GOVERNMENT OF ROMANIA

CONVERGENCE PROGRAMME

2017-2020

- April 2017 -

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FOREWORD

The 2017 edition of the Convergence Programme for 2017-2020 was elaborated on the basis of the *Regulation (EC) no. 1466/1997 of the Council on the strengthening of 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 Program is created by considering the *Code of Conduct on the Specifications of implementation 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 Program 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-regulation pack which came into effect on December 13, 2011), and of the *Macroeconomic Imbalance Procedure* and *Euro Plus Pact*.

The 2017 edition of the Convergence Program is based on the provisions of the *Fiscal and budgetary strategy for 2017-2019* and the updated macroeconomic framework for the period 2017-2020. In 2016, Romania had a deficit of the general consolidated budget in ESA terms of 3.0% of GDP, while the structural deficit was of 2.4% of GDP. For the following period, the ESA deficit remains relatively constant in 2017-2018, and will decrease to 2.0% in 2020. It is estimated that the structural deficit will increase to 3% in 2018 and will enter an adjustment trajectory towards the MTO since 2019.

The European Commission found in the country report analysis that Romania is not facing macroeconomic imbalances. Nevertheless, vulnerabilities were identified with regard to the pro-cyclic fiscal policy, the efficiency of public investments, the net investment position, as well as salary increases.

The Government of Romania maintains its commitment of adhering to the Euro area, but the setting of a concrete date in this regard requires the realization of in-depth analyses, especially with regard to real, structural and institutional convergence, fields in which important progress is necessary. In addition, it is necessary to take into consideration the sustainability of fulfillment of the nominal convergence criteria. The inter-ministry committee for passing to the EUR currency was recently established with the purpose of elaborating the national plan for passing to the EUR currency and the schedule of actions necessary for the adoption of the EUR currency. Under these circumstances, the commitment of adoption of the EUR currency continues to be an important anchor with regard to the implementation of efficient and coherent budgetary, structural and institutional policies, in order to ensure sustainable real convergence (income/inhabitant), to increase the Romanian economy's competitiveness, to reduce regional disparities and the structural deficiencies of the labor market, etc.

In terms of real convergence, assessed through the gaps relative to the European average (EU-28) of the gross domestic product (GDP) per inhabitant expressed through the standard purchase power (SPP), there is the prospect for Romania to reach 70% of the European average in 2020, compared to 57.1% registered in 2015.

1. GENERAL FRAMEWORK OF THE ECONOMIC POLICY

1.1. GENERAL FRAMEWORK OF THE ECONOMIC POLICY

Romania is going through a favorable economic period, given that in 2016 it recorded an acceleration of economic growth to 4.8%, after an advance of 3.9% in 2015. The growth is based on the 7.4% advance of private consumption, determined by salary increases and fiscal relaxation measures, while the gross fixed capital formation recorded a decrease of -3.3%, due to poor accessing of European funds on the debut of implementation of the new financial framework for 2014-2020.

Romania registered in the 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.

After the economic crisis, Romania had a modest economic relaunch, with annual growths below 1%, after which the advance of the real GDP came back to an annual pace of 3.8% in 2013-2016. These favorable evolutions caused the decrease of unemployment, the average annual unemployment rate reaching 5.9% in 2016, and the minimum level of the last eight years.

An economic growth of 5.2% is estimated for 2017, and the effectively realized production is expected to slightly exceed potential production, while the output gap is estimated to close this year.

In spite of this favorable evolution, the poverty rate among the employees remains the highest in the EU.[1] In addition, there still are large gaps between the rural and urban areas, Romania facing very high risks of poverty, social exclusion and inequalities in terms of income. In the rural area, the rate of poverty and social exclusion was double in 2015 than the one registered in the urban area, namely of 50.8% compared to 24.1%[2]. All of these factors slow down the economy's growth potential.

The medium term economic strategy of the Government is oriented towards promoting competitiveness and higher employment, continued implementation of structural reforms, improving the absorption of European funds, consolidating public finances, starting with 2019 and financial stability.

[1] In the case of employed individuals over 18 years of age, the rate of poverty and social exclusion was of 18.8% in 2015.

[2] Overall in the EU, the gap is of only 1.5 percentage points between the rural and urban areas.

1.2. FISCAL POLICY

The beginning of 2017 brought additional measures which accentuate on the whole the fiscal relaxation started in the previous years, with the purpose of stimulating economic growth.

With regard to fiscality, an important change is the decrease by one percentage point of the standard VAT rate to 19% as of January 1, 2017, after a decrease of four percentage points in the previous year. Also, the taxes on income from real estate transactions with a value lower than 450,000 Lei and on income from pensions below Lei 2,000 have been eliminated.

At the same time, in order to stimulate the business environment, a measure of exemption from the payment of corporate income tax was established for the companies which carry out exclusively activities of innovation and research and development, for the first ten years of activity. In addition, both the companies and the population will benefit of the elimination of over 100 non-fiscal charges and the decrease of the overcharge on fuels (of seven Euro cents) as of Q1 of 2017.

