INTERNATIONAL MONETARY FUND

IMF Country Report No. 21/190

ROMANIA

2021 ARTICLE IV CONSULTATION—PRESS RELEASE AND STAFF REPORT

August 2021

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2021 Article IV consultation with Romania, the following documents have been released and are included in this package:

- A **Press Release**
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on lapse-of-time basis, following discussions that ended on May 28, 2021, with the officials of Romania on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on July 22, 2021.
- An **Informational Annex** prepared by the IMF staff.

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

Selected Issues

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

Copies of this report are available to the public from

International Monetary Fund • Publication Services
PO Box 92780 • Washington, D.C. 20090
Telephone: (202) 623-7430 • Fax: (202) 623-7201
E-mail: publications@imf.org Web: http://www.imf.org
Price: $18.00 per printed copy

International Monetary Fund
Washington, D.C.

PRESS RELEASE

PR21/249

IMF Executive Board Concludes 2021 Article IV Consultation with Romania

FOR IMMEDIATE RELEASE

Washington, DC – **August 27, 2021:** On August 26, 2021 the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation[1] with Romania, and considered and endorsed the staff appraisal without a meeting.[2]

The Romanian economy fared relatively well during the COVID-19 crisis, as the GDP contraction in 2020 (-3.9 percent) was significantly milder than the EU average (-6.2 percent). Effective and timely fiscal, monetary and financial policy easing helped to curb the economic downturn and the rise in unemployment. Private consumption and net exports led the decline in 2020, while gross fixed capital formation continued to expand, supported by a pickup in public investment. As a result of pandemic-induced economic disruptions, wage growth slowed substantially, and inflation declined into the lower half of the target band. The fiscal deficit widened markedly to 9.7 percent of GDP to accommodate the crisis support package that comprised measures similar to those in EU peers, including emergency health care expenditures, income support for households as well as support for the affected businesses. Monetary and financial sector policy easing played an important role in ensuring market functioning.

A strong economic recovery is underway in 2021. GDP growth has rebounded sharply, reaching 4.6 percent and 2.8 percent (q/q) in Q4 2020 and Q1 2021—among the strongest pickups in the EU—with output in Q1 2021 surpassing the pre-pandemic peak. Headline inflation has increased, partly reflecting higher energy prices. Nonetheless, inflation expectations remain well-anchored within the target band. Concurrently with the recovery, the current account deficit has widened.

Real GDP growth is projected at 7 percent in 2021, led by private consumption and accompanied by a transitory increase in inflation. Over the medium term, output is projected to recover to its pre-pandemic trajectory, as protracted scarring from the pandemic is expected to

---

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

[2] The Executive Board takes decisions under its lapse-of-time procedure when the Board agrees that a proposal can be considered without convening formal discussions.

be contained. Public investment will be boosted by a pickup of EU-funded projects, including through new resources under the NGEU funds and the EU 2021-27 multiannual budget. The current account deficit is projected to narrow moderately into the medium term as fiscal consolidation proceeds and growth decelerates toward potential.

Executive Board Assessment

Following a relatively mild contraction during the COVID-19 crisis, a strong recovery is underway. The output contraction in 2020 was among the mildest in the EU, helped by effective and timely fiscal and monetary policy responses. Output in Q1 2021 surpassed the pre-pandemic peak and growth for the year is projected at 7 percent. Nevertheless, downside risks remain, including uncertainty about the evolution of the pandemic.

Policy support should shift towards the most affected sectors. Ensuring a speedy vaccine rollout is the most important economic policy to address the pandemic, for which continued generous fiscal resources need to be ensured. Although the broad-based fiscal support measures for incomes and businesses have successfully contained the aggregate economic fallout from the pandemic, the most severely hit sections of the economy continue to be disproportionately impacted. Accordingly, the pandemic support measures should be shifted towards the most affected sectors and disadvantaged groups. At the same time, if the recovery surprises on the upside, the authorities should save the windfall revenues.

As the recovery becomes entrenched, fiscal policy should increasingly prioritize rebuilding space for fiscal maneuver. The 2021 budget appropriately lays the foundation for fiscal consolidation, but significant additional medium-term consolidation efforts will be needed to reduce the deficit to the authorities' target of 3 percent of GDP. The revenue base should be broadened, and revenue administration strengthened to achieve a more equitable distribution of the tax burden and improve tax efficiency. Expenditures should be reprioritized by boosting public investment, while ensuring a sustainable medium-term trajectory for wage and pension spending.

To continue raising incomes towards average EU levels, the authorities should re-energize efforts to overcome subpar governance and government effectiveness. SOE reforms, starting with the strengthening of corporate governance, would help to address these challenges. Governance improvements are integral to reforms of revenue administration. Governance gains are also paramount to improving and speeding up public investment. Strengthening of the anti-corruption framework and ensuring robust implementation (including of the AML/CFT framework) are essential.

Romania should take full advantage of the historic opportunity provided by the RRF grants and EU structural funds, with a total envelope of 20 percent of GDP over the next six years. Successful implementation of RRF reform commitments and investment projects would boost Romania's medium-term growth prospects. Through its focus on digitalization, the RRF should provide critical support for modernizing tax administration. It should also be used to jumpstart efforts to address climate change.

Monetary and financial sector policies should remain accommodative. The National Bank of Romania should sustain monetary and financial accommodation to support the recovery and cushion the impact of fiscal consolidation, while monitoring inflationary risks. If bank asset quality deteriorates, the NBR should balance accommodating stance and prudential concerns. Preparations should be in place to handle any deterioration in bank asset quality once the relief measures expire and ensure efficient insolvency procedures. Once the crisis recedes, exchange rate flexibility should be gradually increased, to absorb external shocks and help address the current account deficit.

Romania: Selected Economic Indicators

Population: 19.3 million (2020)
Quota: 1,811 million SDRs (0.4% of total)

Per capita GDP: US$12,854 (2020)
Literacy rate: 99% (2019)
People at risk of poverty: 31.2% (2019)

Key export markets: European Union (Germany, Italy, France)
Main products and exports: Machinery and transport equipment, manufactured goods

	2019	2020	2021	2022
			Proj.	
Output				
Real GDP growth (%)	4.1	-3.9	7.0	4.8
Output gap (%)	3.0	-2.4	-1.0	0.0
Employment				
Unemployment (%)	3.9	5.0	4.9	4.9
Prices				
CPI inflation (%, period average)	3.8	2.6	3.6	2.7
General government finances (% GDP)				
Revenue	28.9	28.9	30.3	30.0
Expenditure	33.5	38.6	37.1	35.8
Fiscal balance	-4.6	-9.7	-6.8	-5.8
Primary balance	-3.5	-8.4	-5.3	-4.2
Structural fiscal balance 1/	-5.1	-6.1	-5.5	-5.6
Public debt (including guarantees)	36.8	49.8	51.5	53.5
Money and credit				
Broad money (% change)	10.9	15.3	10.2	9.5
Credit to the private sector (% change)	6.6	5.5	9.7	7.9
Policy rate (%)	2.5	1.5	...	...
Balance of payments				
Current account (% GDP)	-4.9	-5.2	-5.4	-5.2
FDI (% GDP)	-2.2	-0.9	-1.6	-1.7
Reserves (months imports)	4.9	4.8	4.5	4.5
External debt (% GDP)	49.2	57.7	57.7	57.6
Exchange rate				
REER (% change)	2.4	2.4	...	...

Sources: Romanian authorities, World Bank, Eurostat and IMF staff calculations.
1/ Fiscal balance (cash basis) adjusted for the automatic effects of the business cycle and one-off effects.

INTERNATIONAL MONETARY FUND

ROMANIA

STAFF REPORT FOR THE 2021 ARTICLE IV CONSULTATION

July 22, 2021

KEY ISSUES

Context. Among EU countries, Romania suffered a relatively shallow recession in the COVID-19 crisis, aided by macroeconomic easing. A strong recovery is projected in 2021. The new government is committed to balance continued pandemic-related support with the start of a medium-term fiscal consolidation trajectory that corrects pre-pandemic excesses, while implementing a range of structural reforms. These efforts, as well as the medium-term recovery, should be bolstered by large Next Generation EU grants.

Key Recommendations:

- **Fiscal Policy.** The 2021 budget appropriately continues COVID-19 crisis support, while laying the ground for medium-term consolidation. Temporary measures should shift towards supporting the most affected sectors and households. At the same time, policies need to strengthen the revenue base and improve its administration to ensure that once temporary support is scaled back, sufficient room for policy maneuver is rebuilt. Growing use of EU funding will continue to support building forward better.

- **Monetary Policy and Financial Sector.** After easing during the crisis, the National Bank of Romania should sustain monetary and financial accommodation to support the recovery and cushion the impact of fiscal consolidation and thereby help achieve its inflation objective. Preparations should be in place to handle a possible deterioration in bank asset quality once the relief measures expire and ensure efficient insolvency procedures.

- **Structural Reforms.** The provision of public services and public investment needs to be improved, including through SOE reforms. Governance improvements are integral to revenue administration reforms and would help raise the quality and absorption capacity of public investment, boosting medium-term growth prospects.

Approved By	
Jörg Decressin (EUR) and Kevin Fletcher (SPR)	Discussions took place by video conference during May 10-28, 2021. The mission met with Prime Minister Cîțu, Finance Minister Nazare, Governor Isărescu, other senior officials, representatives of political parties, labor and business organizations, civil society, and financial institutions. The staff team comprised Jan Kees Martijn (head), Rudolfs Bems, Seng Guan Toh (all EUR), Neil Meads (SPR), Mengxue Wang (FIN) and Georgia Babici (local economist). HQ support was provided by Wei Zhao and Agnesa Zalezakova (both EUR). Nadeem Ilahi (Senior Resident Representative) and Liviu Voinea (OED) attended part of the meetings.

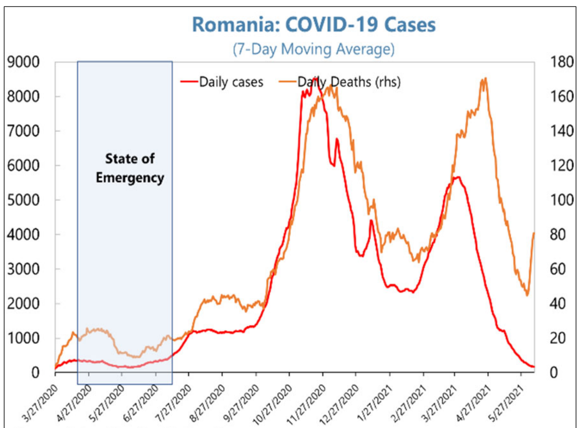
CONTENTS

ANNEXES

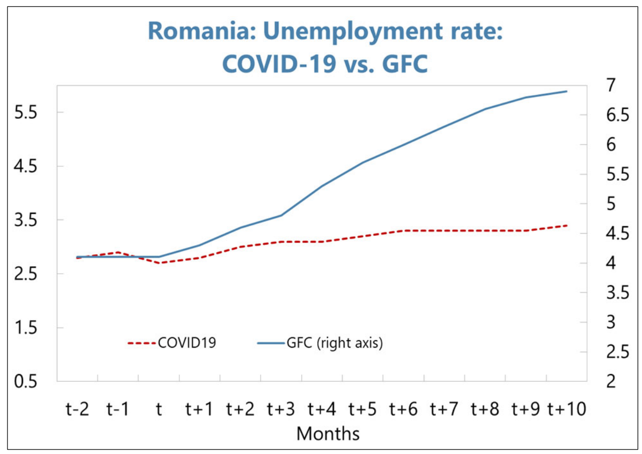
APPENDIX

CONTEXT

1. **The Romanian economy fared relatively well during the COVID-19 crisis.** The GDP contraction in 2020 (-3.9 percent) induced by the pandemic was significantly milder than the EU average (-6.2 percent). This reflected in part a more limited initial virus outbreak and short-lived surges in subsequent virus waves without a second national lockdown. Effective public health measures also helped. Importantly, household and business livelihoods benefitted from coordinated fiscal, monetary, and financial policy easing that helped curb the economic downturn and the rise in unemployment. This was a contrast to the procyclical policy tightening applied in previous economic crises in Romania. Bolstered by global monetary easing and EU support measures, external financing has been favorable.



Source: Johns Hopkins University.

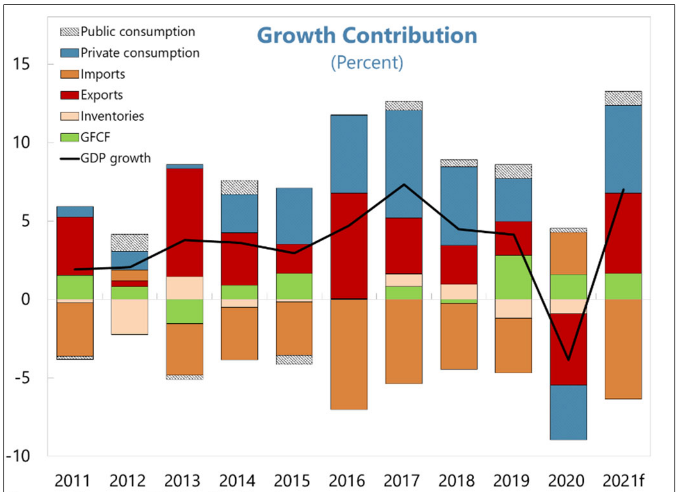


2. **Political developments have turned favorable for reforms.** After the December 2020 elections, the new center-right coalition government led by the Liberal party (PNL) has introduced a budget that balances continued pandemic support with the start of consolidation, and envisages returning the deficit to 3 percent of GDP by 2024, consistent with EU rules. It also is engaging more closely with the EU for support and has committed to structural and governance reforms that had languished over the past several years (Annex I). During the PNL's one-year term as a minority government preceding the elections, the authorities curbed risks to fiscal sustainability, including by capping very large legislated pension hikes. Markets appeared to recognize these reforms and have readily absorbed record Eurobond and domestic issuances.

3. **The focus of discussions with the authorities** was on actions to sustain fiscal support to secure a recovery from the pandemic while laying the ground for consolidation over time to rebuild room for policy maneuver. This should be supported by preserving accommodative monetary and financial conditions. Furthermore, to take advantage of the Next Generation EU (NGEU) funding opportunities, it will be important to undertake structural reforms to enhance EU fund absorption and revenue mobilization. These policies are to be complemented by governance reforms to reinforce the growth trajectory over the medium term.

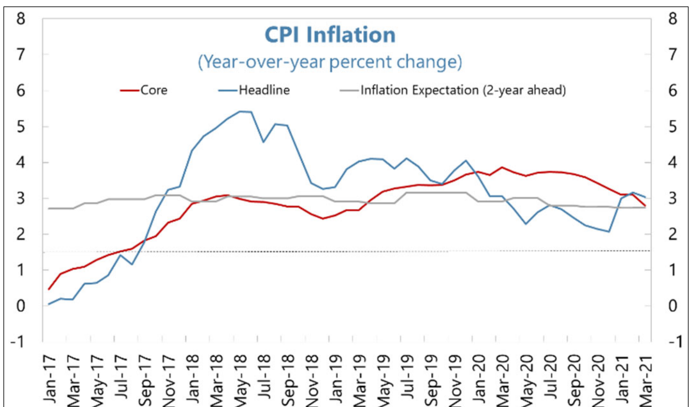
RECENT DEVELOPMENTS

4. GDP has picked up strongly following its contraction in 2020. Private consumption and net exports led the decline in 2020, with agriculture also affected by drought. However, gross fixed capital formation still expanded owing to prior-year construction stimulus measures and a pickup in public investment. After a lockdown-induced plunge in Q2 2020 GDP, the output gap turned negative and wage growth slowed substantially compared to the double-digit increases of previous years. But growth has since rebounded sharply, reaching 4.6 percent and 2.8 percent (q/q) in Q4 2020 and Q1 2021 – among the strongest pickups in the EU.



Sources: Haver and IMF staff estimation.

5. After inflation declined in 2020, it has risen since then. Headline inflation fell to 2.1 percent y/y by December 2020, in the lower half of the target band (1.5–3.5 percent), as economic activity slowed, and commodity prices fell. Core inflation fell more moderately due to the large weight in the CPI of processed food prices, disrupted by COVID-related supply constraints. In the initial months of 2021, headline inflation was pushed up on the re-liberalization of electricity prices[1], higher natural gas prices, and the rebound in global commodity prices. Nonetheless, and with a stable exchange rate, inflation expectations have remained relatively well-anchored within the target band and core inflation remained close to the mid-point of the band.



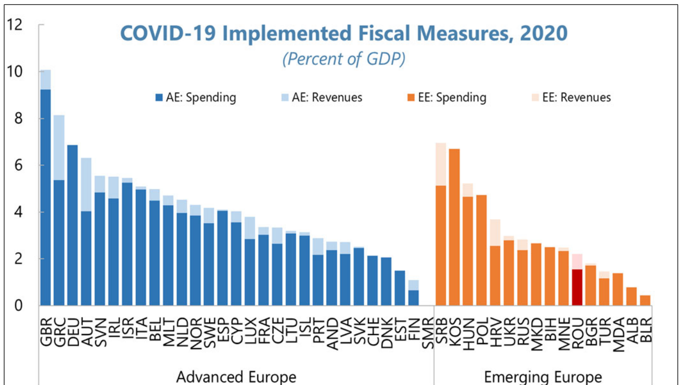
Note: headline and core inflation was impacted by changes in VAT rate, fuel excise, and administered prices (frequent in 2015-17); core inflation is defined as inflation for the CPI basket that excludes VFE (vegetable, fruit and egg), fuel, administered prices, alcohol and tobacco, and electricity.

6. The current account deficit widened modestly in 2020 (to 5.2 percent of GDP from 4.9 percent in 2019)**.** Gross merchandise trade contracted sharply in 2020 H1, but rebounded in H2, although the overall balance continued to deteriorate. This deterioration was somewhat offset by a

[1] Electricity prices surged 17 percent y/y in January-April 2021 following this re-liberalization, which unwound the regulated price regime introduced by GEO 114 since 2019 (see CR/19/278-Annex I)

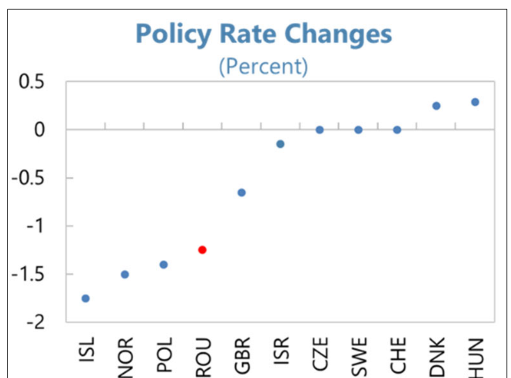
rise in net services exports (with a fall in outbound tourism and increasing IT receipts) and by higher secondary income – on account of higher EU fund inflows. Next Generation EU (NGEU)-related grants are likely to contribute to sustained capital account inflows and add persistence to the current account deficit. Portfolio investment was the main source of current account financing, reflecting significant sovereign bond issuance. As a result, foreign exchange reserves increased, and reserve coverage remains more than adequate (Annex II). Data in early 2021, when compared with early 2020, point towards a further widening in the current account deficit, but may reflect pandemic-related idiosyncrasies.

7. **In response to the pandemic, the fiscal deficit widened markedly.** The deficit in 2020 expanded to 9.7 percent of GDP (2019: 4.6 percent of GDP), as the measures to soften the impact of the pandemic crisis came on top of a structural fiscal expansion in 2019.[2] The implemented fiscal package comprised 2.2 percent of GDP in direct spending and revenue measures and an additional 1.7 percent of GDP in guarantees and other actions. While smaller in size than in many EU peers (chart), the types of support were broadly similar: first, health care expenditures; second, income support measures in the form of temporary wage subsidies, leave and unemployment benefits, and targeted hiring incentives; and third, business support with liquidity extended through tax deferrals and credit guarantees predominantly targeting SMEs (see Annex III and Annex VI Table B). To promote transparency and accountability of the pandemic support measures, key implementing institutions were audited by the Court of Accounts, with follow-ups expected in 2021.



Source: IMF, World Economic Outlook, and IMF Staff calculations.
Note: The numbers on implementation of measures are preliminary. For some countries, these numbers are staff's estimates, while for a couple of countries numbers mentioned in the table are not for 2020 as a whole.

8. **Monetary and financial sector policy easing played an important role in ensuring market functioning throughout the COVID-19 period.** The National Bank of Romania (NBR) reduced policy rates by 125 bps (to 1.25 percent), launched a temporary asset purchase program for domestic government securities (0.5 percent of GDP so far), and provided liquidity as well as regulatory easing and bank loan repayment deferrals (Annex II and Annex VI). These measures helped contain the initial market stresses seen in March-April 2020 and



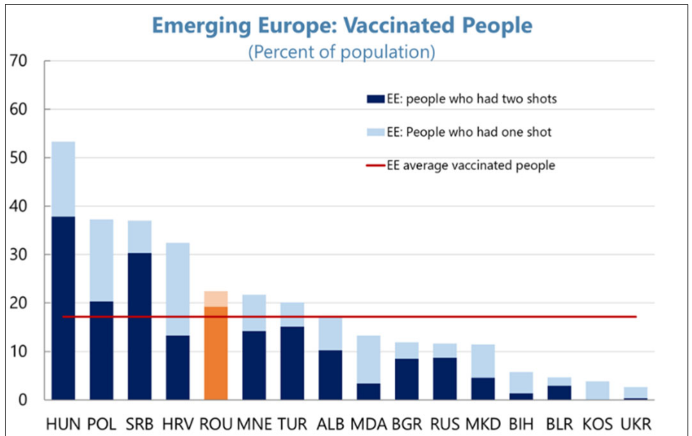
Source: Haver Analytics.

[2] The EU's Excessive Deficit Procedure (EDP), initiated as the 2019 deficit was above 3 percent of GDP, has been suspended due to the EU-wide escape clause activated for the pandemic.

sustained the flow of credit, including for SMEs. Thus, private credit as a share of GDP improved by end 2020, reversing a near decade-long decline.

OUTLOOK AND RISKS

9. A strong growth recovery is projected for 2021. A continued rebound in activity is expected as vaccine coverage has expanded (chart), and vaccine supplies are ample.[3] Factoring in the positive carryover from strong growth in Q4 2020 and Q1 2021, real GDP growth is projected at 7 percent in 2021 led by private consumption. After anticipated increases towards end 2021 due to electricity and fuel-related price adjustments, inflation is projected to return within the target band in 2022 as these transitory effects fade out. A better agricultural harvest later this year is also expected to support output and curb food prices. A small further widening of the current account deficit is projected this year, reflecting the comparatively strong economic growth.



Sources: Our World in Data COVID-19 dataset; and IMF staff calculations.
Note: Data as of June 3rd, 2021.

10. Over the medium term, growth is projected to be supported by EU funds. The growth momentum is projected to continue as consumption and private investment remain robust, although offset in part by the withdrawal of fiscal impulse due to budget consolidation. Public investment will be supported by a pickup of EU-funded projects, including through new resources under the NGEU funds (6 percent of GDP in grants alone for 2021-26, see Box 1) and the EU 2021-27 multiannual budget (around 12 percent of GDP in structural funds). Absent concrete reforms (Selected Issues CR/17/134), staff assumes a moderate pickup in the absorption of EU structural funds, while for NGEU grants full utilization is assumed by 2026 based on Romania's preparations and the EC's focus on speeding up disbursements (text table). The current account

Romania: Macroeconomic Outlook
(Percent)

	2017	2018	2019	2020	2021	2022
Real GDP (yoy)	7.3	4.5	4.1	-3.9	7.0	4.8
Output gap	1.9	2.6	3.0	-2.4	-1.0	0.0
CPI inflation (yoy, eop)	3.3	3.3	4.0	2.1	4.1	2.9
Unemployment rate (average)	4.9	4.2	3.9	5.0	4.9	4.9
(In Percent of GDP)						
Current account balance	-3.1	-4.6	-4.9	-5.2	-5.4	-5.2
Fiscal balance (cash)	-2.8	-2.8	-4.6	-9.7	-6.8	-5.9
Gross general government debt (direct debt only)	34.7	34.5	35.0	46.6	48.7	51.0
Gross external debt	51.8	48.8	49.2	57.7	57.7	57.1

Sources: Eurostat; Romanian authorities; IMF staff projections.

[3] Romania had a comparatively fast start to the vaccination campaign. The government's target is to vaccinate 70 percent of the population (10.4 million) by September 2021. Vaccine contracts cover over twice the population.

deficit is projected to narrow moderately into the medium term as fiscal consolidation proceeds and growth decelerates toward potential.

Estimated Growth Impact of Funds from the Recovery and Resilience Facility

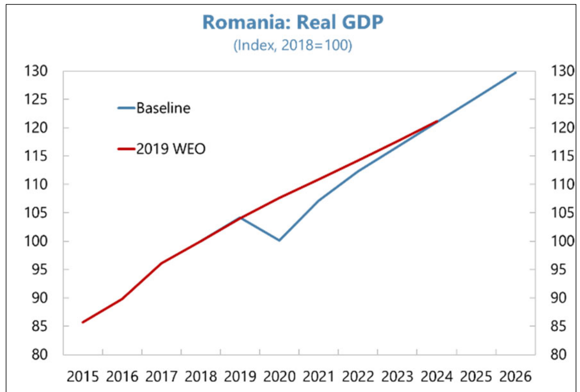
	2021	2022	2023	2024	2025	2026
Total new spending (bn EUR)	1.7	2.7	2.7	2.2	2.2	2.2
Absorption profile for investment grants (annual share)	*0.10*	*0.18*	*0.18*	*0.18*	*0.18*	*0.18*
Projected new investment spending (bn EUR)	*1.2*	*2.2*	*2.2*	*2.2*	*2.2*	*2.2*
Other new spending (bn EUR)	*0.5*	*0.5*	*0.5*			
Total new spending, as % of GDP	**0.7**	**1.0**	**1.0**	**0.8**	**0.7**	**0.7**
Impact on GDP levels (ppt)	0.3	0.7	1.1	1.4	1.7	1.9
Impact on real GDP growth rates (ppt)	**0.3**	**0.4**	**0.4**	**0.3**	**0.3**	**0.3**

Sources: WEO and IMF staff calculations.

Notes: 90/10 split for investment and other spending assumed. Full grant absorption by 2026 with a flat absorption profile assumed, based on indications from the EC about faster disbursment relatitve to absorption rates of EU structural funds. In line with two scenarios in the RRF plan, partial absorption of loans assumed, limited to replacement of existing projects. Impact on GDP growth rates estimated assuming a fiscal multiplier of 0.4 in the short run and medium term (up to 2026), as large and vital infrastructure gaps are addressed.

11. Protracted scarring from the pandemic is expected to be contained. Factoring in the shallow recession in 2020 and the potential growth-enhancing effects of absorbing the sizable new EU funds through higher gross fixed capital formation, output is projected to recover fully to its pre-pandemic trajectory. In discussions with the authorities, staff examined evidence of scarring impacts from the pandemic. The nationwide lockdown of only two months in 2020 limited the duration of the shock. The rise in unemployment across sectors was moderate, helped also by the labor support schemes, and remained so to date in 2021. Adverse impacts were also mitigated by Romania's reliance on manufacturing and agriculture rather than contact-intensive service sectors, compared to the average EU country. The authorities considered that given the effective pandemic support, the strong economic recovery, and the growth in investment, the pandemic will not have a lasting effect on the economy beyond the most affected sectors, with new grant schemes targeted at hard-hit sectors also helping limit scarring (Annex III). Furthermore, its impact on debt service payments and financial sector balance sheets also appears limited thus far (see paragraph 21).

12. Risks are tilted to the downside (Annex V: RAM)**.** The main downside risk stems from adverse unexpected shifts in the pandemic (possibly due to new virus strains, shorter vaccine effectiveness, unwillingness to vaccinate). Unexpected pandemic developments may also prompt global financial markets to reprice risk assets and reassess Romania's vulnerabilities, leading to possible challenges in financing the deficits, albeit mitigated by the fiscal liquidity buffer as well as FX reserves and the ECB repo line. Political risks can emerge as parliamentary alignments can be fluid over time, which can slow structural reforms, and lead to a worse fiscal trajectory than in the baseline. On the other hand, growth in 2021 could exceed the baseline if the strong growth momentum persists beyond the first quarter. Over the medium term, there are upside risks associated with the EU funds, which could boost growth more than expected if used swiftly for public investment projects combined with supporting structural reforms.



Sources: WEO and IMF staff calculations.

Authorities' Views

13. The government concurred that the strong growth momentum through Q1 2021 implied upside risk to their earlier 5 percent growth projection for 2021. They projected medium-term growth somewhat higher than staff, at around 5 percent, factoring in higher absorption of the NGEU funds and assuming stronger positive effects on potential growth. The authorities projected a temporary rise in inflation on account of higher energy prices and continued pressures on the current account deficit given strong economic growth this year, in line with staff. Notwithstanding signs of economic recovery, the authorities reiterated that adverse pandemic-related developments remained the main risk to the outlook, with uncertainties necessitating a continued supportive macroeconomic stance.

