



GOVERNMENT OF ROMANIA

CONVERGENCE PROGRAMME FOR 2019-2022

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FOREWORD

The current edition of the Convergence Programme for 2019-2022 was elaborated on the basis of the Regulation (EC) no. 1466/1997 of the Council on strengthening the surveillance of budgetary positions and the surveillance and coordination of economic policies, as amended through the Regulation (EC) no. 1055/2005 of the Council and the Regulation (EU) no. 1175/2011 of the European Parliament and of the Council.

The Convergence Programme for 2019-2022 has been accomplished by considering the Code of Conduct on the Implementation Specifications of the Stability and Growth Pact and the Guidelines for the format and content of Stability and Convergence Programs of July 05, 2016.

The submission by the Member States and the assessment by the European Commission of the Convergence Programme is a component of the European Semester, which is a cycle of coordination of economic and budgetary policies. The European Semester is the main instrument for the Europe 2020 Strategy, the preventative instrument of the Stability and Growth Pact (amended by the 6-pack regulation which came into effect on December 13, 2011), and of the Macroeconomic Imbalance Procedure and Euro Plus Pact.

The 2019 edition of the Convergence Programme is based on the provisions of the Fiscal and budgetary strategy for 2019-2021 and the updated macroeconomic framework for the period 2018-2022 (the version of Spring 2019). Romania had in 2018 a cash budget deficit estimated at 2.9% of GDP, which corresponds to an ESA deficit estimated at 3.0% of GDP.

Budget planning for 2019 and the estimates for the period of 2020-2021 establish the ESA budget deficit of 2019 at 2.8% of GDP, an adjustment of 0.2 percentage points compared to 2018, which will continue over the horizon 2020-2022, and will reach 2.0% of GDP in 2022. Over the horizon 2019-2021, the fiscal and budgetary policy continues to directly support economic growth, within the margin allowed by the Stability and Growth Pact, respectively an ESA budget deficit of 3% of GDP.

According to statistical data, Romania continues to record a robust economic growth, among the biggest in the European Union. In the last 3 years, the average annual economic growth has been of 5.3%. In 2016, economic growth was 4.8%, in 2017 7%, and in 2018 4.1%.

The high economic growth has reduced Romania's development gaps compared to the other EU Member States. In 2017, GDP per capita in purchasing power standards (PPS) was 62.5% relative to the EU average, compared to 55.9% in 2015 and 59.3% in 2016.

It is estimated that in 2018 the GDP per capita in purchasing power standards had exceeded the ceiling of 65%. According to the Government Program, it is estimated “to exceed in 2021 the threshold of 70% of the EU average regarding GDP per capita in purchasing power standards”.

Romania maintains its commitment to join the Euro Area and in 2018 concrete steps were taken in this respect. Through GEO no. 24/2018 was established the National Commission for Underlying the National Plan for euro adoption, made up of representatives of the Government, independent experts, personalities from the academia, the Presidential Administration, employers’ associations and trade unions, the National Institute of Statistics, the National Bank of Romania, as well as nongovernmental organizations and representatives of the civil society, with the purpose of elaborating the Underlying Report for the National Plan for euro adoption and the National Plan for euro adoption.

At the end of December, the National Commission completed and assumed the two documents, and the Government approved these two strategic documents on January 30, 2019. As of that moment, all ministries are involved in the transposition of the Action Plan, and the strategic documents are publicly available. As an objective, resulting from the Underlying Report, Romania has assumed the euro adoption in 2024.

The Underlying Report analyses the Romanian economy in the perspective of adoption of the euro, emphasizing the issues it is facing, while the Plan for euro adoption draws the actions that Romania must undertake so that the process of accession to the Euro Area is characterized by maximizing the benefits and minimizing the negative effects. The Underlying Report presents scenarios regarding the economic evolution and the degree of convergence with the Euro Area. The Report concludes that through persevering efforts and solidarity of the social forces there are assumptions that in the horizon of 2024 Romania might fulfil the fundamental requirements for the adoption of the euro.

The National Plan for euro adoption emphasizes that in order to reach the objective of adopting the euro in 2024, which implies the entrance in ERM II at least two years before, concerted actions are necessary in strategic fields regarding the modernization and increase of Romanian economy’s robustness, such as:

- sustainable fulfilment of nominal convergence criteria and significant improvement of real convergence;
- budgetary consolidation through reduction of the structural budget deficit and increasing fiscal revenues;
- achieving a robust economic growth, based on investments and without increasing domestic and foreign deficits;

- implementing the structural reforms presented in the Plan of Adoption of the EUR currency;
- developing a macro-prudential monetary and fiscal-budgetary policy;
- amplifying investments in priority fields, namely education, health, and the transport infrastructure;
- improving the convergence and robustness of the banking and non-banking financial system;
- making the labour market more flexible;
- developing sectoral, industrial and small and medium enterprises policies which would lead to the improvement of competitiveness.

1. GENERAL FRAMEWORK AND OBJECTIVES OF THE ECONOMIC POLICY

1.1. GENERAL FRAMEWORK

Romania continued to record a robust economic growth of 4.1% in 2018, determined on the supply-side by industry and services especially, and on the demand-side by a positive contribution of aggregated domestic demand. Private consumption was supported by the reduction of indirect taxes and the increase of salaries in the public and private sectors. Romania has registered in recent years' considerable progress in reducing macroeconomic imbalances, which, together with the monetary policies and structural reforms implemented or in process of implementation, have contributed to maintaining macroeconomic and financial stability.

In perspective, the GDP growth will be at high levels, 5.5% in 2019, 5.7% in 2020, and 5% in the following years respectively. It is estimated that investments will strengthen on the basis of an improvement in the implementation of projects financed from EU funds, of the increase of population's revenues, as well as of the amplification and diversification of national financing budgetary sources.

With regard to the external sector, we estimate a reduction of the negative contribution of net export to the GDP growth from -1.7 p.p. in 2018 to -0.6 p.p. in 2019 and -0.5 p.p. afterwards. In 2018, the current account deficit was 4.5% of GDP and shall be reduced to 3.4% in 2019, being financed mostly from foreign direct investments.

With regard to employment, in Q3 2018, according to the data provided by the National Institute of Statistics (NIS), the employment rate of the population aged 20 to 64 years increased by 1 percentage point compared to the same period of the previous year, to 71.3%, thus exceeding the national target of 70% set within the framework of the Europe 2020 Strategy. The unemployment rate, according to AMIGO, decreased from 4.7% in 2017 (Q3) to 3.9% in 2018 (Q3), the lowest value from the last decade.

At the same time, the labour force in Romania continues to face the restriction represented by the demographic evolution. On January 1, 2017, the resident population in Romania was of 19,644.4 thousand residents, compared to 19,916.5 thousand residents in 2014¹. Negative values of the natural growth, conjugated with those of the international migration balance, made the resident population decrease between July 1, 2014 and January 1, 2017 by 272.1 thousand persons, according to NIS.

In spite of these evolutions, a series of challenges remain, with regard to:

- Economic and social inclusion, because there continue to be big gaps between rural and urban areas, as well as at regional level. Although most regions of Romania have registered progress with regard to certain key indicators for

economic growth, they remain below the EU average, with the exception of the Bucharest-Ilfov region. Thus, in 2016, the GDP/capita in PPS at the level of Bucharest-Ilfov region is over the European average, while in the rest of the regions the GDP/capita in PPS does not exceed 60% of the EU28 average.

- Inequality of revenues: in 2017, Romania registered a value of the Gini indicator of 35.1, a slight increase compared to the previous year (34.7). Also, the S80/S20 ratio reflects the fact that in 2017 the first 20% of Romanians with the biggest revenues earned 7 times more than 20% of those with the lowest revenues, the ratio slightly improving compared to the previous year.
- The participation rates to the labour market, which, in spite of the labour force deficit, remain low in the case of certain categories of individuals considered vulnerable relative to the labour market. The rate of youth aged 15 to 24 years who are unemployed and are not in any form of education or training (NEET rate), although it has decreased as of 2015, continues to be relatively high (compared to the EU average), being at 15.2 in 2017, respectively at 14.8 in Q3 of 2018.
- The structural changes induced by fast technological advancements, like digitization, automation, robotics or artificial intelligence, as well as the skills demand, which is continuously growing and changing, represent considerable challenges for the professional training system and for the adults who are on a labour market that is fast evolving.

1.2. FISCAL POLICY

Regarding budget revenues, a few new measures were implemented in 2019, both with regard to fiscal facilities and to tax increases of . In the field of the personal income tax and mandatory social contributions for the revenues from salaries and assimilated to salaries (comprised between 3000 and 30000 Lei/month) obtained by people who work in the constructions sector, no personal income taxes, health insurance contributions or contributions for special working conditions shall be charged, and the social insurance contribution and the labor insurance contribution shall be reduced. Regarding VAT, the VAT rate was reduced for water supply and sewerage services and the reduced rate of 5% was extended for certain transport services and for housing market. Since the reverse taxation mechanism is considered a useful instrument in order to fight VAT fraud, the enforcement thereof was extended until June 2022. With regard to excise duties, it was

¹ On July 1.

increased the level of the total excise duty of cigarettes and a schedule of gradual increase of this level was provided.

As of January 1, 2018, the transfer rate to the second pension pillar is 3.75%, maintaining the same amount transferred as in 2017², given the transfer of contributions and the increase of gross salaries.

In order to improve voluntary compliance, the creation of technical and procedural conditions for payment of all tax liabilities through all banking instruments is targeted (modernization of the procedures and instruments dedicated to the citizens for registration and payment of tax liabilities through the construction and publication of the electronic register of taxes, local charges and other contributions; digitalized fiscal assistance for the taxpayers). Regarding the reduction of tax evasion and grey economy actions like the following will be implemented: the introduction of the random compliance testing program through fiscal controls, the fight against tax evasion in the field of VAT, including cross-border fraud in this field, control actions designed to stimulate the equipment of economic operators with electronic cash registers and the issuance of fiscal receipts, the fight against customs fraud. In the field of fiscal anti-fraud it is sought to increase the share of controls dedicated to de-structuring of evasion chains, in order to eliminate “ghost” companies from the system, to intensify the use of administrative cooperation instruments in the field of VAT, including multilateral controls and to revise anti-fraud procedures in accordance with the European risk management model.

Regarding expenditure, the minimum gross salary at national level increased, but at a lower rate than previous increases. As of January 2019, the minimum gross salary at national level is set at 2080 Lei, and for the personnel employed on positions that require higher education (with a work seniority of at least one year on a position requiring higher education) it amounts 2350 Lei. For the constructions field, the minimum guaranteed gross salary at national level was set at 3000 Lei per month for the period between January 1, 2019 and December 31, 2019.

Salary increases for the personnel from the public sector continued by an increase of 1/4 of the difference between the salary provided by law for 2022 and the level thereof in 2018. As of September 1, 2019 there will be provided increases of the pension point by 15% and of the social allowance for the retired by 10%. On the other hand, the bonuses, allowances, compensations, premiums and other elements of the salary system that are

² of approximately 7 billion Lei

part, according to law, of the gross monthly salary of the personnel paid from public funds, shall be maintained at most at the level of the amount of December 2018.

At the same time, since April 1, 2019 the allowances for children increased (to 300 Lei for children younger than 2, or up to 3 years of age in the case of children with disabilities; to 150 Lei for children aged between 2 and 18 years, as well as for the youth who turned 18 and are registered in high school or professional education).

1.3. MONETARY AND EXCHANGE RATE POLICIES

In compliance with its Statute³, the primary objective of the National Bank of Romania (NBR) is to ensure and maintain price stability, which is the best contribution monetary policy can make to sustainable economic growth. The NBR formulates and implements monetary policy in the context of inflation targeting⁴, seeking to bring and to maintain over the medium term the annual inflation rate in line with the 2.5 percent ± 1 percentage point inflation target⁵, as well as to lower the annual inflation rate in the longer run to a level compatible with the European Central Bank's quantitative definition of price stability.

From this perspective, the specific context of 2018 called for the further adjustment of the monetary policy stance in 2018 H1 by raising the monetary policy rate, and afterwards warranted the status-quo of the policy rate and of the parameters of key policy instruments. The action steps taken by the NBR supported the return of the annual inflation rate inside the variation band of the target towards end-2018, after having climbed significantly above the upper bound of the band in Q2, and also proved decisive in anchoring longer-term inflation expectations.

The NBR's approach in the first part of the year was warranted by the markedly steeper upward path of the annual inflation rate in the closing months of 2017⁶, which had exceeded expectations, but especially by the outlook for its rise and remaining well above the variation band of the target in the first three quarters of 2018 and significantly above the previously-forecasted values, before probably returning but also levelling off in the upper half of the band starting in January 2019. Specifically, according to the medium-

³ Law No. 312/2004.

⁴ The NBR adopted inflation targeting in August 2005.

⁵ The NBR adopted a multi-annual flat inflation target of 2.5 percent ± 1 percentage point in December 2013.

⁶ The annual inflation rate had picked up from 1.8 percent in September to 3.3 percent in December 2017 – very close to the upper bound of the variation band of the target – owing primarily to the action of supply-side factors: the increase in the electricity price, costlier fuels as a result of higher international oil prices and the reintroduction of the special excise duty on motor fuels, as well as the rise in prices of vegetables, fruit and eggs (VFE) and prices of tobacco products.

term forecasts updated during that period, the annual inflation rate was expected to climb at mid-year and stand still for a few months at around 5 percent – hence above the values projected in November 2017 –, before returning to the vicinity of the upper bound of the variation band of the target in December 2018 and reaching 3.1 percent at end-2019. The forecasted deceleration in inflation was not automatic, but rather implied gradually less accommodative monetary conditions through monetary policy action.

The sizeable fluctuation in the annual inflation rate over the short time horizon was attributable to the transitory action of supply-side factors, anticipated to be even more strongly inflationary in the short run than in the November 2017 forecast, but at the same time generating sturdier disinflationary base effects starting 2018 Q4⁷.

By contrast, steadily rising inflationary pressures – and, in turn, stronger than in the November 2017 forecast – were anticipated to be generated in aggregate by fundamentals, with the annual adjusted CORE2 inflation rate seen rising gradually, from 2.4 percent in December 2017 to 3.4 percent at end-2019 and then to the upper bound of the target band in March 2020⁸. Such pressures were anticipated to stem in 2018 from the cyclical position of the economy and from the steep uptrend in short-term inflation expectations, while in 2019 from the dynamics of import prices; influences in the same direction, albeit relatively softer, were expected throughout the forecast horizon from wage costs, given the labour market tightening.

The outlook for a relatively sharper increase in excess aggregate demand over the near term was driven by the much swifter-than-expected pick-up in economic growth in 2017 Q3⁹ and for the year as a whole – primarily on account of the markedly faster rise in household consumption, prompted by fiscal and wage stimuli –, associated with GDP

⁷ The most notable influences were expected from the hikes recorded towards end-2017 and at the beginning of 2018 in electricity, natural gas and heating prices, as well as from costlier fuels. Similar effects would stem from the likely dynamics of VFE prices, as well as from the hikes in tobacco product prices, all of which overlapped in the early months of 2018 the inflationary base effects associated with the previous cuts and removals of indirect taxes and declines in administered prices, such as: the standard VAT rate cut from 20 percent to 19 percent and the removal of the special excise duty on motor fuels as of 1 January 2017 and the scrapping of non-tax fees and charges in February 2017.

⁸ According to the medium-term forecast published in the May 2018 *Inflation Report*.

⁹ Annual GDP dynamics advanced to a post-crisis high of 8.8 percent in Q3, from 6.1 percent in 2017 Q2; economic growth witnessed the fourth successive faster-than-expected acceleration, implying a notably wider-than-anticipated opening of the positive output gap. As a general rule, statistical data on economic growth are those available at the time of conducting the assessment underlying the monetary policy decision.

dynamics probably remaining above potential in 2018¹⁰, mainly as a result of the protracted expansionary nature of fiscal and income policies¹¹.

Against this background, in the absence of monetary policy measures, the inflation bout anticipated to be driven in the first part of the year by supply-side shocks might have triggered significant second-round effects via the de-anchoring of medium-term inflation expectations, conducive to a protracted and larger rise in consumer prices and implicitly compounding the efforts and economic costs of bringing inflation back under control. The relevance of this risk was heightened by the marked increase – in line with the NBR forecast – in the annual inflation rate during the first quarter of the year¹², inter alia amid the pick-up in core inflation¹³, as well as by the risk of a higher-than-expected rise in fuel prices, given the developments in oil prices and in the exchange rate.

Another matter of concern consisted in the persistently high dynamics of imports of goods and services, amid the overly fast expansion of domestic demand, consumer demand in particular, conducive to a faster worsening – including in the early months of 2018 – of the trade balance, as well as to a sped-up deepening of the current account deficit, with potential implications for the evolution of the exchange rate.

Under these circumstances, after having narrowed the symmetrical corridor of interest rates on standing facilities around the policy rate by a total of ± 0.50 percentage points¹⁴ in 2017 Q4, the NBR embarked on a policy rate hiking cycle at the beginning of 2018, raising the monetary policy rate in January, March and May by 0.25 percentage points

¹⁰ Economic growth was, however, expected to decelerate in 2018, after the exceptional pace recorded in 2017, i.e. 6.9 percent.

¹¹ Amid the implementation in 2018 of a new package of fiscal, wage and other income measures, including: the cut in the personal income tax rate from 16 percent to 10 percent; the cut in the overall rate of mandatory social security contributions from 39.25 percent to 37.25 percent and transferring them in the charge of employees; the hike in the economy-wide gross minimum wage as of 1 January 2018; the raise in the pension point from lei 1,000 to lei 1,100 as of 1 July 2018. Moreover, the unified wage law provided for a 25 percent rise in the gross wages of budgetary sector employees in January 2018, followed by a 20 percent rise in the gross wages of staff in the education sector in March, as well as gradual pay rises by 2022 for each category of employees, except for doctors and nurses, whose wages were to grow in one go in March 2018.

¹² The annual inflation rate stepped up to 4.9 percent in March 2018, significantly above the upper bound of the variation band of the target.

¹³ The annual adjusted CORE2 inflation rate advanced to 3 percent in March 2018, slightly higher than the forecasted level of 2.8 percent and considerably above the midpoint of the target.

¹⁴ The corridor was narrowed by ± 0.25 percentage points in October and November 2017 respectively, to the standard width of ± 1 percentage point.

each time, thus bringing it to 2.50 percent¹⁵. Moreover, in order to strengthen the impact and relevance of the policy rate and its signalling role, implicitly the transmission of impulses of its change, the NBR tightened control over liquidity in the banking system by initiating in mid-April and then further conducting one-week deposit-taking operations, via full-allotment auctions. Against this backdrop, relevant interbank money market rates witnessed a marked increase in Q2, climbing and consolidating towards the end of that quarter significantly above the monetary policy rate, while the EUR/RON exchange rate remained relatively stable.

The NBR discontinued the policy rate hiking cycle in July, keeping the monetary policy rate unchanged at 2.5 percent until end-2018¹⁶, given that – as anticipated – the annual inflation rate had stopped increasing in June¹⁷ and then embarked on a generally downward trend¹⁸, expected to steepen towards year-end¹⁹, while economic growth had seen during H1 overall a sharper-than-forecasted deceleration²⁰ – amid the sudden slowdown in consumer demand, the standstill in investment and the deterioration in net exports –, implying a moderation of the cyclical position of the economy including when compared to forecasts²¹.

A levelling-off, at least temporary, of demand-side inflationary pressures, consumer demand pressure in particular, was also hinted at by developments in adjusted CORE2 inflation, whose annual rate slowed from the 3.1 percent peak recorded in April to 2.8 percent in September²². Unit labour costs increased, however, at a faster pace during the

¹⁵ Accordingly, the deposit facility rate was raised progressively to 1.50 percent and the lending facility rate to 3.50 percent. At the same time, the central bank kept the minimum reserve requirement ratios on both LEU- and foreign currency-denominated liabilities of credit institutions at 8 percent.

¹⁶ At the same time, the deposit facility rate and the lending facility rate were maintained at 1.50 percent and 3.50 percent respectively; furthermore, the NBR preserved the minimum reserve requirement ratios on both LEU- and foreign currency-denominated liabilities of credit institutions at 8 percent.

¹⁷ The annual inflation rate remained in June at its May high of 5.4 percent – only slightly above the forecast.

¹⁸ The annual inflation rate fell in September to 5.0 percent.

¹⁹ Mainly on account of the action of supply-side factors, consisting especially in the disinflationary base effects associated with the evolution of volatile and administered prices; additional influences stemmed from the decreases seen towards year-end by fuel prices and prices of fruit and vegetables.

²⁰ In 2018 Q1, economic growth decelerated to 4 percent from 6.7 percent in 2017 Q4, before posting a marginal reacceleration in Q2, to 4.1 percent.

²¹ The positive output gap narrowed in 2018 Q1, contrary to expectations, but witnessed a renewed, larger-than-anticipated increase in Q2, remaining during H1 as a whole slightly below the values recorded in the latter part of 2017 and the projected levels.

²² The decline was largely attributable to the evolution of international prices of some agro-food items, including the associated base effects, as well as to the relative appreciation of the LEU against the euro.

first three quarters of 2018 overall, against the background of the annual dynamics of average gross nominal wage earnings remaining in the double-digit range, also amid the further tightening of the labour market to a post-crisis high.

Key interbank money market rates saw their positive spread vis-à-vis the monetary policy rate narrow slightly starting August, yet their differential versus those on European financial markets remained substantial, which translated into a relative stability of the EUR/RON exchange rate, even amid the renewed step-up in the growth rate of the current account deficit in Q3 against the same year-earlier period²³, associated with the decrease in its coverage by foreign direct investment and capital transfers.