From the perspective of the budgetary balance, an important issue is related to revenue collection, given that Romania has one of the smallest levels of revenue collection at the State budget in the EU. In this respect, the Government proposed a series of measures dedicated to improving revenue collection and reducing tax evasion.

At the same time, the Government implemented in the first part of 2017 a series of measures which target the increase of collections at the State budget, among which counseling the taxpayers to pay their charges on time and correctly fill in the tax statements; guiding the taxpayers to access payments in installments of their tax liabilities if they are unable to pay their taxes and charges on time; extending the “Virtual Private Space” service to legal entities and other entities without legal personality; garnishments on accounts only for the amount owed to the ANAF in the case of taxpayers under forced execution; starting inspections in the field of on-line commerce and intensifying the controls in order to discover the taxpayers who register false invoices in their accounting records.

On the expenses side, the Government adopted a series of social measures dedicated to increasing the population’s standard of living, among which the increase of the gross minimum wage at national level (from Lei 1250 to Lei 1450); the increase of the salaries of staff from the local public administration, health, education, the increase of scholarships and offering free railway transportation for students. All of these followed salary increases for the staff from education and health adopted in the previous year. With regard to the pension system, the enforcement of the pension law led to the indexation of the pension point as of January 1 by 5.25%, reaching the value of Lei 917.5, with the value of the pension point to increase to 9% as of July 1, 2017, namely to Lei 1,000.

1.3. MONETARY POLICY

In compliance with its Statute[3], 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 achieving sustainable economic growth. The NBR's monetary policy is formulated and implemented in the context of the inflation targeting strategy[4], characterised by a flat inflation target of 2.5 percent ±1 percentage point[5], compatible with the definition of medium-term price stability for the Romanian economy. The NBR's monetary policy is consistently geared towards achieving the flat inflation target over the medium term, as well as towards bringing down the annual inflation rate in the longer run to levels in line with the European Central Bank's quantitative definition of price stability.

In the specific context of 2016, tailoring the monetary policy stance from such a perspective called for extending the status-quo of the parameters of the main policy instruments, the monetary policy rate in particular, implying the preservation of stimulative real monetary conditions.

This approach was warranted by the significant divergence between short-term developments in inflation and its longer-term outlook, as highlighted and reconfirmed by the central bank's successive assessments and forecasts. Essential was also the nature of the drivers of the expected inflation pattern, as well as of the associated uncertainties and risks.

Thus, in line with NBR forecasts, the annual inflation rate moved deeper into negative territory in the first months of 2016[6], under the transitory impact of the cut, starting 1 January, in the standard VAT rate[7] and other indirect taxes (according to the new Tax Code[8]), overlapping the same-way effects exerted by the broadening of the scope of the reduced VAT rate to all food items[9] and by the sharper decline in international oil prices. Furthermore, the outlook for the annual inflation rate to remain in negative territory throughout the first half of the year and well below the lower bound of the variation band of the flat target until end-2016 consolidated, given the expected

[3] Law 312 of 2004.

[4] The NBR moved to inflation targeting in August 2005.

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

[6] Annual inflation rate dropped to -3.0 percent in March 2016 from -0.93 percent in December 2015.

[7] From 24 percent to 20 percent.

[8] The new version of the Tax Code adopted by the Parliament of Romania on 3 September 2015 set forth mainly the following: (i) the cut in the standard VAT rate from 24 percent to 20 percent as of 1 January 2016 and to 19 percent as of 1 January 2017; (ii) the removal of the special excise duty on fuels as of 1 January 2017; (iii) the scrapping of the tax on special constructions and the cut in the tax on dividends from 16 percent to 5 percent as of 1 January 2017. The Code was subsequently amended via Government Emergency Ordinance of 27 October 2015, which approved the implementation, as of 1 January 2016, of the following measures: the cut in the tax on dividends, the broadening of the scope of the reduced 9 percent VAT rate to water supply services to households and the reduction of the income tax for micro-enterprises with hired workers.

[9] The VAT rate applicable to these products was lowered from 24 percent to 9 percent starting 1 June 2015.

prevalence, over the short time horizon, of the disinflationary action of supply-side factors.

At the same time, however, the forecasts updated during 2016 H1 reconfirmed the prospects for the annual inflation rate to witness a significant upward correction at the beginning of 2017 – amid the fading out of the transitory impact exerted by the first standard VAT rate cut[10] –, followed by a relatively fast pick-up to values in the upper half of the variation band of the flat target[11]. Underlying these prospects were the rising inflationary pressures anticipated to emerge from the reversal of the cyclical position of the economy in the second half of 2016 and from the subsequent increase of the positive output gap – amid the forecasted economic growth rate remaining above potential –, as well as from the sustained increase in unit wage costs. These had as major premises and assumptions: (i) the recent and expected easing of fiscal and income policy stance[12]; (ii) the rise in the household real disposable income, also following the successive indirect tax cuts and the persistently low oil price, and (iii) the preservation of stimulative real monetary conditions.

