 billion lei in the event that the CFR Marfa majority prioritization is not concluded, i.e., the conditions precedent in the sale-purchase agreement were not completed and hence the transfer of a majority of shares in CFR Marfa in exchange for payment from the strategic investor could not take place by December 31, 2013.

25. In case one of these enterprises is placed into insolvency procedures, which occurs when it is recorded in the trade registry that the enterprise was placed into insolvency or liquidation procedures, or its majority share is privatized, which occurs when payment is received from an entity, in which the government does not have a controlling interest, in exchange for the majority shares of the enterprise, the aggregate target listed above will not be adjusted by the outstanding payments past due for this firm. If any of the companies listed above is split into a new company, both companies will remain under monitoring. If some of the above companies are merged, the newly created companies will remain under monitoring. However, outstanding payments past due accumulated and reported by active companies while they are under insolvency procedures will be included in the target.

L. Reporting Requirements for the Prior Actions

26. Completion of the prior action related to Hidroelectrica requires receipt by the IMF of the resolution adopted by a general shareholders' meeting with the majority votes of the Department of Energy that the shareholders of (1) Hidroelectrica reconfirmed members of the current board, while procedures for appointing a new board are undertaken in accordance with Government Emergency Ordinance 109/2011; and (2) approved a model for the contract mandate of the current supervisory board without limiting the powers generally given to supervisory boards by the Romanian companies law 31/1990. Completion of the prior action related to Romgaz requires the receipt of a signed letter from the Minister of the Budget of the Ministry of Public Finance indicating the steps taken to clarify the tax treatment of securities of Romanian firms traded on foreign exchanges and a copy of the legal document containing the clarification.

M. Reporting Requirements

27. Performance under the program will be monitored from data supplied to the IMF and EC by the NBR and the MOPF as outlined in the table below. The authorities will transmit promptly to IMF and EC staff any data revisions as well as other information necessary to monitor the arrangement with the IMF and EC.

Romania: Data Provision to the IMF and EC

Item	Periodicity
To be provided by the Ministry of Public Finance	
Preliminary monthly data on general government accounts, including on GFSM 2001 basis	Monthly, on the 25th day of the following month
Quarterly final data on net lending from the Treasury for EU funded projects	Quarterly, on the 5th day past the test date
Preliminary monthly data providing a breakdown of general government expenditures on post-accession EU projects (co-financing, non-eligible spending, corrections, reimbursable funds, and EU top-ups)	Monthly, on the 25th day of the following month
Quarterly final data on general government accounts, including public enterprises as defined by ESA95 and breakdown of general government spending on EU projects	Quarterly cash data, on the 35th day past the test date; Quarterly accrual data, on the 55th day past test date
The budget deficit of the general government using ESA95 definition	Quarterly, with a lag of three months
Preliminary data on below-the-line financing for the general government	Monthly, with a lag of no more than 35 days past the test date
Final quarterly data on below-the-line financing for the general government, including details of the domestic and external issuances and repayments (by currency)	Quarterly, no later than 45 days past the test date
Total accounts payable and arrears of the general government, including local governments and central and local government hospitals	Preliminary monthly, within the next month. Quarterly, within 55 days
Progress report on the status of the audit of the stock of the disputed local arrears.	Quarterly, no later than 45 days past the end of each quarter

Data on payment delays and arears with respect to drug reimbursement by the National Health Insurance House (pharmacies and wholesale), with a particular view on the implementation of directive 7	Monthly, at the end of each month
Stock of the central government external arrears	Daily, with a lag of not more than seven days
Public debt and new guarantees issued by the general government	Monthly, within one month
Preliminary monthly data on general government primary spending, net of EU disbursements	Preliminary monthly data within 25 days
Final quarterly data on general government primary spending, net of EU disbursements	Quarterly, within 35 days from the test date
Time lines showing the expected completion dates for key steps leading to the launching of the initial public offerings of the energy state-owned companies	Quarterly, within 10 days of the end of each quarter
Preliminary data on the operating balance, profits, stock of outstanding payments past due, and personnel expenditures for each key public enterprise as defined in ¶22	Monthly, within 30 days
Final data on the operating balance, profits, stock of outstanding payments past due, and personnel expenditures for each key public enterprise as defined in ¶22	Quarterly, end-May for the previous year and end-August for first half of the current year
Preliminary data on the stock of outstanding payments past due for each public enterprise as defined in ¶21	Quarterly, within 35 days
Final data on the stock of outstanding payments past due for each public enterprise as defined in ¶21	Quarterly, end-May for the previous year and end-August for first half of the current year

Data on EU project grants (reimbursements and advances), capital expenditures and subsidies covered by EU advances or eligible for EU reimbursement on EU supported projects specifically agreed with the EU	Monthly, within three weeks of the end of each month
The balance of the TSA in RON	Monthly, within two weeks of the end of each month
The balance of the two foreign currency accounts used for budget financing and public debt redemption purposes (average, and end-of-period)	Monthly, within two weeks of the end of each month
The balance of the privatization receipts registered in the account of the State Treasury, details on any claims on these receipts and projected net outflows.	Monthly, within two weeks of the end of each month
Reporting of progress in the implementation of the Romanian public administration's functional review	Quarterly, to be sent two weeks before each mission for each of the 12 ministries
Data on subsidies by ministries	Quarterly, one month after the end of the quarter. Additional reporting one week before review mission
Data on public employment and status of ordinance 77/2013 implementation, in particular numbers of staff reductions at central government ministries and staff increases at local governments	Monthly, at the end of each month
To be provided by the National Bank of Romania	
NIR data, by components, in both program and actual exchange rates	Weekly, each Monday succeeding the reporting week and with a 3 working day lag in the case of end-quarter data
Monetary survey data in the format agreed with IMF and EC staff	Monthly, within 30 days of the end of the month

The schedule of contractual external payments of the *banking sector* falling due in the next four quarters, interest and amortization (for medium and long-term loans)	Monthly, 45 days after the end of each month
The schedule of contractual external payments of the *corporate sector* falling due in the next four quarters interest and amortization (for medium and long-term loans)	Monthly, 45 days after the end of each month
The stock of short-term external debt of banks and corporate	Monthly, 45 days after the end of each month
Balance of payments in the IMF format currently used to report	Monthly, 45 days after the end of each month
Exposure (deposits, loans, subordinated loans) of (i) foreign parent banks to their subsidiaries in Romania; (ii) IFI and (iii) other creditors to banks in Romania (by national and foreign currency).	Monthly, 20 days after the end of each month
Detailed bank-by-bank data on restructured loans to households and corporates including SOEs	Quarterly, 45 days after the end of each quarter
Financial soundness indicators[1]	Monthly, 45 days after the end of each month
Foreign currency reserves including information on FX market interventions and swaps by the NBR	Bi-weekly
The IMF and the EC shall be immediately informed in case of sudden loss of reserves exceeding EUR 600 million	Immediately, upon occurrence

[1] Data on solvency should be provided on quarterly basis.