POLICY DISCUSSIONS

Macroeconomic policy accommodation should continue, to help entrench the recovery from the COVID-19 crisis. At the same time, the preparation and implementation of medium-term expenditure reforms, revenue base broadening, and improvements in revenue administration will be needed to correct the significant fiscal imbalances that prevailed already before the crisis. Monetary and financial policies should help cushion the impact fiscal consolidation may have on activity, including by allowing greater exchange rate flexibility as the crisis recedes. Structural reforms focused on governance improvements and quality investment would strengthen the foundations for growth.

A. Fiscal Policy: Balancing Crisis Support with Medium-Term Sustainability

14. The 2021 budget targets a deficit of 7.2 percent of GDP, helped by a restraint on public wages and pensions, some wind down of domestically-financed COVID support in H2 of 2021 and EU-funded support and investment. All broad categories of pandemic support measures have been extended through mid-2021 (see text table and Annex III for details), with increased focus on the most affected sectors. However, the fiscal deficit impact is reduced relative to 2020 because of increased reliance on EU resources. To start rebuilding fiscal space, the authorities have restrained the growth of public sector wage bill and moderated the growth of pension benefits, stipulating no further pension increases during 2021 following a 14 percent increase in Q3 of 2020.[4] At the same time, the budget increases investment expenditures, including by further boosting the utilization of EU structural funds, continuing the trend from 2020. The resulting expenditure shift towards investment should stimulate Romania's medium-term economic capacity. Plans for the EU Recovery and Resilience Facility (RRF) funds have been submitted to the EC, but the associated increase in grant-financed investments was not yet incorporated in the 2021 budget.

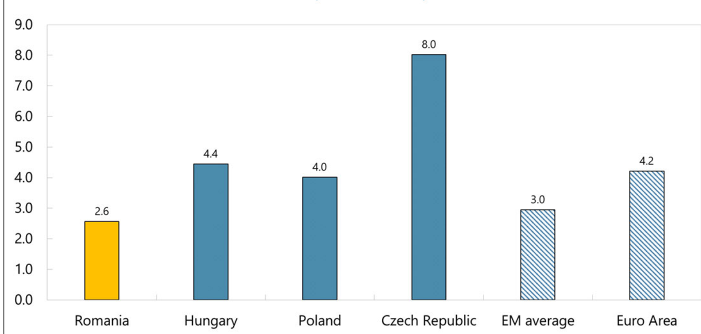
Fiscal support measures for the COVID-19 crisis
(Lei billion)

Support measures	Disbursed in 2020	Planned for 2021
Health system measures	5.6	3.8
Income support for individuals and companies, including grants	10.6	11.5
Other support, including revenue measures and guarantees	25.0	26.1
Overall	**41.2**	**41.5**

Sources: IMF staff estimates.

15. Staff views the 2021 budget plans as broadly appropriate. A premature withdrawal of the crisis support could weaken the recovery and augment risks of scarring. At the same time, the 2021 budget signals a meaningful consolidation effort to financial markets concerned about the fiscal deficit trajectory. Staff estimates that implementing the 2021 budget would bring the fiscal expansion, relative to pre-pandemic levels, marginally below the emerging market average (see figure), which is desirable given Romania's pre-crisis overspending and strong economic recovery. Fiscal financing in 2021 is expected to be manageable, amid currently low external funding costs and lower external amortization than in 2020. In addition, the strong economic recovery in Q1 of 2021 has helped the fiscal outlook. Staff estimates the baseline fiscal deficit for 2021 at 6.8 percent of GDP, 0.4pp below the budget.

Projected deterioration in 2021 Fiscal Deficit Relative to 2019
(Percent of GDP)



Sources: WEO, IMF Staff Calculations.

[4] The fiscal savings from these wage and pension measures are estimated at around 1 percent of GDP.

16. Continued flexibility will be needed to tailor the fiscal response to the evolving pandemic. Speedy vaccine rollout is the most effective policy to combat the pandemic. At the same time, staff suggested maintaining temporary income and business support measures, such as kurzarbeit allowances and grants to SMEs, and further shifting support towards the most affected sectors, including HoReCa and transport, and taking full advantage of the EU's COVID recovery facilities. If the COVID crisis persists into the second half of 2021, the authorities should extend the crisis measures accordingly, accepting a higher deficit.[5] On the other hand, staff recommended that if the crisis abates sooner than expected and economic outturn surprises on the upside, any fiscal consolidation gains should be locked in, to facilitate the medium-term fiscal adjustment.

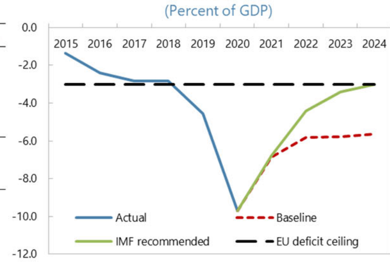
17. To rebuild fiscal buffers over the medium term, significant further consolidation efforts should commence as the economic recovery is becoming entrenched. Staff's baseline scenario foresees moderate ongoing fiscal consolidation over the medium term based on the authorities' commitment to continued moderation in wage and pension growth. However, this scenario still features persistent large fiscal deficits and expanding public debt into the medium term (see figures and Annex IV: DSA). To stabilize the debt, the authorities are targeting a further deficit reduction to under 3 percent of GDP by 2024, which would resolve the EU's EDP. Staff views 3 percent as an appropriate target and has identified a frontloaded set of quality revenue and expenditure measures (see table), compatible with improvements in income distribution and stronger potential growth, which would stabilize public debt at a still relatively low level of 52 percent of GDP by 2022.

Recommended fiscal consolidation and scarring support
(Percent of GDP)

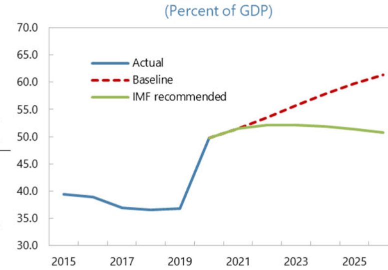
	2020	2021	2022	2023	2024
Budget deficit under current policies 1/	9.7	6.8	5.8	5.8	5.6
IMF recommended budget deficit	9.7	6.8	4.4	3.4	3.0
Implied CAPB	7.5	5.0	2.8	1.8	1.4
Required fiscal adjustment in CAPB		**2.5**	**2.2**	**1.0**	**0.4**
Legislated measures		**2.5**	**0.8**	**0.0**	**0.0**
Impact from (withdrawal of) covid measures		*1.7*	*0.8*		
Measures in the 2021 budget		*0.8*			
Menu of staff's proposed measures		**0.0**	**1.4**	**1.0**	**0.4**
Changes to public wage policy			*0.3*		
Tax policy changes			*0.3*	*0.7*	*0.1*
Revenue collection improvements			*0.3*	*0.3*	*0.3*
EU grants replacing domestic capex			*0.5*		
Memorandum items					
Implied adjustment to structural balance		0.6	1.2	1.0	0.4
Deficit impact of COVID-19 measures 2/	2.5	0.8	0.0	0.0	0.0

Sources: IMF Staff estimates
1/ Staff's estimated fiscal deficit for 2021 of 6.8 percent of GDP deviates from the authorities' 2021 budget target of 7.2 mainly because of more favorable macro projections, reflecting strong economic rebound in Q1 of 2021.
2/ Deficit impact of Covid-19 fiscal measures differs from the overall size of the crisis response package (see Annex 3) because the latter includes government guarantees and is partly financed by EU grants.

Fiscal balance
(Percent of GDP)



Public debt
(Percent of GDP)



- **Expenditure measures.** Fiscal spending has outpaced economic growth in Romania in recent years. Personnel expenditures expanded by 22 percent annually during 2017-2019. The 2021 budget reversed this trend, but ad-hoc measures should be replaced by structural reforms. There is need to establish a viable pension system that addresses social needs without jeopardizing medium-term fiscal sustainability. Public sector wage reform should aim to ensure that compensation, including bonuses, grows in tandem with the overall economic activity and

[5] While large financing needs in 2020 were met without problems, Romania continues to be assessed as having fiscal space at risk.

productivity and is benchmarked to the private sector. Staff estimates that further spending reforms could add 0.3 percent of GDP to fiscal consolidation in 2022.[6]

- **Revenue administration reforms.** Tax efficiency in Romania is among the lowest in the EU, and strengthening tax collection is a cornerstone of the authorities' fiscal consolidation plans. Despite the challenges posed by the pandemic, reforms were initiated in 2020, building on Fund TA that recommended modernizing IT infrastructure, strengthening compliance risk management to combat tax avoidance, improving ANAF governance and addressing staffing shortages and skills mismatches. Revenue gains of 0.5 percent of GDP are built into the staff's baseline scenario and, taking into account historical evidence as well as the complexity of the reform agenda, staff estimates that steadfast implementation could have an additional revenue impact of 0.3 percent per year into the medium term.

- **Revenue consolidation measures.** Staff projects that the above measures would not suffice to reach the 2024 deficit target. To help fill the gap, while acknowledging the government's pledge to avoid tax increases, staff identified options for expanding the tax base and closing loopholes. The suggested measures center on eliminating disparities in income taxation, removing VAT exemptions and reforming property taxation (1.4 percent of GDP; see table). The measures would help to achieve a more equitable distribution of tax the burden, and improve transparency and productivity of the tax system.

Menu of possible measures for revenue consolidation
(percent of GDP)

Measures	Impact
Reduce the turnover threshold for the micro regime below EUR 100,000	0.21
Broadening SSC and PIT tax base	0.22
Increase the tax rate on dividends from 5 to 10 percent	0.16
Remove low tax rates for the PIT and SSC in the IT and construction sectors	0.33
Remove special VAT treatment of financial and insurance services	0.11
Property tax reform	0.25
Apply an ad-valorem excise on all sugar-sweetened beverages packaged for final consumption	0.11
Apply an excise on heated tobacco	0.04
	1.4

18. **The increased availability of EU funds provides a historic opportunity to strengthen medium-term growth prospects and facilitate the fiscal adjustment.** Over the next six years Romania will have access to 20 percent of GDP in RRF grants and EU structural funds.[7] Hence, although the recommended fiscal adjustment--which peaks in 2022 at 2.4 percent of GDP--is sizable, it need not derail the economic recovery. Further improvements in public investment management and government procurement will be imperative for the effective absorption of the additional funds and higher capital spending (see paragraph 28). Furthermore, part of the higher inflows is projected to substitute for the domestic financing of government investments.[8] The

[6] A moderation in growth in personnel expenditures and social transfers is already assumed in the fiscal baseline. The recommended additional public wage policy measures relate to bonus payments.

[7] The EU funding portfolio also includes RRF loans and large ongoing agricultural support. To facilitate EU fund absorption, the authorities have requested Fund support through a public investment management assessment (PIMA).

[8] This substitution with increased reliance on EU funds is projected at 1 percent of GDP in the baseline and an additional 0.5 percent of GDP within the proposed additional measures.

remaining fiscal adjustment, at less than 1 percent of GDP, is expected to have a limited impact on growth[9] that could be offset by monetary and financial policies as well as meaningful progress with governance reforms (see paragraph 28).

Authorities' Views

19. The authorities emphasized the importance of continued pandemic support. Given the strength of the recovery, the authorities noted that the 2021 fiscal outturn might outperform budget plans. At the same time, they noted that some sectors, such as HoReCa, required further help, and that the pandemic support funds would be redirected to industries most in need.

20. The authorities reiterated their commitment to reducing the fiscal deficit to below 3 percent of GDP by 2024. In this context, they highlighted their commitment to key reforms, including of wages, pensions, and tax administration, as presented in their Recovery and Resilience Plan (RRP) submitted to the European Commission (EC). They emphasized the urgency of ANAF reforms and the paramount role that tax collection improvements would play in achieving the medium-term fiscal target, envisaging a possible 2.5pp of GDP improvement in revenue collection by 2024. They also stressed the importance of a sustainable medium-term trajectory for fiscal expenditures, with the focus shifting towards public investment. Tax policy reforms would be implemented gradually and subject to further study.

B. Monetary and Financial Policies: Staying Accommodative While Preparing for Recovery

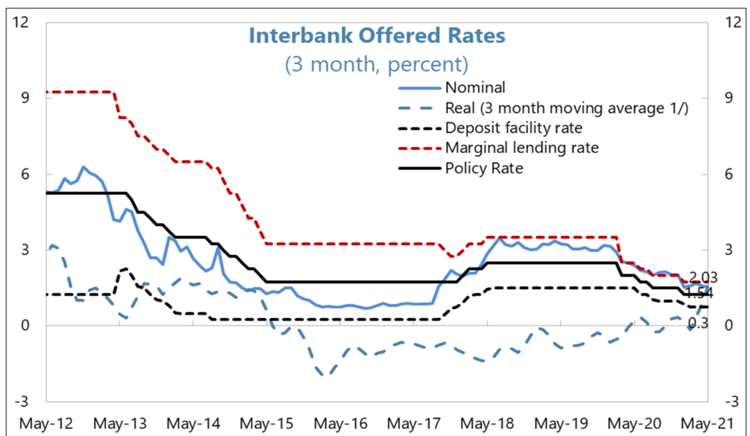
21. The NBR's decisive monetary and financial policy easing in response to the pandemic was broadly appropriate (Annex VI). The measures generally conform with Fund advice, and have also taken advantage of the Romanian banking system's strong initial capital, liquidity, and profitability position (Table 7: FSIs) to accommodate debt service moratoria requests through March 2021. The moratoria requests were concentrated in the initial months of the pandemic, and the pipeline has ebbed, with the overwhelming amount having since been repaid.[10] After the freeze in loan classification standards in 2020, guided by the European Banking Authority, standards have appropriately been restored in 2021, , which will help enhance visibility on asset quality going forward. The strong economic recovery has also benefitted asset quality thus far, with non-performing loans (NPLs) remaining low into 2021. Building on pre-pandemic levels of loan loss provisioning in the banking system (around 60 percent, above the EU average of 45 percent), banks preemptively raised provisions further in 2020 in anticipation of a deep shock that did not materialize. Banks are now planning to release some provisions during 2021. NBR recommendations, mirroring EU-wide guidance, to limit dividend payouts and share buybacks have also helped to raise capital retention in the system. Nonetheless, in the event of COVID setbacks, liquidity pressures on

[9] Estimated in the range of 0.2-0.5 ppt of GDP for the peak adjustment in 2022, accounting for the projected strong growth momentum and broadly closed output gap.

[10] The NBR noted that less than 5 percent of the stock of loans affected by deferrals remained, compared to over a fifth of total household and corporate loans in the peak stage of requests.

firms and households may re-emerge. If lockdowns and distancing measures recur, a deterioration of credit quality could result. NPLs remain low, but nonetheless warrant caution given that problems may be obscured until all the support measures expire.

22. In the event of a significant deterioration in asset quality, the NBR should strike a balance between providing accommodation and ensuring prudent buffers (see Annex VI Table C)**.** Given the continued bank profitability and sustained rise in capital ratios over the course of the pandemic, staff sees as adequate the current restrictions on bank capital distributions, which were extended until September 2021 as a prudent step against lingering uncertainty relating to the pandemic's effects on private-sector balance sheets. If loan portfolios unexpectedly deteriorate materially going forward, the use of capital can be accommodated while allowing a longer period to rebuild.[11] In case of a surge in NPLs, the NBR and the banks are also expected to draw on their 2014-2018 experience in successfully reducing NPLs, including via sales to private asset management companies. Preparations need to be in place for efficiently handling a potential increase in debt restructuring and business insolvencies, which would help mitigate scarring.[12] In this regard, the anticipated transposition later in 2021 of the EU directive on insolvency and restructuring should help.



Sources: Haver; Eurostat; National Bank of Romania; and IMF staff calculations.
1/ Computed using the underlying inflation rate, adjusted for VAT changes.

23. Staff supports continued accommodative monetary policy to help secure the recovery from the pandemic. The degree of monetary easing in 2020 in Romania was more moderate than in other countries in the region, in light of depreciation pressures amidst the twin deficits. Maintaining the current policy rate remains appropriate given anchored inflation expectations within the target band, the negative output gap and muted wage growth projections, and pandemic-related uncertainties. Especially if more frontloaded fiscal consolidation materializes, extending monetary accommodation beyond this year can be appropriate, if consistent with the inflation target. Monetary accommodation can help cushion the impact of the fiscal stimulus withdrawal. Keeping on hand the current set of liquidity-providing tools is also useful in case liquidity pressures on firms and households return. Purchases of government securities can be reactivated if stresses recur to preserve market functioning. On the other hand, in case of a scenario where inflation pressures are more persistent than currently expected, steps to limit monetary

[11] NBR stress tests indicated that accumulated capital buffers were sufficient to absorb potential deterioration, while maintaining minimum regulatory capital levels.

[12] See IMF, 2020, "Private Debt Resolution Measures in the Wake of the Pandemic".

accommodation including strict liquidity management in preparation for rate hikes can be considered.

24. Romania's external position in 2020 was weaker than implied by underlying fundamentals and desirable policies (Annex II). There is unusually high uncertainty in the assessment because of the pandemic although the EBA-lite models suggest overvaluation in both current account and REER models. The NBR intervened in 2020 to stabilize the exchange rate amidst COVID-19 related stresses in the FX market (Annex II footnote 9). As the crisis recedes, staff recommends gradually increasing exchange rate flexibility to absorb external shocks. Such flexibility, together with fiscal consolidation, can also help to address the current account deficit.

Authorities' Views

25. The NBR explained that its easing measures, in concert with EU-wide measures and support since 2020, helped to alleviate the impact of the pandemic by sustaining market functioning and the flow of credit. On the banking sector, it observed that in 2020 supervisors and banks had preemptively prepared for a much more severe pandemic shock than what had unfolded. Loan loss provisioning and capital ratios had continued to increase compared to end-2019, and banks did not have to apply for the regulatory relaxations provided nor draw down on capital buffers. Asset quality remained comfortable even after the expiry of the regulatory relief measures, supported by the stronger-than-expected economic recovery.

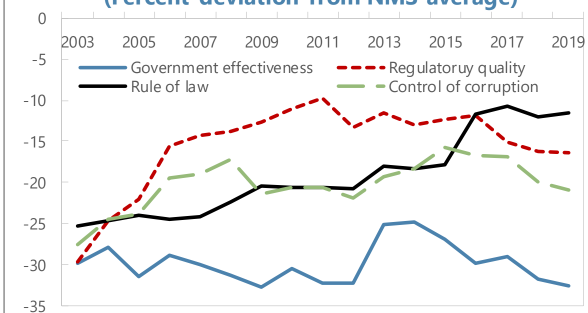
26. The NBR did not see a need to ease monetary policy further, given the ongoing economic recovery. At the same, it considered that its policy stance could remain accommodative factoring in current projections that higher inflation in 2021 was due mainly to transitory energy-price related factors which would fade away in 2022. On the external sector assessment, the authorities expressed reservations about the EBA-lite model's fit and applicability to interpret the current account deficit in 2020 amidst unprecedented pandemic-related uncertainty in Romania and its trading partners. They also noted that the EBA-lite CA model likely underestimated the contribution of cyclical and structural factors to the current account deficit. While open to allowing some more exchange rate flexibility as the crisis recedes, the NBR saw little scope for depreciation to help correct the current account deficit in the absence of fiscal consolidation and structural improvements in productive capacity. They also noted that the foreign exchange sales, albeit smoothed over time to minimize market impact, were essentially the outcome of the longstanding arrangement with the Ministry of Finance to provide lei for foreign currency, which had increased since 2019 with larger foreign currency-denominated fiscal financing.

C. Structural Reforms: Improving Governance to Boost Growth Prospects

27. Romania needs to improve public services and investment. The quality and quantity of infrastructure and the provision of public services continue to lag the EU peers, with significant infrastructure gaps in all key areas, including transport and digitalization (CR/17/134, DP/20/11 and CR/21/2021SIP). To address these challenges, the governance of state-owned enterprises needs strengthening, which will also be paramount for accelerating the absorption of EU funds. Consistent implementation of corporate governance reforms adopted earlier would be a first step.[13] Reversing the worsening financial performance of SOEs in recent years is another priority, requiring enhanced monitoring and necessary reforms in some sectors, such as the SOEs with heavy presence in the energy sector.

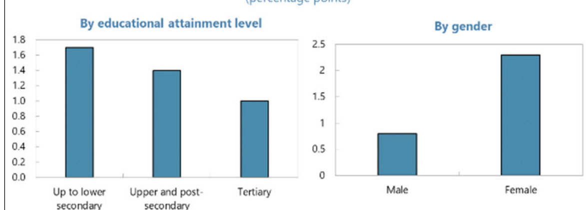
28. Efforts to improve economic governance need to be re-energized. Following significant advances in the fight against corruption and governance reforms during the EU accession period, limited progress was made over the last decade and even reversals in some areas in recent years (see text figure and Annex I). Staff estimates suggest that bridging half of the gap in governance rankings with regional peers could add 0.3 percentage points annually to Romania's medium-term growth (see Box 2). Governance improvements would also help alleviate social challenges such as migration, inequality, and informality. Governance improvements should be an integral part of the revenue administration reforms, including to limit corruption vulnerabilities. Effective governance is also central to strengthening public investment management processes, from planning and procurement to implementation. Equally important is continued progress with judicial reforms and strengthening of the anti-corruption framework, to align with EU norms and requirements and to sustain the fight against high-level corruption. The improved AML/CFT framework, including the recently transposed EU AML/CFT directives, should be followed by robust implementation and strengthened monitoring.

Governance gaps
(Percent deviation from NMS average)



Sources: Worldwide Governance Indicators and IMF staff calculations.
Note: NMS include Bulgaria, Czech Rep., Estonia, Hungary, Latvia, Lithuania, Poland and Slovak Rep. All reported indicators are perception-based and should be interpreted with care, as they are based on opinion surveys and expert assessment. Interpretation of the reported results should also take into account that there is uncertainty surrounding each point estimate.

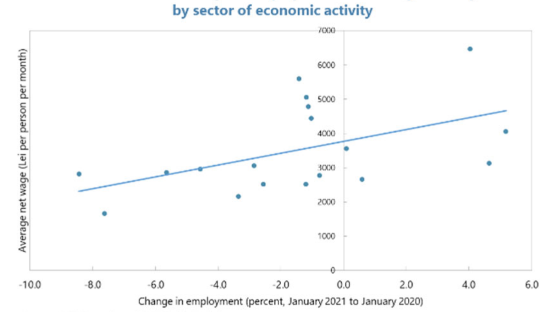
Covid19-induced change in unemployment
(percentage points)



Sources: Eurostat and IMF staff calculation
Notes: Data refers to Q3 of 2020 relative to Q3 of 2019

Sources: Eurostat and IMF staff calculations
Notes: ILO unemployment rate, seasonally adjusted. Data refers to January 2021 relative to February 2020

COVID19-induced change in employment and average earnings by sector of economic activity



Sources: NSI Romania and IMF Staff calculations

29. The pandemic has aggravated inequality. Although Romania's aggregate economy fared relative well during the pandemic, there have been setbacks in human capital accumulation and risks of increased long-term unemployment, with a disproportional negative impact on more disadvantaged groups (see figures). The authorities should refocus policies towards inclusive growth through better-targeted health care, education, and social protection.

---

[13] These reforms were stipulated in GEO 109 and adopted by the Law 111 on SOE Governance in 2016.

30. Romania has committed to contribute to the EU climate and energy targets by 2030 (table below). During recent decades, Romania was among the EU countries with the largest reductions in manufacturing and agricultural emissions. The focus of the RRF on investments and reforms that support climate objectives, is expected to support achievement of the new targets. The authorities have pledged to phase out coal mining and the use of coal for power generation by 2032 and to adopt a law with a mandatory coal replacement schedule by 2022.

Overview of Romania' main objectives and progress towards the 2021-2030 INECP

Area	Target	Progress over last decade
ETS emissions (% compared to 2005)	-43.9	-39.3 in 2015
Non-ETS emissions (% compared to 2005)	-2	-8.3% in 2015
Overall share of renewable energy in gross final energy consumption (2017)	30.7	24.5 in 2017
Final energy consumption (% compared to targets set in PRIMES 2007 baseline scenario)	-40.4	-31.8% in 2015

Source: Romania NECP, PRIMES projections and IMF Staff Calculations.

Authorities' Views

31. There was a broad agreement on the importance of governance reforms to boost Romania's growth prospects. The authorities emphasized that reforms to SOEs were a priority and that concrete reform plans were under development. Improvements in corporate governance and financial performance were the key focus areas. There was also agreement on the importance of eliminating bottlenecks in public investment processes. Public procurement was highlighted as a key issue that the authorities plan to address through both improvements in the legal framework and additional resources to speed up procurement. The authorities expected that necessary judicial reforms would be passed by parliament by end-2021. To facilitate green transition, the authorities were exploring renewable energy sources as well as natural gas as alternatives to coal. The authorities were also exploring a gradually increasing role for environmental taxes. They emphasized that a bold set of governance reforms, covering the above topics, had been incorporated in their RRP.

STAFF APPRAISAL

32. Following a relatively mild contraction during the COVID-19 crisis, a strong recovery is underway. The output contraction in 2020 was among the mildest in the EU, helped by effective and timely fiscal and monetary policy responses. Output in Q1 2021 surpassed the pre-pandemic peak and growth for the year is projected at 7 percent. Nevertheless, downside risks remain, including uncertainty about the evolution of the pandemic.

33. Policy support should shift towards the most affected sectors. Ensuring a speedy vaccine rollout is the most important economic policy to address the pandemic, for which continued generous fiscal resources need to be ensured. Although the broad-based fiscal support measures for incomes and businesses have successfully contained the aggregate economic fallout from the pandemic, the most severely hit sections of the economy continue to be disproportionately impacted. Accordingly, the pandemic support measures should be shifted towards the most affected sectors and disadvantaged groups. At the same time, if the recovery surprises on the upside, the authorities should save the windfall revenues.

34. As the recovery becomes entrenched, fiscal policy should increasingly prioritize rebuilding space for fiscal maneuver. The 2021 budget appropriately lays the foundation for fiscal consolidation, but significant additional medium-term consolidation efforts will be needed to reduce the deficit to the authorities' target of 3 percent of GDP. The revenue base should be broadened, and revenue administration strengthened to achieve a more equitable distribution of the tax burden and improve tax efficiency. Expenditures should be reprioritized by boosting public investment, while ensuring a sustainable medium-term trajectory for wage and pension spending.

35. To continue raising incomes towards average EU levels, the authorities should re-energize efforts to overcome subpar governance and government effectiveness. SOE reforms, starting with the strengthening of corporate governance, would help to address these challenges. Governance improvements are integral to reforms of revenue administration. Governance gains are also paramount to improving and speeding up public investment. Strengthening of the anti-corruption framework and ensuring robust implementation (including of the AML/CFT framework) are essential.

36. Romania should take full advantage of the historic opportunity provided by the RRF grants and EU structural funds, with a total envelope of 20 percent of GDP over the next six years. Successful implementation of RRF reform commitments and investment projects would boost Romania's medium-term growth prospects. Through its focus on digitalization, the RRF should provide critical support for modernizing tax administration. It should also be used to jumpstart efforts to address climate change.

37. Monetary and financial sector policies should remain accommodative. The National Bank of Romania should sustain monetary and financial accommodation to support the recovery and cushion the impact of fiscal consolidation, while monitoring inflationary risks. If bank asset quality deteriorates, the NBR should balance accommodating stance and prudential concerns. Preparations should be in place to handle any deterioration in bank asset quality once the relief measures expire and ensure efficient insolvency procedures. Once the crisis recedes, exchange rate flexibility should be gradually increased, to absorb external shocks and help address the current account deficit.

38. It is recommended to hold the next Article IV consultation on the standard 12-month cycle.

Box 1. Recovery and Resilience Plan

Romania will be a major beneficiary of the EU Recovery and Resilience Facility (RRF), with investment plans structured around six pillars (see table). Within the broader NGEU funds, the authorities have requested to receive the entire envelope under the RRF of around €29 billion (14 percent of 2020 GDP), o/w: €14.3 billion in grants, and €15 billion in loans. The authorities' plan was guided by the requirement to dedicate at least 37% of resources towards climate objectives, and 20% to digital transition. Projects in the plan cover the entire lifetime of the RRF until 2026.

Six Pillars of the Recovery and Resilience Plan

Green Transition		Digital transformation		Smart Growth		Social and territorial cohesion		Health and resilience		Policies for the next generation	
€15.9bn		€1.89bn		€2.8bn		€2.3bn		€2.8bn		€3.6bn	
Water management	1.88	Government Cloud	1.89	Tax and pension reforms	0.5	Local fund for green and digital transition	2.12	Hospitals Fund	2.45	"Romania Educated"	3.6
Forest and biodiversity	1.37										
Waste management	1.20							Social reforms	0.2		
Transport	7.62	Public systems digitalization		Private sector support, R&D, innovation and SOE reform	2.36	Tourism and culture	0.2				
Renovation Fund	2.20							Public administration reform, social dialogue, justice efficiency	0.15		
Renewable energy	1.62										

The proposed plan presents an ambitious and comprehensive reform agenda, covering four broad areas:

- **Fiscal-structural**: reforming pensions and public wage systems (including minimum wage setting), modernizing revenue administration, broadening the tax base, and adopting a minimum inclusion income.

- **Governance**: reforming the SOE framework, amending the justice laws and strengthening the anti-corruption framework, improving the public procurement framework, creating a national development bank, and introducing a new system of admittance and promotion in the public service.