The subsequent statistical data and assessments showed a deeper fall of the annual inflation rate into negative territory in the first part of 2016 Q2[13], almost entirely attributable to the stronger direct and indirect effects exerted, via multiple channels[14], by supply-side global disinflationary shocks consisting in large and persistent declines in international commodity prices, particularly of energy and agricultural produce. At the same time, though, there was evidence of a stronger-than-expected acceleration of economic growth in the first two quarters of 2016[15], primarily underpinned by the expansion in private consumption, implying an earlier reversal of the cyclical position of the economy[16] and a swifter build-up of demand-driven inflationary pressures.

Against this backdrop, the quarterly forecasts updated during 2016 H2 showed a lower than previously anticipated trajectory of the forecasted inflation rate over the short term, yet at least as divergent as in the earlier projection rounds. Specifically, the trajectory was seen remaining in negative territory until end-2016[17] and below the lower bound of the variation band of the flat target in 2017 H1, before climbing to the upper half of the band in 2018 and reaching at the end of the projection horizon levels comparable to those anticipated previously.

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[10] The base effect was anticipated to be somewhat counterbalanced by the opposite influences from the new indirect tax cuts scheduled starting 1 January 2017.
[11] In the May forecasting round, the annual inflation rate was seen at 3.3 percent at the end of the projection horizon, i.e. in 2018 Q1.
[12] The minimum gross wage economy-wide was raised by 19 percent in May. Furthermore, pursuant to Government Emergency Ordinance 20/2016 (June), it was decided to increase the wages for some categories of public sector employees in August.
[13] The 12-month inflation rate hit a historical low of -3.46 percent in May.
[14] Including through higher imports of consumer and intermediate goods, leading to a widening of the trade deficit.
[15] Based on real-time data, annual GDP dynamics stood at 4.3 percent in 2016 Q1 and at 6 percent in Q2.
[16] In 2016 Q1.
[17] Coming in at -0.4 percent in December. Recalculated net of the one-off impact of the standard VAT rate cut to 20 percent, the annual inflation rate was forecasted to end 2016 at 1.0 percent.

Beyond the base effects associated with indirect tax cuts, the upward trajectory of the forecasted annual inflation rate reflected the stronger inflationary pressures anticipated to emerge from the widening of the positive output gap over the projection horizon and from the further high unit wage cost dynamics, also amid the gradual labour market tightening. The wider positive output gap was stemming both from the faster-than-expected pick-up in economic growth in 2016 H1 and from the upward revision of the projected GDP dynamics for 2016 H2, as well as for 2017 and 2018. The major stimuli to economic activity were expected to be provided by the recent/planned measures related to fiscal easing and to hikes in wages and other household income, by the accommodative real monetary conditions, as well as by the gradual recovery in the euro area and global economy.

The latter part of the year also saw the considerable heightening of uncertainties and mixed risks associated with the medium-term inflation forecast, the most significant ones stemming from the fiscal and income policy prospects amid the still pending 2017 budget construction[18]. Equally relevant continued to be the uncertainties surrounding global economic growth and euro area recovery, in the context of the slow upturn in the major emerging economies, the lingering issues facing the European banking system, and the outcome of the UK referendum.

Under the circumstances, throughout 2016, the NBR kept the monetary policy rate unchanged at the historical low of 1.75 percent[19]; additionally, the amplitude of the symmetrical corridor of interest rates on standing facilities around the policy rate was preserved at ±1.50 percentage points. Moreover, the central bank further pursued an adequate management of the money market liquidity and maintained the existing level of the minimum reserve requirement ratio on leu-denominated liabilities of credit institutions[20], in a context of the persistent net liquidity surplus in the banking system. Against this background, interbank money market rates continued to fall, hitting new historical lows during 2016, as did average rates on new time deposits and new loans. At the same time however, given the ongoing contraction in annual terms in foreign currency lending, the NBR cut the minimum reserve requirement ratio on forex-denominated liabilities of credit institutions to 10 percent from 12 percent[21], in order to continue the harmonisation of the reserve requirements mechanism with ECB standards and practices in the field.

The central bank’s actions and approach were aimed at bringing, on a lasting basis, the annual inflation rate back into line with the flat target, amid the improvement in the functioning of the monetary policy transmission mechanism and in a manner conducive to sustainable economic growth. Furthermore, the monetary authority continued to use and diversify its specific tools and means of communicating and

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[18] Given, inter alia, the multitude and nature of fiscal measures initiated/announced in the run-up to the elections, referring to tax cuts, pay rises in the budgetary sector, and higher income in the form of social security benefits.
[19] Reached in May 2015.
[20] At 8 percent.
[21] Starting with the 24 October - 23 November 2016 maintenance period.

detailing the rationale behind the adopted decisions, starting to publish, as of 2016, the minutes of the NBR Board monetary policy meetings[22].

