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Romania: Balance-of-Payments Assistance Programme 2013-2015

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EXECUTIVE SUMMARY

The European Commission and the IMF paid a staff visit to Romania to negotiate a possible third economic adjustment programme. Following Romania's request of 4 July 2013 for such a third programme, and the Commission's preliminary assessment, the EU's Economic and Financial Committee agreed on the opening of negotiations in its meeting on 9 July 2013. The ensuing staff mission (17-31 July) reviewed the macro framework, agreed on the mid-year budget adjustment (in keeping with the 2.4% of GDP deficit target in ESA terms), and negotiated the conditions for, and the modalities of a possible new programme. The conditions are reflected in the draft Memorandum of Understanding (MOU), and the Letter of Intent (LoI)-Memorandum of Economic and Financial Policies (MEFP)-Technical Memorandum of Understanding (TMU) as signed on 12 September 2013 (Annex 6). As to modalities, agreement was reached on a 2-year programme providing precautionary support of up to 4 billion euro (equally split between the EU and the IMF). The World Bank (WB) has made 1 billion euros available under a Development Policy Loan (DPL) with a deferred drawdown option (DDO) valid through December 2015. In addition, the WB will continue providing earlier committed support of 891 euros million of which 514 euros million are still to be disbursed. The Economic and Financial Committee (EFC) approved the new Balance of Payments (BoP) programme in its meeting on 3 October 2013. The EU Council of Ministers adopted the relevant decisions underlying the new programme on 22 October 2013. ([1])

Political situation: The political situation has been relatively stable. The government enjoys a substantial majority in Parliament and the Prime Minister and the President have been cooperating positively on issues pertinent to the EU/IMF-supported programme.

Macro framework: The mission reviewed the macro framework, scaling up **GDP growth** for 2013 from 1.6% (in the 2013 spring forecast) to +1.9% based on better-than-expected (net) exports and a very good agricultural output. Risks to the 2013 forecast are balanced. For 2014, economic growth forecasts remained unchanged since spring and real GDP is expected to grow by 2.2%. **Inflation** is expected to decrease rapidly in the second half of 2013 thanks to a sharp drop in volatile food prices (already observed in recent data), whereas the adverse base effect would also vanish in the second half of 2013. Annual average inflation is estimated to be around 4% in 2013, with yeor-on-year inflation falling below 3.5% in December 2013, thus within the central bank's target range (2.5% ±1pp). A further deceleration is expected in 2014. **Unemployment** has slightly increased in early 2013 and is expected to be, on average, somewhat above 7% in 2013.

Balance of payments: Romania is expected to maintain access to sovereign financing over the programme period barring adverse external developments. CDS spreads with the Bund have reached their lowest levels since 2010. The current-account deficit is expected to decrease from around 4% of GDP in 2012 to around 2% in 2013, mainly thanks to a much lower trade deficit as export is booming and import is slightly decreasing. The importance of portfolio investments for financing the current-account deficit has increased. Foreign direct investment remains sluggish.

Banking sector developments: The Romanian banking sector capitalisation remained at reassuring levels (the capital adequacy ratio stood at 14.7% at end-June 2013), notwithstanding the upward trend in impaired assets. The non-performing loans (NPL) ratio reached 20.3% in June 2013. Nevertheless, risks associated with increasing NPLs have been mitigated by the prudent loan-loss provisioning policy of the supervisor although provisions continue to put a strain on banking sector profitability (the sector returned to positive results with a return on equity of 6% in the first half of 2013 after 3 years of losses). The central bank continues to closely oversee the banks from peripheral euro-area countries, which have, so far, managed to maintain sufficient capital buffers. The spill-overs from the Cypriot crisis were mitigated through the agreement to transfer the local deposit base of the Romanian branch of Bank of Cyprus to Marfin Bank, the subsidiary of Laiki Group. In line with regional developments, the deleveraging process of foreign banks and the reduction in parent bank funding (-14.6% since December 2012) continue to constitute an issue of concern.

([1]) Council Decisions 2013/531/EU and 2013/532/EU of 22 October 2013 published in OJ No L286 of 29 October 2013

POLICY CONDITIONS

In terms of conditionality, the point of departure for a new programme was to preserve the achievements of the previous two programmes and to roll-over yet unfulfilled conditions from the second programme into a new programme.([2]) This is reflected in the MoU where explicit references are made when appropriate. New conditionality was selected on the basis of its significance for overall macroeconomic performance and financial stability. The conditionality partly overlaps with the country-specific recommendations (CSRs) addressed to Romania by the Ecofin Council on 9 July 2013.([3])

Fiscal policy discussions focused on the mid-year budget adjustment and the conditions under a new programme, with a focus on fiscal governance issues. The authorities and the mission agreed upon the mid-year budgetary rectification which preserves the goal of reducing the general government deficit to 2.4% of GDP as previously agreed. With government revenue underperforming and the government's wish to reduce VAT on bread, compensatory measures had to be found. Conditions for a new programme include a requirement for fiscal consolidation to continue in line with the Stability and Growth Pact (SGP) requirements until the achievement of the medium term objective (MTO). As to fiscal governance and other structural fiscal measures, a new programme would target an update of the fiscal framework in line with Fiscal Compact requirements. Other improvements sought relate to the content of the Romanian Fiscal Strategy, to the transparency of the budgeting process, to improvements in the annual and medium-term capital budgeting, to the finalisation of the commitment control system (to prevent new arrears), as well as to improvements in tax administration aimed at more efficient tax collection.

Public debt management has to be further improved so as to establish a deeper and more liquid sovereign debt market, to develop the domestic capital market and to reduce financing risks. Measures agreed include: (i) further improvements in the public debt management strategy; (ii) the finalisation of an electronic auction system for domestic primary issuances, the introduction of an electronic trading platform to monitor transactions in the secondary market; (iii) better outreach to investors in government debt; (iv) the establishment of the necessary framework to carry out buybacks, bond exchanges and repo operations; and (v) involvement of the treasury in a central counterparty clearing house.

Financial sector conditionality focuses on further strengthening the bank resolution framework, the contingency planning for the National Bank of Romania (NBR) and the corporate governance of the Deposit Guarantee Fund. To strengthen financial stability, it was agreed to speed up the process of balance-sheet cleaning and to preserve credit discipline and avoid moral hazard among debtors. To develop the capital market and diversify the sources of funding for banks, authorities agreed to amend the covered-bonds legislation. Finally, to strengthen the supervision of the non-bank financial market, authorities committed to further align the legislation on the Financial Supervisory Authority (FSA) to international good practices.

Administrative capacity: One of the cornerstones of the new programme is the improvement of the country's public administration and governance since its poor state and instability reflects on the capacity to design and implement high-quality policies. The authorities committed to continue following up and reporting on a quarterly basis on the implementation of action plans drawn up in response to the findings of the functional reviews. However, to understand the progress made in this particular area, the authorities were also invited to report every six months to the Economic and Financial Committee (EFC) and the Economic Policy Committee (EPC). The first detailed reporting to the committee(s) should take place in March 2014. The authorities also agreed to establish, by end-2013, a central delivery unit located directly under the Prime Minister, in line with an already existing World Bank project. The new unit should allow improvement of the government-wide policy prioritisation. It will particularly focus on ensuring appropriate follow up to the CSRs issued by the Council in the context of the European Semester (Annex 7).

([2]) See the overall assessment in Ecfin Occasional Paper 156 of July 2013.
([3]) OJ No C 217 of 30 July 2013.

Product markets: While regulatory reforms in the energy and transport sectors initiated under the previous programme are being implemented, some parts of the previous programme conditionality have yet to be fulfilled. In the energy sector, reforms aim at creating functioning electricity and gas markets that should, in turn, lead to more investment in the energy power grid. They include electricity and gas price liberalisation and the finalisation of the unbundling of energy transmission and dispatch operators. In rail transport, proper performance schemes related to delays and incentives for reducing unit costs and charges of the rail infrastructure manager are to be introduced.

Business environment: Romania's poor business environment acts as a drag on growth and investment and its improvement is therefore very important. This is why the new programme features conditionality in this area, focusing on: (i) improving the quality of regulation related to business; (ii) reducing administrative burdens for SMEs; (iii) improving access to finance for SMEs; (iv) supporting SMEs that plan to export; (v) improving the land registry system to allow for a better functioning land and property markets; and (vi) improving incentives for inventions by employees.

Labour markets: Following the measures already taken under the previous programmes, the only new condition is to duly consider a review of labour taxation with a view to reducing, in a budget-neutral manner, the effective tax burden on labour for low- and middle-income earners. Currently, the tax wedge on these categories is relatively high, entailing risks of pricing them out of the market or encouraging the shadow economy.

Pensions: Following the pension reform of late 2010, the Romanian authorities committed to pass the necessary legislation to equalise the pensionable age of men and women in line with the CSRs issued to Romania.

State-owned enterprises play an important role in Romania’s economy, but their management is suboptimal. Reforms are therefore necessary, but have been slow and unambitious. Improvements in corporate governance through the appointment of professional management and boards for state-owned enterprises (SOEs) have been limited. The sale of stakes in SOEs has suffered from setbacks and changes in strategy. For the new program, targets were selected to ensure both an encompassing view on arrears reduction and a detailed follow-up on operational performance improvements in the three railway companies and their subsidiaries, which generate the largest arrears. Timelines have been set for the sale of stakes in a more limited set of key SOEs in the transport and energy sector.

The Romanian healthcare system is facing several challenges, including poor health outcomes, low funding and an inefficient use of resources, turning it into an important source of risks for public finances. The mismatch between spending commitments and available funding has led in the past to the accumulation of arrears, particularly in the hospital sector, and to large budget overruns in the area of pharmaceutical spending. Arrears have been effectively reduced in the hospital sector, but pending necessary structural reforms, the risk of arrears re-accumulation remains. A comprehensive medium-term health strategy, to be prepared by the Ministry of Health and the Ministry of Public Finance by end-2013, is henceforth key to close the current and future financing gaps. In order to improve spending efficiency, the publicly-reimbursable basic-benefits package is being re-defined within the limitations of available funding. The published strategic action plan will have to be implemented. It aims at rationalising and restructuring the hospital structure and increasing the scope for primary care.

PROGRAMME DESIGN AND OBJECTIVES

The third EU medium-term financial programme for Romania will address the remaining risks surrounding the sustainability of the balance of payments of Romania. It continues to provide support to the economic programme of the government aiming, among other things, at consolidating macroeconomic, fiscal and financial stability, enhancing administrative capacity, reforming the tax administration, improving public financial management and control, and increasing the resilience and the growth potential of the Romanian economy.

The Romanian authorities requested support from the EU and the IMF. The EU received a request from the Romanian authorities on 4 July 2013. Following a positive opinion of the EU's Economic and Financial Committee on the opening of negotiations, a joint EU/IMF staff mission was held in the second half of July 2013 to review the macro framework and to negotiate the conditions for a new programme.

Agreement was reached on a 24-months programme providing precautionary support of 4 billion euros, equally split between the EU and the IMF. If activated, the programme will consist of an EU loan of an amount of up to 2 billion euros and IMF support of up to 1.75 billion SDR (around 2 billion euros) provided under a new Stand-By Arrangement. In addition, the World Bank has made 1 billion euros available under a Development Policy Loan (DPL) with a deferred drawdown option (DDO) valid through December 2015. The WB will also continue providing earlier committed support of 891 million euros, of which 514 million euros is still to be disbursed. The conditions of the EU programme are reflected in the Memorandum of Understanding (MOU), and in the Letter of Intent (LoI), the Memorandum of Economic and Financial Policies (MEFP), and the Technical Memorandum of Understanding (TMU) (Annex 6).

The Economic and Financial Committee (EFC) approved the new Balance of Payments (BoP) programme in its meeting on 3 October 2013. The EU Council of Ministers adopted the relevant decisions underlying the new programme on 22 October 2013. [4]

Progress in programme implementation will be monitored by Commission and IMF staff. Monitoring will take place through semi-annual programme reviews in spring and autumn (on which occasions adjustments to the Memorandum of Understanding can be made) and interim missions in-between. The Commission staff will report on the results of these reviews to the Economic and Financial Committee. The Romanian authorities will also report to the EFC and the EPC on progress made in improving its administrative capacity. On the IMF side, the program will be monitored initially through three quarterly reviews followed by two semi-annual reviews as of spring 2014 combined with quarterly performance criteria and quarterly missions in-between. The IMF staff will report on the results of the reviews to its Executive Board.

(4) Council Decisions 2013/531/EU and 2013/532/EU of 22 October 2013 published in OJ No L286 of 29 October 2013

Part I

Macroeconomic developments and outlook

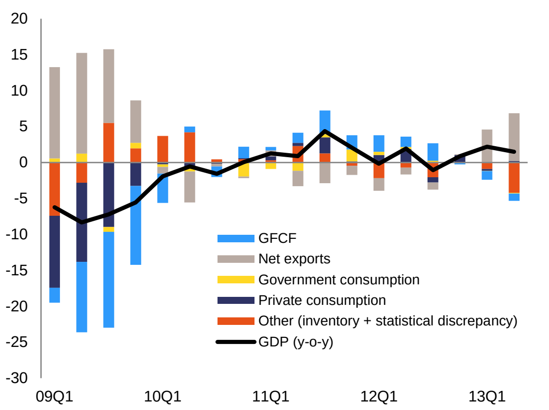
1. GROWTH AND INFLATION

1.1. GROWTH

Following a cumulative contraction of almost 8% in 2009-2010, economic growth in Romania has turned positive in 2011.

Recent developments suggest that GDP growth in 2013 will be at about 2%, i.e. somewhat stronger than the 1.6% projected in the Commission's spring forecast. Provisional second quarter GDP data surprised positively (+ 0.5% q-o-q SA, +1.5% y-o-y). The main drivers behind this are a stellar export performance and an outstanding harvest. Export grew by nearly 11% in H1 in real terms (as compared to H1 2012), mainly on account of the automotive industry and services (graph I.1.1**)**.

Graph I.1.1: **GDP contributions - Expenditure side (2009-2013)**

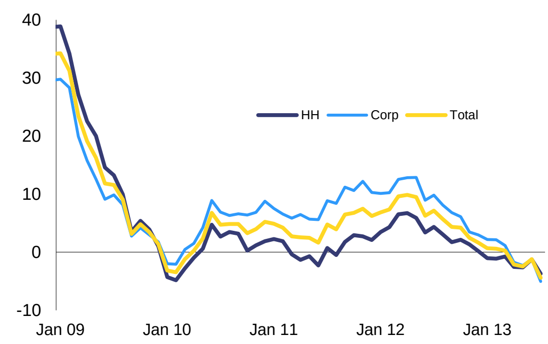


Source: Eurostat and own calculations

These positive trends, however, mask a weak domestic demand, with consumption being flat and investment contracting in the first half of 2013. The weakness of domestic demand is reflected in a decline in import (-0.9% in real terms in H1), although part of the decline can also be ascribed to lower energy imports (thanks in part to a mild winter).

Weak consumption growth reflects continued deleveraging by households and fiscal consolidation by the public sector. Although private consumption had a marginal positive contribution in Q2 (0.2%), it remains constrained by the continuing needs for repairing household' balance sheets.([5]) Lending to households has been contracting since January 2013 (Graph I.1.2) also because of the implementation of tighter credit standards by the central bank on foreign-currency denominated loans while there is still little demand in the market for RON-denominated loans. Moreover, real gross wages have been improving only marginally in H1 2013 (by 0.8% compared to H1 2012). Finally, although inflation came down from 5.1% in January to 2.6% in August 2013, it continues to erode households' purchasing power. Public consumption continues to be constrained by the need for further, albeit more gradual, fiscal consolidation despite the increase by 7.4% of the public sector wages in December 2012.([6])

Graph I.1.2: **Domestic credit to the private sector (Total loans, y-o-y)**



Source: Reuters EcoWin, Commission services calculations

Declining investment reflects a plunge in construction. Both public and private investment contracted in H1 2013 leading to a plunge in construction output in Q2 2013 by 8.3% (y-o-y).([7]) This is likely related to the on-going reduction of public capital expenditure coupled with the still very low pace of EU funds absorption (Annex 3).

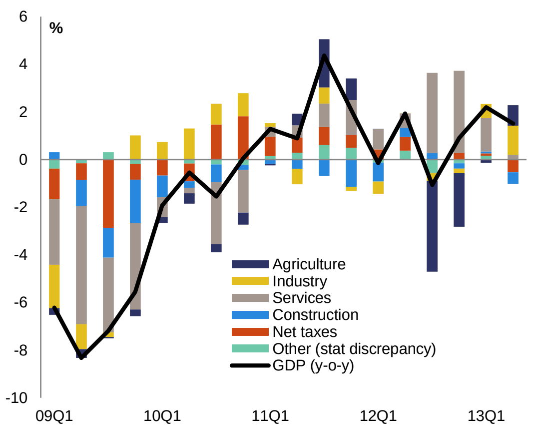
([5]) Many households still suffer from high debt-service-to-income ratios due to high interest rates and low incomes, leaving little margin for consumption. Also, the total non-performing loans continued to increase reaching 20.3% at end-June 2013 (while the non-performing loans ratio for households stood at 13.4% at end-June, NBR data).

([6]) This was the last step in reversing the 25% cut applied to all public wages in 2010, as an emergency measure.

([7]) All three components of the construction output had a negative evolution in Q2 2013: -13.9% y-o-y for residential building and -6.2% y-o-y for non-residential buildings (a proxy for private investments) while civil engineering works (a proxy for pubic investments) decreased by 8.4% y-o-y.

On the supply side, industrial production showed a very good performance in H1 2013 while both construction and retail sales declined. Reflecting the industrial production evolution, the industry gross value added (GVA)([8]) increased by 3.9% in real terms in H1 2013 (compared to H1 2012, see graph I.1.3).

Graph I.1.3: **GDP Contributions - Supply side (2009-2013)**



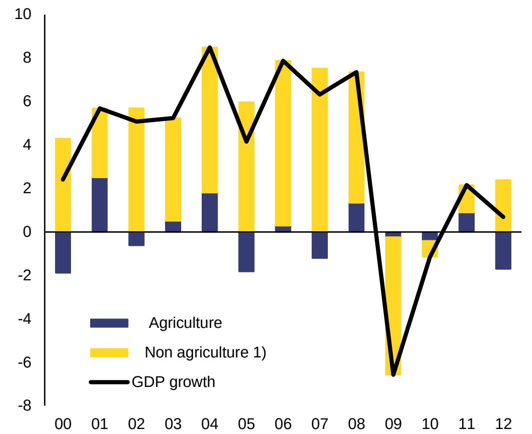
Source: Eurostat

This year's outstanding agriculture harvest ([9]) has already shown up in the Q2 outcome. In Q2 2013, gross value added (GVA) in agriculture already increased by 17.7% (y-o-y) / 4.8% (q-o-q). Moreover, the harvest's impact on GDP can be significant and most analysts expect at least the same values as observed in 2011. Graph I.1.4 illustrates the relatively high impact of the agricultural output on annual real GDP growth despite its low share in the total GDP (ranging between 7-9% of GDP over the last 5 years).

Quarterly growth is expected to accelerate in H2 2013. This is projected to be mainly thanks to a significant impact of the very good agricultural output (expected especially in Q3 2013) and an improving external demand (assuming that the recent positive developments observed in Q2 2013 for the EU were to continue).

During the July negotiation mission, the GDP growth forecast for 2013 has already been revised upwards from 1.6% (in the Commission's spring forecast) to 1.9% with growth being mainly driven by (net) exports and very little support from domestic demand.

Graph I.1.4: **Agriculture contribution to growth**



(1) Net taxes on products are included in the non-agriculture contribution
Source: Eurostat and own calculations

Risks to growth appear more balanced in 2013. Upside risks include a more favourable agricultural output and a higher-than-expected absorption of EU funds. Downside risks stem mainly from a stronger-than-expected deceleration of domestic credit and a sudden worsening of the external environment.

The baseline scenario envisages a gradual recovery in 2014 and 2015 as product and labour market reforms start paying off and the external environment improves.

Real GDP growth is expected to be around 2.2% in 2014. Domestic demand is forecast to be the main driver of growth, as investment regains momentum (supported by a better absorption of EU funds) and private consumption is set to return to positive territory in 2014. Although the external environment is expected to improve and thus to support continued exports growth, net exports are forecast to have a small negative contribution, as imports are also projected to pick up in 2014.

The recovery is expected to continue in 2015 with GDP forecasted to grow by about 2½% in

([8]) The industry GVA has a share of about 30% of the Romanian GDP.

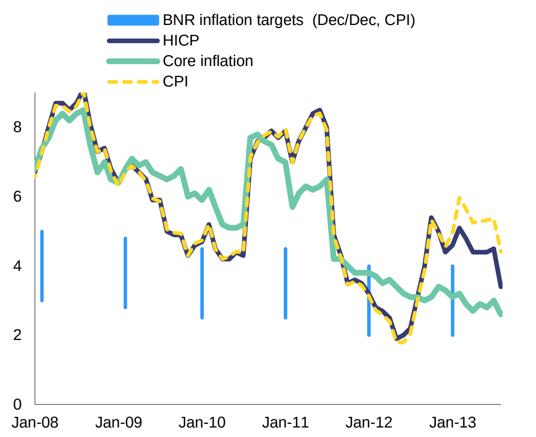
([9]) The Romanian agriculture minister, Mr Constantin, declared that "The figures we have indicate that this year will witness the biggest output of wheat and rye of the past eight years, at 7.3 million tonnes […]. The output is also second largest of the past 43 years." (Agerpres, 9 August 2013)

real terms, slightly above potential. Similarly to 2014, domestic demand is assumed to remain the principal growth driver in 2015 while net exports are forecast to have a negative contribution to growth. As investment picks up and the labour market recovers, the negative output gap is expected to continue to slowly shrink in 2015.

1.2. INFLATION

Although inflation in Romania remained one of the highest in the EU in the first half of 2013, it declined during the summer to reach 2.6% in August 2013 (Graph I.1.5**).** After peaking in January at 5.1% (HICP, y-o-y) due to volatile food prices and hikes in administered prices, inflation come down more than expected and reached 2.6% in August. A sharp drop in food prices (in particular of volatile items such as fruits and vegetables) has been the main reason for this drop in inflation (Graph I.1.6). Although energy price increases (following the roadmaps) put additional pressures on inflation this year, so far, the price liberalisation effect has been lower than originally expected.

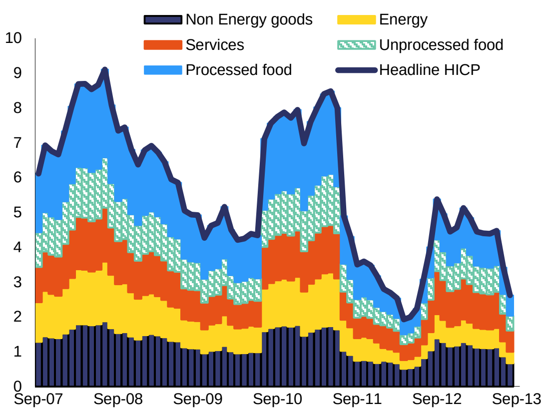
Graph I.1.5: **Inflation (y-o-y)**



Source: Eurostat and NBR

Inflationary pressures are diminishing in H2 2013 and therefore inflation is expected to be within the central bank's target band at end-2013. The disinflationary path from the second half of the year can be attributed to weak domestic consumption, benign wage dynamics, a very good harvest (the adverse base effect will also vanish in H2 2013), and the reduction in VAT from 24% to 9% for bread and other bakery products. Annual average inflation is estimated to be around 4% in 2013, with the y-o-y inflation falling below 3.5% in December 2013, thus within the central bank's target range (2.5% ±1pp). A further deceleration is expected in 2014.

Graph I.1.6: **HICP headline and contributions**

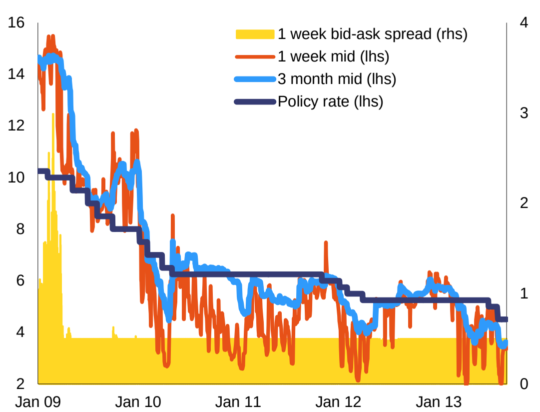


Source: Eurostat

2. MONETARY POLICY AND FOREIGN EXCHANGE DEVELOPMENTS

The central bank accelerated its monetary easing cycle by lowering its key policy rate by 50 bps to 4.50% in August, following a 25 bps cut in July (Graph I.2.1**).** The decision was taken as the National Bank of Romania (NBR) expects inflation to moderate in the second half of 2013 and to fall into the 2½% ±1pp target range by September/October 2013 and to remain within the range thereafter. The NBR indicated that the current outlook enables a gradual easing of the monetary policy stance given the still large output gap, the slow economic recovery and negative credit growth, while anchoring inflation expectations. In spring 2013, the NBR narrowed the interest-rate corridor around the policy rate from ±4 percent to ±3 percent in order to moderate interest rate volatility on the interbank money market and to consolidate the transmission of the policy rate signal. Before, the NBR had kept the key rate unchanged for more than a year as inflation moved above the NBR's target range in autumn 2012. Previously it had lowered its key rate by a total 100 basis points to 5.25% between November 2011 and April 2012. Firmly anchoring inflation expectations remains important, especially since the NBR has reduced its inflation target band for end-2013 to 2½% ±1pp and this will become a continuous target from 2014 onwards. The NBR

Graph I.2.1: **Policy and Interbank rates**

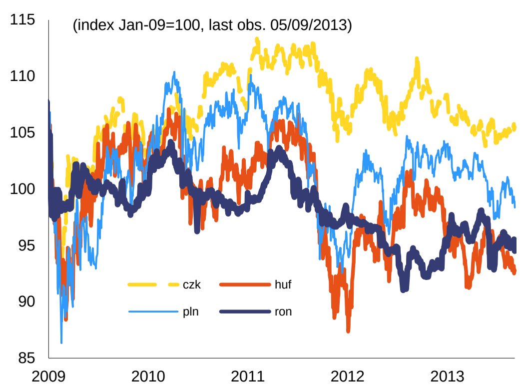


Source: Bloomberg

decided to maintain existing reserve requirements for foreign (20%) and domestic (15%) currency-denominated liabilities of credit institutions.

Liquidity conditions in the interbank market have improved substantially in the first half of 2013. The NBR started the monetary policy easing cycle in March by easing the control over liquidity conditions in the money market, which helped interbank interest rates to decrease. It also removed a cap on the weekly repo refinancing operations introduced in the second half of 2012. Recent abundant liquidity also led to interbank rates moving below the NBR's key policy rate. Over the medium term, strengthening of the interest-rate channel of monetary transmission remains an important challenge for monetary policy, particularly in view of the highly volatile interbank market and persistently weak lei-denominated credit activity.

Graph I.2.2: **NMS floaters - Exchange rate to the euro**



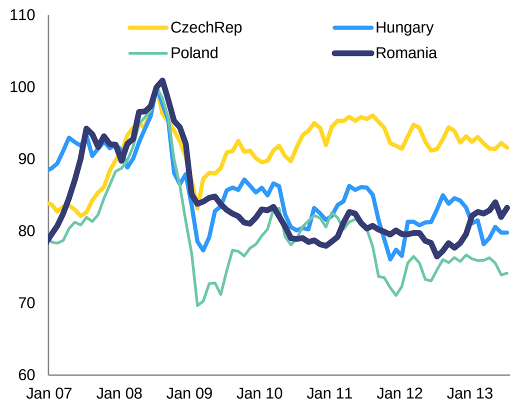
Note: an increase indicates an appreciation of the currency against the euro

Source: Bloomberg

The implementation of monetary policy remains challenging, due to volatile price developments and recurrent swings in global risk sentiment, although short-term price pressures eased significantly. Currently underlying inflationary pressures appear low and as the adverse base effect vanishes, inflation should decrease rapidly in the second half of 2013. Given the weak economy (and still negative output gap), wage pressures are likely to remain subdued and recent increases in the minimum wage (since 1 July 800 lei or about 180 euro) are not likely to have substantial effects on inflation. Taking into account recent developments, annual inflation could average below 4.3% in 2013, falling to below 3.5% by end-2013, within the NBR's target range (2.5% ±1pp) and decelerating further to 3.1% in 2014. Monetary policy should remain prudent going forward while closely monitoring inflation developments.

Within the managed floating regime, the leu has shown some volatility in recent months, however remaining overall relatively stable compared to regional peers. The leu's exchange rate to the euro strengthened somewhat in the first months of 2013, showed some weakening in June following changing market sentiment towards emerging markets, but then gained again since end-June and remained relatively stable thereafter (Graph I.2.2). The real effective exchange rate, calculated using unit labour costs (ULC), weakened by some 15% since the beginning of the financial crisis in 2008 (Graph I.2.3).

Graph I.2.3: **NMS - REER (ULC deflated)**



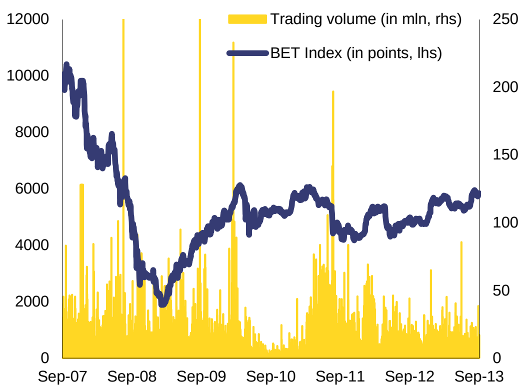
Index Jul-08 = 100
Source: Bloomberg

3. FINANCIAL MARKETS AND BANKING SECTOR DEVELOPMENTS

3.1. FINANCIAL MARKETS

Financial market conditions have significantly improved since the summer of 2012 amid a pick-up in global market sentiment, and following the stabilisation of the domestic political situation towards year-end, moving broadly in tandem with the regional peers and remained relatively favourable in the first half of 2013. The 5-year CDS sovereign spreads for Romania dropped, after reaching nearly 500 basis points in May 2012, to below 200 bps in early January 2013, and hovered slightly above 200 bps since end-June. The BET stock market index recovered after substantial losses in May 2012 until end-2012; it has been volatile thereafter and gained around 10% over 2013 until early-September (Graph I.3.1).

Graph I.3.1: **Stock market evolution**



Source: Bloomberg

3.2. BANKING SECTOR DEVELOPMENTS

Banking sector capitalisation has remained at reassuring levels notwithstanding the upward trend in the share of impaired assets. Despite mounting pressures on asset quality, capital adequacy at system level has remained flat since end-December 2011 and has hovered around 14.5% (14.7% by end-June 2013; Table I.3.1).