INTERNATIONAL MONETARY FUND

ROMANIA

ASSESSMENT OF THE RISKS TO THE FUND AND THE FUND'S LIQUIDITY POSITION

September 12, 2013

Approved By
Andrew Tweedie and Vivek Arora

Prepared by the Finance and Strategy, Policy, and Review Departments

CONTENTS

INTRODUCTION

1. **This note assesses the risks to the Fund arising from the proposed Stand-By Arrangement (SBA) for Romania and its effects on the Fund's liquidity, in accordance with the policy on exceptional access.**[1] The authorities are requesting a 24 month SBA with access equivalent to SDR 1,751.3 million (170 percent of quota). Disbursements are largely evenly phased with SDR 194.7 million (18.9 percent of quota) available upon approval, followed by seven identical amounts, and a final disbursements of SDR 193.7 million (Table 1); the program envisages three quarterly reviews followed by two semi-annual reviews; semi-annual reviews would be combined with continuous and quarterly performance criteria (PCs) and quarterly consultation bands on inflation. Quarterly missions are also expected. The authorities intend to treat the proposed SBA as precautionary.

Table 1. Romania: Proposed SBA—Access and Phasing

			Percent of quota	
Availability	Date 1/	SDR mn	Purchase	Cumulative
2013	September (approval)	194.70	18.9	18.9
	December	194.70	18.9	37.8
2014	March	194.70	18.9	56.7
	June	194.70	18.9	75.6
	September	194.70	18.9	94.5
	December	194.70	18.9	113.4
2015	March	194.70	18.9	132.3
	June	194.70	18.9	151.2
	September	193.74	18.8	170.0
	Total	1,751.34	170.0	

Source: Finance Department.

1/ Starting in December 2013, purchases will depend on the completion of a review and/or observance of performance criteria as established under the Program.

BACKGROUND

2. **Romania has had an extensive financial relationship with the Fund (Table 2).** Romania is currently the fourth largest Fund borrower, with credit outstanding at SDR 7,467.9 million as of end-July 2013. Since 1991 a total of nine SBAs have been approved. In May 2009, an

[1] See paragraph 5 of Decision No. 14064-(08/18), adopted 2/22/2008, as amended, and The Acting Chair's Summing Up of the Review of Access Policy Under the Credit Tranches and the Extended Fund Facility, and Access Policy in Capital Account Crises—Modifications to the Supplemental Reserve Facility and Follow-Up Issues Related to Exceptional Access Policy (BUFF/03/28, 3/5/03).

SBA with access equivalent to SDR 11,443 million (1,111 percent of quota), the largest at the time, was approved. Subsequently, the Fund approved the 2011 SBA with access equivalent to SDR 3,090.6 million (300 percent of quota), which was treated as precautionary by the authorities. Building on the achievements of the previous arrangement, it aimed at supporting further fiscal consolidation while undertaking deeper economic reforms, providing an effective mechanism to insure against possible future shocks while aiding the authorities in maintaining policy discipline. Romania completed the final reviews under the precautionary SBA on June 26, 2013. All obligations to the Fund under previous arrangements have been met in a timely manner.

Table 2. Romania: IMF Financial Arrangements, 1991-2020 1/
(In millions of SDRs, unless otherwise indicated)

Year	Date of		Amount Agreed		Amount Drawn	Purchases	Repurchases	Fund Exposure 2/
	Approval	Expiration / Cancellation	in SDR millions	As a Percent of Quota				
1991	11-Apr-91	10-Apr-92	380.5	72.7	318.1	565.8		565.8
1992	29-May-92	28-Mar-93	314.0	41.6	261.7	338.5	153.4	750.9
1993								750.9
1994	11-May-94	22-Apr-97	320.5	42.5	94.3	245.1	89.6	906.4
1995						37.7	245.8	698.3
1996							245.4	453.0
1997	22-Apr-97	21-May-98	301.5	40.0	120.6	120.6	98.4	475.2
1998							92.3	382.8
1999	05-Aug-99	28-Feb-01	400.0	38.8	139.8	53.0	102.0	333.8
2000						86.8	72.9	347.7
2001	31-Oct-01	15-Oct-03	300.0	29.1	300.0	52.0	91.7	308.0
2002						82.7	75.7	314.9
2003						165.3	79.6	400.6
2004	07-Jul-04	06-Jul-06	250.0	24.3	0.0		115.3	285.4
2005							102.8	182.6
2006							113.7	68.9
2007							68.9	
2008								
2009	04-May-09	03-May-11	11,443.0	1,110.8	10,569.0	6,088.0		6,088.0
2010						3,712.0		9,800.0
2011	25-Mar-11	15-Mar-13	3,090.6	300.0	0.0	769.0		10,569.0
2012							1,307.3	9,261.8
2013 3/	*25-Sep-13*	*24-Sep-2015*	*1,751.3*	*170.0*		*389.4*	*4,051.8*	*5,599.4*
2014 3/						*778.8*	*3,881.1*	*2,497.1*
2015 3/						*583.1*	*1,232.8*	*1,847.4*
2016 3/							*120.5*	*1,727.0*
2017 3/							*340.7*	*1,386.2*
2018 3/							*705.7*	*680.6*
2019 3/							*534.9*	*145.7*
2020 3/							*145.7*	*0.0*

Source: Finance Department.

1/ All Stand–By Arrangements.
2/ As of end-December.
3/ Figures under the proposed Stand-By Arrangement are in italics.

3. Romania's public sector external debt remains moderate and is owed mainly to multilateral institutions (Table 3). Total external debt has exceeded 70 percent of GDP over the last three years and stood at 75 percent of GDP at end-2012. Almost two-thirds of total external debt was owed by the private sector—mainly by non-monetary institutions. Public sector external debt remains at a moderate level of 26.5 percent of GDP at end-2012, despite its rapid increase since the global crisis erupted in 2008. The majority of external debt is long-term debt.

Romania's total and public external debt are in the medium range compared to recent exceptional access cases (Figure 1).

4. Romania's external debt service burden is high, but only a quarter of it is borne by the public sector. A debt service ratio of about 87 percent of exports of goods and services places Romania at the higher end of the most recent exceptional access cases (Figure 1, Panel C). The debt service ratio is substantially higher than the one for the 2009 and 2011 SBAs. About 29 percent of external debt service is borne by the public sector.