The NBR extended the status-quo of the parameters of its main monetary policy instruments during the first months of 2017, given that the annual inflation rate had risen at a slower-than-anticipated pace towards end-2016[23], while its forecasted path was revised downwards over the short term[24] – implying the postponement of its return inside the variation band of the target until 2017 Q4 –, but upwards over the longer time horizon. A major role in reassessing the inflation path played the slight change in the dynamics of inflationary pressures anticipated to be exerted over the projection horizon by the positive output gap, unit wage costs, and import prices. The new inflation outlook was surrounded by heightened uncertainties and risks, stemming from both domestic and external environment.

Looking ahead, the NBR will further gear monetary policy towards bringing, and maintaining in the medium run, the annual inflation rate into line with the flat target, in a manner supportive of sustainable economic growth. Both in the short run and over the longer term, the calibration of the parameters of monetary policy instruments, including the NBR's key interest rate, in the context of ensuring adequate real monetary conditions, will be correlated mainly with the intensity of inflationary pressures coming in the future from the positive output gap, as well as with the behaviour of medium-term inflation expectations and the related risks. Important also remain the characteristics of the monetary policy transmission mechanism, especially of lending to the private sector and of the saving behaviour.

An essential part in substantiating the decisions will further play the uncertainties and configuration of the balance of risks associated with the medium-term inflation forecast, including the probability of their materialising. From the perspective of the NBR's latest medium-term forecast[25], especially relevant are the uncertainties and risks stemming from: (i) the fiscal and income policy stance, given the possible deviation of the budget execution from the coordinates of the 2017 budget; (ii) possible additional consumption stimulus to the detriment of planned public investment, likely to affect the growth potential and competitiveness of the Romanian economy; (iii) euro area economic developments amid the elections scheduled for 2017 and the Brexit talks; (iv) the consequences of the divergent monetary policy stances of the world's major central banks on the local financial market, also in the context of the regional economic and financial environment both in the current period and in the period ahead. Equally important in terms of monetary policy conduct and implementation remain the characteristics of structural reforms and EU funds

[22] Starting with the monetary policy meeting of September 2016.

[23] Reaching -0.54 percent in December 2016.

[24] Largely under the impact of the two new unanticipated supply-side shocks occurring November 2016 through February 2017, namely the cut in the prices of compulsory motor third-party liability insurance policies and the removal of non-tax fees and charges.

[25] According to which annual inflation rate is seen climbing into the upper half of the variation band of the flat target at the beginning of next year and nearing the upper bound of the band in December 2018.

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 and lasting economic growth.

1.4. STRUCTURAL POLICIES

In the Government Program for 2017-2020 the Government proposes to promote smart, sustainable and inclusive economic growth, based on changing the industrial model focused on intensive use of poorly qualified workforce in industries with low processing degree, with a model based on high technological intensity industries. At the same time, the Government is considering to apply public policies which would make more dynamic and flexible the labor market, so as to improve the population's access to quality jobs, according to their skills and competences, to decent income and without discrimination.

Measures have been implemented to facilitate the employment of people with difficulties related to insertion on the labor market. The Government has adopted measures to increase the mobility of the workforce by giving three categories of premiums (non-taxable subsidies) for the people who get a job in a different locality than their domicile. Another measure refers to stimulating the resumption of activity by the unemployed who do not receive unemployment benefits, by giving them a premium of activity conditioned on getting full-time employment for at least three months. Also, employers are stimulated (by being granted increased subsidies) to employ on a full-time basis and for undetermined periods of time the graduates of educational institutions, people with disabilities, unemployed over 45 years of age or long-term unemployed, unemployed who are single parents that support single parent families, etc. Certain measures were taken in order to reduce unemployment among the youth, which refer both to supporting young graduates (by ensuring an income during the apprenticeship period, or a salary of Lei 2500 for graduates who obtained the bachelor's degree), and employers, by granting subsidies thereto (50% of the salary expenses).

At the same time, the Government seeks to create an environment favorable to investments through a process of elimination of bureaucracy and simplification of administrative procedures. Also in 2016 were started several programs of support of the activity of small and medium enterprises, which refer to ensuring guarantees for the facilitation of financing, supporting start-ups incorporated by young entrepreneurs, financing investments for micro-industrialization and supporting the incorporation and development of SMEs in the rural area. In addition, in 2017 started the program Romanian Start-up Nation, with a total value of two billion Lei (which provides non-reimbursable financing of Lei 200,000 with no need for co-financing), as well as other programs meant to stimulate individual or young entrepreneurial initiative. Also, in order to stimulate exports, for the period of 2017-2020 was established a program dedicated to the companies which have the capacity and want to export. On the other hand, the processes of restructuring or privatization are continued for a series of State-owned companies.

2. ECONOMIC PERSPECTIVES

2.1. GLOBAL ECONOMY/TECHNICAL ASSUMPTIONS

The winter forecasts of the European Commission estimate an acceleration of economic growth at global level by 3.4% in 2017 and by 3.6% in 2018, estimates similar to those of the International Monetary Fund. According to the IMF, advanced countries are expected to record an average increase of 1.9% in 2017 and, respectively, 2% in 2018, while developing countries will have an average economic growth of 4.5% in 2017 and 4.8% in 2018. China's economic growth was revised to 6.5% for 2017, 0.3 p.p. over the estimate from October 2016, based on the expectations related to the continued implementation of growth policies. Nevertheless, the risk of China's economic growth slowing continues to be relatively high, given that growth is based to a large extent on the State's incentives, corroborated with the expansion of crediting and slow progress in reducing companies' debts. Thus, for 2018 it is estimated that China's economic growth rate will drop to 6%.