At the same time, the medium-term forecasts updated in the second half of the year showed and reconfirmed slightly improved prospects for inflation, whose annual rate was expected to decline to 3.5 percent in December 2018 and then to 2.9 percent at end-2019²⁴ versus 3.6 percent and 3.0 percent respectively in the May forecast²⁵. Slightly lower-than-previously-forecasted annual rates were also envisaged for core inflation, which was expected to step up more visibly its easing trend towards end-2018²⁶, before regaining momentum starting with mid-2019 H1, in the context of simultaneous, gradually rising inflationary pressures anticipated to stem from aggregate demand and wage costs, as well as from short-term inflation expectations and import prices.

Excess aggregate demand was seen to increase in 2019, given that the pace of economic growth – after a likely stronger-than-previously-projected moderation in 2018 – was expected to regain momentum and markedly exceed the potential rate in 2019. The outlook was compatible with the expansionary nature of fiscal policy abating in 2018 and remaining unchanged in 2019, as well as with less accommodative monetary conditions. However, it also assumed an improvement in EU funds absorption and still robust economic growth in the euro area/EU and globally, albeit slightly slower than in the previous forecasts.

²³ Owing primarily to the worsening of the trade balance.

²⁴ The forecast updated in August even saw inflation at 2.7 percent at the end of 2019, but this level was revised to 2.9 percent in the November forecasting round.

²⁵ The slowdown was anticipated to be driven primarily by the action of supply-side factors, with a decisive contribution from disinflationary base effects associated with the sizeable increases recorded starting with 2017 Q4 by all CPI exogenous components (administered prices, fuel prices, tobacco product prices and VFE prices), but also by some processed food prices.

²⁶ Reflecting the fadeout of the impact exerted on processed food prices by the increase, towards the end of the previous year, in the prices of some agro-food commodities on international markets.

At the same time though, the prospects for the European economy were surrounded by strong uncertainty, owing to heightened risks posed by the protectionist trade policies, the UK's exit from the EU, the political tensions in some European countries, as well as by international financial market volatility. Domestically, major sources of uncertainties and risks were consumer confidence and the pace of EU funds absorption, but also labour market conditions and the fiscal and income policy stance. Nevertheless, the ECB's monetary policy stance continued to be particularly relevant, also in relation to the decisions taken by central banks in the region.

In this context, ensuring adequate monetary conditions from the perspective of anchoring medium-term inflation expectations and maintaining the annual inflation rate in line with the medium-term forecast, while safeguarding financial stability, warranted the policy rate status-quo.

According to subsequently released data, the annual inflation rate saw an even larger-than-expected downward correction in 2018 Q4— returning in November and consolidating in December in the upper half of the variation band of the target²⁷ –, while the economic growth momentum stuck to a slight uptrend in Q3²⁸ solely on account of the much swifter-than-expected step-up in agricultural output, thus signalling a halt in the widening of the positive output gap. In turn, the medium-term forecast updated in February 2019 reconfirmed the outlook for the annual inflation rate to decline further in the first three quarters of the year, due to the action of supply-side factors, but also to climb and remain slightly below the upper bound of the variation band of the target in the latter part of the forecast horizon²⁹, amid the likely strengthening of inflationary pressures from fundamentals.

The uncertainties associated with the medium-term forecast were, however, significantly compounded by the new fiscal and budgetary measures effective 1 January 2019, as well as by the still pending 2019 draft budget, with implications for the future fiscal and income policy stance. To these added heightened uncertainties related to the slowdown in euro area and global economic growth, owing to higher risks stemming from the trade row and the UK's exit from the EU, as well as from the tightening trend of financial conditions.

²⁷ The annual inflation rate dropped to 3.4 percent in November (4.2 percent in October) and then to 3.3 percent in December.

²⁸ The annual GDP dynamics picked up to 4.2 percent.

²⁹ The annual inflation rate was seen at 3.0 percent in December 2019 and at 3.1 percent in March 2021 (end of the projection horizon).

Moreover, further relevant were the monetary policy stance of the ECB and the probable stance of central banks in the region.

Under these circumstances, the monetary authority extended the status-quo of monetary policy instruments into the early months of 2019.

Looking ahead, given another jump of the inflation rate above the variation band of the target in 2019 Q1, monetary policy will further be geared towards bringing and keeping the annual inflation rate in line with the flat target, inter alia via the solid anchoring of inflation expectations over the longer time horizon, in a manner conducive to supporting sustainable economic growth and amid safeguarding financial stability.

Both in the short run and over the longer time horizon, the dosage and pace of potential future adjustments in the monetary policy parameters, the NBR's policy rate included, in the context of tailoring real monetary conditions, will be correlated mainly with the intensity of inflationary pressures anticipated to be exerted by the positive output gap and by wage costs, as well as with the behaviour of medium-term inflation expectations and the related risks.

The uncertainties and configuration of the balance of risks associated with the medium-term inflation forecast, including the probability of their materialising, will further play an essential part in substantiating the NBR Board's decisions. The monetary policy stance of the ECB and the stance of central banks in the region will also remain particularly relevant.

Moreover, the characteristics of the monetary policy transmission mechanism will continue to be very important landmarks, especially those concerning lending to the private sector and the saving behaviour, which will likely be influenced by the fiscal and budgetary measures implemented this year, especially those regarding the banking sector.

Particularly important in terms of monetary policy conduct and implementation also remain the characteristics of fiscal policy, of structural reforms, and of EU funds absorption, given that ensuring a balanced macroeconomic policy mix and enhancing the economic growth potential are pivotal to meeting the medium-term price stability objective, as a prerequisite for sustainable economic growth, but also to strengthening the capacity of the Romanian economy to withstand potential adverse developments.

2. ECONOMIC PERSPECTIVES

2.1. GLOBAL ECONOMY/TECHNICAL ASSUMPTIONS

The forecasts from the Spring Forecast of the International Monetary Fund estimate an economic growth at global level of 3.3% for 2019, which shall accelerate to 3.6% in 2020. According to the IMF, advanced countries are expected to record an average increase of 1.8% in 2019 and, respectively, 1.7% in 2020, while developing countries will have average advances of 4.4% in 2019 and 4.8% in 2020.

According to the Winter Forecast of the European Commission, the real GDP of the EU is forecasted to reduce its growth rhythm to 1.5% in 2019, but starting with 2020 a recovery is provided, the expected growth for this year being of 1.8%. With regard to the Euro Area, it is estimated a growth rate of 1.3% for 2019, and in 2020 will be recorded an improvement of the dynamics of real GDP up to 1.6%.

With regard to the economic growth rhythm at world level (excluding the EU), the forecast of the European Commission shows robust dynamics, respectively an advance of GDP by 3.8% in real terms both in 2019 and in 2020.

The economic evolution of Germany, Romania's main commercial partner and the main engine of the EU economy, is designed to slow down to 1.1% in 2019. For 2020 is provided an intensification of the economic activity by 1.7% in real terms, with a positive effect on Romanian exports. Also, for Italy, the second commercial partner of Romania, it is foreseen a dynamic of the GDP in 2020 of 0.8%, after a relative stagnation in 2019 (+0.2%). With regard to France, it is expected an acceleration of GDP growth from 1.3% in 2019 to 1.5% in 2020, based on growing imports.

According to the forecasts of the European Commission, for the EU it is expected that basic inflation rate, which excludes energy and non-processed food price volatility, will remain at moderate rates.

In the Euro Area, inflation reached 1.7% in 2018. It is estimated that this rate will be of 1.4% in 2019 and shall marginally increase to 1.5% in 2020, based on the increase of salaries.

In the Winter Forecast, the European Commission emphasized the fact that the price of Brent oil reached in the last period of 2018 the value of 55 USD/barrel, then it followed an ascending trend, as a result of Saudi Arabia's intention of reducing oil export. On the forecast horizon 2019-2020 it is expected that the price of Brent oil will reach 61 USD/barrel, on average, although in the last months of 2019 the price of oil significantly increased, exceeding the ceiling of 70 USD/barrel.

Considering the evolution of the world economy in the following period, in Romania, for the time interval 2019-2020 are estimated average annual growths of the exports of goods by 8.8% and of the imports by 9.3%. After in 2018 the FOB-CIF commercial deficit registered a weight of 7.5% in GDP, it will marginally extend to 7.8% in 2019 and 8.1% in 2020.

Table 1: Evolutions at global level

	2018	2019	2020
Real economic growth, at global level (%)	3.6%	3.3%	3.6%
Real economic growth - EU (%)	2.1%	1.5%	1.8%
Economic growth - Euro area	1.8%	1.3%	1.6%
Inflation rate - EU	1.8%	1.6%	1.7%
Brent oil price (\$/barrel)	71.5	61.2	61.2

Source: IMF and the European Commission

2.2. CYCLICAL EVOLUTIONS AND CURRENT PERSPECTIVES

2.2.1. CURRENT PERSPECTIVES

In 2018, Romania registered **a robust growth of the gross domestic product, of 4.1%** in real terms, one of the biggest economic growth rates among the EU Member States. While the economic growth of 2018 of the Euro Area was of only 1.8%, **Romania continued the fast real convergence process towards the level of development and welfare of this area.**

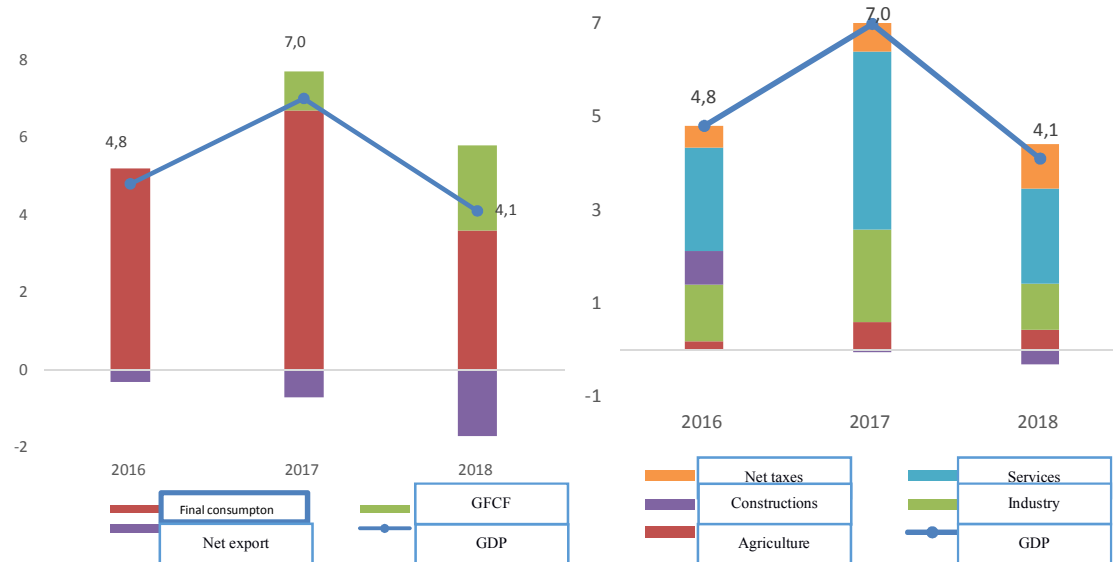
In 2018, the value of the gross domestic product was of 944.2 billion Lei, which means a plus of 87.5 billion Lei compared to 2017, relative to an increase of 91.6 billion Lei in 2017 and of 52.5 billion Lei in 2016.

Domestic demand increased by 5.7% in 2018, out of which, final consumption increased by 4.5%, while population consumption, based on a higher inflation and a more restrictive monetary policy, tempered the growth it manifested in the last 2 years, and increased by 5.3%. Also significant is the fact that gross accumulation (gross investments plus stock accumulation) accelerated its growth to 9.6% in 2018 (from 4.2% in 2017).

Investments in the economy, respectively gross accumulation, reached in 2018 a value of 200.4 billion Lei, compared to only 175 billion Lei in 2017, an increase of 14.5%. Within them, gross fixed capital formation decreased by 3.2% compared to 2017. At the same time, stock variation registered a positive contribution of 2.9 percent.

Exports of goods and services increased in real terms by 5.4%, while import of goods and services increased by 9.1%. Within them, export of services increased by 8.5%, and import of services by 14.4%, so that the surplus from foreign trade with services is maintained at over 4% of GDP. These evolutions made **net export** register a negative contribution to the growth of gross domestic product of 1.7 percent.

Graph 1: Contribution to real growth GDP growth



Source: National Institute of Statistics

In terms of domestic offer, **industry represented the engine of this evolution**, with a contribution to real growth of the gross domestic product of one percentage point, the value added by this branch increasing by 4.1%. The branch “Commerce, transport and storage, hotels and restaurants” had a contribution of 0.7%.

Also, **agriculture** had a substantial contribution, the gross added value of this branch increasing by 10% compared to 2017, the contribution being of 0.4 percentages.

A second defining element is represented by **the evolution of modern services with high added value**, respectively IT and scientific and technical services. The branch “Information and communications” registered a dynamic of 7.2% and a contribution of 0.4%. The branch “Professional, scientific and technical activities; activities of administrative services and activities of support services” increased its gross added value by 5.7%, which means a contribution of 0.4% to the economic growth of 4.1%.

Looking at the big picture, it can be assessed that four branches (industry, agriculture, information and communications, as well as scientific and technical services) have ensured almost 54% of economic growth (2.2 percentages of 4.1%).

In 2018, **consumer prices** increased on average by 4.63% compared to the previous year, based on the increase of prices for non-food goods (6.20%), while prices of food goods increased by 3.75%, and services tariffs by 2.53%. The increase registered in 2018 was due both to the exceeding of the statistical effect associated to the fiscal relaxation measures from the beginning of 2017 (the reduction of the VAT rate and the elimination of over-excise and of certain non-fiscal duties), and to the increase of international quotations for oil (+33.1% compared to 2017), as well as to the energy group (+10.4% in 2018 compared to the previous year). An important contribution was brought by the nominal depreciation of the national currency, which was of 1.84%.

In March 2019, annual inflation was of 4.03%, based on the increase of prices for food goods by 4.45% and of non-food goods by 4.15%, while services tariffs increased by 3.18%. Compared to December 2018, consumer prices increased by 2.13%, an evolution determined by the increase of prices for food goods by 3.08%.

In 2018, **employment** decreased by 0.2% based on the data from the National Accounts. The number of employees in the economy increased by 1.7%, representing 76% of the employed population. The increase was mainly due to the evolution from industry and services, where the number of employees increased by 1.0% and 2.2%, respectively. Significant is the fact that the number of employees from agriculture accelerated its growth to 2.3% in 2018 (from 1.4% in 2016 and 1.5% in 2017). The unemployment rate, according to AMIGO, continued its descending trajectory, decreasing from 4.9% in 2017 to 4.2% in 2018, a historical minimum.

2.2.2. CYCLICAL EVOLUTIONS

Romania benefits of one of the fastest growths of potential GDP at European level, a growth which will be around the value of 5% yearly on medium term. These estimates were made on the basis of the common methodology agreed by all EU Member States.

The forecasted GDP evolution is the result of positive contributions of all production factors, the most important being that of the total productivity of the factors, followed by the significant contribution of capital stock.

Table 2: Contribution of the factors to potential GDP's growth

	Potential GDP (%)	Contributions - percentage points -			Output Gap (%)
		Capital	Labor	PTF	
2018	4.7	0.6	0.6	3.4	0.0
2019	5.0	0.8	0.6	3.5	0.5
2020	5.1	1.1	0.5	3.5	1.0
2021	5.0	1.2	0.2	3.5	1.0
2022	4.8	1.4	-0.1	3.4	1.2

Note: Differences when summing up, where applicable, are due to rounding offs

Source: National Commission of Strategy and Prognosis

The **Output-gap**, the difference between the levels of GDP and potential GDP, expressed as percentage of the potential GDP, was closed in 2018, from a positive value of 0.7% of the potential GDP in 2017. Domestic estimates show that, as of 2018, the output gap is following a slightly positive trend (approximately 1% of the potential GDP).

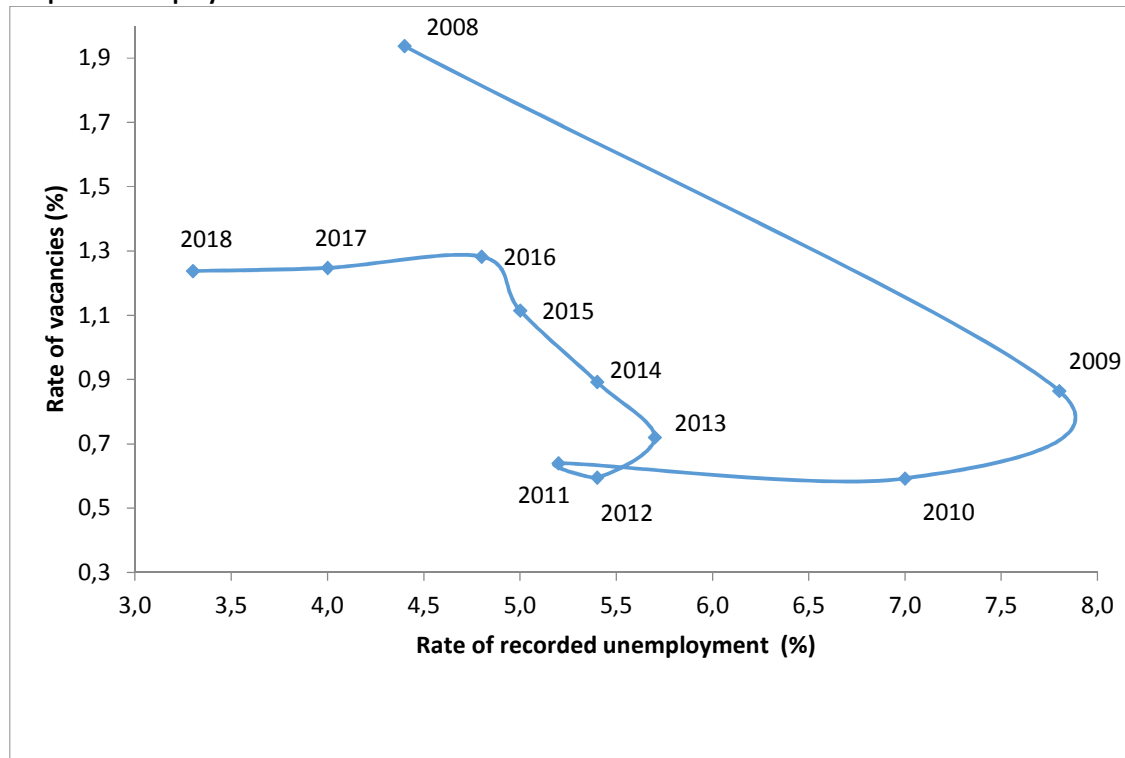
The main contribution to the potential growth comes on the side of **total productivity of the factors**, this positive trait of the Romanian economy representing a trend valid for approximately a decade, both in national estimates and in the estimates of the European Commission.

In perspective, **a significant increase of the contribution of capital stock** to real growth of the potential GDP is expected, from 0.6 percentage points in 2018 to 1.4 percentage points on the forecast horizon. The labor factor has a decreasing contribution decisively determined by the constant decrease of the working aged population. The main restrictive factor of the growth potential of Romanian economy is represented by the demographic factor, the population at working ages being 4.7% smaller in 2018 than in 2010. Nevertheless, the negative evolution of the demographic factor is compensated on medium term by an ascending trend of the activity rate.

Also significant is the fact that the BIM unemployment rate has gotten closer to the **NAWRU (Non Accelerating Wages Rate of Unemployment)** rate, an indicator which shows labor market sustainability. Romania has currently one of the lowest natural rates of unemployment among the Member States. In the horizon of year 2022, an unemployment rate of 3.8% is foreseen, given that NAWRU, estimated with the help of the common methodology at European level, reaches 3.9%. Thus, it can be said that Romania's economy will operate on medium term at full occupancy.

The data regarding the evolution of unemployment and of the rate of vacancies reveals that in the current period of economic growth, the labor force market has been operating optimally, given the increased demand.

Graph 2: Unemployment rate and rate of vacancies



Source: National Institute of Statistics

Thus, as a result of the measures implemented in 2017 and 2018 to support the business environment and a proactive salary policy, the significant decrease of the unemployment rate in the last two years occurred under the conditions of a constant and low level of the rate of vacancies.

Given that in the last two years, on the whole, only on a salary basis approximately 350 thousand jobs were created, the evolution of the rate of vacancies showing that the operation of Romanian economy at full occupancy is sustainable.

2.3. MEDIUM TERM SCENARIO

The macroeconomic framework for the Convergence Program considered: (i) the positive impact of the measures provided in the Governance Program on the business environment and on the population's purchase power, as well as a consolidation of the investment process; (ii) the European and global framework, emphasized in the European Commission's Winter Forecast; (iii) the economic and social achievements of 2018 and the first months of 2019. As a result, it is expected that Romania's economy will continue to obtain performances, and the gross domestic product will increase on average by 5.3% yearly, slightly over the potential.

For 2019, an economic growth of 5.5% was estimated, as result of a positive contribution of domestic demand (6.1 percentage points) and of a slightly negative contribution of net export (-0.6 percentage points). Within domestic demand, it was estimated that gross investments (gross fixed capital formation) will be increased by 6.9%.

Table 3: GDP components

Percentage changes	2018	2019	2020	2021	2022
Real GDP	4.1	5.5	5.7	5.0	5.0
Final consumption	4.5	5.9	5.7	4.8	4.8
- Private consumption expenses	5.2	6.4	6.2	5.5	5.4
- Public consumption expenses	1.8	4.1	3.8	2.3	2.3
Gross fixed capital formation	-3.2	6.9	7.9	7.4	7.5
Exports of goods and services	5.4	6.9	7.1	7.0	7.0
Imports of goods and services	9.1	7.8	7.9	7.8	7.8

Source: National Commission of Strategy and Prognosis

For 2020-2022 it is estimated that Romanian economy will increase at a more sustained pace, with an average annual pace of 5.2%. Domestic demand (consumption and investments) will continue to represent the main engine of economic growth during this interval.