- **Climate:** decarbonizing transport, introducing green taxation, including a new system of road pricing and promotion of zero emissions, phasing out coal and supporting production of hydrogen, reducing illegal forest logging, and increasing recycling rates.

- **Health and education:** reforming the healthcare system and building new health infrastructure, digitalizing education, developing an early education system, reforming the mandatory education cycle through higher school autonomy, and reducing school dropout.

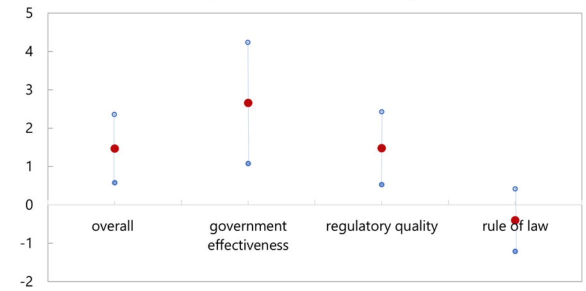
Box 2. Governance Reforms and Medium-Term Growth in Romania

A sustained governance reform effort in Romania would boost medium-term growth prospects, with government effectiveness improvements providing the largest gains. The reforms would also increase investment and improve public infrastructure (see CR/21/xx).

Empirical evidence for EMs shows that governance improvements increase GDP. Building on the 2019 Oct WEO (Chapter 3), the analysis identifies the impact of changes in governance on GDP by analyzing 94 EMs during 1996-2015. A two standard deviation change in the governance score leads to a large and persistent increase in output, estimated at 1.3 percent on impact and 1.5 percent after 6 years. Among the components of governance, improvements in government effectiveness increases the medium-term output by most.

Output response to governance reforms

6 years after the reform, % change

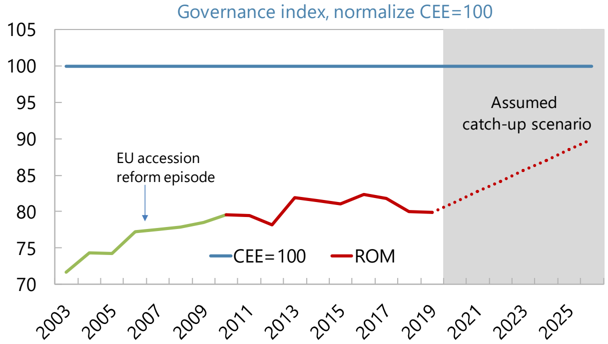


Sources: WDI, WGI, WEO and IMF staff calculations
Note: Overall index refers to the average of the three subindices, government effectiveness, regulartory quality and rule of law. The red dots denote point estimations. The blue dots denote 90 percent confidence bands

These results suggest that a feasible governance reform effort in Romania would significantly boost medium-term growth prospects. A reform scenario, motivated by the pace of governance reforms observed during the EU accession period, suggests that closing ½ of the governance gap with the EU peers by 2026 would increase annual medium-term GDP growth rate by 0.3pp. The persistent reform effort would close ¼ of Romania's income gap with its EU peers by 2026. The impact could be even larger if reforms target gains in government effectiveness, where the gap with peers is the largest.

Governance gap with CEE peers

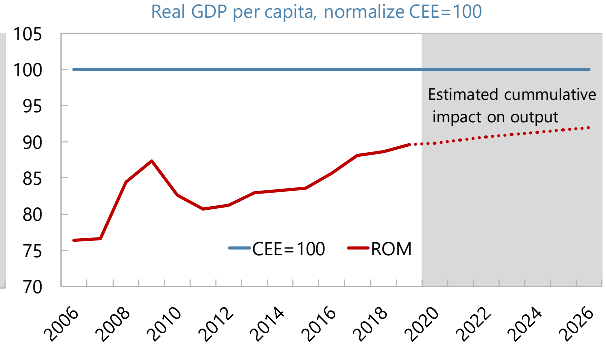
Governance index, normalize CEE=100



Sources: Worldwide Governance Indicators and IMF staff calculations.
Note: The governance indicator is perception-based and should be interpreted with care as it is based on opinion surveys and expert assessment. Interpretation of the reported results should also take into account that there is uncertainty surrounding each point estimate.

Output catch-up with CEE peers

Real GDP per capita, normalize CEE=100

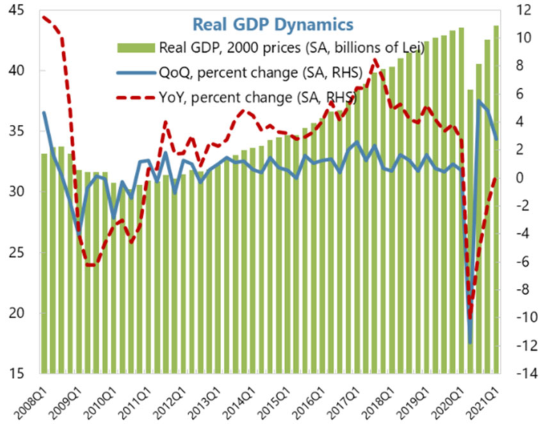


Sources: WEO and IMF staff calculations
Note: Impact on output cummulated from yearly governance improvement shocks and estimated impulse response for output (see Annex VIII).

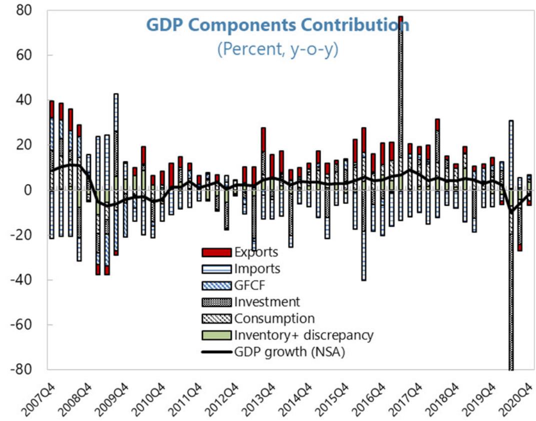
The main channel of impact involves public investment. The effect of governance improvements via public investment and private investment each comprises 1/3 of the total impact on output, highlighting the centrality of efficient public investment management for output gains.

Figure 1. Romania: Real Sector, 2007–21

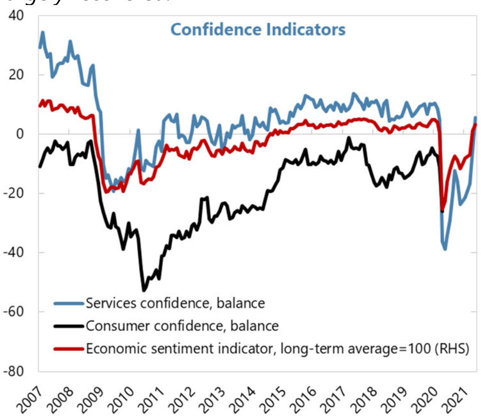
COVID-19 hit economic activity in Q2 2020 on the nationwide lockdown, but rebounded thereafter…



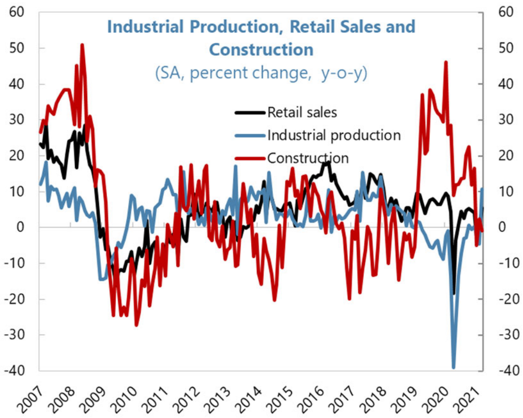
… mainly on consumption after a partial reopening since May 2020. Construction-related investment was sustained by carry forward of past measures and public investment.



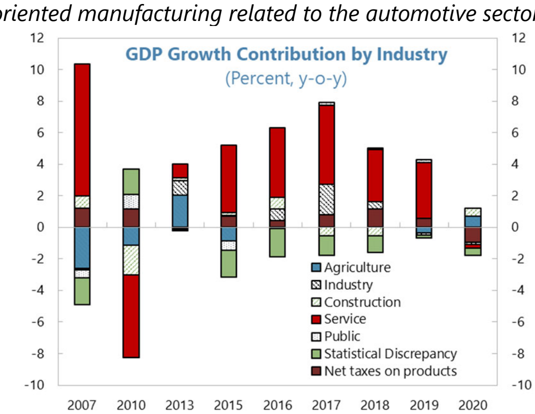
Economic sentiment and confidence indicators have largely recovered.



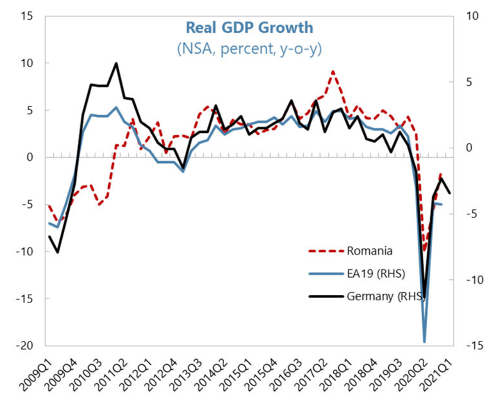
Retail sales have resumed positive growth and industrial production has normalizing recently, while the construction boom in 2019-20 has started to ebb.



Growth contracted in 2020 as the pandemic affected a range of contact-intensive services as well as export-oriented manufacturing related to the automotive sector.



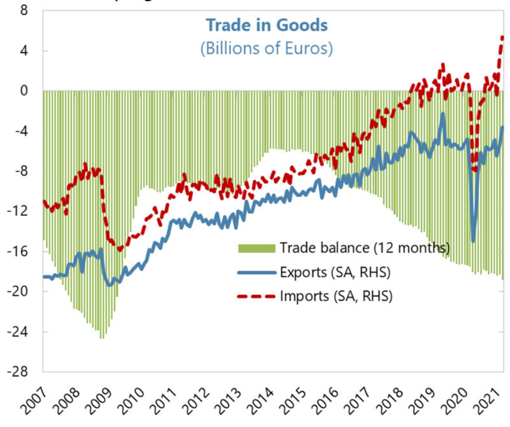
Romania has remained closely integrated with the Euro Area, with the downturn and recovery broadly synchronized.



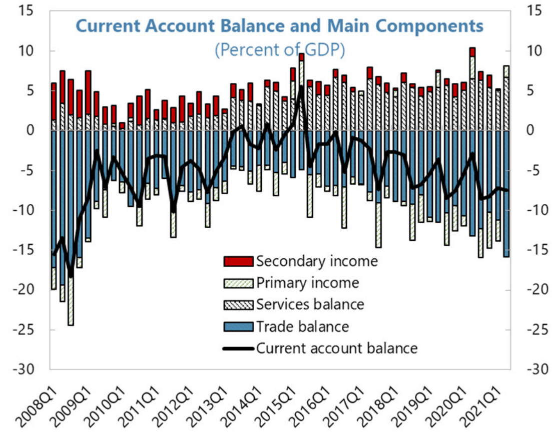
Sources: Haver Analytics; and IMF staff calculations.

Figure 2. Romania: External Sector, 2007–21

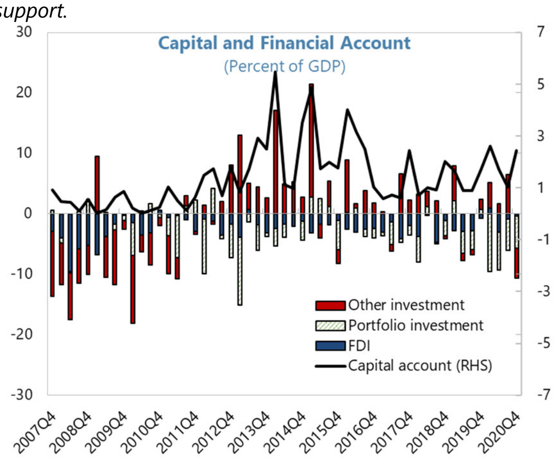
Exports initially plunged more than imports but have since rebounded, helping to stabilize the trade balance …



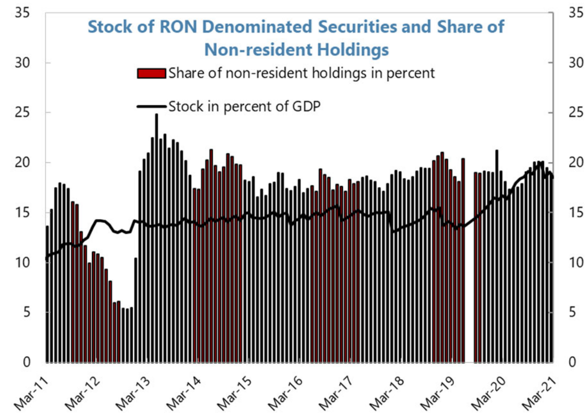
…contributing to also moderate the widening trend in the current account deficit.



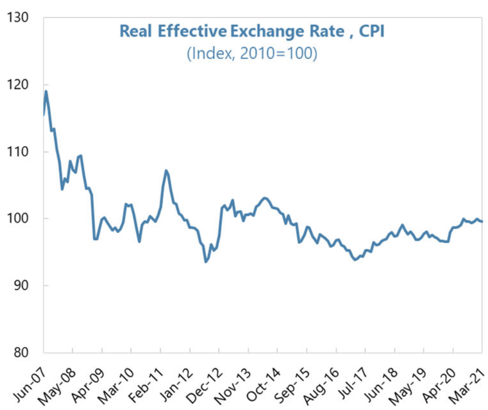
Net FDI flows contracted markedly in the COVID-19 crisis, but portfolio and capital account inflows (higher EU funds) offered support.



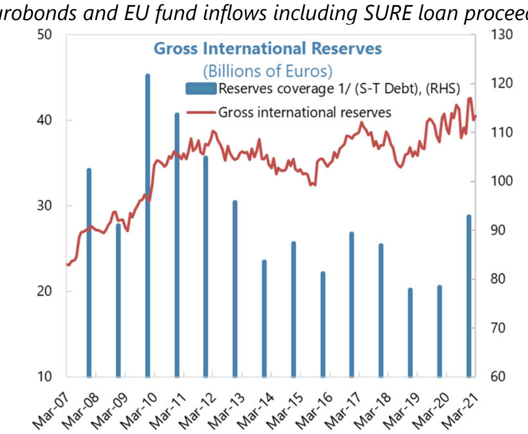
Higher government debt issuance in 2020 was supported by continued non-resident holdings.



The real exchange rate remained relatively stable.



Foreign reserve coverage improved at end 2020 on ramped-up Eurobonds and EU fund inflows including SURE loan proceeds.

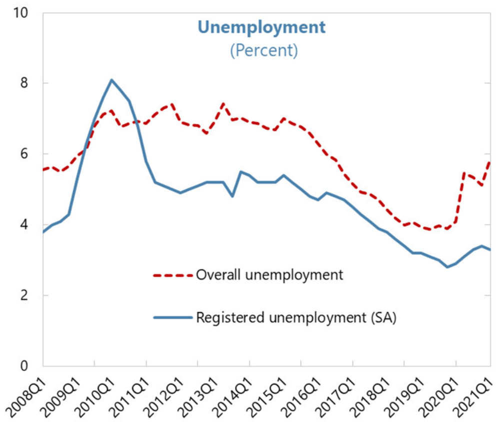


Sources: Haver Analytics; National Bank of Romania, IMF Information Notice System (INS); and IMF staff calculations.

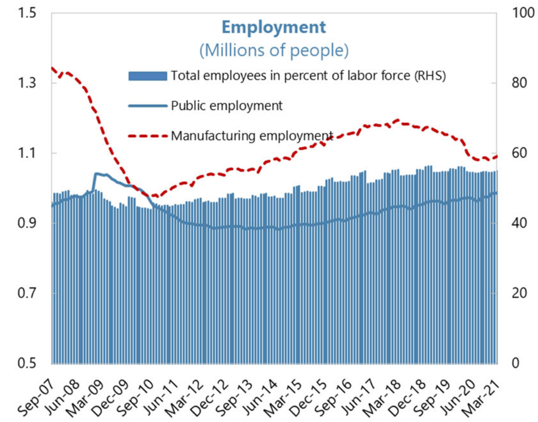
1/ Reserves coverage is based on end-of-year data.

Figure 3. Romania: Labor Market, 2007–2021

Starting from record lows, the rise in unemployment rate has been restrained by labor support measures during the COVID-19 crisis…

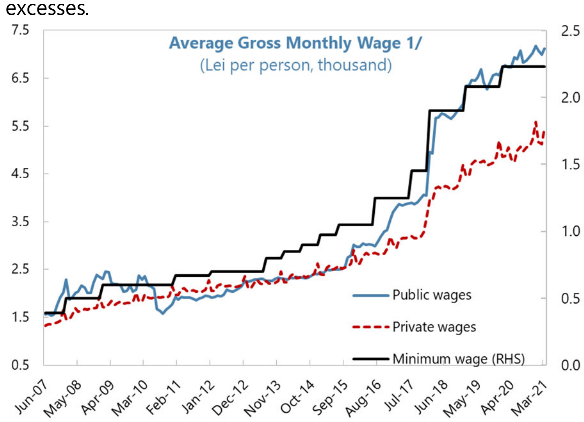


… with the drop in employment also relatively moderate so far compared to the GFC downturn.

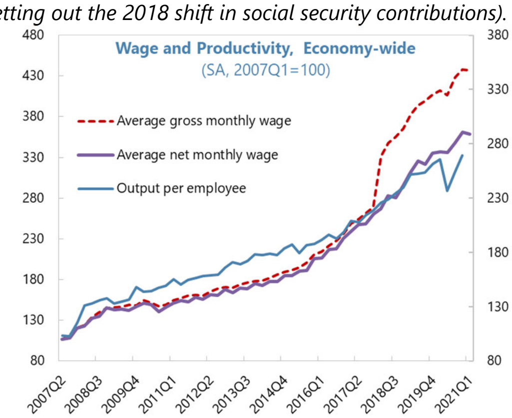


Real wage growth continued in 2020 but was more moderate than in recent years…

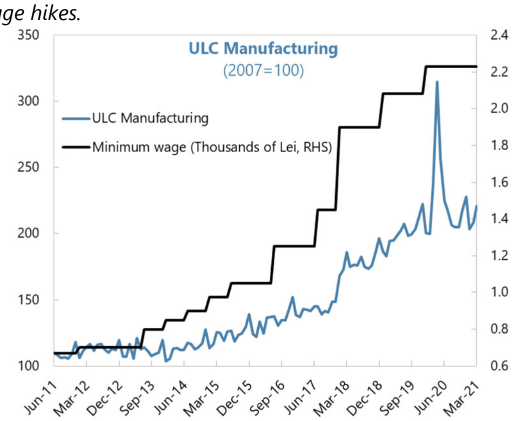
… with more moderate public sector and minimum wage hikes, and recently a public wage freeze in 2021 to curb past excesses.



Nonetheless, cumulative wage increases in past several years have exceeded the economy-wide productivity gains (even netting out the 2018 shift in social security contributions).



Unit labor costs in the manufacturing sector have been on an upward trend, accompanied until recently by large minimum wage hikes.

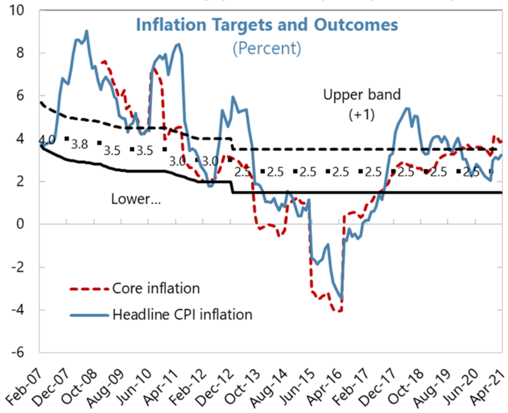


Sources: Eurostat, Haver Analytics; and IMF staff calculations.

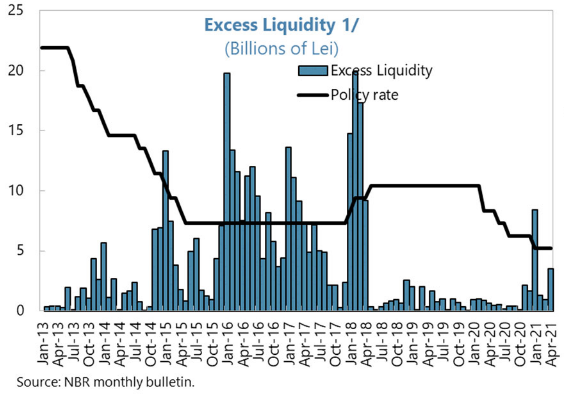
1/ Year 2018 reflects the upward adjustment of gross wages, including gross minimum wages, due to the implementation of the shift in social security contributions from employers to employees, which kept net wages and costs to employers unaffected.

Figure 4. Romania: Monetary Sector, 2007–21

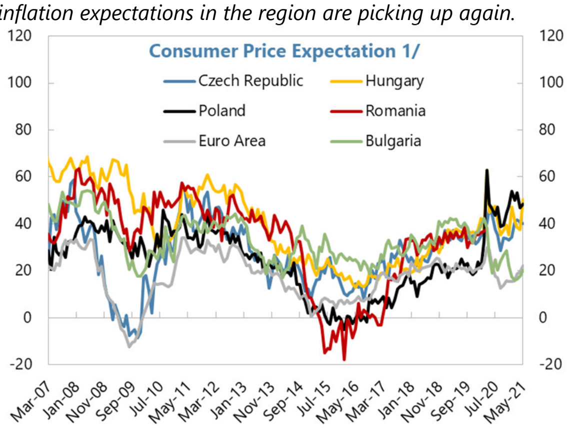
Headline inflation declined to the lower half of the target band by end 2020, but has surged in 2021 following the re-liberalization of electricity prices and pickup in fuel prices.



The NBR has kept excess liquidity generally tightly controlled over the past two years to avoid sharp currency depreciation.

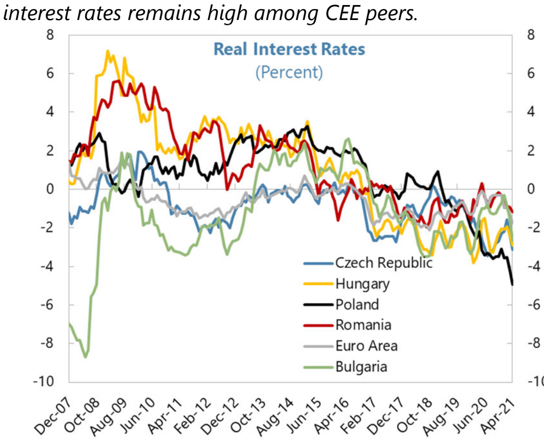


Affected by shifts in COVID-19 pandemic developments, inflation expectations in the region are picking up again.

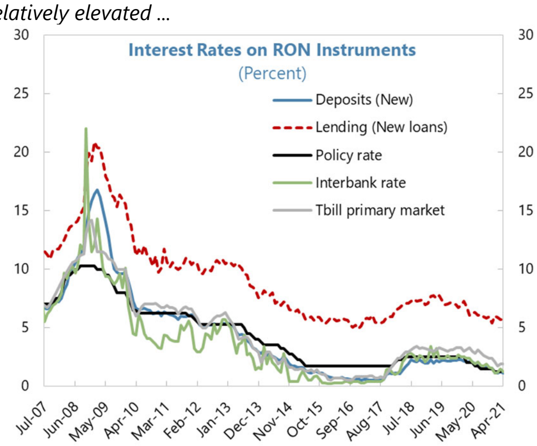


1/ Equals to the percentage of favorable answers minus the percentage of unfavorable answers in the survey on price trends over the next 12-month.

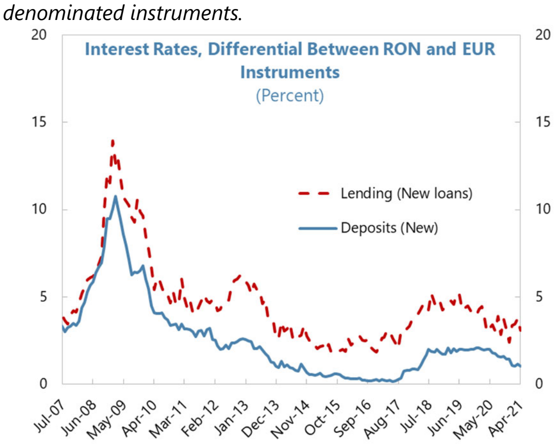
Despite cuts in the policy rate from 2020, Romania's real interest rates remains high among CEE peers.



… and interest rates for domestic currency instruments remain relatively elevated …



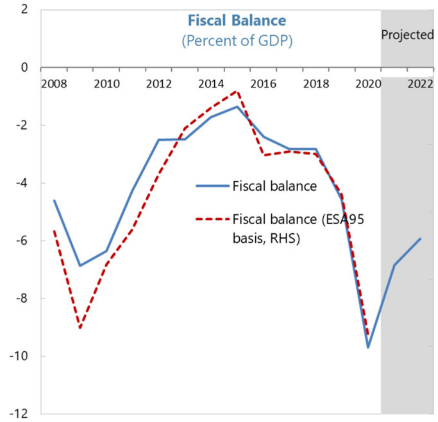
… keeping wide the differential with the rates on Euro-denominated instruments.



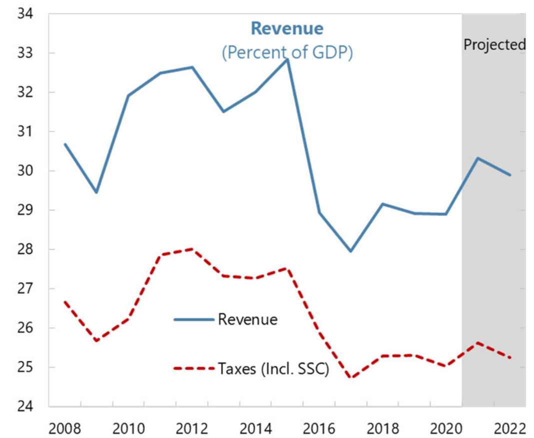
Sources: Haver Analytics; National Bank of Romania; Eurostat; Consensus Forecast; and IMF staff estimates.

Figure 5. Romania: Fiscal Operations, 2008–22

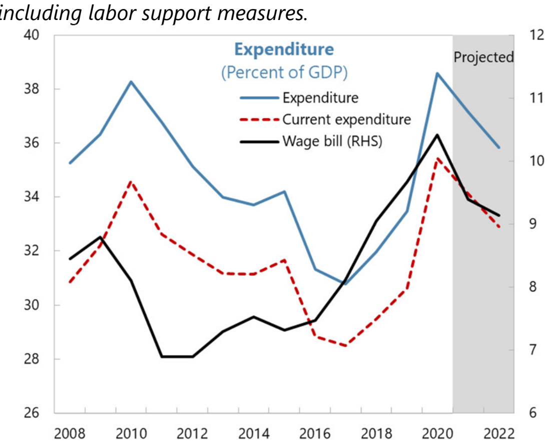
The fiscal deficit approached 10 percent of GDP in 2020 due to the severe economic contraction and COVID-19 support, but consolidation is in train.



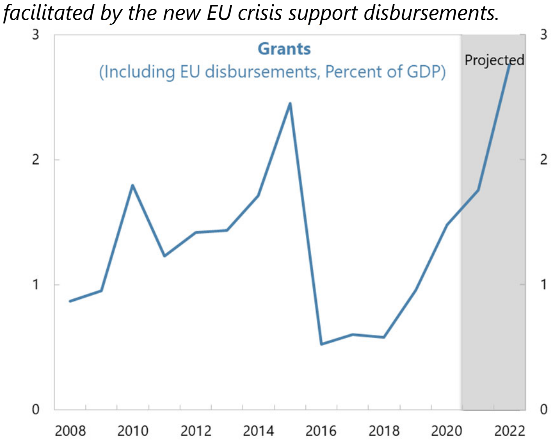
Tax revenues contracted in line with nominal GDP, keeping the ratios broadly stable…



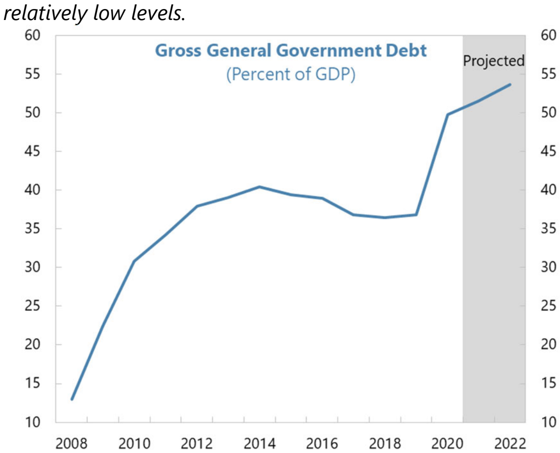
…expenditures surged, led mainly by higher social spending, including labor support measures.