Previous expectations regarding a possible levelling-off of non-performing loans at the end of 2012 or the first months of 2013 have not materialised. Non-performing loans (90 days overdue) have continued to increase and slightly passed the 20% threshold by end-June 2013. However, the risks associated with the still on-going increase in non-performing loans have continued to be mitigated by the prudent loan-loss provisioning policy of the banking supervisor. In accounting terms, loan-loss provisions stood at 62.8% by end-June 2013, whereas in prudential terms (i.e. with prudential filters) they reached 88.3% during the same period. But the increase in

Table I.3.1: **Banking sector - Financial soundness indicators**

(%)	07	08	09	10	11	12	Mar.12	Jun.12	12Q3	12Q4	13Q1	13Q2
Capital Adequacy												
Capital Adequacy Ratio	13.8	13.8	14.7	15.0	14.9	14.9	14.6	14.7	14.7	14.9	15.0	14.7
Leverage Ratio	7.3	8.1	7.6	8.1	8.1	8.0	8.6	8.4	8.3	8.0	8.2	8.0
Ratio of level 1 own funds to credit risk exposure	10.7	11.8	13.4	14.2	14.3	16.6	16.5	16.4	16.2	16.6	16.7	16.4
Asset quality												
NPL's (90 days overdue)	-	2.8	7.9	11.9	14.3	18.2	15.9	16.8	17.3	18.2	19.1	20.3
NPL's (60 days overdue)	4.0	6.5	15.3	20.8	23.3	29.9	25.6	26.1	26.8	29.9	30.0	30.5
Profitability												
Return on assets (after tax)	1.0	1.6	0.3	-0.2	-0.2	-0.6	0.1	-0.1	0.0	-0.6	0.6	0.7
Return on equity (after tax)	9.4	17.0	2.9	-1.7	-2.6	-5.9	1.3	-1.0	-0.3	-5.9	5.1	6.0
Liquidity												
Immediate liquidity	38.7	34.4	35.3	37.8	37.2	35.9	37.5	35.4	35.6	35.9	37.6	37.8

Source: NBR

loan-loss provisions has continued to put strain on banking sector profitability. Nevertheless, after the losses registered in 2012, the banking sector returned to profitability in the first half of 2013 (the return on equity stood at 6% by end-June 2013).

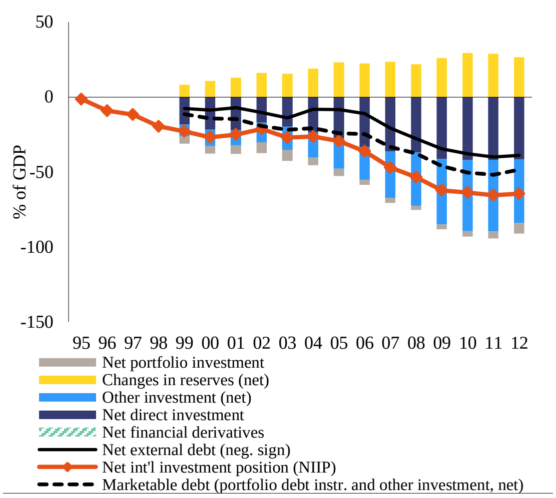
The NBR has continued to closely oversee the banks with parents from peripheral euro area countries. The banks with Greek and Cypriot capital, which still make up for an important share (about 14%) of the total banking sector assets, have managed to maintain sufficient capital buffers, but the still increasing loan-loss provisions are weighing on their profitability. The local deposit base of these banks has also become more stable in recent months following some volatility during the peak of the Cypriot crisis in April 2013. The spill-overs from this crisis to the banks with Cypriot capital operating on the Romanian market were mitigated through the agreement to transfer the local deposit base of the Romanian branch of Bank of Cyprus to Marfin Bank, the subsidiary of Laiki Group. Currently, a buyer is sought for Marfin, but not much progress has been achieved so far.

In line with regional developments, the deleveraging process of foreign banks and the reduction in parent bank funding continue to constitute an issue of concern. While the deleveraging process has been orderly so far, it continued throughout the first half of 2013, *inter alia*, due to the reduction in the exposure of foreign banks to Romania. The nine euro area parent banks which committed to maintain their exposure to Romania during the first phase of the European Bank Co-ordination "Vienna" Initiative have further reduced their exposure to Romania. The combined exposure of these nine banks to Romania stood at roughly 86% of the March 2009 benchmark level at the end of July 2013. Similarly, parent bank funding has also been on a declining path. As of end-August 2013, total parent funding declined by 14.6% compared with end-December 2012 and by roughly 7% compared with the first quarter of 2013.

4. BALANCE OF PAYMENTS

Romania should be able to finance itself during 2013-2015 on the market, barring negative external developments. Developments on the balance of payments front are encouraging. The current-account deficit for 2013 is estimated at around 2% of GDP, a significant improvement over the past two years (4% of GDP) (see Box below). For 2014, a current-account deficit below 2.5% of GDP is projected. Most recent data however hints towards better outcomes. This development reduces the external financing needs of the Romanian economy and will thus, especially in the medium and long run, further improve the sustainability of Romania's external position. At these levels the NIIP, which abstracting from valuation effects is the sum of past current-account deficits, continues on a downward path (Graph I.4.1). Until 31 August 2013, Romania has already repaid IMF credits of 2.6 bn SDR (around 3 bn euros ([10]) and is scheduled to repay another 1.4 bn SDR (around 1.6 bn euros) in the rest of the year. With further repayments to the IMF and the Commission over the programme period, gross international reserves are expected to decline to 29.8 bn euros by the end of 2015, which would still exceed 5 months of imports. The financing of the Romanian balance of payments is on a solid footing; still, risks remain in case of adverse international developments.

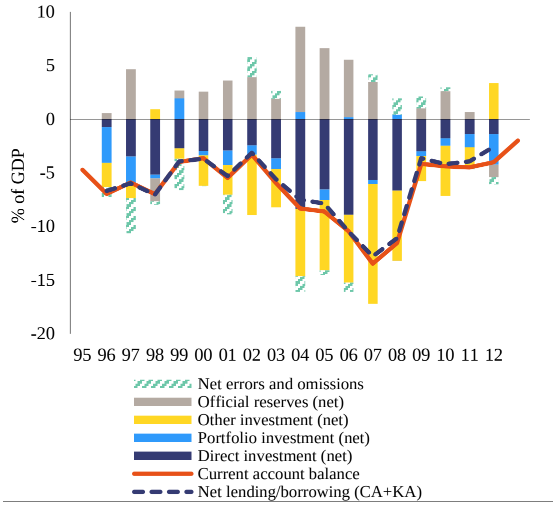
Graph I.4.1: **Decomposition of the NIIP**



Source: Eurostat

Foreign direct investment remains weak and the importance of portfolio investments for the balance of payments increases. In 2013 H1, FDI inflows were 577 m euros, down from 776 m euros in 2012 H1. These are particularly low if pre-crisis levels are taken into account. In 2007, FDI inflows amounted to 7 bn euros. A more stable macroeconomic environment should help attract more FDI in the future. For 2013, initial public offerings (IPO) are expected for instance for Romgaz (15%) and Nuclearelectrica (10%) which will probably attract foreign capital. Portfolio investments have increased threefold, from 1.0 bn euros for 2013 H1, to 3.7 bn euros in 2012 H1, due to stronger use of lei-denominated bonds. This marks an important shift in Romania's external financing (Graph I.4.2) and shows stronger interest from international financial markets. At the same time, as portfolio investments tend to be relatively volatile, this increases the vulnerability of the financing of the Romanian balance of payments to external developments. This holds true, especially in face of an unfavourable net international investment position (NIIP), which stood at 64.5% of GDP end 2012. Also, a correction of the loose global monetary policy stance might contribute to a reduction in capital inflows into emerging markets, including into Romania.

Graph I.4.2: **Current account financing**



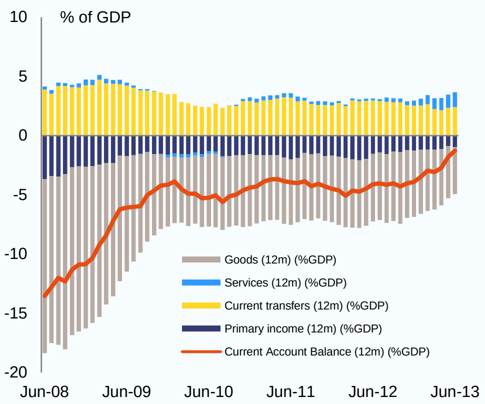
Source: Eurostat, Commission projection for CA 2013

([10]) Exchange rate of 30 August: 1 SDR= 1.14 EUR

Box I.4.1: Recent improvements of the current account balance

The current account has significantly improved over the past year. In the first half of 2013, the current account has turned positive with a surplus of 3.1 bn lei (circa 0.5% of projected annual GDP). For 2013 as a whole, a current-account deficit of around 2% of GDP is forecasted. The improvement was continuous over the past six months. Graph 1 illustrates the speed of the adjustment, which is comparable to the adjustment after the financial crisis. The average current-account deficit over the past 36 months (07/2010-06/2013) now stands at 3% of GDP. Table 1 shows the contributing factors comparing 2012 H1 data with 2013 H1. While primary income improved, this was counterbalanced by a deterioration in current transfers. The main part of the adjustment was due to the better trade balance; it contributed to an improvement of 5.7% of GDP over the first six months of the year and is now nearly balanced. Trade in goods contributed to an improvement of 3.7% of GDP, whereas trade in services contributed 1.9% of GDP in the first half of 2013.

Graph 1: **Current account decomposition**



Source: NBR balance of payment data, Eurostat

Foreign trade shows stronger exports and slightly weaker imports. Recent data on the trade of goods show that exports of goods have grown by 6.1%, whereas imports have decreased by 2.6% in 2013 H1 compared to 2012 H1. Export growth is mainly driven by cars, machinery and other manufactured articles. Weaker imports are linked to low levels of consumption and lower levels of energy and petroleum imports thanks to mild weather. The trade deficit for mineral fuels and related categories has nearly halved from 9.6 bn lei in 2012 H1 to 5.0 bn lei in 2013 H1. This accounts for 45% of the improvement in the trade in goods. Trade diversification still remains limited with dependence on cars (e.g. Dacia, Ford) rising and dependence on the EU as main export partner only slowly abating. As the number of car producers with significant operations increases, however, one could expect some intra industry diversification along different price categories.

Table 1:
Contributions to current account improvements (first 6m, %GDP)

	CA balance	goods	services	income	transfers	trade balance
2012 H1	-4.9	-6.1	0.0	-2.2	3.5	-6.2
2013 H1	1.1	-2.4	1.9	-1.5	3.1	-0.5
change	6.0	3.7	1.9	0.7	-0.4	5.7

Source: NBR balance of payment data, Eurostat

The improvement of the current account seems sustainable but downside risks remain. Recent improvements occurred despite weak economic development in the Eurozone and the EU, which are Romania's most important trading partners, accounting for 70% of goods exports in 2012. Also, the exchange rate has remained stable, not providing an additional boost to exports. Still, with consumption being sluggish in the first half of 2013 though, some downwards pressure on the trade balance might materialize once consumption picks up again. Moreover, the mild winter weather in early 2013 provided a considerable one-off improvement of the trade balance. The geographical and functional diversification of exports points towards slightly improved resilience against sector or country specific external shocks.

Part II

Policy implications and conditionalities

1. FISCAL POLICY

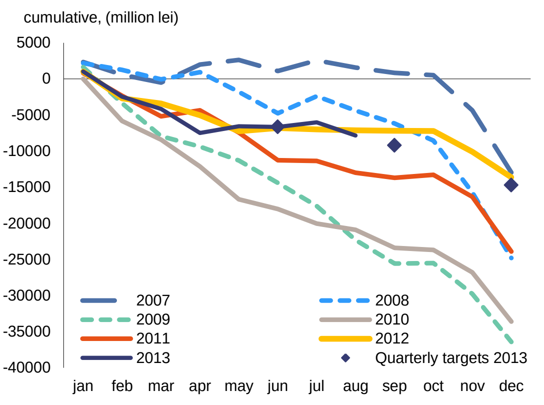
1.1. FISCAL CONSOLIDATION

Following Romania's exit from the EDP in 2013, a new programme would support the government's further fiscal consolidation efforts, with a view to reaching the MTO (medium-term objective) of a structural budget deficit of 1% of GDP by 2015, in line with the fiscal country-specific recommendation (CSR). Romania exited the EDP in June 2013, based on a budget deficit outcome of 2.9% in 2012 in ESA terms and on the Commission's Spring Forecast showing further consolidation over the forecast horizon. The authorities committed to stick to the previous programme's deficit target of 2.4% in ESA terms for 2013 and 2% of GDP in 2014, in line with the SGP requirements of a structural fiscal effort of at least 0.5% of GDP and consistent with the plans outlined in Romania's 2013 convergence programme. The 2.4% of GDP ESA target for 2013 corresponds to a cash deficit target of 2.3% of GDP, which is the sum of the previous cash deficit of 2.1% of GDP and an off-budget expenditure programme worth 0.2% of GDP (PNDI – National Programme of Development and Investments) which was stopped and folded in the budget. The 2% of GDP ESA target for 2014 corresponds to a cash target of 2%. The mission and the authorities worked on the mid-year budget adjustment and discussed briefly the plans for the 2014 budget, which will be detailed during the next mission (end October-beginning of November).

The end-June cash deficit of 1.1% of GDP was in line with projections, but the revenue underperformance requires increased vigilance on the authorities' side. Most of the revenue underperformance in the first 6 months stemmed from lower-than-expected corporate profit tax (mainly due to bank losses in 2012) and from lower-than-expected VAT (likely due to the less tax-rich growth, as imports were declining and VAT exports refunds were on the rise). This was offset by lower expenditure in social transfers and lower spending on corrections related to EU Funds.

The authorities and the mission agreed on the revised 2013 budget, which continues to target a deficit of 2.3% in cash terms (corresponding to a 2.4% ESA target). The revised budget caters for lower revenues and adjusts expenditure downwards in domestic capital investments, provisions for corrections related with EU Funds and transfers to other public administration units. Spending on EU Funds was below projections overall, with expenditure for co-financing being in line with projections and reimbursable and contingency([11]) expenses being below projections.

Graph II.1.1: **General government surplus/deficit**



Source: Romanian authorities, European Commission

The government also enacted a cut in the VAT rate for bread and its production chain from 24% to 9%. The revenue loss from this measure will be offset by increasing the excise rate for alcohol and some luxury goods. Data received after the mission (end-August data) also showed weak revenues, which the authorities mostly attribute to the recent reorganization of its tax administration (ANAF). Given concerns that this might not be temporary, the authorities formally re-affirmed their commitment to take any measures necessary to meet the annual target, should revenues underperform also in September.

The revised budget supports a possible future improvement in absorption of EU funds. The programme allows for an adjustor of 0.6 billion lei for co-financing: in case the resources (about 7 billion lei for the year) set aside in the budget for co-financing EU projects are exhausted, the authorities can spend an extra 0.6 billion lei to

([11]) Amounts set aside for non-eligible expenditure and for possible corrections.

support absorption. Additionally, possibilities to pre-finance EU projects for Structural and Cohesion funds, given lags in reimbursement, were enlarged: the quarterly net lending ceiling was doubled to 3 billion lei.

The 2014 budget targets an ESA deficit of 2% of GDP. The authorities are looking into ways to increase revenues, mainly via base broadening. While detailed projections will be done in the Oct/Nov review mission, various options for increased revenues were discussed. In the context of the need to increase funding to support the healthcare sector reform recommended to Romania in the CSRs, the authorities will consider broadening the base for social contributions. A first step in this direction is being taken by end-September with the approval of legislation to apply health contributions on the rental income of individuals as of the beginning of 2014. By end-2013, the authorities should present a study detailing the policy options for a more comprehensive review of labour taxation, which also aims to reduce the tax burden for low and middle-income earners in a budget neutral manner. The authorities are preparing, with technical assistance from the IMF, a revision of the property tax base by end-2013.

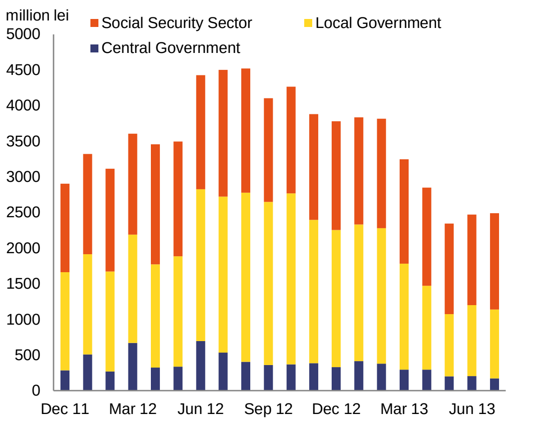
On the expenditure side, one challenge for the 2014 budget is the implementation of the Unified Wage Law. The move to the wage grid set-up by the law has to be done gradually, within the available budgetary envelope and without prejudice to the principles of the law. With the 1-in-7 staffing rule now removed and with a 1-in-1 rule in place, the authorities also need to determine the optimal level of employment for the public sector; they committed to develop staffing plans for each Ministry, also drawing on results of the World Bank's functional reviews, and a staffing methodology for local governments.

1.2. FISCAL GOVERNANCE

With the main part of the fiscal consolidation having been achieved, the focus will shift to improving fiscal governance.

Arrears have to be maintained at a constant low level and their causes have to be tackled through more structural measures. Arrears (90-360 days) will have to be maintained below the thresholds of the last programme (below 300 million lei for local government arrears and below 20 million lei for central government arrears). End-July data shows that while the local government arrears target is met([12]), the central government arrears are slightly above target, although remaining on a decreasing trend. Figures for overdue payments (0-360 days) show a rather constant evolution in July, but compared to end-May, spending pressures still seem to accumulate at the local government level (see Graph II.1.2).

Graph II.1.2: **Stock of general government overdue payments (0-360 days)**



(1)Data starting January 2013 excludes "disputable arrears" worth 360 million lei.
Source: Romanian authorities, European Commission

The new programme focuses more on tackling the underlying causes of arrears accumulation. In the short-term, given the liquidity problems of local governments, the Finance Ministry will consider a scheme to compensate overdue bills and tax arrears, while putting the beneficiary local units under more intense monitoring, to prevent moral hazard. At the same time, the government will publish quarterly reports on arrears for each local unit, to increase transparency. As to the medium-term, work towards the finalization of the commitment control system is underway. An important milestone in this respect is the pilot roll-

([12]) The target is met with the proviso that at the end of the previous programme, "disputable arrears" worth 360 million lei were removed from the standard data series. The Court of Accounts should shed some light into the status of these possible disputes. The authorities undertook to present the audit schedule, as well as quarterly progress reports for the audit of the "disputable arrears".

out of the IT application in January 2014 for a central and a local government unit. The government passed an ordinance in September which defines commitments to be included in the system.

Prioritization of investments and the alignment of capital spending with multi-annual budget planning are key priorities. As first steps, the authorities are working on the staffing of the Public Investment Monitoring Unit set up within the finance ministry during the previous programme. In September, the authorities also approved legislation which defines the criteria for prioritization. The government undertook to approve a list of prioritized investments by the next review mission, to serve as a basis for the preparation of the 2014 budget. Moving further, the role of the unit in vetting public investment projects financed at the central administration level (including projects co-financed with local administration) should be consolidated. The unit will also further develop its database with a view to preparing and publishing a list of budgeted investment projects together with their rolling three-year budget allocations. This should increase predictability as well as improve medium-term budgeting for capital investments. With a view to making the best use of various financing options for investments, the authorities also agreed to carefully analyze the eligibility of investment projects for EU funds and to increase their capacity of analyzing risks related with Public-Private-Partnerships (PPP) before embarking on developing PPP projects.

The new programme seeks to strengthen fiscal governance and institutions. The implementation of the Fiscal Compact by end-2013 is an opportunity to update the fiscal governance framework put in place in 2010 during the first BoP programme: the Fiscal Responsibility Law has to be updated, the role of the Fiscal Council should be strengthened and a structural budget balance rule together with an automatic correction mechanism should be introduced. Beyond the changes required by the Fiscal Compact, conditionality also foresees targeted improvements in the existing framework: improvements in the content of the Fiscal Strategy, increased transparency regarding budget assumptions, a stronger role for the Fiscal Council in anchoring fiscal policy in Romania by publishing their own revenue forecast at the start of the budgeting process as well as improved capacity at the Finance Ministry to assess the fiscal impact of legislative proposals, including the possible structural fiscal impact.

1.3. TAX ADMINISTRATION

Tax efficiency indicators suggest that improving tax collection remains a challenge for Romania.([13]) The cost of tax compliance can be reduced through e.g. pre-filled tax returns using third-party information and electronic services, which would translate in a reduction in non-compliance.

The implementation of a comprehensive tax compliance strategy will start as of September 2013 and should gradually lead to improved tax collection through a reform of the tax administration (ANAF). The reform, deemed necessary by the fiscal-related CSR, will be supported by a 5-year World Bank project. The reform includes the definition of a services catalogue for the taxpayers by July 2014, the improvement of the VAT reimbursement procedure by reviewing the criteria for ex-ante control, the increased use of e-filing for companies' tax returns and the improvement of filing compliance by mid-2015.

Prevention, inspection and fraud combat are to be reinforced. The current 221 tax offices of ANAF will be grouped into eight regional directorates by September 2013 and will be consolidated into 47 local tax offices by 2015. Around 1,700 staff members are to be reallocated, mostly from support functions to prevention and inspection, and to strengthen resources in the Bucharest Region to combat fraud. ANAF would also take over the responsibilities and 1,100 staff of the Financial Guard, which will be abolished. The new positions will be directed to the units focused on prevention, fighting tax evasion and tax customs fraud and will be filled following strict selection procedures.

Voluntary compliance is improving, following the High Net-Wealth Individual taxpayers (HNWI) initiative. The programme has been

([13]) Commission, 2013. Tax reforms in EU member states.

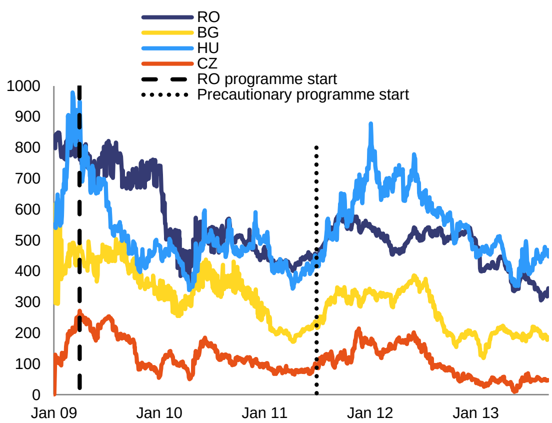
published on the website of ANAF and notification letters on the risks of non-filing foreign income have been sent to 360 individuals. Simultaneously the personal income tax audits have been refined. The development of a "one stop shop" for taxpayer services on ANAF's website by 30 June 2014 is expected to increase voluntary compliance further.

2. GOVERNMENT FINANCIAL SITUATION

2.1. SOVEREIGN MARKET DEVELOPMENTS

Against the backdrop of a respite in the European sovereign debt crisis and of a general rally on financial markets, financing conditions in Romania have eased markedly. The economic performance of the country, in particular on the fiscal side with the abrogation of the EDP and the implementation of numerous structural reforms during the second BoP programme, along with the inclusion of the country in JP Morgan's emerging market index have helped foster investor sentiment. These positive developments are reflected in the CDS 10-year spread with the Bund reaching its lowest level since 2010 (Graph II.2.1).

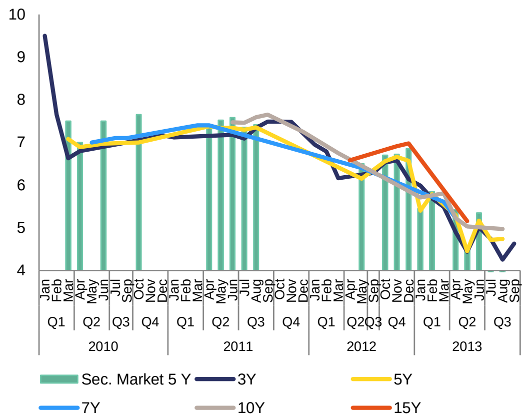
Graph II.2.1: **Romania - 10-year bond spread vs. Bund**



Source: Ecowin, European Commission.

Recent auctions of government securities on the domestic and external markets have attracted more foreign investors and show a significant improvement of financing conditions with e.g. average yields for 10Y paper at record lows of 5% (Graph II.2.2).

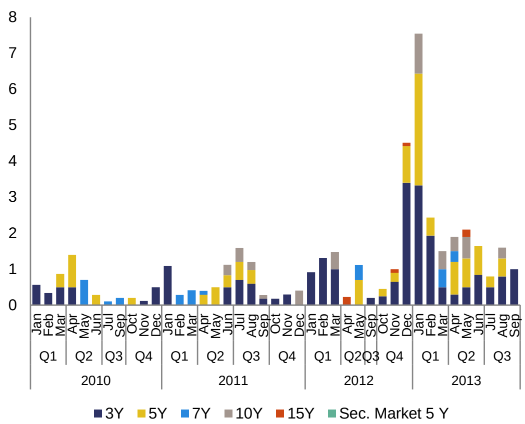
Graph II.2.2: **Romania – Average yields of medium and long-term bond auctions, %**



Source: Bloomberg, European Commission.

The volume of issuances in 2013 has also been larger than in previous years (Graph II.2.3), allowing the Treasury to secure financing early in the year (45% of funding needs raised by end-April). Romania also accessed international markets, raising 1.5 billion US dollars of 10-year bonds in February 2013, with a 4.5% yield (below Hungary's) and 1.5 billion euros of 7-year paper in September 2013. The Treasury plans another external issuance in Q4 if market conditions allow, thereby fully covering external redemptions due this year.

Graph II.2.3: **Romania – Amounts sold at auctions, bn lei**



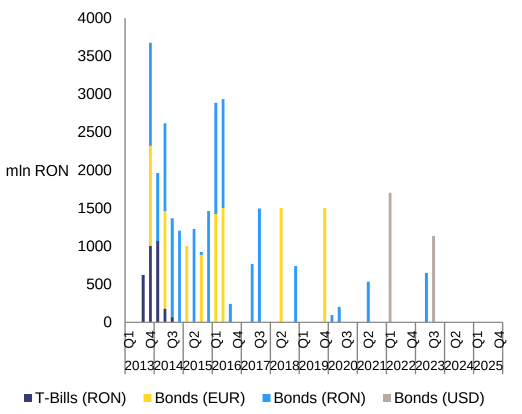
Source: Bloomberg, European Commission.

2.2. FINANCING NEEDS

Financing needs for 2013 amount to 62.2 billion lei of which 14.7 billion lei to finance the deficit and 47.5 billion lei for maturing securities. As of end-September 84% of financing needs had been covered by government securities issuances. In addition to this, repayment of financial assistance amounts to 4.§ billion euros in 2013; out of which the part of the IMF loan repaid by the Ministry of Public Finance is 0.9 bn euros and the part repaid by the National Bank of Romania is 3.7 bn euros.(14) Thanks to successful issuances in foreign exchange and the 1 billion euros DDO-DPL loan granted by the World Bank, funds on the Romanian Treasury cash buffer currently covers roughly 5 months-worth of average financing needs.

For 2014, total financing needs add up to 66 billion lei, with the cash deficit projected at about 13.2 billion lei, sovereign redemption of securities at 33.0 billion lei (based on the government securities active at end-September 2013) and official loan repayments at 4.4 billion euros; out of which the part of the IMF loan repaid by the Ministry of Public Finance is 1.0 bn euros and the part repaid by the National Bank of Romania is 3.4 bn euros.

Graph II.2.4: **Romania - Sovereign Redemptions, mn lei**



Source: Bloomberg, European Commission.

Despite satisfactory market access of the sovereign lately, caution is warranted moving forward as redemptions remain sizeable.

2.3. CURRENT ISSUANCE STRATEGY

The yearly review of the Debt Management Strategy (DMS) has been conducted on time in March 2013 as agreed under the previous programme. In particular, the strategy sets guidelines for managing foreign currency, refinancing and interest rate risks and sets operational benchmarks. Romania's issuance strategy aims at financing the budget deficit and sovereign redemptions, keeping the same shares of domestic and external issuances. Foreign currency debt should be predominantly contracted in euros (at least 70% of forex-denominated debt). The Treasury also pursues the aim of extending average debt maturity to four years.

2.4. STEPPING UP DEBT MANAGEMENT

Notwithstanding the progress made over the last year (notably the inclusion in JP Morgan's and Barclays' indices, better pricing, attraction of new funds), Romania still ranks as a frontier market. To graduate to the Emerging Market class, a number of structural improvements have to be made and have been taken up in the conditionality on debt management (see Annex 6). MoU conditionality thus foresees measures to consolidate the progress achieved under the previous programme (review and update of the Debt Management Strategy) and increase the predictability and market presence of the sovereign (calendar issuances, consultations with market participants). Building up sovereign market infrastructures is another important goal served with the foreseen introduction of an automated platform for primary issuances, an electronic system to monitor secondary market transactions and the involvement of the sovereign in a future central counterparty (CCP), which would enhance the functioning of the domestic financial market. These measures should further improve market efficiency and help the Treasury build up the sovereign yield curve.

(14) Romania is expected to fall below the IMF exceptional access level in November 2013.

2.5. POTENTIAL FINANCING GAP

Given Romania's current sovereign financing situation along with the latest Balance-of-payments developments (see Chapter I.4), no sovereign or external financing gap (see Gross Financing Requirements Table displaying a negative financing gap, Annex 4) should materialise in the next two years under baseline assumptions.

However, Romania remains vulnerable to rapid exchange rate fluctuations, changes in market sentiment and the ensuing capital movements. Likewise, an adverse macroeconomic shock could impede sovereign market access. In this case, a first line of defence would be the funds of the Treasury cash buffer (about 5-month of financing needs) and to a lesser extent the NBR's reserves. Should Romania experience protracted and acute financing difficulties, the precautionary programme could be activated and the funds available (2 billion euros from the EU disbursable in two instalments and 2 billion euros from the IMF Stand-By Arrangement) would allow to cover sovereign financial and budgetary commitments. A new programme would also provide a reassurance to the financial markets that Romania is committed to pursuing the economic reform agenda already launched under the two previous programmes.

3. FINANCIAL SECTOR

The bank resolution framework, the governance arrangements for the Deposit Guarantee Fund and the NBR contingency planning will be further strengthened during the programme period. The authorities committed to amend the legislation on the setting-up and the operation of the Deposit Guarantee Fund in the Banking System to strengthen the corporate governance of the Deposit Guarantee Fund, in particular the incompatibility provisions for board members and executive directors. In this respect, authorities committed to pay particular attention to the provisions regarding conflicts of interest. Furthermore, authorities will amend by end-2013 the provisions of the banking law on stabilisation measures after consultation with the EC on the interpretation of the new EU state aid rules. Subsequently, the NBR will amend the internal procedures for bridge-banks by end-2013. The NBR will also continue updating its contingency planning on an on-going basis as well as the bank-by-bank contingency plans.

The overhang of non-performing loans requires more forceful action both in terms of monitoring and efforts made by banks to clean their balance sheets. The NBR has committed to continue to closely monitor bank practices to avoid evergreening as well as the assessment of credit risk of restructured loans, so that they remain prudent and in line with good international practices. The NBR will collect supervisory data on restructured loans, including loans to SOEs, on a quarterly basis by end-September 2013. Furthermore, the NBR has committed to perform a comprehensive analysis of the asset quality in the banking sector and to produce a report containing granular information, migration matrixes and vintage analysis of impaired assets in the banking sector by end-October 2013. Moreover, the NBR undertook to perform, by end-December 2013, on-site inspections on a selected sample of 20 large, medium and small sized banks focused on their strategies to deal with impaired assets. These on-site inspections will focus on the following aspects: (i) the adequacy of IT systems to deal with impaired assets; (ii) the NPL work-out strategies currently used by banks; and (iii) the restructuring/ rescheduling policies applied by banks. The analysis of the IT adequacy of banks should be finalised by end-2013. Based on the outcome of this analysis, an action plan for the resolution of NPLs will be agreed in consultation with the EC and IMF. Subsequently, on-site inspections in the remaining banks will take place until end-March 2014. Similar to 2012, to assess the adequacy of loan-loss provisions, the NBR is currently conducting a collateral audit exercise.