Private consumption expenses will increase on average by 5.7% yearly, based on the improvements from the labor market. Gross fixed capital formation will record an accelerated growth rhythm (7.6% yearly, on average), based on the improvement of the investment climate through the measures that are considered, as well as on the financing conditions both from budget sources and from structural and investment funds.

Medium term economic growth will create the conditions for improvement of employment, especially with regard to the number of employees. Thus, it is estimated that the working population will gradually increase until 2021, the structure changing in favor of the employees whose share is estimated to be close to 77% in 2022 compared to 74% in 2018. Thus, the unemployment rate, according to AMIGO, will continue to decrease, from 4.2% in 2018 to 3.8% in 2022.

For 2019, it is estimated that **inflation** will be reduced both as annual average, down to 3.4%, as well as at the end of the year, down to 3.2%.

It is expected that inflation will continue its descending trend between 2020 -2022 in the absence of other shocks, reaching 2.2% in 2022 at the end of the year and 2.4% as annual average.

2.4. BALANCE OF THE EXTERNAL SECTOR

In 2018, the increase of goods exports was of 8.1% compared to 2017, while imports increased by 9.6%. Under these circumstances, the FOB-CIF commercial deficit increased by 16.8% compared to 2017.

In the first two months of 2019, Romania's exports increased by 4.8%, while imports registered an increase of 10.1% compared to the corresponding period of the previous year. Thus, the FOB-CIF commercial balance closed at the end of the first two months of 2019 with a deficit of 2.4 billion EUR, 45.2% bigger than the one from the similar period of 2018.

It is expected that export will remain in 2019 a component of demand which supports Romania's economic growth. Thus, it is estimated an increase of goods export by 8.9% and for the import of goods by 9.4%. On the whole, the forecast for 2019 shows that commercial deficit will have a share in the GDP of 7.8%.

For the interval 2019-2022, average annual increases of the exports of goods of 8.6% and for imports of 9.1% are expected. The share of FOB-CIF commercial deficit in GDP will reach the level of 8.5% in 2022. It is assessed that commercial exchanges with the EU Member States will intensify, so that the share of exports of goods to the EU will increase from 76.7% in 2018, to approximately 79% in 2022, while the value of imports coming from the Community area will represent 74% of the value of total imports in the perspective of year 2022, from approximately 75% registered in 2018.

In 2018, the current account of the payment balance registered a deficit 53.5% higher than 2017, reaching a weight of the GDP of 4.5%. The financing of the current account deficit was made up to 54.4% through foreign direct investments, which reached the value of EUR 5 billion and were bigger by 4% compared to 2017.

Table 4: Balance of the external sector

% of GDP	2018	2019	2020	2021	2022
1. Net balance, compared to the rest of the world	-3.3	-1.7	-0.8	-0.3	-0.1
Of which:					
- the balance of goods and services	-3.2	-2.4	-2.2	-1.9	-1.7
- the balance of primary income and secondary income	-1.3	-1.0	-0.8	-0.8	-0.7
- capital account	1.2	1.6	2.2	2.3	2.3

Source: National Commission of Strategy and Prognosis

In the first two months of 2019, the current account of the payment balance registered a deficit of 568 million EUR compared to a negative balance of 425 million EUR as it had in the similar period of 2018, due to the increase of the negative balance of the commercial balance.

In 2019, the current account deficit of the external payment balance is expected to reach a value of 7.3 billion EUR, representing 3.3% of GDP. Direct foreign investments will cover the current account deficit up to 75%.

On medium term, the level of the current account deficit will be maintained at a value between 7.3 and 6.6 billion EUR, with a weight in GDP of 3.3% in 2019 and 2.4% in 2022. Between 2019 and 2020, the share in GDP of the net balance compared to the rest of the world, considering the capital account as well, will remain negative, with a slightly ascending trend, given a high contribution of the capital account.

2.5. STRUCTURAL REFORMS

2.5.1. STRUCTURAL REFORMS IN THE FIELD OF STATE-OWNED COMPANIES

According to the Government Program for 2018-2020, the improvement of corporate governance in State-owned companies is one of the structural reforms considered for implementation.

In agreement with this intention, the Ministry of Transport, in its capacity of tutelary authority, continues the activities performed in order to select the professional management of public enterprises from the transport field. Thus, some of the progress registered is represented by the completion of the procedures of recruitment and selection of applicants for appointment in order to appoint the members of the Board of Directors and the execution of the mandate agreements with the directors appointed at public enterprises who operate under the authority of the Ministry of Transport.

Also, the procedures of recruitment and selection of applicants for appointment in order to appoint the members of the Board of Directors are in progress and in different stages of completion.

The Ministry of Energy continues the restructuring process in order to make more efficient the activity of the Company Complexul Energetic Oltenia S.A. and of Societatea Nationala a Uraniului S.A., as well as the reorganization process of the Company Complexul Energetic Hunedoara S.A.

With regard to Complexul Energetic Oltenia, it was approved in 2018 the CEO Strategy for 2019-2030, which refers to restructuring and rendering more efficient the activity in order to increase the company's attractiveness for investors.

Also, the company started a series of investment projects for modernization and alignment to environmental standards. In 2018, it started the project which refers to capital repairs for group no. 5 of 330 MW from Rovinari, and shall continue the major investments started in previous years.

With regard to Compania Nationala a Uraniului S.A. (CNU), we make the mention that it is process of restructuring for efficiency, after which the European Commission issued a decision authorizing the award of rescue aid for Compania Nationala a Uraniului SA (CNU). Thus, the company elaborated and notified the European Commission about a Restructuring Plan in collaboration with an independent consultant, a plan which is currently being revised, and shall contain a series of operational, technical, technological and environmental restructuring measures.

With regard to the situation of the Company Complexul Energetic Hunedoara S.A., at the end of 2018 the European Commission issued Decision C (2018) 7308 final, establishing that the loans awarded in favor of CEH represent State aid awarded illegally in Romania, in violation of art. 108 para. (3) in TFEU and is incompatible with the internal market. Thus, the MPF is required to recover the incompatible aid through the ANAF. Different scenarios of reorganization of CEH's activity are currently being analyzed by the Ministry of Energy, the Ministry of Public Finance, ANAF and the Competition Council.

Also, an independent expert (the company Glowny Institut Gornictwa - Poland) made a study meant to assess the size of the risk associated with the sudden closure of Lonea and Lupeni mines of CEH. This study shall be submitted to the EC in order to identify the optimal solutions for safe closing of these two mines, for which Romania has notified a closure program.

Also, the Government is considering the initiation of primary public tenders for the sale of a package of 10% of newly issued shares in SPEEH Hidroelectrica S.A., respectively 15%

of newly issued shares in the Company Complexul Energetic Oltenia S.A., through share capital increase.

We mention that the Ministry of Energy has completed the procedure of selection of the members of the Board of Directors/Supervision, in accordance with GEO no. 109/2011, as subsequently amended and supplemented. Through the Decisions of the General Ordinary Meetings of Shareholders it was approved the choice thereof for the following companies:

- The Company OIL TERMINAL S.A. (through HAGOA no. 5/04.04.2018),
- SNGN Romgaz S.A. (through HAGOA no. 8/27.6.2018),
- The Company CONPET S.A. (through HAGOA no. 5/28.08.2018),
- The Company Electrocentrale Grup S.A. (through HAGOA no. 15/17.09.2018),
- The Company Uzina Termoelectrica Midia S.A. (through HAGOA no. 9/08.11.2018),
- The National Company Nuclearelectrica S.A. (through HAGOA no. 12/28.09.2018);

The financial and non-financial performance indicators substantiated on the basis of the management plan and expectation letters were negotiated for the Company OIL TERMINAL S.A. and the Company CONPET S.A.

2.5.2. MEASURES IN THE FIELD OF EDUCATION

The public policies of the Ministry of National Education, consistent with the Government Program for 2018-2020, the Europe 2020 Strategy, the ET 2020 Strategic Framework and other programming documents are included in the National Strategic Framework for Education and Professional Training made up of 4 sector strategies:

- The Strategy for reducing early dropout in Romania - the field of pre-university education (access and participation to inclusive and quality education);
- The National strategy on lifelong learning for 2015-2020 - field of permanent education, elaborated in 2015;
- The National strategy for tertiary education for 2015-2020 - field of university education, elaborated in 2015;
- Romania's strategy on education and professional training for 2016-2020- field of professional and technical pre-university education.

These strategies promote inclusive and quality education for all children and young people in Romania and respond to the main challenges in the field: development of early education, renewal/revision of the curricula and evaluation, teacher training, use of new technologies in the processes of education-teaching-evaluation, content digitization, school counseling and guidance, correlation with employers' requirements, encouraging

lifelong learning, increasing university performances.

The main indicator for pre-university education, early school dropout, is decreasing, going down from 18.1% in 2017 to 16.9% in 2018 (EUROSTAT preliminary data). At municipal level, this rate is of 6.2%, less than the target set at the level of the European Union level, in the rural area being of 26.6%, and in cities and suburbs by 17.4%, leading to an unsatisfactory average at national level. A series of projects, including that with the International Bank for Reconstruction and Development, are in process of implementation to reduce school dropout.

In the following period, it is considered the implementation of the following programs/projects:

1. The national project Digital Romania - project with external non-reimbursable financing, dedicated to change the teaching - learning - evaluation system, respectively equipping every desk with a tablet, purchase of tablets/laptops for the teachers, as well as smart boards for the classrooms, with a value of 2,000 million Lei.
2. *The Program "Merg la școală" (I go to school)* for the primary, secondary, vocational and from State high school students, with a budget of 790 million Lei, allocated for school supplies, school textbooks, the *Euro 200 Program*, transport for pupils and students, competitions, activities of sports clubs and children's palaces.
3. Improving of the conditions in 1,489 schools functioning with sanitary groups located in the yard, without running water and sewage, with a budget estimated at 65 million Lei.

Romania's strategy on education and professional training for 2016-2020- (professional and technical pre-university education fields) was elaborated in 2016.

- As of school year 2017-2018, the Ministry of National Education is promoting dual professional education, a form of professional education with a bigger involvement of economic operators and a higher rate of insertion on the labor market (the number of pupils from professional education being of 29,588, of which 4110 in dual education, in school year 2018-2019).
- The calls for projects *Increasing the relevance of initial professional training through anticipation of professional training needs for the labor market and developing the component of education on the job* and *Formation of entrepreneurial competences - VET*, were reunited in the Call of *Systemic*

development of professional and technical education in accordance with the needs of social and economic development at national, regional, and local level.

- In the call for Internships, 87 financing agreements have been signed so far, and the agro-food, industry and services sectors have had a total allocation of 47.88 million EUR.

2.5.3. STRUCTURAL MEASURES CONCERNING SOCIAL SERVICES AND OCCUPATION

The Government aims to accelerate the process of reforming policies, programs and interventions in the social services field through an integrated, harmonized and coordinated approach.

The Government's concerns, as the main initiator of social policies and promoter of social rights, aim at changing mentality, approaching the system, as well as transforming it into a proactive system. Such a measure can be achieved by shifting the focus from assistance granted in a passive manner to the individual to building alternative measures, meaning strengthening the role of the individual, the family, reducing the dependence of people in difficulty, and promoting active aging.

For 2018 were planned a series of legislative measures and amendments, mainly aimed at strengthening the capacity of public services of social assistance of supplying quality social services, which are accessible and adequate to the individual needs of the vulnerable people from the community, as follows:

1. Proposal of amendment of the legal framework on social assistance, especially in order to develop the capacity of the public assistance service to initiate, coordinate, and implement measures to prevent and combat situations of marginalization and social exclusion.
2. Revision of quality and cost standards for social services.
3. Approval by government decision of the amendments to the framework regulations for the organization and functioning of the public social assistance services and the guiding staff structure.
4. Amendment and completing the law on quality assurance in the field of social services in order to facilitate the implementation of the accreditation procedure of the providers and the licensing of social services provided by them, clarification, amendment/completing of the attributions of the institutions/staff involved in the quality assurance process.
5. Approval by government decision of the program of national interest "Community services at domicile for dependent elderly individuals" and of the program of

- national interest “Increasing the capacity of public social assistance services from certain administrative-territorial units”.
6. Approval of the framework model of the Annual action plan on social services - an instrument foreseen in the Social assistance law to implement local strategies for the development of social services. It includes information on existing and necessary social services, funding programs, planning of public information activities, as well as the training program for staff working in the field of social services.
 7. The implementation in 2018-2020 of 4 projects, in accordance with the Sector plan of research and development of the Ministry of Labor and Social Justice, in the field of social services:
 - a. Informal care in the long-term care of the elderly - development of support services and financing schemes,
 - b. Measures aimed at increasing the social inclusion of elderly people,
 - c. Quality of the dependent elderly people in Romania,
 8. Continuous monitoring methodology of the quality of care in the institutions that provide Long-term care services.
 9. One of the key lessons in the field of social services is represented by the development of community teams of integrated intervention, through an integrated approach regarding the provision of services, the establishment of local multi-disciplinary teams of specialists and of inter-sector cooperation, the investment in the employment of a bigger number of specialists better trained in the social sector, improving the coordination in the field of social services.

In 2018 was started the project *Creation and implementing integrated community services to reduce poverty and social exclusion*, financed through POCU 2014-2020: Axis 4 - Social inclusion and fighting poverty. The project will support 139 disadvantaged communities in terms of human capital, formal employment and living conditions - through the creation of integrated community teams and the development of procedures, methodologies and working tools to strengthen of the capacity of the public social assistance service initiate, coordinate, and implement measures to prevent and combat situations of marginalization and social exclusion.

The Ministry of Labor and Social Justice (MLSJ), in partnership with the National Agency for Payments and Social Inspection, is running, starting with May 2, 2018 the project of “Increasing the efficiency of interventions both in the MLSJ, and in the structures

coordinated by the MLSJ” - code SIPOCA 390/MySMIS 115657, co-funded by the Social European Fund through the 2014-2020 Operational Program of Administrative Capacity. The project aims, among other things, to develop a monitoring and assessment system of the measures from the National Strategy regarding Social Inclusion and Poverty Reduction for 2015-2020, as provided by Government Decision no. 383/2015, as well as the update of social inclusion indicators and of the national mechanism for promotion of social inclusion in Romania.

The MLSJ is undergoing the procedure of contracting of the Project of Development of the social assistance system for fighting poverty and social exclusion, code MySMIS 126924, which seeks to consolidate the capacity of public social assistance services of initiating, coordinating, and implementing measures of prevention and fighting of situations of marginalization and social exclusion, in 350 marginalized communities, through the provision of adequate human resources and the improvement of the level of competences of the personnel operating in the social assistance sector.

In order to remedy the deficit of labor force, the Romanian Government made **a new revision of active policies in the field of labor force**³⁰, focusing in particular on **increasing the amount of subsidies granted** from the unemployment insurance budget, to the employers who employ people belonging to social categories whose access to employment is more difficult³¹. The increase of subsidies is foreseen to be reflected in wages granted by the beneficiary employers, so that the vacant jobs will be more

³⁰ Government Emergency Ordinance no. 60/2018 amending and supplementing certain legislative acts in the field of labor force

³¹ Employers who: employ for undetermined term, graduates of educational institutions (the subsidy is awarded monthly, for a term of 12 months, for every graduate employed); employ for an undetermined term, graduates from among the people with handicaps; employer for an undetermined term, unemployed over 45 years old, unemployed who are single parents that support a single parent family, long-term unemployed or NEET youth (the subsidy shall be awarded monthly, for a term of 12 months, for every person employed from the aforementioned categories, provided the labor or service relationship is maintained for at least 18 months); relative to the number of employees, they fulfilled their legal obligation to employ people with handicaps, as well as if, not having this legal obligation, they employ for an undetermined term people with handicaps and keep their labor or service relationships for at least 18 months; they employ unemployed who, within 5 years as of the date of employment, fulfill, under the law, the requirements to claim partial anticipatory pension or old age pension, if they do not fulfill the requirements for claiming partial anticipatory pension (the subsidy shall be awarded monthly, throughout the term of employment, until the date of fulfillment of those requirements).

attractive for the labor force from the country and from abroad. In this respect, the revised legislative framework provides for an amount of 2,250 Lei/month.

Similarly, the subsidy for employers who conclude an internship agreement was increased to 2,250 Lei/month, being granted for the entire term of performance of the internship agreement (6 months/12 months/24 months/36 months, depending on the level of skill required to practice the activity for which the scheme is organized, respectively 1, 2, 3, or 4). The same value was set for the subsidy for employers who conclude an internship agreement for graduates of higher education, and it is awarded throughout the entire term of the internship agreement (6 months).

Also, according to the revised legal framework, employers who employ young people at risk of social marginalization, who resort to customized social accompaniment on the basis of a solidarity agreement, shall benefit on a monthly basis for every person in this category of an amount equal to the basic salary established on the date of employment of the youth, but not more than four times the value of the reference social index in force on employment date, until expiry of the term of the solidarity agreement.

At the same time, in order to ensure adequate support for the registered unemployed who do not benefit of unemployment allowance of the type that would facilitate their integration on the labor market, it was set to increase the amount of the activation premium granted to them in full-time employment for a period of at least 3 months, from 500 Lei to 1,000 Lei.

Considering that these legislative amendments may respond only partially to the problem of labor force deficit, the Romanian Government proposes **to continue the planned reform of the public employment service** in order to offer efficient employment services relative to the employment opportunities and which would reflect a personalized approach on the labor market.

Within the meaning of such an approach the public employment service is currently implementing **the profiling procedure**, through which identifies the job seekers profile and their classification on employability levels (easily employable, averagely employable, difficult to employ and very difficult to employ), in order to establish the measures that can be awarded under the law for the beneficiaries to become employed on the labor market and to eliminate the risk of them becoming long-term unemployed.

Also, apart from the establishment of the legislative and inter-institutional coordination framework for implementation of the Council's recommendations on integrating long-

term unemployed on the labor market³², the implementation efforts meant to genuinely ensure integrated packages of measures for this category, including through the conclusion of labor integration agreements, according to law³³.

The governmental actions in support of integrating on the labor market the young people belonging to the NEET category shall be focused on the key reforms and initiatives dedicated to early intervention and activation, set out in the framework document “Implementation plan of the Youth Guarantee for 2017-2020”, approved through Memorandum by the Government of Romania in July 2017.

The changes in the economy due to fast technological evolution, to digitalization, automation, are reflected in the constant need for advanced or new knowledge, other than those acquired through education and initial training. Thus, in order to respond to the challenge regarding the lack of skills, including basic skills, as well as the increasing needs of re-qualification and update of the skills of adults with low levels of education and qualification, a series of legislative measures were launched during 2018 respond to identified challenges.

MLSJ, together with the Sectoral committees, social dialogue institutions of public benefit, which participate to the elaboration of the national and sector strategies in the field of professional training, identified in COR in the major group 9 - Unqualified workers - a series of occupations for which they need to be trained holding basic knowledge and specific skills, of qualification level 1. Following this process, it was decided to modify the current structure of COR within the meaning of renaming the major group 9 Unqualified workers as Elementary jobs.

Then, through order of the minister of labor and social justice, was approved the list of elementary jobs through which qualification programs of level 1 can be organized, for the purpose of improving the knowledge, skills and competences in any personal, civic, social context and/or related to labor force employment. In order to be able to develop qualifications of level 1 which would lead to employment on one of these jobs included in the list, it is necessary to develop Occupational Standards. Therefore, the MLSJ, together

³² The memorandum themed “Implementation of the Council’s Recommendation, of February 15, 2016” and Government Emergency Ordinance no. 73/2017 supplementing Law no. 202/2006 on the organization and operation of the National Employment Agency, as well as the amendment of art. 24 in Government Ordinance no. 129/2000 on professional training of adults.

³³ Order of the president of the National Employment Agency no. 254/2018 approving the Implementation procedure of the provisions of art. 58 para. (5) in Law no. 76/2002 on the system of unemployment insurance and stimulation of employment, as well as the model of the labor integration agreement.

with the Ministry of National Education, updated the Methodology of elaboration, validation, approval and management of occupational standards and the standard occupational model, approved through common order of the two ministers.

In order to support the adults that did not finalize secondary education and do not have the minimum competences requested by employers to get a job was also amended Law no. 279/2005 on internships and was introduced the possibility of organizing internships programs of qualification level 1, with a duration of 6 months. At the same time, were regulated aspects related to the improvement of contractual relationships for the people who conclude internship agreements, in order to ensure fair and equal treatment with regard to working conditions, access to social protection and professional training.

As of 2017, when the MLSJ took over the coordination of authorization of professional training providers, started the consultation with the relevant actors and stakeholders and started the elaboration of the legislation regarding the assurance of quality of professional training of adults. In 2018 was completed the draft Methodology for implementation of the quality assurance principles, which proposes the creation of the quality regulatory framework for professional training of adults and also, the establishment in the Ministry of Labor and Social Justice of the National Commission for Assurance of Quality and Control. The draft legislative act is under public consulting.

2.5.4. MEASURES REGARDING ROAD INFRASTRUCTURE

For the road sector, the POIM (Operational Program of Large Infrastructure), OS 1.1 (Increasing mobility through development of road transport on the TEN-T road network), OS 2.1 (Increasing mobility on the TEN-T road network) and OS 2.2 (Increasing the accessibility of areas with low connectivity to the TEN-T road infrastructure), until Q1 of 2019 have been submitted 65 projects (with a total eligible value of 5,099.73 million EUR³⁴). 35 of them were contracted (10 projects of technical assistance and 25 works projects).

The projects are in different stages of implementation: of the 14 phased projects (4 or them approved by COM), 3 projects have been finalized (Timisoara - Lugoj Highway, Giurgiu Bridge, Ciheiului Passageway) and 11 are undergoing implementation; for the 4 of the 11 new works projects contracted were submitted the financing applications (2 approved by COM - "Campia Turzii - Ogra - Targu Mures Highway" and "Sebes - Turda Highway").