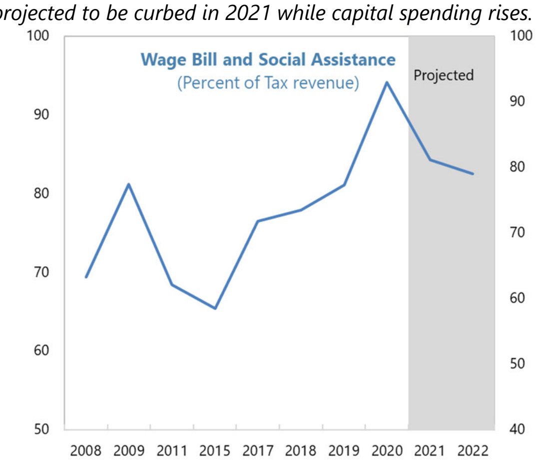
Absorption of EU funds improved somewhat in 2020, facilitated by the new EU crisis support disbursements.



Large fiscal deficits in response to the crisis are projected to markedly raise government debt, albeit from Romania's relatively low levels.



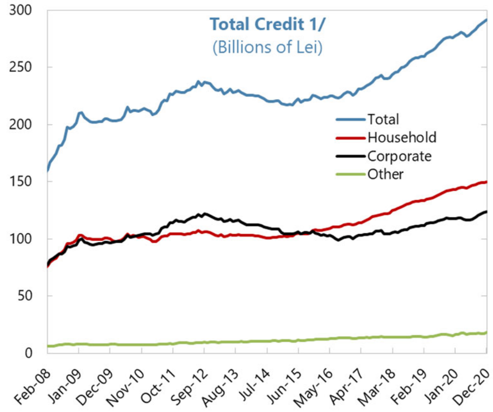
Rigidities in the budget structure were driven by wages, pensions and childcare allowances increases in 2020, but are projected to be curbed in 2021 while capital spending rises.



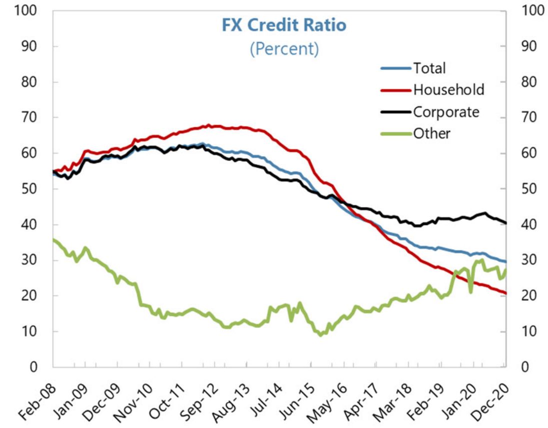
Sources: Romanian authorities; and IMF staff estimates and projections.

Figure 6. Romania: Financial Sector, 2008–20

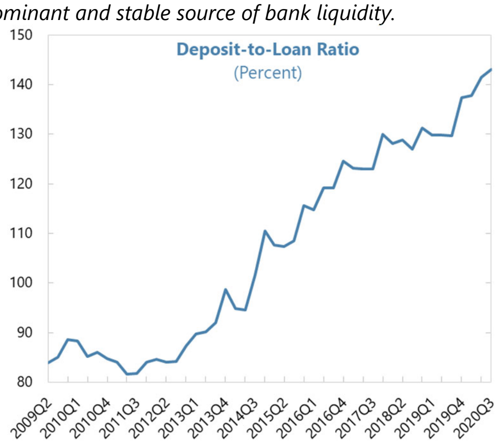
Local-currency lending continued to grow, supported by government guaranteed loans and crisis easing measures to sustain the flow of credit to households and businesses...



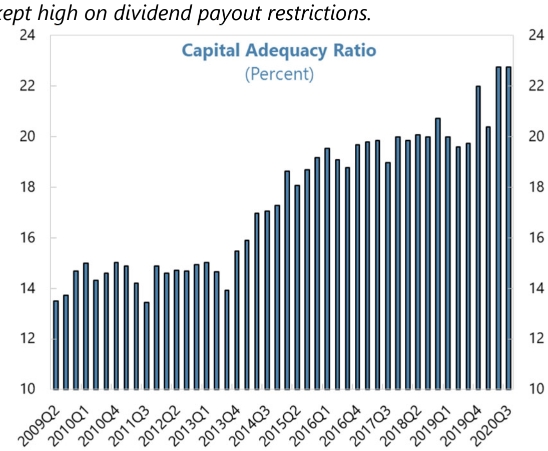
... while share of FX loans in total credit has continued its long decline to around 30 percent.



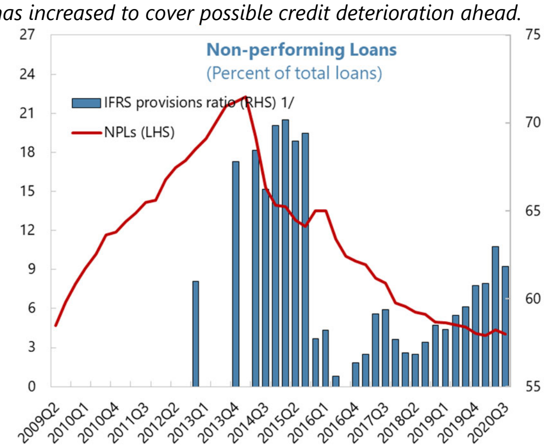
Liquidity is ample as the deposit-to-loan ratio has been on an uptrend in the past few years, and retail deposits are the dominant and stable source of bank liquidity.



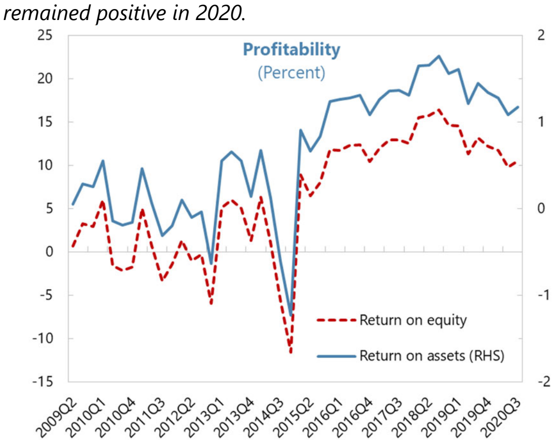
Capital buffers are substantial, and capital ratios grew to more than 20 percent prior to the COVID crisis, and have been kept high on dividend payout restrictions.



NPLs ratios remain low so far in the crisis, while provisioning has increased to cover possible credit deterioration ahead.



...while bank profitability has declined but on average remained positive in 2020.

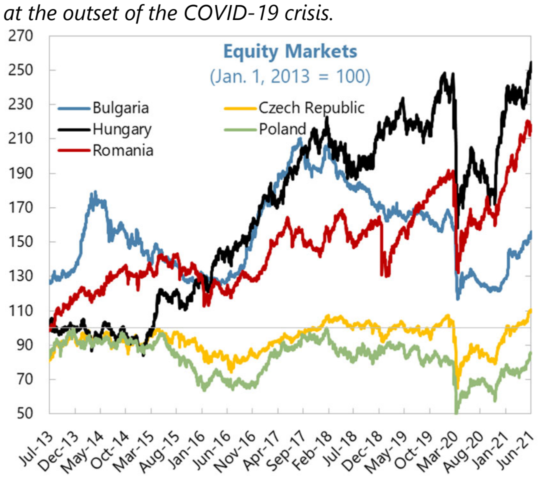


Sources: Dxtime; and National Bank of Romania.

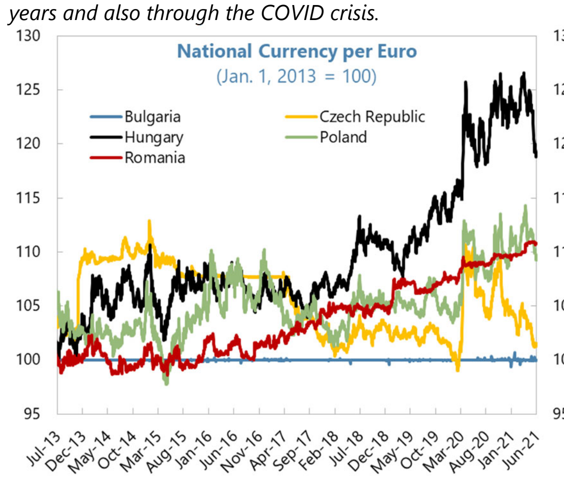
1/ In December 2015, the NBR moved from a national definition to an EBA methodology-based definition of NPL's.

Figure 7. Romania: Financial Developments, 2013–21

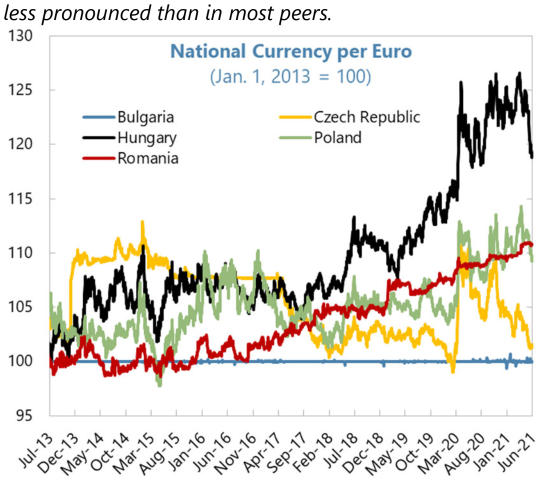
Romania's stock market has fully recovered from the plunge at the outset of the COVID-19 crisis.



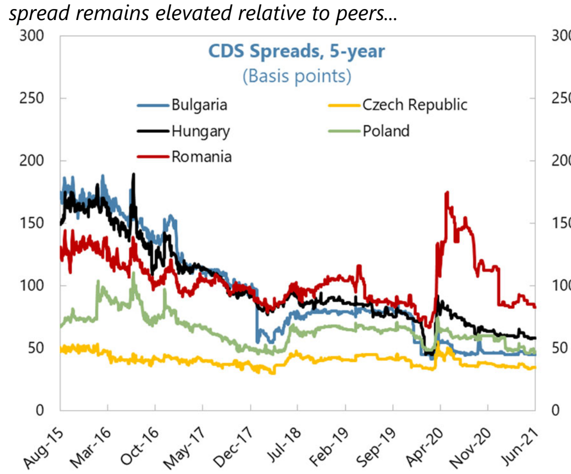
Leu volatility has been modest compared to peers in recent years and also through the COVID crisis.



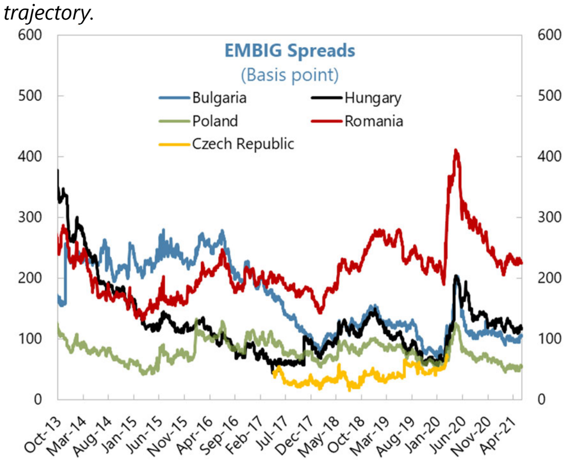
...notwithstanding modest real depreciation in 2020 which was less pronounced than in most peers.



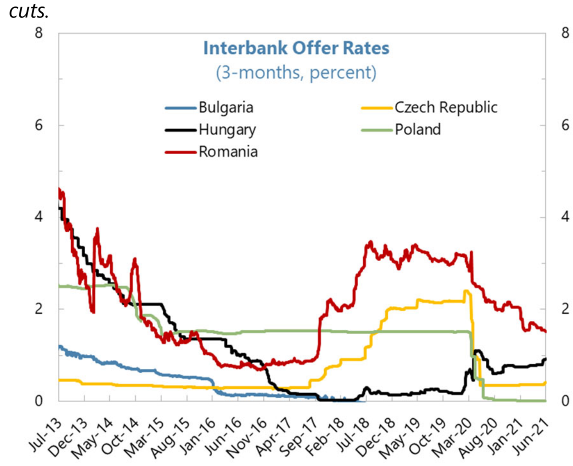
While narrowing after the initial crisis shock, Romania's CDS spread remains elevated relative to peers...



...while Romania's EMBIG spreads have shown a similar trajectory.



Interbank rates also remain higher than in peers, despite rate cuts.



Sources: Bloomberg; and Haver Analytics.

Table 1. Romania: Selected Economic and Social Indicators, 2014–22

	2014	2015	2016	2017	2018	2019	2020 Prel.	2021 Proj.	2022 Proj.
Output and prices	(Annual percentage change)								
Real GDP	3.6	3.0	4.7	7.3	4.5	4.1	-3.9	7.0	4.8
Domestic demand 1/	3.8	4.6	4.9	8.9	5.9	5.1	-2.1	8.4	5.0
Contributions to GDP growth									
Domestic demand 1/	3.7	4.5	4.9	9.1	6.2	5.5	-2.0	8.3	5.4
Private consumption	2.5	3.6	4.9	6.8	5.0	2.8	-3.5	5.6	3.5
Government consumption	0.9	-0.6	0.0	0.6	0.4	0.9	0.3	0.9	0.3
Net exports	-0.1	-1.5	-0.2	-1.8	-1.8	-1.3	-1.9	-1.3	-0.5
Consumer price index (CPI, average)	1.1	-0.6	-1.6	1.3	4.6	3.8	2.6	3.6	2.7
Consumer price index (CPI, end of period)	0.8	-0.9	-0.5	3.3	3.3	4.0	2.1	4.1	2.9
Core price index (CPI, end of period)	1.2	-3.1	0.3	2.4	2.5	3.7	3.3	3.3	2.9
Producer price index (average)	-0.1	-2.2	-1.8	3.5	5.0	4.0	0.0	...	...
Unemployment rate (average)	6.8	6.8	5.9	4.9	4.2	3.9	5.0	4.9	4.9
Nominal wages, gross 2/	5.3	8.5	12.8	14.8	35.4	13.0	6.4	5.0	6.4
Saving and Investment	(In percent of GDP)								
Gross domestic investment 1/	24.8	25.1	23.4	23.4	22.8	23.7	24.5	24.4	24.8
Gross national savings	24.5	24.3	21.8	20.3	18.1	18.8	19.3	18.9	19.6
General government finances 3/									
Revenue	32.0	32.8	28.9	28.0	29.2	28.9	28.9	30.3	30.0
Expenditure	33.7	34.2	31.3	30.8	32.0	33.5	38.6	37.1	35.8
Fiscal balance	-1.7	-1.4	-2.4	-2.8	-2.8	-4.6	-9.7	-6.8	-5.8
External financing (net)	1.9	-0.5	0.7	0.8	0.6	0.9	4.6	3.3	2.6
Domestic financing (net)	1.2	1.0	2.2	2.4	2.5	3.2	5.4	3.5	3.2
Primary balance	-0.2	-0.1	-1.1	-1.7	-1.5	-3.5	-8.4	-5.3	-4.2
Structural fiscal balance 4/	-0.1	0.1	-1.7	-3.5	-3.7	-5.1	-6.1	-5.5	-5.6
Gross public debt (including guarantees)	40.4	39.4	39.0	36.8	36.5	36.8	49.8	51.5	53.5
Money and credit	(Annual percentage change)								
Broad money (M3)	8.4	9.3	9.7	11.5	8.8	10.9	15.3	10.2	9.5
Credit to private sector	-3.3	3.0	1.2	5.7	8.0	6.6	5.5	9.7	7.9
Interest rates, eop	(In percent)								
NBR policy rate	2.50	1.75	1.75	1.75	2.5	2.5	1.5	...	...
NBR lending rate (Lombard)	4.75	4.25	3.25	2.75	3.5	3.5	2.0	...	...
Interbank offer rate (1 week)	0.7	0.6	0.6	1.5	2.4	2.9	1.8	...	...
Balance of payments	(In percent of GDP)								
Current account balance	-0.3	-0.8	-1.6	-3.1	-4.6	-4.9	-5.2	-5.4	-5.2
Merchandise trade balance	-4.4	-5.1	-5.7	-6.8	-7.5	-8.0	-8.8	-9.1	-8.8
Exports (goods)	31.1	30.7	30.7	30.5	30.2	28.3	26.4	28.2	29.0
Imports (goods)	-35.5	-35.7	-36.4	-37.3	-37.7	-36.3	-35.2	-37.3	-37.8
Capital account balance	2.6	2.4	2.5	1.2	1.2	1.3	1.9	2.4	2.4
Financial account balance	0.2	0.3	0.2	-1.9	-2.1	-2.2	-5.8	-5.0	-5.1
Foreign direct investment balance	-1.8	-1.8	-2.7	-2.6	-2.4	-2.2	-0.9	-1.6	-1.7
International investment position	-56.5	-53.8	-48.7	-46.5	-43.7	-43.3	-46.9	-46.1	-45.7
Gross official reserves	23.6	22.2	22.3	19.8	18.0	16.8	19.5	19.2	18.9
Gross external debt	62.9	57.0	54.7	51.8	48.8	49.2	57.7	57.7	57.4
Exchange rates									
Lei per euro (end of period)	4.48	4.52	4.54	4.66	4.66	4.78	4.87	…	…
Lei per euro (average)	4.44	4.44	4.49	4.57	4.65	4.75	4.84	…	…
Real effective exchange rate									
CPI based (percentage change)	0.7	-3.4	-1.8	-1.5	2.8	-0.4	1.5	…	…
GDP deflator based (percentage change)	1.4	0.3	2.1	1.7	4.3	2.4	2.4	…	…
Memorandum Items:									
Nominal GDP (in bn RON)	669.7	711.9	763.7	857.9	951.7	1058.2	1055.5	1176.9	1270.7
Potential output growth	3.2	3.3	3.5	3.7	3.7	3.7	1.5	5.4	3.8

Social and Other Indicators

GDP per capita: US$12,797 (2020); **GDP per capita, PPP:** current international $32358.3 (2019)

People at risk of poverty or social exclusion: 30.4% (2020)

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

1/ Including potential statistical uncertainty related to large inventory contribution in 2018.

2/ Year 2018 reflects the upward adjustment of gross wages due to the implementation of the shift in social security contributions from employers to employees, which kept net wages and costs to employers unaffected (see Box 1 in the 2018 Article IV staff report).

3/ General government finances refer to cash data.

4/ Fiscal balance (cash basis) adjusted for the automatic effects of the business cycle and one-off effects.

Table 2. Romania: Medium-Term Macroeconomic Framework, Current Policies, 2017–26

	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026
				Prel.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
GDP and prices (annual percent change)										
Real GDP	7.3	4.5	4.1	-3.9	7.0	4.8	3.8	3.8	3.6	3.5
Agriculture 1/	11.2	9.0	-4.5	-11.8	...	...	...	...	...	...
Non-Agriculture 1/	7.2	4.2	4.5	-2.5	...	...	...	...	...	...
Real domestic demand	8.9	5.9	5.1	-2.1	8.4	5.0	4.0	3.7	3.5	3.7
Consumption 2/	9.5	6.8	4.7	-3.6	7.7	4.7	3.2	3.3	3.1	3.3
Investment (GFCF) 2/	3.5	-1.1	13.0	6.8	6.4	6.4	6.4	4.8	4.8	4.8
Exports	7.8	5.3	4.6	-9.7	11.7	11.8	7.1	7.2	7.3	6.8
Imports	11.5	8.6	6.8	-5.1	12.4	11.0	6.9	6.5	6.7	6.6
Consumer price index (CPI, average)	1.3	4.6	3.8	2.6	3.6	2.7	2.8	2.6	2.5	2.5
Consumer price index (CPI, end of period)	3.3	3.3	4.0	2.1	4.1	2.9	2.7	2.5	2.5	2.5
Saving and investment (in percent of GDP)										
Gross national saving	20.3	18.1	18.8	19.3	18.9	19.6	20.3	20.7	21.3	21.8
Gross domestic investment 2/	23.4	22.8	23.7	24.5	24.4	24.8	25.4	25.6	25.9	26.3
Government	3.3	3.3	4.1	5.1	5.6	5.6	5.6	5.7	5.7	5.8
Private 2/	20.2	19.4	19.6	19.4	18.8	19.2	19.8	19.8	20.2	20.5
General government (in percent of GDP)										
Revenue	28.0	29.2	28.9	28.9	30.3	30.0	29.6	29.7	29.9	30.1
Expenditure	30.8	32.0	33.5	38.6	37.1	35.8	35.4	35.4	35.3	35.3
Fiscal balance	-2.8	-2.8	-4.6	-9.7	-6.8	-5.8	-5.8	-5.6	-5.4	-5.2
Structural fiscal balance 3/	-3.5	-3.7	-5.1	-6.1	-5.5	-5.6	-5.6	-5.5	-5.3	-5.0
Gross general government debt (direct debt only)	34.7	34.5	35.0	46.6	48.7	50.9	53.3	55.6	57.6	59.3
Gross general government debt (including guarantees)	36.8	36.5	36.8	49.8	51.5	53.5	55.7	57.9	59.7	61.4
Monetary aggregates (annual percent change)										
Broad money (M3)	11.5	8.8	10.9	15.3	10.2	9.5	8.7	8.5	8.5	8.5
Credit to private sector	5.7	8.0	6.6	5.5	9.7	7.9	6.7	6.6	5.7	5.7
Balance of payments (in percent of GDP)										
Current account	-3.1	-4.6	-4.9	-5.2	-5.4	-5.2	-5.1	-4.9	-4.7	-4.5
Trade balance	-6.8	-7.5	-8.0	-8.8	-9.1	-8.8	-8.6	-8.4	-8.3	-8.3
Services balance	4.4	4.1	3.9	4.3	4.2	4.2	4.2	4.3	4.4	4.5
Income balance	-1.4	-1.8	-1.4	-1.7	-1.7	-1.7	-1.7	-1.7	-1.7	-1.6
Transfers balance	0.8	0.6	0.7	0.9	1.1	1.0	1.0	0.9	0.9	0.9
Capital account balance	1.2	1.2	1.3	1.9	2.4	2.4	2.4	2.7	2.9	3.1
Financial account balance	-1.9	-2.1	-2.2	-5.8	-5.0	-5.1	-5.8	-5.4	-5.8	-5.6
Foreign direct investment, balance	-2.6	-2.4	-2.2	-0.9	-1.6	-1.7	-1.9	-2.0	-2.1	-2.1
Memorandum items:										
Gross international reserves (in billions of euros)	37.1	36.8	37.5	42.5	45.9	49.0	52.9	56.4	60.8	65.1
Gross international reserves (in months of next year's imports)	4.8	4.4	4.9	4.8	4.7	4.7	4.7	4.6	4.6	4.6
International investment position (in percent of GDP)	-46.5	-43.7	-43.3	-46.9	-46.1	-45.7	-45.5	-45.5	-45.4	-45.2
Real effective exchange rate (annual average, percent change)	-1.5	2.8	-0.4	1.5	1.1	1.7	1.9	1.0	0.8	-0.6
External debt (in percent of GDP)	51.8	48.8	49.2	57.7	57.7	57.4	57.3	57.6	57.6	57.5
Short-term external debt (in percent of GDP)	15.4	15.4	15.9	15.2	15.2	15.1	15.1	15.1	15.1	15.1
Export volume (percent change)	7.8	5.3	4.6	-10.7	11.7	11.8	7.1	7.2	7.3	6.8
Import volume (percent change)	11.5	8.6	6.8	-4.5	12.4	11.0	6.9	6.5	6.7	6.6
Terms of trade (merchandise, percent change)	-2.3	0.6	0.0	5.1	0.6	0.0	0.1	0.0	0.2	0.4
Nominal GDP (in billions of lei)	857.9	951.7	1,058.2	1,055.5	1,176.9	1,270.7	1,361.6	1,452.7	1,548.0	1,645.6
Nominal GDP (in millions of Euros)	187,801	204,519	223,000	218,219	239,088	258,986	279,594	298,288	317,865	337,906
Output gap (percent of potential GDP)	1.9	2.6	3.0	-2.4	-1.0	0.0	0.0	0.0	0.0	0.0
Potential GDP (percent change)	3.7	3.7	3.7	1.5	5.4	3.8	3.8	3.8	3.6	3.6

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

1/ Based on gross value added data from the National Institute of Statistics (NIS) in Romania. Note that there is a small discrepancy between the supply side GDP data from the NIS and the demand side data from Eurostat.

2/ Domestic demand components potentially distorted by statistical issues related to large inventory contribution in 2018, which from past experience are subsequently revised to reallocate to consumption and investment components. Investment in 2019 also potentially distorted by construction sector incentives to encourage reported activity.

3/ Actual fiscal balance adjusted for the automatic effects related to the business cycle and one-off effects.

Table 3. Romania: Balance of Payments, 2017–26

	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026
				Prel.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
Current account balance	-5.8	-9.5	-10.9	-11.4	-13.0	-13.6	-14.2	-14.5	-14.9	-15.1
Merchandise trade balance	-12.8	-15.3	-17.9	-19.2	-21.7	-22.7	-24.0	-25.0	-26.4	-28.0
Exports (f.o.b.)	57.2	61.8	63.1	57.6	67.4	75.1	80.5	87.1	94.8	102.4
Imports (f.o.b.)	70.0	77.2	80.9	76.7	89.1	97.8	104.4	112.2	121.2	130.3
Services balance	8.2	8.4	8.7	9.4	10.2	10.9	11.7	12.7	13.9	15.2
Exports of non-factor services	21.7	23.8	27.1	23.8	27.8	31.2	33.5	36.4	39.7	43.0
Imports of non-factor services	13.5	15.4	18.4	14.3	17.7	20.3	21.8	23.7	25.8	27.9
Primary income, net	-2.7	-3.8	-3.2	-3.7	-4.1	-4.3	-4.7	-5.0	-5.3	-5.5
Receipts	5.2	5.3	6.3	5.8	6.1	6.4	6.7	6.9	7.2	7.4
Payments	7.9	9.0	9.5	9.5	10.2	10.8	11.4	11.9	12.5	13.0
Secondary income, net	1.5	1.3	1.5	2.0	2.6	2.6	2.8	2.8	2.9	3.2
Capital account balance	2.2	2.5	2.9	4.2	5.3	5.3	5.3	5.9	6.4	6.9
Financial account balance	-3.5	-4.4	-4.9	-13.0	-11.1	-11.4	-12.9	-12.0	-13.0	-12.5
Foreign direct investment balance	-4.9	-4.9	-4.8	-1.9	-3.7	-4.5	-5.2	-5.9	-6.6	-7.2
Portfolio investment balance	-3.1	-2.8	-2.5	-13.9	-8.3	-7.9	-8.9	-7.5	-7.9	-6.9
Other investment balance	4.4	3.4	2.5	2.7	0.9	1.1	1.2	1.4	1.5	1.6
General government	2.0	1.0	0.4	1.1	0.0	0.0	0.0	0.0	0.0	0.0
Domestic banks	1.3	0.8	1.6	0.5	1.0	1.1	1.2	1.3	1.4	1.4
Other private sector	-0.6	-0.1	0.5	-1.2	-0.1	-0.1	0.0	0.1	0.1	0.1
Errors and omissions	0.5	1.8	2.9	-0.2	0.0	0.0	0.0	0.0	0.0	0.0
Multilateral financing	-0.7	-1.4	-1.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
European Commission	-1.2	-1.4	-1.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
World Bank	...	...	0.3	...	...	...	...	...	...	...
EIB/EBRD/IFC	...	...	...	...	...	...	...	...	...	...
Overall balance	-0.2	-2.1	-1.2	5.6	3.3	3.1	3.9	3.4	4.5	4.2
Financing	0.2	2.1	1.2	-5.6	-3.3	-3.1	-3.9	-3.4	-4.5	-4.2
Gross international reserves (increase: -)	-0.4	0.8	0.3	-5.6	-3.3	-3.1	-3.9	-3.4	-4.5	-4.2
Use of Fund credit, net	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Purchases	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Repurchases	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other liabilities, net	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:										
Current account balance	-3.1	-4.6	-4.9	-5.2	-5.4	-5.2	-5.1	-4.9	-4.7	-4.5
Foreign direct investment balance	-2.6	-2.4	-2.2	-0.9	-1.6	-1.7	-1.9	-2.0	-2.1	-2.1
Merchandise trade balance	-6.8	-7.5	-8.0	-8.8	-9.1	-8.8	-8.6	-8.4	-8.3	-8.3
Exports	30.5	30.2	28.3	26.4	28.2	29.0	28.8	29.2	29.8	30.3
Imports	37.3	37.7	36.3	35.2	37.3	37.8	37.3	37.6	38.1	38.6
Gross external financing requirement	20.4	23.9	23.1	24.2	21.3	22.1	21.9	21.8	21.0	20.6
capital account	1.2	1.2	1.3	1.9	2.2	2.1	1.9	2.0	2.0	2.0
Terms of trade (merchandise)	-2.35	0.6	0.0	5.1	0.6	0.0	0.1	0.0	0.2	0.4
Export volume	7.8	5.3	4.6	-10.7	11.7	11.8	7.1	7.2	7.3	6.8
Import volume	11.5	8.6	6.8	-4.5	12.4	11.0	6.9	6.5	6.7	6.6
Export prices	3.1	3.0	0.6	1.0	4.9	-0.2	0.2	1.1	1.5	1.2
Import prices	2.9	2.0	0.4	-4.0	4.3	-0.4	0.0	1.0	1.4	0.9
Gross international reserves	37.1	36.8	37.5	42.5	45.9	49.0	52.9	56.4	60.8	65.1
Excluding Fund credit	37.1	36.8	37.5	42.5	45.9	49.0	52.9	56.4	60.8	65.1
months of imports	4.8	4.4	4.9	4.8	4.7	4.7	4.7	4.6	4.6	4.6
GDP	187.8	204.5	223.0	218.2	239.1	259.0	279.6	298.3	317.9	337.9

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

Table 4. Romania: Gross External Financing Requirements, 2016–21

	2016	2017	2018	2019	2020	2021 Proj.
Total financing requirements	**44.1**	**44.3**	**48.4**	**50.4**	**54.4**	**52.0**
Current account deficit	3.5	-5.8	9.0	10.5	11.4	13.0
Short-term debt	30.3	26.4	28.6	29.5	31.7	32.3
Public sector	9.0	6.8	7.0	7.9	9.6	9.6
Banks	8.8	6.3	7.5	6.4	6.2	6.3
Corporates	12.5	13.3	14.2	15.2	16.0	16.4
Maturing medium- and long-term debt	8.2	8.3	8.1	7.8	5.1	5.7
Public sector	1.3	0.8	1.0	1.7	0.8	2.0
Banks	2.5	3.5	2.9	2.0	1.2	1.0
Corporates	4.4	3.9	4.2	4.0	3.1	2.7
Other net capital outflows 1/	2.1	3.6	2.7	2.6	**6.2**	**1.0**
Total financing sources	**45.7**	**44.9**	**47.7**	**48.9**	**60.2**	**55.9**
Foreign direct investment, net	4.5	4.9	4.9	4.8	1.9	3.7
Capital account inflows	4.3	2.2	2.5	2.9	4.2	5.3
Short-term debt	29.9	27.6	29.9	30.3	32.0	33.4
Public sector	9.1	6.8	6.8	7.9	9.6	9.6
Banks	7.5	6.8	7.7	6.4	6.0	6.3
Corporates	13.3	14.0	15.4	15.9	16.4	17.6
Medium- and long-term debt	7.0	10.2	10.3	10.9	22.2	13.5
Public sector	2.2	3.7	4.4	5.4	17.8	9.8
Banks	0.7	2.0	1.8	0.9	0.8	1.0
Corporates	4.1	4.5	4.2	4.6	3.6	2.7
Errors and omissions	0.8	0.6	1.3	2.5	-0.2	0.0
Increase in gross international reserves	2.3	0.4	-0.8	-0.3	5.6	3.9
Financing gap	**-0.1**	**-0.7**	**-1.4**	**-1.2**	**0.0**	**0.0**
Memorandum items:						
Gross external financing needs (in percent of GDP)	25.9	23.6	23.7	22.6	24.9	21.7
Rollover rates for amortizing debt ST (in percent)						
Public sector	101	100	98	101	100	100
Banks	85	107	103	99	97	100
Corporates	106	105	109	105	102	107
Rollover rates for amortizing debt MLT (in percent)						
Public sector	169	456	428	310	2192	485
Banks	29	56	61	44	71	104
Corporates	93	114	100	114	116	99
Rollover rates for total amortizing debt (in percent)						
Public sector	110	138	140	139	263	167
Banks	72	89	91	86	93	101
Corporates	103	107	107	107	105	106
Gross international reserves	37.9	37.1	36.8	37.5	42.5	45.9
Coverage of gross international reserves						
Months of imports of GFNS (next year)	5.4	4.8	4.4	4.9	4.8	4.7
Short-term external debt (in percent)	116.6	94.0	90.8	90.3	112.5	104.7

Sources: Romanian authorities; and IMF staff estimates and projections.
1/ Includes portfolio equity, financial derivatives and other investments.