Against the backdrop of the still on-going increase in asset impairments, preserving credit discipline contributes significantly towards safeguarding financial stability. In order to avoid threats to financial stability, authorities have committed, under a new programme, to continue to refrain from adopting legislative initiatives (such as the personal insolvency law or proposals for the debt collecting law) with unwarranted impact on credit discipline. Furthermore, authorities have committed to ensure that court cases involving abusive clauses are dealt with by higher ranking courts or by a unique specialised court and will take all other necessary measures to ensure a harmonised application of these provisions, such as training of judges. Moreover, as corporate insolvencies are among the main culprits for the increase in non-performing loans, the NBR, together with the Romanian Banking Association, will explore possibilities for setting up a database of shareholders of companies in insolvency as well as implement more effective data reporting of the Association of Insolvency Practitioners.

Authorities aim at further developing the capital market and diversifying the sources of bank funding. In order to further develop the capital market and diversify the sources of funding for banks, authorities will adopt the amendments to the covered bonds legislation by end-2013. At the same time, authorities will ensure that the adoption of this legislation is coupled with the implementation of appropriate safeguards to preserve financial stability. Furthermore, any possible prolongation of the Prima Casa programme after its foreseen expiry date (end-September 2013) should be restricted to mortgage lending denominated in domestic currency. Apart from removing a bias that induced consumers to assume forex risks, it will help develop a pool of long-term assets denominated in lei and thereby foster covered bonds issuances denominated in domestic currency.

To strengthen the supervision of the non-bank financial market, authorities have committed to further align the legislation on the Financial Supervisory Authority to international good practices. Authorities will amend by end-September 2013 the legislation on the Financial Supervisory Authority (ASF), in particular the provisions regarding the size of the ASF managing board (which should be restricted to maximum nine members), the minimum required professional qualifications of ASF board members, the statutory protection of supervisory staff and of the institution as well as the rules on the avoidance of conflicts of interest, notably any connection of these members with Parliament. Furthermore, in order to create synergies and make the institution fully operational, the ASF will: (i) swiftly complete the integration of the former three supervisory authorities for securities, insurance and pensions while ensuring the smoothing functioning of supervisory activities; (ii) develop a human resources policy geared first and foremost towards qualified staff to perform on-site supervision, off-site analysis, validation of internal models; (iii) ensure an adequate public disclosure of all fees and commissions charged to the supervised entities; and (iv) hire, by September 2013, an independent consultancy company to assess staffing levels and staff. Based on this external assessment, the ASF will develop an action plan to streamline its staff with a view to realising expenditure savings in 2014.

4. STRUCTURAL REFORMS

4.1. ADMINISTRATIVE CAPACITY

The enhancement of the country's public administration is one of the cornerstones of the new programme. This is important since its quality is a fundamental feature of the institutional environment and has, inter alia, a direct impact on Romania's capacity to absorb EU funds (see Annex 3). The need to enhanced public administration is also underlined in the CSRs. With a view to monitoring progress made in this area, the authorities were also invited to report every six months to the EFC/EPC. The first detailed reporting should take place in March 2014.

The authorities agreed to continue to follow up and report on a quarterly basis on the implementation of action plans derived from the findings of the functional reviews. As these reviews were conducted in 2010-2011 (see Box below), the mission agreed with the Romanian authorities' proposal to review and update the current action plans by end-2013. Moreover, it was also agreed to establish, by end-2013, a central delivery unit in line with the already existing World Bank project. This new unit would be located directly under the Prime Minister and should allow improvement of the government-wide policy prioritisation, implementation and coordination including the implementation of the EU Council's country-specific recommendations to Romania.([15])

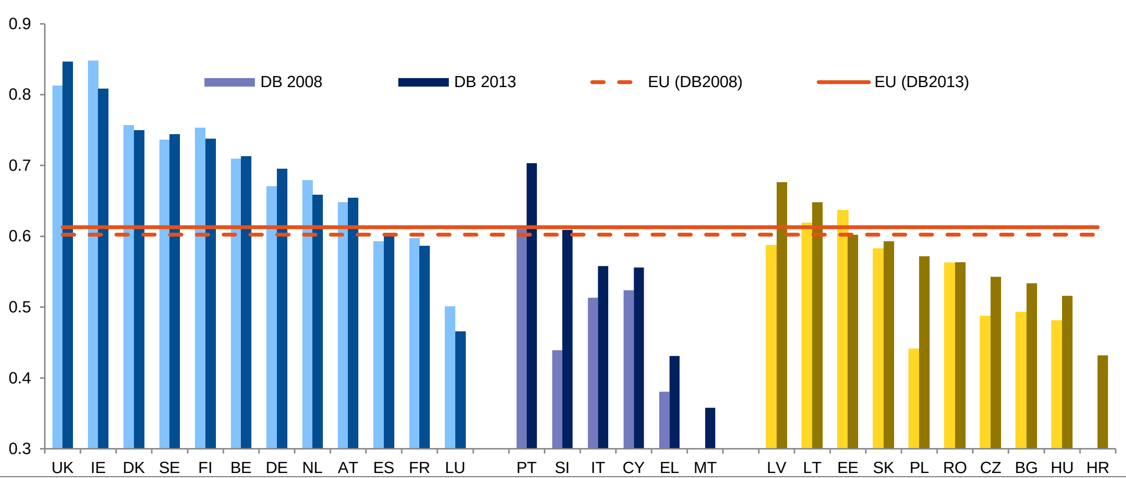
4.2. BUSINESS ENVIRONMENT

Romania's business environment needs to be improved significantly to attract more FDI and to foster the catching up process. According to the World Bank Doing Business report 2013([16]) (Graph II.4.1), Romania ranked 72nd in the global ranking on the ease of doing business. On a scale from 0 (least attractive) to 1 (most attractive) Romania's position (0.56) is below the EU average (0.6). What is even more worrying is that Romania's position has remained unchanged between 2008 and 2013 while positions of almost all other new EU member states have improved. Under a new programme, the authorities will seek to improve the business environment in various ways. They plan to: (i) improve the quality of regulation related to business and reduce administrative burdens for SMEs, (ii) improve access to finance for SMEs and to support SMEs that plan to export; (iii) improve the land registry system; and (iv) make the research environment more attractive for private investment. These measures will help Romania to address the CSRs.

([15]) Council Recommendation 2013 C217/17 of 9 July 2013, OJ NO C217 of 30 July 2013.

([16]) http://www.doingbusiness.org/reports/global-reports/doing-business-2013

Graph II.4.1: **Business environment indicators, WB Doing Business reports**



Source: Commission calculations based on WB data

Box II.4.1: Main weaknesses of the public administration in Romania

The independent functional reviews (FR) requested by the Commission and financed from EU structural and cohesion funds were conducted by the World Bank in 2010-2011 and they were aimed at improving the efficiency and effectiveness of the Romanian public administration. They focused on 12 key sectors (ministries and institutions) of the central public administration.[1]

The sectors and institutions included in these reviews differed in their characteristics, strengths and challenges but there were a number of **common themes** across all, as identified by the World Bank (WB) in the various reports issued over time as briefly described below.[2] Although some efforts have already been made to implement the action plans based on the FR, most of their findings are still relevant today.

Sector and institution governance

1. Lack of oversight and accountability for results and low enforcement of public policies

2. Governance issues in both government institutions and SOEs, and inadequate separation of roles and division of responsibilities among institutions

3. Poor coordination within and across sectors and insufficient inter-ministerial collaboration to manage effectively cross-sector topics (e.g. climate change and energy efficiency)

For instance, the functional reviews reports detailed how the transport and the economy ministries had (and still have) multiple conflicting roles: they set the policy for their sectors, they owned the SOEs, despite the fact that, at the same time, the ministries also bought their services and regulated them. This creates potential conflicts of interest, undermining the effective governance. Moreover, in this context, it is very difficult to determine who is accountable for the decisions taken by these SOEs.

Coordination issues were identified within and across almost all sectors reviewed as part of the FR (e.g. finance, labour, environment, forestry, agriculture, and coordination across EU co-funded projects).

Strategies and decision-making

1. Lack of sector-wide strategies

2. High politicisation of the administration

3. Low quality of, and insufficient usage of, information for decision-making

4. Inadequate policy formulation and insufficient stakeholders' consultation

Sector-wide strategies lacked entirely in some cases, as in the regional development sector, or there were multiple parallel efforts that lacked integration, as with the national reform programme and the national agenda for improving the business environment. These strategies are critically needed to set the direction, and reinforce accountability for results by setting realistic and measurable objectives. Lack of integration between strategic planning and budgeting processes, however, has undermined prioritisation of expenditure. Little progress has been made so far but, for example, a new Public Investment Evaluation Unit is currently being set up within the finance ministry. In the medium term, this should help strengthen quality control in the preparation, prioritisation, appraisal and management of new significant public investment projects.

In some sectors, especially in transport and energy, political appointments to SOEs Boards were still widespread. With the leverage of the financial assistance programmes, the Government has adopted the law on Corporate Governance for SOEs (GEO 109/2011) introducing the OECD principles of corporate governance for SOEs. It tackles important areas such as reporting and monitoring, the role of minority shareholders, or selection of professional management all aiming at increasing transparency and improving the economic situation of public enterprises. Yet, the implementation of this law is lagging behind and political appointments do not seem to have been eradicated.

[1] The 12 FR reports are available here: http://www.sgg.ro/index.php?politici_publice_documente

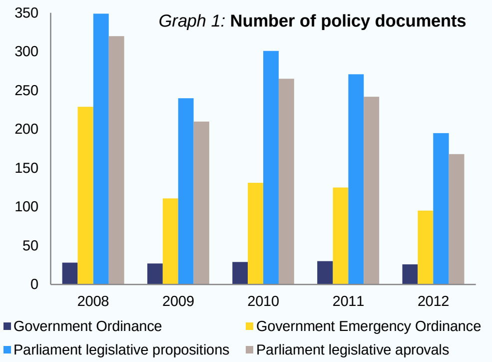
[2] http://www.sgg.ro/docs/File/UPP/doc/rapoarte-finale-bm/etapa-I/09_FR1%20Dalberg.pdf

(Continued on the next page)

Box (continued)

Many policy decisions were, and still are, taken on an ad-hoc basis or they were not sufficiently informed by analysis. An unusual feature of the Romanian system is the frequent use of "emergency" ordinances to override approved parliamentary laws or to implement new laws awaiting parliamentary approval. On a number of occasions, the Cabinet has evoked the lengthy procedures usually applied by the Parliament. Even if otherwise correct, the arguments seem to have been overused.

Graph 1: **Number of policy documents**



Source: General secretariat of the government

Common challenges across the institutions reviewed included inadequate capacity and limited use of the Public Policy Unit (PPU) within several ministries. Therefore, strategic planning processes are suffering. Moreover, although the Romanian legislation makes public consultation mandatory for major legal initiatives, in practice, deadlines for providing feedback are very tight and there is little opportunity for modifying the initial draft proposals.

Investment decisions are taken on an ad-hoc basis, according to the personal agenda of each new minister and without proper multi-annual budgeting. Ingenious schemes – such as the PNDI (National Programme for Infrastructure Development) – are put in place ignoring budget rules and constraints. An essential policy measure under the financial assistance programme was the creation of a database with all investments. While some progress has been made in gathering the information for the database, work is currently underway for setting up the Public Investment Evaluation Unit for effective investments prioritisation.

Organisation

1. Lack of strategic human resource management

2. Organisational structure not aligned with the evolving needs of the sectors

3. Insufficient professional management in SOEs

At the time when the functional reviews were conducted, strategies for the allocation and management of human resources (HR) were lacking in most of the public institutions reviewed. Additionally, in many cases, institutional structures in the sectors were fragmented and not aligned with the needs of the sectors as they evolved.

A more strategic approach for human resources management (HRM) was and still is needed. This included aligning job descriptions with responsibilities, improving monetary and non-monetary incentives and the introduction of elements of performance management. Although, a "Unified Wage Law" was initially adopted in 2010 to tackle some of the issues, it has not yet been fully implemented. For example, a first step forward is underway at the finance ministry which is drafting a five-year HRM strategy note with the WB support to be presented to senior management for review in September 2013.

The importance of recruiting professional managers for some government agencies and SOEs administered by ministries was also underlined in the findings of the reviews. This issue was an on-going conditionality in the two financial support programmes and some progress has already been made with professional managers already recruited for a small number of SOEs[1]. The corporate governance law (GEO 109/2011) requires that professional boards and management be appointed in all SOEs that remain under majority government ownership. Once again, however, the implementation of the law has so far been poor as it has not been properly observed by all companies and, even in those that have applied it, the selection process was not always conducted professionally.

[1] According to "*Fondul Proprietatea*" minority shareholders in many SOEs only 5 professional board and managers (out of 21 SOEs) have been appointed so far.

Inefficient bureaucracy has been identified as one of the major shortcomings in the Romanian business environment. The quality of business regulation should thus be improved while administrative burdens for SMEs should be further reduced. The national 'Better regulation strategy' is to be fully implemented and a common methodology for impact assessments including the 'SME test' is to be developed. Quality control mechanisms are to be established in the selected four ministries. To reduce administrative burdens on the SMEs, as referred to in the CSRs, is envisaged to facilitate property registration and construction permits, notably by: (i) simplifying the procedures, (ii) making electronic submission possible; and (iii) correctly implementing the 'only once' principle of the EU Small Business Act of 2008 that helps ensure that information submitted once to the administration is not requested again by another service.

According to the Global Competitiveness report([17]), access to finance remains one of the most problematic factors for doing business in Romania. Lack of access to finance stops firms from realising their growth potential and might lead to going out of business of structurally sound enterprises. Under the programme, the Mihail Kogălniceanu programme that aims at facilitating SMEs' access to credit, as recommended by the Council, by subsidising interest rates for a limited number of applicants and also provides partial bank loan guarantees would be extended from its current one-year format to a multi-year scheme. The authorities also committed to review the functioning of the National Loan Guarantee Fund for SMEs that is managed by the finance ministry to improve the currently very low take-up of the scheme. To increase the transparency of the bank lending conditions, the finance ministry and economy ministry, in cooperation with the Romanian banking association, committed to introduce a requirement for minimum transparency standards to be published by banks by mid-2014. Finally, to make the best use of EU funds, the authorities committed to further explore options related to equity financing for SMEs with a certain risk sharing between the state and the private sector and to adopt legislation to this purpose.

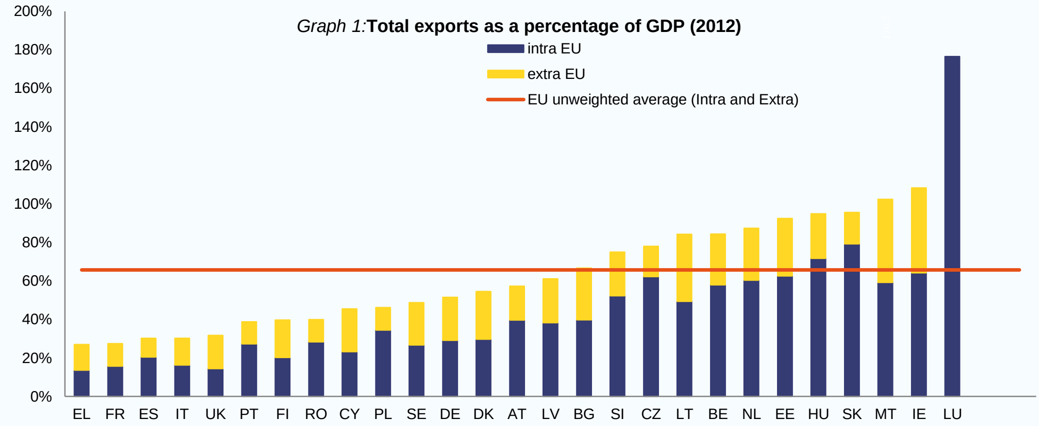
([17]) http://www.weforum.org/reports/global-competitiveness-report-2013-2014

Romania's trade deficits and country's relatively low trade-to-GDP ratio indicate that more can be done to improve the country's export performance. Relatively modest ULC increases (around 5% per year over 2010-12) and a limited change in the real effective exchange rate (based on HICP deflators) (depreciation by around 2% per year over 2010-12), suggest that cost competitiveness is not the main hurdle for Romanian exports. Interestingly, the technology content of Romanian exports also seems to be relatively high and improving (see Box II.4.2). Thus, Romanian exports seem to be held back by other non-cost competitiveness factors, such as poor knowledge of market opportunities abroad and a lack of participation in international business networks. Against this background, it is important to strengthen public services to support SMEs that plan to export. A scheme called 'passport to exports' should be launched by mid-2014, while the network of regional export centres should be established by end 2014. The capacity, including staffing, of the territorial SME offices should be strengthened to be able to assist a larger number of SMEs in order to allow them to make a better use of government services. These activities are expected to facilitate the information flow about market opportunities and procedural requirements for exporting activities and encourage networking among foreign and Romanian companies.

Improved coverage of digitalised land registry should help to strengthen property and land markets. Currently only 15% of the country's land is digitally registered which means that the land and property markets are highly illiquid. This also hampers credit development as land/housing property are often used as collateral for household loans. The authorities committed to speed up the digitalisation of the land registration by simplifying procedures for systematic registrations, strengthening the capacities of the land registry agency with a view to implementing a multi-annual land registration project; and encourage a better use of out-of-court dispute resolutions. Another issue that the authorities agreed to tackle under a new programme would be the undebated inheritance cases. Under the current rules, the number of inheritance transactions is limited due to the high charge associated with such transactions (a notary fee and a transaction tax of 1% of the market value of the property assets that are charged to each heir).

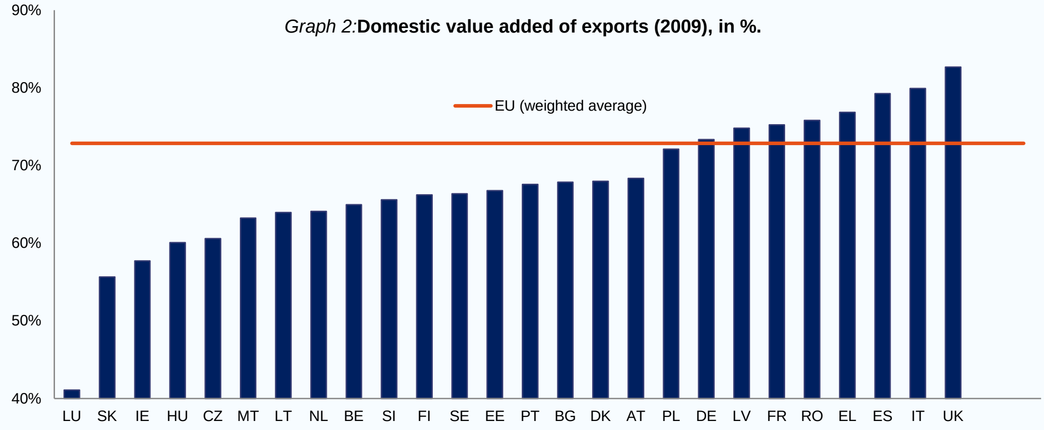
Box II.4.2: **Romania's export performance in EU comparison**

In comparison to similar-sized EU member states, Romania is underperforming in its export performance. On average, exports represent around 40% of GDP in Romania, while the EU (unweighted) average is at around 66% of GDP (see Graph 1). Romania's extra-EU exports are particularly under-developed in comparison to peers: they represent around ¼ of overall exports.



Source: Eurostat, Commission calculations.

For a catching-up economy, such as Romania, a high share of domestic value creation in exports is an indicator that the country is underrepresented in the international division of labour. The domestic value added of Romanian exports is currently above the EU (weighted) average while most of Romania's peer countries (the new EU member states) have much lower values (see Graph 2).



Source: OECD, Commission calculations.

The non-price competitive position of Romanian exports seems to be good. A high share of exports of knowledge-intensive goods and services indicates a shift towards high value-added activities. At around 50% of total exports, the share of knowledge intensive exports in Romania is only somewhat below the EU (weighted) average that stands at around 55% (see Graph 3).

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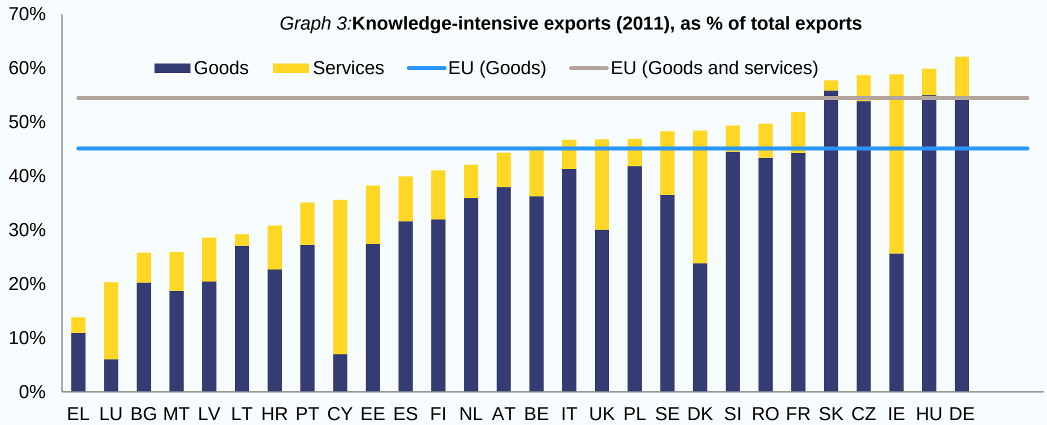
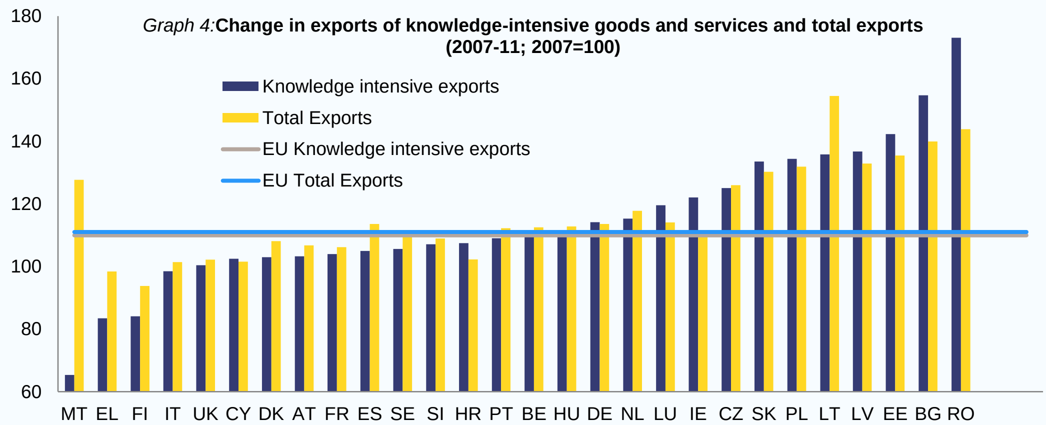
Box (continued)



Note: Services = exports of non-financial knowledge-intensive services, Goods = exports of medium-to-high-tech goods; CY (2010). EU weighted average is used.

Source: UN database, Eurostat, Commission calculations

Over 2007-11, Romania's exports of goods with a high technology content have increased by around 170%, the highest value among the new EU Member States – while total exports increased by around 140% (see Graph 4). While acknowledging that this high increase is also due to a favourable base effect, it still indicates a significant catching up.



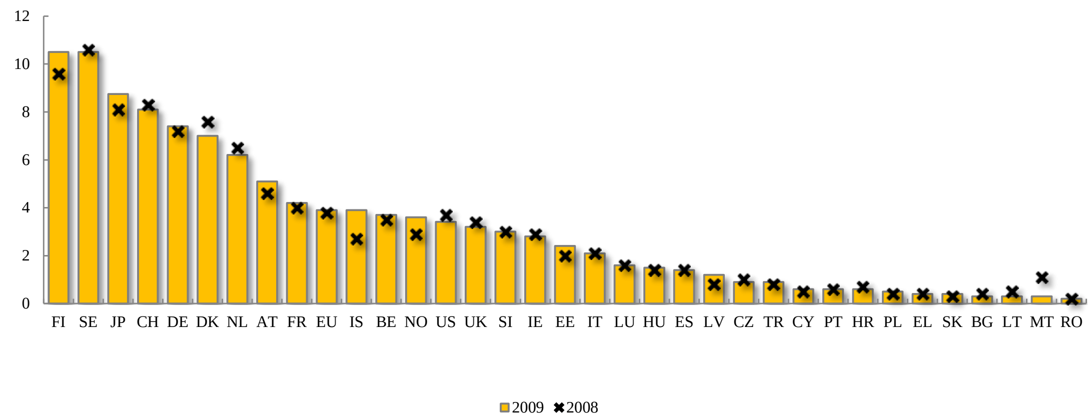
Note: CY data for 2010. EU weighted average is used.

Source: UN database, Eurostat, Commission calculations

This contributes to a highly illiquid property market in which property is often registered on deceased people. Under a new programme authorities should seek to find a solution to kick-start the property market. The current discussions in the government are around having a flat notary fee charged per case (not per heir) and either exempting the payment of the transaction tax or deferring the payment of the tax until the first transaction on the respective assets. These measures should help authorities to reach the target of a 25% digital coverage of the land registry by mid-2015.

In comparison to its peers (new EU member states) Romania is underperforming regarding its innovation activities with the number of international patent applications remaining the

Graph II.4.2: **Number of international (Patent Cooperation Treaty) patent applications per 1 billion GDP, in PPP (2008-9).**



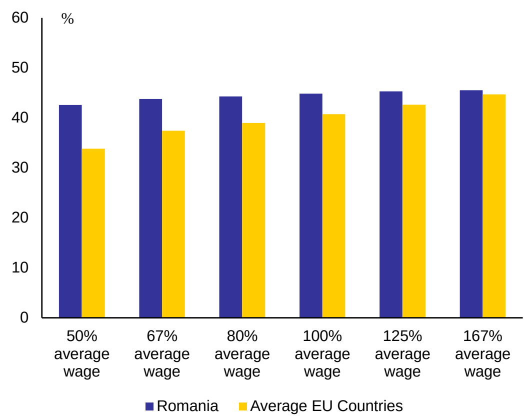
Source: European Patent Office data, Commission calculations, Innovation Union 2013

lowest in the EU (see Graph II.4.2**).** Reforms under the proposed programme aim at attracting more private investment in research and development activities, in line with the country-specific recommendations issued to Romania. The authorities committed to adopt new legislation on inventions to make investments in R&D more attractive for the employers by giving companies more freedom regarding the distribution of benefits arising from the commercial exploitation of employee inventions. At the same time, the authorities have committed to develop guidelines in this regard in line with international best practices so as to create a level playing field for all companies.

4.3. LABOUR MARKET

The tax burden on labour faced by low and middle income earners is high in Romania compared to other EU countries. While tax wedge for a single person is at 34% and 39% of the average wage (for salaries corresponding to 50% and 100% of the average wage, respectively), in Romania it is at 43% and 44% (see Graph II.4.3). It is important to address it so as to increase the incentives to labour participation thanks to higher net incomes for workers and lower labour costs for employers**,** reducing the incentives to work in the shadow economy, in line with the CSRs. To this end, and also taking into consideration that health insurance contributions may have to be revised to ensure adequate funding for the healthcare system (see Section 4.7), the government is expected to submit a study by end-2013 detailing the tax policy reform options to reduce the labour tax wedge for low and middle income earners in a budgetary neutral manner.

Graph II.4.3: **Tax wedge on labour for a single person - different levels of earnings expressed as % of the average wage (2011)**



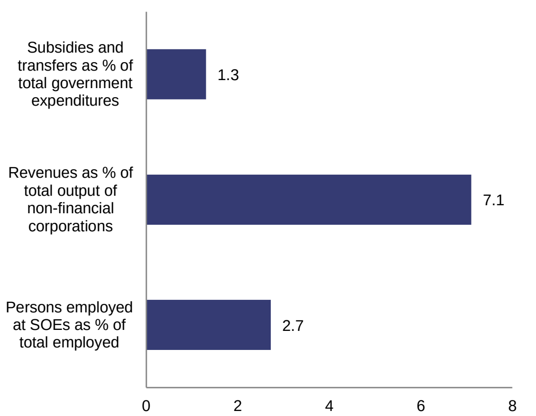
Source: Joint OECD-Commission tax and benefit indicators database

On pensions, the authorities committed to enact legislation to equalise pensionable age for men and women by further raising the pensionable age for women from 63 years in 2030 to 65 years in 2035. The legislative amendments shall be enacted by end-2013, addressing the CSR in this area.

4.4. STATE-OWNED ENTERPRISES

The new programme continues the emphasis on restructuring and sales of stakes in selected state-owned enterprises. State-owned enterprises (SOEs) play an important role in Romania's economy, but their management is suboptimal. Central-government-owned SOEs account for almost 3% of the employed labour force and 7% of annual output (Graph II.4.4). Faced with inefficient SOEs, the government can: (i) take measures to improve their performance; (ii) sell minority or majority stakes in these SOEs, thereby bringing in fresh capital and know-how; or (iii) if the company continues to post losses, close it down. To improve performance, the programme focuses on corporate governance reform, reductions in arrears and operational losses and the sale of stakes in SOEs in the transport and energy sectors. This will help addressing the CSRs.

Graph II.4.4: **Importance of central-government owned SOEs in the Romanian economy**

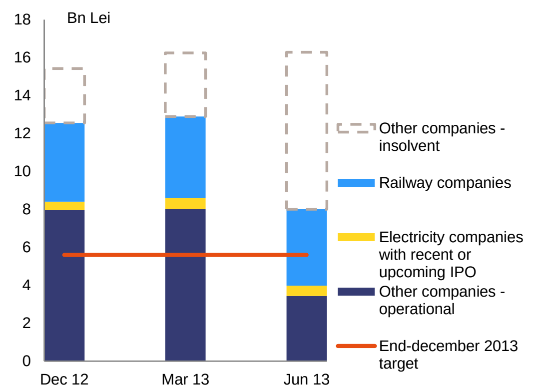


Source: Ministry of Public Finance data

Despite delays, corporate governance reforms are being pursued and professional managers are being brought into key SOEs. The authorities have begun to implement the requirements of the new corporate governance law. A professional Board and CEO have been appointed in a number of large SOEs, although there are indications that political considerations have prevailed over professional ones in a number of cases. Hence, the implementation of the new corporate governance code for state-owned enterprises of 2011 (Emergency Ordinance 109/2011) is not fully satisfactory.

The reduction of arrears of state-owned companies has to be pursued. A quarterly quantitative indicative target on the cumulative arrears of all central-government owned enterprises has been defined in the Technical Memorandum of Understanding (TMU) annexed to the Letter of Intent, bringing the cumulative arrears down from 8.2 billion lei in June 2013 (around 1.3% of GDP) to 3.7 billion lei in June 2014 (about 0.6% of GDP) (See table II.4.1 and graph II.4.5).

Graph II.4.5: **Payments past due date at central-government owned enterprises**



(1) The railway companies are CN Căi Ferate CFR, CFR Călători, CFR Marfă and their respective subsidiaries
(2) The electricity companies with recent or upcoming IPO's are Electrica, Nuclearelectrica, Hidroelectrica, Oltenia and Romgaz
(3) Payments past due date of companies under insolvency on June 30 are excluded from the target. Payments past due date that accumulate while a company is in insolvency will be considered when assessing performance against the payments past due target.
(4) The change between March and June data is driven by CN a Huilei entering insolvency in 2013Q2 with 4.9 bn lei payments past due date
(5) The end-December 2013 target will be adjusted upwards by 1.2 billion lei in the event that the CFR Marfă majority privatization could not be concluded.
Source: Ministry of Public Finance data

Setting a target on the total arrears of all central-government owned enterprises pressures the government and the management of SOEs to restructure their companies. The target can be achieved through a combination of operational improvements, debt/equity swaps with the government and the completion of the majority privatization of CFR Marfă.