³⁴ The values calculated by considering the InforEur exchange rate for the month of February 2019: 1 EUR = 4.7551 Lei

The new major project “Integrated infrastructure for the orbital area of Bucharest Municipality”, amounting to a total of 1.5 billion EUR, was also sent for approval to COM.

For other 6 major projects (Transilvania Highway, sectors Nadaselu - Suplacu de Barcau and Suplacu de Barcau - Bors, Bucharest’s Northern Bypass and Sibiu-Pitesti Highway, Craiova - Pitesti Express Road and the Suspended bridge in Braila) are in preparation the financing applications and the support documentations.

2.5.5. MEASURES REGARDING RAILWAY INFRASTRUCTURE

For the railway sector from the POIM (Operational Program of Large Infrastructure), OS 1.2 (Increasing mobility on the central TEN-T railway network) and OS 2.7 (Increasing the sustainability and quality of railway transport), were submitted and contracted 9 projects with a total eligible value of 2,260.7 million EUR, the only new project (whose financing received approval from COM) being that of “Rehabilitation of the railway section at km. 614 - Gurasada - Simeria.”

Investment projects for the development and modernization of the railway infrastructure located on the central and global TEN - T (Trans-European Transport Network) are in different stages of implementation or preparation, as well as the procurement of the ERTMS (European Railway Traffic Management System) system corresponding to the modernized railway infrastructure and the modernization of 47 railway stations.

In August 2018, the Railway Reform Authority (ARF) concluded the consulting services agreement for elaboration of the study *Sustainability and efficiency of Romania’s railway network*, and the financing agreement from ERDF was concluded on January 16, 2019³⁵. The purpose of the study is to analyze in technical and economic terms 113 railway lines and to identify concrete measures to make the railway network more efficient.

Within the European Interconnection Mechanism (CEF) in the railway sector were signed 2 financing agreements for works, amounting to 1,335.64 million EUR for the railway sectors Brasov - Apata, Cata - Sighisoara, and Apata - Cata. Also, 4 other financing agreements were signed (18.84 million EUR) for the feasibility studies for the following railway sections: Predeal – Braşov, Craiova – Drobeta Turnu Severin – Caransebeş, Craiova – Calafat, Port Constanţa.

2.6. IMPACT OF EUROPEAN FUNDS ON PUBLIC FINANCE

The funds allocated to Romania by the European Union represent a key source for short, medium and long-term development of the Romanian economy and society, as well as a

³⁵ The eligible value of the project is of approximately 4.75 million Lei (ERDF+SB), and the implementation term is of 18 months (September 1, 2018 - February 28, 2020).

central element of budget sustainability through the non-reimbursable nature of these funds.

During financial year 2007-2013, Romania benefited of an EU allocation of 17.57 billion EUR for the 7 Operational Programs financed within the Convergence Objective (Regional Operational Program, Sector Operational Program for Transport, Sector Operational Program for the Environment, Sector Operational Program of Increasing Economic Competitiveness, Sector Operational Program of Human Resources Development, Operational Program of Administrative Capacity Development and Operational Program of Technical Assistance).

According to the closure schedule of operational programs for 2007-2013, by March 31, 2017 were sent the documents corresponding to the closure package (payment application of the final balance, expenditure declaration, final implementation report of the operational program, closure declaration accompanied by the final control report of the Audit Authority), for all operational programs, according to the requirements of European regulations.

Until the present, the total amounts received from the European Commission, representing pre-financing and reimbursements, for the OP financed through the Cohesion Policy - objective 1, as mentioned above, are of approximately 16.98 billion EUR, which represents approximately 96% of the EU allocation that corresponds to these programs. The European Commission reimbursed the amount of 14.88 billion EUR thereof.

We mention that the final absorption rate can be calculated only after the Commission accepts the closure package.

With regard to the programming period 2014-2020, Romania has over 43 billion EUR available, in accordance with the Multi-annual financial framework for 2014-2020, of which the allocation for European Structural and Investment Funds (ESIF) is of approximately 31 billion EUR. The allocation for the cohesion policy, financed within ESIF, is of approximately 23 billion EUR (OP Regional; OP Large Infrastructure; OP Competitiveness; OP Human Capital; OP Technical Assistance; OP Administrative Capacity).

Until the present have been launched project calls for all operational programs managed by the MEF and the MRDPA. The total budget for the launched calls is of approximately 25 billion EUR, which represents 90.7% of the total allocation available for the implementation of these programs.

Thus, on February 22 of this year, the contracting rate was of approximately 70.7% of the EU allocation of the OP financed from ESIF and FEAD, being signed 5,781 financing agreements with the beneficiaries of non-reimbursable funds, totaling approximately 20.5 billion EUR, of which 16.3 billion EUR in EU contribution. Within the signed agreements, the management authorities made payments amounting to a total value of approximately 4.7 billion EUR.

The total amounts received from the European Commission until the present as pre-financing and reimbursements for the programs financed from ESIF (OP Large Infrastructure, OP Competitiveness, OP Regional, OP Administrative Capacity, OP Technical Assistance, OP Human Capital, NP of Rural Development, OP Fishing and Marine Affairs) are of approximately 8.56 billion EUR, which means approximately 28% of the EU allocation that corresponds to these programs.

In addition, the EC has reimbursed approximately 6.3 billion EUR for direct payments in agriculture.

We mention that in the European Union the average rate of amounts received from the European Commission is currently of approximately 29%.

With regard to the legislative/institutional/procedural measures of horizontal nature promoted in the MEF in order to increase the absorption rate and improve the governance of European funds on medium term (2019-2022), we mention the following:

- Creating of an implementation framework as predictable as possible for the implementation of projects by the beneficiaries.
- Observance of the procedural terms by the MA/IB;
- Careful monitoring of each project, through the introduction of the position of monitoring officer in the MAs;
- The reallocation of funds to the sectors with maximum absorption potential within and among the Operational Programs:
 - increasing the allocation dedicated to SMEs;
 - creating a new axis to support small cities;
 - the possibility of financing the regional smart specialization strategies;
- The introduction of simplified cost options:
 - the use of flat rates;
 - the introduction of standards for unit costs;

- Simplifying the procedures for the construction permits of the projects of national interest provided in the general transport master plan, through issuance of construction permits without the prior elaboration and approval of a territory arrangement or urbanism documentation (without affecting the provisions regarding construction quality and discipline).
- Continuous improvement of the legal framework through the amendments made by GEO no. 40/2015 on financial management of European funds:
 - the pre-financing mechanism ensures for the beneficiaries the liquidities necessary for implementation (generally, by providing installments of up to 10% of the project's value and up to 40%, under observance of certain requirements, in the case of beneficiaries subject to State/de minimis aid rules);
 - the categories of expenditures that can be included in the payment claims (salaries, subsidies, scholarships) were extended;
 - the assumptions for over-contracting up to 200% were created according to the operational program;
 - the amounts necessary to support public hospitals which could not ensure co-financing of their projects were ensured through the budget of the Ministry of Health;
 - settlement from European funds of the investments started by the central/local public authorities and paid from other sources (State/local budget or loans);
 - unitary approach for all programs on the level of private co-financing to at most 2% for the beneficiaries/partners who are non-profit legal entities of private law, established under the law in force, including universities, trade unions and employers' associations.
- Supporting local authorities - through promotion of GEO no. 27/2017 on the adoption of certain fiscal and budgetary measures, the administrative-territorial units/subdivisions were able to request in 2017 from the MPF, including for the inter-Community development associations, the contracting of loans from privatization revenues, within the limit of 500,000 thousand Lei, to ensure pre-financing and/or co-financing of projects financed from external non-reimbursable funds from the period 2014-2020, including for the ineligible expenditures associated with the projects; the measure was extended for 2018-2019 as well,

through GEO no. 11/March 1, 2018 on the adoption of certain budgetary measures.

- The introduction of standard models of contracting of works (design and execution) through GD no. 1/2018 on the approval of the general and specific requirements for certain categories of procurement agreements that correspond to the investment objectives financed from public funds;
- Establishment of a European funds settlement mechanism for the expenditures made for the works executed under its own management within the POIM, for the exceptional cases in which the beneficiaries undertake under certain conditions to finalize the infrastructure projects that have been executed up to at least 80% and have been abandoned by the constructors (MPEF no. 558/2018 on the conditions for deduction from European funds of the expenditures made for the works executed by own means within the POIM).

At the same time, we mention that in the Ministry of European Funds are constantly taken the measures necessary to identify the actions needed to make more urgent the implementation of the operational programs for 2014-2020, ensuring at the same time the maximization of the impact of European funds, as well as the transparency of the entire process.

3. BALANCE OF THE GENERAL CONSOLIDATED BUDGET

3.1. POLICIES STRATEGY

The fiscal and budgetary policy will continue to directly support economic growth, by continuing the implementation of the measures included in the Government Program for 2018-2020, as the fiscal-budgetary space will allow it.

The implementation of the fiscal and budgetary policy in the 2019-2021 timeframe will be made without affecting the long-term sustainability of public finance, i.e. maintaining a nominal budget deficit within the margin allowed by the Treaty on the Functioning of the European Union (TFEU)³⁶.

Romania is under the preventive arm of the Stability and Growth Pact (SGP), which states that the EU Member States must reach the medium-term budgetary objective (MTO) within a certain period of time.

Maintaining the MTO is necessary in order to prevent the increase of the nominal deficit over 3% of GDP in the case of an economic downturn.

The EU Council decided, in accordance with article 121 paragraph (4) in the Treaty on the Functioning of the European Union, that a significant deviation from the MTO occurred in Romania starting with 2016.³⁷

In 2019, the structural budget deficit is estimated to reach a level of 2.8% of GDP, compared to a level of 3.2% of GDP in 2017. The increase of the structural deficit in 2019 by 0.1 p.p. and by 0.2 p.p. in 2020 (reaching a level of 3% of GDP) reflects the one-off measures, the positivity of the output gap and the cyclical component. Nevertheless, we estimate that the structural deficit will enter an adjustment trajectory towards the MTO starting with 2021, reaching a level of 2.4% of GDP in 2022.

The deviation from the MTO would occur while maintaining a sustainable level of public debt below 38% of GDP, over the entire planning horizon, with Romania recording a public debt of 35% of GDP in 2018, a decline of 0.2pp compared to 2017.

³⁶ An ESA budget deficit below 3% of GDP.

³⁷ The target structural deficit is of -1% of GDP, according to the Fiscal Compact.

3.2. THE FISCAL AND BUDGETARY POLICY IN 2018

Main fiscal amendments regarding revenues starting in 2018

In the field of corporate income tax

- Fighting aggressive fiscal planning and the eroding of the taxable base through assurance of equitable and efficient competition conditions for all taxpayers who pay corporate income tax, who are encouraged to transparently declare their fiscal liabilities. This improvement of the legislative framework of taxation of profits corresponds to the approaches from the European Union, as they were expressed in the “Directive 2016/1164 of the Council laying down rules against tax avoidance practices that directly affect the functioning of the internal market”, whose transposition into the national legislation was made in this way.
- The consolidation of revenues from corporate income tax, through extension of the taxation base, and a limitation of deduction of expenditures generated by operations of receivable assignment.
- As of 2018 were amended the requirements for Romanian legal entities to be classified into the category of microenterprises: i) increasing the level of revenues obtained by December 31 of the previous fiscal year from EUR 500,000 to EUR 1,000,000; ii) eliminating the requirement regarding the obtaining of revenues from consultancy and management up to 20% of total revenues; iii) eliminating the activities for which taxpayers do not apply this taxation system (the Deposit Guarantee Fund in the Banking System, the Investor Compensation Fund, the Guarantee Fund for Private Pensions, the Guarantee Fund for the Insured).
- Microenterprises which subscribed a share capital of at least 45,000 Lei and have at least 2 employees may opt, only once, to apply the provisions of title II “Corporate income tax”, starting with the quarter when these requirements are cumulatively fulfilled, the option being definitive.

In the field of personal income tax

- Reducing the personal income tax rate from 16% to 10%.
- Increasing the level of the gross monthly salary according to which the personal deduction is given, as well as increasing the level of personal deductions in fixed amount awarded to the persons who obtain revenues from salaries and assimilated to salaries of up to Lei 1,950 and increasing the personal deductions awarded in a digressive manner to private individuals who obtain revenues from salaries and assimilated to salaries up to the value of Lei 3,600, inclusive.

- Simplifying the declarative obligations of private individuals, by merging 7 declarations into a single declaration and making the payments anytime during the year until March 15, inclusive, of the year following that of realization of the revenues.

In the field of mandatory social contributions

- Reducing the total share of mandatory social contributions, on the whole by 2 percentage points.
- The level of contributions decreased by 2 percentage points, so that in the total of 39.25% contributions paid for one gross salary, are paid 38.25%. Of the total of 22.75% contributions owed by the employer, 20 percentage points were transferred to the employee. In total, of the gross salary, 35% are contributions withheld by the employer in the name of the employee and the contributions left to the employer, namely 2.75%, decreased to 2.25% and cover the risks of unemployment, labor accidents, medical leave and salary liabilities. The latter are included in a single contribution, which is called the labor insurance contribution.
- Changing the manner of establishment of CAS and CASS in the case of private individuals who carry out independent activities or other categories of revenues, meaning that these individuals no longer owe social contributions on the revenue they obtain: i) the calculation base of CAS is the chosen revenue, which is at least equal to the minimum gross salary at country level; ii) the calculation base of CASS is the minimum gross salary at country level.

In the field of VAT

Optional application of a **VAT** collection mechanism (split payment) and for certain categories of taxable individuals the mandatory application of the mechanism of distributed payment of VAT, namely those who:

- at December 31, 2017 register tax liabilities representing VAT, with the exception of those whose forced execution is suspended, amounting to more than 15,000 Lei in the case of large taxpayers, 10,000 Lei in the case of medium taxpayers, 5,000 Lei for the rest of taxpayers, if these liabilities are not paid by December 31, 2018;
- as of January 1, 2018 they register tax liabilities representing VAT, outstanding payments, not paid within 60 business days as of the due date, with the exception of those whose forced execution is suspended, amounting to more than 15,000 Lei in the case of large taxpayers, 10,000 Lei in the case of medium taxpayers, 5,000 Lei for the rest of taxpayers.

- are subject to the national legislation regarding procedures of prevention of insolvency and the insolvency procedure.

In the field of excise duties

Increasing the level of **excise duties** for finely cut smoking tobacco used for rolling cigarettes, and for other smoking tobacco from Lei 383.78/kg to Lei 398.70/kg.

Table 5: Main fiscal measures with an impact on budgetary revenues in 2018

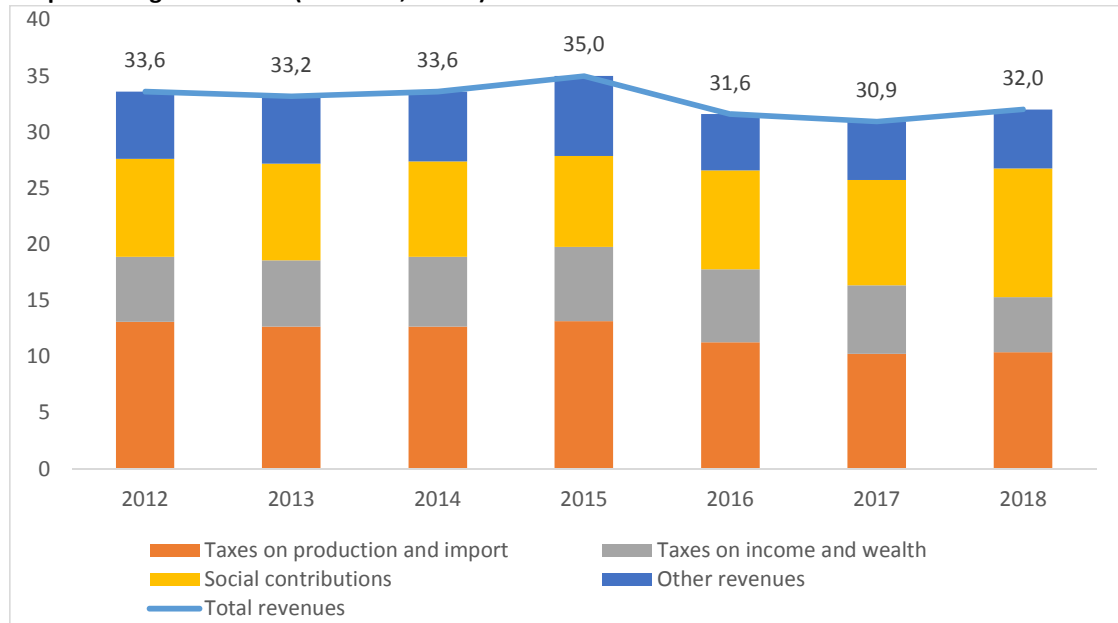
	Estimated impact (million Lei)
Reduction of the personal income tax rate from 16% to 10% as of January 01, 2018 (according to GEO 79/2017)	-13,538
Reform of social contributions and transfer thereof from the employer to the employee	5,754
Amendment of the taxation rate of microenterprises of 1% of the turnover for those who have one or several employees, setting the ceiling at 1,000,000 EUR, optionally for those with 2 employees and capital of at least 45,000 Lei	-283
Introduction of the Labor insurance contribution	5,398
Reduction of the transfer rate to pillar II from 5.1% to 3.75% as of January 01, 2018.	2,100

In 2018, the share of total revenues in GDP, in ESA terms, was of 32%, a 1.1 percentage points increase compared to the previous year.

Structurally, the increase of the share of revenues in GDP, in ESA terms, is due to the increase of revenues from social contributions (+2.1 p.p.), Taxes on production and import that increased by 0.1 p.p., as well as to the category of “other revenues” which increased by 0.1 p.p.

In the case of Taxes on income and wealth, the decrease of 1.2 p.p. was mainly due to the reduction of the personal income tax rate from 16% to 10%, starting with the 1st of January 2018, a measure which was reflected in revenues starting with February 2018.

Graph 3: Budget revenues (ESA 2010, %GDP)



Source: Ministry of Public Finance

At the same time, the weight of total revenues in GDP in ESA terms was of 35%, a 1.4 percentage points increase compared to the previous year.

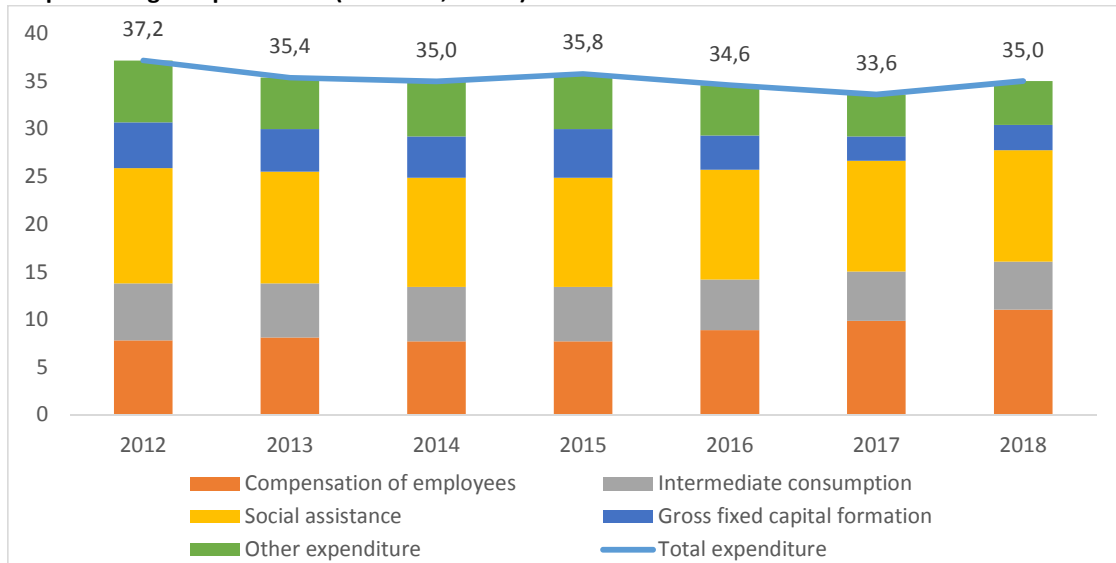
Personnel expenditures expressed as share in the GDP in ESA terms increased by 1.1 p.p. compared to the previous year, reaching 11% of GDP, mainly due to salary increases granted under Framework Law no. 153/2017 on the remuneration of staff paid out of public funds.

Social assistance expenditures increased by 0.1 p.p., mainly due to the increase by 9% of the pension point as of July 1, 2017 (reaching 1,000 Lei), respectively by 10% as of July 1, 2018 (reaching 1,100 Lei).

Expenditures representing interim consumption decreased by 0.1 p.p., and the category of "other expenditures" increased by 0.2 p.p.

At the same time, gross fixed capital formation increased its share in the GDP in 2018 compared to 2017 by approximately 0.1 p.p., reaching 2.6% of GDP.