Global growth is threatened by risks related to the reduction of consensus regarding the benefits of globalization, corroborated with a possible strengthening of protectionist measures, determined by the deepening of the global imbalances and the exchange rates fluctuations.

In 2016, the EU economy faced significant challenges (terrorist attacks and geo-political tension, migration flows, Brexit, risks associated with the banking system, etc.) and, in spite of all this, it registered a 1.9% growth rate. This growth was supported to the largest extent by consumption, while investments did not evolve as expected. The real GDP growth rate of the EU is forecasted to decrease to 1.8% both in 2017 and in 2018.

With regard to the Euro area, it is also estimated a decrease of the economic activity by 0.1 percentage points in 2017 (1.6%) compared to the level of 2016, when it was of 1.7%. For year 2017 a slight economic growth is foreseen, the real GDP being forecasted to increase by 1.8%.

Compared to the fall forecast, the European Commission estimates with regard to economic growth for 2017 were revised in an ascending direction both for the EU as a whole (0.2 percentage points) and for the Euro area (0.1 percentage points). For year 2018, the EU's economic growth remained at the level forecasted in the fall of 2016 but, for the Euro area, the estimate of economic growth was increased by 0.1 percentage points.

With regard to the global economic growth (excluding the EU), the forecast of the European Commission shows an improvement of the economic perspectives for the years 2017 and 2018, estimating annual growth rates of the real GDP of 3.7% and 3.9%, respectively, an increase of 3.2% in 2016.

The economic evolution of Germany, Romania's main commercial partner and the main driver of the EU's economy, was positive for year 2016, with an economic growth of 1.9%, higher by 0.2 percentage points above that of 2015. For year 2017 it is foreseen a slowing of the economic activity by 0.3 percentage points compared to 2016 (1.6%) and in 2018 the economic growth will reach 1.8%. Also, for Italy, the second commercial partner of Romania, it is foreseen a maintenance of the dynamics of the GDP in year 2017 at the same level as that of 2016, respectively of 0.9%, followed by a slight acceleration in 2018 up to 1.1%. With regard to France, after a slight deceleration of economic growth in 2016 compared to 2015 (1.2% compared to 1.3%), higher growth rates are estimated for years 2017 and 2018, of 1.4% and 1.7%, respectively.

The forecast of Brent oil prices was revised in an ascending direction, from 44.8 $/barrel in 2016, to 56.4 $/barrel in 2017. For year 2018, it is estimated a slight increase of the Brent oil price, to 56.9$/barrel.

Considering the evolution of world economy in the following period, in Romania, for the time interval 2017-2018 are estimated average annual growths of exports of goods by 7.6% and of imports by 8.5%. After the FOB-CIF trade deficit registered a share of 5.9% in GDP, in 2016, afterwards it will follow an ascending trend, reaching the level of 6.3% in 2017 and of 6.4% in 2018.

Table 1 - Evolutions at global level

	2016	2017	2018
Real economic growth, at global level (%)	3.1%	3.4%	3.6%
Real economic growth - EU (%)	1.9%	1.8%	1.8%
Economic growth - Euro area	1.7%	1.6%	1.8%
Inflation rate - EU	0.3%	1.8%	1.7%
Brent oil price ($/barrel)	44.8	56.4	56.9

Source: IMF and the European Commission

2.2.CYCLIC EVOLUTIONS AND CURRENT PERSPECTIVES

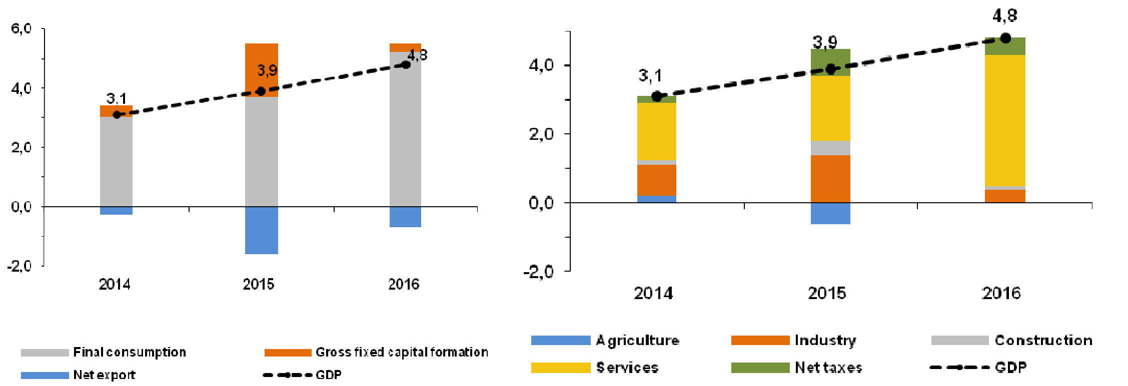
2.2.1. CURRENT PERSPECTIVES

In 2016, Romania registered an economic growth of 4.8%, being the sixth consecutive year of growth (after 1.1% in 2011; 0.6% in 2012; 3.5% in 2013; 3.1% in 2014, and 3.9% in 2015). The growth of 2016 was due to the positive contribution of domestic demand for consumption, as a result of the measures of fiscal relaxation and of salary increases, which improved the population's purchase power. Under these circumstances, private consumption increased by 7.4% and government consumption by 4.5%, compared to year 2015.