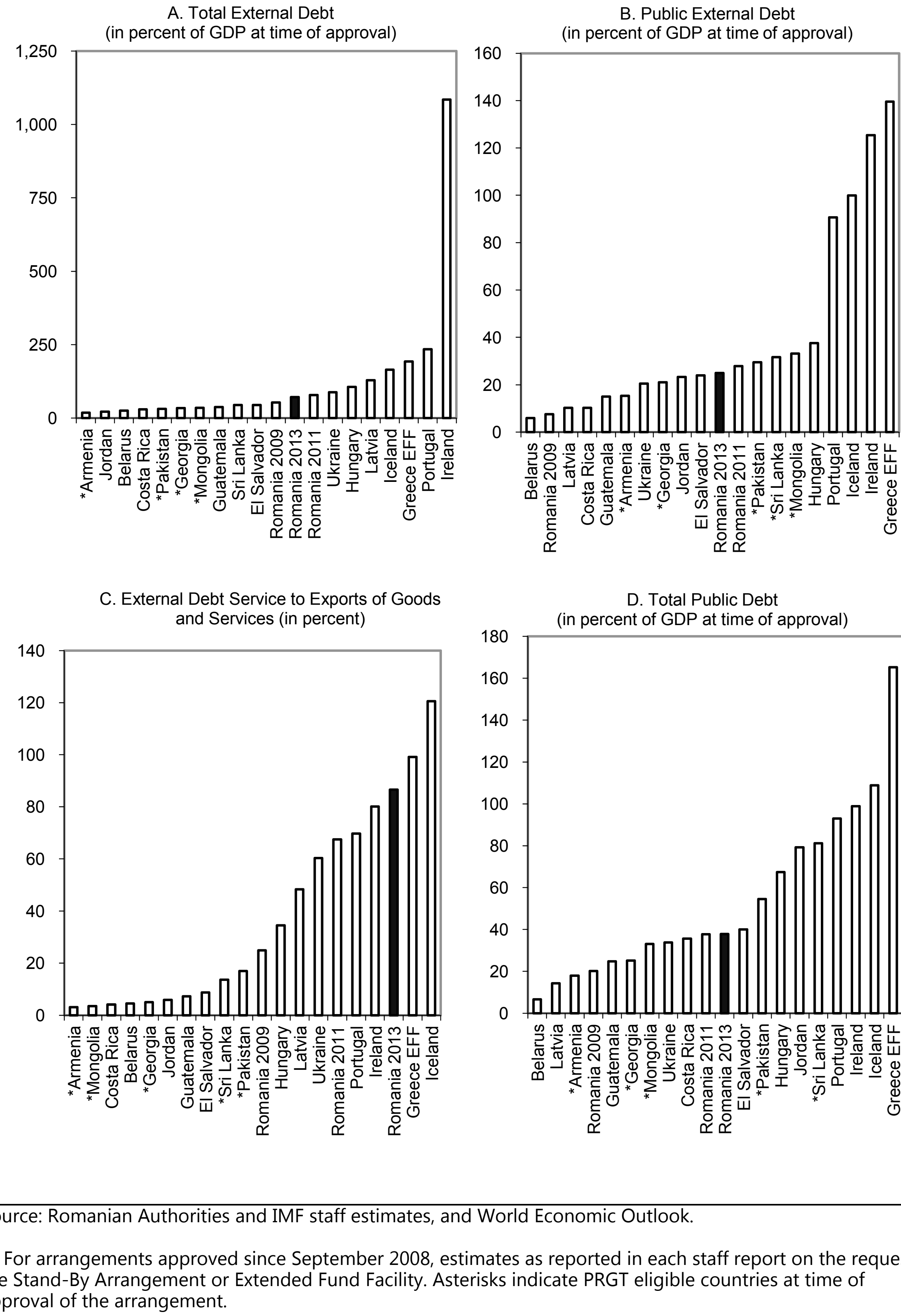
Table 3. Romania: Total External Debt, 2007-2012 1/

	2007	2008	2009	2010	2011	2012
	(In Millions of U.S. Dollars)					
Total External Debt	85,473	98,564	118,553	122,216	130,108	130,579
of which:						
Public	15,286	15,197	29,055	37,622	43,882	46,091
Loans	6,795	7,340	20,638	28,621	33,261	31,404
Multilateral	6,680	7,251	20,557	28,540	33,199	31,346
Bilateral	115	89	82	81	62	58
Bonds	3,556	3,596	4,049	3,832	5,664	11,159
Private	70,187	83,367	89,498	84,594	86,226	84,488
Short-term	28,622	27,498	21,715	23,841	27,426	25,195
Long-term	40,461	55,554	67,524	60,587	58,797	59,141
	(In Percent of GDP)					
Total External Debt	47.0	51.8	68.7	74.3	75.2	75.1
of which:						
Public	8.4	8.0	16.8	22.9	25.3	26.5
Loans	3.7	3.9	12.0	17.4	19.2	18.1
Multilateral	3.7	3.8	11.9	17.4	19.2	18.0
Bilateral	0.1	0.0	0.0	0.0	0.0	0.0
Bonds	2.0	1.9	2.3	2.3	3.3	6.4
Private	38.6	43.8	51.8	51.4	49.8	48.6
Short-term	15.7	14.4	12.6	14.5	15.8	14.5
Long-term	22.3	29.2	39.1	36.8	34.0	34.0

Source: Romanian authorities and IMF staff estimates.

1/ End of year unless otherwise indicated.

Figure 1. Debt Ratios for Recent Exceptional Access Arrangements 1/



Source: Romanian Authorities and IMF staff estimates, and World Economic Outlook.

1/ For arrangements approved since September 2008, estimates as reported in each staff report on the request of the Stand-By Arrangement or Extended Fund Facility. Asterisks indicate PRGT eligible countries at time of approval of the arrangement.

THE NEW STAND–BY ARRANGEMENT—RISKS AND IMPACT ON FUND'S FINANCES

A. Risks to the Fund

5. Access under the proposed arrangement is 170 percent of quota; cumulative access for Romania would exceed the cumulative access limit but would be low compared to other exceptional access cases on a number of indicators.[2]

- Access of SDR 1,751.3 million under the proposed arrangement would be low compared to recent exceptional access cases (Figure 2, Panel A).
- If all purchases and repurchases were made as scheduled, Romania's outstanding use of GRA resources would peak at 644 percent of quota after the first purchase, and would fall continuously to reach zero in 2020 (Figure 3).
- If all purchases were made as scheduled, the Fund's peak exposure to Romania in terms of GDP, gross international reserves and total external debt would be towards the lower end of the range compared to recent exceptional access cases (Figure 4). If all purchases were made as scheduled, GRA credit outstanding to Romania would be equivalent to 4.6 percent of GDP and 18.7 percent of gross international reserves at end-2013 (Table 4). Outstanding use of GRA resources would represent 6.4 percent of total external debt, and 18.3 percent of public external debt.