Table 5a. Romania: General Government Operations, 2017–2026 1/

(In percent of GDP)

	2017	2018	2019	2020	2021 Proj.	2022 Proj.	2023 Proj.	2024 Proj.	2025 Proj.	2026 Proj.
Revenue	28.0	29.2	28.9	28.9	30.3	30.0	29.6	29.7	29.9	30.1
Taxes	24.7	25.3	25.3	25.0	25.6	25.3	25.1	25.2	25.4	25.6
Corporate income tax	1.9	1.9	1.9	1.7	1.8	1.8	1.8	1.8	1.8	1.8
Personal income tax	3.6	2.5	2.3	2.4	2.3	2.3	2.3	2.3	2.3	2.4
VAT	6.2	6.3	6.2	5.8	6.5	6.4	6.3	6.3	6.3	6.3
Excises	3.1	3.0	3.0	2.9	3.0	3.0	3.0	3.0	3.0	3.0
Customs duties	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Social security contributions	8.4	10.3	10.5	10.7	10.6	10.5	10.3	10.4	10.6	10.8
Other taxes	1.4	1.2	1.3	1.4	1.4	1.3	1.3	1.3	1.3	1.3
Nontax revenue	2.5	2.9	2.6	2.3	2.5	2.4	2.4	2.3	2.3	2.3
Capital revenue	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Grants, including EU disbursements 2/	0.6	0.6	1.0	1.6	2.2	2.2	2.1	2.2	2.1	2.2
Expenditure	30.8	32.0	33.5	38.6	37.1	35.8	35.4	35.4	35.3	35.3
Current expenditure	28.7	29.7	31.0	35.6	34.3	33.0	32.7	32.6	32.5	32.6
Compensation of employees	8.1	9.1	9.7	10.4	9.4	9.1	9.0	8.9	8.9	8.9
Goods and services	4.7	4.7	5.0	5.4	5.0	4.7	4.6	4.5	4.5	4.4
Interest	1.2	1.4	1.1	1.4	1.6	1.7	1.8	1.9	1.9	2.0
Subsidies	0.7	0.7	0.7	0.8	0.7	0.6	0.6	0.6	0.5	0.5
Transfers	13.9	13.8	14.5	17.6	17.6	16.9	16.6	16.7	16.7	16.7
Pensions	6.7	6.6	6.6	7.7	7.6	7.5	7.5	7.6	7.7	7.9
Other social transfers	4.1	4.0	4.2	5.4	4.6	4.2	4.0	3.9	3.7	3.6
Other transfers 3/	2.5	2.5	2.9	3.7	4.8	4.6	4.6	4.7	4.7	4.8
Other spending	0.6	0.7	0.7	0.8	0.6	0.6	0.5	0.5	0.5	0.5
Projects with external credits	0.0	0.0	0.0	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Capital expenditure 4/	2.3	2.5	2.8	3.1	3.0	2.9	2.9	2.9	2.9	2.9
Reserve fund	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net lending and expense refunds	-0.1	-0.2	-0.3	-0.2	-0.2	-0.2	-0.2	-0.2	-0.2	-0.2
Fiscal balance	-2.8	-2.8	-4.6	-9.7	-6.8	-5.8	-5.8	-5.6	-5.4	-5.2
Primary balance	-1.7	-1.5	-3.5	-8.4	-5.3	-4.2	-4.1	-3.8	-3.5	-3.2
Financing	2.8	2.8	4.6	9.7	6.8	5.8	5.8	5.6	5.4	5.2
External borrowing (net)	0.8	0.6	0.9	4.6	3.3	2.6	2.6	2.4	2.4	2.2
Domestic borrowing (net)	2.4	2.5	3.2	5.4	3.5	3.2	3.2	3.2	3.0	3.0
Use of deposits	-0.3	-0.2	0.2	-0.3	0.0	0.0	0.0	0.0	0.0	0.0
Privatization proceeds	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financial liabilities										
Gross general-government debt 5/	36.8	36.5	36.8	49.8	51.5	53.5	55.7	57.9	59.7	61.4
Gross general-government debt excl. guarantees	34.7	34.5	35.0	46.6	48.7	50.9	53.3	55.6	57.6	59.3
External	17.0	16.1	16.3	21.9	23.0	23.9	24.9	25.8	26.6	27.2
Domestic	17.7	18.4	18.7	24.7	25.7	27.0	28.4	29.8	31.0	32.1
Memorandum items:										
Total capital spending	3.3	3.3	4.1	5.1	5.6	5.6	5.6	5.7	5.7	5.8
Fiscal balance (ESA2010 basis)	-2.9	-3.0	-4.4	-9.3	…	…	…	…	…	…
Output gap 6/	1.9	2.6	3.0	-2.4	-1.0	0.0	0.0	0.0	0.0	0.0
Cyclically adjusted balance 7/	-3.4	-3.7	-5.6	-8.7	-6.5	-5.8	-5.8	-5.7	-5.4	-5.2
CAPB 7/	-2.3	-2.3	-4.4	-7.5	-5.0	-4.2	-4.1	-3.9	-3.5	-3.2
Structural fiscal balance 7/	-3.5	-3.7	-5.1	-6.1	-5.5	-5.6	-5.6	-5.5	-5.3	-5.0
Gross general government debt (authorities definition) 8/	42.9	42.1	42.4	55.9	…	…	…	…	…	…
Nominal GDP (in billions of lei)	857.9	951.7	1,058.2	1,055.5	1,176.9	1,270.7	1,361.6	1,452.7	1,548.0	1,645.6

1/ Unless otherwise noted, the table is on a cash basis following GFSM 86. The general government is composed of the central government, local governments, social security funds, and the road fund company.

2/ For data comparability, does not include the EU agricultural subsidies reflected in authorities' budget reports starting 2016.

3/ Includes EU-financed capital projects. For data comparability, does not include the EU agricultural subsidies reflected in authorities' budget reports starting 2016.

4/ Does not include all capital spending.

5/ Total consolidated general-government debt, including state government debt, local government debt, and guarantees.

6/ Percentage deviation of actual from potential GDP.

7/ Expressed in percentage of potential GDP.

8/ Includes guarantees and intra-governmental debt.

Table 5b. Romania: General Government Operations, 2017–2026

(In millions of lei)

	2017	2018	2019	2020	2021 Proj.	2022 Proj.	2023 Proj.	2024 Proj.	2025 Proj.	2026 Proj.
Revenue	239,867	277,452	305,947	304,934	356,401	381,170	403,706	432,033	462,726	495,883
Taxes	211,947	240,611	267,840	264,132	301,154	321,958	342,101	365,683	392,989	421,903
Corporate income tax	16,149	17,875	20,331	18,190	21,285	22,982	24,626	26,272	27,997	29,762
Personal income tax	30,751	23,631	24,320	25,257	26,969	28,877	30,962	33,152	35,895	38,852
VAT	53,544	59,609	65,421	60,817	76,399	80,881	85,417	91,200	97,050	103,056
Excises	26,604	28,518	31,463	30,715	34,846	37,765	40,466	43,171	46,005	48,905
Customs duties	933	1,050	1,160	1,120	1,336	1,472	1,563	1,682	1,820	1,958
Social security contributions	71,706	98,101	111,473	112,884	124,395	132,914	140,920	150,971	163,864	177,858
Other taxes	12,260	11,827	13,672	15,149	15,924	17,067	18,147	19,233	20,359	21,510
Nontax revenue	21,874	27,189	27,093	23,975	29,001	30,718	32,393	34,043	35,745	37,475
Interest Revenue	400	127	500	498	556	600	643	686	731	777
Capital revenue	830	849	867	776	830	870	903	938	971	1,005
Grants 1/	5,186	5,511	10,150	16,390	25,416	27,624	28,309	31,369	33,021	35,500
Financial operations and other	29	3,291	-4	-339	0	0	0	0	0	0
Expenditure	264,161	304,302	354,247	407,189	436,931	454,937	482,341	514,059	546,442	581,391
Current expenditure	245,814	282,516	327,846	375,822	403,108	419,874	444,771	473,978	503,729	535,986
Compensation of employees	69,611	86,138	102,341	109,964	110,096	115,652	122,412	129,391	137,669	146,476
Goods and services	40,685	44,612	52,782	57,012	59,163	59,982	62,992	65,946	68,978	72,060
Interest	10,125	12,944	12,151	14,510	18,312	21,312	24,064	26,997	30,057	33,182
Subsidies	6,201	6,670	7,108	8,140	7,732	7,637	7,850	8,054	8,260	8,470
Transfers	118,914	131,765	153,032	185,439	207,133	214,565	226,675	242,759	257,881	274,858
Pensions	57,081	62,885	70,074	81,434	89,505	94,985	101,587	109,981	119,290	129,212
Other social transfers	35,490	38,479	44,665	57,119	54,094	53,604	55,097	56,532	57,974	59,451
Other transfers 2/	21,112	23,368	30,672	38,545	56,386	58,675	62,529	68,629	72,844	78,261
Other spending	5,232	7,032	7,620	8,341	7,148	7,301	7,462	7,617	7,773	7,932
Projects with external credits	277	388	432	757	672	726	778	830	884	940
Capital expenditure 3/	19,559	23,585	30,070	33,178	35,842	37,243	39,906	42,575	45,369	48,229
Reserve fund	0	0	0	0	0	0	0	0	0	0
Net lending and expense refunds	-1,212	-1,799	-3,669	-1,811	-2,019	-2,181	-2,337	-2,493	-2,656	-2,824
Fiscal balance	-24,295	-26,851	-48,300	-102,255	-80,530	-73,766	-78,635	-82,027	-83,716	-85,509
Primary balance	-14,570	-14,034	-36,649	-88,244	-62,773	-53,054	-55,213	-55,715	-54,389	-53,103
Financing	24,295	26,851	48,300	102,255	80,530	73,766	78,635	82,027	83,716	85,509
External borrowing (net)	6,508	6,103	9,683	48,416	39,339	33,103	35,063	35,542	37,276	36,140
Domestic borrowing (net)	20,321	24,039	33,748	56,677	41,191	40,663	43,572	46,485	46,440	49,368
Use of deposits	-2,158	-2,149	1,809	-2,749	0	0	0	0	0	0
Privatization proceeds	0	0	0	0	0	0	0	0	0	0
Financial liabilities										
Gross general-government debt 4/	316,015	347,076	389,662	525,685	606,215	679,981	758,615	840,642	924,358	1,009,866
Gross general-government debt excl. guarantees	297,953	328,493	370,467	492,204	572,733	646,500	725,134	807,161	890,877	976,385
External	145,909	153,250	172,706	231,255	270,594	303,697	338,760	374,301	411,577	447,717
Domestic	152,044	175,243	197,761	260,949	302,139	342,803	386,375	432,860	479,300	528,668
Memorandum item:										
Total capital spending	28,065	31,684	43,610	53,926	65,992	71,381	76,315	83,480	88,811	95,369
Gross general government debt (authorities definition) 5/	368,449	400,923	449,015	590,363	…	…	…	…	…	…

1/ For data comparability, does not include the EU agricultural subsidies reflected in authorities' budget reports starting 2016.

2/ Includes EU-financed capital projects. For data comparability, does not include the EU agricultural subsidies reflected in authorities' budget reports starting 2016.

3/ Does not include all capital spending.

4/ Total consolidated general-government debt, including state government debt, local government debt, and guarantees.

5/ Includes guarantees and intra-governmental debt.

Table 5c. Romania: Consolidated General Government Balance Sheet, 2014-19

(In millions of lei, unless otherwise indicated)

	2014	2015	2016	2017	2018	2019
Net worth and its changes:	**522,273**	**559,802**	**593,199**	**617,070**	**653,086**	**668,976**
Nonfinancial assets	**665,701**	**706,420**	**757,194**	**796,236**	**841,122**	**901,587**
Fixed assets	648,789	687,028	737,410	775,136	817,896	876,245
Buildings and structures	....	....	....	....	....	....
Machinery and equipment	....	....	....	....	....	....
Other fixed assets	....	....	....	....	....	....
Inventories	16,912	19,392	19,784	21,100	23,226	25,342
Valuables	....	....	....	....	....	....
Nonproduced assets	....	....	....	....	....	....
Financial assets	**186,827**	**190,783**	**204,677**	**207,324**	**227,097**	**236,904**
by instrument						
Monetary gold and SDRs	-	-	-	-	-	-
Currency and deposits	49,973	46,751	62,155	58,116	50,930	36,601
Securities other than shares	197	100	104	247	1,581	2,039
Loans	15,043	16,056	16,719	19,139	23,854	27,902
Shares and other equity	74,762	72,799	72,328	77,247	90,423	105,167
Insurance technical reserves	23	123	52	55	64	96
Financial derivatives	-	-	-	-	-	-
Other accounts receivable	46,829	54,955	53,319	52,520	60,246	65,099
by debtor						
Domestic	166,962	165,285	179,723	182,538	196,132	198,538
Foreign	19,865	25,498	24,953	24,786	30,965	38,366
Liabilities	**330,255**	**337,401**	**368,672**	**386,490**	**415,133**	**469,516**
by instrument						
Special Drawing Rights (SDRs)	-	-	-	-	-	-
Currency and deposits	6,755	8,754	8,409	7,412	6,954	9,183
Securities other than shares	199,583	210,816	228,992	249,911	278,897	336,144
Loans	75,256	69,395	66,106	59,924	53,658	51,055
Shares and other equity	-	-	-	-	73	100
Insurance technical reserves	202	259	303	358	388	417
Financial derivatives	-	-	-	-	-	-
Other accounts payable	48,460	48,177	64,862	68,885	75,163	72,618
by debtor						
Domestic	173,694	182,944	197,612	204,204	227,077	259,632
Foreign	156,561	154,456	171,059	182,287	188,056	209,883
Memorandum items						
Net financial worth	(143,428)	(146,618)	(163,995)	(179,166)	(188,036)	(232,611)
Maastricht debt	262,195	269,151	284,999	300,750	330,519	373,497
Memorandum:						
Nominal GDP (Lei - billions)	669.7	711.9	763.7	857.9	951.7	1,058.2

Sources: Romanian authorities; Eurostat; and IMF staff calculations.

Table 6. Romania: Monetary Survey, 2014-21
(In millions of lei, unless otherwise indicated; end of period)

	2014	2015	2016	2017	2018	2019	2020 Prel.	2021 Proj.
				I. Banking System				
Net foreign assets	**94,282**	**108,650**	**144,983**	**158,989**	**166,578**	**181,847**	**236,505**	**249,158**
In millions of euros	21,035	24,014	31,927	34,120	35,716	38,049	48,570	51,162
o/w commercial banks	-11,778	-9,799	-5,781	-1,691	-1,231	1,255	7,929	8,880
Net domestic assets	**167,549**	**177,605**	**169,151**	**191,123**	**214,498**	**240,781**	**250,945**	**288,013**
General government credit, net	39,194	46,676	36,415	46,132	56,699	81,666	89,139	102,869
Private sector credit	211,164	217,399	220,101	232,603	251,100	267,574	282,370	309,708
Other	-82,809	-86,470	-87,365	-87,613	-93,302	-108,459	-120,564	-124,564
Broad Money (M3)	**261,831**	**286,256**	**314,135**	**350,112**	**381,075**	**422,629**	**487,450**	**537,170**
Money market instruments	258	129	109	107	0	0	0	0
Intermediate money (M2)	261,573	286,126	314,026	350,005	381,075	422,629	487,450	537,170
Narrow money (M1)	118,582	149,550	179,980	210,636	235,126	276,936	337,559	420,605
Currency in circulation	39,890	46,482	54,672	63,273	67,704	74,122	88,163	109,853
Overnight deposits	78,691	103,069	125,308	147,364	167,422	202,813	249,396	310,752
				II. National Bank of Romania				
Net foreign assets	**147,071**	**152,988**	**171,235**	**166,868**	**172,318**	**175,849**	**197,894**	**205,912**
In millions of euros	32,813	33,813	37,708	35,811	36,947	36,794	40,640	42,282
Net domestic assets	**-78,694**	**-78,998**	**-85,769**	**-69,018**	**-71,968**	**-67,600**	**-98,142**	**-81,620**
General government credit, net	-41,757	-37,675	-47,449	-41,079	-37,424	-23,101	-88,593	-86,593
Credit to banks, net	-24,064	-27,465	-22,897	-13,396	-17,746	-21,037	-5,189	-5,189
Other	-12,873	-13,857	-15,423	-14,543	-16,798	-23,463	-4,360	10,162
Reserve money	**68,377**	**73,990**	**85,466**	**97,850**	**100,350**	**108,249**	**99,752**	**124,293**
				(Annual percent change)				
Broad money (M3)	8.4	9.3	9.7	11.5	8.8	10.9	15.3	10.2
NFA contribution	13.9	5.5	12.7	4.5	2.2	4.0	12.9	2.6
NDA contribution	-5.5	3.8	-3.0	7.0	6.7	6.9	2.4	7.6
Reserve money	-0.4	8.2	15.5	14.5	2.6	7.9	-7.8	24.6
NFA contribution	21.7	8.7	24.7	-5.1	5.6	3.5	20.4	8.0
NDA contribution	-22.1	-0.4	-9.2	19.6	-3.0	4.4	-28.2	16.6
Domestic credit, real	-5.7	6.5	-2.3	5.2	6.9	9.1	4.2	8.0
Private sector, real	-4.1	3.9	1.8	2.3	4.5	2.4	3.4	6.7
Public sector, real	-13.2	20.2	-21.6	22.6	19.0	38.4	6.9	12.3
Broad money (M3), in real terms	7.5	10.4	10.3	7.9	5.4	6.6	13.0	7.2
Private credit, nominal	-3.3	3.0	1.2	5.7	8.0	6.6	5.5	9.7
Memorandum items:								
CPI inflation, eop	0.8	-0.9	-0.5	3.3	3.3	4.0	2.1	2.8
NBR inflation target band	1.5 - 3.5	1.5 - 3.5	1.5 - 3.5	1.5 - 3.5	1.5 - 3.5	1.5 - 3.5	1.5 - 3.5	1.5 - 3.5
Interest rates (percent), end of period								
Policy interest rate	2.75	1.75	1.75	1.75	2.50	2.50	1.50	…
Interbank offer rate, 1 week	0.7	0.6	0.6	1.5	2.4	2.9	1.8	…
Corporate loans 1/	5.9	4.4	3.7	4.9	5.8	5.8	4.6	…
Household time deposits, average 1/	2.8	1.5	0.9	0.8	1.8	2.0	1.5	…
Share of foreign currency private deposits	33.9	33.3	32.3	32.8	34.2	35.4	36.1	…
Share of foreign currency private loans	56.4	49.3	42.8	37.2	34.0	32.4	30.5	…

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

1/ Rates for new local currency denominated transactions.

Table 7. Romania: Financial Soundness Indicators, 2012–20

(In percent)

	2012 Dec.	2013 Dec.	2014 Dec.	2015 Dec.	2016 Dec.	2017 Dec.	2018 Dec.	2019 Dec.	2020 Sept.
Core indicators									
Capital adequacy									
Capital to risk-weighted assets	14.9	15.5	17.6	19.2	19.7	20.0	20.7	22.0	22.8
Tier 1 capital to risk-weighted assets 1/	13.8	14.1	14.6	16.7	17.5	18.0	18.6	20.0	20.8
Asset quality									
Nonperforming loans to total gross loans 2/	18.2	21.9	20.7	13.5	9.6	6.4	5.0	4.4	4.1
IFRS Provisions for NPLs / NPLs	76.7	67.8	56.6	57.7	56.3	57.7	58.5	60.6	61.8
Earnings and profitability									
Return on assets	-0.6	0.0	-1.3	1.2	1.1	1.3	1.6	1.3	1.2
Return on equity 3/	-5.9	0.1	-12.5	11.8	10.4	12.5	14.6	12.2	10.5
Net interest income to operating income	62.3	58.8	58.6	58.5	56.3	58.8	65.4	66.4	68.0
Noninterest expense to operating income (cost to income)	58.7	56.5	55.5	58.4	53.0	55.1	53.2	54.3	53.9
Personnel expense to operating income	26.0	25.5	24.9	26.6	24.7	26.1	25.6	24.6	26.0
Liquidity									
Liquid assets 4/ to total assets	57.6	56.2	57.4	54.1	53.4	53.4	52.6	53.2	53.7
Liquid assets 4/ to short-term liabilities 5/	147.7	156.3	158.9	163.4	156.3	145.6	170.6	165.3	161.0
Foreign exchange risk									
Net open position in foreign exchange, in percent of capital	1.3	2.5	-2.0	0.7	0.5	0.8	0.7	0.9	0.8
Foreign-currency-denominated loans to total loans	62.5	60.9	56.2	49.3	42.8	37.2	34.0	32.4	31.4
Foreign currency liabilities, in percent of total liabilities	37.5	35.9	34.9	33.8	31.1	30.3	30.9	30.3	30.4
Encouraged indicators									
Deposit-taking institutions									
Leverage ratio 6/	8.0	7.9	7.4	8.2	8.9	8.9	9.3	10.2	9.8
Personnel expenses to noninterest expenses	44.3	44.9	45.0	46.1	46.6	47.4	48.2	45.2	48.3
Customer deposits to total (non-interbank) loans	87.3	98.7	109.5	115.6	124.6	130.0	131.3	137.4	143.1
Loan-to-Deposit (LTD) Ratio	117.4	104.6	91.3	85.4	79.1	74.7	73.6	71.0	68.9
Structural indicators (December 2018)									
Number of banks: 34; Number of foreign-owned subsidiaries/branches: 21/7;									

Source: National Bank of Romania.

1/ For 2010, market and operational risk are not used in compiling risk weighted assets.

2/ In December 2015, the NBR moved from a national definition to an EBA methodology-based definition of NPL's.

3/ Return on equity is calculated as net profit/loss to average own capital.

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

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

6/ Tier 1 capital to average assets.

Annex I. Implementation of Past Article IV Recommendations

Key Recommendations (2019 Article IV)	**Policy Actions**
	Fiscal
Fiscal consolidation should start by meeting the 2019 deficit target with quality measures.	Romania's fiscal position continued to deteriorate in 2019. The fiscal deficit was much higher than originally expected (-4.6% of GDP instead of -2.8%) due mainly to the build up of major spending commitments (especially regarding wages and pensions) but also revenue underperformance. This triggered the opening of an Excessive Deficit Procedure (EDP) by the European Union (EU). With the onset of the COVID-19 crisis, multifaceted fiscal response has been provided in 2020 for essential support for jobs and business. In 2021, the new center-right government has signaled a trajectory of fiscal consolidation by capping the 2021 budget deficit close to 7 percent of GDP, and pledging to return the deficit to 3 percent of GDP by 2024.
Measures to lower the deficit should avoid further deterioration of the budget structure (i.e. rigid wages and pension spending) and protect capital spending. Implementation of the new pension law should balance social and equity needs and fiscal costs.	In 2019, share of rigid items increased, and it continued to deteriorate in 2020 given the onset of the pandemic. The government amended the new pension law and capped the 2020 increase at a lower level. The policy measures proposed for 2021 intend to partly correct for pre-pandemic expenditure excesses, including a public sector wage freeze and freezing the pension benefits. Public investment will be supported by a pickup of EU-funded projects, including through new resources under the Next Generation EU (NGEU) funds.
Modernize revenue administration by upgrading IT systems and improving compliance risk management. Strengthen expenditure reviews and the procurement process.	Despite the challenges relating to the COVID-19 pandemic, there was some progress by the revenue administration on developing modern compliance risk management processes, introducing a broad set of e-services and access to external data sources, including financial information from banks. A four-year IT Strategy has identified priorities for further IT deployment, building a more digital administration. Centralized procurement process was launched but its implementation has been slow and limted in scope. Progress on spending reviews has been modest.
	Monetary and financial
Continue tightening monetary policy to curb inflationary pressures.	Inflation ended year 2019 above the target band. NBR maintained tight liquidity management during that year but did not raise policy rates further after the hikes in 2018. Inflation pressures receded with the onset of the COVID-19 crisis and the NBR began reducing policy rates from March 2020. Inflation ended year 2020 in the lower half of the target band.
Arising from the FSAP, address vulnerabilities from exposure of banks to the government and the real estate sector, including continuing to scale back the Prima Casa guarantee program.	No restrictions on exposure of banks to the government were introduced in 2019, and in 2020 following the onset of the pandemic the EU relaxed bank exposure guidance for non-euro area sovereign bonds. The Prima Casa program was continued in 2019 with modifications to expand eligibility, but size of guarantees for 2021 were reduced.
	Structural reforms
Public investment rate should be increased by focusing on public infrastructure and improving utilizatin of EU structural funds.	Public investment rate increased somewhat in 2019, but mostly on the account of domestic public infrastrucutre investment. EU funds absorption remained relatively low in 2019 for the programming period 2014-2020 but showed signs of improvement in 2020. For the coming years, the government is looking to further boost the utilization of EU funds and is preparing a new Recovery and Resilience Plan.
SOE governance reforms require a re-start to raise the quality of public goods and services.	There was no progress with implementation of SOE governance reforms in 2019. The new government in early 2021 pledged to strengthen the governance of state-owned enterprises and introduced tighter monitoring criteria for SOEs.
AML/CFT framework shold be strengthened further. The new AML/CFT legislation should be followed by robust implementation.	The new AML/CFT law, adopted in June 2019, and supplementary legislation from 2019 addresses many of outstanding deficiencies in Romania's AML/CFT framework, bringing Romania to "largely compliant" status with regard to FATF standards. EU AML/CFT directives were fully transposed in May 2021.
Minimum wage hikes should be moderated and linked to a set of objective criteria that reflect productivity developments.	Minimum wages were significantly raised in early 2019 without reference to criteria, but starting 2020 a formula was established based on inflation and labor productivity.