Gross fixed capital formation recorded a decrease in real terms, based on a poor accessing of European funds, as well as of the significant decrease of public investment expenses.

Exports of goods and services increased by 8.3%, while imports of goods and services registered an increase of 9.8%, net external demand having a negative contribution (0.7 percent), mainly because the domestic demand increase could not be entirely covered from domestic production.

Chart 1 - Contributions to real growth of GDP



Source: National Institute of Statistics

In terms of domestic demand, it was noted a significant increase of the gross value added in the services sector by 7.0%. Positive evolutions were recorded in the sectors of industry and constructions as well, where the gross value added increased by 1.8%, while a stagnation was registered for agriculture compared to 2015.

In 2016, compared to 2015, consumer prices decreased for the second consecutive year, both as annual average (-1.55%) and at the end of the year (-0.54%). These price decreases were based on the decrease of the VAT rate from 24% to 20% in the rest of product categories, a measure entered into force on January 1, 2016.

Apart from this measure, other disinflation measures overlapped, which manifested on the domestic market, arising mainly from the administered prices for energy products. In their case, additional price decreases were registered compared to those due to the decrease of the VAT rate in January, being more accentuated by the change of market conditions, through the suspension of the liberalization framework of natural gas prices and the continued process of liberalization of electricity prices, which was materialized through a decreasing price for household consumption. These influences were added in the case of electricity to the decrease of the contribution for co-generation and of transmission tariffs. At the same time, more modest monthly evolutions were registered for the increase of prices of food products, based on an offer surplus on this segment of products in the Community area.

In March 2017, annual inflation was of 0.18%, based on the price increase for food products by 1.67%. Compared to December 2016, consumer prices registered in March a decrease of 0.20% caused by the decrease by 1.8% of services tariffs. The important decrease of services tariffs was based on the decrease by 16.80% of prices for radio and TV subscriptions.

In 2016, employment decreased by 0.9% on the basis of the data from the National Accounts. The number of employees in the economy increased by 1.9%, representing 75% of the employment. The increase was mainly due to the evolution from agriculture and constructions, where the number of employees increased by 10.7% and 6.3%, respectively. The unemployment rate, according to AMIGO, decreased from 6.8% in 2015 to 5.9% in 2016.

2.2.2. CYCLICAL EVOLUTIONS

In 2017-2020, the potential gross domestic product will increase at an annual average pace of 5.0%. These estimates were made on the basis of the common EC methodology agreed by all 28 Member States. The forecasted potential GDP evolution is the result of positive contributions of all production factors, the most important being that of the total factor productivity , followed by the significant contribution of capital stock.

The labor factor (expressed through the total number of worked hours) passes to a positive contribution to potential growth as of 2016, which is considerably improved on medium term. This evolution is determined on the one hand by the measures from the Government Program, whose objective is to stimulate investments and job creation, and on the other hand on the structural improvements on the labor market: increasing the employment rate and the number of employees; increasing the share of employed labor to the detriment of other categories of working population; reducing unemployment. After a decrease of 1.0% in 2016, the employed population will increase by 1.6% in 2017 and reach an increase of 0.6% in 2020, in a context of negative demographic evolutions.

After a stagnation in 2015 at 6.8%, the unemployment rate (according to the ILO definition) followed a descending trend as of 2016, when it decreased to 5.9%. The unemployment rate continues to decrease in the horizon of year 2020, reaching 5.3%. It must be mentioned that the unemployment rate has got close to the NAWRU value, calculated under comparable conditions in all Member States of the EU.

Also, the total number of hours worked has a positive evolution, in accordance with the increase of the number of jobs generated by the economy's development, but provided labor productivity is maintained. On medium term, the dynamics of the number of hours worked relative to the employed population decreases from 0.2% in 2016 to 0% in 2019 and 2020.

Table 2 - Evolution of unemployment and hours worked - % -

	2014	2015	2016	2017	2018	2019	2020
Unemployment rate	6.8	6.8	5.9	5.7	5.5	5.4	5.3
NAWRU	6.9	6.6	6.2	5.8	5.5	5.4	5.4
Total hours worked	0.0	-0.4	-0.7	0.8	1.0	1.0	1.0

Source: NIS, NCP

Total factor productivity (TFP), whose trend is calculated in accordance with the degree of use of production capacities from the manufacturing and services, has the biggest contribution to potential growth. The evolution in recent years of the degree of use of production capacities is the following:

Table 3 - Evolution of the degree of use of the production capacity -%-

	2015T2	2015T3	2015T4	2016T1	2016T2	2016T3	2016T4	2017T1
Manufacturing	75.7	76.5	77.5	78.9	78.6	77.5	76.9	77.9
Services	86.0	85.2	87.7	90.9	86.9	92.5	88.6	91.0

Source: DGECFIN

Output-gap, the difference between the GDP and the potential GDP levels, expressed as percentage of the potential GDP, shall be closed in 2017.