Box II.4.3: Privatization of SOEs

SOEs under the responsibility of the Ministry of Transport

The 51% privatization of CFR Marfă (rail freight transport) has been approved by the government. The approval of the privatization contract by the government on 24 July, during the programme negotiation mission to Bucharest, marked the start of political discussions between President Băsescu, presiding the Supreme Defence Council, and Prime Minister Ponta, interim Minister of Transport, which attracted extensive media coverage. The government decision was published in the Romanian Official Journal on 14 August. On 2 September the contract was signed by the buyer, Grup Feroviar Român (GFR), who had to notify the Competition Council within 10 days but has not done so yet. An escrow account will be set up within 30 days, into which GFR will have to pay 20 million euros within 2 days after the setup of the account.

The deal is subject to clearance by the Romanian Competition Council, which might need up to six months to come to a final decision on the sale: one month to gather all documentation and five months to reach a decision. Once the file includes all necessary documentation, the Competition Council will examine within one month whether the decision falls under their jurisdiction or under the responsibility of the European Commission. If it falls under national jurisdiction, the Competition Council will have five months as of the date of full documentation to conclude whether: (i) the transaction is rejected due to significant competition distortions; (ii) the transaction is authorized; or (iii) the transaction is authorized subject to remedial measures to be implemented by the parties.

The long timeframe puts the deal at risk, as the published government decision calls for a full payment and transfer of ownership within 60 days of publication, i.e. 14 October, while the buyer conditioned full payment of the agreed 905 million lei (202 million euros) on the endorsement of the Competition Council. The 60-days deadline may have to be extended by a new government decision.

If the deal is not closed however, the authorities committed to sell a majority share of the company to another strategic investor.

SOEs under the responsibility of the Ministry of Economy, Department of Energy

The Initial Public Offering (IPO) of Nuclearelectrica (nuclear electricity producer) started on 9 September and closed successfully on 20 September 2013. The general shareholders meeting's decision on the capital increase was published in Romania's Official Journal on 7 August. The IPO auctions a capital increase representing 11% of the existing share capital, which once the transaction is completed will result in a division of 90% of capital in previously-existing shares and 10% of capital in new shares.

An IPO of 15% of the government's shares in Romgaz (natural gas producer) is planned to be launched by mid-November 2013. It has been decided to list the shares on the Bucharest Stock Exchange, accompanied by the issuance of global depository receipts in London. This required amendments to financial regulation by the Romanian Financial Supervision Authority to allow for global depository receipts. The prospectus now has to be approved by the Financial Supervision Authority. Under current planning, the IPO would be performed by early November.

A new permanent supervisory board for Hidroelectrica (hydropower electricity producer) has to be appointed by November 2013 (in accordance with the (government emergency ordinance 109/2011). The company exited insolvency in July, and has since then been supervised by an interim board. A general shareholder meeting on 6 September authorized the interim board to take decisions in accordance with law 31/1990 (i.e. no limitations beyond the stipulations in the bylaws).

An IPO through a capital increase of 10% of the shares of Hidroelectrica is to be launched by end-June 2014. A court ruling against the initial decision to hold the IPO has delayed the original deadline of end-October 2013. The Romanian government and Hidroelectrica have submitted requests to the Court of Appeal to formally withdraw their appeals to this court ruling. This

(Continued on the next page)

Box (continued)

allows the government to issue a new decision on the IPO that observes all legal requirements.

An IPO of 15% of the shares of Oltenia (thermoelectric energy producer) is to be launched by end-June 2014, prior to the planned capital increase. Prior to that, a study will be conducted to value the company's coal reserves. The June 2014 deadline allows for the use of audited financial statements for 2013 in the prospectus.

An IPO of a majority of the shares in Electrica (electricity distribution, supply and service) is to be completed by end-May 2014, after the planned capital increase. In line with conditions laid out in the memorandum of economic and financial policies, the transaction advisor was hired in September 2013.

Table II.4.1: **Ceilings on outstanding payments past due date (bn lei)**

January-December 2012 (actual)	12.6
January-June 2013 (preliminary)	8.2
January-September 2013 (target)	7.5
January-December 2013 (target)	5.6
January-March 2014 (indicative)	4.7
January-June 2014 (indicative)	3.7

Source: TMU

The list of central-government-owned enterprises can evolve due to placement into insolvency, the launch of liquidation procedures or the privatization of companies. A list of 248 solvent central-government-owned enterprises was established (Table II.4.2).

Table II.4.2: **Central-government owned SOEs by type**

Type of entity	Total	Of which solvent	Of which insolvent
Companies	112	99	13[1]
Regii Autonome[2]	15	15	
Subsidiaries majority owned by parent companies	92	91	1
Research institutes	44	43	1
Total	263	248	15

(1) Of which one company is in dissolution and one in bankruptcy
(2) Government business enterprises considered as not to be privatised. These include e.g. the national bank's printing office and the meteorological institute
Source: Ministry of Public Finance data

The operational performance of the railway companies will be closely monitored. Quarterly ceilings are set on the size of operating losses of CN Căi Ferate CFR, CFR Călători, CFR Marfă and their subsidiaries[18] combined, emphasizing the focus on reforms in order to improve the viability of these companies (Table II.4.3).

Table II.4.3: **Railway operating performance targets (bn lei)**

January-December 2012 (actual)	-3.3
January-June 2013 (preliminary)	-1
January-September 2013 (target)	-1.6
January-December 2013 (target)	-2.3
January-March 2014 (indicative)	-0.5
January-June 2014 (indicative)	-0.8

Source: TMU

As soon as the majority privatization of CFR Marfă has been concluded, its operational losses would be excluded from the monitored figure for cumulative operating performance, in order to provide an incentive to ensure completion of the transaction. The target has been set in such a way that the required reduction in operating loss can be reached through the privatization of CFR Marfă and a reduction in operating loss of 10% for CFR Căi Ferate and CFR Călători by end 2014.

Privatization timelines focus on the transport and energy sectors. SOEs are dominant in these sectors. They are often loss-making and in need of big investments. Suboptimal performance of SOEs in these sectors weighs on public finances and economic growth. Yet, the sale of stakes in SOEs

(18) CN Căi Ferate CFR and five of its subsidiaries (S.C. Intervenţii Feroviare S.A., Informatică Feroviară S.A., S.C. Sere şi Pepiniere S.A., S.C. Electrificare CFR S.A., and S.C. Întreţinere Mecanizată S.A), CFR Călători and its subsidiary (S.C. de reparaţii locomotive CFR SCRL Braşov S.A.), and CFR Marfă and its subsidiary (S.C. Întreţinere şi Reparaţii Locomotive şi Utilaje S.A.)

Table II.4.4: **Electricity and gas price increases, commitments of the authorities and implementation**

	Share of electricity sourced from the competitive market, in %			Gas price convergence to the market price level, in %		
	Corporates	Households	Status	Corporates	Households	Status
01/09/2012	15	0	implemented	-	-	
01/12/2012	15	0		35	33	implemented on 01/02/2013
01/01/2013	30	0	implemented	35	33	
01/04/2013	45	0	implemented	40	33	implemented
01/07/2013	65	10	implemented	47	36	implemented
01/09/2013	85	10	implemented	47	36	
01/10/2013	85	10		51	37	
01/01/2014	100	20		55	38	
01/04/2014	100	20		71	41	
01/07/2014	100	30		91	44	
01/10/2014	100	30		100	46	
01/01/2015	100	40		100	47	
01/04/2015	100	40		100	49	
01/07/2015	100	50		100	52	
01/10/2015	100	50		100	54	
01/01/2016	100	60		100	56	
01/04/2016	100	60		100	60	
01/07/2016	100	60		100	64	
01/10/2016	100	70		100	66	
01/01/2017	100	80		100	69	
01/04/2017	100	80		100	73	
01/07/2017	100	80		100	78	
01/10/2017	100	90		100	81	
01/01/2018	100	90		100	83	
01/04/2018	100	100		100	89	
01/07/2018	100	100		100	97	
01/10/2018	100	100		100	100	

Gas price convergence is calculated as the gap between the producer prices and imported prices
Source: Electricity and gas roadmaps, Romanian authorities

has proven to be very cumbersome and has, so far, met with little success.

4.5. TRANSPORT SECTOR

On the regulatory framework of the rail sector, the programme includes the requirement to implement remaining, yet unfulfilled, policy commitments from the previous programme. These relate to performance schemes linked to delays and incentive structure of the infrastructure manager. Romania's transport sector still needs a lot of improvement. While regulatory issues in the rail sector have largely been tackled under the previous programme, the conditionality of the proposed programme requires completing the outstanding reforms. By end-2013, the government committed to introduce performance schemes related to delays as well as to introduce incentives for the infrastructure manager to reduce unit costs and charges. These reforms are supported by a World Bank project on performance schemes. It is important to note that, in September 2013, the Commission launched an infringement procedure against Romania that looks into regulatory shortcomings that are partially covered by the yet unfulfilled programme conditionality.

4.6. ENERGY SECTOR

Conditionality in the energy sector relates to remaining unfulfilled parts of the previous programme and the implementation of the earlier agreed measures. This notably entails, in line with the CSRs: (i) the implementation of the price road maps for phasing out regulated prices for gas and electricity; (ii) unbundling of transmission and dispatch operators; and (iii) further development of gas and electricity markets through trading platforms and improved cross-border integration of energy networks.

Phasing out regulated electricity and gas prices should allow supply and demand to define a fair market price. This would allow for a more efficient allocation of resources in the economy rather than continuing the current practice of cross-subsidisation across sectors. Price liberalisation should also allow generating resources for urgently needed investment in the power grid and should also help improve energy efficiency. For electricity, according to the agreed roadmap, complete deregulation of electricity prices for corporate consumers is scheduled to be achieved by end-2013 and for households by end-2017. For natural gas, prices are expected to be brought to a pre-defined market level for non-residential consumers by end-2014 (with a possible extension to end-2015, should a significant gap to the market prices remain by end-2014) and for households by end 2018 (see Table II.4.4). While the energy regulator (ANRE) insists on a full and timely implementation of the gas and electricity roadmaps, its independence and impartiality are being tested as the industry is lobbying for delays in gas price liberalisation. It is important to acknowledge that, in reaction to energy price increases, the authorities took measures to protect the vulnerable consumers, i.e. the poorest households. They have introduced a top-up of 8.5% on the minimum income benefit in July 2013 and are planning to introduce another increase of 4.5% in January 2014; the family and child allowances were also increased.

The continued unbundling of transmission system operators (TSOs) is a policy condition under the proposed programme. Production and supply, on the one hand, and transmission and dispatch of energy, on the other, should be separated according to the EU acquis. The unbundling should allow avoiding oligopolistic tendencies in price formation and to provide a level playing field for all energy producers. While the TSOs have formally been transferred to the finance ministry, the dispatching has remained with the economy ministry that manages the state's shares in energy production and supply companies. Consequently, full unbundling has not yet taken place. The government has now committed to fully unbundle the TSOs in line with the EU acquis and to transfer the dispatch centres to the finance ministry. The energy regulator has already notified the Commission concerning the electricity TSO certification. However, the implementation of unbundling by the government requires a legal change that is still outstanding.

A further development of gas and electricity markets is important because it would allow for greater liquidity, better transparency and thus more efficient use of the country's natural resources. Network charges applying to exports and imports of electricity were eliminated from 1 August 2013. The much-needed standard contract/product for large electricity consumers on the OPCOM electricity exchange is close to being finalised. On cross-border integration, the coupling of the Romanian electricity market with Slovakia, the Czech Republic and Poland will be implemented by September 2014. On the security-of-gas-supply obligation, the required reports and emergency plans should be finalised by end-2013.

4.7. HEALTHCARE SECTOR

The Romanian healthcare system is facing several challenges, including poor health outcomes, low funding and an inefficient use of resources. The pursuit of health sector reforms to increase its efficiency, quality and accessibility is covered by the CSRs Life expectancy is considerably below the EU average. Public and private spending on health are also considerably below the EU average and in fact among the lowest in the EU (Table II.4.5). In addition, there is scope to increase the efficiency of spending in terms of shifting resources from a hospital-centric health system towards a more cost-effective system based on strong primary and ambulatory care sectors (Table II.4.6), which is also in line with the CSRs.

Table II.4.5: **Life-expectancy and health expenditure as % of GDP – 2011 or latest data**

Country	Life expectancy at birth for females	Life expectancy at birth for males	Total health expenditure as % GDP	Public health expenditure as % of GDP
Bulgaria	77.4	70.3	7.3	4.2
Latvia	78.4	68.6	6.8	4.1
Lithuania	78.9	68.0	7.0	5.6
Hungary	78.6	70.7	7.9	5.1
Poland	80.7	72.1	6.9	4.8
Romania	**77.4**	**69.8**	**5.7**	**4.5**
EU	83.0	77.1	8.7	6.4

Source: Eurostat

The authorities committed to explore all options to address the mismatch between spending commitments and available funding. In the past, this led to the accumulation of arrears, particularly in the hospital sector and to large budget overruns in the area of pharmaceutical spending. To reduce payment delays in the health sector from 210 to 60 days as required by the EU late payments directive (Directive 2011/7/EU), an additional budget of 3.4 bn lei was allocated to healthcare in 2013. In addition, the Ministry of Health and the pharmaceutical industry agreed on longer payment delays for the time being. Arrears have been effectively reduced in the hospital sector, but pending necessary structural reforms, the risk of arrears re-accumulation remains.

On the commitment side the authorities undertook to redefine the publicly-reimbursable basic-benefits package within the limitations of available funding. To increase spending efficiency, it will be based on objective, verifiable criteria including the criterion of cost-effectiveness in future revisions of the basket. On the revenue side, a framework for a private supplementary insurance market aimed at increasing the share of private in total expenditure on health will be established. In addition, a comprehensive medium-term health strategy, to be prepared by the health ministry and the finance ministry by end-2013, is key with respect to closing the current and future financing gap. This includes defining the priorities for future investments by European funds in the 2014-2020 programming period.

Table II.4.6: **Characteristics of health expenditure – 2011 or latest data**

Country	Public health as % of total government expenditure	Private as % of total health expenditure	Public hospital expenditure	Public ambulatory care expenditure
			as % of public health expenditure	
Bulgaria	12.9	42.5	61.0	19.5
Latvia	10.7	40.1	57.0	20.5
Lithuania	13.9	20.6	47.0	23.0
Hungary	10.3	35.0	44.0	17.3
Poland	10.8	29.7	47.0	26.6
Romania	**8.6**	**21.1**	**51.0**	**13.5**
EU	13.6	26.8	47.3	22.5

Source: Eurostat

The authorities have published a strategic action plan aimed at reducing the distortions and inefficiencies in the service delivery structure that need to be addressed resolutely. Primary care services, including preventive services and promotional programmes, play a minor role so far and will be allocated a 10% share of available health insurance funds instead of the 6% available currently. Hospital over-capacity will be reduced, and hospital services will be shifted from in-patients towards more cost-effective day care services. The fragmented hospital structure will be rationalized, reducing mono-profile hospitals and developing a truly specialized secondary ambulatory care system and the referral system that surrounds them from primary health to post-hospital care as well as patient pathways in the health system. This will be based on a future government project for health sector reform financed by the World Bank, slated for Board Approval by end-2013, and possibly supported by corresponding European funds.

Further elements of the reform focus on strengthening the financial and quality controls in order to reduce fiscal risks and increase the efficiency of service delivery. Key measures in this respect relate to: (i) preserving and improving budget control mechanisms (such as the claw-back tax on pharmaceuticals and monthly hospital budget reporting); (ii) producing reports comparing hospital performance on structural input and output and quality-of-care indicators; (iii) introducing centralized purchasing and procurement for medical goods; (iv) implementing health-technology assessments for introducing new drugs on the basic-benefits package; and (v) improving IT-structures (central patient database, e-prescription, e-health cards).

Annexes

ANNEX 1
Financial Assistance Programmes in 2009-2013

Table A1.1: **Financial assistance programmes with Romania**

Institution and type of programme/ support	Financial support
2009-2011 programme	
European Commission (EC): Balance of Payments programme – EU medium term financial assistance [1]	€5 billion
International Monetary Fund (IMF): Stand-By Arrangement (SBA)	SDR 11.4 billion (~ €12.9 billion; 1,110.77% of Romania's IMF quota)
World Bank (WB): Loans	€1 billion
European Investment Bank (EIB) & European Bank for Reconstruction and Development (EBRD) - Loans	€1 billion
TOTAL financial support received from IFIs during 2009-2011	**€19.9 billion [2]**
2011-2013 programme	
European Commission (EC): Balance of Payments programme – precautionary EU medium term financial assistance [1]	€1.4 billion
International Monetary Fund (IMF): Stand-By Arrangement (SBA) treated as precautionary	SDR 3.09 billion (~ €3.5 billion; 300% of Romania's IMF quota)
World Bank (WB): development loan programme (DPL of EUR 400 million) and results based financing for social assistance and health (of EUR 750 million)	€1.15 billion
TOTAL financial support available in 2011-2013	**€6 billion**
2013-2015 programme	
European Commission (EC): Balance of Payments programme – precautionary EU medium term financial assistance [1]	€2 billion
International Monetary Fund (IMF): Stand-By Arrangement (SBA) treated as precautionary	SDR 1,751.34 million (~ €EUR 2 billion; 170% of Romania's IMF quota)
World Bank (WB): EUR 1 billion were made available under a development policy loan with a deferred drawdown option (DPL/DDO) and the bank will continue to provide earlier commited support (of EUR 891 million)	€1.891 billion
TOTAL financial support available in 2013-2015	**€5.891billion**

Source: EC, IMF, and WB

ANNEX 2
Repayment schedule to the EU and the IMF

Table A2.1: **Repayment schedule to the EU and the IMF**

Yearly data	EU (€ mn)*			IMF (SDRs mn)**			Grand total (€ mn)
	Charges	Principal	Total	Charges	Principal	Total***	
2013	151.6	-	151.6	234.0	4,051.6	4,285.6	5,111.6
2014	151.6	-	151.6	65.8	3,880.3	3,946.1	4,718.6
2015	151.6	1,500.0	1,651.6	8.1	1,231.9	1,240.0	3,086.7
2016	104.8	-	104.8	0.2	96.0	96.2	216.1
2017	104.8	1,150.0	1,254.8			-	1,254.8
2018	77.4	1,350.0	1,427.4			-	1,427.4
2019	33.8	1,000.0	1,033.8			-	1,033.8

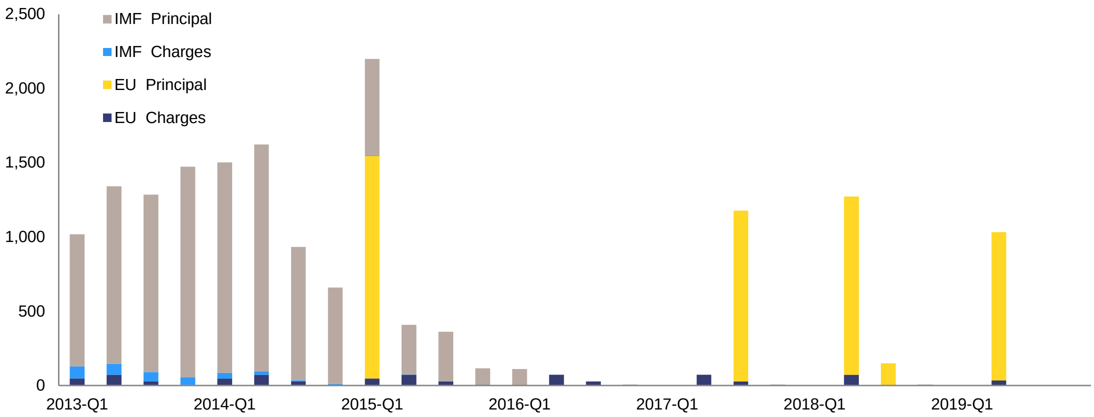
* EU BoP assistance has been in full chanelled to the MoPF

**The 2nd & 3rd IMF disbursements (out of 6) were made 50:50 to the MoPF and the NBR, all other disbursements were made fully to the NBR.

***Out of the total, The ministry of public finance shall repay SDR 47 mn on charges and SDR 837 mn in principal in 2013, respectively SDR 12 mn and SDR 866 mn in 2014 and SDR 1 mn and SDR 136 mn in 2015.

Source: Commission services and the IMF

Graph A2.1: **Quarterly repayment schedule to the EU and the IMF, € mn**



Source: Commission services and the IMF

ANNEX 3
EU Funds absorption

Table A3.1: **Cumulative EU Funds Absorption**

Date	EAFRD	% of total EAFRD	SCF	% of total SCF	Grand total	% of total
Mar-09	*171*	*2.1%*	*87*	*0.5%*	*258*	*0.9%*
Dec-10	1436	17.7%	368	1.9%	1804	6.6%
Mar-11	*1552*	*19.1%*	*548*	*2.9%*	*2100*	*7.7%*
Dec-11	2209	27.2%	1066	5.5%	3275	12.0%
Dec-12	3323	40.9%	2204	11.5%	5527	20.2%
Sep-13	4070	**50.1%**	4160	21.7%	8230	**30.1%**

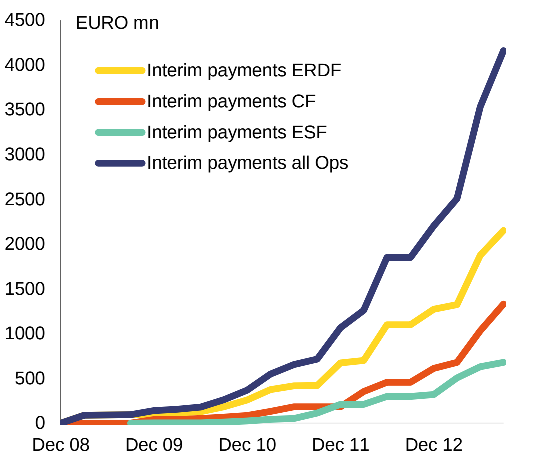
Legend
EAFRD: European Agricultural Fund for Rural Development
SCF: Structural and Cohesion Funds

Total EAFRD	8124
Total SCF	19213
Total Funds	27337

Source: Commission services

Although some progress was made in the first half of 2013, Romania still displays the lowest EU funds absorption rate in the EU with EUR 8.2 bn absorbed as of end-August 2013 (i.e. 30.1% of the total structural, cohesion and agricultural funds allocated for the 2007-2013 programming period; see Table A3.1).

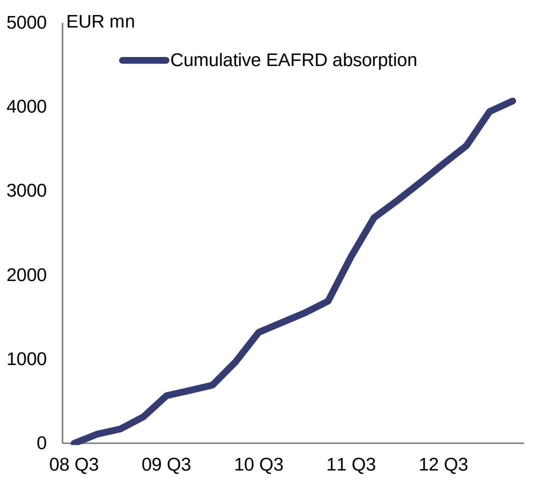
Graph A3.1: **Cumulative SCF absorption**



Source: Commission services

With an absorption rate of 21.7% as of end-August for the SCF (Graph A3.1**), Romania stands to lose several billion of euros at the end of 2013 due to the application of the automatic decommitment rules.** Only one operational programme (OP) is still blocked, the Competitiveness OP, therefore the Commission expects to see more payment requests coming through from the other OPs until the end of 2013; however these requests are highly unlikely to amount to the needed sum for avoiding decommitment in 2013. For this particular reason, the Commission has proposed for allowing Romanian and Slovakia to apply an n+3 decommitment rule for the commitments made in 2010 and 2011 thus reducing the risk of decommitment in both 2013 and 2014. Nevertheless, the end-date for eligibility of expenditure for the 2007-2013 programming period remains unchanged as end-December 2015.

Graph A3.2: **Cumulative EAFRD absorption**



Source: Commission services

The current EAFRD absorption rate is 50.1% (Graph A3.2**) and there is some risk of de-commitment of funds in 2013.** Although the EU funds absorption situation is much better on the agricultural funds arena, Romania is also lagging behind its regional pears.

The 95% "top-up" issue: As soon as a third financial assistance programme would be approved, Romania would be able to benefit again from the "top-up", the 95% co-financing rate. This measure was designed to accelerate investments and improve the availability of EU funding in Member States experiencing or threatened with financial difficulties. However, the same regulation stipulates that the "top-up" is valid until end-2013 only([19]) and thus Romania would be able to (re-)apply it for only a couple of months. However, the Commission proposed the extension of this deadline until end-2015 in the same document proposing the change in the rules of decommitment, but final agreement by the European Parliament is still pending.

([19]) Regulations 1311/2011 and 1312/2011

New partnership agreement with the Commission: The Romanian authorities are preparing the new partnership agreement paper setting up the EU funding priorities for Romania for the next programming period (2014-2020). A new draft of the document was submitted to the Commission services in October 2013.

ANNEX 4
Key economic indicators

Table A4.1: **Key economic indicators for Romania (Overview, 2007-2015)**

	2007	2008	2009	2010	2011	2012	2013*	2014*	2015*
Gross Domestic Product	*(annual percentage change, unless otherwise indicated)*								
Nominal GDP (in bn RON)	#N/A	515	501	524	557	587	624	657	689
Real GDP	6.3	7.3	-6.6	-1.1	2.2	0.7	2.1	2.2	2.4
Private Consumption	11.9	9.0	-10.1	-0.3	1.1	1.1	0.0	1.5	2.3
Public Consumption	-0.1	7.2	3.1	-4.7	0.2	1.7	0.0	2.0	1.3
Gross fixed capital formation	30.3	15.6	-28.1	-1.8	7.3	4.9	-2.1	5.7	5.1
Exports	7.8	8.3	-6.4	13.2	10.3	-3.0	7.4	4.6	5.4
Imports	27.3	7.9	-20.5	11.1	10.0	-0.9	0.5	5.7	5.9
Contribution to GDP growth									
Domestic demand	15.9	11.9	-15.0	-1.5	2.6	2.2	-0.6	2.7	2.9
Inventories	0.0	-3.5	1.4	0.4	0.1	-0.7	-0.1	0.1	-0.1
Net exports	-9.6	-1.0	7.0	0.0	-0.5	-0.8	2.8	-0.6	-0.4
Prices									
HICP inflation (average)	4.9	7.9	5.6	6.1	5.8	3.4	3.6	2.7	3.4
HICP inflation (year-end, quarterly)	6.8	6.9	4.5	7.8	3.4	4.7	3.8	3.1	3.1
NBR target	4.0	3.8	3.5	3.5	3.0	3.0	2.5	2.5	2.5
Labour market									
Total employment	9364.8	9365.9	9181.0	9156.1	9058.1	9197.9	9345.1	9391.8	9438.8
Unemployment rate (registered, year-end)	4.1	4.4	7.8	7.0	5.1	5.6	*5.0*	n.a.	n.a.
Unemployment rate (LFS, year-end)	6.4	5.8	6.9	7.3	7.4	7	7.2	7	7
General Government Accounts	*(in percent of GDP, cash)*								
Total revenues	30.6	32.2	31.4	32.3	32.7	33.1	33.3	n.a.	n.a.
Total expenditures	32.8	37.0	38.7	38.7	37.2	35.6	35.7	n.a.	n.a.
Current	29.4	32.1	34.8	35.1	33.0	32.3	32.8	n.a.	n.a.
Capital	3.5	5.0	4.4	3.7	4.1	3.3	2.9	n.a.	n.a.
Govn deficit, cash definition	-2.3	-4.8	-7.3	-6.4	4.5	2.5	-2.3	n.a.	n.a.
Government deficit, ESA95 definition, target [1)]	-2.9	-5.7	-9.0	-6.8	-5.6	-2.9	-2.4	-2.0	-1.8
Gross debt, general govn, ESA95 definition	12.8	13.4	23.6	30.5	34.7	37.9	39.4	40.0	39.6
Balance of payments	*(in percent of GDP)*								
Current account balance **	-13.6	-11.4	-4.2	-4.4	-4.5	-4.0	-1.8	-2.1	-2.3
Trade balance	-13.9	-13.0	-6.0	-5.7	-5.3	-5.2	-2.2	-2.7	-3.0
Capital and financial account balance	14.0	12.8	5.0	4.6	4.2	3.2	n.a.	n.a.	n.a.
FDI balance	5.7	6.7	3.0	1.8	1.4	1.3	n.a.	n.a.	n.a.
Net international investment position	-43.5	-49.4	-62.4	-62.6	-64.3	-64.9	n.a.	n.a.	n.a.
Foreign exchange reserves (in bn Euro)	47.0	51.8	68.7	74.4	75.2	75.1	n.a.	n.a.	n.a.
Gross external debt	25.3	26.2	28.3	32.4	33.2	31.2	*32.2*	n.a.	n.a.
Monetary and exchange rate developments									
Broad money M3 (annual % change, end of the period)	33.70	17.49	8.97	6.93	6.63	2.69	*2.00*	n.a.	n.a.
NBR policy rate (in %, end of period)	7.50	10.25	8.00	6.25	6.00	5.25	*5.25*	n.a.	n.a.
Exchange rate (lei/euro, end of period)	3.61	4.01	4.24	4.23	4.33	4.40	*4.41*	n.a.	n.a.
REER (Unit Labour Costs deflator, % change)	19.9	8.0	-13.0	-3.6	0.5	-2.3	*8.8*	n.a.	n.a.
Financial market & banking sector developments									
Private credit growth (y-o-y)	60.4	33.7	0.9	4.7	6.6	1.3	*-4.4*	n.a.	n.a.
Capital Adequacy									
CAR	13.8	13.8	14.7	15.0	14.9	14.6	*15.0*	n.a.	n.a.
Leverage ratio	7.3	8.1	7.6	8.1	8.1	8.0	*8.3*	n.a.	n.a.
Ratio of level 1 own funds	10.7	11.8	13.4	14.2	14.3	16.6	*16.7*	n.a.	n.a.
Asset quality									
NPLs (90 dpd)	-	2.8	7.9	11.9	14.3	18.2	*19.5*	n.a.	n.a.
NPLs (60 dpd)	4.0	6.5	15.3	20.8	23.3	29.9	*30.0*	n.a.	n.a.
Profitability									
ROA (after tax)	1.0	1.6	0.3	-0.2	-0.2	-0.6	*0.6*	n.a.	n.a.
ROE (after tax)	9.4	17.0	2.9	-1.7	-2.6	-5.9	*5.5*	n.a.	n.a.
Liquidity									
Immediate liquidity	38.7	34.4	35.3	37.8	37.2	35.9	*37.9*	n.a.	n.a.