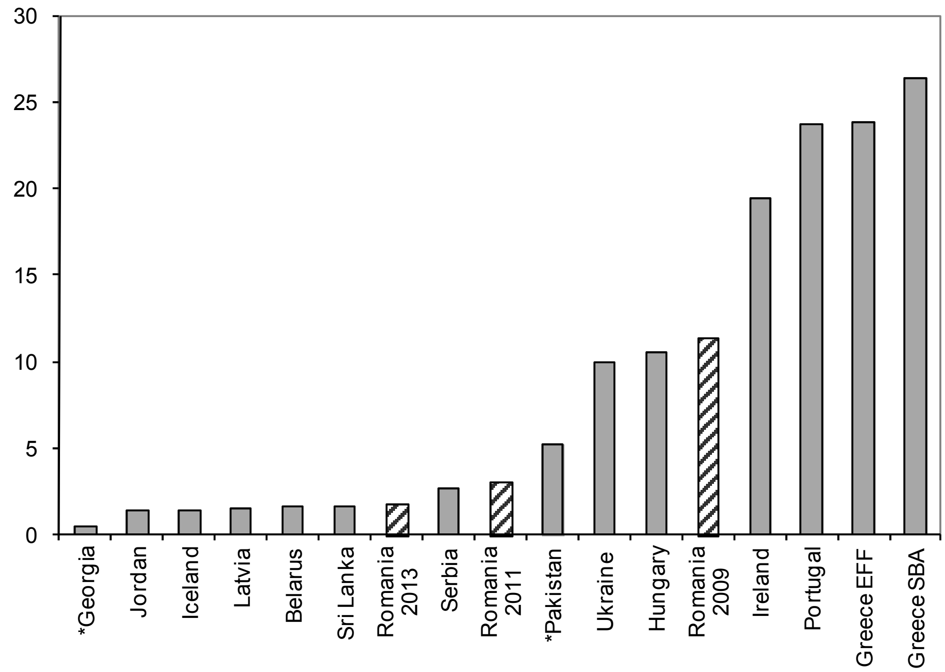
6. If all purchases were made as scheduled, Romania's peak debt service burden to the Fund would be significant. Romania's projected debt service to the Fund would peak at SDR 3,967 million in 2014, reflecting the purchases made under the 2009 SBA. Peak debt service to the Fund as a share of exports of goods and services, at 7.7 percent, would be above the median share for most recent exceptional access cases, but comparable to the burden under the 2011 SBA (see Figure 4).[3] Peak total external debt service in percent of exports of goods and services of close to 87 percent in 2013 would place Romania at the higher end relative to most recent exceptional access cases.

[2] Cumulative access for Romania is expected to fall below 600 percent of quota in November 2013.

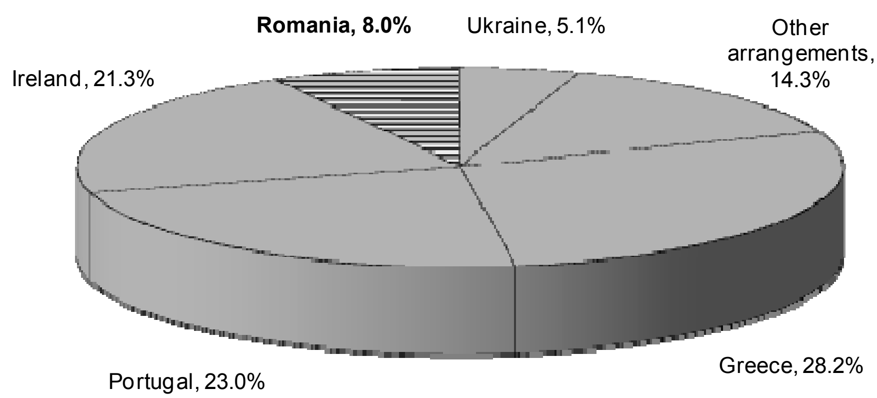
[3] Debt service to the Fund is calculated assuming that all repurchases are made as scheduled, i.e., each purchase is repurchased in eight quarterly installments, beginning in 3¼ years after each purchase and ending after 5 years. As for level-based surcharges, they are calculated according to the current schedule: 100 basis points for credit outstanding over 200 percent of quota and 200 basis points for credit outstanding above 300 percent of quota.

Figure 2. Exceptional Access Levels and Credit Concentration

A. Total Access of Recent Exceptional Access Arrangements 1/
(In billions of SDRs)



B. Credit Concentration of Fund GRA Exposure 2/
(As a percentage of total credit outstanding)



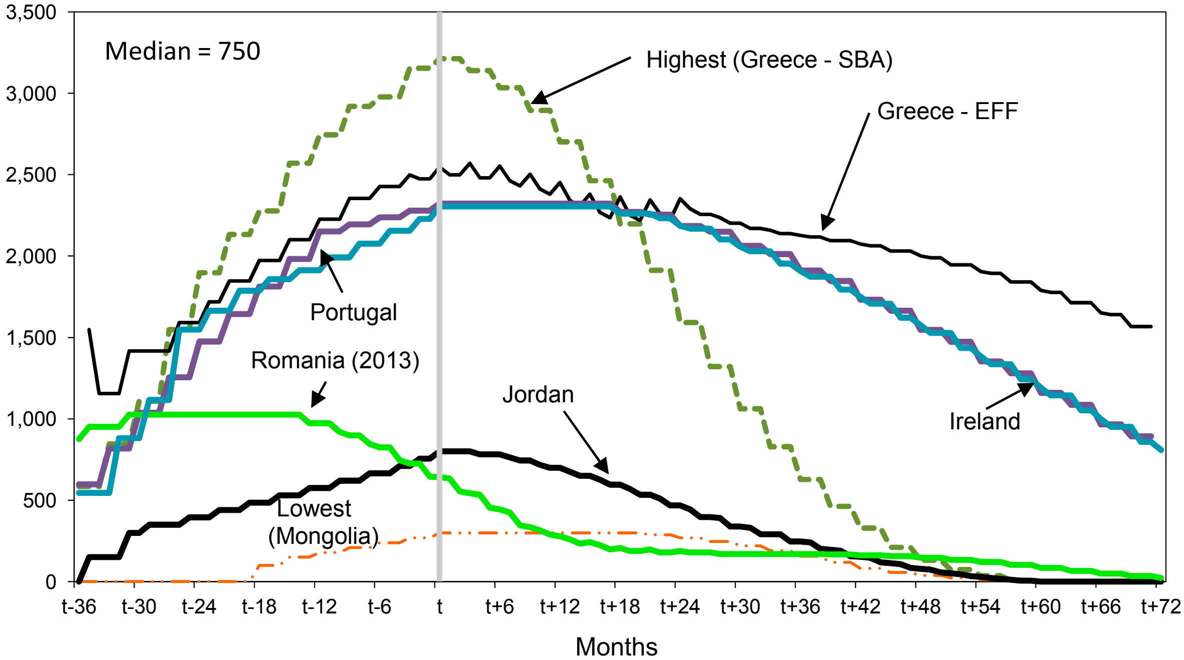
Source: Finance Department.

1/ Does not include FCL arrangements. Asterisks indicate PRGT eligible countries at the time of approval of the arrangement.
2/ Credit outstanding as of August 28, 2013 plus first purchase under the proposed arrangement with Romania.