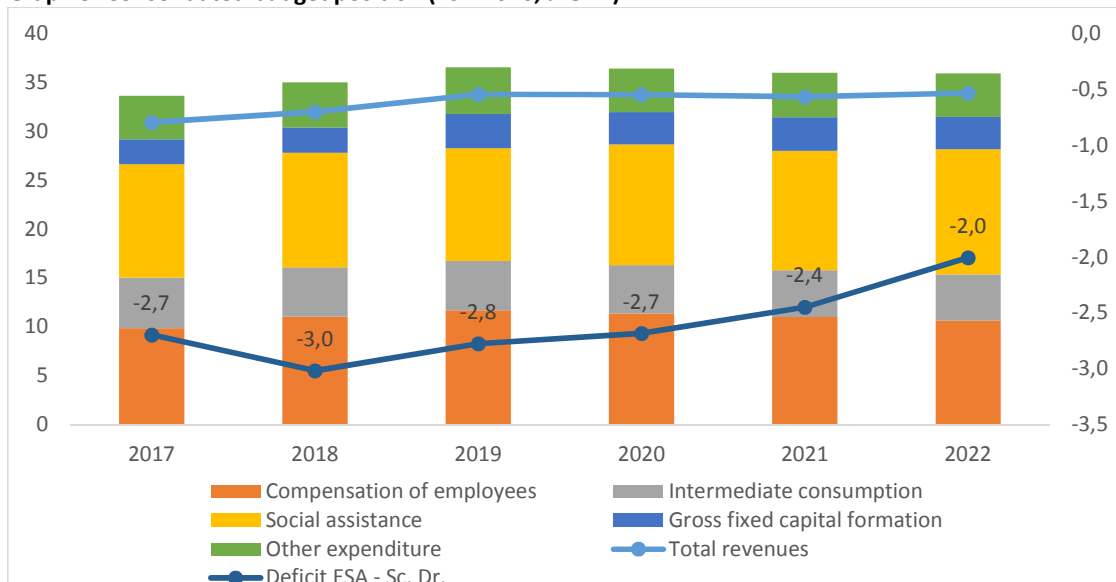
Graph 4: Budget expenditures (ESA 2010, %GDP)



Source: Ministry of Public Finance

The budget deficit calculated in accordance with the ESA methodology was at the limit of the reference level of the Stability and Growth Pact, recording a level of 3.0% of GDP in 2018. The deficit increased marginally (+0.3 p.p.) from the value recorded in the previous year, accommodating fiscal relaxation measures, as well as the increase of public wages and pensions.

Graph 5: Consolidated budget position (ESA 2010, %GDP)



Source: Ministry of Public Finance

3.3. MEDIUM TERM BUDGET PERSPECTIVES

The budget projection for 2019 and on medium term is based on the provisions and objectives listed in the Fiscal and budgetary strategy for 2019-2021, namely:

- Stimulating, continuing, consolidating and maintaining smart, sustainable, and inclusive economic growth, meant to provide the premises for consolidating a strong, proactive state and a balance society, in order to increase the investor confidence in the Romanian economy;
- Allocating significant funds to support public investments by prioritizing significant public investments to ensure infrastructure and services, to improve quality of life, with a multiplier effect and direct contribution to gross fixed capital formation;
- Creating a predictable fiscal policy to support the business environment and stimulate investments in sectors with high added value, simplifying fiscality and making internal processes more fluid, in order to create the assumption for sustainable economic growth;
- Measures adopted by the Government regarding the stimulation of consumption through the adoption of salary and social measures ensuring social protection and security for the elderly, the pensioners and the most vulnerable categories;
- Developing and diversifying public debt management instruments;
- Improving, applying and consolidating budgetary governance, increasing budgetary transparency and making public spending more efficient.

Measures on budget revenues considered when elaborating the budget of 2019:

- the increase of taxation in the field of gambling;
- the increase of the level of excise duties for tobacco products;
- the enforcement in 2019 as well of the measures of distribution of at least 90% of the net profit made under the form of payments to the State or local budget, in the case of autonomous administrations, or of dividends in the case of national companies and fully or majority State-owned companies;
- as of 2019, enforcing the measure through which State-owned companies pay as dividends 35% of the amount allocated to other reserves, as well as of the amounts allocated for investments which have not been used.
- reduction of labor taxation for companies from the construction sector;
- selling the licenses for 5G technology;

Table 6: The impact on the budget revenues of the main fiscal and budgetary measures in 2019

	Estimated impact (million Lei)
Total impact of the measures from GEO 114/December 2018	1,274.4
Increasing the minimum salary in the field of constructions and of the amendments of the taxation system	-2,206.9
Pensions contribution	1,013.1
Health contribution	-2,048.3
Labor insurance contribution	-346.4
Personal income tax	-825.4
Revenues from dividends according to art. 43 in GEO 114 (35% of the amounts allocated to other reserves, as well as of the amounts allocated for investments which have not been used).	1,500.0
Revenues from the increase of excise duties for tobacco	615.5
Revenues from the amendments of the charge on gambling, net impact	524.8
Increase of own revenues of ANRE and ANCOM, net impact	841.0

One-off measures:	Million Lei
Revenues from the sale of 5G licenses (scheduled for December 2019)	2,100

Main fiscal and budgetary measures on expenditures considered when elaborating the budget of 2019

- As of September 1, 2019, the value of the pension point will be increased by 15%, respectively from Lei 1,100 to Lei 1,265;
- as of September 1, 2019, the guaranteed social allowance for the retired will be increased by 10%, respectively from Lei 640 to Lei 704;
- as of the month following that of entry into force of the law of the State budget for 2019, the amount of the State allowance for children will be increased from Lei 200 to Lei 300 for children up to 2 years of age or up to 3 years of age, in the case of handicapped children; from Lei 84 to Lei 150 for children with ages between 2 years and 18 years, as well as for 18 year olds who are enrolled in high school or professional studies organized under the law, until they complete said studies, and

from Lei 200 to Lei 300 for children with disabilities aged between 3 and 18 years, in the case of handicapped children.

- as of January 1, 2019, the minimum gross salary guaranteed at country level provided by art. 164 para. (1) in Law no. 53/2003 - Labor Code, as republished, as subsequently amended and supplemented, shall be established in money, without inclusion of bonuses and other additions, at the amount of 2,080 Lei per month;
- as of January 1, 2019, the basic salaries, the position based military pay/position based salaries, the employment allowances shall be increased by 1/4 from the difference between the basic salary, the position based military pay/position based salary, the employment allowance provided by law for year 2022 and that from the month of December 2018;
- as of January 1, 2019, the amount of the bonuses, allowances, compensations, premiums and other elements of the salary system they are part of, according to law, from the gross monthly salary, the monthly military pay of which the personnel paid from public funds benefits, shall be maintained at most at the level of the amount awarded for the month of December 2018;
- the award between 2019 and 2020 of holiday vouchers according to the provisions of GEO no. 8/2009;
- the award between 2019-2020 of the meal benefit provided by art. 18 in Framework law no. 153/2017;
- between 2019 and 2021 for the military personnel, policemen and public servants with special status from the system of administration of penitentiaries, the allowances, compensations, premiums, aids, compensatory payments, reparations, monthly compensations for rent and other rights awarded in accordance with the legislative acts in force, which are not part of the gross monthly military pay/gross monthly salary, shall be maintained at the level of the month of December 2018;
- between 2019 and 2021, the amount of the money compensation, respectively of the value allowance for meal rights and, respectively, the annual financial value of equipment standards, as well as the financial value of the equipment rights shall be maintained at the level set for the month of December 2018;
- between 2019 and 2021 shall be maintained in payment at the level awarded/due for the month of December 2018 certain allowances paid to disadvantaged people,

- like: the allowances for the people politically and ethnically persecuted, the allowances for the members of the Romanian Academy, and so on
- Between 2019 and 2021, the life annuities provided by art. 64 in the Law of physical education and sports no. 69/2000, as subsequently amended and supplemented, shall be awarded in the amount payable in December 2018;
 - Also, when establishing the personnel expenditures for 2019 it was considered the continued application of some of the measures which refer to the limitation of expenditures approved in previous years.
 - increase of children allowance;

The execution of the general consolidated budget on the first quarter of 2019, on the basis of the operative execution data in cash terms ended with a deficit of 5.5 billion Lei, i.e. 0.54% of GDP.

The revenues of the general consolidated budget in the first quarter are of Lei 74.7 billion, representing 7.2% of GDP, compared with 7% of the GDP in 2018. In percentages, the revenues were 12.5% bigger in nominal terms than in the same period of the previous year.

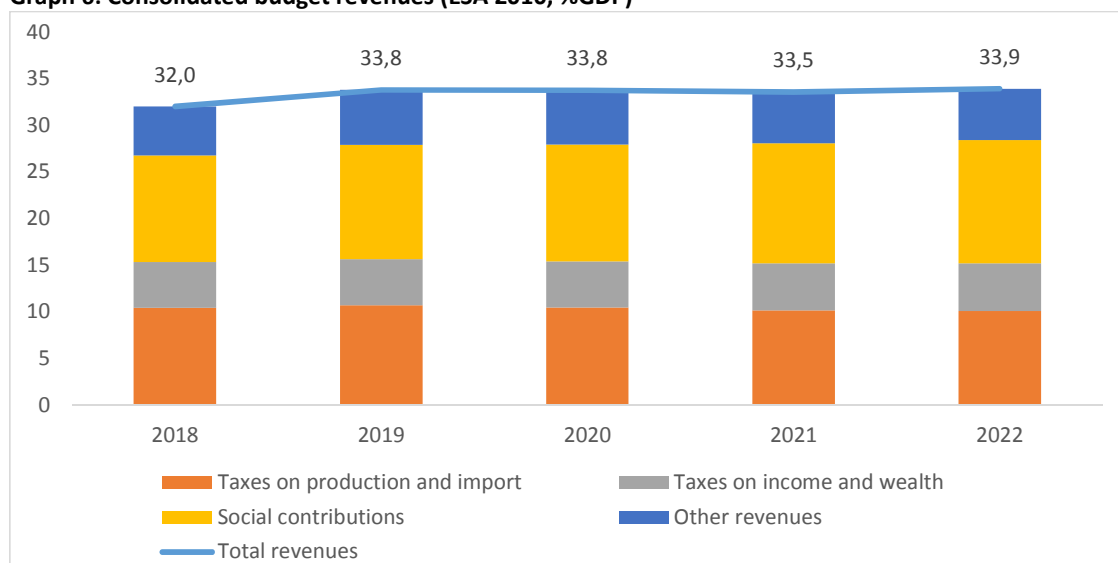
- Increases are registered compared to the first quarter of the previous year in the case of revenues from insurance contributions (+21.9%), excise duties (+16.8%), VAT (+14.8).
- Revenues from insurance contributions were influenced by the increase of the number of employees from the economy, of the average gross salary, of the minimum salary, as well as by the new legislative conditions regarding the transfer of contributions from the employer to the employee, regulated by GEO no. 79/2017 and the revenues from VAT increased by 14.8% compared to those of the same period of 2018, reaching a value of 15.3 billion Lei.
- Also, the revenues from taxes and charges on property increased by 8%.
- Decreases were registered for the revenues from the salaries and personal income tax, by 16%, based on the decrease as of January 01, 2018 of the personal income tax rate from 16% to 10%, a measure which was reflected into the revenues as of February 2018.
- The amounts from the European Union on account of payments made are of 3.8 billion Lei.

The expenditures of the general consolidated budget are of 80.2 billion Lei, i.e. 13.2% bigger than in the previous year.

- Personnel expenditures are 25.7% bigger than in the first three months of 2018, the increase being caused by the salary increases given on the basis of the Framework Law no. 153/2017 on the salaries of personnel paid from public funds.
- Expenditures for goods and services increased by 18% compared to the first three months of the previous year. Significant increases are recorded both for the budget of the national single fund of health insurance, and for the State budget.
- Increases are also recorded for interest expenditures, by 15.5%.
- Social assistance expenditures increased compared to the same period of the previous year by 15%, being mainly influenced by the increase of the pension point by 10% as of July 1, 2018, reaching 1,100 Lei from 1,000 Lei, by the increase of the level of the social allowance for the retired from 520 Lei to 640 Lei.
- Investment expenditures, which include capital expenditures, as well as the expenditures corresponding to development programs financed from domestic and foreign sources, were of Lei 4.9 billion.

Total budget revenues are projected to slightly increase from the level of 32% of GDP in 2018 to a level of 33.5% of GDP in 2021, especially on the basis of the increase of the share in the GDP of social contributions. For 2019, the estimated level of budget revenues is of 33.8% (according to the ESA methodology).

Graph 6: Consolidated budget revenues (ESA 2010, %GDP)



Source: Ministry of Public Finance

In structure, the revenues from current corporate income and personal income taxes are provided to remain at the same level as in 2018, namely of 4.9% in GDP. On medium term, they are foreseen to increase by 0.1 p.p. in 2020 and in 2022. Revenues collected from

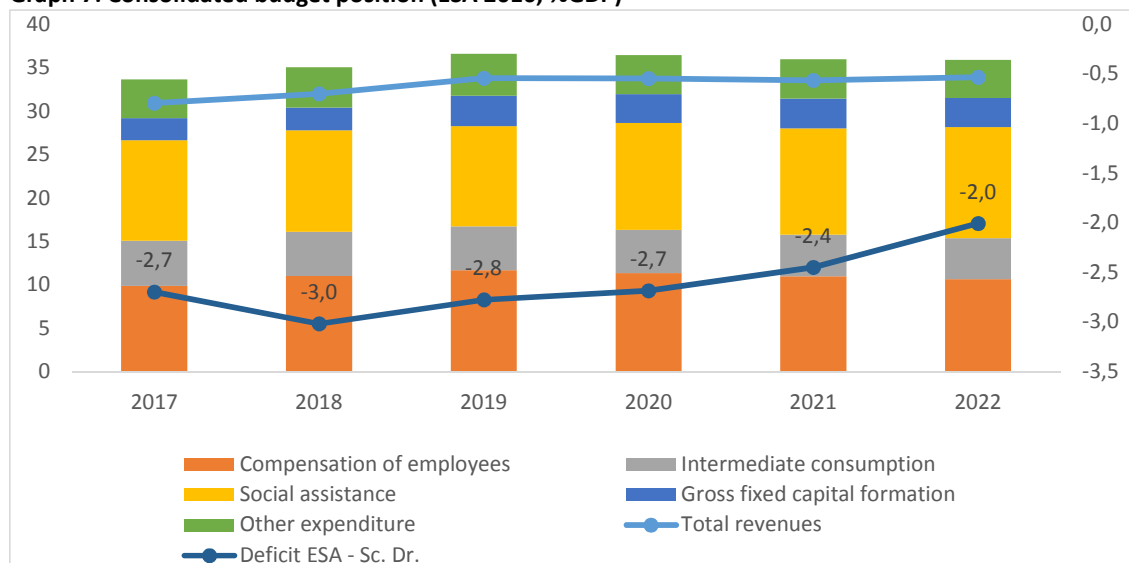
personal income tax are influenced by the negative impact generated by the exemption given to employees from the constructions sector, according to GEO no. 114/2018, and on medium term, by the favorable evolution of the salaries fund from the economy.

It is estimated that the revenues from taxes on goods and services will register an increase of 0.3 percentage points (reaching 10.7% of GDP) in 2019 compared to 2018. This is mainly due to the ANAF's commitment of collecting additional revenues of 6 billion Lei in VAT and of 1 billion Lei in excise duties, as a result of the measures related to improving collection and fighting evasion. On medium term, revenues collected from these taxes will be at 10.5% of GDP in 2020, respectively 10.2% of GDP in 2021.

Revenues from social insurance contributions in 2019 are estimated to increase by 0.9 pp of GDP compared to 2018, being mainly influenced by the significant increase of the salaries fund in the economy, by the application on the entire year of the new legislative conditions compared to 11 months of application in 2018 and by the provisions of GEO no. 114/2018 which create the assumptions for salary increases differentiated on the fields of activity in the case of employees from the constructions sector, at the same time as the exemption from payment of the contribution owed to privately managed pension funds (Pillar II) within the limit of 3.75% between 2019 and 2028, inclusive. On medium term, the evolution of revenues from social insurance contributions is determined by the forecasted increase of the average salary and of the number of employees, the share of revenues from this source being forecasted to reach 12.9% of GDP in 2021.

Total budget expenditures are forecasted to increase in 2019, reaching 36.6% of GDP, and on medium term it is estimated a slight decrease, down to 36% of GDP in 2021.

Graph 7: Consolidated budget position (ESA 2010, %GDP)



Source: Ministry of Public Finance

Personnel expenditures as share in GDP are forecasted to increase at the beginning of the forecast horizon to 11.7% of GDP, and for 2021 are estimated at 11% of GDP. Gross fixed capital formation indicates the increase of allocations for investment expenditures on medium term from 2.6% of GDP in 2018 to 3.4% of GDP in 2021.

Social assistance expenditures will be at 11.5% of GDP in 2019 and shall increase to 12.2% of GDP in 2021.

Both cash and ESA deficit are planned for 2019-2021 to meet the threshold of 3% of GDP. The Government sent a draft budget of 2019 to the Parliament with a target cash deficit of 2.55%, but after the approval of the children allowances the cash deficit increased to 2.76%. After which in 2016-2018 the ESA budget deficit has constantly stimulated economic growth, 2019 marks the entrance on a trajectory of gradual adjustment thereof, for 2022 being estimated a budget deficit of 2% of GDP.

Table 7: General consolidated budget balance (% of GDP)

	2017	2018	2019	2020	2021	2022
	Achieved	Achieved	Estimates	Estimates	Estimates	Estimates
ESA methodology balance	-2.7	-3.0	-2.8	-2.7	-2.4	-2.0
Structural balance	-3.2	-2.7	-2.8	-3.0	-2.8	-2.4

Source: Ministry of Public Finance, National Commission of Strategy and Prognosis

Following the discussions with the European Commission, one-off measures were reflected in 2018 and 2019, which led to the amendment of the estimates regarding structural deficits compared to the level forecasted in the Fiscal and Budgetary Strategy for 2019-2021. Thus, the structural deficit is estimated at 2.7% of GDP in 2018 and 2.8% in 2019, compared to the previous forecast of 3% for these years.

The increase of the structural deficit in 2019 by 0.1 p.p. and by 0.2 p.p. in 2020 (reaching a level of 3% of GDP) reflects the one-off measures, the positivity of the output gap and the cyclical component. Nevertheless, we estimate that the structural deficit will enter an adjustment trajectory towards the MTO as of 2021, reaching a level of 2.4% of GDP in 2022.

4. EVOLUTIONS AND LEVEL OF GOVERNMENT DEBT³⁸

Government debt and Government public debt management strategy

The government debt in accordance with the EU methodology was at 35% of GDP at the end of 2018, that is much lower the ceiling of 60% set through the Maastricht Treaty. Out of the total Government debt, the domestic debt represented 18.3% of GDP, and the foreign debt was of 16.7% of GDP.

The objectives of the Government public debt management strategy on medium term are the following:

- Ensuring the necessary financing of the central public administration, on the basis of the minimization of medium and long term costs;
- Limiting the risks associated with the government public debt portfolio;
- Developing the domestic market for the government securities.

In 2018, domestic financing was made in accordance with the financing plan announced at the beginning of the year through auctions of government securities with maturities ranging between 6 months and 15 years (residual maturity of at least 12.8 years). The total volume borrowed on the domestic market was of Lei 45.78 billion, out of which 10.06% on short-term debt, 54.85% on medium-term debt and 35.08% on long-term debt. Additionally, Lei 2.07 billion was borrowed under the form of government securities to individuals, within the Program TEZAUR.

Although non-residential holdings of government securities issued on the domestic market remained at a relatively stable level throughout the year (approximately 18-18.5%), a slight increase was recorded at the end of 2018 (20.2%).

³⁸ All the indicators used in this chapter are compliant with the EU methodology.

Graph 8: Yields of government securities on the primary market



Source: Ministry of Public Finance

In 2018 the Program TEZAU/CENTENAR was launched. The government securities issued under the programme are dedicated to individuals that have a preference to such saving instruments offered by the State, similar to those distributed in the past (between 2000 and 2005). The retail government securities are issued in dematerialized form, through the State Treasury network and the outlets of the National Company “Posta Romana”. The MoPF will maintain its strategy regarding issuances of government securities to individuals, with the objective to diversify the investor base and to extend the distribution channels for such savings instruments dedicated to individuals. Up to date³⁹, the issuances have been launched with maturities ranging between 1 to 5 years where more than 77,894 persons invested Lei 3.51 billion. In 2019, the indicative estimated amount to be raised as retail bonds is approximately Lei 5 billion.

In 2018 the external financing was mainly made through three Eurobond transactions, as follows:

- On February 1, 2018, EUR 2 billion EUR was raised through the issuance of Eurobonds in two tranches, out of which EUR 750 million with a maturity of 12 years (yield of 2.585%, coupon of 2.50%) and EUR 1.25 billion with a maturity of 20 years (yield of 3.450%, coupon of 3.375%).
- On June 7, 2018, USD 1.2 billion was raised through Eurobonds with maturity of

³⁹ April 30, 2019

30 years (yield of 5.130%, coupon of 5.125%) together with an exchange transaction in amount of USD 231.1 million of USD notes due in 2022.

- On October 04, 2018, EUR 1.75 billion was raised through the issuance of Eurobonds in two tranches, out of which EUR 1.15 billion with a maturity of 10 years (yield of 3.029%, coupon of 2.875%) and EUR 600 million with a maturity of 20 years (yield of 4.234%, coupon of 4.125%).

In 2019, the gross financing is at approximately Lei 72 billion, the total volume of loans to be borrowed by the Ministry of Public Finance from the domestic and external markets being determined by an estimated level of budget deficit at 2.76% of GDP and a volume of debt to be refinanced in 2019 of RON 44 billion. In order to fulfill the objectives to reduce the currency risk and to support the development of the domestic market, up to 75% of the budget deficit will be financed from the domestic market.

In 2019, the indicative volume of government securities to be issued on the domestic market is approximately Lei 49-50 billion, while the amount to be mobilized from the external market is approximately EUR 4.25 billion (equivalent) through issuances of Eurobonds within the MTN Programme and loans from international financial institutions (IFIs).

So far⁴⁰, the MoPF has raised over RON 11.76 billion (of which Lei 1.44 billion through the TEZAUR Program) from the domestic market, which corresponds to approximately 23.5% coverage of the financing plan on the domestic market.

With regard to external financing, on March 27, 2019 an Eurobond in three tranches was launched for an amount of 3 billion EUR, out of which EUR 1.15 billion with a maturity of 7 years (yield of 2.132%, coupon of 2.000%), EUR 500 million with a maturity of 15 years (yield of 3.618%, coupon of 3.500%), and EUR 1.35 billion with a maturity of 30 years (yield of 4.625%, coupon of 4.657%). This is the largest eurobond transaction ever made by the Ministry of Public Finance, the first ever issuance in three installments and the longest maturity of 30 years issued by Romania in EUR currency on the external capital markets. The amount raised through the aforementioned issuances covers 70.6% of the financing plan on the external market.