Source: European Commission, National authorities

Table A4.2: **General government accounts, 2007-2013**

	2007 Final	2008 Final	2009 Final	2010 Final	2011 Final	2012 Final	2013 Proj
	(in percent of GDP, cash projection)						
TOTAL REVENUES	30.6	32.2	31.4	32.3	32.7	33.1	33.3
Profit tax	2.5	2.5	2.4	1.9	1.9	1.9	1.9
Income and wage tax	3.5	3.6	3.7	3.4	3.4	3.6	3.7
VAT	7.5	7.9	6.8	7.5	8.6	8.6	8.5
Excises	3.0	2.7	3.1	3.3	3.4	3.5	3.5
Social insurance contributions	9.3	9.5	9.6	8.7	9.1	8.8	8.7
Non fiscal revenue	1.9	3.1	3.1	3.8	3.3	3.2	3.0
Other fiscal taxes	1.9	2.0	2.0	2.6	1.7	2.0	1.9
Revenue from capital	0.9	0.8	0.8	0.9	1.2	1.5	2.2
TOTAL EXPENDITURES	32.8	37.0	38.7	38.7	37.2	35.6	35.7
Current expenditures	29.4	32.1	34.8	35.1	33.0	32.3	32.8
Personnel expenditures	6.2	8.9	9.3	8.2	6.9	7.0	7.4
Goods and services	6.2	6.3	5.7	5.7	5.7	5.8	6.3
Interest	0.7	0.7	1.2	1.4	1.6	1.8	1.8
Subsidies	1.7	1.5	1.4	1.3	1.2	1.0	0.9
Transfers	14.7	14.7	16.7	18.2	17.3	16.3	16.3
Social Assistance	9.2	10.5	12.8	13.1	12.2	11.5	11.1
Other transfers	5.5	4.1	3.9	5.1	5.0	4.8	5.2
Other	0.0	0.0	0.4	0.3	0.4	0.3	0.2
Capital expenditures	3.5	5.0	4.4	3.7	4.1	3.3	2.9
Other expenditure (net lending)	0.0	-0.1	-0.5	-0.1	0.1	0.1	0.0
Government deficit, cash definition	-2.3	-4.8	-7.3	-6.4	4.5	2.5	-2.3
Government deficit, ESA95 definition, gov target 1)	-2.9	-5.7	-9.0	-6.8	-5.6	-2.9	-2.4
Government deficit, ESA95 definition, EC Spring forecast 1)	-2.9	-5.7	-9.0	-6.8	-5.6	-2.9	-2.6
Gross debt, general government, ESA95 definition, EC Spring Forecast	12.8	13.4	23.6	30.5	34.7	37.9	39.4

Source: European Commission, National authorities

Table A4.3: **Key monetary indicators, 2007-2013**

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

	2007	2008	2009	2010	2011	2012	Jul-13	2013**
Broad money (M3)	**148,116**	**174,028**	**189,630**	**202,763**	**216,208**	**222,018**	**225,905**	…
Intermediate money (M2)	148,044	173,629	188,013	199,586	212,059	221,830	225,700	…
Money market instruments	72	399	1,617	3,177	4,149	188	205	…
Narrow money (M1)	79,914	92,549	79,361	81,605	85,835	89,020	92,007	…
Currency in circulation	21,442	25,287	23,968	26,793	30,609	31,477	33,016	…
Overnight deposits	58,473	67,262	55,394	54,812	55,226	57,543	58,992	…
Time deposits*	68,129	81,080	108,652	117,982	126,224	132,809	133,693	…
Money and credit (Annual percentage change, eop)								
Broad money (M3)	33.7	17.5	9.0	6.9	6.6	2.7	2.0	…
- NFA contribution	…	-10.7	5.0	0.7	-1.4	6.7	11.0	…
- NDA contribution	…	28.2	4.0	6.2	8.0	-4.0	-9.0	…
Intermediate money (M2)	…	17.3	8.3	6.2	6.2	4.6	2.1	…
Narrow money (M1)	…	15.8	-14.2	2.8	5.2	3.7	2.8	…
Currency in circulation	…	17.9	-5.2	11.8	14.2	2.8	0.4	…
Overnight deposits	…	15.0	-17.6	-1.1	0.8	4.2	4.2	…
Time deposits*	…	19.0	34.0	8.6	7.0	5.2	1.6	…
p.m. Credit to private sector	60.4	33.7	0.9	4.7	6.6	1.3	-4.4	…
Interest rates (In percent, eop)								
Robor, 3 m	8.4	15.6	10.4	6.3	6.3	6.0	4.5	5.5
Robor, o/n	8.1	12.1	10.2	3.0	5.2	5.8	4.7	…
NBR policy rate***	7.5	10.3	8.0	6.3	6.0	5.3	4.5	…
NBR credit facility rate***	12.0	14.3	12.0	10.3	10.0	9.3	7.5	…
NBR deposit facility rate***	2.0	6.3	4.0	2.3	2.0	1.3	1.5	…
Exchange rates								
Lei per euro (end of period)	3.61	4.01	4.24	4.23	4.33	4.40	4.41	4.42
Lei per euro (average)	3.34	3.70	4.22	4.20	4.24	4.50	4.42	4.41
Real effective exchange rate (percentage change)								
HICP based	8.4	-4.9	-7.7	2.5	3.1	-5.5	7.9	…
ULC deflator based	19.9	8.0	-13.0	-3.6	0.5	-2.3	8.8	…

*** Maturity of up to two years
Source: NBR, Commission services

Table A4.4: **Gross external financing requirements and sources, 2012-2015**

	2012	2013					2014					2015
		Q1	Q2	Q3	Q4	Year	Q1	Q2	Q3	Q4	Year	
	Act	Act	Proj	Proj	Proj	Proj.	Proj	Proj	Proj	Proj	Proj.	Proj.
I. Total financing requirements	**43.4**	**8.0**	**7.8**	**7.2**	**10.0**	**33.0**	**7.3**	**8.2**	**7.7**	**9.3**	**32.5**	**34.7**
I.A. Current account deficit	5.2	-0.3	-0.4	1.4	2.0	2.7	1.2	0.5	0.9	1.0	3.6	4.1
I.B. Short-term debt	25.8	5.5	4.7	4.1	4.9	19.2	4.2	4.6	4.6	5.5	19.0	19.8
Public sector	7.5	2.0	1.8	0.9	0.9	5.6	0.9	0.7	0.9	0.9	3.4	3.6
Banks	14.2	2.6	2.1	1.9	2.7	9.2	2.1	3.1	2.3	3.1	10.7	11.0
Corporates	4.2	1.0	0.8	1.3	1.3	4.4	1.1	0.8	1.5	1.5	4.9	5.2
I.C. Maturing medium- and long-term debt	12.0	2.7	3.6	2.1	3.3	11.6	2.0	3.1	2.2	3.0	10.4	11.4
Public sector	2.8	0.4	0.8	0.6	1.0	2.8	0.5	0.9	0.6	0.6	2.5	3.7
Banks	4.9	1.6	2.0	0.7	0.5	4.8	0.6	1.1	0.9	0.9	3.5	3.3
Corporates	4.3	0.7	0.8	0.8	1.7	4.0	0.9	1.1	0.8	1.5	4.4	4.4
I.D. Other net capital outflows 1/	0.5	0.1	-0.1	-0.3	-0.3	-0.6	-0.1	-0.1	-0.1	-0.2	-0.5	-0.6
II. Total financing sources	**41.6**	**10.3**	**9.3**	**7.1**	**9.9**	**36.7**	**7.5**	**7.9**	**9.3**	**9.8**	**34.4**	**36.5**
II.A. Foreign direct investment, net	1.7	0.2	0.4	0.5	0.4	1.4	0.2	0.5	0.7	0.7	2.1	2.4
II.B. Capital account inflows	1.9	0.3	0.7	0.5	0.5	1.9	0.2	0.4	0.5	0.8	1.9	1.9
II.C. Short-term debt	23.3	4.9	5.4	4.5	5.5	20.3	4.4	4.7	4.8	5.6	19.5	20.0
Public sector	6.7	1.9	1.8	0.9	0.9	5.5	0.9	0.7	0.9	0.9	3.4	3.6
Banks	11.9	1.9	2.7	2.1	3.1	9.9	2.3	3.1	2.4	3.1	10.9	11.0
Corporates	4.6	1.1	0.8	1.5	1.5	4.9	1.2	0.9	1.5	1.6	5.2	5.3
II.D. Medium- and long-term debt	14.7	4.9	2.9	1.7	3.6	13.1	2.7	2.3	3.2	2.6	10.9	12.2
Public sector	6.6	3.7	1.4	0.4	1.5	7.0	1.3	0.1	1.6	0.2	3.2	3.5
Banks	5.1	0.9	1.0	0.6	0.5	3.0	0.6	1.1	0.8	0.9	3.3	3.6
Corporates	3.0	0.3	0.5	0.7	1.6	3.1	0.9	1.1	0.8	1.5	4.3	5.1
Errors and Omissions	1.0	-0.4	0.1	0.0	0.0	-0.4	0.0	0.0	0.0	0.0	0.0	0.0
III. Increase in gross reserves	-1.5	1.0	0.4	-1.2	-1.4	-1.3	-1.2	-1.8	0.7	-0.2	-2.5	-1.1
IV. Financing Gap	**-0.6**	**-0.9**	**-1.2**	**-1.2**	**-1.4**	**-4.6**	**-1.4**	**-1.5**	**-0.9**	**-0.6**	**-4.4**	**-2.9**
V. Program financing	**-0.6**	**-0.9**	**-1.2**	**-1.2**	**-1.4**	**-4.6**	**-1.4**	**-1.5**	**-0.9**	**-0.6**	**-4.4**	**-2.9**
IMF	-1.6	-0.9	-1.2	-1.2	-1.4	-4.6	-1.4	-1.5	-0.9	-0.6	-4.4	-1.4
Purchases	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Repurchases	-1.6	-0.9	-1.2	-1.2	-1.4	-4.6	-1.4	-1.5	-0.9	-0.6	-4.4	-1.4
European Commission	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	-1.5
Disbursements	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Principal repayments	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	-1.5
Others	1.0	…	…	…	…	…	…	…	…	…	…	…
World Bank	0.0	…	…	…	…	…	…	…	…	…	…	…
EIB/EBRD/IFC	1.0	…	…	…	…	…	…	…	…	…	…	…
Memorandum items:												
Gross international reserves	35.4	…	…	…	…	34.1	…	…	…	…	31.6	30.5

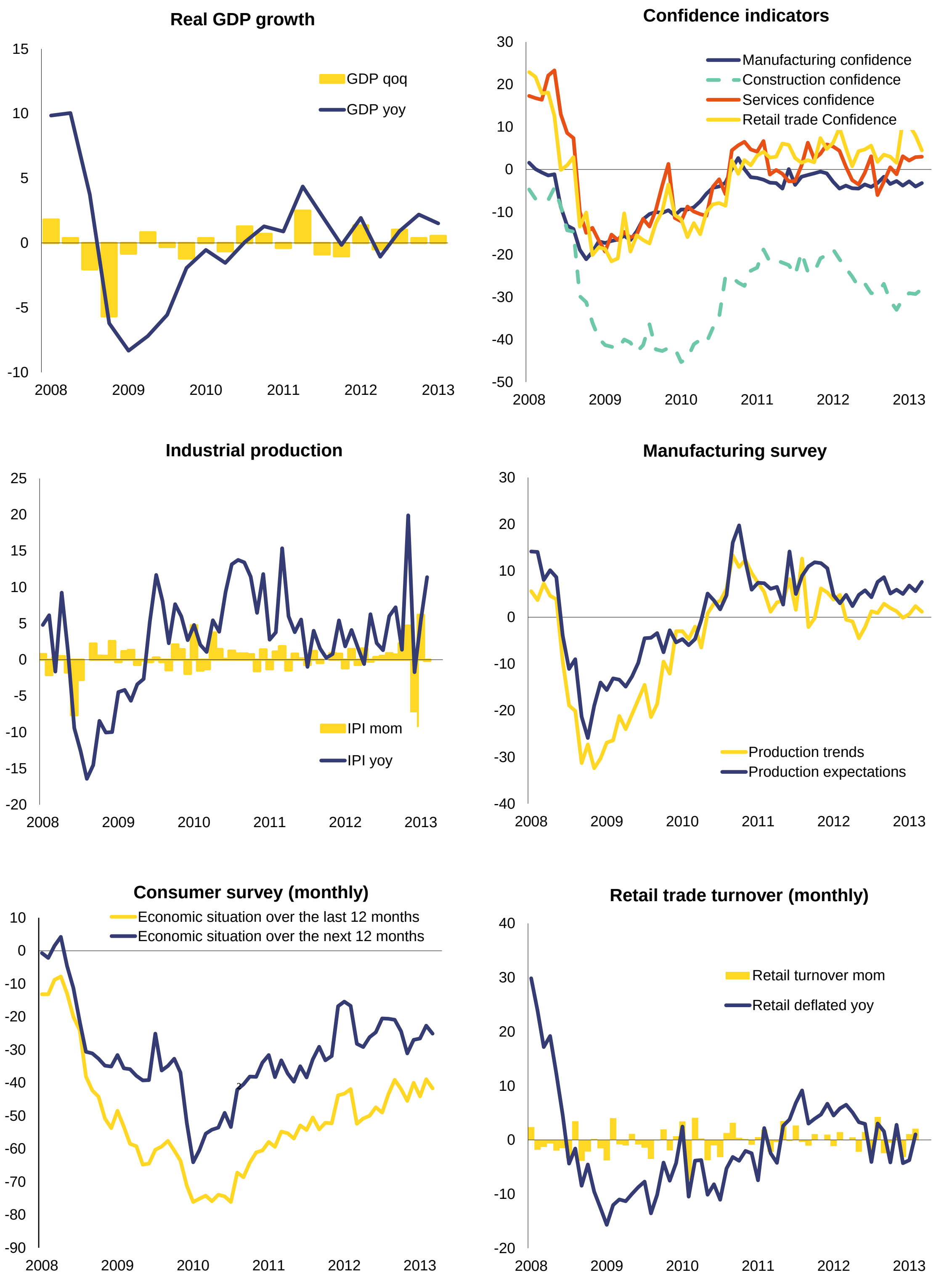
(1) The figures in this table are based on balance-of-payments methodology, hence possible discrepancies with figures and forecasts based on national-accounts methodology.
Source: National authorities and IMF staff estimates

Table A4.5: **Key labour market indicators, 2007-2013**

	2007	2008	2009	2010	2011	2012	2013 Q1	2012-2011
1 - Population (total, 1000 pers.)	21551.3	21516.5	21484.3	21446.7	21384.1	21336.1	:	-0.2 %
2 - Population (working age:15-64, 1000 pers.)	15046.3	15042.3	15028.2	14999.4	14967.5	14928.3	:	-0.3 %
3 - Labour force (15-64, 1000 pers.)	9479.169	9461.607	9482.794	9539.618	9474.427	9583.968	:	1.2 %
4 - Activity rate (% of population 15-64)	63	62.9	63.1	63.6	63.3	64.2	:	0.9 pps
Young (15-24)	30.5	30.4	30.9	31.2	31.1	30.9	:	-0.2 pps
Prime age (25-54)	79	78.3	78.5	79.5	79.1	79.8	:	0.7 pps
Older (55-64)	42.4	44.2	43.9	42.5	41.5	42.9	:	1.4 pps
Nationals (15-64)	63	62.9	63.1	63.6	63.3	64.2	:	0.9 pps
Non-nationals (15-64)	67	62.7	65	:	:	:	:	
Male	70.1	70.6	70.9	71.5	70.7	72.1	:	1.4 pps
Female	56	55.2	55.4	55.8	56	56.4	:	0.4 pps
5 - Employment rate (% of population 15-64)	58.8	59	58.6	58.8	58.5	59.5	:	1.0 pps
Young (15-24)	24.4	24.8	24.5	24.3	23.8	23.9	:	0.1 pps
Prime age (25-54)	74.6	74.4	73.7	74.4	74.1	74.9	:	0.8 pps
Older (55-64)	41.4	43.1	42.6	41.1	40	41.4	:	1.4 pps
Low-skilled (15-64)	40.3	41	42	43	40.5	41.9	:	1.4 pps
Medium-skilled (15-64)	63.9	63.5	62.2	62.2	62.3	63.1	:	0.8 pps
High-skilled (15-64)	85.8	85.7	84.1	82.4	82.1	81.4	:	-0.7 pps
Nationals (15-64)	58.68297	58.91099	58.53478	58.77001	58.47392	59.45782	:	1.0 pps
Non-nationals (15-64)	0.117032	0.089012	0.065223	0.029993	0.026077	0.042185	:	
Male	64.8	65.7	65.2	65.7	65	66.5	:	1.5 pps
Female	52.8	52.5	52	52	52	52.6	:	0.6 pps
6 - Employed persons (15-64, 1000 pers.)	8842.5	8882.2	8804.7	8822	8750	8885.6	:	1.5 %
7 - Self employed (% of total employment)	22.44558	21.9466	21.84789	22.69351	20.85272	21.01742	:	0.2 pps
8 - Temporary employment (% of total employment)	1.6	1.3	1	1.1	1.5	1.7	:	0.2 pps
9 - Part-time (% of total employment)	9.7	9.9	9.8	11	10.5	10.2	:	-0.3 pps
10 - Unemployment rate (harmonised:15-74)	6.4	5.8	6.9	7.3	7.4	7	:	-0.4 pps
Young (15-24)	20.1	18.6	20.8	22.1	23.7	22.7	:	-1.0 pps
Prime age (25-54)	5.6	5	6.1	6.4	6.4	6.2	:	-0.2 pps
Older (55-64)	2.3	2.5	3	3.3	3.7	3.4	:	-0.3 pps
Low-skilled (15-64)	8.6	8.6	8.9	7.2	8.6	8.1	:	-0.5 pps
Medium-skilled (15-64)	6.9	6	7.3	8.3	8.1	7.6	:	-0.5 pps
High-skilled (15-64)	3	2.7	4.4	5.4	5.2	5.6	:	0.4 pps
Nationals (15-64)	5.7	5	6.2	6.9	7.1	6.7	:	-0.4 pps
Non-nationals (15-64)	:	:	:	:	:	:		
Male (harmonised:15-74)	7.2	6.7	7.7	7.9	7.9	7.6	:	-0.3 pps
Female (harmonised:15-74)	5.4	4.7	5.8	6.5	6.8	6.4	:	-0.4 pps
11 - Long-term unemployment (% total unemployment)	50	41.3	31.6	34.9	41.9	45.3	:	3.4 pps
12 - Worked hours (average actual weekly hours)	39.7	39.6	39.4	39.2	39.2	39.1	:	-0.3 %
13 - Indicator board on wage developments (% change)								
Compensation per employee	22.0256	31.91209	-1.88576	-3.28649	4.162494	5.163929	:	1.0 pps
Real compensation per employee (GDP deflator)	7.511543	14.40771	-5.84046	-8.50189	0.060033	0.34726	:	0.3 pps
Hourly labour costs (Eurostat labour cost index)	19.78708	22.58658	10.825	0.812092	4.520016	4.520016	:	0.0 pps
Wage and salaries	22.8231	36.30338	-6.56122	-7.50232	7.663199	7.316782	2.93	-0.3 pps
Labour productivity (real GDP/person employed)	5.930048	7.3362	-4.69449	-0.88017	2.934704	-1.17493	:	-4.1 pps
Nominal unit labour costs	:	:	2.9	-2.4	0.9	6.4	:	5.5 pps
14 - Sectoral breakdown of unit labour costs								
Business economy	23.45	21.425	11.3	6	7.125	6.2	:	-0.9 pps
15 - Sectoral breakdown of compensation per employee								
Manufacturing	27.62356	36.30875	-29.087	8.483415	:	:	:	
Construction	6.991908	37.90615	15.33494	-28.751	12.52191	3.659221	:	-8.9 pps
Trade, transport and information services	12.73029	29.58039	3.403207	-7.91178	9.520307	6.09644	:	-3.4 pps
Finance and business services	41.91938	13.34324	-0.11896	10.05196	8.837704	9.8324	:	1.0 pps
Non-market related services	27.59995	34.26348	1.020656	-7.2396	-11.8374	5.706105	:	17.5 pps

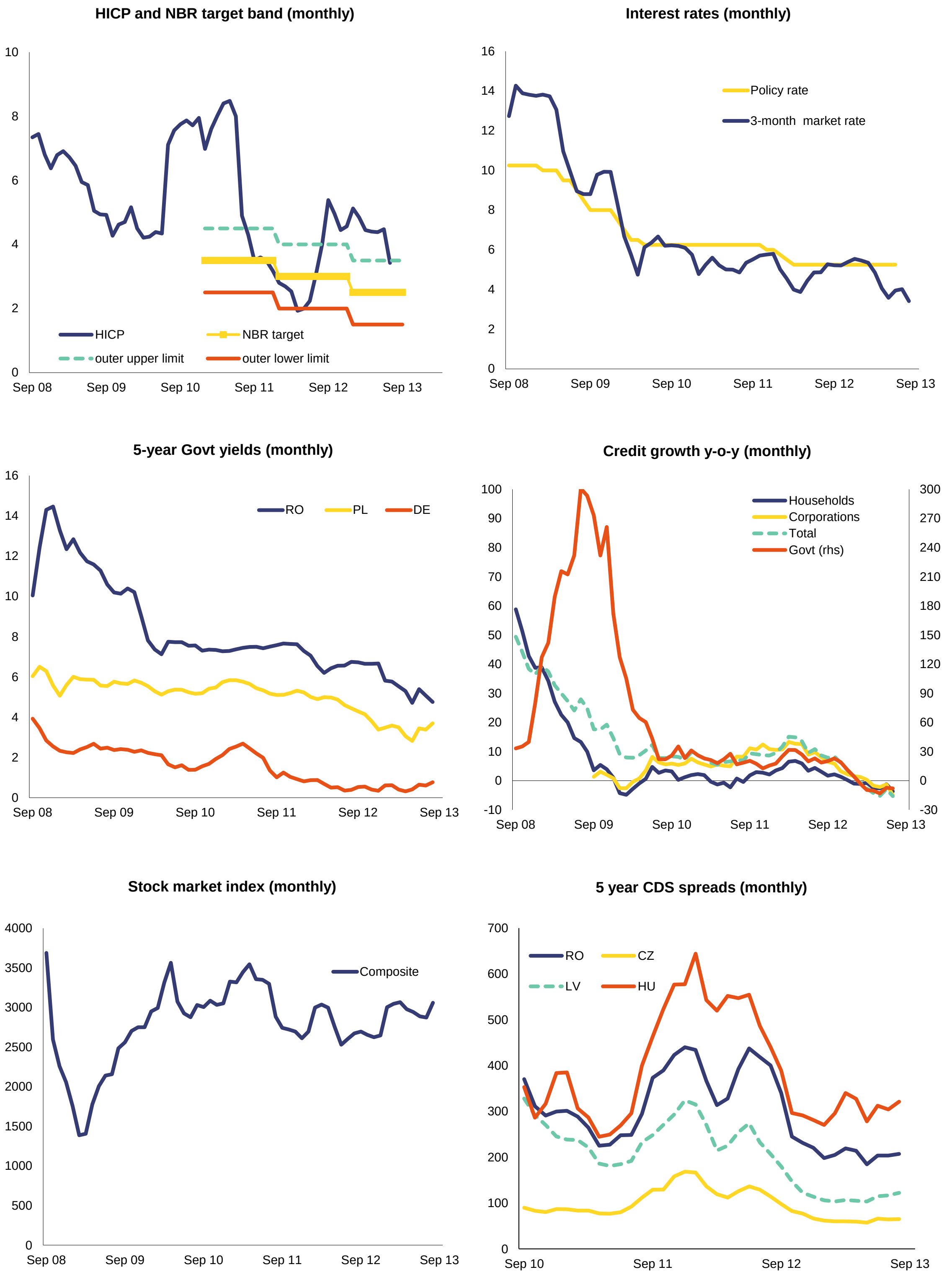
Source: European Commission

Graph A4.1: **Key economic indicators, 2007-2013**



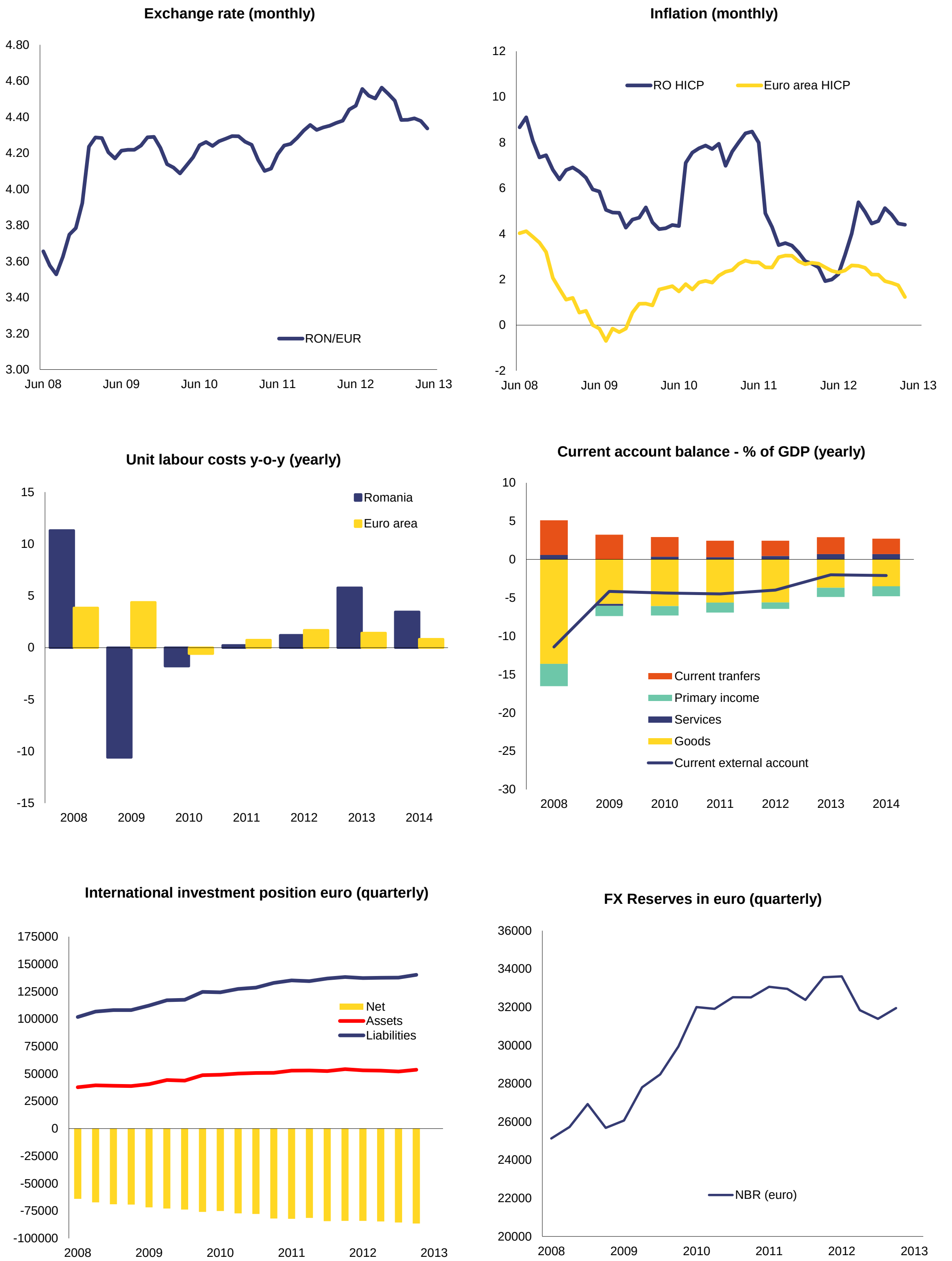
Source: European Commission, National authorities

Graph A4.2: **Monetary and financial market indicators, 2007-2013**



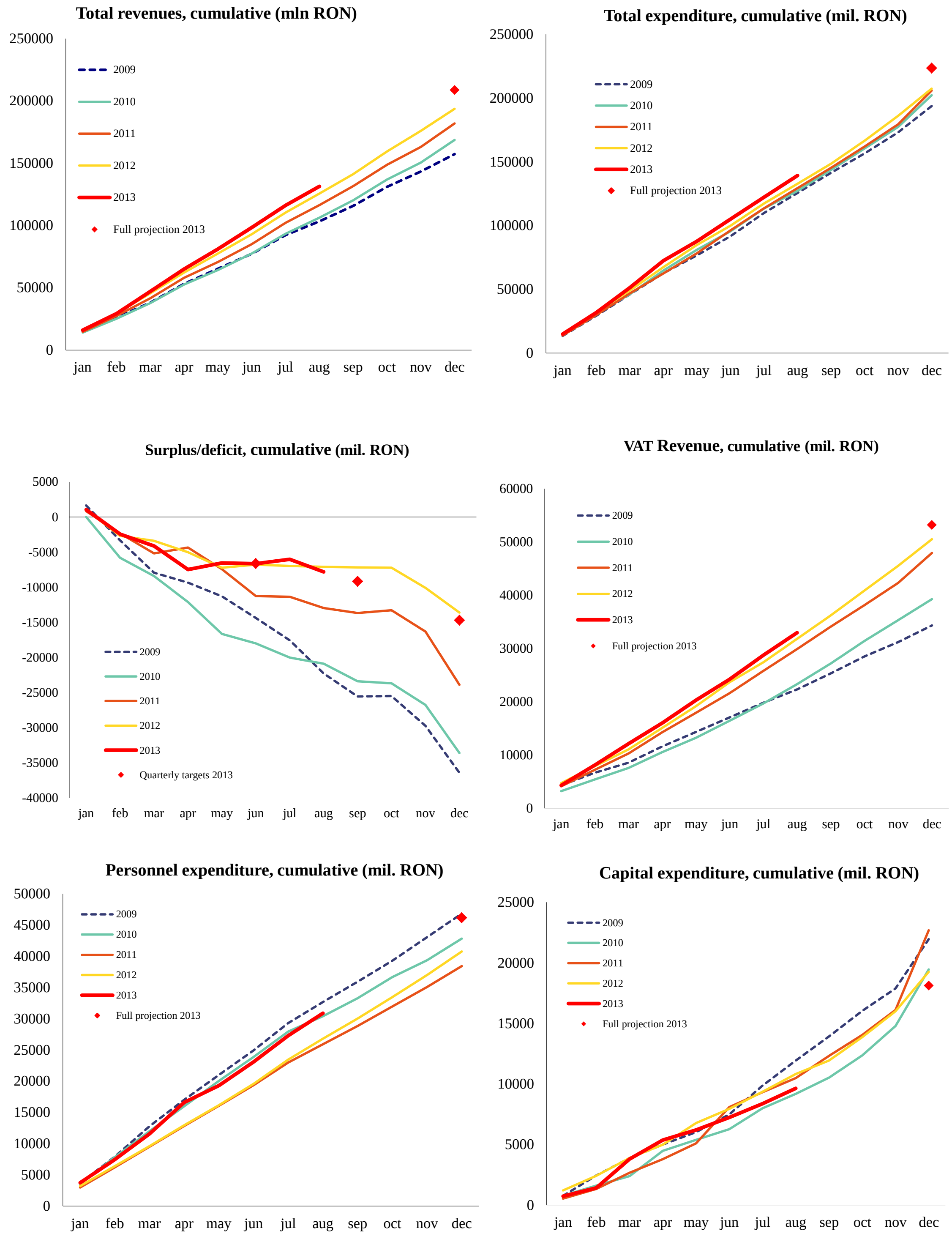
Source: European Commission, National authorities