Figure 3. Fund Credit Outstanding in the GRA around Projected Peak Borrowing 1/

(In percent of quota)

Approved Exceptional Access Cases since September 2008 2/

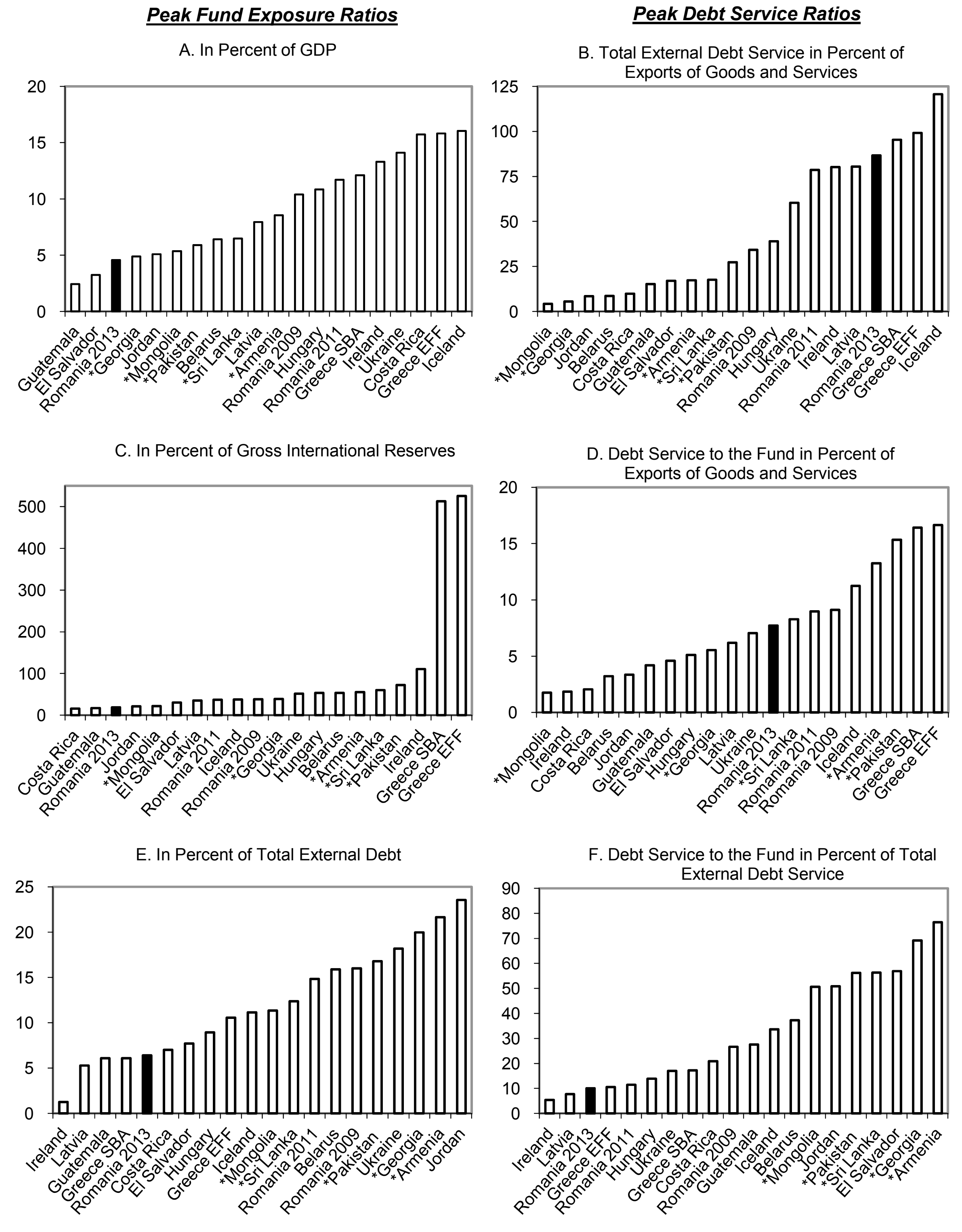


Source: IFS, Finance Department, and IMF staff estimates.

1/ Projected peak at time of approval. Peak borrowing "*t*" is defined as the highest level of credit outstanding for a member.

2/ Median credit outstanding at peak is 750 percent of quota; average is 997 percent of quota.

Figure 4. Peak Fund Exposure and Debt Service Ratios for Recent Exceptional Access Cases 1/



Source: Romanian authorities, IMF staff estimates, and World Economic Outlook.

1/ Asterisks indicate PRGT eligible countries at the time of approval of the arrangement.

Table 4. Romania—Capacity to Repay Indicators 1/

	2013	2014	2015	2016	2017	2018	2019	2020
Exposure and Repayments (In SDR millions)								
GRA credit to Romania 2/	5,599.4	2,497.1	1,847.4	1,727.0	1,386.2	680.6	145.7	0.0
(In percent of quota)	(543.5)	(242.4)	(179.3)	(167.6)	(134.6)	(66.1)	(14.1)	(0.0)
Charges due on GRA credit 3/	47.8	85.6	26.1	19.9	18.7	14.1	6.7	1.8
Debt service due on GRA credit 4/	1,759.4	3,966.7	1,258.9	140.4	359.5	719.8	541.6	147.5
Debt and Debt Service Ratios 5/								
In percent of GDP								
Total external debt	71.3	70.4	67.6	65.0	62.9	60.0	-	-
External debt, public	24.9	25.0	24.6	23.4	22.6	20.9	-	-
GRA credit to Romania	4.6	2.0	1.4	1.2	0.9	0.4	-	-
Total external debt service	34.4	31.0	27.0	24.2	23.4	22.6	-	-
Public external debt service	9.9	7.9	4.7	2.7	2.6	2.5	-	-
Debt service due on GRA credit	1.4	3.1	0.9	0.1	0.2	0.4	-	-
In percent of Gross International Reserves								
Total external debt	293.2	325.6	345.7	330.1	318.7	311.0	303.5	296.2
External debt, public	102.2	115.8	125.7	118.8	114.4	108.4	105.7	103.2
GRA credit to Romania	18.7	9.0	7.0	6.1	4.5	2.1	-	-
In percent of Exports of Goods and Services								
Total external debt service	86.6	76.8	66.4	59.2	56.5	53.9	51.5	49.2
Public external debt service	24.9	19.6	11.6	6.5	6.2	6.0	5.7	5.4
Debt service due on GRA credit	3.6	7.7	2.3	0.2	0.6	1.0	-	-
In percent of Total External Debt								
GRA credit to Romania	6.4	2.8	2.0	1.8	1.4	0.7	-	-
In percent of Total External Debt Service								
Debt service due on GRA credit	4.2	10.0	3.4	0.4	1.0	1.9	-	-
In percent of Total Public External Debt								
GRA credit to Romania	18.3	7.8	5.6	5.1	4.0	2.0	-	-
In percent of Total Public External Debt Service								
Debt service due on GRA credit	14.5	39.4	19.7	3.7	9.0	17.3	-	-

Sources: Romanian authorities, Finance Department, World Economic Outlook, and IMF staff estimates.