Also, in order to diversify the investor base and to extend the average maturity of government public debt, the MoPF intends to launch buybacks mainly targeting the Eurobonds denominated in USD launched in the past with high coupons and which could

⁴⁰ April 30, 2019

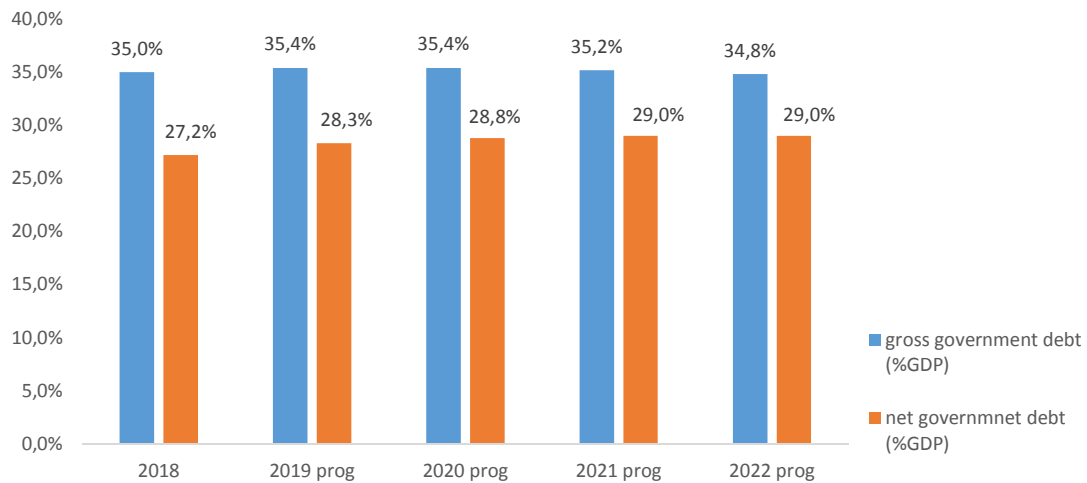
be exchanged for new eurobonds in USD with longer maturities and lower coupons.

For the purpose of improving the management of public debt and avoiding seasonal pressures in the assurance of the financing sources of the budget deficit and for the refinancing of the Government public debt, in order to reduce the refinancing risk and liquidity risk, the Ministry of Public Finance is considering to maintain the financial reserve (*buffer*) in foreign currency available to the State Treasury at an equivalent coverage of 4 months of financing needs.

Until June 2018, the Ministry of Public Finance, acting through the General Directorate of Treasury and Public Debt, has benefited of technical assistance from the World Bank Treasury, under the project “Developing the capacity for government public debt management through the use of derivative financial instruments” code SIPOCA 10, for the creation of the legal, procedural and technical framework related to derivative financial instruments (currency swaps and interest rate swaps). The project was financed from the European Social Fund, within the Operational Program of Administrative Capacity for 2014-2020. Following the completion of the project and based on the reports provided by the World Bank, the Government Emergency Ordinance no. 64/2007 on public debt was amended with the Government Ordinance no. 14/2018, whereby new definitions and concepts for the use derivatives were introduced and MoPF was enabled to perform such transactions. The Ministry of Public Finance, together with the National Bank of Romania, will work on finalizing the procedural framework in order to launch these instruments.

On the basis of the economic growth and of deficits calculated in accordance with the EU methodology of up to 3% of GDP, in 2019-2020 we estimate that the weight of gross government public debt will not exceed 38% of GDP.

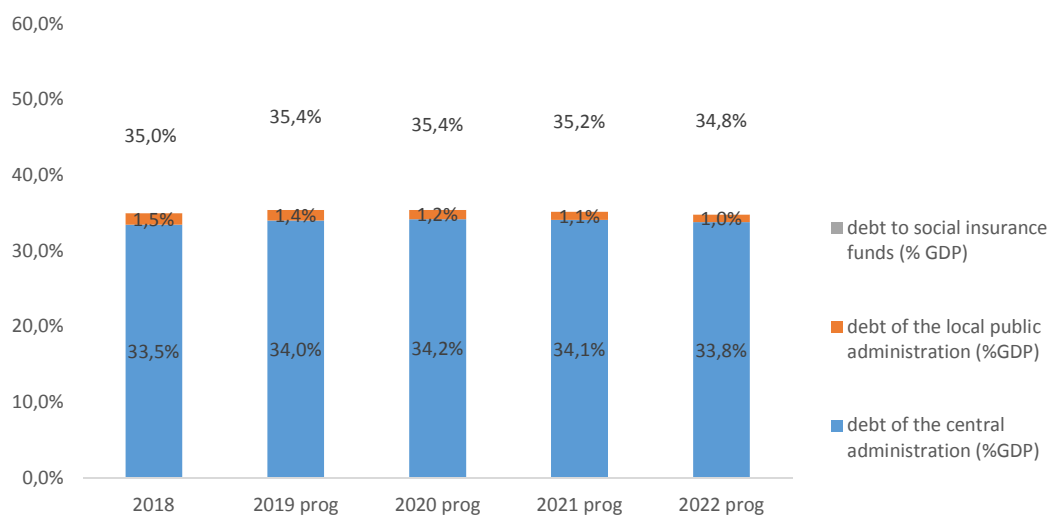
Graph 9: Gross Government public debt according to the EU methodology



Source: Ministry of Public Finance

If the liquid financial assets are considered⁴¹, the level of net government public debt (representing the gross government public debt minus the liquid financial assets) during the period under analysis will not exceed 30% of GDP.

Graph 10: The Government public debt according to the EU methodology



Source: Ministry of Public Finance

The factors which influence the change of the share of government debt in GDP in 2019-2022, including the stocks-flows adjustments, are presented in appendix 4.

⁴¹ Financial assets refer to the following instruments: AF1 - gold and DST, AF2 - deposits and cash, AF3 - securities, other than shares consolidated at market value, AF5 - shares and other capital participations, if quoted on the stock exchange, including shares of mutual funds.

5. SENSITIVITY ANALYSIS AND COMPARISON WITH THE PREVIOUS VERSION OF THE CONVERGENCE PROGRAMME

5.1. RISKS

The risks which can affect the real economy and implicitly the economic growth objective are mainly of external nature. The Romanian economy, as part of the European economy, depends on the international economic context and especially on the economic growth in the main commercial partner countries.

One first risk on medium term is represented by the conditions under which shall be made Great Britain's exit from the EU. The provisions of the draft agreement show that in terms of commercial changes there are no adverse factors, at least until 2022. Thus, the estimates of the European Commission and of the National Commission for Strategy and Prognosis, which indicate a moderate impact of Brexit, assessed at maximum 0.2% of GDP on the whole EU (lower in the case of Romania), might prove in the end to be even lower. Moreover, protection of Romanian workers' rights in Great Britain, according to the draft agreement, will have a positive effect on the current account of the payment balance. The result of the Brexit process will have an impact on the financial markets and on investors. If no understanding is reached, this would lead to a more disruptive impact on the commercial relationships between the EU and the United Kingdom and on the economic activity in Europe than currently provided in the purely technical hypothesis regarding the commercial relationships after the United Kingdom exits the EU, as provided by this interim forecast.

The negative risks related to the world context are growing in the framework of high uncertainty with regard to the United States' economic and commercial policies. A possible overheating of the American economy might trigger a faster worsening of the monetary policy, with negative impact on emerging markets, determined by the migration of capital flows from these areas towards the USA, attracted by bigger interests. Considering the open nature of the EU's economy, it would also be affected.

Slowing Romania's export markets in the EU, especially Germany and Italy, might have a negative effect on growth and investments.

Commercial tensions between the USA and China have been recently reduced, but there is still great uncertainty with regard to the nature and scope of the possible agreement between the two countries. The entrance into force of the commercial agreements, including the Trans-Pacific Partnership and the EU - Japan Economic Partnership Agreement, should contribute to avoiding a generalized escalation of commercial protectionism. Although the risk of increase of commercial tensions seems to have

decreased to a certain extent in the last months, it might continue to affect the perspectives of global economy. An interruption of global value chains and a decrease of the growth perspectives in China and the United States might also lead to a reevaluation of risks of the financial market. The risks of a more accentuated economic slowdown in China remains high, because the authorities are facing domestic policy restrictions, increasing concerns about the effectiveness of political stimuli, the possibility of continued deterioration of trade and the potential of weaker domestic demand.

At the domestic level, risks are generally positive. Also, the recovery of demand on the real estate market, on the housing segment, might trigger a relaunch of constructions activity.

Domestic risks associated with the evolution of inflation are given by the occurrence of unfavorable meteorological conditions with an effect on the prices of agro-food products, in the framework in which the forecast considers the normal agricultural years. At the same time, international events which amplify geopolitical tensions might lead to a bigger depreciation of the exchange rate than the estimated one. These risks might lead to inflation rates over the forecasted level.

5.2. SENSITIVITY OF BUDGETARY PROJECTIONS TO DIFFERENT SCENARIOS AND ASSUMPTIONS

Given that revenues from taxes are strongly correlated with the evolution of the employment rate in the economy, of the medium earning and economic growth, the table below presents the impact on the budget revenues of the variation of economic variables considered independent, based on year 2017.

Compared to the basic scenario, the highest risk in case of decrease of the economic indicators is associated with the revenues from value-added tax and social insurance contributions.

Table 8: Sensitivity of the budget forecasts for different scenarios and assumptions

Category of taxes and charges	Macroeconomic base	Changes of the macroeconomic base (pp)	Changes of the revenues (% of GDP) 2018
1. Personal income tax	Gross average salary	Reduced by 1 p.p.	-0.034
	Employment level	Reduced by 1 p.p.	-0.029
2. Social insurance contributions	Gross average salary	Reduced by 1 p.p.	-0.081
	Employment level	Reduced by 1 p.p.	-0.083
3. Corporate income tax	GDP	Reduced by 1 p.p.	-0.022
4. Value-added tax	GDP	Reduced by 1 p.p.	-0.096

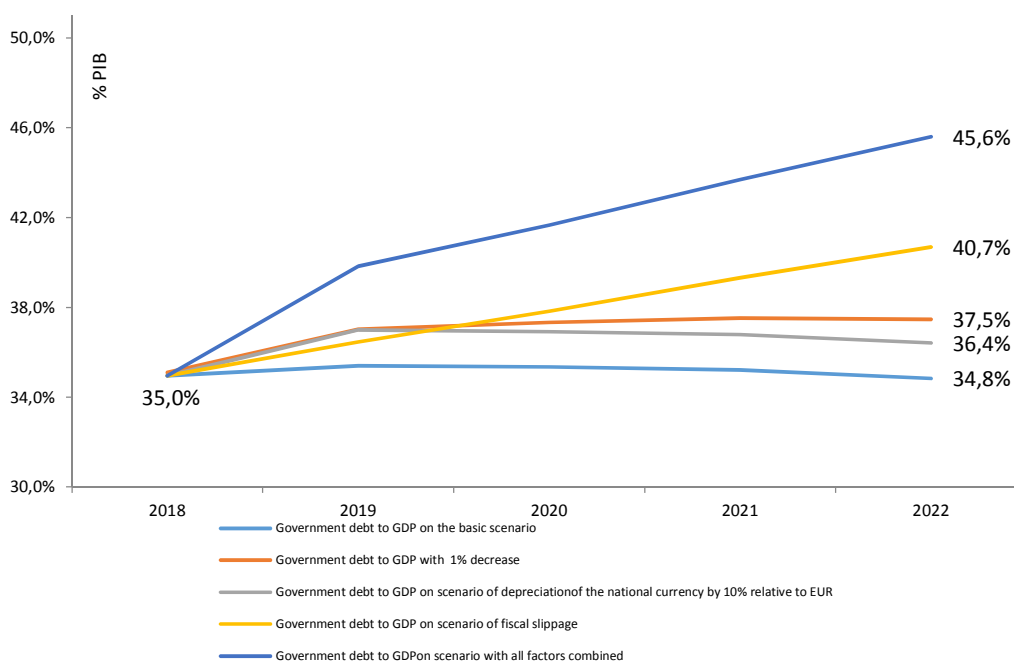
Source: Ministry of Public Finance

5.3. PUBLIC DEBT SENSITIVITY

Public debt sensitivity analysis⁴²

1. the influence of economic growth, of the depreciation of the national currency, as well as of the fiscal slippage on the government debt balance, and
2. the influence of the depreciation of the national currency and of the amendment of the interest rates on interest payments.

Graph 11: Influencing factors of government debt



Source: Ministry of Public Finance

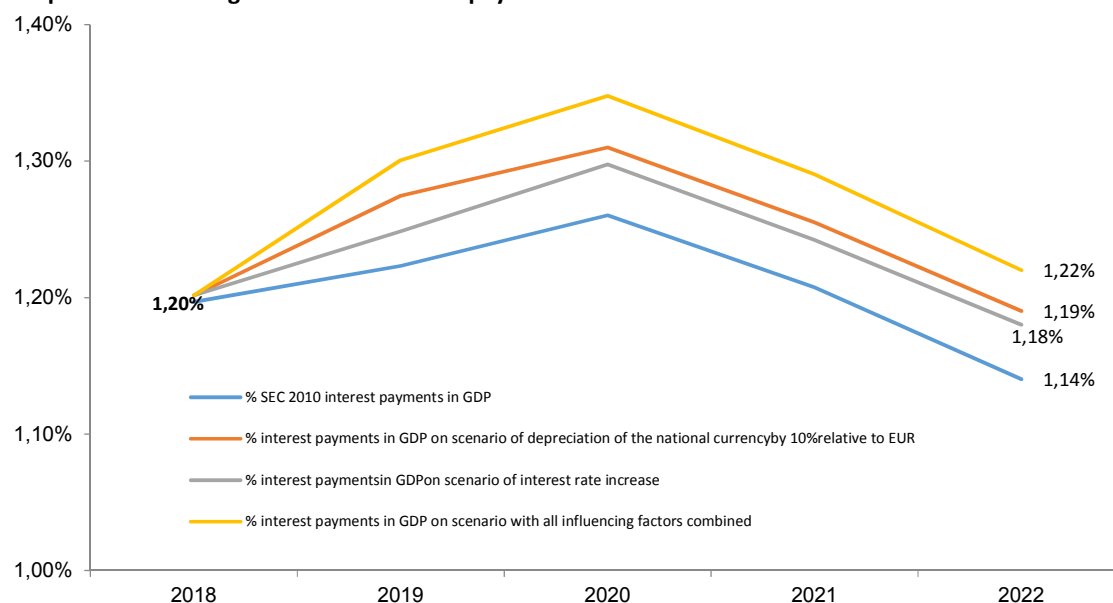
In the chart above it can be noted that the influence of an economic decrease of 1% of GDP would have a negative impact on the indebtedness level, of increase by 2.7% of GDP in 2022, and the depreciation of the national currency by 10% compared to EUR, the main foreign currency in which the Government debt in foreign currency is denominated, would cause the increase of the weight of government debt in GDP of up to 1.6% of GDP in 2022. A fiscal slippage transposed into a cash deficit to finance of 3.8%⁴³ of GDP in 2019-2020 would lead to an increase of the indebtedness degree by up to 5.9% of GDP in 2022, while the combined influence of these factors on the weight of government debt in GDP

⁴² All the indicators used in this sub-chapter are compliant with the EU methodology.

⁴³ The determination of this indicator took into account the summer forecast of the EC, which estimates for 2019 an ESA2010 deficit of 3.8 of GDP

determines an increase of this indicator by 10.8% of GDP in 2022.

Graph 12: Influencing factors over interest payments



Source: Ministry of Public Finance

In the chart above it can be noted that the depreciation of the national currency relative to EUR⁴⁴ would have a low negative impact on interest payments, within the meaning of increasing the weight thereof in the GDP by up to 0.04% of GDP in 2022, while the increase of interest rates by 1% would lead to a more accentuated increase of the weight of interest payments in GDP by up to 0.05% in 2022. The combined influence of these factors on interest payments would cause an increase of these payments by 0.08% of GDP in 2022.

5.4. COMPARISON WITH THE PREVIOUS VERSION OF THE PROGRAMME

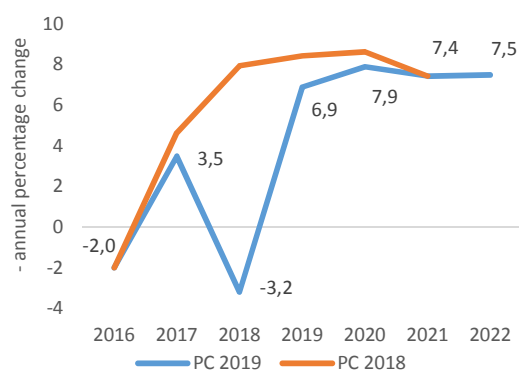
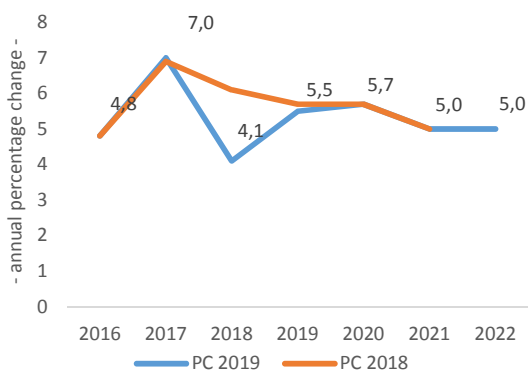
The medium-term macroeconomic development scenario presented in this program does not differ significantly from the scenario of the previous version of the Convergence Programme, namely the version of April 2018, with regard to the evolution of GDP being presented only slight revisions with respect to private consumption and GFCF, mainly as a result of publication of the provisional data for 2018. Thus, if the CP of 2018 provided for last year a dynamic of GFCF of 7.9%, provisional data indicate a decrease of 3.2%, while for private consumption the provisional increase for year 2018 is of 5.2% compared to 6.5% as it was considered when elaborating the CP for 2018. To this is added a more unfavorable contribution of net export (-1.77 pp compared to -0.6 pp in the CP of 2018), which makes

⁴⁴ The other foreign currencies in which debt is denominated follow the same tendency of appreciation

the real dynamic of the GDP for year 2018 to be, provisionally, of 4.1% compared to 6.1% in the previous edition.

Considering, on the one hand, the circumstantial nature of the slowing of economic growth in 2018, and, on the other hand, the measures from the Government Program and the evolutions from the first part of 2019, we estimate that for 2019-2020 the macroeconomic scenario does not differ significantly from that presented in the previous edition.

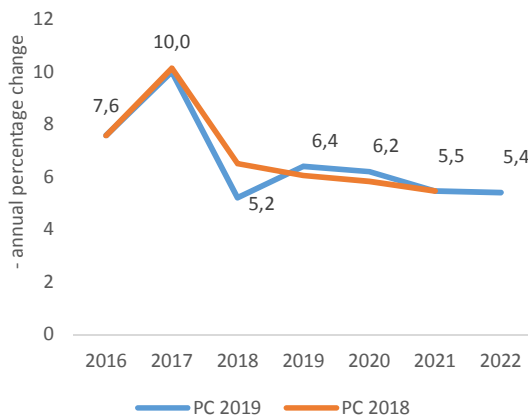
Graph 13: Comparisons between the current and the previous edition of the Convergence Programme
Comparison between the GDP increase forecasts Comparison between the GFCF increase forecasts



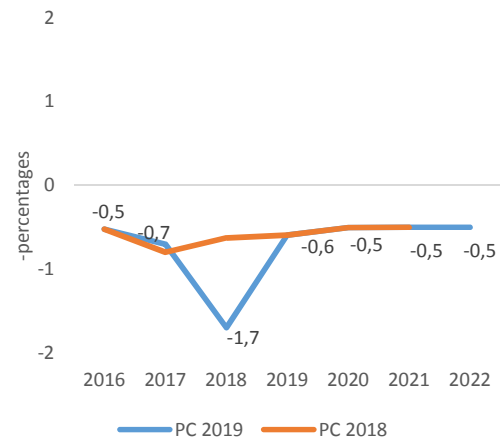
Source: National Commission of Strategy and Prognosis

Source: National Commission of Strategy and Prognosis

Comparison between the private consumption increase forecasts



Comparison between the contributions of net export to GDP increase



Source: National Commission of Strategy and Prognosis

Source: National Commission of Strategy and Prognosis

6. LONG-TERM SUSTAINABILITY OF PUBLIC FINANCE

Public finance viability for the Member States of the European Union is analyzed once every three years, both in the Fiscal Sustainability Report and in the Ageing Report, which comprises economic and budgetary forecasts for the 28 Member States of the European Union. The 2018 Fiscal Sustainability emphasized for Romania the absence, on short term, of risks against sustainability and a moderate level of these risks on medium and long term (on the forecast horizon of 2060.)

With regard to the Ageing Report, the projections of 2018 estimate that the share of pension expenditures in GDP will be maintained until the end of the projection period (year 2070, starting with the current round of projections), below the EU average. Risks would increase if the primary structural balance came back to the values registered in 1998-2012. The level of public debt is forecasted to remain significantly below the reference value of 60% of GDP, but measures of consolidation could be considered in order to limit the increase of costs due to population ageing (especially pension costs).

Compared to the 2015 exercise, for which 26 of the 28 Member States foreseen a decreasing total variation of budgetary costs related to population ageing compared to the previous exercise (2012), the current round of projection presents a balanced share, of course in the framework of extension of the forecast horizon by 10 years. The general effort among the Member States continues to remain in the direction of adjustments and reforms from the pensions, health and social assistance sectors.