Graph A4.3: **Price and competitiveness indicators, 2007-2013**



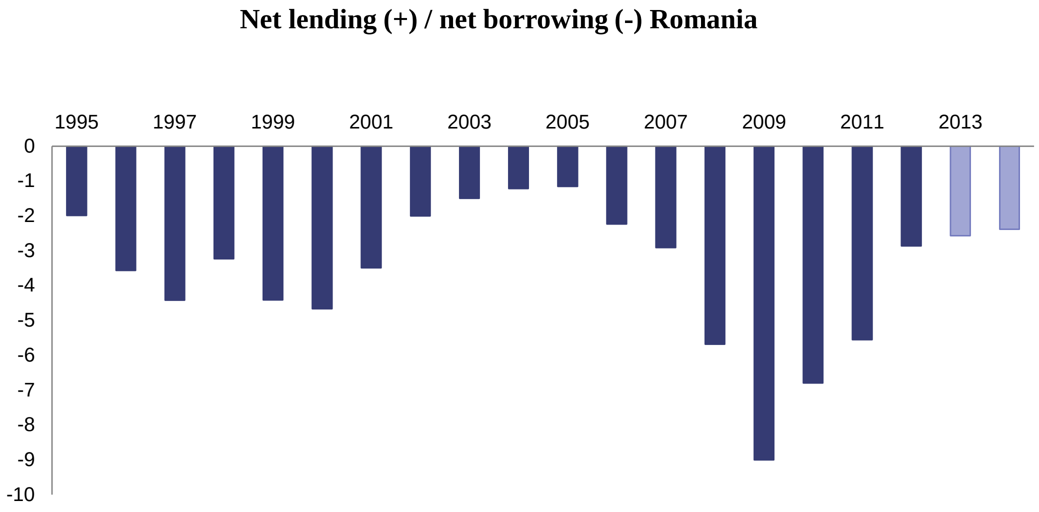
Source: European Commission, National authorities

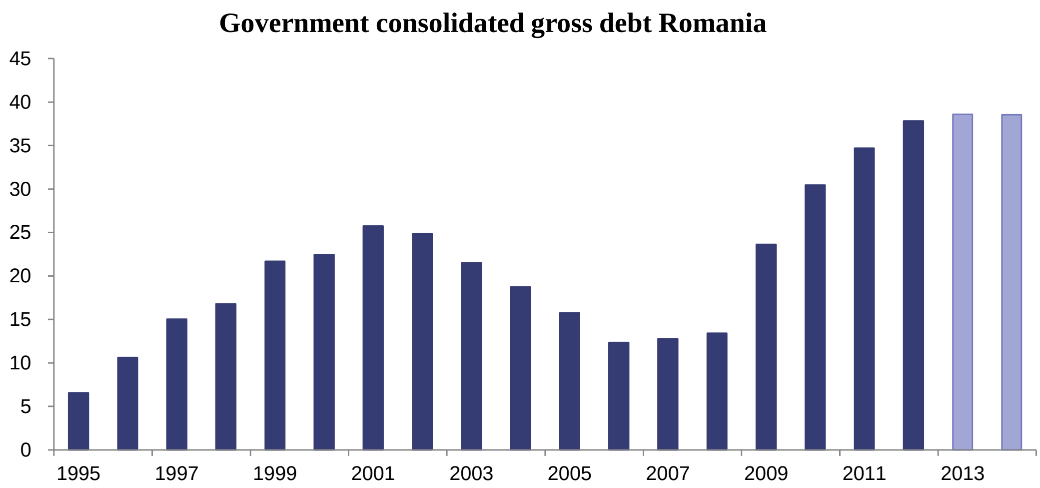
Graph A4.4: **Budgetary execution, 2009-2013**



Source: European Commission, National authorities

Graph A4.5: **Evolution in government deficit and debt (ESA definition)**

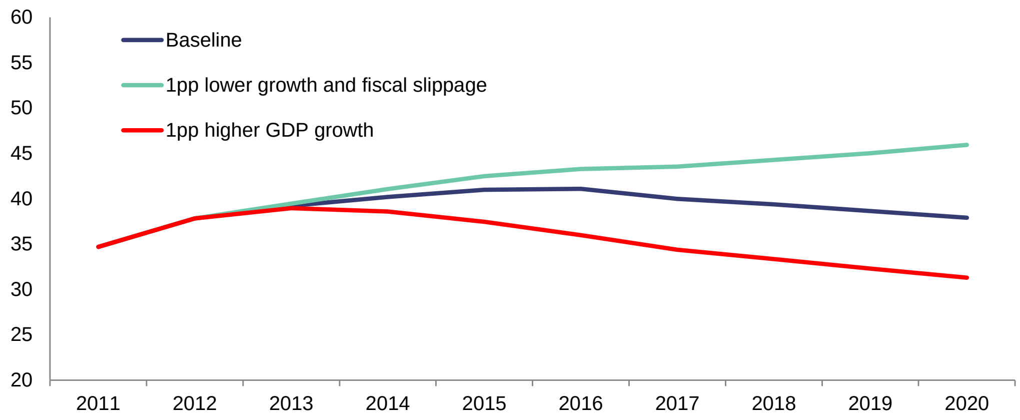




Source: European Commission

Note: Figures for 2013 and 2014 reflect the EC Spring forecast.

Graph A4.6: **Debt sustainability scenarii (Public sector debt in %GDP)**



Source: Commission services

Note: In the baseline, the MTO is reached in 2015 and the primary budget is balanced from 2017 onwards. Interest rates for new issuances are assumed at 5%. The GDP growth path is based on the Commission's forecasts as set out in Table A.4.1 and the Commission internal calculations for long run trends. "Fiscal slippage" in the downside scenario refers to a deterioration of the primary balance by 0.25% of GDP compared to the baseline. Inflation is expected to decrease further until, from 2015 onwards, a plateau at 3.2% is reached.

ANNEX 5
List of abbreviations

ANRE	National Energy Regulatory Authority
BG	Bulgaria
BoP	Balance of Payments
CA	Current Account
CDS	Credit Default Swap
CF	Cohesion Fund
CZ	Czech Republic
DGF	Deposit Guarantee Fund
DMO	Debt Management Office
DPL/DDO	Development Policy Loan with a Deferred Drawdown Option
EA	Euro Area
EAFRD	European Agricultural Fund for Rural Development
EBCI	European Bank Coordination Initiative
EC	European Commission
EDP	Excessive Deficit Procedure
EMTN	European Medium Term Notes
ERDF	European Regional Development Fund
ESA	European System of Integrated Economic Accounts
ESF	European Social Fund
EU	European Union
FDI	Foreign Direct Investment
FR	Functional Reviews
FRL	Fiscal Responsibility Law
FX	Foreign Exchange
GDP	Gross Domestic Product
GSG	General Secretariat of the Government

GVA	Gross Value Added
HICP	Harmonised Index of Consumer Prices
HU	Hungary
IFRS	International Financial Reporting Standards (www.ifrs.org)
ILO	International Labour Organisation
IMF	International Monetary Fund (www.imf.org/external/country/rou/index.htm, www.fmi.ro)
IPO	Initial Public Offering
JEREMIE	Joint European Resources for Micro to Medium Enterprises
LoI	Letter of Intent
MEFP	Memorandum of Economic and Financial Policies
MIP	Macroeconomic Imbalances Procedure
(S)MoU	(Supplemental) Memorandum of Understanding
MTO	Medium Term Objective
NBR/BNR	National Bank of Romania/ Banca Naţională a României (www.bnr.ro)
NIIP	Net International Investment Position
NIS	National Institute of Statistics
NMS	New Member States
NPL	Non-Performing Loans
OP	Operational Programme
PL	Poland
PNDI	National Programme for Infrastructure Development / Programul Naţional de Dezvoltare a Infrastructurii
PPP	Public-Private Partnership
PSC	Point of Single Contact
RAS	Romanian Accounting Standards
REER	Real Effective Exchange Rate

ROA	Return on Assets
ROE	Return on Equity
RON	ROmanian New lei (leu/lei)
SA	Seasonally Adjusted
SAPARD	Special Accession Programme for Agriculture and Rural Development
SBA	Stand-by Arrangement
SCF	Structural and Cohesion Funds
SDR	Special Drawing Rights
SGP	Stability and Growth Pact
SME	Small and Medium size Enterprise
SOE	State-Owned Enterprise
TFP	Total Factor Productivity
TMU	Technical Memorandum of Understanding
WB	The World Bank (www.worldbank.org)
YOY (y-o-y)	Year-on-year

ANNEX 6
Programme documentation

A6.1. MEMORANDUM OF UNDERSTANDING (MOU)

MEMORANDUM OF UNDERSTANDING between THE EUROPEAN UNION and ROMANIA

1. On 22 October 2013, the Council of the European Union adopted a decision making available precautionary medium-term financial assistance of up to EUR 2 billion for Romania until 30 September 2015.([20]) The EU assistance for Romania under the Balance of Payments (BoP) facility comes in conjunction with IMF support through a Stand-by Arrangement (SBA) in the amount of SDR 1,751.34 million (about EUR 2 billion, 170% of Romania's IMF quota), approved on 27 September 2013, which the authorities will also treat as precautionary. The World Bank (WB) has made EUR 1 billion available under a Development Policy Loan (DPL) with a deferred drawdown option (DDO) valid through December 2015. In addition, the WB will continue providing earlier committed support of EUR 891 million, of which EUR 514 million is still to be disbursed mainly in support of Social Assistance Modernization project (EUR 300 million), a Revenue Modernization project (EUR 70 million), and the agricultural sector (EUR 61 million). The WB is also preparing a Health Sector Operation expected to be submitted for Board Approval late this calendar year or in the first half of 2014. A new Country Partnership Agreement between Romania and the WB is being prepared and is expected to be submitted for Board Consideration in the first half of next year. It will spell out any additional financial support that might be provided over the next 3 years to public investments or the policy agenda. The EU precautionary assistance will be conditional upon the implementation of a comprehensive economic policy programme, with a particular focus on structural reform measures including those country-specific recommendations of the EU semester aiming at reducing remaining vulnerabilities and at increasing the resilience and the growth potential of the Romanian economy. These measures relate to administrative capacity, product market reforms, the business environment, labour markets, pensions, state-owned enterprises, and healthcare. In parallel, the programme ensures the continuation of fiscal consolidation, the reform of the tax administration, improvements in public financial management and control as well as external, monetary, financial stability, and financial market reform. In its totality, the programme is geared towards: (i) Romania reaching its medium-term budgetary objective by 2015, in line with Stability and Growth Pact requirements; (ii) improving growth potential; and (iii) decreasing the future likelihood of renewed excessive structural imbalances in the Romanian economy, including through strengthening governance where needed.

2. EU financial assistance will be of a precautionary nature, i.e. the overall loan amount would only be made available, upon a request for activation from Romania, in case of an unforeseen marked deterioration in the economic and/or financial situation due to factors outside the control of the authorities, leading to the opening of an acute financing gap. The availability for activation of the assistance is subject to, amongst others, the entry into force of the present Memorandum of Understanding (MoU) and the corresponding Precautionary Loan Facility Agreement (PLFA). The parties will conclude and sign the PLFA, containing the main terms and conditions applicable to all the potential disbursements within the precautionary EU financial assistance programme, but any disbursement would be subject to the activation of the facility. The Commission will decide, after having consulted the EFC, on the activation of the programme and on the amount to be made available within the EUR 2 billion ceiling for disbursements in the form of instalments.

3. Precautionary EU financial assistance is made available for activation following the request of Romania for a support programme continuing the previous precautionary BoP facility of EUR 1.4 billion.([21])

([20]) Council Decision (2013/531/EU), OJ L286.
([21]) Council Decision 2011/288/EU of 12 May 2011 (OJ No. L132 of 19.5.2011).

4. Activation of the precautionary assistance, and the subsequent provision of loan instalments, shall also be conditional on a positive assessment by the Commission of the implementation of the economic reform programme of the Romanian Government at six-monthly intervals. Specific economic policy criteria will be attached to these reviews. A detailed description of those criteria is given in Annex 1 of the MoU. The overall objectives of the programme are the following:

A: Fiscal consolidation

Following the correction of its excessive deficit, Romania is expected to reduce its structural budget balance by at least 0.5% per year until it reaches its medium-term objective of a structural general government deficit of 1% of GDP by 2015, and maintain it thereafter. Furthermore, the programme will continue efforts to prevent a new build-up of government arrears, both at central and local government level. The public sector wage bill will need to stay on a sustainable footing, limiting wage growth as well as public sector employment levels.

B: Fiscal governance and structural fiscal reform

The programme will support the Romanian government to further strengthen the fiscal governance framework. This will ensure that fiscal consolidation is politically and institutionally anchored. The implementation of the Fiscal Compact is crucial in this respect. The Fiscal Council scrutinises fiscal policy. Improvements in multi-annual budgetary planning will ensure a more sustainable fiscal policy.

Fiscal governance will strongly benefit from on-going Technical Assistance provided by the IMF and the World Bank in the area of Public Financial Management and Control. The implementation of a commitment control system, which will be rolled out in several steps, will ensure the reduction and control of arrears. In the health sector, budget control mechanisms will be strengthened through improved reporting and monitoring frameworks, in particular with regard to hospitals and pharmaceutical spending in order to avoid a re-accumulation of payment arrears. Prioritisation of public investments will be strengthened, to enhance the country's growth potential.

C: Public debt management

The authorities will carry out necessary steps to improve public debt management with a view on reducing risks and building up the yield curve for sovereign debt.

D: Financial sector regulation and supervision

In the financial sector, authorities will continue upgrading the bank resolution framework and the legislation on the Deposit Guarantee Fund by amending GO 39/1996 and GEO 99/2006. To speed up the process of balance sheet cleaning, the National Bank of Romania (NBR) has clarified the provisions applicable to the write-off of loans with the Romanian Banking Association and will produce a comprehensive analysis of the asset quality in the banking sector. In order to further develop the capital market and diversify the sources of funding for banks, authorities will amend the covered bonds legislation. Preserving credit discipline and avoiding moral hazard among debtors contributes significantly to enhancing financial stability. Therefore, the government will continue refraining from adopting legislative initiatives (such as the personal insolvency law) and promoting provisions in the debt collection law, which would undermine credit discipline. Authorities will consult extensively with all relevant stakeholders, having in view also the impact assessment finalised by the NBR, on the new provisions on abusive clauses in the law for the application of the civil procedure code and will ensure that court cases involving abusive clauses are dealt with by higher ranking courts or by a unique specialised court and will take all other necessary measures to ensure a harmonised application of these provisions. To strengthen the supervision of the non-bank financial market and foster consumer protection, authorities will ensure that the legislation on the integrated non-bank financial regulator, the

Financial Supervisory Authority/Autoritatea de Supraveghere Financiară (FSA/ASF), will be amended to comply with international best practices.

E: Structural reforms

The structural reforms aim at improving market functioning, at increasing resilience to external shocks and at strengthening Romania's long-run growth potential. The structural reform agenda of this programme covers part of the country-specific recommendations addressed to Romania in the context of the European Semester. This agenda does not exempt the Romanian government from fully implementing the country-specific recommendations of the EU semester which are not covered in this programme.

The restructuring of state-owned enterprises (SOEs), including privatisation, will be stepped up in order to reduce risks to the general government budget from accumulated arrears and operational losses, while increasing the financial viability of most of these companies' operations. Authorities will take measures to strengthen corporate governance of SOEs, including in the financial sector.

In the energy sector outstanding measures agreed under the two previous programmes will be implemented, among which the implementation of the roadmaps for the gas and electricity market liberalisation.

One of the cornerstones of this programme is the enhancement of the efficiency and effectiveness of the country's public administration. Moreover, the Romanian authorities would be invited to report every six months to the Economic and Financial Committee (EFC)/Economic Policy Committee (EPC) on the progress made in this area.

Improvement of the business environment and facilitating access to finance for the small and medium-size enterprises (SMEs) is another important pillar of the structural reform agenda of the programme. The programme aims at reducing administrative burden for the SMEs, facilitating their access to bank and equity capital, reducing the legal uncertainty by improving the land and property registration and supporting SMEs when going abroad. Furthermore, the programme supports the reform of the regulatory framework related to innovation, with the view to attract foreign direct investment in research and innovation activities.

In the field of labour markets, the programme supports the completion of the 2010 pension reform by equalising the pensionable age for men and women.

F: Monetary Policy

Monetary policy will remain geared towards price stability with a view to inflation staying within the National Bank of Romania’s inflation target band (2.5% ± 1 percentage point).

5. In case Romania requests the activation of the European Union (EU) assistance to cope with the emergence of an acute financing gap, the Romanian Government shall make this request in writing to the Commission. Any such request for activation, as well as any request for disbursement, is to be made no later than 30 September 2015. The Commission will assess financing needs in close co-operation with the International Monetary Fund (IMF). After the EFC has delivered its opinion, the Commission shall decide on the amount to be made available for disbursement in the form of instalments. The funds of the overall programme will be made available in a maximum of 2 instalments.

6. Any changes in conditionality will be specified in a supplement to this MoU (Supplemental Memorandum of Understanding).

7. In case a disbursement has taken place, the EFC shall be kept informed by the Commission of possible refinancing of the borrowings or restructuring of the financial conditions.

8. If Romania requests the disbursement of an instalment under the PLFA and such a disbursement takes place, the European Central Bank shall act as an agent to the Commission and shall transfer the proceeds of the loan to a euro account of the Ministry of Public Finance of Romania (the Treasury), held at the NBR, that will act as an agent for Romania.

9. The updates to the Romanian Convergence Programme and the Romanian National Reform Programme under the EU 2020 Strategy shall reflect and be fully in line with the objectives and actions required under the economic reform programme committed by the Romanian Government for the purposes of this EU assistance. While the balance-of-payments programme comprises specific actions that fall under the EU Council's country-specific recommendations, it does not in any way substitute for other actions covered by the country-specific recommendations to which Romania is expected to provide adequate follow-up.

10. The Ministry of Public Finance shall retain a special account with the NBR for the management of the European Union's financial assistance. This special account will be a sub-account of the euro-account of the Ministry of Public Finance within the NBR.

11. During the availability period of the assistance, the Romanian authorities shall make available to the Commission without delay all the relevant information for the monitoring of its economic and financial situation and for the assessment of progress in economic conditions and reform measures as specified in the Technical Memorandum of Understanding negotiated with the authorities and submitted by the latter together with their Letter of Intent (LoI) and the Memorandum of Economic and Financial Policies (MEFP). Prior to the acceptance of the disbursement of any instalment, there will be a compliance report by the Commission, the favourable outcome of which is a precondition for each of the instalments.

12. Investigation and satisfactory treatment of any suspected and actual cases of fraud, corruption or any other illegal activity in relation to the management of the EU financial assistance shall be ensured. All such cases, as well as measures related thereto taken by national competent authorities, shall be reported to the Commission without delay.

13. Without prejudice to Article 27 of the Statute of the European System of Central Banks and of the European Central Bank, the European Court of Auditors shall have the right to carry out any financial controls or audits in Romania that it considers necessary in relation to the management of this assistance. The Commission, including the European Anti-Fraud Office, shall thus have the right to send its own officials or duly authorised representatives to carry out technical or financial controls or audits that it considers necessary in Romania in relation to the assistance.

14. An independent ex-post evaluation of the assistance may be carried out by the Commission or its duly authorised representatives. The Romanian authorities are committed to supply relevant information for the evaluation. The draft evaluation report will be made available to them for comments.

15. The Romanian authorities will ensure, as appropriate, close co-operation with the Commission and the EFC.

16. The Romanian authorities commit to consult Commission staff before adopting new measures that may have implications for the objectives of the programme. In particular, they will consult in a timely manner and provide all necessary information regarding any measures and reforms that may have an impact on fiscal developments. The Romanian authorities will also consult the ECB on any draft

legislative provision in its fields of competence, as stipulated in Articles 127 (4) and 282 (5) of the Treaty on the Functioning of the European Union.

17. The Annexes form an integral part of this Memorandum of Understanding.

18. All notices in relation with the Memorandum shall validly be given if in writing and sent to:

For the European Union

European Commission

Directorate General for Economic and Financial Affairs, B-1049 Brussels

Fax No.: +32 2 299 35 23

For the Prime Minister

Prime Minister's Office

1, Piaţa Victoriei, Sector 1, 011791 Bucharest

Fax No.: +40 21 319 15 88

For the Ministry of Public Finance of Romania

Ministry of Public Finance of Romania

17, Strada Apolodor, Sector 5, 050741 Bucharest

Fax No.: +40 21 312 16 30

For the National Bank of Romania

National Bank of Romania

25, Strada Lipscani, Sector 3, 030031 Bucharest

Fax No.: +40 21 312 62 60

19. For Romania, the MoU shall become effective after completion of internal procedures required under the Laws of Romania. The MoU may be amended upon mutual agreement of the parties in the form of a Supplement. Any such supplement will be an integral part of the MoU and become effective according to the same procedures as the MoU.

Done in Brussels on 6.11.2013 and in Bucharest on 5.11.2013 in five originals in the English language.

ROMANIA

Represented by

[Signed]

Victor-Viorel Ponta

The Prime Minister

[Signed]

Daniel Chiţoiu

Deputy Prime Minister and Minister of Public Finance

[Signed]

Liviu Voinea

Minister Delegate for Budget

[Signed]

Mugur Isărescu

Governor of the National Bank of Romania

EUROPEAN UNION

Represented by

EUROPEAN COMMISSION

[Signed]

Olli Rehn

Vice-President of the European Commission

Annex 1 to the MoU: Specific Economic Policy Criteria

A. Fiscal consolidation

No.	Measures
1	Continue fiscal consolidation towards the achievement of the medium term objective of a structural deficit of 1% of GDP by 2015 and respect this thereafter, in line with Stability and Growth Pact requirements.

B: Fiscal governance and structural fiscal reform

No.	Measures
2	Preserve the achievements of the previous two programmes, implement the further measures agreed under those programmes, and fulfil any remaining parts of yet unfulfilled conditionality. This applies in particular to: i) the Unified Wage Law (and the related suppression of the "stimulente"); ii) the medium-term sustainability of the public sector wage bill; iii) the pension reform; and iv) the reduction of payment delays in the health sector.
3	Strengthen the fiscal governance framework. Ensure the implementation and enforcement of the Fiscal Compact provisions, as well as adherence to best practice in terms of fiscal governance. Strengthen the Fiscal Council's capacity to contribute to the improvement of fiscal policy. Increase its role in assessing and publishing revenue projections after each macroeconomic forecast round (autumn and spring) and in the calculation of the deficit target ahead of the start of the budgeting process and the publication of its opinion thereon.
4	Further strengthen multi-annual budgetary planning. Improve the content of the Fiscal Strategy, inter alia by increasing transparency regarding assumptions and including an analysis of fiscal risks and liabilities. Ensure that the line ministers are involved in the medium-term budget planning process, by designing and implementing procedures for internal coordination arrangements. Improve the database for budget planning. Increase the capacity of the Ministry of Public Finance to estimate the structural deficit and the structural impact of measures. In order to comply with existing fiscal rules, strengthen the capacity to perform fiscal impact assessments of legislative proposals, and improve the impact assessment's quality and binding nature.
5	Improve the prioritisation of public investments, the enforcement of consistency of capital spending with budget envelopes and the alignment of investment planning with multi-annual budgetary planning. Set up a list of prioritised investments based on a sound cost/benefit analysis at central government level. Strengthen the Ministry of Public Finance (MoPF) with respect to the staffing of its Public Investment Evaluation Unit and to its role in project selection to enable it to guide the prioritisation and selection of investment projects. A milestone will be the government's approval of an updated list of priority investments before the end of 2013.
6	Establish an effective commitment control system for all levels of government in order to control overall expenditure and prevent the accumulation of payment arrears. The commitment control system will cover expenditures on goods and services as well as investments. A crucial milestone on this path is the rollout of the web based application at the MoPF and at least one additional unit at both the central and local government levels by end-January 2014.

No.	Measures
7	Establish a regular flow of fiscally-relevant data to the Ministry of Public Finance. A protocol will be set up, also to guide reporting obligations to the European Commission (Commission) and the International Monetary Fund.
8	Improve tax collection by implementing a comprehensive tax compliance strategy, in line with the respective World Bank project. In particular, define a services catalogue for the taxpayers by July 2014. Further, improve the VAT reimbursement procedure by reviewing the criteria for ex-ante control, increase the e-filing rate for the tax returns for companies from 89% to 93% and improve the filing compliance by mid-2015.
9	Reduce arrears for state-owned enterprises through restructuring to be undertaken in line with the EU state aid rules and prevention of future losses. In particular, reduce the stock of outstanding payments not made by due date of SOEs owned by the central government from 8.2 bn lei at end-June 2013 to 5.6 bn lei at end-December 2013, as specified in the Technical Memorandum of Understanding. Also, all SOEs should file, in accordance with existing regulations, quarterly financial information with the Ministry of Public Finance by the 25th day following quarter end.

C: Public debt management

No.	Measures
10	Update and publish, before end-March, the public debt management strategy (DMS) and the auction calendar on yearly basis, as well as quarterly announcement of the government securities auctions with indicative volumes by debt instruments (T-bills and bonds). The DMS should detail instruments, maturities, auction frequency that would be adherent to the maturity extension, risk management and cash buffer targets. It should also include a plan to improve cash management.
11	Continue to consolidate the financing buffer to protect against unforeseen external shocks at a level covering a number of months of gross financing. For 2013 this will cover four months of gross financing needs.
12	Finalise, by end-March 2014, the electronic auction system for domestic primary issuances (with the National Bank of Romania (NBR) acting as the agent of the MoPF).
13	Introduce, by end-September 2014, an electronic trading platform to monitor transactions in the secondary market.
14	In line with the measures considered in the DMS to increase the transparency and predictability of the government securities market, the MoPF should organise, as of end-2013, quarterly consultations with primary dealers, mutual funds, pension funds, and life insurance companies as well as quarterly conference calls with the international investor community and non-deal road shows.
15	Enlarge, as of end-2013, the investor base and facilitate the access of individuals to government securities.
16	To support a benchmark building strategy and increase the liquidity of the domestic government securities market, the MoPF will establish, by end-September 2014, the legal, procedural and operational framework necessary to carry out buybacks, bond exchanges, and

No.	Measures
	repo operations.
17	Establish, by end-2014, involvement of the Treasury in a central counterparty (CCP) clearing house.

D: Financial sector regulation and supervision

No.	Measures
18	Corporate governance of the Deposit Guarantee Fund in the Banking System will be strengthened, in particular to avoid any perceived conflict of interest for board members and executive directors. Furthermore, authorities will amend the provisions of Government Emergency Ordinance (GEO) 99/2006 on stabilisation measures and Government Ordinance (GO) 39/1996 after consultation with the Commission on the interpretation of the new EU state aid rules by end-2013 in line with CRD IV implementation deadline. Subsequently to the amendments to the banking law, the NBR will amend the internal procedures for bridge-banks by end-2013. The NBR will also continue updating its contingency planning on an on-going basis as well as the bank-by-bank contingency plans.
19	To speed up the process of balance sheet cleaning, the NBR has clarified with the Romanian Banking Association that the only provisions in place for the write-off of loans are those foreseen in the IAS 39 on the de-recognition of financial assets and which do not necessarily request banks "to exhaust all legal means" in order to write off. Any amendments to the current treatment of the prudential filters will be agreed with the Commission and the IMF. Furthermore, authorities will finalise by end-December 2013 an impact assessment on the fiscal cost resulting from the tax deductibility of sales of intra-group bank receivables.
20	The NBR will continue to closely monitor bank practices to avoid evergreening as well as the assessment of credit risk of restructured loans, so that they remain prudent and in line with good international practices. The NBR has collected supervisory data on restructured loans, including loans to SOEs, on a quarterly basis by end-September 2013. The NBR will conduct a comprehensive analysis of the asset quality in the banking sector and produce a report containing granular information, migration matrixes and a vintage analysis of the banks' non-performing loans (NPLs) by end-October 2013.
21	The NBR will perform by end-December 2013 on-site inspections on a selected sample of 20 large, medium and small-sized banks focused on the strategies of banks to deal with impaired assets. These inspections will cover the following aspects: (i) the adequacy of IT systems to deal with impaired assets; (ii) the NPL work-out strategies of banks; (iii) the restructuring/rescheduling policies applied by banks. The analysis of the banks’ IT adequacy will be finalised by end-2013. In a second phase, on-site inspections in the remaining banks will take place until end-March 2014. In consultation with the Commission and the IMF, an NPL resolution action plan will then be agreed by end-May 2014.
22	In order to further develop the capital market and diversify the sources of funding for banks, authorities will adopt the amendments to the covered bonds legislation by end-2013 through Government Ordinance, while appropriate safeguards to preserve financial stability are implemented. Any possible prolongation of the "Prima Casa" programme after its expiry should be restricted to mortgage lending denominated in RON. This will help develop a pool of long-term assets denominated in RON thereby fostering covered bonds issuances denominated

No.	Measures
	in domestic currency.
23	As preserving credit discipline and avoiding moral hazard among debtors contributes significantly towards enhancing financial stability, authorities will continue refraining from adopting legislative initiatives (such as the personal insolvency law or proposals for the debt collecting law), which would undermine credit discipline. Furthermore, in order to avoid threats to financial stability, authorities will consult extensively with all relevant stakeholders, having in view also the impact assessment finalised by the NBR, on the new provisions on abusive clauses in the law for the application of the civil procedure code. Authorities will ensure that court cases involving abusive clauses are dealt with by higher ranking courts or by a unique specialised court and will take all other necessary measures to ensure a harmonised application of these provisions, such as training of judges. Moreover, as corporate insolvencies are increasingly fuelling the still on-going deterioration in asset quality, the NBR together with the Romanian Banking Association will explore possibilities for setting up a database of shareholders of companies in insolvency as well as implement more effective data reporting of the Association of Insolvency Practitioners.
24	To strengthen the supervision of the non-bank financial market and foster consumer protection, authorities will ensure that the legislation on the ASF/FSA (Autoritatea de Supraveghere Financiară/Financial Supervisory Authority), will be amended by end-September 2013 to comply with international best practices, in particular regarding the size of the managing and council board which should be restricted to maximum 9 members, minimum required professional qualifications of ASF board members, statutory protection of supervisory staff and of the institution as well as avoidance of conflicts of interest, notably the connection of these members with Parliament. Furthermore, the ASF: (i) will swiftly complete the integration of the former three supervisory authorities for securities, insurance and pensions while ensuring the smoothing functioning of supervisory activities; (ii) will develop a human resources policy geared first and foremost towards qualified staff to perform on-site supervision, off-site analysis, validation of internal models; (iii) will further enhance transparency and public accountability by ensuring an adequate public disclosure of all fees and commissions charged to the supervised entities; and (iv) will hire, in September 2013, a professional and independent consultancy company to assess staffing levels and staff. Based on this, within two months of the consultancy company's assessment, an action plan will be developed to streamline the ASF with a view to realising the savings in 2014.
25	The authorities will swiftly implement the World Bank recommendations on the ROSC (Report on the Observance of Standards and Codes), and following the comprehensive public consultation in September 2013 as well as with the Commission, the IMF and the World Bank, will send the amended insolvency code draft for approval to parliament by end-October 2013. All relevant stakeholders will be consulted before the insolvency code is approved by parliament.