1/ Assumes the last purchase under the existing arrangement is made and the schedule of purchases indicated in Table 1.
2/ Repurchases follow the obligations schedule.
3/ Includes GRA basic rate of charge, surcharges and service fees.
4/ Includes charges due on GRA credit and payments on principal.
5/ Staff projections for external debt, GDP, gross international reserves, and exports of goods and services, as used in the staff report that requests the proposed SBA.

B. Impact on the Fund's Liquidity Position and Risk Exposure

7. The impact of the proposed arrangement on the Fund's liquidity would be small, and would marginally increase the Fund's credit risk exposure to Romania.

- **The proposed arrangement would reduce the Fund's modified forward commitment capacity (FCC) by about 0.7 percent (Table 5).** Commitments under the proposed arrangement would reduce the FCC, which currently stands at SDR 264 billion, by about SDR 1.8 billion.[4]

- **Potential GRA exposure to Romania would represent about 58 percent of the Fund's current level of precautionary balances (Table 5).** The GRA commitment to Romania under the proposed arrangement represents 15 percent of the Fund's current level of precautionary balances. Fund exposure to Romania (assuming all purchases and repurchases are made as scheduled), in terms of the current level of precautionary balances, will fall continuously from about 58 percent upon approval to about 18 percent at the end of the program.

- **Were Romania to accrue arrears on charges under the proposed arrangement, the Fund's burden sharing capacity would be severely strained (Table 5).[5]** Charges on the GRA obligations would equal about SDR 47.8 million in 2013, about 6 times the current estimated residual burden sharing capacity of the Fund.[6] Charges would peak in 2014 at SDR 85.6 million if purchases were made as scheduled.

- **If the first purchase is made, Fund credit to Romania would represent 8 percent of total GRA credit outstanding, making Romania the fourth largest user of Fund resources (Figure 2, Panel B).[7]** In terms of size, the proposed arrangement would be small, but it would come on top of already sizeable exposure. The share of the top five users of Fund resources of total outstanding credit would increase only marginally (see Table 5).

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[4] The FCC measures the Fund's capacity to make new credit commitments. It reflects resources available under the NAB during the current NAB activation period. The FCC does not include about US$461 billion in bilateral pledges from members to boost IMF resources. These resources will only be counted towards the FCC once: (i) individual bilateral agreements are effective and (ii) the associated resources are available for use by the IMF, in accordance with the borrowing guidelines and the terms of these agreements.

[5] Under the burden-sharing mechanism, the financial consequences for the Fund that stem from the existence of overdue financial obligations are shared between creditors and debtors through a decrease in the rate of remuneration and an increase in the rate of charge, respectively. The mechanism is used to compensate the Fund for a loss in income when debtors do not pay charges. The Executive Board has set a floor for remuneration at 85 percent of the SDR interest rate. No corresponding ceiling applies to the rate of charge.

[6] Burden sharing capacity has declined recently, despite the increase in credit outstanding, reflecting the steep decline in the SDR interest rate.

[7] Romania is currently the fourth largest user of Fund resources.

Table 5. SBA for Romania—Impact on GRA Finances
(In SDR millions, unless otherwise indicated)

	As of 8/28/2013
Liquidity measures	
Current one-year Forward Commitment Capacity (FCC) 1/	264,611.4
Impact on FCC on approval 2/	1,751.3
Prudential measures	
Fund GRA credit outstanding to Romania 3/	
In percent of current precautionary balances 4/	57.6
In percent of total GRA credit outstanding	8.0
Fund GRA credit outstanding to top five borrowers	
In percent of total GRA credit outstanding	85.6
In percent of total GRA credit outstanding including first Romanian purchase	85.7
Romania's annual GRA charges in percent of Fund's residual burden sharing capacity for 2013	583.8
Memorandum items	
Fund's precautionary balances (FY 2013) 4/	11,500
Fund's residual burden sharing capacity 5/	8.2

Sources: Romanian authorities, Finance Department, World Economic Outlook, and IMF staff estimates.

1/ The FCC measures the Fund’s capacity to make new credit commitments. It reflects resources available under the NAB during the current activation period. The FCC does not include about US$461 billion in bilateral pledges from members to boost IMF resources. These resources will only be counted towards the FCC once: (i) individual bilateral agreements are effective and (ii) the associated resources are available for use by the IMF, in accordance with the borrowing guidelines and the terms of these agreements.
2/ A single country's negative impact on the FCC is defined as the country's sum of Fund credit and undrawn commitments minus repurchases one-year forward.
3/ Projected credit outstanding for Romania at time of approval of the proposed arrangement based on the current repayment schedule and including first drawing.
4/ Precautionary balances exclude amounts in Special Reserves attributable to profits on gold sales in FY2010.
5/ Burden-sharing capacity is calculated based on the floor for remuneration at 85 percent of the SDR interest rate. Residual burden-sharing capacity is equal to the total burden-sharing capacity minus the portion being utilized to offset deferred charges and takes into account the loss in capacity due to nonpayment of burden-sharing adjustments by members in arrears.

ASSESSMENT

8. **The proposed arrangement aims to provide an important policy anchor to support macro-critical structural reforms.** Building on the achievements under the previous programs, the proposed arrangement will provide a reserve buffer against heightened external uncertainty, while aiding the authorities in strengthening Romania’s institutional fiscal framework. It aims to boost Romania’s growth potential and competitiveness through structural reforms, and to foster confidence and facilitate private capital flows by improving policy stability and business climate.

9. There are financial risks associated with the proposed arrangement for Romania. Romania is the Fund's fourth largest borrower and debt service to the Fund will be moderate, particularly during 2013 and 2014. Potential risks to the program that could affect Romania's capacity to repay the Fund include:

- Higher and unexpected volatility in capital markets as well as a sudden reversal of capital flows could affect the capacity of the country to service its external debt, particularly considering its already high external debt service burden.
- Escalation of domestic political tensions, particularly in advance of presidential elections in November 2014 could lead to policy reversals, which could put the attainment of program objectives at risk.
- A deeper recession or renewed financial tension in the euro area would dampen exports, affect foreign investment, and worsen bank deleveraging. In such circumstances, there would also be a risk that foreign banks will be unable to maintain their exposure to Romania.
- Prospects of monetary tightening in advanced economies could trigger capital outflows as investors rebalance their portfolios.

10. These risks are mitigated by the authorities' strong commitment to the program and Romania's sound track record under the 2009 and 2011 SBAs. The authorities are committed to the program which will in turn assist in maintaining policy discipline. Performance under the two preceding SBAs was strong and the proposed arrangement will help to safeguard the gains made. In addition, Romania's excellent track record of servicing external obligations provides comfort that financial obligations to the Fund will be met in a timely manner.

ROMANIA

September 24, 2013

REQUEST FOR A STAND-BY ARRANGEMENT—SUPPLEMENTARY INFORMATION

Approved By
Poul M. Thomsen and Vivek Arora

Prepared By
The European Department

1. **This supplement updates the staff report issued on September 13, 2013 for recent economic and policy developments**. The additional information does not change the thrust of the staff appraisal.