Table 4 - Contribution of the factors to potential GDP's growth

		Contributions -%-			
	Potential GDP	**Capital**	**Labor**	**TFP**	**Output Gap**
2015	3.3	1.1	-0.5	2.7	-1.6
2016	3.9	0.8	0.0	3.1	-0.8
2017	4.5	1.0	0.2	3.3	-0.1
2018	5.0	1.2	0.3	3.4	0.4
2019	5.3	1.4	0.3	3.6	0.7
2020	5.4	1.6	0.2	3.6	1.0

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

Source: National Commission of Prognosis

The average annual rhythm of growth of the potential GDP estimated by the European Commission is of 3.8% for the interval 2017-2018. For the same period, the annual growth rhythm in the national estimates is of 4.8%. This discrepancy of 1 percentage point comes mainly from two sources, namely bigger dynamics of the gross fixed capital formation in the case of the national forecast and a forecast horizon of 2 years in the case of DGECFIN (2018) compared to one of 4 years in the case of the Member States (2020).

2.3. MEDIUM TERM SCENARIO

The macroeconomic framework for the Convergence Program considered: (i) the positive impact of the measures provided by the Government Program on the business environment and on the population's purchasing power, (ii) the uncertainties related to the European and global framework mentioned in the winter forecast of the European Commission, which create less favorable conditions for the acceleration of development; (iii) the positive impact of the low oil price for the Romanian economy; (iv) the economic and social achievements of 2016.

For 2017 it was estimated an economic growth of 5.2%, based exclusively on domestic demand. Within this growth it was estimated that investments (gross fixed capital formation) will increase by 6.9% after the decrease registered in 2016, and final consumption by 6.3%.

Table 5 - GDP components

	2016	2017	2018	2019	2020
Real GDP	4.8	5.2	5.5	5.7	5.7
Final consumption	6.9	6.3	5.8	5.6	5.4
- Private consumption expenditures	7.4	7.3	6.4	6.2	6.0
- Public consumption expenditures	4.5	1.8	2.8	2.7	2.8
Gross fixed capital formation	-3.3	6.9	7.9	8.4	8.6
Export of goods and services	8.3	6.8	6.3	6.9	7.0
Import of goods and services	9.8	8.5	7.9	8.1	8.0

Source: National Commission of Prognosis

For 2018-2020 it is estimated that Romanian economy will increase at a more sustained pace, with an average annual pace of 5.6%. Domestic demand (consumption and investments) will continue to represent the engine of economic growth.

Private consumption expenditure will increase on average by 6.2% yearly. Gross fixed capital formation will accelerate on the basis of improvement of financing in the economy, at an average annual pace of 8.3%.

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 employment will gradually increase until 2020, the structure changing in favor of the employees whose share is estimated to be close to 79% in 2020 compared to 75% in 2016. The unemployment rate, according to AMIGO, will gradually decrease, from 5.9% in 2016 to 5.3% in 2020.

For 2017 it is expected that consumer prices register an increase of 1.9% compared to December 2016, and as annual average they will increase by 1.1%. As of 2018, inflation will remain relatively constant, being as annual average between 2.2% and 2.5%. The continuance of maintenance of inflation at a low level will be sustained by keeping the firm conduct of monetary policy, in order to ensure price stability on medium term. The forecasts took into account the normal agricultural years and a moderate increase for the international price of oil.

2.4. BALANCE OF THE EXTERNAL SECTOR

In 2016, the increase of goods exports was of 5.1% compared to 2015, while imports increased by 7.0%. Under these circumstances, the FOB-CIF trade deficit increased by 19.0% compared to that registered in 2015.

In the first two months of 2017, Romania's exports increased by 9.2%, while imports registered an increase of 10.9% compared to the corresponding period of 2016. Thus, the FOB-CIF trade balance closed at the end of February 2017 with a deficit of 1.3 billion EUR, 27.0% bigger than the one from the comparison period of the previous year.

It is estimated that export will remain in 2017 a component of demand which supports Romania's economic growth. Thus, for year 2017 it is estimated an increase of goods export by 7.7% and for the import of goods by 8.9%. On the whole, the forecast for 2017 shows that trade deficit will have a share in the GDP of 6.4%.

For the interval 2017-2020 are estimated average annual increases of the exports of goods of 7.7% and for imports of 8.3%. The share of FOB-CIF trade deficit in GDP will reach the level of 6.9% in 2020. It is estimated that international trade with the Member States of the EU will intensify, so that the share of exports of goods towards the EU will increase from 75.1% in 2016 to approximately 78% in 2020, and the share of imports of goods from 77.1% in 2016 to 77.2% in 2020.