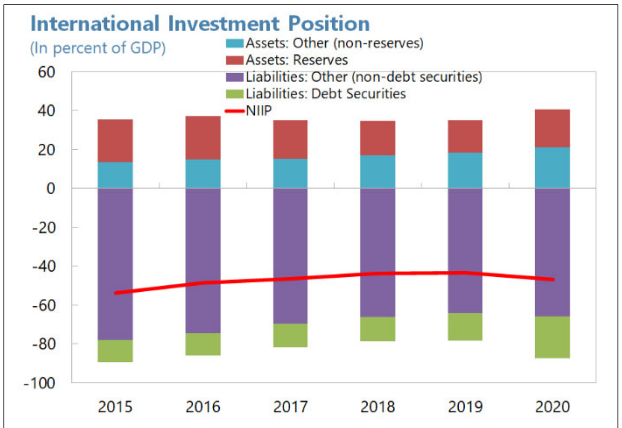
Annex II. External Sector Assessment

Overall Assessment: *The external position of Romania in 2020 was weaker than the level implied by fundamentals and desirable policies. The current account deficit widened slightly to 5.2 percent of GDP in 2020 and is expected to widen slightly further in 2021, suggesting continued external imbalances and exchange rate overvaluation. Staff assesses the current account gap to be around -3.7 percent of GDP, implying a REER overvaluation of 12.2percent, in line with the EBA model results while noting uncertainty around point estimates, especially given shifts in external positions in response to the COVID-19 pandemic. Policy recommendations to address the external imbalances should include durable fiscal consolidation, greater exchange rate flexibility, and structural reforms to boost competitiveness. Reserves increased in 2020 on the back of strong sovereign bond issuance and are assessed to be adequate according to most metrics.*

Foreign Assets and Liabilities: Position and Trajectory

Background. Romania's net international investment position (NIIP) widened in 2020 to -46.9 percent of GDP, unwinding some of the improvements observed over the past five-years. The deterioration was driven by an increase in liabilities as external debt increased because of the larger fiscal deficit – itself related in large part to COVID-19 related spending needs. The deterioration in the NIIP was mitigated somewhat by increases in foreign reserves and other investment balances.

While the NIIP deteriorated sharply as a share of GDP in 2020, the deterioration was somewhat more modest in nominal terms (6 percent) – reflecting the sharp decline in output in 2020. External debt issuance is likely to remain elevated in 2021 and is susceptible to shocks (See Annex IV: DSA). But, the NIIP is expected to improve slightly as a share of GDP as output rebounds. By end-2020, direct investment represented about 5.5 percent of gross assets and 44.7 percent of gross liabilities, while portfolio investment was about 2.6 percent of gross assets and 23 percent of gross liabilities.

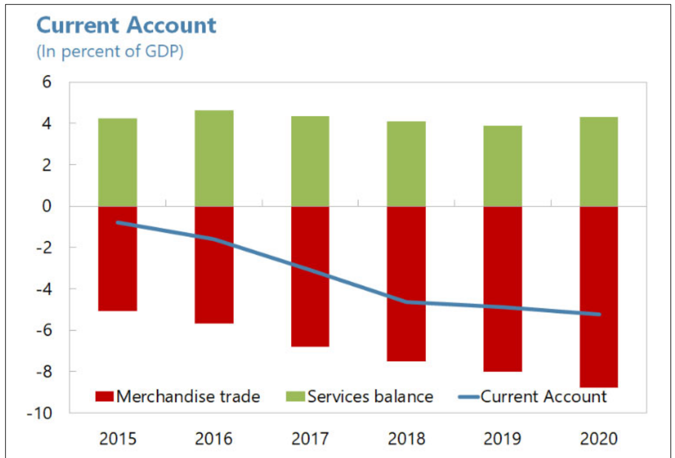


Sources: Authorities Data

Assessment. The external balance sheet does not appear to be a major source of risk for Romania's external sustainability. Nevertheless, vulnerabilities to a sudden tightening of financial conditions increased in 2020—other investment liabilities rose by 1.4 percentage points to close to 20 percent of GDP, while external debt liabilities jumped by 7.4 percentage points to 21.8 percent of GDP. According to staff's projections, the NIIP is expected to average around -45.6 percent of GDP over 2021-26.

Current Account

Background. Romania's current account (CA) deficit deteriorated slightly in 2020 to 5.2 percent of GDP. This builds on prior deteriorations observed over the last 5-years. In previous years, the increase in the current account deficit reflected surging consumption imports. In 2020, the merchandise trade balance continued to deteriorate, as exports declined by more than imports in response to the COVID pandemic. This was somewhat offset, however, by a larger fall in services imports (notably tourism payments) relative to service exports (aided by increasing IT receipts) and by higher secondary income – on account of EU Fund inflows. The current account balance is expected to increase slightly in 2021 as both exports and imports rebound, and to stay above 4.5 percent over the medium-term.



Sources: Authorities data.

Assessment. The CA model of the EBA-lite methodology suggests that Romania's external position at end-2020 was weaker than implied by medium-term fundamentals and desirable policy settings. The cyclically adjusted CA norm is estimated at a deficit of 1.5 percent of GDP, implying a CA gap of -3.7 percent of GDP in 2020 and a real effective exchange rate (REER) overvaluation of about 12 percent, albeit with uncertainty around these point estimates, especially in relation to the impacts of the COVID pandemic on the current account position. Despite a negative contribution from Romania's fiscal policy gap, a larger global fiscal policy gap contributed to a positive relative policy gap for Romania.

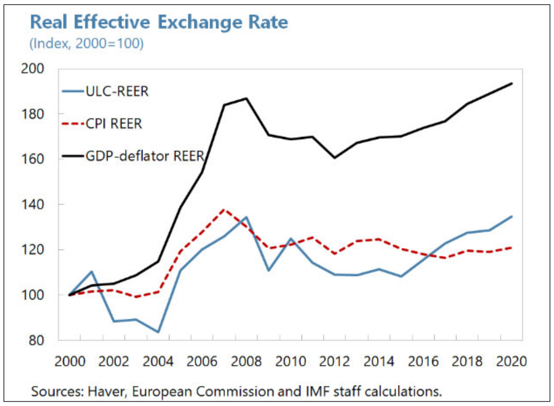
Romania: Model Estimates for 2020 (in percent of GDP)

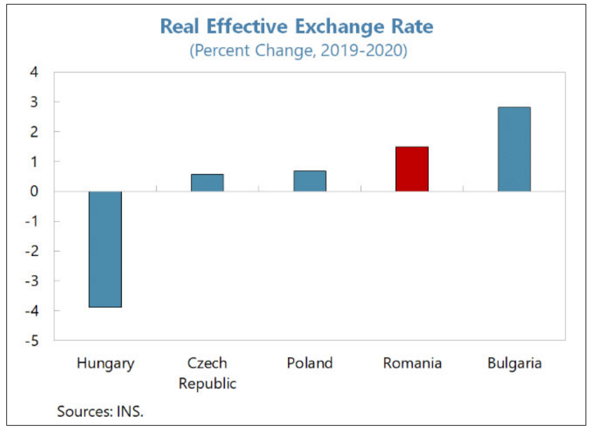
	CA model	REER
CA-Actual	**-5.2**	
Cyclical contributions (from model) (-)	-0.2	
COVID-19 adjustor (+) 1/	-0.3	
Additional temporary/statistical factors (+)	0.0	
Natural disasters and conflicts (-)	0.0	
Adjusted CA	**-5.3**	
CA Norm (from model) 2/	**-1.5**	
Adjusted CA Norm	**-1.5**	
CA Gap	**-3.7**	**-4.0**
o/w Relative policy gap	1.9	
Elasticity	-0.31	
REER Gap (in percent)	**12.2**	**12.9**

1/ Additional cyclical adjustment to account for the temporary impact of the pandemic on oil trade balances (0.08 percent of GDP) and on tourism (-0.35 percent of GDP).
2/ Cyclically adjusted, including multilateral consistency adjustments.

Real Exchange Rate

Background. The real exchange rate (CPI-based) appreciated by 1.5 percent during 2020. The Leu exchange rate has been relatively stable over the past 5-years, and the appreciation observed in 2020 was broadly comparable to real exchange rate movements of most comparator countries. The GDP-deflator based real exchange rate appreciated by 2.8 percent. Moreover, a measure based on unit-labor costs increased by around 4.7 percent.

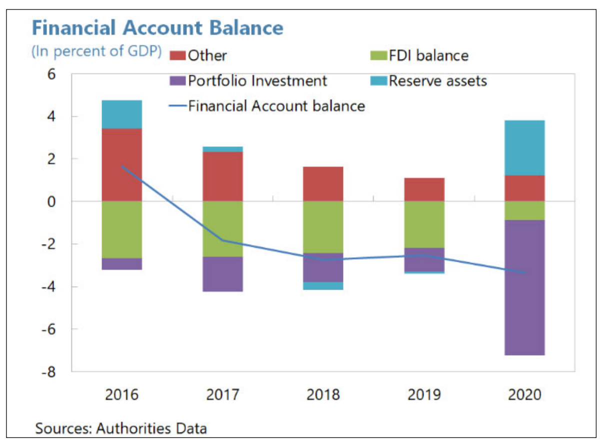




Assessment. The CA-model based assessment implies a REER overvaluation of 12.2 percent in 2020 (applying an estimated elasticity of 0.31). The EBA-light Index of Real Effective Exchange Rate (IREER) model approach is broadly consistent – pointing to an overvaluation of 12.9 percent. Consistent with the CA gap, staff assesses the REER to be overvalued by 12.2 percent.

Capital and Financial Accounts: Flows and Policy Measures

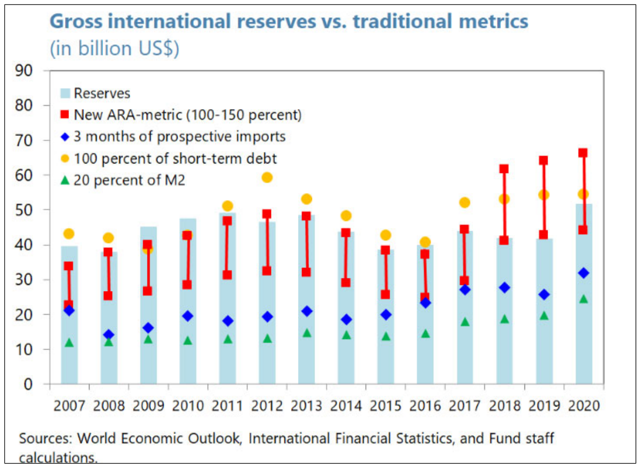
Background. Based on preliminary data, the capital account recorded inflows of 1.9 percent of GDP, somewhat above the 5-year trend of 1.6 percent of GDP, largely reflecting larger EU grants. Portfolio investment – driven by sovereign bond issuance – was the main source of financing the CA deficit in 2020. Net FDI inflows declined sharply to just 0.9 percent of GDP – under half of pre-pandemic shares – on the back of a sharp decline in intra-company flows during the pandemic. There are no restrictions on the capital and financial account.



Assessment. Capital account inflows are expected to increase supported by a pick-up in EU funded projects, including through new resources under the Next Generation EU (NGEU) funds and EU 2021-27 multiannual budget. There is also scope for higher absorption of EU funds. FDI inflows are expected to rebound as pandemic-related uncertainty abates, but medium-term prospects remain unclear (due to poor infrastructure, rising labor costs and remaining policy uncertainty). Portfolio investment flows may continue to be sizeable given only gradual fiscal consolidation, and the currently favorable low-interest rate environment.

FX Intervention and Reserves Level

Background. Romania's exchange rate regime was classified as crawl-like in 2020. Reserves increased sharply in nominal U.S. dollar terms – about 24 percent – in 2020, reflecting strong sovereign bond issuance combined with U.S. dollar depreciation. Overall, gross international reserves stood at 19.5 percent of GDP and could cover about 4.8 months of prospective imports or about 42 percent of M2 and 95 percent of ST debt.



Assessment. The increase in nominal reserves restored Romania's reserve coverage to around 117 percent of the Fund's reserve-adequacy metric for emerging markets with a de-facto 'fixed' exchange rate regime.[1] Reserve adequacy would be above 160 percent of the ARA metric if a floating exchange rate regime is assumed, and is comfortably above thresholds for most other traditional metrics.

[1] Romania's exchange rate was re-classified retroactively as crawl-like from floating from July 2016. As a result, Romania's reserve adequacy metric in recent years is based off that for a 'fixed' exchange rate regime.

Annex III. Key Policy Responses to the COVID-19 Crisis

Policy responses	2020		2021	
	Disbursed		Announced	
	million RON	GDP	million RON	GDP
Fiscal measures	**41,249**	**3.9**	**41,483**	**3.5**
SPENDING	**16,222**	**1.5**	**15,380**	**1.3**
Health system measures	**5,614**	**0.5**	**3,840**	**0.3**
Risk bonuses of EUR 500 per month for the medical and social assistance staff in direct contact with the coronavirus	330	0.0	100	0.0
Accessing the World Bank disaster and risk management facility	154	0.0	140	0.0
Increasing the health budget for health programs, emergency purchase of sanitary equipment, sick leaves	4,324	0.4	1,850	0.2
COVID vaccination program		-	1,400	0.1
Health emergency stocks	560	0.1	350	0.0
Financial support to quarantine centers	246	0.0		-
Purchase of medical and protective equipment (reallocation of EU Funds)		-		-
Income support measures for individuals and companies	**9,539**	**0.9**	**3,950**	**0.3**
The state finances 75% of the gross salary of employees in technical unemployment (up to 75% of the average gross wage) in firms affected by the outbreak, i.e. firms that either stopped their activity completely or partially due to the state of emergency or have reduced their revenues by at least 25% (compared to the average level of Jan-Febr 2020)	4246.0	0.4		-
One parent can receive paid leave (75% of the gross salary, up to 75% of the standard gross average salary) when a child's educational institution is temporarily shut down by authorities due to extreme circumstances (for children up to 12 years old or up to 18 years old for children with disabilities and when working from home is not possible)	94.0	0.0		-
The state finances 75% of gross wage to affected self-employed and individual enterprises	955.0	0.1		-
The state finances 75% of the gross salary for proffesional athletes	103.0	0.0		-
Since 1 June, employers whose employees had their individual employment agreements suspended for at least 15 days and who received the technical unemployment allowance, can benefit, for a period of three months, of a wage subsidy amounting to 41.5% of the basic salary (up to 41.5% of the average gross earnings and conditionned to maintaining the employment relationship until 31 December 2020)	2691.0	0.3	1,900	0.2
Employers hiring jobseekers over 50 or below 30 or Romanian citizens returning to the country after losing their jobs abroad, between 1 June and 31 December 2020, can receive a monthly allowance of 50% of the gross salary (up to RON 2500) during one year. This measure is condionned to maintaining the employment relationship for one additional year after the end of the hiring support measure	0.0	-		-
Bonuses public administration COVID related	1,450	0.1	2,050	0.2
Grants to business	**1,069**	**0.1**	**7,590**	**0.6**
Interest and fees IMM Invest	109	0.0	630	0.1
State aid scheme HoReCA		-	2,500	0.2
State aid scheme for investment (EU Funds)	960	0.1	4,460	0.4
REVENUE	**7,000**	**0.7**	**-**	**-**
Tax and contribution policy changes	**900**	**0.1**	**-**	**-**
Bonus for the payment of the corporate income tax in April for all companies (reduction of 5% for large companies, 10% for medium businesses and microenterprises)	900	0.1		-
VAT exemptions on imports of medical and sanitary devices that can be used to prevent, limit and combat COVID-19		-		-
Capping the fee on medicine sales (claw back tax)		-		-
Exempting the specific tax for hospitality industry		-		-
Deferral of taxes and social security contributions	**6,100**	**0.6**	**-**	**-**
The payment deadlines for local taxes (cars, building, land) have been postponed		-		-
Interest and penalties on outstanding corporate tax debt will not be charged for companies paying debt principal arrears		-		-
Acceleration of VAT refunds	2,300	0.2		-
Tax defferals by tax administration	3,800	0.4		-
Suspension of most tax audits and of foreclosures on overdue debtors, amendments of the tax debt restructuring programme and of the calculation of the corporate income tax base		-		-
Loan guarantees by the state benefiting private borrowers	**16,277**	**1.5**	**26,103**	**2.2**
The State guarantee scheme has been expanded and subsidised interest rates for small and microenterprises will be temporarily allocated (up to RON 20 billion)	11,937	1.1	15,000	1.3
State guarantees for leasing of work equipment for SMEs. The guarantee is up to 80% loan for IT equipment, and 60% for other technological equipment. The maximum value of the financing will be 5,000,000 RON. The leasing period will be 72 months.	0	0.0	2,000	0.2
State guarantee scheme for large companies (turnover above 20 million RON)	2,164	0.2	8,103	0.7
State guarantee scheme for factoring	0	-	1,000	0.1
State guarantee scheme insurance trade credit	0	-		-
SURE Guarantee	1,916	0.2		-
Loan payments moratoria for individuals	261	0.0		-
Government Loans	**1,750**	**0.2**	**-**	**-**
Loan to the state-owned company UNIFARM for the emergency purchase of sanitary equipment	1150	0.1		-
Loan to low-cost carrier Blue Air and state-owned airline Tarom	600	0.1		-

Monetary policy and prudential regulation				
Monetary policy				
Cut in the policy rate by 0.50 percentage points				
Cut in the lending (Lombard) facility rate by 1 percentage point (to 2.5%, the deposit facility rate is maintained at 1.5%)				
Provision of liquidity to credit institutions through REPO operations				
Purchase of government securities denominated in national currency on the secondary market				
Cut policy rate by 0.25 percentage point on 2 June (from 2% to 1.75%) and maintained that it will continue injecting liquidity to the market and purchase local currency denominated government securities on the secondary market				
Prudential regulation				
Credit institutions are allowed to temporarily reduce or suspend loan amortisation payments without applying the regulatory provisions on the level of indebtedness, the loan-to-value limit, and the maximum maturity of consumer credit				
The EU regulatory framework will be applied in the prudential and accounting fields. Banks are allowed to use capital buffers and operate with lower liquidity ratio				
The pension funds will be allowed to increase the weight of government papers in their portfolios above the statutory 70% limit, for a period of one year				
Measures to promote burden sharing within the private sector				
Loan payments can be suspended for 9 months for individuals and firms affected by the outbreak.				
SMEs obtaining an emergency certificate can benefit from an extension of the payment deadlines for utility services (electricity, natural gas, water, telephone and internet services) and rents.				
Other				
Ban exports of medicines and other health products for six months				
Cap on prices of utilities and fuel				
Temporary subordination of some regional entities to central administration (local police, fire departments, health units)				
Introducing high criminal penalties for those breaching the national emergency regulations (quarantine, movement restrictions etc.)				
Dedicated hotline for info and support, travel warnings, regular communication by the task force				
Waiving contests for hiring in the healthcare, defense and public order sectors (contracts of 6 months only)				
Waiving procurement procedures for all products required to fight the epidemic				

Annex IV. Debt Sustainability Analysis

Romania's public debt ratio has increased significantly, albeit from a low initial level, and is expected to remain on an upward trajectory throughout the projection horizon. Under the baseline scenario, the public debt-to-GDP ratio is projected to reach 61.4 percent by 2026 from the current level of 49.8 percent. Gross financing needs (10.9 percent on average over the projection horizon) are projected to fall relative to 2020 but will continue to modestly exceed the 10 percent threshold into the medium-term. The main vulnerabilities for debt sustainability stem from high external financing requirements, a high non-resident share in public debt holdings and exposure to exchange rate risk. Debt levels are also sensitive to a recession shock, which would push the ratio to 68 percent by 2026.

1. Following broadly stable public debt levels of around 35 percent of GDP during 2016 2019, the ratio has increased sharply in 2020 due to COVID-19 crisis. The evolution of public debt in recent years has been characterized by deteriorating fiscal balances, with the primary deficit reaching 3.5 percent of GDP in 2019, countered by off-setting strong growth in economic activity. This trend of relative stability was abruptly interrupted in 2020, with the public debt to GDP ratio surging from 37 percent in 2019 to 50 percent in 2020. The increase was driven by the COVID19-induced economic contraction and the sizable package of fiscal measures that was implemented to address the extraordinary emergency and its economic fallout.

Baseline and Realism of Projections

2. Debt level. Under the baseline scenario, gross debt level (including guarantees) is projected to rise over the medium term, reaching 61.4 percent in 2026. This rise is reflected in gross financing needs over the 2021-26 period, which are projected to exceed 10 percent of GDP, averaging 10.9 percent of GDP over the projection horizon.

3. Fiscal balance and adjustment. The main driver of the rise in public debt is persistent and high primary fiscal deficits. In the baseline projection, the primary budget deficit is expected to decrease over the projection horizon, relative to the 2020 level of 8.4 percent of GDP. The gradual improvement in the budget deficits over the projection horizon is driven by a withdrawal of pandemic support measures, the authorities' announced fiscal consolidation plans, a recovery in economic activity and increased availability and improved absorption of EU structural and RRF funds. However, the baseline includes only those consolidation measures that are already in place, and not the authorities' medium-term consolidation objective. As a result, the baseline projects a sizable medium-term primary deficit of 3.2 percent of GDP, partly reflecting fiscal excesses that predate the March 2020 COVID-19 crisis.[1] Taking into account the distribution of historical fiscal adjustment episodes provided in the DSA template, the projected 3-year adjustment in the cyclically-adjusted primary balance (CAPB) of 2.5 percent of GDP is close to the top quartile of adjustment episodes, highlighting the large size of the projected adjustment. The 3-year average level of the CAPB places Romania at the bottom of the distribution for historical comparator

[1] Romania entered EU's EDP in February 2020, after recording a fiscal deficit of 4.6 percent of GDP in 2019.

episodes, partly made possible by the Romania's relatively low level of public debt and high growth rates and partly reflecting the unprecedented nature of the current pandemic crisis.

4. Growth. Compared to outcomes, past projections of growth suggest moderate forecast errors, with the median forecast error in line with comparator countries or on the pessimistic side. Considering the high sensitivity of Romania's debt dynamics to surprises in GDP growth, there is no evidence for a systematic overly optimistic projection bias in the baseline assumption for growth that could undermine the DSA assessment. The current real GDP growth projection of 7 percent for 2021 exceeds the authorities' most recent estimate of 5.0 percent, while medium-term growth is expected to stabilize at 3.5 percent of GDP, below the authorities' estimate of 4.9 percent by 2024. The boom-bust analysis is not triggered because the three-year cumulative change in the credit-to-GDP ratio does not exceed 15 percent in Romania.

Debt Profile Vulnerabilities

5. The main vulnerabilities for debt sustainability stems from high external financing requirements, reflecting Romania's sizable and persistent twin deficits—capital inflows that funded domestic demand and were facilitated by expansionary past fiscal policies. To address the heightened exposure to international outflows, the authorities maintain a foreign currency financing buffer (excluding privatization proceeds), estimated at around 3.5 percent of GDP at the end of 2020. The authorities have also strived to extend the maturity profile of public debt, with the average time to maturity increasing from 5.9 years in 2017 to 7.4 years by end-2020. Public debt is also vulnerable to exchange rate risk, with the share of foreign currency debt (at 51 percent of total debt) and non-resident holdings of public debt (45 percent of total) close to the upper early warning benchmarks.

Stochastic Simulations

6. The fan charts illustrate the possible evolution of the debt ratio over the medium term and are based on both the symmetric and asymmetric distributions of risk. Under the symmetric distribution of risk, there is a high probability that debt will continue to increase into the medium term and will most likely (56 percent probability) exceed 60 percent of GDP by 2026 (threshold under the Stability and Growth Pact). If restrictions are imposed on the nature of the primary balance shocks[2], the probability that debt will exceed 60 percent of GDP in the medium-term increases to 80 percent.

Stress Tests

7. Real GDP growth. In the stress test scenarios, the public debt ratio is most sensitive to the real GDP growth shock, under which debt reaches 68 percent of GDP by 2026. This scenario also results in significantly increased public gross financing needs, peaking at 14.2 percent of GDP in 2023, 3.1 percentage points of GDP above the baseline gross financing needs for the

[2] This is the asymmetric scenario, where it is assumed that there are no positive shocks to the primary balance.

same year and marginally exceeding the 14.1 percent of GDP in gross financing that Romania secured during the COVID-19 crisis in 2020.

8. Combined shock. A combined shock incorporates the largest effect of individual shocks on all relevant variables (real GDP growth, inflation, primary balance, exchange rate and interest rate). Under this scenario, debt would reach 73 percent of GDP in 2026. Gross financing needs peak at around 14.7 percent of GDP in 2023 and averaging 12.6 percent in the remaining years of the projection horizon.

External Debt

9. External debt rose sharply in 2020 to stand at 57.7 percent of GDP. After peaking in 2012, gross external debt declined on the back of public and private sector deleveraging to reach 48.8 percent in 2018. A slight increase in 2019 – on the back of higher public borrowing – was followed by a more substantial increase in 2020 on the back of substantial Eurobond issuance. As a result, public external debt, at 27 percent of GDP, reached similar levels to those observed in 2012.

10. External debt is expected to plateau in the coming years. Under the baseline scenario, despite robust growth a continued need to finance elevated fiscal deficits externally, external debt is projected to remain broadly stable at 57.5 percent of GDP in 2026. Debt dynamics under the baseline scenario are slightly higher than in a scenario where key variables are kept at their historic levels. Gross external financing needs are expected to gradually decline, but to remain above 20 percent of GDP. Roll-over risks of the non-banking sector are limited, as a large portion of debt stems from inter-company lending.

11. Staff analysis indicates that Romania's debt dynamics are susceptible to shocks. Debt stays close to the 2020 level under the interest rate shock scenario, while it increases under the growth-rate and current account shock scenarios. In a tailored combined shocks scenario (permanent ½ standard deviation shock applied to growth, current account, and interest rate), external debt reaches 69 percent of GDP in 2026. And in a stress scenario, with a 30 percent depreciation in 2022, external debt would increase sharply to 86 percent of GDP and remain around that level over the medium-term.

Annex IV. Figure 1. Romania: Public Sector Debt Sustainability Analysis (DSA) – Baseline Scenario

(In percent of GDP, unless otherwise indicated)

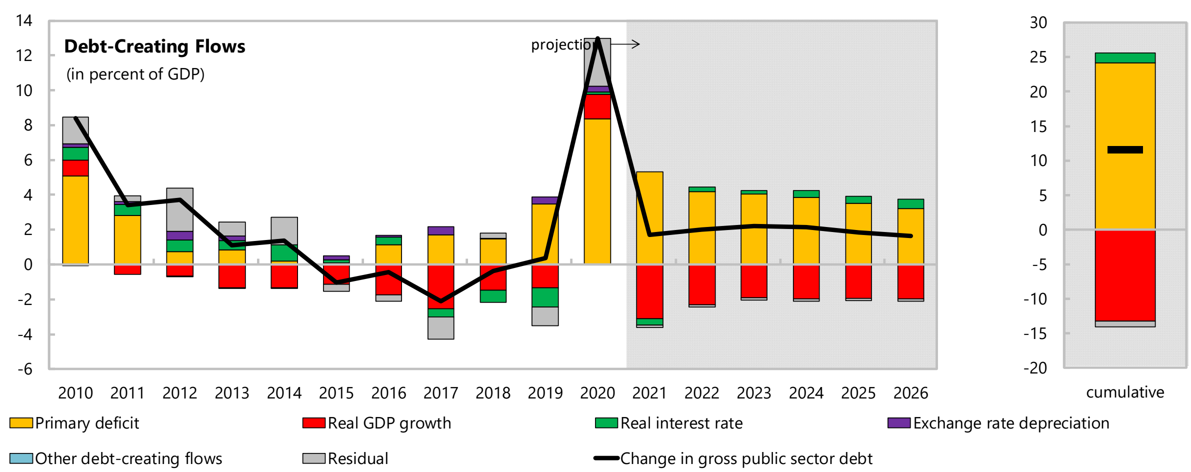
Debt, Economic and Market Indicators [1/]

	Actual			Projections					
	2010-2018 [2/]	2019	2020	2021	2022	2023	2024	2025	2026
Nominal gross public debt	37.1	36.8	49.8	51.5	53.5	55.7	57.9	59.7	61.4
Of which: guarantees	2.3	1.8	3.2	2.8	2.6	2.5	2.3	2.2	2.0
Public gross financing needs	10.2	9.1	14.1	11.2	10.9	11.1	11.2	10.4	10.8
Real GDP growth (in percent)	3.0	4.1	-3.9	7.0	4.8	3.8	3.8	3.6	3.5
Inflation (GDP deflator, in percent)	3.7	6.8	3.8	4.2	3.0	3.2	2.8	2.9	2.7
Nominal GDP growth (in percent)	6.8	11.2	-0.2	11.5	8.0	7.2	6.7	6.6	6.3
Effective interest rate (in percent) [4/]	4.9	3.7	3.9	3.7	3.7	3.7	3.7	3.7	3.7

As of March 03, 2021		
Sovereign Spreads		
EMBIG (bp) 3/		177
5Y CDS (bp)		86
Ratings	Foreign	Local
Moody's	Baa3	Baa3
S&Ps	BBB-	BBB-
Fitch	BBB-	BBB-

Contribution to Changes in Public Debt

	Actual			Projections							
	2010-2018	2019	2020	2021	2022	2023	2024	2025	2026	cumulative	debt-stabilizing primary balance [9/]
Change in gross public sector debt	1.6	0.4	13.0	1.7	2.0	2.2	2.2	1.8	1.7	11.6	
Identified debt-creating flows	1.0	1.4	10.2	1.9	2.1	2.3	2.3	2.0	1.8	12.4	
Primary deficit	1.6	3.5	8.4	5.3	4.2	4.1	3.8	3.5	3.2	24.1	-1.4
Primary (noninterest) revenue and grants	31.0	28.9	28.8	30.2	29.9	29.6	29.7	29.8	30.1	179.4	
Primary (noninterest) expenditure	32.6	32.3	37.2	35.6	34.1	33.7	33.5	33.4	33.3	203.6	
Automatic debt dynamics [5/]	-0.6	-2.0	1.9	-3.5	-2.0	-1.7	-1.5	-1.5	-1.4	-11.8	
Interest rate/growth differential [6/]	-0.8	-2.5	1.5	-3.5	-2.0	-1.7	-1.5	-1.5	-1.4	-11.8	
Of which: real interest rate	0.3	-1.1	0.1	-0.3	0.3	0.2	0.4	0.4	0.5	1.5	
Of which: real GDP growth	-1.1	-1.4	1.4	-3.1	-2.3	-1.9	-2.0	-1.9	-2.0	-13.2	
Exchange rate depreciation [7/]	0.2	0.4	0.3	…	…	…	…	…	…	…	
Other identified debt-creating flows	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Privatization receipts (negative)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Please specify (2) (e.g., ESM and Euroarea loans)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Residual, including asset changes [8/]	0.6	-1.1	2.7	-0.2	-0.1	-0.1	-0.1	-0.1	-0.1	-0.8	



Source: IMF staff.