E: Structural reforms

No	**Measures**
	Administrative capacity
26	Implement the Action Plans adopted in response to the findings of the functional reviews carried out in 2010-2011 in a timely manner. Continue to report on their implementation on a quarterly basis. Review and update the action plans by end-2013.
27	Establish a central delivery unit in line with the World Bank project by December 2013 to improve the government-wide policy prioritisation, implementation and coordination with particular reference to the implementation of the EU Council's country-specific recommendations not covered in this assistance programme.
	Product markets
28	Preserve the achievements of previous two programmes and implement outstanding measures agreed under those programmes: - continue the implementation of the roadmaps for gas and electricity market liberalisation. Complete deregulation of electricity prices for non-residential consumers by 1 January 2014. For households, implement the deregulation steps for electricity prices in January and July 2014 and in January and July 2015, as set out in the electricity roadmap, with the share of electricity acquired from competitive market reaching 50%. For natural gas, continue price deregulation as planned in the gas roadmap with intermediary steps to be taken in October 2013, January, April, July and October 2014. If necessary, continue gas price liberalisation for non-residential consumers in 2015 as to achieve full price deregulation by end 2015. For residential consumers, continue gas price deregulation in 2015 with intermediary steps taken in January, April, July 2015 by which 52% of gas price convergence with the market should be achieved. Allow the pass-through mechanism for electricity and gas purchases by the supply companies to be applied. - continue the development of gas and electricity trading platforms; - continue the unbundling of energy transmission and dispatch operators; - improve cross-border integration of energy networks and provide for security-of-supply measures. Preserve the achievements of the previous two programmes and implement outstanding policy commitments in the transport area: - introduce performance schemes related to delays between the infrastructure company, on the one hand, and the passenger/freight companies, on the other hand, by end-2013; - introduce incentives for infrastructure manager to reduce unit costs and charges in CFR Infrastructure by end-2013; - facilitate improved payment of infrastructure access and electricity charges from the state-owned passenger rail company (CFR Calatori) and CFR Marfa through reforms of those enterprises and settle outstanding debts among the three main railway companies;

No	Measures
	- further amend the formula for calculation of the PSO to give more weight to passenger-train kilometers travelled starting in January 2014.
	Business environment
29	Bring the national "Better regulation strategy" in line with the EU smart regulation agenda by making impact assessments of the new legislation related to business activities obligatory by end-2013. Develop a common methodology for impact assessments including the "SME test"' and establish a quality control mechanism by mid-2014. Implement pilot projects in four selected ministries by end-2014.
30	Further reduce administrative burdens on SMEs by: (i) making online submission and payment of taxes fully operational by mid-2014; and (ii) simplifying procedures regarding property registration and construction permits through a reduction of 25% before end-2013 of the information obligation procedures and through making electronic submission possible by mid-2014. To reduce delays, introduce standard deadlines and automatic approval after the deadline by mid-2014. To ensure that information submitted once to the administration is not requested again by another service, introduce data sharing within the e-government system by end-2014. Streamline the "one-stop shop" and the "point of single contact" into fully-operational and interconnected electronic platforms with a single entry point.
31	Increase the number of properties registered in the digitalised national land registry from currently 15% to 25% by mid-2015. To this end: (i) by end-2013, amend the law on the cadastre to allow for simplified procedures for systematic registrations in particular by using public display as quality control; (ii) find appropriate arrangements for a swift resolution of undebated inheritance cases; (iii) strengthen project management capacities of the national agency for the cadastre and land registry by mid-2014 with the view to implement the multi-annual land registration project; and (iv) increase the number of solved land disputes per year by 10% by end-2014 including through out-of-court dispute resolutions. For concession and leasing contracts related to the state domain make land and property registration compulsory prior to contract signature.
32	By end-2013, adopt a law on inventions by employees so as to encourage investment, in particular from private sources, in patenting activities. By end-2014, provide guidelines, in line with international best practices, including on the distribution of benefits arising from the commercial exploitation of the invention.
33	To improve access to finance for SMEs, extend the duration of the Mihail Kogălniceanu programme beyond 2013 to a multi-annual programme and strengthen the existing support schemes by rendering the National Loan Guarantee fund for SMEs more effective, especially as regards the maturity, price, and rollovers of the guaranteed loans, as well as the implementation process for the guarantee execution. Together with the Romanian Banking Association, introduce minimum transparency standards defining a minimum set of information regarding bank-lending conditions, to be published by banks by mid-2014. Strengthen services, including those related to access to finance that are provided by the SME territorial offices by increasing the number of assisted companies from 2013 to 2014 by 20%. To diversify sources of SME financing, adopt legislation on equity financing with risk sharing options, in particular as regards venture capital and business angels by mid-2014.
34	Improve export promotion and development for SMEs by starting a "passport-to-exports" scheme by mid-2014 and by making fully operational the pilot regional export centres by

No	Measures
	end-2014. Reinforce the electronic trade portal and improve the effectiveness of the trade counsellor schemes outside Romania with 30% more companies assisted in 2014 than in 2013.
	Labour markets and pensions
35	Preserve the achievements of the previous two programmes, in particular by monitoring the implementation of the Labour Code and Social Dialogue Code and ensuring that any further amendment to labour legislation will be undertaken in consultation with all stakeholders through ordinary legislative procedures.
36	Considering the funding needs of the healthcare system and the possible need to adjust health insurance contributions, conduct a comprehensive review of labour taxation with a view to reducing, in a budget-neutral manner, the effective tax burden on labour for low- and middle-income earners. To this end, a study will be submitted for review by end-2013, detailing the tax policy reform options and plans for their implementation.
37	Enact the necessary legislation before end-2013 to equalise the pensionable age for men and women, by increasing the pensionable age for women from 63 to 65 years by the year 2035.
	State-owned enterprises
38	Continue the corporate governance reform of state-owned enterprises (SOEs). Strengthen Ministry of Public Finance capacities to monitor operating performance and budgets of SOEs and prepare high-quality assessments of SOE performance on an annual basis. The Fiscal Council plans a report on the operations of SOEs and their fiscal implications. All SOEs should submit their 2014 budgets one month after the approval of the state budget. Improve the operating performance of a the largest railway companies and their subsidiaries (CFR Infrastructura, CFR Calatori, and CFR Marfa) so as to ensure that arrears clearance measures are complemented by reforms that improve the viability of these companies. The cumulative operating loss should not be larger than 2.3 bn lei by end-December 2013, as specified in the Technical Memorandum of Understanding. Appoint a supervisory board by end-November 2013 for Hidroelectrica in accordance with GEO 109/2011 (SOE Corporate Governance law).
39	Ensure the sale of stakes in Romgaz, Hidroelectrica, Oltenia, Nuclearelectrica, Electrica and CFR Marfã as specified in the Memorandum of Economic and Financial Policies (MEFP) and the Technical Memorandum of Understanding (TMU).
40	By end-June 2014, the government will, in agreement with the Commission, adopt legislation to regulate the remunerations obtained by public employees for attending privatisation commissions and for positions on boards of SOEs.
	Healthcare sector
41	The authorities are to consult in a timely manner with Commission staff and provide all necessary information regarding any proposals for legislative amendments that may have material impact on the fiscal sustainability or efficiency of the healthcare sector. The authorities will start early consultations to ensure a timely implementation of the legislative

No	Measures
	process.
42	Preserve the achievements of the previous programmes and continue implementing outstanding measures, in particular but not exclusively with reference to: i) clearing arrears in the health sector; ii) preserving budget control mechanisms (such as the claw-back tax on pharmaceuticals and monthly hospital budget reporting); and iii) implementing e-health solutions.
43	Define, by end-September 2013, the publicly-reimbursable basic benefits package based on objective, verifiable criteria, to be financed within the limitations of available funding and establish the framework for a private supplementary insurance market aiming at increasing the share of private in total expenditure on health. As of 2015, the revision of the basic benefits package will be based on a cost-effectiveness analysis.
44	The authorities will prepare a comprehensive health strategy covering also the revenue side together with the MoPF by end-2013.
45	Improve efficiency and effectiveness in the healthcare system. This will be done by shifting resources from hospital-based care towards primary care and ambulatory care and by continuing the reduction of bed capacity in in-patient acute care hospitals in accordance with the national health strategy. Also, the budget for primary care will be increased via use of performance based payments to at least 10% of public health expenditure managed by the health house within the next 2 years.
46	Implement according to the deadlines the binding action plan for health care reform as committed to by the authorities, specifying the plan with measureable indicators, objectives and publishing supporting evidence and impact assessments of the reform proposals.
47	Continue the preparation of the reorganisation and rationalisation of the hospital network based on the government's project financed by the World Bank for health sector reform, slated for Board Approval by end-2013. This includes streamlining hospital services, shifting the delivery of health services to outpatient services, building physical and functional integrated referral networks, including regional hospitals, and the referral system that surrounds them from primary health to post-hospital care as well as patient pathways in the health system.

F: Monetary policy

Throughout the implementation of the financial assistance programme, performance in the following area will be monitored:

Price stability and reserve management

No.	**Measures**
48	Monetary policy should remain geared towards price stability and the achievement of the NBR's inflation target (central point 2.5% with a band of ±1 percentage point by end-2013, as of 2014, a continuous central point of 2.5% with a band of ±1 percentage point). The NBR will conduct discussions with Commission staff should the observed year-on-year rate on consumer-price index (CPI) inflation fall outside the bands specified in the Technical Memorandum of Understanding.
49	Authorities to confer with Commission staff if reserve losses exceed EUR 600 million in any given day.

Table A6.1: **Chronological overview of measures**

No.	Measure	Date
Continuous monitoring		
No.	**Measure**	**Date**
9	Reduce arrears for SOEs all SOEs should file, in accordance with existing regulations, quarterly financial information with the Ministry of Public Finance by the 25th day following quarter end.	Continuous, as specified in the TMU
18	The NBR will continue updating its contingency planning on an on-going basis as well as the bank-by-bank contingency plans.	Continuous
20	The NBR will continue to closely monitor bank practices to avoid evergreening as well as the assessment of credit risk of restructured loans, so that they remain prudent and in line with good international practices.	Continuous
22	Restrict any possible prolongation of the "Prima Casa" programme after its expiry in September 2013 to mortgage lending denominated in RON.	Continuous
23	Continue refraining from adopting legislative initiatives (such as the personal insolvency law or proposals for the debt collecting law), which would undermine credit discipline.	Continuous
28	Continue the implementation of the roadmaps for gas and electricity market liberalisation;	Continuous
28	Facilitate improved payment of infrastructure access and electricity charges from the state-owned passenger rail company (CFR Calatori) and CFR Marfa through reforms of those enterprises and settle outstanding debts among the three main railway companies.	Continuous
38	Continue the corporate governance reform of state-owned enterprises (SOEs).	Continuous
38	Strengthen Ministry of Public Finance capacities to monitor operating performance and budgets of SOEs and prepare high-quality assessments of SOE performance on an annual basis.	Continuous
38	All SOEs should submit their 2014 budgets one month after the approval of the state budget.	Continuous
39	Ensure the sale of stakes in Romgaz, Hidroelectrica, Oltenia, Nuclearelectrica, Electrica and CFR Marfă as specified in the Memorandum of Economic and Financial Policies (MEFP) and the Technical Memorandum of Understanding (TMU).	As specified in the TMU
41	Consult in a timely manner with Commission staff and provide all necessary information regarding any proposals for legislative amendments that may have material impact on the fiscal sustainability or efficiency of the healthcare sector. Start early consultations to ensure a timely implementation of the legislative process.	Continuous
46	Implement according to the deadlines the binding action plan for health care reform as committed to by the authorities.	Continuous
48	Monetary policy should remain geared towards price stability and the achievement of the NBR's inflation target (central point 2.5% with a band of ±1 percentage point by end-2013, as of 2014, a continuous central point of 2.5% with a band of ±1 percentage point). The NBR will conduct discussions with Commission staff should the observed year-on-year rate on consumer-price index (CPI) inflation fall outside the bands specified in the Technical Memorandum of Understanding.	Continuous
49	Confer with Commission staff if reserve losses exceed EUR 600 million in any given day.	Continuous
By end-September 2013		
No.	**Measure**	**Date**
20	The NBR has collected supervisory data on restructured loans, including loans to SOEs, on a quarterly basis by end-September 2013.	End-September 2013
24	Amend the legislation on the ASF/FSA (Autoritatea de Supraveghere Financiară/Financial Supervisory Authority) to comply with international best practices.	End-September 2013
24	The ASF will hire a professional and independent consultancy company to assess staffing levels and staff. Based on this, within two months of the consultancy company's assessment, an action plan will be developed to streamline the ASF with a view to realising the savings in 2014.	End-September 2013
38	The Fiscal Council publishes a report on the operations of SOEs and their fiscal implications.	End-September 2013
43	Define the publicly-reimbursable basic benefits package based on objective, verifiable criteria, to be financed within the limitations of available funding and establish the framework for a private supplementary insurance market aiming at increasing the share of private in total expenditure on health.	End-September 2013
By end-October 2013		
No.	**Measure**	**Date**
9	all SOEs should file, in accordance with existing regulations, quarterly financial information with the Ministry of Public Finance by the 25th day following quarter end.	End-October 2013
20	The NBR will conduct a comprehensive analysis of the asset quality in the banking sector and produce a report containing granular information, migration matrixes and a vintage analysis of the banks' non-performing loans (NPLs).	End-October 2013

(Continued on the next page)

Table (continued)

No.	Measure	Date
25	Implement the World Bank recommendations on the ROSC (Report on the Observance of Standards and Codes), and send the amended insolvency code draft for approval to parliament.	End-October 2013
By end-November 2013		
No.	**Measure**	**Date**
38	Appoint a supervisory board for Hidroelectrica in accordance with GEO 109/2011 (SOE Corporate Governance law).	end-November 2013
By end-December 2013		
No.	**Measure**	**Date**
3	Implement and enforce the Fiscal Compact provisions	End-December 2013
5	Approve an updated list of priority public investments	End-December 2013
9	reduce the stock of outstanding payments not made by due date of SOEs owned by central government from 8.2 bn lei in end June 2013 to 5.6 bn lei in end December 2013, as specified in the Technical Memorandum of Understanding.	End-December 2013
11	Consolidate the financing buffer at four months of gross financing needs	End-December 2013
14	Organise quarterly consultations with primary dealers, mutual funds, pension funds and life insurance companies as well as quarterly conference calls with the international investor community and non-deal road shows	End-December 2013
15	Enlarge the investor base and facilitate the access of individuals to government securities.	End-December 2013
18	The NBR will amend the internal procedures for bridge-banks.	End-December 2013
18	Amend the provisions of Government Emergency Ordinance (GEO) 99/2006 on stabilisation measures and Government Ordinance (GO) 39/1996 after consultation with the Commission on the interpretation of the new EU state aid rules in line with CRD IV implementation deadline.	End-December 2013
19	Finalize an impact assessment on the fiscal cost resulting from the tax deductibility of sales of intra-group bank receivables.	End-December 2013
21	The NBR will perform on-site inspections on a selected sample of 20 large, medium and small-sized banks focused on the strategies of banks to deal with impaired assets and will finalize the analysis of the banks' IT adequacy.	End-December 2013
22	Adopt the amendments to the covered bonds legislation through Government Ordinance, while implementing appropriate safeguards to preserve financial stability.	End-December 2013
26	Implement the Action Plans adopted in response to the findings of the functional reviews carried out in 2010-2011 in a timely manner. Continue to report on their implementation on a quarterly basis. Review and update the action plans by end-2013.	End-December 2013
27	Establish a central delivery unit in line with the World Bank project to improve the government-wide policy prioritisation, implementation and coordination with particular reference to the implementation of the EU Council's country-specific recommendations not covered in this assistance programme.	End-December 2013
37	Enact the necessary legislation before end-2013 to equalise the pensionable age for men and women, by increasing the pensionable age for women from 63 to 65 years by the year 2035.	End-December 2013
38	Improve operating performance of a the largest railway companies and their subsidiaries (CFR Infrastructura, CFR Calatori, and CFR Marfa) as to ensure that arrears clearance measures are complemented by reforms that improve the viability of these companies. The cumulative operating loss should not be larger than 2.3 bn lei by end December 2013, as specified in the Technical Memorandum of Understanding.	End-December 2013
By end-January 2014		
No.	**Measure**	**Date**
6	Roll out a web based application for the commitment control system at the MoPF and at least one additional unit at both the central and local government levels.	End-January 2014
30	Further amend the formula for calculation of the PSO to give more weight to passenger-train kilometers travelled starting in January 2014.	End-January 2014
By end-March 2014		
No.	**Measure**	**Date**
10	Update and publish the public debt management strategy, the yearly auction calendar, quarterly announcements of government securities auctions.	End-March 2014
12	Finalise the electronic auction system for domestic primary issuances.	End-March 2014
21	The NBR will perform on-site inspections in the remaining banks.	End-March 2014
26	Submit the quarterly progress report on the action plans implementation.	End-March 2014
By end-May 2014		
No.	**Measure**	**Date**
21	The NBR in consultation with the Commission and the IMF will agree an NPL resolution action plan.	End-May 2014
By end-June 2014		
No.	**Measure**	**Date**
8	Define a service catalogue for the taxpayers.	End-June 2014
26	Submit the quarterly progress report on the action plans implementation.	End-June 2014

(Continued on the next page)

Table (continued)

No.	Measure	Date
29	Develop a common methodology for impact assessments of new legislation related to business activities including the "SME test"' and establish a quality control mechanism.	End-June 2014
30	Make online submission and payment of taxes fully operational for SMEs.	End-June 2014
30	Simplify procedures regarding property registration and construction permits through making electronic submission possible.	End-June 2014
30	Introduce standard deadlines and automatic approval after the deadline for property registration and construction permits.	End-June 2014
31	Strengthen project management capacities of the national agency for the cadastre and land registry.	End-June 2014
33	Introduce minimum transparency standards defining a minimum set of information regarding bank-lending conditions, to be published by banks by mid-2014.	End-June 2014
33	Adopt legislation on equity financing with risk sharing options, in particular as regards venture capital and business angels.	End-June 2014
34	Start a "passport-to-exports" scheme to improve export promotion and development for SMEs.	End-June 2014
40	Adopt legislation to regulate the remunerations obtained by public employees for attending privatisation commissions and for positions on boards of SOEs; in agreement with the Commission.	End-June 2014
By end-September 2014		
No.	**Measure**	**Date**
13	Introduce an electronic trading platform to monitor transactions in the secondary market.	End-September 2014
16	Establish the legal, procedural and operational framework necessary to carry out buybacks, bond exchanges, and repo operations.	End-September 2014
26	Submit the quarterly progress report on the action plans implementation.	End-September 2014
By end-December 2014		
No.	**Measure**	**Date**
17	Establish involvement of the Treasury in a central counterparty (CCP) clearing house.	End-December 2014
26	Submit the quarterly progress report on the action plans implementation.	End-December 2014
29	Implement pilot projects for impact assessments of new legislation related to business activities in four selected ministries.	End-December 2014
30	Introduce data sharing within the e-government system.	End-December 2014
31	Increase the number of solved land disputes per year by 10% including through out-of-court dispute resolutions.	End-December 2014
32	Provide guidelines, in line with international best practices, including on the distribution of benefits arising from the commercial exploitation of the invention.	End-December 2014
33	Strengthen services, including those related to access to finance that are provided by the SME territorial offices by increasing the number of assisted companies from 2013 to 2014 by 20%.	End-December 2014
34	Make the pilot regional export centres fully operational.	End-December 2014
34	Reinforce the electronic trade portal and improve the effectiveness of the trade counsellor schemes outside Romania with 30% more companies assisted in 2014 than in 2013.	End-December 2014
43	Base the revision of the basic benefits package on a cost-effectiveness analysis.	End-December 2014
By end-March 2015		
No.	**Measure**	**Date**
26	Submit the quarterly progress report on the action plans implementation.	End-March 2015
By end-June 2015		
No.	**Measure**	**Date**
26	Submit the quarterly progress report on the action plans implementation.	End-June 2015
31	Increase the number of properties registered in the digitalised national land registry from currently 15% to 25%.	End-June 2015
To be met within the programme period, deadline yet to be defined		
No.	**Measure**	
1	Reduce the structural fiscal deficit to 1% of GDP.	
3	Strengthen the role of the Fiscal Council regarding the assessment of revenue projections and the calculation of the deficit target.	
4	Improve the content of the fiscal strategy.	
4	Design and implement procedures for internal coordination arrangements, to involve line ministries in the medium-term budget planning.	
4	Increase the capacity of the MoPF to estimate the structural deficit.	
4	Strengthen the capacity to perform fiscal compact assessments of legislative proposals.	
6	Establish an effective commitment control system for all levels of government.	
7	Set up the protocol for a regular flow of fiscally-relevant data to the MoPF.	
8	Implement a comprehensive tax compliance strategy in line with the respective World Bank project	
8	Improve VAT reimbursement procedure.	

(Continued on the next page)

Table (continued)

8	Increase the e-filing rate for the tax returns for companies from 89% to 93%.
18	Strengthen corporate governance of the Deposit Guarantee Fund in the Banking System, in particular to avoid any perceived conflict of interest for board members and executive directors.
23	Ensure that court cases involving abusive clauses are dealt with by higher ranking courts or by a unique specialised court and take all other necessary measures to ensure a harmonised application of these provisions, such as training of judges.
23	The NBR together with the Romanian Banking Association will explore possibilities for setting up a database of shareholders of companies in insolvency as well as implement more effective data reporting of the Association of Insolvency Practitioners.
24	The ASF will swiftly complete the integration of the former three supervisory authorities for securities, insurance and pensions while ensuring the smoothing functioning of supervisory activities.
24	The ASF will develop a human resources policy geared first and foremost towards qualified staff to perform on-site supervision, off-site analysis, validation of internal models.
24	The ASF will further enhance transparency and public accountability by ensuring an adequate public disclosure of all fees and commissions charged to the supervised entities.
28	Continue the development of gas and electricity trading platforms.
28	continue the unbundling of energy transmission and dispatch operators.
28	Improve cross-border integration of energy networks and provide for security-of-supply measures.
30	Streamline the "one-stop shop" and the "point of single contact" into fully-operational and interconnected electronic platforms with a single entry point.
31	Find appropriate arrangements for a swift resolution of undebated inheritance cases.
31	For concession and leasing contracts related to the state domain make land and property registration compulsory prior to contract signature.
42	Continue implementing outstanding measures, in particular but not exclusively with reference to: i) clearing arrears in the health sector; ii) preserving budget control mechanisms (such as the claw-back tax on pharmaceuticals and monthly hospital budget reporting); and iii) implementing e-health solutions.
45	Improve efficiency and effectiveness in the healthcare system. This will be done by shifting resources from hospital-based care towards primary care and ambulatory care and by continuing the reduction of bed capacity in in-patient acute care hospitals in accordance with the national health strategy. Also, the budget for primary care will be increased via use of performance based payments to at least 10% of public health expenditure managed by the health house within the next 2 years.
47	Continue the preparation of the reorganisation and rationalisation of the hospital network based on the government's project financed by the World Bank for health sector reform.

Source:

A6.2. LETTER OF INTENT

Bucharest, 12 September, 2013

Mr. Olli Rehn

Vice-President of the European Commission

responsible for Economic and Monetary Affairs and the Euro

European Commission, BERL 10/299

B-1049 Brussels, Belgium

Mr Rimantas Šadžius

Minister of Finance

Ministry of Finance of the Republic of Lithuania,

Lukiškių 2, LT-01512 Vilnius, Lithuania

r.sadzius@finmin.lt

Dear Mr. Rehn,

Mr Šadžius,

1. Under two consecutive economic programs supported by the International Monetary Fund (IMF), the European Union (EU), and the World Bank (WB) we have made significant progress in reducing macroeconomic imbalances and rebuilding fiscal and financial buffers. However, structural reforms in key areas are ongoing and Romania remains vulnerable to external shocks and turmoil in international capital markets. We therefore request approval of a new 24-month medium-term financial assistance programme of up to EUR 2 bn that we intend to treat as precautionary. The new balance-of-payments programme will support our comprehensive economic program for 2013-2015 to maintain sound macroeconomic policies and financial sector stability, and continue structural reforms in an environment of large external uncertainties. In conjunction with a new 24-month Stand-By Arrangement (SBA) totaling SDR 1,751.34 million (about €2 billion, 170 percent of quota) with the IMF, which we intend to treat as precautionary, and €1 billion under a Development Policy Loan (DPL) with a deferred drawdown option (DDO) provided by the WB, this arrangement will signal the international community's continued support for our policies and provide a buffer against external shocks.

2. We believe that the policies and measures set forth in the attached Memorandum of Economic and Financial Policies (MEFP) are adequate to achieve the objectives of our economic programme. We also remain committed to preserving the achievements of the preceding two programmes and adhering to previously made commitments. We stand ready to take additional measures as appropriate to ensure achievement of these objectives. We will consult with the European Commission (EC) and the IMF before modifying measures contained in this Letter and the attached MEFP or adopting new measures that

would deviate from the goals of the programme, and will provide the EC and the IMF with the necessary information for program monitoring.

3. We authorise the EC and the IMF to publish the Letter of Intent and its attachments, and the related staff reports. This letter is being copied to Mme. Lagarde.

Sincerely,

[Signed]	*[Signed]*
Daniel Chiţoiu	Mugur Isărescu
Deputy Prime Minister	Governor of the National Bank of Romania
and Minister of Public Finance	

[Signed]

Liviu Voinea

Minister Delegate for Budget

A6.3. MEMORANDUM OF ECONOMIC AND FINANCIAL POLICIES

Recent Economic Developments and Outlook

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

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

Fiscal Policy

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

4. Given the weak revenues and increasing spending pressures, we are undertaking several measures to achieve the deficit target. Public employment has been kept broadly stable as we have now removed the 1 for 7 rule and introduced a 1 for 1 rule while restructuring public administration. In June, we approved Government Emergency Ordinance 77/2013 eliminating the vacancies in public employment while maintaining a tight control on new hires and shifting employment from the central towards local governments. Nevertheless, current expenditures remain under pressure as agricultural subsidies have been frontloaded and goods and services spending has increased even as the implementation of the Payments Directive 7, shortening the settling of unpaid bills in the pharmaceutical sector, has been postponed from June to August. In addition, we have approved an Government Emergency Ordinance 42/2013 increasing the Guaranteed Minimum Income and family allowances, and increased eligibility thresholds and we also plan to simplify the asset test for these benefits to mitigate the impact of gas and energy price liberalization. Furthermore, we extended by three years the existing legislation to provide a top-up to unemployment benefits for some SOE layoffs and have so far provided the benefit to one large SOE. Spending commitments at the local government level is also on the rise as shown by increasing overdue bills. We are also reducing the VAT on bread and the production chain from

September. To offset the revenue loss, we will increase excises on alcohol and luxury cars and goods. Unspent allocations for EU funds corrections will provide some savings while further cuts in domestically financed capital spending will also be needed. Moreover, all unexecuted contracts for PNDI projects have been cancelled while projects executed under the PNDI have been folded within the budget. An independent audit of the projects committed under the PNDI program will be conducted to ensure that they are properly executed and invoiced. In the event of lower than forecasted revenues, the government remains committed to achieving the annual deficit target.

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

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

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

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

- To ensure that arrears are brought fully under control, especially at the local government level, we will publish monthly arrears reports and corrective measures being taken by the central and local governments, by unit, on a quarterly basis from end-September 2013 (structural benchmark). We will seek to maintain arrears for the central and local governments at a low level consistent with the targets under the program. The Court of Accounts shall submit a schedule of audits of the disputed invoices presented to the local governments (360 million lei) with the objective of preparing the first quarterly progress report on the status of the findings by mid-November 2013. We will evaluate the possibility of central government transfers to local government units to cover the unpaid bills that represent valid liabilities of the government as verified by the Central Harmonization Unit for Financial Management and Control Systems, which in turn will be used to cover the suppliers' tax payables. In such cases, the central government will undertake stricter control of the local government unit's total spending, consistent with Government Emergency Ordinance 46/2013.

- We have made progress in the implementation of the commitment control system. We have put in place a manual commitment control for new investments for local governments. We will approve a government ordinance to provide standard definitions of commitments (prior action) so that the commitment control system under development, supported by necessary legal and procedural changes, will be fully operational and cover expenditures of the MoPF and at least one additional unit at both the central and local government levels by end-January 2014 (structural benchmark) and fully operational for all general government entities by end-June 2014 (structural benchmark).

- The consolidated fiscal reporting system would be rolled out to all government entities by June 2014 (structural benchmark) and will run in parallel with the existing system until the end of 2014. Consolidated general government accrual based financial statements and ESA95 based reports will be prepared from the system and published from June 2015 (the first sets of reports will be for the year ended December 31, 2014), be reconciled with each other and with cash-based budget execution reports (structural benchmark).

- To improve fiscal transparency and ensure more consistency with ESA, we will request that the IMF undertake a fiscal transparency assessment. We will provide the fiscal data required to transition fully to GFSM 2001 for the 2014 budget.

- By end-2013, a report on fiscal risks will be published as part of the annual budget. This will commence with the 2014 budget. The report will take into account risks, including those related to contingent liabilities, the debt composition, the banking system, all PPPs, and all SOEs.

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

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

- As the managing authorities seek to ramp up spending, better budgetary planning will be necessary to accommodate higher co-financing and needed financial corrections. We will prepare medium-term financial projections, by mid-October 2013, that properly identifies the fiscal implications of EU funded projects (structural benchmark) and allows proper monitoring of the spending on EU funded projects by managing authorities. To allow greater flexibility in financing of EU funded projects given lags in reimbursement, net lending of EU structural and cohesion fund projects will be provided within a ceiling on net lending of 3 billion lei (set as an indicative target). We will ensure that spending on non-eligible projects is limited to 2 billion RON. We will continue to implement fully the Priority Action Plan for the absorption of Structural and Cohesion Funds.

- Before contracting public-private partnerships (PPPs) and issuing guarantees for PPPs and concessions, the World Bank will assess MoPF capacity to (1) provide inputs to the PM/Line ministries unit to develop a methodology for identifying and evaluating fiscal commitment to PPPs, (2) assess the affordability of PPP fiscal commitment as an input to approval of any initiative, and (3) develop guidelines for incorporating PPP project in decision-making at the level of MoPF at various stages of PPP project life cycle (identification, preparation, bidding, implementation).

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

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

- As part of ANAF restructuring and modernization, the current 221 tax offices will be consolidated to eight regional directorates by September 2013 and 47 local tax offices by 2015. We are also reallocating around 1,700 staff away, mostly from support functions to prevention and inspection, and will increase resources in Bucharest Region to combat fraud. ANAF will take over the responsibilities of the Financial Guard by November 1, 2013, which will cease to exist, adding a further 1,100 staff to ANAF's disposal. The new positions will be directed to the new prevention and fighting tax evasion and tax customs fraud structure and will be filled following strict selection procedures. We will provide additional professional training to all staff involved in combating tax evasion. We ratified the loan agreement with the World Bank concerning a project to support the modernization of the tax administration.

- We continue to make progress on our High Net-Wealth Individual (HNWI) taxpayers initiative. We started 30 prior desk audits for HNWI following the tax procedure code in the first half of the year and re-launched our notification campaign by sending out letters on the risks of non-filing foreign income to 360 individuals. We have also published our program on ANAF's website. Voluntary compliance appears to be improving. We have improved the quality of our personal income tax audits more generally. We will strengthen our auditing further using the indirect proofs method, expanding the definition of un-sourced income and clarifying the taxability of dividend payments, which are currently often disguised as non-taxable loan repayments to businesses. To help us achieve these goals, we have undertaken training programs with the assistance of partner-country tax administration specialists and IMF technical assistance in April.

- We also aim to develop taxpayer services, for example, offered through ANAF's portal (considered as a "one stop shop") by June 30, 2014 and by ensuring that the interpretation of the tax law is unambiguous. To this end we will issue a common procedure with the MoFP and set up single channel dealing with all enquiries on tax law interpretation by December 31, 2014. Moreover, we will streamline the VAT reimbursement procedures based on a risk analysis, in order to significantly diminish the time allocated tax audits in this field and for decreasing the time needed for solving refund cases by June 2014 and will set up a central database that will allow us to manage and assess together with local authorities data regarding taxes and contributions owed to the general consolidated budget as well as information on properties. This will be an important source of information for taxpayers and should also raise compliance by December 31, 2014. Finally we will make all efforts to ensure SME in distress are granted payments terms in instalments to clear tax arrears.