2. **Positive economic growth continues on the strength of exports.** Preliminary estimates indicate that real GDP grew 0.5 percent quarter-on-quarter in the second quarter of 2013 (1.5 percent year-on-year), as robust exports of machinery and transportation equipment offset a contraction in domestic demand. For the first half of 2013, real GDP increased 1.8 percent over the same period in 2012, in line with staff estimates.

3. **Annual inflation fell further to 3.7 percent in August**. Disinflation was faster than expected, reflecting a sharper drop in volatile food prices, particularly for vegetables and fruits. Core inflation remained low at 2.2 percent.

4. **Fiscal revenues underperformed in August**. Recent restructuring efforts at the tax administration agency have undermined collection efforts exacerbating the already weak revenues from a slump in domestic demand. The authorities have tightened discretionary spending and remain committed to taking necessary expenditure measures to achieve the 2013 deficit targets should revenues fail to recover.

5. **Romania raised additional financing on international markets.** Romania issued a €1.5 billion, seven-year euro-denominated bond in mid-September at a yield of 4.77 percent. The authorities had also tapped international markets for $1.5 billion at a U.S. dollar-bond sale in February.

6. **The government completed the prior actions.** The government approved ordinances defining commitments for the commitment control system and prioritization

criteria for public investment projects. It also approved an ordinance broadening the social contributions base through a mandatory tax on rental income of individuals. Through general shareholders meetings of Hidroelectrica, the state-owned hydro-electric power producer, the government empowered the current Board to take decisions in accordance with the Companies law 31/1990. Finally, the authorities clarified the tax treatment of securities bought on foreign stock exchanges for the planned initial public offering (IPO) in Romgaz, the state-owned natural gas producer.

7. Progress was made in fulfilling other commitments under the structural reform agenda proposed in the program. The energy regulator implemented as planned the electricity price increase in September, in line with the price liberalization roadmap, and announced plans to implement the next gas price increase as scheduled on October 1. The authorities also launched and successfully concluded an IPO of 10 percent of the shares in Nuclearelectrica, the state-owned nuclear power generator, and signed a contract with a transaction advisor for an IPO of the majority of the shares in Electrica, the state-owned electricity distributor and supplier.

Table 1. Romania: Proposed Conditionality

	Measure	Target Date
Prior Actions		
1.	Approve a government ordinance to provide standard definitions of commitments for the commitment control system.	Met
2.	Approve a government ordinance defining the prioritization criteria for public investment projects.	Met
3.	Approve a government ordinance to broaden the social contributions base by applying a mandatory tax (health contribution) on rental income of individuals, to be implemented from January 1, 2014.	Met
4.	Authorize, through a General Shareholder's Meeting of Hidroelectrica, the current interim board to take decisions in accordance with law 31/1990, while it seeks to appoint a professional board in accordance with the SOE Corporate Governance ordinance.	Met
5.	Clarify the tax treatment of securities bought in Romgaz traded on the foreign stock exchange and adopt, if needed, the necessary legal basis.	Met
Structural benchmarks		
1.	Start publishing monthly arrears reports and corrective measures being taken by the central and local governments, by unit, on a quarterly basis.	End-September 2013
2.	Prepare the basic health package within the existing spending envelope which will also define the scope of the private sector in the health care system in the future.	End-September 2013
3.	Prepare medium-term financial projections that properly identify the fiscal implications of EU-funded projects, including co-financing needs, financial corrections and non-eligible spending.	Mid-October 2013
4.	Approve, by government memorandum, a list of significant priority projects, based on the prioritization criteria, to help prepare for the 2014 budget.	Mid-October 2013
5.	Launch an initial public offering of 15 percent of the government's shares in Romgaz.	Mid-November 2013
6.	Appoint a professional board in Hidroelectrica in accordance with the provisions of Ordinance 109/2011.	End-November 2013
7.	Approve Covered Bond legislation.	End-December 2013
8.	Fully operationalize the commitment control system, supported by necessary legal and procedural changes and cover expenditures of the MoPF and at least one additional unit at both the central and local government levels.	End-January 2014
9.	Launch an initial public offering of a majority of the government's shares in Electrica, after the planned capital increase.	End-May 2014
10.	Fully operationalise the commitment control system for all general government entities.	End-June 2014
11.	Launch an initial public offering of 15 percent of the government's shares in Oltenia, prior to the planned capital increase.	End-June 2014
12.	Launch an initial public offering of 10 percent of the government's shares in Hidroelectrica, after the planned capital increase.	End-June 2014
13.	Roll out the consolidated fiscal reporting system to all government entities.	End-June 2014
14.	Resolve possible discrepancies in the fiscal code and IFRS accounting rules on the treatment of NPLs sold to domestic debt management companies in line with the outcome of the pending EC infringement case.	End-December 2014
15.	Prepare and publish consolidated general government accrual based financial statements and ESA95 based reports from the system (the first sets of reports will be for the year ending 2014), and reconcile with each other and with cash-based budget execution reports.	End-June 2015

Press Release No. 13/367
FOR IMMEDIATE RELEASE
September 27, 2013

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Approves New €1.98 Billion Precautionary Stand-By Arrangement for Romania

The Executive Board of the International Monetary Fund (IMF) today approved a new 24-month Stand-By Arrangement (SBA) in an amount equivalent to SDR 1.75 billion (about €1.98 billion, or 170 percent of Romania's quota in the Fund). The authorities have informed the IMF that they intend to treat the new arrangement as precautionary, and therefore do not plan to draw under it. The authorities have also requested precautionary support from the European Union of €2 billion.

Following the Executive Board's discussion on Romania, Ms. Nemat Shafik, First Deputy Managing Director and Acting Chair, stated:

"Under the authorities' economic programs supported by the last two SBAs with the Fund, Romania has reduced large external and fiscal imbalances and begun structural reforms in a variety of areas. However, real GDP has yet to return to its pre-crisis level, the economy is still vulnerable to external shocks, including volatile capital flows, and the reform agenda remains unfinished. The new SBA will support policy continuity, provide a reserve buffer, and catalyze growth-enhancing reforms. It will also put Romania on the path toward exiting from Fund support.

"The current orientation of monetary and fiscal policies is broadly appropriate. The authorities should be commended for their plans to further reduce at a gradual pace the budget deficit in line with Romania's commitments under the EU's Stability and Growth Pact. Pressure to rollback previous fiscal reforms should be resisted, and institutional reforms to clear arrears, prioritize public investment, and increase absorption of EU funds should be accelerated. Measures to broaden the tax base, strengthen tax administration, and reform the healthcare system are also needed.

"Macro-critical reforms in the transportation and energy sectors are important to improve the business climate. The gradual deregulation of energy prices, supported by measures to protect vulnerable consumers, should be continued. Likewise, the authorities' commitment to undertake long-delayed reforms of state-owned enterprises, including improvement in governance and the expansion of private-sector involvement, is welcome.