1/ Public sector is defined as general government and includes public guarantees.

2/ Based on available data.

3/ EMBIG.

4/ Defined as interest payments divided by debt stock (excluding guarantees) at the end of previous year.

5/ Derived as [(r - π(1+g) - g + ae(1+r)]/(1+g+π+gπ)) times previous period debt ratio, with r = interest rate; π = 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).

6/ The real interest rate contribution is derived from the numerator in footnote 5 as r - π (1+g) and the real growth contribution as -g.

7/ The exchange rate contribution is derived from the numerator in footnote 5 as ae(1+r).

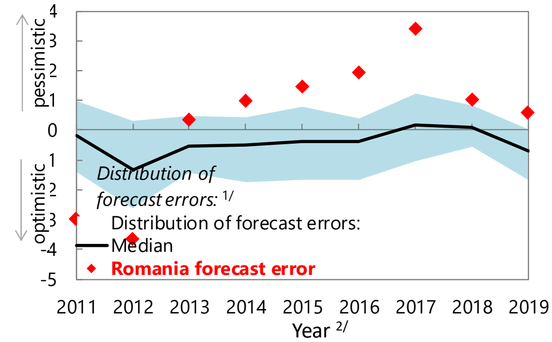
8/ Includes changes in the stock of guarantees, asset changes, and interest revenues (if any). For projections, includes exchange rate changes during the projection period.

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.

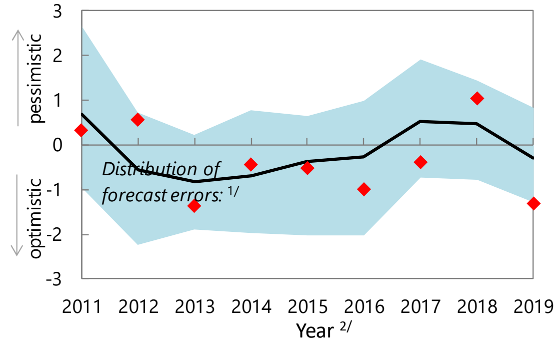
Annex IV. Figure 2. Romania: Public DSA – Realism of Baseline Assumptions

Forecast Track Record, versus all countries

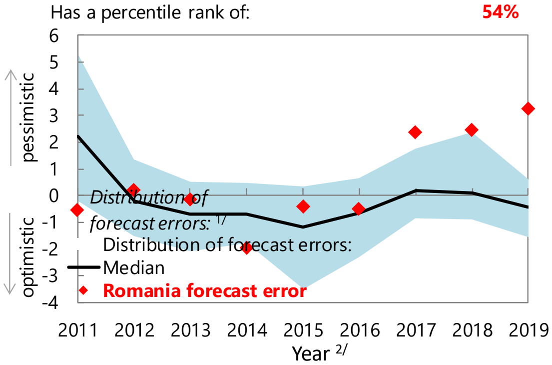
Real GDP Growth
(in percent, actual-projection)
Romania median forecast error, 2011-2019: **0.98**
Has a percentile rank of: **92%**



Primary Balance
(in percent of GDP, actual-projection)
Romania median forecast error, 2011-2019: **-0.43**
Has a percentile rank of: **36%**

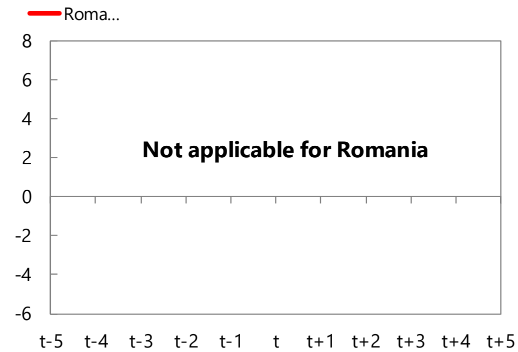


Inflation (Deflator)
(in percent, actual-projection)
Romania median forecast error, 2011-2019: **-0.16**
Has a percentile rank of: **54%**



Boom-Bust Analysis 3/

Real GDP growth
(in percent)



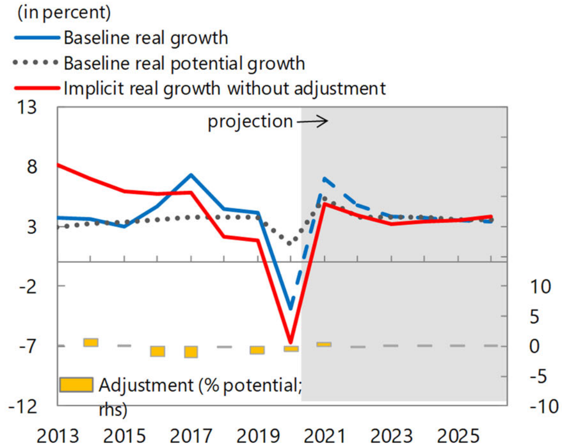
Source : IMF staff.
1/ Plotted distribution includes all countries, percentile rank refers to all countries
2/ Projections made in the spring WEO vintage of the preceding year
3/ Not applicable for Romania, as it meets neither the positive output gap criterion nor the private credit growth criterion.

Annex IV. Figure 3. Romania: Public DSA – Realism of Baseline Assumptions (concluded)

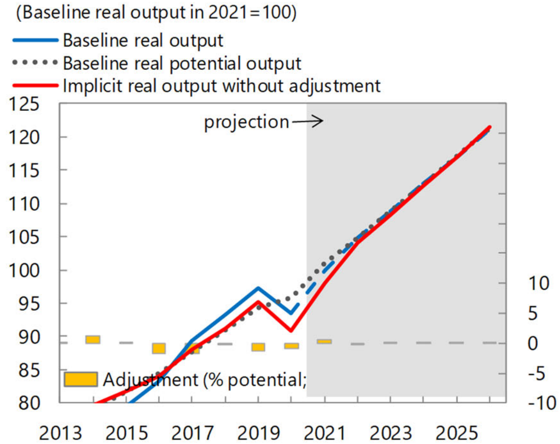
Growth and Level of Output in Absence of Fiscal Adjustment

Assumed multiplier of 1, persistence of 0.6

Real GDP Growth
(in percent)

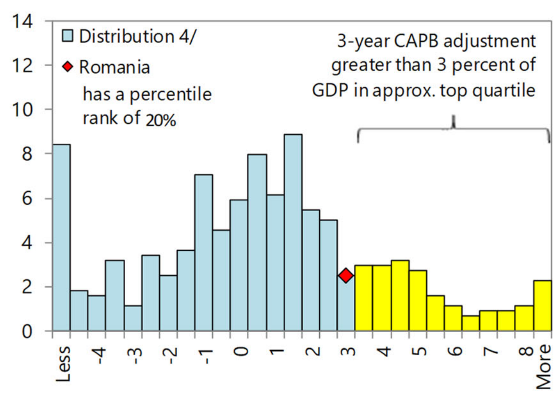


Real Output Level
(Baseline real output in 2021=100)

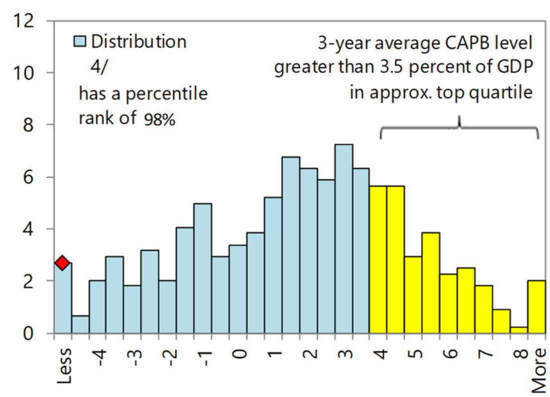


Assessing the Realism of Projected Fiscal Adjustment

3-Year Adjustment in Cyclically-Adjusted Primary Balance (CAPB)
(Percent of GDP)



3-Year Average Level of Cyclically-Adjusted Primary Balance (CAPB)
(Percent of GDP)



Source : IMF staff.
4/ Data cover annual obervations from 1990 to 2011 for advanced and emerging economies with debt greater than 60 percent of GDP. Percent of sample on vertical axis.

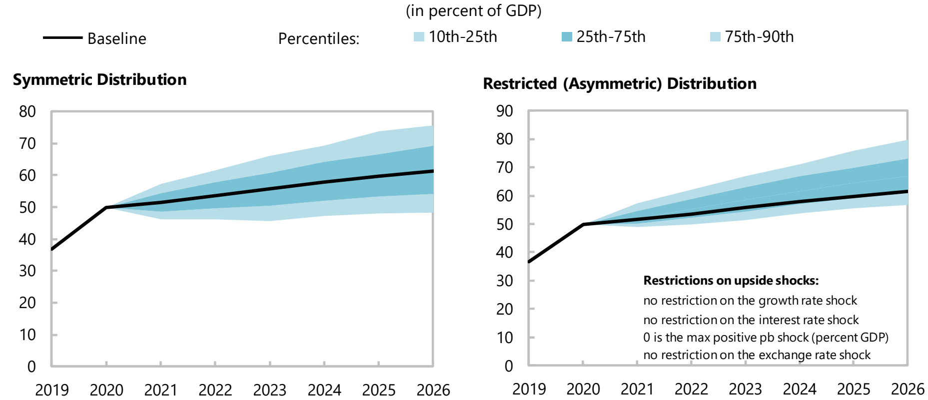
Annex IV. Figure 4. Romania: Public DSA Risk Assessment

Heat Map

Debt level [1/]	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability shock
Gross financing needs [2/]	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability Shock
Debt profile [3/]	Market Perception	External Financing Requirements	Change in the Share of Short-Term Debt	Public Debt Held by Non-Residents	Foreign Currency Debt

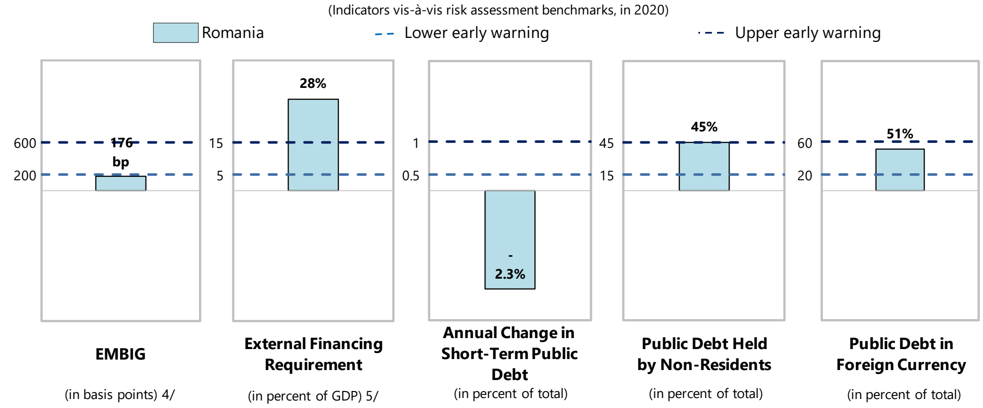
Evolution of Predictive Densities of Gross Nominal Public Debt

(in percent of GDP)



Debt Profile Vulnerabilities

(Indicators vis-à-vis risk assessment benchmarks, in 2020)



Source: IMF staff.

1/ The cell is highlighted in green if debt burden benchmark of 70% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

2/ The cell is highlighted in green if gross financing needs benchmark of 15% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

3/ The cell is highlighted in green if country value is less than the lower risk-assessment benchmark, red if country value exceeds the upper risk-assessment benchmark, yellow if country value is between the lower and upper risk-assessment benchmarks. If data are unavailable or indicator is not relevant, cell is white.
Lower and upper risk-assessment benchmarks are:

200 and 600 basis points for bond spreads; 5 and 15 percent of GDP for external financing requirement; 0.5 and 1 percent for change in the share of short-term debt; 15 and 45 percent for the public debt held by non-residents; and 20 and 60 percent for the share of foreign-currency denominated debt.

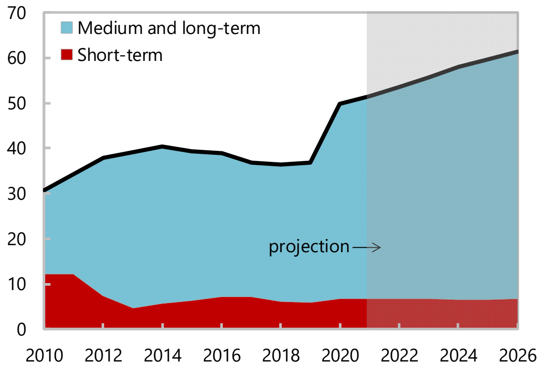
4/ EMBIG, an average over the last 3 months, 03-Dec-20 through 03-Mar-21.

5/ External financing requirement is defined as the sum of current account deficit, amortization of medium and long-term total external debt, and short-term total external debt at the end of previous period.

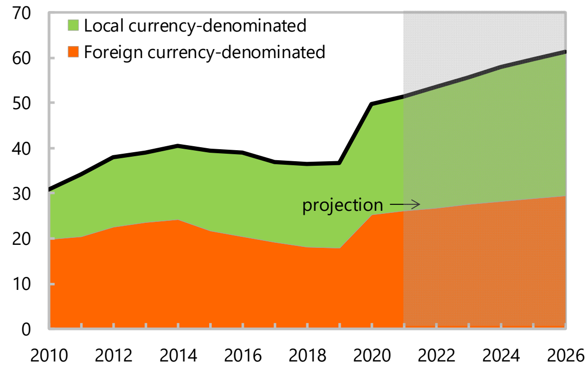
Annex IV. Figure 5. Romania: Public DSA – Composition of Public Debt and Alternative Scenarios

Composition of Public Debt

By Maturity
(in percent of GDP)



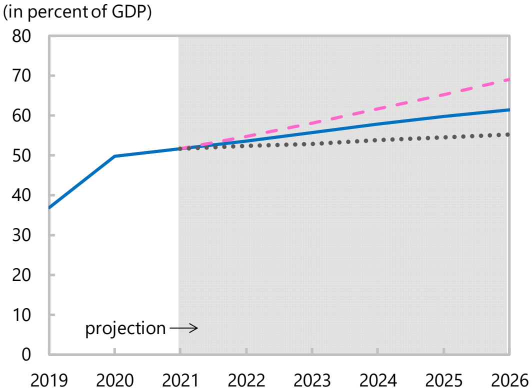
By Currency
(in percent of GDP)



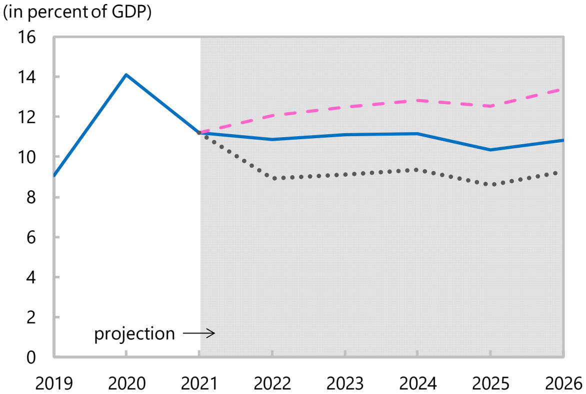
Alternative Scenarios

Baseline   Historical   Constant Primary Balance

Gross Nominal Public Debt
(in percent of GDP)



Public Gross Financing Needs
(in percent of GDP)



Underlying Assumptions
(in percent)

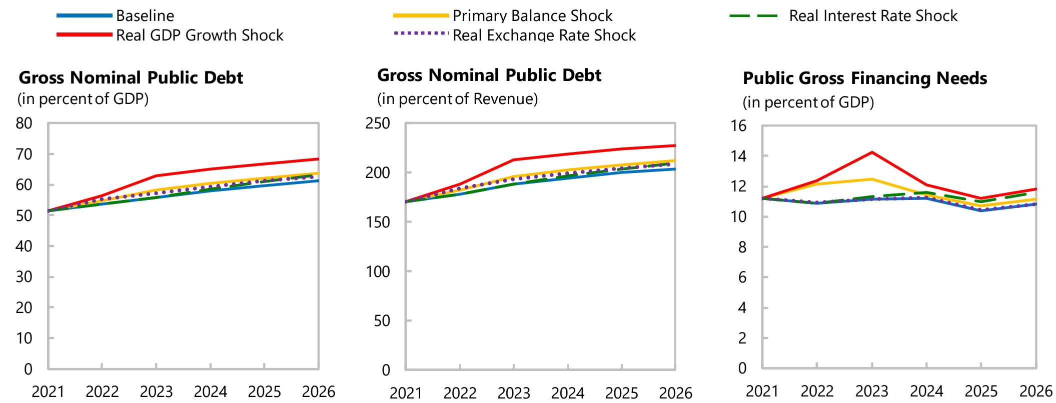
Baseline Scenario	2021	2022	2023	2024	2025	2026
Real GDP growth	7.0	4.8	3.8	3.8	3.6	3.5
Inflation	4.2	3.0	3.2	2.8	2.9	2.7
Primary Balance	-5.3	-4.2	-4.1	-3.8	-3.5	-3.2
Effective interest rate	3.7	3.7	3.7	3.7	3.7	3.7
Constant Primary Balance Scenario						
Real GDP growth	7.0	4.8	3.8	3.8	3.6	3.5
Inflation	4.2	3.0	3.2	2.8	2.9	2.7
Primary Balance	-5.3	-5.3	-5.3	-5.3	-5.3	-5.3
Effective interest rate	3.7	3.7	3.7	3.7	3.7	3.7

Historical Scenario	2021	2022	2023	2024	2025	2026
Real GDP growth	7.0	3.1	3.1	3.1	3.1	3.1
Inflation	4.2	3.0	3.2	2.8	2.9	2.7
Primary Balance	-5.3	-2.1	-2.1	-2.1	-2.1	-2.1
Effective interest rate	3.7	3.7	3.7	3.7	3.7	3.6

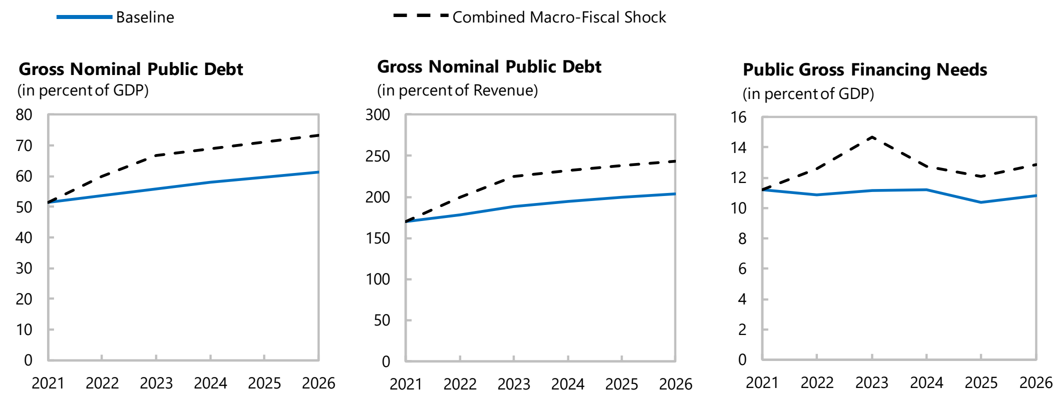
Source: IMF staff.

Annex IV. Figure 6. Romania: Public DSA – Stress Tests

Macro-Fiscal Stress Tests



Additional Stress Tests



Underlying Assumptions
(in percent)

Primary Balance Shock	2021	2022	2023	2024	2025	2026
Real GDP growth	7.0	4.8	3.8	3.8	3.6	3.5
Inflation	4.2	3.0	3.2	2.8	2.9	2.7
Primary balance	-5.3	-5.4	-5.3	-3.8	-3.5	-3.2
Effective interest rate	3.7	3.7	3.8	3.9	3.8	3.8
Real Interest Rate Shock						
Real GDP growth	7.0	4.8	3.8	3.8	3.6	3.5
Inflation	4.2	3.0	3.2	2.8	2.9	2.7
Primary balance	-5.3	-4.2	-4.1	-3.8	-3.5	-3.2
Effective interest rate	3.7	3.7	4.1	4.5	4.8	5.0
Combined Shock						
Real GDP growth	7.0	1.9	0.9	3.8	3.6	3.5
Inflation	4.2	2.3	2.5	2.8	2.9	2.7
Primary balance	-5.3	-5.4	-6.5	-3.8	-3.5	-3.2
Effective interest rate	3.7	3.9	4.1	4.5	4.8	5.0

Real GDP Growth Shock	2021	2022	2023	2024	2025	2026
Real GDP growth	7.0	1.9	0.9	3.8	3.6	3.5
Inflation	4.2	2.3	2.5	2.8	2.9	2.7
Primary balance	-5.3	-5.4	-6.5	-3.8	-3.5	-3.2
Effective interest rate	3.7	3.7	3.8	3.9	3.9	3.9
Real Exchange Rate Shock						
Real GDP growth	7.0	4.8	3.8	3.8	3.6	3.5
Inflation	4.2	6.3	3.2	2.8	2.9	2.7
Primary balance	-5.3	-4.2	-4.1	-3.8	-3.5	-3.2
Effective interest rate	3.7	3.9	3.7	3.7	3.7	3.7

Source: IMF staff.

Annex IV. Table 1. Romania: External Debt Sustainability Framework, 2016-2026

(In percent of GDP, unless otherwise indicated)

	Actual													
	2016	2017	2018	2019	2020			2021	2022	2023	2024	2025	2026	**Debt-stabilizing non-interest current account 6/**
Baseline: External debt	54.7	51.8	48.8	49.2	57.7			**57.7**	**57.4**	**57.3**	**57.6**	**57.6**	**57.5**	**0.4**
Change in external debt	-2.3	-2.9	-3.0	0.4	8.5			0.0	-0.3	-0.1	0.3	0.0	-0.1	
Identified external debt-creating flows (4+8+9)	1.0	0.6	2.9	3.1	7.2			3.4	4.5	5.0	4.9	4.9	4.7	
Current account deficit, excluding interest payments	0.1	1.9	3.6	3.8	4.2			3.2	3.2	3.2	3.1	3.0	2.9	
Deficit in balance of goods and services	1.0	2.5	3.4	4.1	4.5			4.8	4.6	4.4	4.1	3.9	3.8	
Exports	41.8	42.0	41.9	40.4	37.3			39.8	41.0	40.8	41.4	42.3	43.0	
Imports	42.8	44.5	45.3	44.5	41.7			44.7	45.6	45.2	45.6	46.3	46.8	
Net non-debt creating capital inflows (negative)	2.7	2.7	2.5	2.2	0.9			1.6	1.8	1.9	2.0	2.1	2.2	
Automatic debt dynamics 1/	-1.8	-4.0	-3.2	-3.0	2.1			-1.5	-0.5	-0.1	-0.2	-0.3	-0.3	
Contribution from nominal interest rate	1.5	1.2	1.1	1.1	1.0			2.2	2.1	1.9	1.8	1.7	1.6	
Contribution from real GDP growth	-2.5	-3.6	-2.1	-1.8	1.9			-3.7	-2.6	-2.0	-2.0	-1.9	-1.9	
Contribution from price and exchange rate changes 2/	-0.8	-1.5	-2.1	-2.2	-0.9			...	...	...	...	...	...	
Residual, incl. change in gross foreign assets (2-3) 3/	-3.3	-3.5	-5.9	-2.6	1.3			-3.3	-4.7	-5.1	-4.6	-4.8	-4.8	
External debt-to-exports ratio (in percent)	131.0	123.4	116.6	121.8	154.9			144.9	140.0	140.7	139.1	136.2	133.7	
Gross external financing need (in billions of Euros) 4/	34.2	38.3	49.0	51.4	52.9			50.8	57.3	61.2	65.2	66.8	69.6	
in percent of GDP	20.1	20.4	23.9	23.1	24.2			21.3	22.1	21.9	21.8	21.0	20.6	
Scenario with key variables at their historical averages 5/								**57.5**	**56.4**	**55.3**	**54.0**	**52.5**	**51.0**	**0.6**
Key Macroeconomic Assumptions Underlying Baseline						10-Year Historical Average	10-Year Standard Deviation							
Real GDP growth (in percent)	4.7	7.3	4.5	4.1	-3.9	3.1	2.9	7.0	4.8	3.8	3.8	3.6	3.5	
GDP deflator in Euros (change in percent)	1.4	2.9	4.2	4.7	1.8	2.6	1.8	2.4	3.3	4.0	2.8	2.9	2.7	
Nominal external interest rate (in percent)	2.8	2.4	2.3	2.4	2.0	2.8	0.6	4.2	3.9	3.6	3.3	3.1	2.9	
Growth of exports (Euro terms, in percent)	7.2	11.1	8.5	5.3	-9.8	7.5	8.0	17.1	11.6	7.3	8.4	8.9	8.1	
Growth of imports (Euro terms, in percent)	7.7	14.7	10.8	7.3	-8.3	6.6	7.0	17.3	10.6	6.9	7.6	8.2	7.6	
Current account balance, excluding interest payments	-0.1	-1.9	-3.6	-3.8	-4.2	-1.4	2.3	-3.2	-3.2	-3.2	-3.1	-3.0	-2.9	
Net non-debt creating capital inflows	-2.7	-2.7	-2.5	-2.2	-0.9	-2.0	0.6	-1.6	-1.8	-1.9	-2.0	-2.1	-2.2	

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.

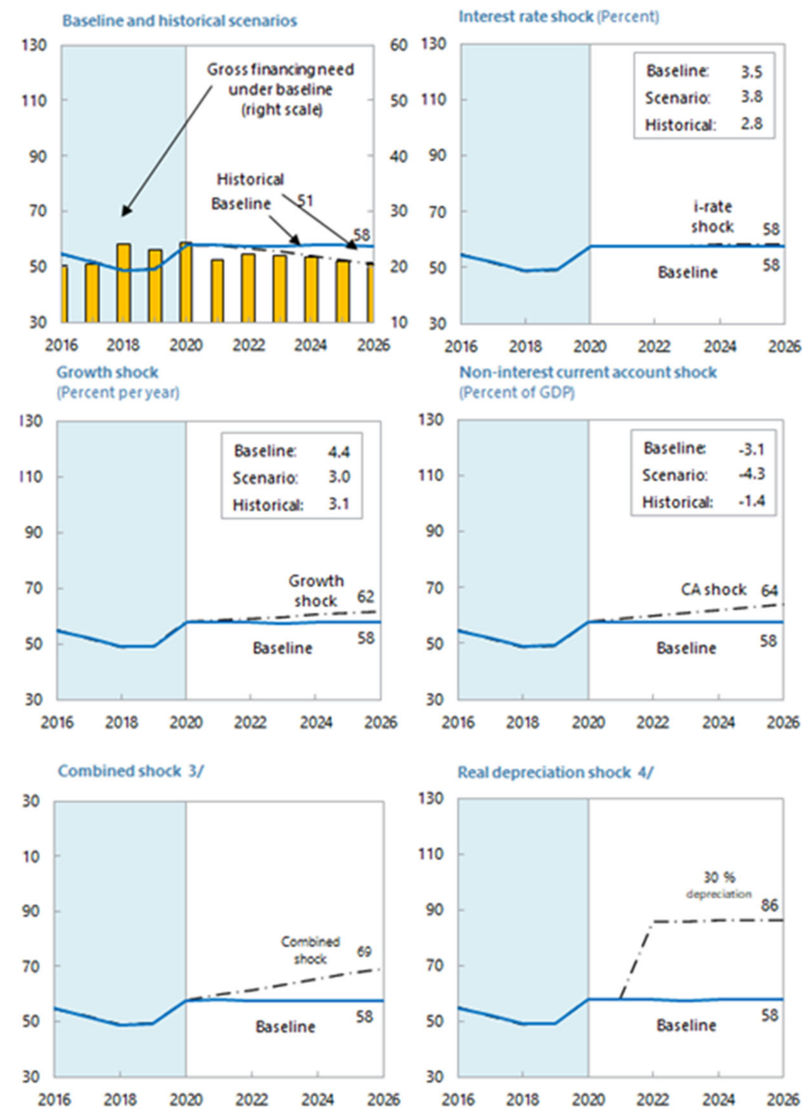
4/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

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.