The updated projection of increasing age-related expenditures indicates for Romania an increase of 2.2 p.p. of GDP for the period 2016-2070 (compared to a variation of 2.1 p.p. forecasted in the previous exercise for the period 2013-2060), the European average being of 1.8 p.p. on both rounds. On the main expenses components:

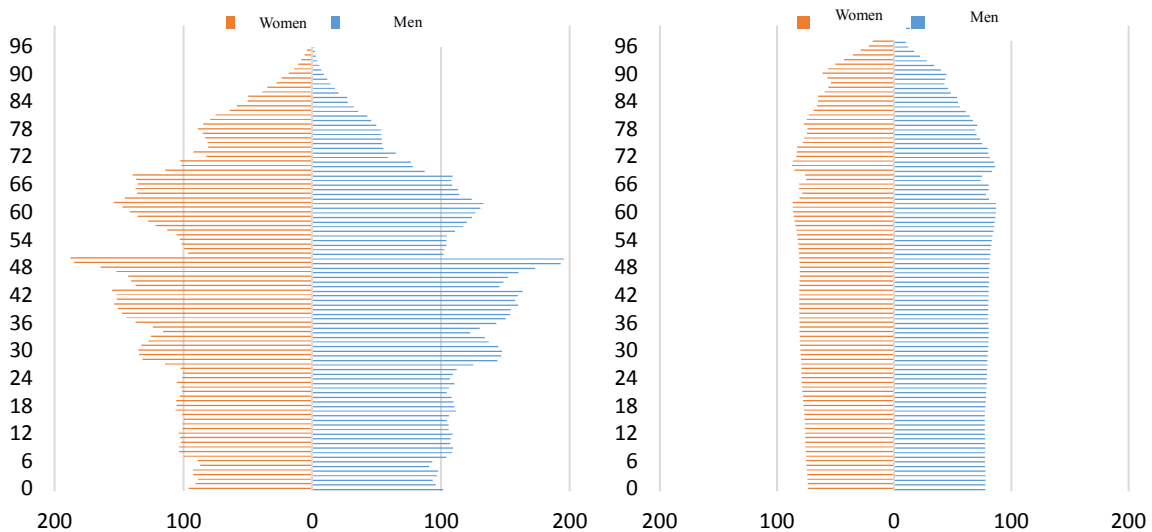
- 0.7 p.p. of GDP represents the increase of pension expenditures (the European average being of -0.2 p.p.)
- 1.2 p.p. of GDP represents the increase of health and long-term care expenditures (the European average is of 2.1 p.p.);
- 0.3 p.p. of GDP represents the increase of educational expenses (the European average is of 0.0 p.p.).

Compared to the evolutions at European level, the rhythm of increase the age-related expenses is marked in Romania by a more accentuated overturn of the age pyramid.

Graph 14: Structure of Romania's population in year 2018-2080

Structure of Romania's population in year 2018

Structure of Romania's population in year 2080



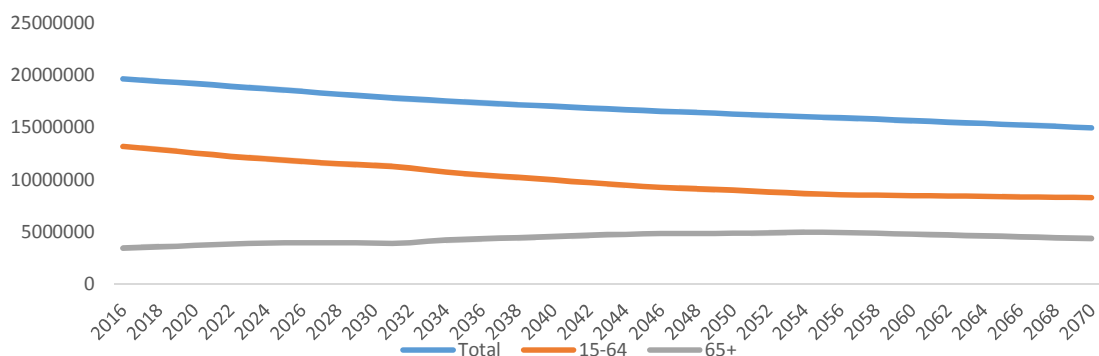
Source: Eurostat projections - EUROPOP 2016

Source: Eurostat projections - EUROPOP 2016

Demographic changes will change the structure of Romania's population. The amplitude and speed of population ageing depend on the future tendencies with regard to life expectancy, fertility and migration.

The fast ageing process will change the ratio between the population at retirement age and the active population, which will lead to major changes in the age structure and to negative implications on the labour market. The ratio between people aged over 65 years and those at working ages (15 to 64 years) increases significantly, which means that in the perspective of the following years the public pension system will have much reduced resources relative to expenditures.

Graph 15: Population evolution



Source: Eurostat- EUROPOP 2016

The composition on ages of the population will be profoundly affected in 2016-2070: the share of working population (15-64 years) will record a significant decrease of 11.8 percentage points in the period of the forecast interval, while the share of population older than 65 will increase during this interval by 11.6 percentage points.

The population's ageing process is also a consequence of the low fertility level: in 2015, the fertility rate was of 1.58 children per woman, being below the optimal reproduction level. It is projected to increase to 1.89 in 2070, according to Eurostat estimates.

The results of the demographic forecast offered by Eurostat for Romania ⁴⁵, indicates a significant decrease of the population, by 4.7 million people less in 2070 compared to year 2016. Although the young population is decreasing, due to the ever lower number of women at fertility ages, there are a series of positive signals of increase of the fertility rate.

Table 9: Demographic indicators

	2013	2020	2030	2040	2050	2060
Fertility rate	1.65	1.73	1.79	1.81	1.82	1.83
Population - total mill.	20.02	19.69	19.00	18.46	17.97	17.44
of which:						
Men	9.76	9.59	9.26	9.02	8.81	8.57
Women	10.26	10.10	9.74	9.44	9.16	8.87
Life expectancy at birth						
Men	70.8	72.8	75.4	77.8	80.0	82.0
Women	77.9	79.5	81.6	83.5	85.1	86.7
Life expectancy at 65 years of age						
Men	14.5	15.5	16.9	18.3	19.6	20.8
Women	17.8	18.8	20.1	21.4	22.7	23.9

Source: Eurostat- EUROPOP 2013

⁴⁵Eurostat – EUROPOP 2013

According to Eurostat estimates (EUROPOP2016), in Romania, life expectancy at birth for men is estimated to increase by approximately 12 years throughout the projection period, from 71/2 in 2013 to 86/6 years in 2070. Life expectancy at birth is estimated to increase by 10 years for women, from 78/5 years in 2015 to 88/3 years in 2070, which indicates a slight convergence of life expectancy between men and women. Life expectancy at 65 years is foreseen to evolve as follows:

Men 14/5 years (2015) - 22/0 years (2070)

Women 17/9 years (2015) - 25/1 years (2070)

On medium and long term, the evolution of the pensions sector is strongly influenced by the demographic perspectives given by the evolution of the natality rate and of life expectancy and by the unavoidable process of population ageing.

Table 10: Long-term forecast of pension expenditures

	2016	2017	2020	2030	2040	2050	2060	2070
1st Pension pillar	8.0	7.3	7.3	6.6	7.7	8.7	8.9	8.7
2nd Pension pillar	-	-	-	0.2	0.5	0.8	1.0	1.1

Source: National Commission of Strategy and Prognosis

The results estimated through the pension model indicate an increase of the weight of pension expenses from the 1st pillar, from 8.0% of GDP in 2016 to approximately 9.0% of GDP in the middle of the 2050-60 decade, followed by a gradual decrease towards the end of the forecast period until the weights at the end of years 2040 (8.7%).

2 Pension pillar will have a more and more significant weight in the total pension expenses, reaching a weight of 1.1% of GDP at the end of the forecast horizon.

The projections included in the 2018 Ageing Report, whose results are presented in this chapter, were made before promoting the fiscal measures entered into force at the beginning of year 2018.

7. PUBLIC FINANCE QUALITY

The structural measures for increase of public spending transparency, analysis and improvement of their efficiency, modernization of public procurement, prioritization of investments, strengthening corporate governance in State-owned enterprises will lead on the medium term to improving public finance quality.

Efficient management of public investments

One of the major concerns in the budgetary spending policy is the optimization of the structure towards an architecture that stimulates sustainable economic development, especially through the reorientation of public investment expenses, in order to make a gradual passing from the investments financed entirely from national sources to investments financed from EU funds. An important step in this policy is represented by budget planning and the prioritization of significant public investment projects, in order to increase the absorption of EU funds, so as to create fiscal space and support economic growth.

The existing legal framework has been improved during 2016-2018 in order to consolidate the link between the prioritization and budgeting process. Thus, the national authorizing institution were obliged to finance with priority depending of needed funding those public investment projects which obtain high scores according to the prioritization principles and criteria.

According to the existing prioritization methodology of significant public investment projects (Chapter II of G.E.O. no. 88/2013, as subsequently amended and supplemented, and GD no. 225/2014, as subsequently amended and supplemented), in 2018 the Ministry of Public Finance presented to the Government for approval the Memorandum themed: Approval of the prioritization results of significant public investment projects, which were used in the process of elaboration the State budget for 2019. The list of prioritized public investment projects, approved through memorandum, comprises 136 significant public investment projects (values over 100 million Lei), the biggest share being held by the transport sector projects(84%).

At the same time, one of the the World Bank recommendations in the technical assistance project of “The improvement of public investment management” carried out in 2014-2015, was to rationalize the portfolio of public investments.

In this regard, the Ministry of Public Finance, in collaboration with the Ministry of Transport, started a pilot exercise of rationalization in order to test the rationalization mechanisms and criteria proposed by the World Bank. It is estimated that by the end of 2019 the activities of the work group will be completed, and the rationalization criteria

that were identified will be approved by the management of the Ministry of Public Finance, and following to be part of a regulatory proposal which will be presented to the Government.

Starting from the World Bank recommendations within the same technical assistance project, it was amended the frequency of reports presented by the National Authorizing Institution in order to monitor the implementation of significant public investment projects. Thus, following Methodological norms amendments on the prioritization of public investment projects in 2018, the progress of significant public investment projects is monitored quarterly.

Also, based on these new regulations, at the Ministry of Public Finance level has been elaborated and subsequent approved, a draft order establishing the framework content for reporting by the main spending authorities of the progress and result indicators corresponding to significant public investment projects. The provisions of this order entered into force in January 2019.

Public-private partnership

The current Government has profoundly changed the current legal framework for PPP, in order to make more simple and efficient the process of assignment and implementation of investment projects in PPP. In May 2018 was approved the Emergency Ordinance no. 39/2018 on public-private partnership. The main provisions of Emergency Ordinance no. 39/2018 are:

- Public-private partnerships have the object to create or, as applicable, to rehabilitate and/or extend an asset or certain assets which will belong to the public partner's patrimony and/or the operation of a public service.
- Public-private partnership stipulates that more than half of the revenues that shall be obtained by a project company from the use of the good/goods or the operation of the public service that forms the object of the project comes from payments made by the public partner or by other public entities to the benefit of the public partner.
- The forms of public-private partnership are the following:
 - contractual public-private partnership - public-private partnership made on the basis of an agreement concluded between the public partner, the private partner and a new company whose share capital is held entirely by the private partner who will act as project company;
 - institutional public-private partnership - public-private partnership made on the basis of an agreement concluded between the public partner and the private partner, whereby the public partner and the private partner establish a new company, which will act as project company and after registration in the

companies register, acquires the capacity of party to the public-private partnership agreement.

- Financing for investments within public-private partnerships, can be ensured as follows:
 - Entirely, from financial resources provided by the private partner;
 - From financial resources provided by the private partner, together with the public partner.
- The share of the public partner's contribution to financing investments within a PPP agreement must not exceed 25% of the total investment.
- For the purpose of concluding and initiating the implementation of the obligations in the PPP agreement, it is necessary for the following stages to be followed:
 - The performance of a substantiation study by the public partner;
 - The approval by the Government of the substantiation study for the projects from the central administration or, as applicable, by the competent authorities for the projects from the local public administration;
 - The assignment procedure of the PPP agreement;
 - The approval by the Government of the PPP agreement resulting after the completion of negotiations started by the parties, in the case of projects from the central administration or, as applicable, by the competent authorities for the projects from the local public administration;
 - Signing of the PPP agreements.
 - Fulfillment of all requirement for repealing provided by the PPP agreement, including completion;

According to GEO no. 39/2018, the institution in charge of the preparation and assign of strategic PPP projects is the National Commission for Strategy and Prognosis. According to Emergency Ordinance no. 28/2018, the National Commission for Strategy and Prognosis is the central unit of underlying and asign the strategic investment projects carried out between the public sector and one or several private partners.

A Government Decision established that 22 strategic investment projects should be assigned to the public partners that will implement by the National Commission of Strategy and Prognosis.

According to the new legislation, the following projects are in different stages of implementation :

- Ploiesti-Brasov Highway
- "Dr. Calistrat Grozovici" Multi-functional Clinic
- Targu - Neamt - Iasi Highway

- Arrangement of the river Arges for navigation
- Construction and operation of a national bank for blood, human plasma and stem cells.

Making budget expenditures more efficient

In 2017 was established the Inter-ministry analysis and efficiency of public spending committee (Decision no. 397/2017 of the prime-minister), a structure led by the prime-minister (president) and by the minister of public finance (vice-president), whose objective is to support at political level the activity specific to public spending efficiency analyses.

For education and health fields, the working groups established in the Directorate of analyses and efficiency of public spending (MPF) have elaborated diagnostic analyses, terms of reference and sheets of measures (measures that were discussed in the working groups with representatives of the MH, CNAS, and MNE).

Pilot spending analyses were made in the fields of transport, health, education, etc. through the Memorandum themed: "Approval of the public spending review framework and establishing the fields for which efficiency reviews will be carried out in 2017", approved in 2017. The analysis in the transport field will continue with the elaboration of the final report.

In October 2018 the Government organized meetings with the representatives of all ministries, in order to identify real measures for reduction of expenditures for each ministry, a centralization of the measures of reduction of these expenditures being presented to the prime-minister on October 15, 2018.

During the meetings were identified 40 efficiency measures, classified into the following categories: reorganization/decentralization, public spending management, public procurement, expenditures made by the public entity as a member in international bodies and for participation to conventions, utilities spending, car fleet spending, reducing the administrative effort by renouncement on paper documents, increasing the revenues and consolidating the activities for attracting of European funds.

The action continues in 2019: as of March shall be carried out an extensive process of the public administration's spending analysis at the level of the main, secondary and tertiary authorizing institution, having completion term in July, aiming that the measures identified for spending reduction to be implemented on the first budget rectification of this year.

One of the priorities of the following period is the elaboration of a legislative act in order to integrate the process of public spending analysis into the public financial management system.

Improving the collection of taxes and charges

In 2018, the National Agency for Fiscal Administration NAFA collected 15.2% over the level of revenues collected in 2017, given an economic growth of 4.1% in 2018 compared to 2017.

The collection of budget revenues was significantly influenced by the provision of quality terms of the assistance requested by the taxpayers, by the inspection and control activities made by the structures of NAFA (inspection, anti-fraud, customs, revenues, control for private individuals) based on the risk analysis, which determined the increase of the degree of voluntary compliance at payment by 1 p.p., from 85.4% to 86.4%.

In order to increase the voluntary compliance among taxpayers, was updated and published on the website the “brochure regarding the procedure of enforcement and the civil offences under the Law on prevention no. 270/2017”. At the same time, was elaborated a document whereby the users of the Virtual Private Space were informed about the possibility and the conditions of benefiting of payments in installments for their tax liabilities. In 2018 were approved 10,607 applications for payment in installments of the outstanding budget liabilities of 2,179.1 million Lei. The amounts collected from the payment installments increased by 8.7% compared to the previous year

In the field of tax inspection, in 2018 were issued a total number of 27 anticipated individual fiscal solutions (13 decisions of rejection) and 3 unilateral agreements for prices in advance. At the same time, in order to facilitate voluntary compliance of economic operators, NAFA conceived a series of instruments implemented with the of National Center for Financial Information’s support : a dedicated section on the NAFA’s portal “Electronic cash registers”; extending the modalities of communication of the documents that correspond to the process of request and assign of a unique identification number for the electronic cash registers through the Virtual Private Space service.

In the Program of improvement of fiscal compliance of high net worth individuals (HNWI), the Agency carried out education campaigns following which the amounts declared by these individuals increased from 130 million Lei for 2016 to 334.1 million Lei for 2017.

In the field of tax evasion reduction and shadow economy, in 2018 ANAF made 143,335 verifications at legal entity and private individual taxpayers, following which were attracted to the general consolidated budget total additional amounts of 6,068.8 million lei.

The activities performed by fiscal inspection aimed the performance of controls regarding the taxpayers and sectors of activity identified as presenting high fiscal risk in terms of voluntary compliance, thus confirming the internal analyses that had been carried out. In 2018 were established liabilities of approximately 5,997.2 million Lei following the performance of 25,719 fiscal inspections (general and partial) and 15,233 controls (unannounced controls, cross-controls and findings on the spot).

The anti-fraud structures acted on the line of prevention, discovery, fighting tax evasion, the lines of action being analysis, investigation and instrumentation, as well as cooperation with the criminal prosecution bodies of organized and systematic fiscal fraud cases, with a significant impact on the accomplishment of the revenues of the general consolidated budget. Following the control actions carried out by the anti-fraud structures were established/quantified prejudices corresponding to the notifications submitted to criminal prosecution bodies and sanctions for civil offences were applied for a total amount of 1,234.3 million Lei. The value of the notifications with prejudices bigger than 1 million Lei represents 94.6% of the total value of the prejudices corresponding to those notifications.

The efforts in fraud fighting in the field of VAT, including cross-border fraud, continued in 2018. The share of VAT in the total liabilities estimated in the notifications is approximately 42%.

Also, the anti-fraud structure continued the measures of stimulation the issuance of fiscal receipts. In the first quarter of 2018, NAFA started the process of registration of information about the electronic cash registers. In 2018 was ordered the suspension of the activity for 615 economic operators. In 486 cases the suspension was ordered for deviations from the legal provisions regarding equipment with and use of electronic cash registers.

With regard to administrative cooperation on the line of VAT with the Member States, it was ensured the coordination of 7 multilateral controls (of which two started by ANAF) carried out in order to fight fraud in the field of intra-Community transactions with motor vehicles, electronics, mobile phones, consumer products. Two of the controls refer to the taxation of salaries for workers detached to another Member State and transfer pricing.

In the customs field, in 2018 were submitted and processed 659,157 customs declarations for placement of goods in free circulation, being established rights of import and other charges of 18,968.6 million Lei.

By the end of 2018, following the fiscal controls regarding the personal income tax corresponding to 410 private individuals, were completed 184 personal fiscal verification

actions and partial fiscal inspections, for 118 were issued taxation decisions and for 66 termination decisions. Through the 118 taxation decisions were found additional revenues of 336.3 million Lei, whereby were established fiscal liabilities of 87.1 million Lei. Following the control actions, in 26 cases were notified the criminal prosecution bodies, the total value of the prejudices brought to the State budget being 39.1 million Lei.

At the end of 2018 the concept of single counter was implemented in 78 fiscal units, for the other units this action being in process of implementation.

In all territorial fiscal units was implemented the concept of “self-service”, which consists in the installation of a computer in dedicated spaces to be used by the taxpayers, with the ANAF personnel assistance, in order to support in using remote services. Also, 38 fiscal units have operational systems of queue management and report the data extracted

With regard to increasing the efficiency of collection, in order to reduce financial and time costs both for the taxpayers and for the administration, were simplified the procedures of use of the on-line declaration service. In 2018 was registered a degree of electronic declaration of 95.2% compared to 88.1% in 2017.

NAFA’s strategic objectives for 2019-2022

The strategic objectives of NAFA in 2019-2022 consists in priority actions on the following directions: increasing voluntary compliance, reducing tax evasion and underground economy, improving the relationship with the taxpayers, increasing collection efficiency, modernizing the agency.

In order to improve voluntary compliance it is targeted the creation of technical and procedural conditions for payment of all tax liabilities through all banking instruments (modernization of the procedures and instruments dedicated to the citizens for registration and payment of tax liabilities through the construction and publication of the electronic register of taxes, local charges and other contributions; digitalized fiscal assistance for the taxpayers). Furthermore, the possibility of granting payment facilities is promoted. At the same time, it is targeted the increase of voluntary compliance in the field of transfer pricing through prevention of the eroding of the taxable base by promotion the possibilities of issuance the unilateral/bilateral/multilateral advance pricing agreements, as well as of the possibilities of initiating the amicable procedure in the case of transactions adjusted as a result of fiscal documents issued by other jurisdictions fiscal authorities .

In the field of reduction tax evasion and shadow economy will be continued actions like: the introduction of the random compliance testing program through fiscal controls, the fight of tax evasion in the field of VAT, including of cross-border fraud, control actions to

stimulate the equipment of economic operators with electronic cash registers and the issuance of fiscal receipts, the fight of customs fraud.

In the field of fiscal anti-fraud it is sought to increase the share of controls dedicated to de-structuring evasion chains and to eliminate from the system “ghost” companies, as well as to intensify the use of administrative cooperation instruments in the field of VAT, including multilateral controls. Anti-fraud procedures will be revised, in accordance with the European noncompliance risk management model.

In order to improve the methodological and procedural framework necessary to reduce the under-declaration of taxes, charges and contributions will be developed a modular training program for fiscal inspection. At the same time, the NAFA will develop, together with the MPF, a system of individual anticipated solutions for complex fiscal fields.

The relationship with the taxpayers will be improved through the increase of the role of taxpayer services, the increase of the institution’s transparency and of its role of prevention and the decrease of compliance costs for taxpayers following the simplification of the administrative framework, the encouragement of migration of taxpayers to the electronic environment and the development of the functionalities of the Virtual Private Space.

For the taxpayers support will be developed a new, interactive service, “Web seminars”, like presentations, courses, conferences carried out through the World Wide Web, where the audience is actively participating and may address questions to the lecturers in real time.