"The banking system is well capitalized and foreign bank deleveraging remains orderly. However, balance sheet repair needs to accelerate as non-performing loans continue to rise. The amendment of the insolvency code and the adoption of covered bond legislation would be important steps in this direction. As an additional policy priority, the governance structure at the non-bank financial supervisor should be brought in line with international standards," Ms. Shafik stated.

Statement by Menno Snel, Executive Director for Romania,
and Serban Matei, Senior Advisor to Executive Director
September 27, 2013

The last economic program, supported by the Fund, the European Commission, and the World Bank, contributed significantly in reducing macroeconomic imbalances and restoring stability in the Romanian economy. Recent economic developments all point into the right direction, including a pick-up in GDP growth, a decrease in inflation, declining unemployment and an improving current account balance. Despite these positive developments, the economy is growing below potential and remains vulnerable to external risks. My Romanian authorities therefore ask for a follow-up program, which they intend to treat as precautionary.

The Romanian authorities are convinced that a follow-up precautionary program would provide a policy anchor and reserve safety net, while catalyzing broader support for macro-critical structural reforms, focused on reforming the state-owned enterprises and healthcare sector. The program would also help preserving access to international financial markets and securing Romania's recent gains on macroeconomic and financial sector stability. Moreover, the program would support a continued strengthening of the fiscal institutional framework and contribute to further fiscal policy adjustment.

Recent economic developments

All main macroeconomic indicators have been moving in the desired direction recently. GDP growth has picked up after the recovery slowed in 2012, increasing 0.5 percent q-o-q in the second quarter of 2013, as weak domestic demand was more than offset by increased exports. At the same time, a drop in investment and a relatively mild winter contributed to a decline in imports, in particular of energy. As a consequence, the current account went from a deficit of 3.9 percent in 2012 to a surplus of 1.1 percent of GDP in the first half of 2013. The unemployment rate came down to 7.5 percent, with the expectation that this declining trend will continue. Inflation has started easing from a peak of 6 percent in January 2013 to 3.7 percent in August 2013, in line with NBR projections. The fiscal deficit has come down and fiscal buffers have increased beyond the targeted four months of gross financing needs.

Fiscal policy

Romania exited the EU Excessive Deficit Procedure in June 2013. Further fiscal consolidation remains a key objective of the authorities. The aim is to reach the medium-term budgetary objective of a 1 percent of GDP structural deficit in 2015. The authorities target a fiscal deficit cash target of 2.3 percent of GDP in 2013, and a cash deficit of 2 percent in 2014. Fiscal buffers have reached the level of four months of gross financing needs, and the authorities are fully committed to consolidate this achievement.

To achieve the goals of further fiscal adjustment and building buffers, the authorities will revise the Fiscal Responsibility Law to integrate structural fiscal targets and corrective actions, and focus on better public finance management, especially to contain arrears, both on central and local level. The EU funds absorption and public investment planning is a key priority of the government and, as of 2014, the authorities envisage that no new public investment project will be approved without ensuring its eligibility for EU funds financing. Moreover, actions to reduce public sector employment have been effective and will continue, and a comprehensive reform of the tax administration has been initiated aimed at raising the revenue and efficiency of tax collection.

Monetary policy

The NBR's inflation targeting framework has proved to be successful. In August 2013, inflation eased to 3.7 percent and is expected to drop further through end-2013. Annual inflation is expected to structurally re-enter the medium-target band of 2.5±1 percentage points in September/October 2013. The NBR was able to lower the policy rate by a cumulative 75 basis points to 4.5 percent in July and August, due to low and declining inflation, a negative output gap, negative credit growth and a gradual economic recovery. The real exchange rate remains broadly in line with fundamentals and the central bank will continue to restrict its eventual interventions to limiting excess volatility of the *leu* exchange rate. In the period ahead, repayments to the Fund and the EC will weigh on international reserves, but are being partly offset by regular sovereign issuance in both euro and US dollars.

Financial sector

The Romanian banking sector maintains adequate capital buffers and provisioning but faces pressures from increasing non-performing loan ratios and foreign bank deleveraging. Annual real credit growth to both corporate and households has been negative and non-performing loans rose to 20.3 percent of total loans at end-June 2013. However, provisions were sufficient to cover 88.2 percent of NPLs, with the IFRS provisioning ratio standing at 62.8 percent at end-June.

Although banks returned to profitability in the first half of 2013, prospects for bank profitability remain challenging in light of the difficult economic environment and continued adjustment of corporate and household balance sheets. Nonetheless, the capitalization of the banking sector remained strong at 14.7 percent at end-June 2013. While the liquidity situation has improved for the banking system as a whole, funding conditions are still differentiated among some banks. The pace of foreign-owned bank deleveraging has accelerated in line with regional developments but remains orderly so far. The above-mentioned trends may continue to form an impediment to the recovery of credit growth to the real sector.

Structural reforms

The Romanian authorities are committed to steadfastly implement further structural reforms in order to foster growth, enhance investment, and facilitate the development of energy resources. They are convinced that implementation of these reforms is essential to reduce existing bottlenecks and to bring the economy back on a sustainable growth trajectory. The reforms will focus on the energy, transportation and health care sectors.

With regard to the energy and transportation sectors, the reforms are especially aimed at enhancing the operational and financial performance and overall transparency of the state-owned enterprises (SOEs) that dominate these sectors. In this respect, the authorities envisage a three-pronged approach. In the first phase, the authorities will strengthen measures to reduce SOE arrears, including placing companies into the insolvency process with the aim of liquidating or restructuring. In the second phase, the authorities will implement measures aimed at improving governance, transparency, and monitoring of SOEs. In the third phase, the authorities will continue to improve the pricing framework and efficiency of the energy and transportation sectors by further implementing the electricity and gas price road maps and applying the pass-through mechanism for electricity and gas purchases by the supply companies.

In the energy sector, the European Union's third energy directive has been transposed into national law and another law was promulgated in order to ensure the independence of the energy regulator ANRE. ANRE started the implementation of the electricity price liberalization roadmap in September 2012 and has also started the implementation of the gas price liberalization road map, raising the domestic gas producer price by almost 40 percent.

In the transportation sector, an agreement for the sale of a 51 percent stake in the state-owned freight railway company (CFR Marfa) has been approved by the government. To help improve the financial performance of the state-owned passenger rail company (CFR Calatori), measures have been taken to improve its finances, including closing of the most unprofitable routes for passenger traffic.

Regarding the healthcare system, the authorities seek comprehensive reforms to make the system financially sustainable, raise its efficiency, and improve health outcomes. The reforms will strengthen the contributions base, streamline hospital services reducing the redundant capacity for in-patient services, shift the delivery of health services away from hospitals to ambulatory and primary health care providers, develop capacity in Health Technology Assessments and evidence-based protocols, and allocate more resources towards primary and secondary preventive care.

Conclusion

In conclusion, my authorities concur that the proposed precautionary Stand-By Arrangement would foster policy discipline and provide a reserve buffer, while helping to continue the implementation of difficult structural reforms and put Romania on a firm path toward successfully exiting from Fund support.