Annex IV. Figure 7. 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 0.5 standard deviation shocks applied to real interest rate, growth rate, and current account balance.
4/ One-time real depreciation of 30 percent occurs in 2022.

Annex V. Risk Assessment Matrix (RAM)[1]

Risk	Relative Likelihood and Transmission Channels	Expected Impact if Risk is Realized	Policy Response
	Global risks		
1. Unexpected shifts in the COVID-19 pandemic: Prolonged pandemic (conjunctural)	**Medium** The disease proves harder to eradicate (e.g., due to new virus strains, short effectiveness of vaccines, unwillingness to vaccinate), requiring costly containment efforts and prompting persistent behavioral changes adversely impacting economic activity.	**High** Economic activity is disrupted, accompanied by higher unemployment. Negative global spillover through trade, capital flows and confidence effects on financial markets and investment. Slowing activity resulting in weaker fiscal revenues and increase in borrowing costs.	Prioritize public health responses to curb the disease. Allow fiscal automatic stabilizers to operate. Use fiscal space to provide targeted support. Maintain broadly accommodative monetary and financial settings. Advance structural reform agenda to facilitate reallocation of resources.
2. Sharp rise in risk premia that exposes financial and fiscal vulnerabilities (conjunctural)	**Medium** A reassessment of market fundamentals (e.g., in response to adverse COVID-19 developments) triggers a widespread risk-off event. Investors may sell Romanian financial assets after reassessment of risks, as outflows could arise from foreign holdings of government bonds and short-term debt. Financial market volatility could lead to a rapid and significant rise in interest rates and currency depreciation.	**Medium** Increase in borrowing costs. Risk of exchange rate overshooting and financial instability. NPLs could rise due to weakened repayment capacity of borrowers of lei and FX loans.	Tighten monetary settings, allow greater exchange rate flexibility. Utilize some of fiscal liquidity buffer for financing, on a temporary basis, until markets settle down.
3. Unexpected shifts in the COVID-19 pandemic: Faster containment (conjunctural)	**Medium** Pandemic is contained faster than expected due to the rapid production and distribution of vaccines, boosting confidence and economic activity.	**Medium** Faster economic recovery, notably with domestic demand rebounding on relaxation/removal of restrictions on activity. Higher private investment as confidence returns. Improved fiscal revenues and reduced pandemic related support expenditures.	Lock in budgetary gains for fiscal consolidation beyond the targeted deficit. Allow pandemic related support to expire but avoiding cliff effects. Phase out exceptional crisis-related monetary and financial sector accommodation. Accelerate implementation of structural reforms amidst the stronger growth environment.
	Domestic risks		
4. Political risks from a change in government due to parliamentary shifts in ruling coalition hamper implementation of reform plans (conjunctural)	**Medium** Fiscal reforms and consolidation trajectory is disrupted, with reemergence of populist initiatives. Associated worsening of market sentiment and fiscal financing turns challenging. Lack of progress on correcting EU's Excessive Deficit Procedure triggering further official actions. Risk of credit rating downgrade on fiscal and debt trajectory.	**Medium** Persistence of deficits lead to increased financing constraints. Possible feedback loops through banks, given debt exposures (sovereign-bank nexus).	Design package of policies with scope to mitigate political pushback against prudent reforms: deepen education and health reforms to address inequality; combine government spending restraint (wages and pensions) with provision of public investment and structural reforms to raise growth; and provide compensation to displaced or more affected groups and sectors, as well as support programs to facilitate transition and smooth reallocation of resources.
5. Significantly better absorption of EU funds (structural)	**Medium/Low** The government's envisaged medium-term fiscal reforms are assumed to materialize, taking opportunity of the large envelope of available EU resources (notably grants and non-reimbursable cohesion funds) to facilitate budget deficit reduction (including substituting domestic spending) while also cushioning the contractionary impact of the consolidation trajectory on growth. Public investment management reforms strongly raise the absorption level of EU funded projects.	**Medium/High** Budget financing constraints for investment are significantly reduced, helping promote quality fiscal consolidation without adding to debt. Quality infrastructure and digitalization and green investments help to accelerate transition to higher productivity and more efficient economy.	Prioritize and accelerate reforms of public investment management institutions and processes to raise EU fund absorption.

[1] The Ram shows events that could materially alter the baseline path. (The scenario most likely to materialize in the view of IMF staff). The relative likelihood of risks is staff's subjective assessment of risks surrounding the baseline. The Ram reflects views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly.

Annex VI. Monetary and Financial Policies During the Pandemic

Table A. Policy Roadmap [1/]

	Lockdown phase	Reopening phase	Recovery phase
Monetary Policy	Easing totaling 125 bps in policy rate to 1.25 percent, with a further 50 bps narrowing of interest rate corridor, and asset purchase program (APP, below).	Accommodative monetary stance maintained.	Maintain monetary policy accommodation until the policy objectives (e.g., inflation target) are achieved, and at least through 2021 to entrench recovery.
Liquidity to core funding markets	APP in the form of secondary market purchases of government bonds (½ percent of GDP to date); FX intervention to sustain smooth FX market functioning. Reduced statutory reserve requirements in FX from 8 to 5 percent. Precautionary ECB repo line of Euro 4.5 billion (initially to end 2020, extended to March 2022)	NBR asset purchases kept domestic market financing costs and premia contained during periods of market stress since March. APP paused in August 2020 but resumed modestly in March-April 2021 to address pressures from higher global yields. FX intervention sales continued.	Withdraw support.
Liquidity to financial institutions	Repos to banks as well as APP providing liquidity.	Maintained monetary operations and asset purchase operations as required.	Maintain operations as required for monetary policy accommodation.
Provision of credit: ease macro-prudential stance, support households and businesses, suspend dividends	Allowed use of previously built capital buffers; waived compliance with minimum liquidity ratio; restriction on dividend payouts (in line with ESRB guidance); government guaranteed loan program (predominantly to SMEs, see Table B) applying banks' underwriting criteria.	Macroprudential flexibility has been retained. Dividend restrictions have been continued, and extended until September 2021.	Re-build capital and liquidity buffers gradually over time while ensuring financial institutions' capacity to extend credit. Maintain tight restrictions on bank capital distributions (dividends and share buy-backs) until uncertainty relating to the pandemic's duration and its effects on private-sector balance sheets is more firmly resolved.
Addressing problem assets	Freeze on classification and provisioning standards arising from pandemic-related relief measures (in line with EBA guidance at the time in 2020).	Measures have been maintained through the reopening phase, with EBA guidance on moratoria to March 2021. NBR has guided banks to raise loan loss provisioning to 65 percent coverage (above EU average of 45 percent) and to keep NPL ratios under 5 percent.	Fully enforce classification and provisioning rules. Banks to undertake NPL diagnostics and develop credible plans to reduce problem assets. Support creation of private asset management companies and markets for problem assets, with more comprehensive, multifaceted strategy to address solvency in both corporate and financial sectors as needed, differentiating by types of impaired assets.

Table A. Policy Roadmap [1/]

	Lockdown phase	Reopening phase	Recovery phase
Private debt restructuring	Debt service moratoria, with loan repayment deferrals up to 9 months allowed.	Loan deferrals window extended to March 15, 2021. No enhancements of restructuring mechanisms so far.	Facilitate debt restructuring to reduce debt burden. Prepare for efficient and effective insolvency procedures. Transpose EU Directive on insolvency and restructuring.

[1/] See October 2020 Global Financial Stability Report, Chapter 1, which presents roadmap of appropriate actions for three phases of the pandemic. Description of Romanian authorities' actions as of May 2021. Colors from yellow to green indicate increasing degree of consistency with suggested roadmap. White blocks indicate recommended future steps

Table B. Summary targeting of SMEs on state guarantee schemes for corporates launched since 2020

The flagship is the IMM Invest program exclusively for SMEs, which provided a ceiling of RON 35 billion across 2020 and 2021 (out of about 44 billion cumulative corporate guarantees ceiling by the government so far). The programs have a limited government guarantee up to 80 percent of loan value for medium enterprises and 90 percent for small and micro enterprises, with loan tenor of between 3-6 years differentiated by purpose of loan, and interest rates starting from 3-month ROBOR + 2 percent per annum. Banks' underwriting criteria are maintained for approval.

Share of credit guarantees to SMEs	2020 73 percent of value of executed guarantees	2021 (planned) 71 percent of value of guarantees
Distribution of IMM Invest guarantees by number of enterprises	52 percent to Micro-category (0-9 employees) 38 percent to Small-category (10-49 employees) 10 percent to Medium-category (50-249 employees)	

Selected viability-related eligibility criteria under IMM Invest:

Share capital: not lost more than half of its share capital in the last two years and more than a quarter of this capital in the last 12 months.

Credit and liability status performance: not have outstanding payments on other loans or tax arrears, has not a ban to issue checks on the date of credit approval and does not appear with major incidents with promissory notes in the last 6 months, is not a defendant under litigation with the Ministry of Finance, and not under insolvency.

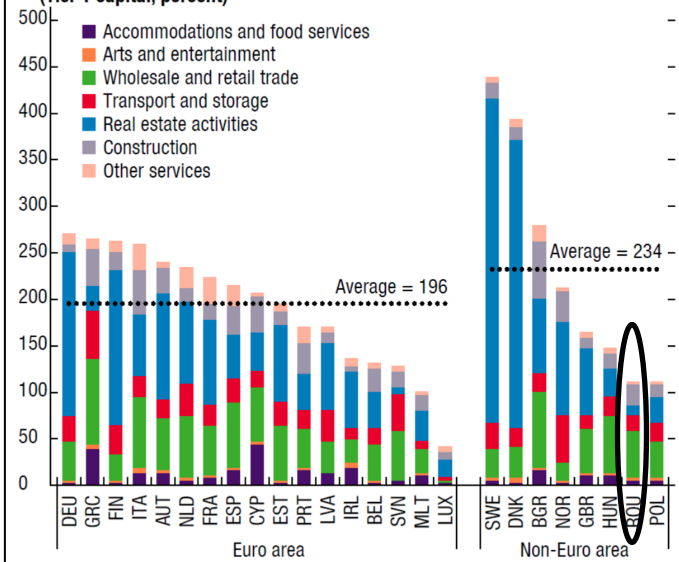
Main industries provided with IMM Invest guarantees	construction, road transport, agriculture (cereals and vegetables), restaurants

Sources: As of March 2021. IMM Invest, national authorities

Discussion Issue: Navigating the Banking System Through the COVID-19 Recovery Phase

12. The banking system entered the COVID-19 crisis in a strong position. Systemwide as of end-2019, capital (solvency) ratios reached 22 percent, profitability was strong at 1.3 percent return-on-assets (also compared to average Western EU banks), and liquidity ample (liquidity ratio of 2.3 versus the regulated threshold of 1.0, and loan-to-deposit ratio about 70 percent). Further, NPL ratios had been declining since the last peak in 2014 to reach levels close to EU averages, encouraged by conservative supervision of the NBR which also fostered maintaining high loan loss provisioning of around 60 percent (vs 45 percent EU average). As Romania is not tourism-intensive and comparatively less urbanized, bank credit exposure to the most COVID-affected sectors such as HoReCA was limited (chart 1).

1. EU+UK: Large Banks' Exposure to Highly Affected Sectors
(Tier 1 capital, percent)



Sources: European Banking Authority 2020 Transparency Exercise; and IMF staff calculations.
Note: Data labels in the figure use International Organization for Standardization (ISO) country codes.

13. Policy interventions and regulatory relief measures helped cushion the impact of the COVID-19 crisis (see Table A above). Many of these measures were also seen in other EU countries, guided by EU-wide initiatives such as by the European Banking Authority (EBA. As a result, liquidity has been provided to alleviate stresses, credit market functioning has been protected and the flow of credit to households and businesses has been sustained. Financial intermediation improved – private credit to GDP rose in 2020 after declining since 2011. Financial sector measures also reinforced the fiscal support and monetary policy easing as part of broad counter-cyclical package.

14. As the economy has entered a recovery phase in 2021, the following discusses how the calibration of banking sector policies could evolve across three dimensions—borrower support measures, supervisory guidance and capital conservation, and balance sheet repair—to balance necessary but targeted accommodation while safeguarding financial stability (Table C).

Table C. Three dimensions for recalibrating bank policies in recovery phase

	Developments 1/	Discussion on actions
I. Borrower Support Measures		
Debt service moratoria	Take-up on these loan deferrals peaked at over a fifth of total outstanding household and corporate loans in the initial months in 2020, but the bulk has since been repaid and the request pipeline has ebbed. By Q1 2021, the outstanding stock of these were very low (estimated at less than 5 percent of total loans previously under moratoria).	The window to request loan deferrals was appropriately allowed to expire on March 15, 2021. Even without such legislative moratoria, banks retain flexibility to extend repayment plans for clients, which can be more targeted and tailored, while also likely mitigating potential cliff effects.
Government credit guarantees to corporates	Directly predominantly to SMEs, the cumulative ceiling has risen to around 4 percent of GDP, half taken up by end-2020. The schemes were augmented for 2021. See Table B above for details on targeting and eligibility criteria.	While useful to extend this program for 2021, part of liquidity from credit could be gradually replaced by government grant schemes (some EU funded) that have recently becoming operational for COVID-affected SMEs, which would also help on solvency.
II. Supervisory guidance and capital conservation		
Supervisory guidance on availability and duration of relief	Despite the EBA-guided freeze in 2020 on loan classification and provisioning standards, NBR has been actively asking banks to be conservative on classification and report risk assessments of loans. Banks reported that loss provisioning turned out to be more than ample in 2020 and were in a position to release some in 2021. No banks have applied for relaxation to use capital buffers, and capital ratios systemwide have continued to increase since end 2019.	Loan classification standards were appropriately restored in 2021, which will help improve visibility on asset quality going forward. In case significant losses are recognized ahead (albeit not expected), a longer period to rebuild capital can be allowed.
Capital conservation measures	Dividends and share buy-back restrictions began in 2020 as per EU-wide guidelines and were extended to September 2021 as recommendations. This measure was the key driver of rising capital ratios given the sustained good profitability of Romanian banks even during the pandemic.	Given high foreign ownership of the banking system (over 70 percent), the extension of the restrictions through most of 2021 is prudent to retain resources for capital until a fuller picture on the extent of loss write-downs becomes apparent after all the relief measures expire.
III. Bank balance sheet repair		
Managing NPLs that emerge	Reported NPLs remain low into 2021 even as classification standards have been restored, but once all support and relief measures such as moratoria expire, a rise in bankruptcies and loan defaults may yet follow. Obstacles to NPL resolutions also exist following several distortionary legislative initiatives in place since 2018 (e.g., onerous tax treatment on NPL sales).	The NBR may draw from its successful experience of reducing NPLs between 2014-2018, including by facilitating sales to private asset management companies. The legislative obstacles that hinder NPL disposals should be amended to facilitate efficient reduction of NPLs that emerge.

Table C. Three dimensions for recalibrating bank policies in recovery phase		
	Developments 1/	**Discussion on actions**
Facilitating efficient insolvency and restructuring	Current insolvency regime needs to be strengthened, particularly lacking fast-track procedures for restructuring debt. Further, out-of-court restructuring options are not clear.	Useful changes to the insolvency law are envisaged for 2021 to transpose the EU Directive on insolvency and restructuring.
1/ Information as of mission in May 2021.		

15. The banking system has also performed better to date than a historically based simulated stress test exercise. This is compared to an illustrative exercise of historically derived bank stresses during past economic downturns in Romania, using the methodology and results derived from a recent IMF paper[1] for European banks, which simulated shocks using IMF's World Economic Outlook projections. The simulation suggested that for a sample of 11 Romanian banks that common equity Tier-1 (CET1) bank capital would have been projected to be drawn down by around 3½ percentage points between end-2019 and end-2021, even with a subset of the policy support measures factored in (chart below), albeit still remaining above various required thresholds. In contrast, actual outturns show capital ratios have continued to rise over 2020 and 2021 to date, and bank profitability has been largely sustained despite the pandemic, in contrast to projected losses if assuming historical relationships from past Romania economic crisis.

[1] Aiyar, Dao, Jobst, Mineshima and Mitra (2021). EUR departmental paper: "COVID-19: How Will European Banks Fare?"

Annex VI. Figure 1. Romania Banks: Solvency Stress Test (Extended Coverage), April 2021 WEO
(CET1 ratio, percent)

Sources: EBA; ECB; ESRB; FitchConnect; S&P Market Intelligence; and IMF staff estimates.
Note: CCB=capital conservation buffer, CET1=common equity Tier 1, MDA=maximum distributable amount (weighted average). The grey shaded area of the boxplots shows the inter-quartile range (25th to 75th percentile), with whiskers at the 5th and 95th percentile of the distribution. */ Debt repayment relief (moratoria) for businesses and households, public credit guarantees, deferred bankruptcy proceedings, and dividend restrictions (only in 2020); The analysis covers all three channels affecting the capital adequacy ratio under stress - profitability (net interest income and provisions), nominal assets (net lending and charge-offs after reserves), and risk exposure (changes in credit risk weights). The crisis-specific risk drivers of these channels are: (1) write-offs due to the projected insolvency of illiquid and insolvent firms (weighted by outstanding debt and mapped to the sector-by-sector corporate exposure of sample banks), (2) the profitability impact of policy measures (lower provisions for guaranteed loans to solvent corporates, loss forbearance on eligible loans under moratoria, and decline in interest income due to duration of debt moratoria), and (3) the increase in risk weights to the general increase of the default risk of mortgages and corporates. In addition, there is a general change in net operating income after general provisions and losses on other noninterest income due to lower GDP growth and higher unemployment rate, including impairment charges for non-corporate exposures.

ROMANIA

July 22, 2021

STAFF REPORT FOR THE 2021 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

Prepared By European Department

CONTENTS

FUND RELATIONS

(as of May 31, 2021)

Membership Status	Joined 12/15/72	Article VIII
General Resources Account	**SDR million**	**% Quota**
Quota	1,811.40	100.00
Fund holdings of currency	1,811.40	100.00
Reserve Tranche Position	0.00	0.00
SDR Department	**SDR million**	**% Allocation**
Net cumulative allocation	984.77	100.00
Holdings	989.93	100.52
Outstanding Purchases and Loans	**SDR Million**	**% Quota**
Stand-By Arrangements	0.00	0.00

Financial Arrangements

Type	Approval Date	Expiration Date	Amount Approved (SDR million)	Amount Drawn (SDR million)
Stand-By	09/27/13	09/26/15	1,751.34	0.00
Stand-By	03/31/11	06/30/13	3,090.6	0.00
Stand-By	05/04/09	03/30/11	11,443.00	10,569.00
Stand-By	07/07/04	07/06/06	250.00	0.00
Stand-By	10/31/01	10/15/03	300.00	300.00
Stand-By	08/05/99	02/28/01	400.00	139.75
Stand-By	04/22/97	05/21/98	301.50	120.60
Stand-By	05/11/94	04/22/97	320.50	94.27
Stand-By	05/29/92	03/28/93	314.04	261.70
Stand-By	04/11/91	04/10/92	380.50	318.10

Overdue Obligations and Projected Payments to Fund[1]

(SDR million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2021	2022	2023	2024	2025
Principal					
Charges/interest		0.02	0.02	0.02	0.02
Total		0.02	0.02	0.02	0.02

[1] When a member has overdue financial obligations outstanding for more than three months, the amount of such arrears will be shown in this section.

Exchange Rate Arrangement

Romania has accepted the obligations of Article VIII and maintains an exchange rate system free of multiple currency practices and restrictions on making of payments and transfers on current international transactions except for those maintained solely for preservation of national or international security in accordance with UNSC resolutions and that have been notified to the Fund under the procedure set forth in Executive Board Decision No. 144-(52/51). De jure exchange rate arrangement is managed floating and the de facto exchange rate arrangement was reclassified to “crawl-like” from “stabilized” (effective August 23, 2019).

Technical Assistance

Capacity building in Romania has been supported by substantial technical assistance from multilateral agencies and bilateral donors. The Fund has provided support in several areas with almost 30 technical assistance missions and expert visits since 2012.

Date	Purpose	Department
	Tax Administration	
March–April 2012	Strengthening the capacity of the National Agency for Fiscal Administration (ANAF).	FAD
July–August 2012	Organizational reforms, strategic direction, plan for restructuring of ANAF and implementation of a compliance strategy.	FAD
August–September 2012	Follow-up on the reorganization of ANAF.	FAD
November–December 2012	Follow-up with ANAF, particularly on the antifraud unit.	FAD
March–April 2013	Training to improve high net wealth individual compliance.	FAD
Apr., Sep., Nov. 2013, Jan. 2014	Follow-up with ANAF.	FAD
April 2014	Assistance to ANAF on pilot structural compliance project targeted at undocumented labor. Training on payroll audit.	FAD
April 2014	Stock taking on assistance and identification of future TA focus: compliance risk management, reorganization of ANAF, pilot projects.	FAD
January–February 2015	Follow-up and training to improve high net wealth individual compliance.	FAD
July-August 2015	Review of the performance of the large taxpayer office and tax compliance management concerning high wealth individuals.	FAD
April 2016	Tax compliance risk analysis related to large businesses.	FAD
November 2016	ANAF performance outcomes compare to international best practice.	FAD
May 2020	Modernizing tax administration to support revenue mobilization.	FAD
	Tax Policy	
September 2013	Strengthening the property tax and natural resource tax regime.	FAD
September 2014	Follow-up assistance with creating a new natural resource tax regime.	FAD
June 2015	Workshop on petroleum tax regime design.	FAD
	Public Financial Management	
March 2012	Setting up commitment control and fiscal reporting systems.	FAD
October 2012	Follow-up assistance in setting up commitment control and fiscal reporting systems, especially methodologies and functionalities.	FAD
April 2013	Follow-up assistance in setting up commitment control and fiscal reporting systems, including methodology to verify arrears of local government.	FAD
December 2013	Follow-up assistance in setting up commitment control and fiscal reporting systems, including requirements from decentralization plans.	FAD
February 2014	Fiscal Transparency Evaluation.	FAD
January 2015	Follow-up assistance in setting up commitment control and fiscal reporting systems, review of public investment practices and program budgeting.	FAD
June 2015	Follow-up assistance on strengthening public investment management and implementing public expenditure reviews.	FAD

June 2016	Assistance on institutionalizing spending reviews and preparing spending review reports.	FAD
October 2016	Follow-up assistance to advise on piloting spending reviews.	FAD

Date	Purpose	Department
	Financial Sector Issues and Monetary Policy	
November 2012	Follow-up on program-related financial sector issues, including progress with contingency planning.	MCM
October 2014	Assessment of the monetary policy framework.	MCM
	Accounting and NPL	
October 2013	Achieving timely NPL write-off within the IFRS framework.	MCM

Expert Fund assistance has focused in recent years mostly on structural fiscal reforms, in particular modernizing tax administration, strengthening public financial management, and reviewing tax policy options. Technical assistance to the National Bank of Romania focused on upgrading contingency planning, dealing with non-performing loans, and reviewing monetary and exchange rate policy tools.

Article IV Consultations

Romania is on a 12-month consultation cycle. The previous Article IV consultation was concluded by the Executive Board on August 28, 2019.

FSAP and ROSC

A joint IMF-World Bank mission conducted an update assessment of Romania's financial sector as part of the Financial Sector Assessment Program (FSAP) during October 21-November 31, 2017, and January 11-23, 2018. The Financial Sector Assessment Report (FSSA) was discussed at the Board in June 2018.

A pilot of the IMF's new Fiscal Transparency Evaluation took place in February 2014 and the findings were published in March 2015. It assessed the government's fiscal reporting, forecasting, and risks management practices against the IMF's revised Fiscal Transparency Code.

Resident Representative

Since September 2019, the local Fund office in Bucharest overseen by the Senior Regional Resident Representative, Mr. Nadeem Ilahi.

COLLABORATIONS WITH OTHER INTERNATIONAL FINANCIAL INSTITUTIONS

- As of June 23, 2021, Romania has collaborations with the World Bank Group, the European Bank for Reconstruction and Development, and the European Investment Bank.

- Further information can be obtained from the following hyperlinks.

International Financial Institution	Hyperlink
The World Bank Group	https://www.worldbank.org/en/country/romania/overview#4
The European Bank for Reconstruction and Development (EBRD)	https://www.ebrd.com/country/romania.html
The European Investment Bank	https://www.eib.org/en/projects/regions/european-union/romania/index.htm

STATISTICAL ISSUES

(as of June 23, 2021)

I. Assessment of Data Adequacy for Surveillance
General: Data provision is adequate for surveillance.
National accounts: Quarterly and annual national accounts statistics are produced by the National Institute for Statistics (INS) using the *European System of Accounts 2010 (ESA 2010)*. Estimates are reported to the Fund on a timely basis for publication in the *International Financial Statistics (IFS)*. Provisional and semi-final versions are disseminated in the *Statistical Yearbook* and other publications, as well as on the web (www.insse.ro).
Prices: The Consumer Price Index is subject to standard annual reweighting, and is considered reliable. In January 2004, the INS changed the coverage of the Producer Price Index (PPI) to include the domestic and export sectors. PPI weights are revised every five years with revisions finalized three years after the new base year.
Labor market: Labor market statistics are broadly adequate. The definition used for employment is consistent with *ESA 2010*.
Public finances: Annual GFS data for the general government sector, including public corporations operating on a non-market basis, are reported on an accrual basis derived from cash data using various adjustment methods. Tax revenues are adjusted using the time-adjusted cash method; expense data are adjusted using due-for-payments data; and interest payments are calculated on an accrual basis. Accrual data are also available on a quarterly basis three months after the end of each quarter. EUR receives monthly cash budget execution data. Consolidated data on general government operations, financial assets and liabilities are reported for inclusion in the IMF *GFS annual database*.
Monetary and financial statistics: The National Bank of Romania (NBR) reports monetary and financial statistics for publication in the *IFS,* using the Standardized Report Forms (SRFs). The SRFs for the central bank and other depository corporations are reported on a monthly basis, while the SRF for Other Financial Corporations (OFCs) is reported on a quarterly basis. The NBR also reports data on some key series and indicators of IMF's Financial Access Survey including gender disaggregated data, mobile money and the two indicators adopted by the UN to monitor Target 8.10 of the Sustainable Development Goals (commercial bank branches 100,000 adults and ATMs per 100,000 adults). **Financial Soundness Indicators (FSIs)**: The NBR reports all core and most encouraged FSIs for Deposit Takers on a quarterly basis. In addition, the NBR reports FSIs for the nonfinancial corporations (NFCs) and households (HHs) sectors, as well as those for real estate markets. However, FSIs for NFCs are reported with a long lag.

External sector statistics: The NBR routinely reports quarterly and annual balance of payments and international investment position statistics to the Fund and external debt statistics to the World Bank's QEDS database in a timely fashion. Since September 2014 the authorities implemented the sixth edition of the *Balance of Payments and International Investment Position Manual* (*BPM6*), in line with other European countries. Romania participates in the IMF's Coordinated Portfolio Investment Survey (CPIS), Coordinated Direct Investment Survey (CDIS) and reports International Reserves and Foreign Currency Liquidity (IRFCL) Data Template.	
II. Data Standards and Quality	
Romania is a subscriber to the Fund's Special Data Dissemination Standard Plus (SDDS Plus) since November 1, 2019.	A Data ROSC was published in November 2001.

Romania: Table of Common Indicators Required for Surveillance
(as of July 2021)

	Date of latest observation	Date received	Frequency of Data[6]	Frequency of Reporting[6]	Frequency of Publication[6]
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	June 2021	July 2021	D and M	D and M	M
Reserve/Base Money	May 2021	June 2021	D and M	W and M	M
Broad Money	May 2021	June 2021	M	M	M
Central Bank Balance Sheet	May 2021	June 2021	M	M	M
Consolidated Balance Sheet of the Banking System	May 2021	June 2021	M	M	M
Interest Rates[2]	June 2021	July 2021	M	M	M
Consumer Price Index	May 2021	June 2021	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4]	May 2021	July 2021	M	M	M
Stocks of Central Government and Central Government-Guaranteed Debt[5]	Q1 2021	June 2021	Q	Q	Q
External Current Account Balance	Apr 2021	June 2021	M	M	M
Exports and Imports of Goods and Services	Apr 2021	June 2021	M	M	M
Gross External Debt	Apr 2021	June 2021	M	M	M
International Investment Position[7]	Q1 2021	May 2021	Q	Q	Q

[1] Any reserve assets that are pledged or otherwise encumbered should be specified separately. Also, data should comprise short-term liabilities linked to a foreign currency but settled by other means as well as the notional values of financial derivatives to pay and to receive foreign currency, including those linked to a foreign currency but settled by other means.
[2] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[3] Foreign, domestic bank, and domestic non-bank financing.
[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds), and state and local governments.
[5] Including currency and maturity composition.
[6] Daily (D), weekly (W), monthly (M), quarterly (Q), annually (A), irregular (I); and not available (NA).
[7] Includes external gross financial asset and liability positions vis-à-vis nonresidents.