In order to increase collection efficiency, to make the administration activity more efficient, is planned to maximize the involvement of ANAF in the establishment of the legal framework through elaboration of an external communication plan. At the same time, an arrear recovery strategy will be elaborated. Futhermore, is envisaged to improve the way of forecasting and reporting of fiscal revenues.

The agency’s modernization considers actions whose effect will be the reduction of budget revenues collection cost: maintaining an efficient planning system for the labor force necessary to ensure optimal employee allocation, to consolidate policies and practices of training and development of the employees, as well as to elaborate and implement leadership training programs, to modernize customs offices.

Measures regarding the introduction into the national legislation of the European directives in the field of taxation and participation to European initiatives

In 2016, Romania received an invitation from the OECD to be an associate in the BEPS Project (Base Erosion and Profit Shifting) and was represented at the first meeting which took place in Kyoto, in the period of June 30 - July 1, 2016.

The BEPS plan brings recommendations for legislative amendments, both in the national fiscal legislations and in the international provisions, to counteract the situations that occur as a result of the use by multinational enterprises of unintentional legislative inconsistencies provided by the national fiscal systems of the countries where these enterprises extend their activities. Such inconsistencies are successfully used by multinational enterprises to make their profits “disappear” for fiscal purposes or be “shifted” to jurisdictions where their activity is low or non-existent, but where the taxation level is lower or null, so that the corporate income tax paid by such multinational enterprises should be as little as possible or zero.

Under these circumstances, Romania becoming member, it approaches the issue of avoidance of double taxation, of counteracting damaging fiscal practices, limiting taxable base erosion through limitation of deductibility of interest expenditures, as well as the regulation of transfer pricing and of a multilateral judicial system.

Directive (EU) 2016/1164 of the Council was adopted, laying down rules against tax avoidance practices that directly affect the functioning of the internal market, which ensures a coherent and coordinated common framework.

This approach in the Member States also ensures the judicial certainty according to which the measures in question are compatible with the Union law, as well as the fact that in this manner it is improved the operation of the internal market and the positive effects of the BEPS initiative are maximized.

Romania adheres to the BEPS Plan as an associated member:

- it will join the activities related to technical issues, for example, in the field of fiscal treaties and transfer pricing. This includes the works regarding the development of the transfer pricing guide and of double taxation avoidance conventions;
- It will implement the four minimum standards of BEPS (Action 5 regarding damaging fiscal practices, Action 6 regarding abuse of fiscal treaties, Action 13 regarding country by country reporting, and action 14 regarding dispute settlement mechanisms);
- It will monitor the evolution of taxes as a result of the challenges of the digital

economy (Action 1), 4, as well as through economic analysis of BEPS (Action 11);

- It joins the key decision makers in the international fiscal field, like the Commission for Fiscal Affairs of the OECD and its subsidiaries;

It was continued the implementation of **Directive 2016/1164**, respectively of the amendments made thereto through Directive 2017/952 of the Council;

- **fiscal consolidation** will be able to reduce the administrative burden and will give the possibility to the groups to better organize their financial flows. Also, the creation and development of Romanian holdings will be stimulated, as well as investments in Romania. Within the same meaning, it eliminates the competitive disadvantages of groups of Romanian legal entities against foreign groups.

At the same time, considering Romania's obligation in its capacity as Member State of the European Union to harmonize the national legislation with the legislation of the European Union was elaborated a draft law which transposed into the national legislation the provisions of the following directives:

- **Directive (EU) 2016/1065** of the Council of June 27, 2016 amending Directive 2006/112/EC with regard to treatment applied to value coupons and
- **Art. 1 in Directive (EU) 2017/2455** of the Council of December 5, 2017 amending Directive 2006/112/EC and Directive 2009/132/EC as regards certain value added tax obligations for supplies of services and distance sales of goods.

8. ANNEXES

Table no. 1 – Macroeconomic projections

	Code Sec	2018	2018	2019	2020	2021	2022
		Level ¹⁾ Billion Lei	Percentage change				
1. Real GDP	B1*g	891.8	4.1	5.5	5.7	5.0	5.0
2. Nominal GDP	B1*g	944.2	10.2	9.2	7.7	7.0	7.0
Real GDP components							
3. Private consumption expenses	P3	568.6	5.2	6.4	6.2	5.6	5.5
4. Public consumption expenses	P3	136.7	1.8	4.1	3.8	2.3	2.3
5. Gross fixed capital formation	P51	185.8	-3.2	6.9	7.9	7.4	7.5
6. Change of stocks and net securities procurement (% of GDP)	P52+ P53	33.6	2.9	0.0	0.0	0.0	0.0
7. Exports of goods and services	P6	375.1	5.4	6.9	7.1	7.0	7.0
8. Imports of goods and services	P7	408.1	9.1	7.8	7.9	7.8	7.8
Contributions to GDP growth							
9. Final domestic demand		891.2	2.9	6.1	6.2	5.5	5.5
10. Change of stocks and net securities procurement	P52+ P53		2.9	0.0	0.0	0.0	0.0
11. Net export	B11		-1.7	-0.6	-0.5	-0.5	-0.5

The real level of GDP and its components is in the prices of the previous year.

Table no. 1 b – Price evolution

	2018	2019	2020	2021	2022
	Percentage change				
1. GDP deflator	5.9	3.5	1.9	2.0	2.0
2. Private consumption deflator	3.7	2.7	1.4	1.5	1.6
3. Harmonized consumer price index	4.1	3.5	2.6	2.5	2.4
4. Public consumption deflator	14.7	2.6	2.1	2.2	2.4
5. Investments deflator	7.8	2.6	1.2	1.0	0.8
6. Export deflator (goods and services)	4.8	2.7	-0.5	-0.2	-0.3
7. Import deflator (goods and services)	3.8	-0.2	-1.6	-1.4	-1.4

Table no. 1 c - Labor force market evolution

	CODE SEC	2018	2018	2019	2020	2021	2022
		Level thousand persons	Percentage change				
1. Total working population ¹⁾		8668.3	0.2	1.4	1.2	1.2	1.0
2. Working population, thousand hours worked ²⁾		15710672	0.3	1.0	1.1	1.1	1.1
3. Unemployment rate -% ³⁾		379.7	4.2	4.1	4.0	3.9	3.8
4. Labor productivity ⁴⁾			3.9	4.1	4.4	3.7	3.9
5. Hourly work productivity ⁵⁾			3.8	4.5	4.5	3.8	3.8
6. Payment of employees million Lei	D1	376603	20.4	10.3	8.4	7.7	7.6
7. Payment per employee - Lei		57191	18.4	8.1	6.1	5.5	5.4

¹⁾ Working population, the definition for the internal concept from the national accounts

²⁾ The definition from the national accounts

³⁾ The definition harmonized with Eurostat (Labor Force Survey – AMIGO)

⁴⁾ Real GDP per working person

⁵⁾ Real GDP per hour worked

Table no. 1 d – Sector balances

% of GDP	CODE SEC	2018	2019	2020	2021	2022
1. Net balance, compared to the rest of the world	B9	-3.3	-1.7	-0.8	-0.3	-0.1
Of which:						
- the balance of goods and services		-3.2	-2.3	-2.1	-1.9	-1.7
- the balance of primary income and secondary income		-1.3	-1.0	-0.8	-0.7	-0.7
- capital account		1.2	1.6	2.2	2.3	2.3
2. Net private sector balance	B.9	-0.3	1.1	1.9	2.1	1.9
3. Net government sector balance	EDP B.9	-3.0	-2.8	-2.7	-2.4	-2.0
4. Statistical discrepancy		0	0	0	0	0

Table no. 2 a– Consolidated budget projection

	CODE SEC	2018	2018	2019	2020	2021	2022
		LEVEL MILLION LEI	% of GDP				
Bet balance (EDP B9), per sub-sectors							
1. Consolidated budget	S.13	-28,496.6	-3.0	-2.8	-2.7	-2.4	-2.0
2. Central administration	S.1311	-30,719.8	-3.3	-3.3	-3.0	-2.7	-2.4
3. State administration	S.1321	M	M	M	M	M	M
4. Local administration	S.1313	-697.5	-0.1	0.0	0.0	0.1	0.1
5. Social insurance fund	S.1314	2,920.7	0.3	0.5	0.2	0.1	0.2
Consolidated budget (S13)							
6. Total revenues	TR	302,261.6	32.0	33.8	33.8	33.5	33.9
7. Total expenditure	TE ¹⁾	330,758.2	35.0	36.6	36.4	36.0	35.9
8. Net balance	EDP B.9	-28,496.6	-3.0	-2.8	-2.7	-2.4	-2.0
9. Interests	EDP D.41	11,299.7	1.2	1.2	1.3	1.2	1.1
10. Primary balance ²⁾		-17,196.9	-1.8	-1.6	-1.4	-1.2	-0.9
11. One-off and other temporary measures ³⁾		-3,183.7	-0.3	-0.1			
Selected revenue components							
12. Total taxes (12=12a+12b+12c)		144,696.9	15.3	15.6	15.4	15.2	15.2
12a. Production and import taxes	D.2	98,322.0	10.4	10.7	10.5	10.2	10.1
12b. Current taxes on income, fortune, etc.	D.5	46,374.9	4.9	4.9	5.0	5.0	5.1
12c. Capital taxes	D.91						
13. Social contributions	D.61	108,072.1	11.4	12.3	12.5	12.9	13.2
14. Property taxes	D.4	10,891.3	1.2	1.1	1.0	1.0	1.0
15. Others ⁴⁾		38,601.3	4.1	4.8	4.8	4.4	4.5
16=6. Total revenues	TR	302,261.6	32.0	33.8	33.8	33.5	33.9
Selected expenses components							
17. Employee payment + interim consumption	D.1+P.2	152,014.5	16.1	16.7	16.3	15.8	15.4
17a. Employee payment	D.1	103,915.0	11.0	11.7	11.4	11.0	10.6
17b. Interim consumption	P.2	48,099.5	5.1	5.0	4.9	4.8	4.7
18. Social contributions (18=18a+18b)		110,307.4	11.7	11.5	12.3	12.2	12.8
of which Unemployment aid ⁵⁾		608.2	0.1	0.0	0.1	0.1	0.1
18a. Social contributions in kind	D.6311, D.6312, D.63131	8,148.8	0.9	0.8	0.8	0.8	0.8
18b. Social contributions, others	D62	102,158.6	10.8	10.7	11.5	11.5	12.0
19=9. Interests	EDP D.41	11,299.7	1.2	1.2	1.3	1.2	1.1
20. Subsidies	D.3	3,403.3	0.4	0.4	0.4	0.4	0.4
21. Gross fixed capital formation	P.51	24,909.7	2.6	3.5	3.3	3.4	3.3
22. Capital transfers	D.9	12,348.2	1.3	1.3	1.0	1.0	1.0
23. Others ⁶⁾		16,475.4	1.7	1.9	1.8	1.9	1.9
24=7. Total expenses	TE1	330,758.2	35.0	36.6	36.4	36.0	35.9

¹⁾ Adjusted with the net swap flow, namely TR-TE=EDP B9

²⁾ The primary balance is calculated as (EDP B9, point 8) plus (EDP D.41, point 9)

³⁾ The plus sign means the reduction of deficit following one-off measures

⁴⁾ P.11+P.12+P.131+D.39+D.7+D.9 (different than D.91)

⁵⁾ Includes cash benefits (D.621 and D.624) and in kind benefits (D.631), related to unemployment aid

⁶⁾ D.29+D4 (different than D.41)+D.5+D.7+D.9+P.52+P.53+K.2+D.8

Table no. 2b – Projections in the situation of preservation of current policies¹

	2018	2018	2019	2020	2021	2022
	Level	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP
1. Total revenues in case of preservation of current policies	302,261.6	32.0	33.8	33.8	33.5	33.9
2. Total expenses in case of preservation of current policies	330,758.2	35.0	36.6	36.4	36.0	35.9

¹⁾ The projections must start at the time when the Stability or convergence programme is elaborated and shows the trend of revenues and expenses, presupposing „no policy amendment” occurs. Therefore, the figures for X-1 will correspond to the current data for revenues and expenses.

Table no. 2 c – Amounts which must be excluded from the reference value of expenditures

	2018	2018	2019	2020	2021	2022
	Level (million Lei)	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP
1. Expenses from EU programs covered completely from EU funds	8,995.8	1.0	1.6	1.2	0.9	0.9
1.a. of which expenditures of the type of investments financed from EU funds	6,746.9	0.7	1.2	0.9	0.7	0.7
2. Cyclical expenses for unemployment aid ¹	-56.5	-0.0011	0.0004	-0.0004	-0.0011	-0.0011
3. Effect of discretionary measures related to revenues ²	3,394.0	0.36	0.04	0	0	0
4. Increase of the revenues imposed by law	0	0	0	0	0	0

¹⁾ The methodology used to obtain the cyclical component of the expenses that correspond to unemployment aid, as it is defined by COFOG under code 10.5

$$E_t^{UC} = E_t^U \cdot \frac{u_t - NAWRU_t}{u_t}$$

The following formula was used: where:

E_t^U represents unemployment expenses and E_t^{UC} represents the cyclical component of unemployment aid expenses.

²⁾ The increase of revenues imposed by law must not be included in the effect of the discretionary measures related to revenues: the data reported on rows 3 and 4 must be mutually excluded.

Table no. 3 – Public administration expenditures, by function % of GDP

	CODE COFOG	2017	2022
1. General public services	1	4.2	n.a.
2. Defense	2	1.8	n.a.
3. Public order and national safety	3	2.0	n.a.
4. Economic relations	4	4.4	n.a.
5. Environmental protection	5	0.5	n.a.
6. Domiciliary and community services	6	0.9	n.a.
7. Health	7	4.3	n.a.
8. Recreation, culture, and religion	8	1.0	n.a.
9. Education	9	2.8	n.a.
10. Social protection	10	11.7	n.a.
11. Total expenses (=point 7=24 in Table 2a)	TE	33.6	n.a.

*) data from 2017 updated according to EDP April 2019.

Table no. 4 – Government debt evolution

% OF GDP	SEC CODE	2018	2019	2020	2021	2022
1. Gross government debt ¹⁾		35.0	35.4	35.4	35.2	34.8
2. Government debt change		-0.2	0.4	0	-0.2	-0.4
Contribution to the gross debt change						
3. Primary balance ²⁾		-1.8	1.6	-1.4	-1.2	-0.9
4. Interest ³⁾	EDP D.41	1.2	1.2	1.3	1.2	1.1
5. Stock-flow adjustments		-3.2	-2.4	-2.7	-2.6	-2.4
<i>Of which:</i>						
- Differences between interests paid and accrual ⁴⁾		0.1	0.1	0.0	0.0	0.0
- Net accumulation of financial assets ⁵⁾		-0.4	0	0	0	0
<i>of which:</i>						
- from privatization		0	0	0	0	0
- Effects of the assessment and others ⁶⁾		-2.9	-2.5	-2.7	-2.6	-2.4
p.m. Implicit interest rate over debt ⁷⁾		3.8	3.8	3.8	3.7	3.4
Other relevant variables						
6. Liquid financial assets ⁸⁾	% of GDP	7.8	7.1	6.6	6.2	5.8
7. Net financial debt (7=1-6)	% of GDP	27.2	28.3	28.8	29.0	29.0
8. Amortization of the debt (existing obligations) as of the end of the previous year ⁹⁾	% of GDP	4.6	4.6	3.6	2.9	2.5
9. Percent of the debt denominated in foreign currency	% of debt	50.4	47.0	45.9	46.8	45.4
10. Average maturity ¹⁰⁾	years	6.5	6.5	-	-	-

¹⁾ Defined in accordance with Regulation 3605/93 (not an ESA concept)

²⁾ According to position 10 in table 2a;

³⁾ According to position 9 in table 2a;

⁴⁾ The differences regarding interest expenses, other expenses and revenues can be distinguished when they are relevant or if the debt ratio in GDP is over the reference value;

⁵⁾ Liquid assets (foreign currency), government securities, assets in third countries, enterprises controlled by the State and the difference between quoted and non-quoted assets can be distinguished when they are relevant or if the debt ratio in GDP is over the reference value;

⁶⁾ Changes due to the variation of exchange rates and to operation on the secondary market can be distinguished when they are relevant or if the debt ratio in GDP is over the reference value;

⁷⁾ The associated proxy variable is represented in the report between the annual interest payments and the debt balance of the previous year;

⁸⁾ AF1, AF2, AF3 (consolidated at market value), AF5 (if quoted on the exchange; including the shares of mutual funds);

⁹⁾ Indicator calculated on the basis of the outstanding debt - at 12/31/2018;

¹⁰⁾ Average maturity left.

Table no. 5 – Cyclical evolutions

% OF GDP	SEC CODE	2018	2019	2020	2021	2022
1. Real GDP growth (%)		4.1	5.5	5.7	5.0	5.0
2. Net consolidated balance	EDP B.9	-3.0	-2.8	-2.7	-2.4	-2.0
3. Interest expenses	EDP D.41					
4. Temporary and <i>one-off</i> measures ¹⁾		-0.3	-0.1	0.0	0.0	0.0
5. Potential GDP increase (%)		4.7	5.0	5.1	5.0	4.8
Contributions:						
- labor		0.6	0.6	0.5	0.2	-0.1
- capital		0.6	0.8	1.1	1.2	1.4
- total factor productivity		3.4	3.5	3.5	3.5	3.4
6. Output Gap		0.0	0.5	1.0	1.0	1.2
7. Cyclical component		0.0	0.2	0.3	0.3	0.4
8. Cyclically adjusted balance (2-7)		-3.0	-2.9	-3.0	-2.8	-2.4
9. Cyclically adjusted primary balance (8+3)						
10. Structural balance (8-4)		-2.7	-2.8	-3.0	-2.8	-2.4

¹⁾ A plus sign means *one-off* measures of budget deficit reduction

Table no. 6 - Differences from the previous version

	SEC CODE	2018	2019	2020	2021	2022
GDP increase (%)						
Previous version		6.1	5.7	5.7	5.0	
Updated version		4.1	5.5	5.7	5.0	5.0
Difference		-2.0	-0.2	0.0	0.0	
Budget balance (% of GDP)						
Previous version	EDP B.9	-3.0	-2.4	-1.8	-1.5	
Updated version	EDP B.9	-3.0	-2.8	-2.7	-2.4	-2.0
Difference		0.0	-0.4	-0.9	-0.9	
Gross government debt (% of GDP)						
Previous version		35.4	35.8	35.4	34.5	
Updated version		35.0	35.5	35.4	35.2	34.8
Difference		-0.4	-0.3	0.0	0.7	

Table no. 7 - Long-term sustainability of public finance

% OF GDP	2007	2010	2020	2030	2040	2050	2060	2070
Total expenses								
Of which: Age related expenses	13.2	17.0	14.3	14.1	15.8	17.1	17.5	17.3
- Pension expenses	6.3	9.2	7.3	6.6	7.7	8.7	8.9	8.7
- Social insurance expenses								
Pensions for age and anticipated pensions	5.1	7.6	6.3	5.5	6.5	7.5	7.7	7.5
Other pensions (disability, survivorship)	1.2	1.6	1.0	1.1	1.2	1.2	1.2	1.2
Occupational pensions (if related to the central administration)								
- Health care	3.5	3.7	4.4	4.8	5.1	5.3	5.3	5.2
- Long-term care (previously included under "health care")	0.5	0.6	0.3	0.4	0.5	0.5	0.6	0.6
- Education expenses	2.8	3.5	2.3	2.3	2.5	2.6	2.7	2.8
Other age related expenses								
Interest expenses								
Total revenues								
Of which revenue from properties								
Of which: from pensions contributions (or social contributions, as applicable)	5.9	6.1	5.8	5.4	5.2	5.3	5.5	5.9
Assets for the funds for pension reserves								
Of which consolidated assets of the public pension funds (other assets than the liabilities of the central administration)								
Systemic pension reforms¹⁾								
Social contributions directed towards the mandatory private pension system ²⁾	0	0.4	1.5	1.9	2.3	2.5	2.6	2.9
Expenses for pensions paid by the mandatory private pension system ³⁾	0	0	0.1	0.2	0.5	0.8	1.0	1.1
Assumptions								
Labor productivity increase rate (by hour)	2.7	0.7	3.6	3.9	2.7	2.2	1.9	1.7
Real GDP growth	6.8	3.8	3.5	2.7	1.4	1.2	1.4	1.3
Participation rate among men (20-64 years)	76.4	77.3	80.3	82.0	80.7	81.0	82.1	82.2
Participation rate among women (20-64 years)	61.2	60.0	61.0	60.4	58.0	58.0	59.3	59.3
Total participation rate (20-64 years)	68.7	68.6	70.7	71.4	69.5	69.7	70.8	70.8
Unemployment rate - BIM	6.8	6.8	5.1	5.6	5.9	5.8	5.8	5.9
Population aged 65 and more out of the total population	14.9	16.1	17.3	21.2	24.6	28.9	30.8	29.8

The average paces refer to the period between the mentioned years For the forecast period the paces are calculated on the basis of the potential GDP estimated in the exercise of assessment of public finance sustainability for 2015.

¹⁾ Systemic pension reform refer to the pension reforms which introduce a multi-pillar system, which includes a mandatory pillar with total own fund; in 2014, 1.0% of GDP was directed towards pension Pillar II.

²⁾ Social contributions or other revenues obtained by the mandatory pillar with total own fund, for coverage of pension related liabilities, attracted in accordance with the systemic reform

³⁾ Pension expenses or other social benefits paid by the mandatory pillar with total own fund, with respect to pension related liabilities, attracted in accordance with the systemic reform

Table no. 7 a - Potential liabilities

% of GDP	2018	2019
Public guarantees*)	2.1%	2.2%
<i>Of which: related to the financial sector</i>	0.0%	0.0%

*) corresponding to the public administration sector, with elimination of the guarantees given between entities of the public administration sector