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

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

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

- The reforms will strengthen the contributions base; streamline hospital services reducing the redundant capacity for inpatient services in line with the national health strategy and shifting the delivery of health services away from hospitals to ambulatory and primary health care providers; develop capacity in Health Technology Assessments and evidence-based protocols; and allocate more resources towards primary and secondary preventive care. Rather than adopting a new framework law, we have decided to pursue a more gradual approach based on modifying existing legislation. This should allow individual initiatives to proceed at different speeds and to be completed without necessarily relying on the success of all other initiatives. In April we formulated a strategic action plan for this year. We published the agreed plan on the ministry's website as a statement of government policy agreed with the IFIs, we will meet all the deadlines set and, in particular, will prepare the basic health package within the existing spending envelope by end-September 2013, which will also define the scope of the private health insurance in the health care system in the future (structural benchmark). We will also prepare a comprehensive health strategy covering also the revenue side, together with the MOPF, including a timetable for implementing legislative changes and progress indicators.

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

- To increase the share of spending on primary and ambulatory services in total health spending, we will revise by end-December 2013 the list of services, which can be contracted with primary care providers as part of the 2014 health care framework agreement. We will publish a revised list of compensated drugs by end-December 2013, to be approved by government ordinance, based on the methodology provided by a newly established unit conducting health technology assessments. The centralized procurement system for pharmaceuticals and medical devices for hospitals became operational in the first half of 2013. We will assess the system's performance at the end of 2013 and progress on the design of a centralized IT system.

- To avoid the future build-up of arrears in the hospital sector, we have shifted some financial resources from hospitals with limited competences to those in the network of regional emergency hospitals. This objective will be achieved through adjustments of the weighted-per case tariffs, while ensuring that arrears will not accumulate in hospitals with decreased funding. We amended the contracts of hospital managers in June 2013 so that they will be replaced automatically if the hospital has run arrears for three consecutive months.

- We will continue to monitor public hospital budgets to ensure that they are consistent with the expenditure programmed in the general government budget, will collect and analyze the cost of service provision across hospitals with the aim of developing benchmarks in the future, and have published online up-to-date financial statements of all public hospitals since October 2012. We signed a contract with the National Printing Office to produce 7½ million patient cards by end 2013 and the remainder for the eligible population by mid 2014. By September, we will decide on the mechanism for distribution of these cards. The electronic prescription system is now established, with 34m prescriptions produced by end of June 2013. To promote awareness and encourage the increased use of generic drugs, we will print from January 2014 the patient rights with respect to pharmacists' obligation to provide full information on available drugs on the printed prescription.

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

Monetary and Exchange Rate Policy

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

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

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

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

Financial Sector

21 The Romanian banking sector maintains reassuring capital buffers and provisioning but faces continues pressures on asset quality, and from foreign bank deleveraging, while also remaining vulnerable to external shocks. Annual credit growth to both corporates and households remains negative. Non-performing loans (NPLs) rose to 20.3 percent of total loans at end-June 2013 (compared to 14.3 percent at end-2011) reflecting the difficult economic environment, slow credit growth, deteriorating quality of loans, and difficulties in removing NPLs from bank balance sheets. However, provisions (with a prudential filter) were sufficient to cover a comfortable 88.3 percent of NPLs while the IFRS provisioning ratio stood at 62.8 percent at end-June.([22]) The provisioning requirements along with the high cost base led to a loss in the banking system in 2012 but allowed for a small profit in the first half of 2013. In light of the still difficult economic environment, in particular as regards corporate and household balance sheets as well as low credit demand, prospects for bank profitability remain challenging. The capitalization of the banking sector remained strong at 14.7 percent at end-June 2013 albeit with some differences between banks. Overall, system household and corporate deposits have only increased by around 10 percent since end-2011. While the liquidity situation has improved for the banking system, funding conditions are still uneven among some banks. The pace of foreign-owned bank deleveraging has accelerated in line with regional developments but remains orderly so far with a parent funding decline of 26 percent since 2011. Risks from continuing parent funding retrenchment remain elevated and could be an impediment to the credit growth recovery should credit demand pick up sizably. The system-wide loan-to-deposit ratio stood at around 114 percent at end-June 2013, declining from 117 percent at end-2012 and at end -2011.

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

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

NBR will continue to regularly conduct top-down and bottom-up solvency stress tests as well as liquidity stress tests of the banking industry.

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

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

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

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

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

28. To foster the development of a viable distressed debt market, we will resolve possible discrepancies in the fiscal code and accounting rules on the treatment of NPLs sold to domestic debt management companies in line with the outcome of the pending EC infringement case structural benchmark, by end-December, 2014. We will also conduct an impact study on the fiscal costs from the tax deductibility of the sale of intra-group bank receivables (by end-December 2013) and of non-bank receivables (by end-August 2014).

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

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

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

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

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

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

Energy and transportation sector reforms

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

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

- ***Energy sector:*** We transposed the European Union's third energy directive into national law and promulgated a law to ensure the independence of the energy regulator (ANRE). ANRE started the implementation of the electricity price liberalization roadmap in September 2012 and continued the quarterly schedule in January, April, and July 2013. After an initial delay, ANRE started the implementation of the gas price liberalization road map and has raised the domestic gas producer price by almost 40 percent in accordance with the road map. The state-owned hydro-electric producer, Hidroelectrica, exited from the insolvency process on July 1, 2013. Under insolvency, the Legal Administrator cancelled or renegotiated below market bilateral contracts with the electricity released from contracts being sold at the OPCOM Power Exchange. The Administrator also cancelled hundreds of smaller contracts and investment projects deemed to be against the interest of Hidroelectrica.

- ***Transportation sector:*** We initialed a sale-purchase agreement for the sale a 51 percent stake in the state-owned freight company (Marfa) for RON 905 million and took a government decision approving the sale-purchase agreement. We also approved an arrears clearance scheme in June whereby CFR Marfa's arrears would be reduced by over 90 percent upon conclusion of the sale. To help improve the financial performance of the state-owned passenger rail company (Calatori), we changed the formula for calculation of the subsidy for the public service obligations (PSO) and removed the international and inter-city trains from the PSO. We also closed the most unprofitable routes for passenger traffic.

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

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

39. The second leg will continue measures to improve the governance, transparency, and monitoring of SOEs. We have taken note of observations made about the new boards appointed recently to energy SOEs. We will appoint a professional board in Hidroelectrica by end-November 2013 (structural benchmark) following the letter and spirit of the procedures specified in the SOE corporate governance Government Emergency Ordinance 109/2011. In the meantime, the current interim board appointed upon Hidroelectrica's exit from insolvency will continue to be in charge and we will authorize through a General Shareholders Meeting the current interim board to take decisions in accordance with law 31/1990

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

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

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

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

- **Romgaz** (natural gas producer)**:** Launch an IPO of 15 percent of the government's shares by mid-November 2013 (structural benchmark). In advance, we will obtain approval of the Financial Supervision Authority (FSA) for use of global depository receipts and complete an environmental impact study. A decision to expand the size of Romgaz's board following the IPO has also been taken. As a prior action, we will clarify the tax treatment of securities bought in Romgaz traded on the foreign stock exchange and adopt, if needed, the necessary legal basis.

- **Electrica** (electricity distribution, supply, and service)**:** Launch an initial public offering of a majority of the government's shares, after the planned capital increase, by end-May 2014 (structural benchmark). In preparation, we will hire a transaction advisor for the IPO by mid-September 2013. Work is currently underway to determine what to do with five of Electrica's six regional service companies. At least three, but possibly all five may have to be separated from Electrica for eventual liquidation. Electrica's minority shareholdings in already privatized distribution companies could be a major area of uncertainty for the IPO and these share holdings will be taken out of Electrica prior to the IPO. We will also address the issue of non-payment by CFR for its electricity purchases from Electrica ahead of the IPO.

- **Oltenia** (thermoelectric generator)**:** In view of Oltenia's investment needs, we planned ahead of majority privatization an IPO of a 15 percent of the government's shares, prior to the planned capital increase, by end-October 2013 and hired a transaction advisor for this in May 2013. Subsequently, we decided to delay the IPO until end-June 2014 (structural benchmark) after the audited financial statements for 2013 are available and a study of the coal reserves is conducted.

- **Hidroelectrica** We planned an IPO of a 10 percent of the government's shares, after the planned capital increase, by end-October 2013. However, a court challenge to the government decision to conduct the IPO and the government's subsequent appeal of the court decision has delayed the process. The Ministry of Economy, the General Secretariat of the Government and Hidroelectrica submitted to the Court of Appeal the withdrawal of their respective appeals and asked for the Court to consider the withdrawal requests on an expedited basis. We will issue a new government decision for an IPO of 10 percent, in accordance with all required procedures. The government will sign a contract with the transaction advisor selected through a competitive process already in 2012 for the IPO which will be launched by end-June 2014 (structural benchmark), provided a Court decision is made by end-September, 2013.

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

- **CFR Marfa:** We will fulfill our obligations under the sale purchase agreement for the majority sale of CFR Marfa and close the transaction (exchange of payment for shares) by the mid-October 2013. In this context, merger control approval will be sought from the relevant regulatory authority. If the privatization process encounters insurmountable obstacles, we will reopen the tender for the majority privatization of Marfa abiding to a process that follows best international practices.

- **CFR Infrastructura and CFR Calatori:** We will allow the appointed boards of these companies to implement the approved administrative plans without interference. We will complete the procedure for appointing new management in CFR Infrastructura following the letter and spirit of the procedures specified in the SOE Corporate Governance ordinance (109/2011). We also intend to lease out an additional 1,500 kilometers of inoperable track, raise passenger tariff rates in September 2013, and further amend the formula for calculation of the PSO to give more weight to passenger-train kilometers travelled starting in January 2014. More broadly, we will continue to explore measures to rationalize the network, improve absorption of EU funds, strengthen the procurement process, and reduce costs. We will address the issue of non-payment by CFR Infrastructura to Electrica ahead of Electrica's IPO which would otherwise be undermined.

43. A high quality and extensive road network is a critical infrastructure component of a welcoming business environment for investment and a well functioning economy. To focus our efforts on increasing the absorption of EU funds in the 2014-2020 funding period, we will create an agency within the government dedicated to the development of highways eligible for EU funding. The state-owned roads company also intends to minimize capital spending on existing projects in 2013, with a view to reducing

arrears towards zero. The company will not lengthen the invoice certification procedures outside legal requirements.

Labor Markets

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

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

Table 1. Romania: Quantitative Program Targets

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

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

Table 2. Romania: Proposed Conditionality

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

A6.4. TECHNICAL MEMORANDUM OF UNDERSTANDING

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

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

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

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

A. Floor on the Change in Net International Reserves

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

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

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

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

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

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

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

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

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

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

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

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

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

Inflation Consultation Band

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

C. Performance Criterion on General Government Balance

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

Cumulative Floor on General Government Balance[1]

	(In millions of lei)
End-June 2013 (actual)	-6621
End-September 2013 (performance criterion)	-9181
End-December 2013 (performance criterion)	-14700
End-March 2014 (indicative)	-4000
End-June 2014(indicative)	-6200

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

11. The cumulative floor on the general government balance will be adjusted downward by the spending on national cofinancing of EU funded projects (excluding cofinancing from the top-up funds) exceeding 4221 million RON at end-September 2013 and 5886 million RON at end-December 2013, up to a limit of 600 million RON.

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

+ (i) net external financing, excluding valuation gains and losses;

+ (ii) change in net domestic credit from the financial system, excluding valuation gains and losses from deposits denominated in foreign currency and including adjustments for;

+ (a) received EU funds not yet spent (advance payments);

+ (b) claims of the government on EU funds;

+ (c) property fund obligations not yet paid;

+ (iii) change in the stock of issued government securities, net of valuation changes;

+ (iv) net changes in other financing;

of which: (a) temporary financing for EU projects;

(b) reimbursement payments from EU for the EU projects

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

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

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

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

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

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

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

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

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

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

End-December 2013 (performance criterion)	.02
End-March 2014 (indicative)	.02
End-June 2014 (indicative)	.02

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

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

H. Indicative Target on General Government Current Primary Spending

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

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

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

I. Indicative Target on Local Government Arrears

19. The indicative target on the stock of domestic payments arrears of local governments contemplates no accumulation of new arrears and their reduction during the program period. In case of need, the government will take corrective measures to prevent the accumulation of new spending arrears. For the purpose of the program, arrears mean accounts payable past the due date by 90 days (in line with ESA95 definitions for expenditures). As a memorandum item, arrears of local government hospitals will be reported separately on a quarterly basis.

Stock in Local Government Arrears	(In billions of lei)
End-June 2013 (actual)	.143

End-September 2013 (performance criterion)	.300
End-December 2013 (performance criterion)	.300
End-March 2014 (indicative)	.300
End-June 2014 (indicative)	.300

J. Absorption of EU Funds

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

K. Monitoring of Public Enterprises

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

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

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

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

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

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

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

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

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

L. Reporting Requirements for the Prior Actions

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

M. Reporting Requirements

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

Romania: Data Provision to the IMF and EC

Item	Periodicity
To be provided by the Ministry of Public Finance	
Preliminary monthly data on general government accounts, including on GFSM 2001 basis	Monthly, on the 25th day of the following month
Quarterly final data on net lending from the Treasury for EU funded projects	Quarterly, on the 5th day past the test date
Preliminary monthly data providing a breakdown of general government expenditures on post-accession EU projects (co-financing, non-eligible spending, corrections, reimbursable funds, and EU top-ups)	Monthly, on the 25th day of the following month
Quarterly final data on general government accounts, including public enterprises as defined by ESA95 and breakdown of general government spending on EU projects	Quarterly cash data, on the 35th day past the test date; Quarterly accrual data, on the 55th day past test date
The budget deficit of the general government using ESA95 definition	Quarterly, with a lag of three months
Preliminary data on below-the-line financing for the general government	Monthly, with a lag of no more than 35 days past the test date
Final quarterly data on below-the-line financing for the general government, including details of the domestic and external issuances and repayments (by currency)	Quarterly, no later than 45 days past the test date
Total accounts payable and arrears of the general government, including local governments and central and local government hospitals	Preliminary monthly, within the next month. Quarterly, within 55 days
Progress report on the status of the audit of the stock of the disputed local arrears.	Quarterly, no later than 45 days past the end of each quarter
Data on payment delays and arears with respect to drug reimbursement by the National Health Insurance House (pharmacies and wholesale), with a particular view on the implementation of directive 7	Monthly, at the end of each month
Stock of the central government external arrears	Daily, with a lag of not more than seven days
Public debt and new guarantees issued by the general government	Monthly, within one month
Preliminary monthly data on general government	Preliminary monthly data within 25 days

primary spending, net of EU disbursements	
Final quarterly data on general government primary spending, net of EU disbursements	Quarterly, within 35 days from the test date
Time lines showing the expected completion dates for key steps leading to the launching of the initial public offerings of the energy state-owned companies	Quarterly, within 10 days of the end of each quarter
Preliminary data on the operating balance, profits, stock of outstanding payments past due, and personnel expenditures for each key public enterprise as defined in ¶22	Monthly, within 30 days
Final data on the operating balance, profits, stock of outstanding payments past due, and personnel expenditures for each key public enterprise as defined in ¶22	Quarterly, end-May for the previous year and end-August for first half of the current year
Preliminary data on the stock of outstanding payments past due for each public enterprise as defined in ¶21	Quarterly, within 35 days
Final data on the stock of outstanding payments past due for each public enterprise as defined in ¶21	Quarterly, end-May for the previous year and end-August for first half of the current year
Data on EU project grants (reimbursements and advances), capital expenditures and subsidies covered by EU advances or eligible for EU reimbursement on EU supported projects specifically agreed with the EU	Monthly, within three weeks of the end of each month
The balance of the TSA in RON	Monthly, within two weeks of the end of each month
The balance of the two foreign currency accounts used for budget financing and public debt redemption purposes (average, and end-of-period)	Monthly, within two weeks of the end of each month
The balance of the privatization receipts registered in the account of the State Treasury, details on any claims on these receipts and projected net outflows.	Monthly, within two weeks of the end of each month
Reporting of progress in the implementation of the Romanian public administration's functional review	Quarterly, to be sent two weeks before each mission for each of the 12 ministries
Data on subsidies by ministries	Quarterly, one month after the end of the quarter. Additional reporting one week before review mission
Data on public employment and status of ordinance 77/2013 implementation, in particular numbers of staff reductions at central government ministries and staff increases at local governments	Monthly, at the end of each month

To be provided by the National Bank of Romania	
NIR data, by components, in both program and actual exchange rates	Weekly, each Monday succeeding the reporting week and with a 3 working day lag in the case of end-quarter data
Monetary survey data in the format agreed with IMF and EC staff	Monthly, within 30 days of the end of the month
The schedule of contractual external payments of the *banking sector* falling due in the next four quarters, interest and amortization (for medium and long-term loans)	Monthly, 45 days after the end of each month
The schedule of contractual external payments of the *corporate sector* falling due in the next four quarters interest and amortization (for medium and long-term loans)	Monthly, 45 days after the end of each month
The stock of short-term external debt of banks and corporate	Monthly, 45 days after the end of each month
Balance of payments in the IMF format currently used to report	Monthly, 45 days after the end of each month
Exposure (deposits, loans, subordinated loans) of (i) foreign parent banks to their subsidiaries in Romania; (ii) IFI and (iii) other creditors to banks in Romania (by national and foreign currency).	Monthly, 20 days after the end of each month
Detailed bank-by-bank data on restructured loans to households and corporates including SOEs	Quarterly, 45 days after the end of each quarter
Financial soundness indicators([23])	Monthly, 45 days after the end of each month
Foreign currency reserves including information on FX market interventions and swaps by the NBR	Bi-weekly
The IMF and the EC shall be immediately informed in case of sudden loss of reserves exceeding EUR 600 million	Immediately, upon occurrence

([23]) Data on solvency should be provided on quarterly basis.

A6.5. COUNCIL DECISION GRANTING MUTUAL ASSISTANCE FOR ROMANIA

COUNCIL DECISION

of 22 October 2013

granting mutual assistance for Romania

(2013/532/EU)

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Article 143 thereof,

Having regard to the recommendation from the European Commission made after consulting the Economic and Financial Committee,

Whereas:

(1) Romania has implemented a substantial reform programme since 2009. Under two balance-of-payments programmes, Romania has largely corrected its external macroeconomic imbalances. In addition, on 21 June 2013, the Council, by Decision 2013/318/EU ([24]), abrogated Decision 2009/590/EC ([25]) on the existence of an excessive deficit in Romania. Fiscal consolidation should be continued in line with the Stability and Growth Pact requirements with a view to meeting the medium-term objective in 2015. The Government has regained full access to market-based financing and the exchange rate has been broadly stable since mid-2009.

(2) Macroeconomic and financial stability should be consolidated through the pursuit of prudent policies. Structural reforms that were initiated under the previous programmes should be pursued and, where appropriate, reinforced to reduce vulnerabilities and strengthen the basis for future growth and catching up.

(3) The Council is to review on a regular basis the economic policies implemented by Romania, in particular in the context of the annual reviews of Romania's update of the Convergence Programme and implementation of the National Reform Programme and the regular review of progress made by Romania in the context of the convergence report.

(4) While in the baseline scenario of the economic programme, total gross financing needs until the end of 2015 are fully covered, and the Government continues to have access to market-based financing, the risks surrounding the baseline scenario support Romania's request for a financial assistance of a precautionary nature as a follow on to the assistance granted under Council Decisions 2009/458/EC ([26]) and 2011/289/EU ([27]).

([24]) Council Decision 2013/318/EU of 21 June 2013 abrogating Decision 2009/590/EC on the existence of an excessive deficit in Romania (OJ L 173, 26.6.2013, p. 50).
([25]) Council Decision 2009/590/EC of 7 July 2009 on the existence of an excessive deficit in Romania (OJ L 202, 4.8.2009, p. 48).
([26]) Council Decision 2009/458/EC of 6 May 2009 granting mutual assistance for Romania (OJ L 150, 13.6.2009, p. 6).
([27]) Council Decision 2011/289/EU of 12 May 2011 granting mutual assistance for Romania (OJ L 132, 19.5.2011, p. 18).

(5) The Romanian authorities have requested financial assistance from the Union and other international financial institutions to support balance of payments sustainability and to ensure that international currency reserves can be kept at a prudent level even in the case of adverse economic developments.

(6) Despite improvements in its current account, Romania remains vulnerable to exchange-rate volatility and volatile international capital movements. In an adverse scenario marked by a retrenchment of the current abundant liquidity, situations could arise in which the financing costs for Romania would increase and possibly do so in a rapid way. Furthermore, adverse developments in the euro area could cause renewed pressures on the banking sector. The remaining vulnerabilities justify the granting of mutual assistance by the Union,

HAS ADOPTED THIS DECISION:

Article 1

The Union shall grant mutual assistance to Romania.

Article 2

This Decision shall take effect on the date of its notification.

Article 3

This Decision is addressed to the Member States.

Done at Luxembourg, 22 October 2013.

For the Council

The President

L. LINKEVIČIUSEN

As published in OJ No L286 of 29 October 2013.

A6.6. COUNCIL DECISION PROVIDING PRECAUTIONARY EU MEDIUM-TERM FINANCIAL ASSISTANCE TO ROMANIA

COUNCIL DECISION

of 22 October 2013

providing precautionary EU medium-term financial assistance to Romania

(2013/531/EU)

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Council Regulation (EC) No 332/2002 of 18 February 2002 establishing a facility providing medium- term financial assistance for Member States' balances of payments ([28]) and in particular Article 3(2) thereof,

Having regard to the proposal from the European Commission made after consulting the Economic and Financial Committee,

Whereas:

(1) By Decision 2013/532/EU ([29]), the Council has decided to grant mutual assistance to Romania.

(2) Precautionary medium-term financial assistance for Romania under the balance-of-payments facility for Member States is appropriate under the current circumstances of unstable capital flows affecting in particular emerging markets, risks to the macroeconomic scenario, and remaining vulnerabilities in the banking sector. While under present market conditions Romania does not intend to request the disbursement of any instalment, the precautionary assistance can be expected to help consolidate macroeconomic, budgetary and financial stability and, through the pursuit of structural reforms, increase the resilience and the growth potential of the Romanian economy.

(3) If negative risks materialise, Romania may not be able to cover its external financing needs from available funding resources. These risks are associated with, among others, important external debt and financial sector roll-overs, a high negative net investment position, and spill-overs from adverse developments in the euro area. In such a stress scenario, the residual financing needs may have to be covered from activating the precautionary medium- term financial assistance.

(4) It is appropriate to provide Union support to Romania of up to EUR 2 000 million on a precautionary basis under the facility providing medium-term financial assistance for Member States' balance of payments established in Regulation (EC) No 332/2002. That assistance should be provided in conjunction with support from the International Monetary Fund (IMF) through a Stand-by Arrangement in the amount of SDR 1 751,34 million (about EUR 2 000 million, 170 % of Romania's IMF quota), approved on 27 September 2013, which the authorities are also to treat as precautionary medium- term financial assistance. The World Bank has made EUR 1 000 million available under a Development Policy Loan

([28]) OJ L 53, 23.2.2002, p. 1.
([29]) See page 4 of this Official Journal.

with a deferred drawdown option valid through December 2015. In addition, the World Bank is to continue to provide earlier committed support of EUR 891 million, of which EUR 514 million is still to be disbursed.

(5) The precautionary medium-term financial assistance should be managed by the Commission which is to agree with the authorities of Romania, after consulting the Economic and Financial Committee (EFC), on the specific economic policy conditions attached to that assistance. Those conditions should be laid down in a Memorandum of Understanding.

(6) In view of the precautionary nature of the medium-term financial assistance, Romania will not request the disbursement of any instalment under the Union loan, unless difficulties as regards its balance of current payments or capital movements emerge. If Romania makes a request for funding to the Commission, the latter is to decide, after having consulted the EFC, on the activation of the programme and on the amount and timing of such instalments. The detailed financial terms related to possible disbursements is to be laid down in a Precautionary Loan Facility Agreement (PLFA).

(7) The precautionary medium-term financial assistance should be provided with a view to contributing to the successful implementation of the Government's economic policy programme, and, in this way, should support the sustainability of Romania's balance of payments,

HAS ADOPTED THIS DECISION:

Article 1

1. The Union shall make available to Romania precautionary medium-term financial assistance amounting to a maximum of EUR 2 000 million. In case the facility is activated and disbursements are provided, that assistance shall be provided in the form of a loan with a maximum average maturity of eight years.

2. Activation of the precautionary medium-term financial assistance and disbursements thereof may be requested until 30 September 2015.

Article 2

1. The precautionary medium-term financial assistance shall be managed by the Commission in a manner consistent with Romania's undertakings and the recommendations by the Council, in particular in the context of the implementation of Romania's National Reform Programme (NRP) and of the annual update of its Convergence Programme (CP).

2. The Commission shall agree with the Romanian authorities, after consulting the EFC, on the specific economic policy conditions attached to the precautionary medium-term financial assistance as listed under Article 3(3) of this Decision. Those conditions shall be laid down in a Memorandum of Understanding (MoU) consistent with the undertakings and recommendations referred to in paragraph 1 of this Article. The detailed financial terms shall be laid down by the Commission in a PLFA.

3. The Commission shall verify at regular intervals, in collaboration with the EFC, that the economic policy conditions attached to the precautionary medium-term financial assistance are fulfilled.

Article 3

1. The activation of the precautionary medium-term financial assistance shall be examined by the Commission, following a written request by Romania to the Commission. The Commission, after consulting the EFC, shall decide whether the activation of the assistance and the request for

disbursements under that assistance are justified, and shall decide on the amount and timing of such disbursements. In the event that that assistance is being activated, the funds may be made available in not more than two instalments. Each instalment may be disbursed in one or more tranches.

2. Upon activation of the precautionary medium-term financial assistance, the Commission shall decide on the disbursement of the Union loan, or parts thereof, after having obtained the opinion of the EFC.

3. Any disbursement shall be made on the basis of a satisfactory implementation of the economic programme of the Government to be included in both the CP and the NRP.

Furthermore, the specific economic policy conditions laid down in the MoU, shall include, inter alia:

(a) the adoption of budgets and the implementation of policies in line with the fiscal consolidation path derived from Romania's obligations under the Stability and Growth Pact with a view to reaching Romania's medium-term budgetary objective by 2015, and to maintaining it thereafter;

(b) the full preservation of the measures agreed under the previous two programmes and the implementation of any remaining parts of yet unfulfilled conditionality;

(c) the further strengthening of the fiscal governance framework, including through the implementation of the Treaty on Stability, Coordination, and Governance, so as to ensure that fiscal consolidation is well anchored. Particular attention shall be given to reinforcing multi- annual budgetary planning, to the implementation of an effective commitment control system, to improving tax collection, and to improving the capital budgeting process;

(d) the implementation of the action plans adopted in response to the findings of the functional reviews carried out by the World Bank in 2010-2011 in a timely manner and the establishment of a central delivery unit to improve the government-wide policy prioritisation;

(e) the clearing of arrears and the strengthening of budget control mechanisms in the health sector through improved reporting and monitoring frameworks;

(f) the implementation of the strategic action plan for healthcare, rationalising the hospital structure and increasing the scope for primary care activities, in order to improve health outcomes;

(g) the improvement of public debt management with a view to reducing risks and to consolidating and extending the yield curve for sovereign debt;

(h) the further strengthening of the bank-resolution framework, the Central Bank of Romania's contingency planning and the corporate governance of the Deposit Guarantee Fund, as well as the implementation of measures to speed up the process of national banks' balance sheet cleaning and the preservation of credit discipline in the banking sector;

(i) the alignment of the legislation on the Financial Supervisory Authority to international good practices to strengthen the supervision of the non-banking financial market;

(j) the restructuring of state-owned enterprises (SOEs), including sales of stakes in their capital, and strengthening the corporate governance of SOEs;

(k) the further implementation of measures to improve the business environment, including through the reduction of administrative burdens for the small and medium-sized enterprises (SMEs), and measures to facilitate access to finance for SMEs.

4. If required in order to finance the loan, the prudent use of interest rate swaps with counterparties of highest credit quality shall be permitted. The EFC shall be kept informed by the Commission of possible refinancing of the borrowings or restructuring of the financial conditions.

Article 4

This Decision shall take effect on the day of its notification.

Article 5

This Decision is addressed to Romania.

Done at Luxembourg, 22 October 2013.

For the Council

The President

L. LINKEVIČIUS

As published in OJ No L286 of 29 October 2013.

ANNEX 7
2013 Country-specific recommendations to Romania

THE COUNCIL OF THE EUROPEAN UNION,

[…]

HEREBY RECOMMENDS that Romania take action within the period 2013-2014 to:

1. Complete the EU/IMF financial assistance programme.

2. Ensure growth-friendly fiscal consolidation and implement the budgetary strategy for the year 2013 and beyond as envisaged, thus ensuring achieving the MTO by 2015. Improve tax collection by implementing a comprehensive tax compliance strategy and fight undeclared work. In parallel, explore ways to increase reliance on environmental taxes. Continue the pension reform started in 2010 by equalising the pensionable age for men and women and by promoting the employability of older workers.

3. Pursue health sector reforms to increase its efficiency, quality and accessibility, in particular for disadvantaged people and remote and isolated communities. Reduce the excessive use of hospital care including by strengthening outpatient care.

4. Improve labour market participation, as well as employability and productivity of the labour force, by reviewing and strengthening active labour market policies, to provide training and individualised services and promoting lifelong learning. Enhance the capacity of the National Employment Agency to increase the quality and coverage of its services. To fight youth unemployment, implement rapidly the National Plan for Youth Employment, including for example through a Youth Guarantee. To alleviate poverty, improve the effectiveness and efficiency of social transfers with a particular focus on children. Complete the social assistance reform by adopting the relevant legislation and strengthening its link with activation measures. Ensure concrete delivery of the National Roma integration strategy.

5. Speed up the education reform including the building up of administrative capacity at both central and local level and evaluate the impact of the reforms. Step up reforms in vocational education and training. Further align tertiary education with the needs of the labour market and improve access for disadvantaged people. Implement a national strategy on early school leaving focusing on better access to quality early childhood education, including for Roma children. Speed up the transition from institutional to alternative care for children deprived of parental care.

6. Strengthen governance and the quality of institutions and the public administration, in particular by improving the capacity for strategic and budgetary planning, by increasing the professionalism of the public service through improved human resource management and by strengthening the mechanisms for coordination between the different levels of government. Significantly improve the quality of regulations through the use of impact assessments, and systematic evaluations. Step up efforts to accelerate the absorption of EU funds in particular by strengthening management and control systems and improving public procurement.

7. Improve and simplify the business environment in particular through reducing administrative burdens on SMEs and implementing a coherent e-government strategy. Ease and diversify access to finance for SMEs. Ensure closer links between research, innovation and industry, in particular by prioritising research and development activities that have the potential to attract private investment. Step up efforts to improve the quality, independence and efficiency of the judicial system in resolving cases and fight corruption more effectively.

8. Promote competition and efficiency in network industries, by ensuring the independence and capacity of national regulatory authorities, and by continuing the corporate governance reform of state-owned enterprises in the energy and transport sectors. Adopt a comprehensive longterm transport plan and improve broadband infrastructure. Continue to remove regulated gas and electricity prices and improve

energy efficiency. Improve the cross-border integration of energy networks and speed up implementation of the gas interconnection projects.

Done at Brussels, 9 July 2013, For the Council, The President

As published in OJ No C 217 of 30 July 2013.

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