In 2016, the current account of the payment balance registered a deficit two times bigger than the one of 2015, reaching a share in GDP of 2.3%. The financing of the current account deficit was made entirely through foreign direct investments, which reached the value of EUR 4.1 billion and were bigger by 19.4% compared to 2015.

Table 6 – The balance of the external sector

% of GDP	2016	2017	2018	2019	2020
1. Net balance, compared to the rest of the world	0.2	0.4	0.8	0.9	0.9
Of which:					
- the balance of goods and	-0.9	-1.2	-1.4	-1.3	-1.2

services					
- the balance of primary income and secondary income	-1.4	-1.2	-1.0	-0.8	-0.8
- capital account	2.5	2.8	3.2	3.1	2.9

Source: National Commission of Prognosis

In the first two months of 2017, the current account of the payment balance registered a surplus of 204 million EUR compared to a negative balance of 139 million EUR as it had in the similar period of 2016, due to passing the balance of primary income from a negative balance to a positive value.

In 2017, the current account deficit of the external payment balance is expected to reach a value of 4.4 billion EUR, representing 2.4% of GDP. foreign direct investments will cover entirely the current account deficit.

On medium term, the level of the current account deficit will be maintained at a value between 4.4 and 4.5 billion EUR, with a share in GDP of 2.4% in 2017 and 2.0% in 2020. Between 2017 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 positive, with a slightly ascending trend, given a high contribution of the capital account.

3. BALANCE OF THE GENERAL CONSOLIDATED BUDGET AND OF DEBT

3.1. THE FISCAL AND BUDGETARY POLICY

The budget deficit policy continues to directly support economic growth, within the margin allowed by the Stability and Growth Pact, i.e. an ESA budget deficit 3% of GDP.

In the framework of the fiscal relaxation measures started in 2015-2016 in order to stimulate economic growth (the new fiscal code and the salary increases, as well as the increases of rights of the type of social assistance) and continued through the recently adopted measures (the elimination of the social health insurance contributions for the retired, the non-taxation of the pensions below 2000 Lei, the increase of salaries for certain categories of public employees, the increase of the pension point to Lei 1000 as of July 1, 2017, and so on), which produce effects as of 2017, it is estimated that the ESA budget deficit will remain within the limit of 3% of GDP in 2017. It is expected that the budgetary balance relative to GDP should come back on an adjustment trajectory as of 2019.

In structural terms, it is estimated that the significant deviation registered in 2016 from the Medium Term Objective (MTO) set for Romania (namely of 1% of GDP) will be adjusted as of 2019. Nevertheless, on the entire planning horizon, public debt will be maintained at a sustainable level of below 40% of GDP.

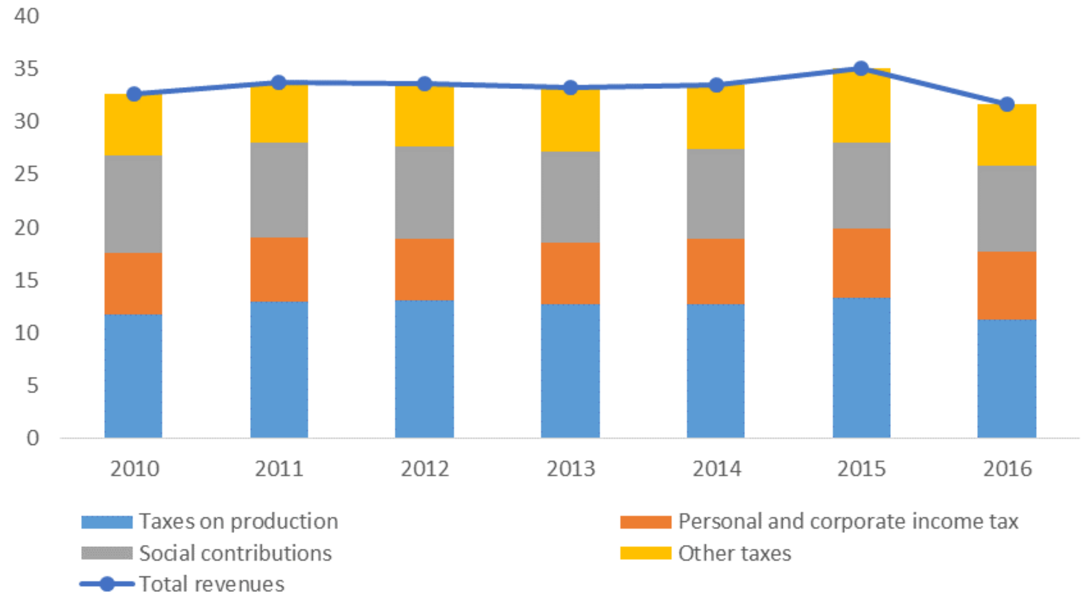
One of the major concerns in the budgetary expenses policy is the optimization of the structure thereof towards an architecture that stimulates sustainable economic development, especially through the reorientation of public investment expenses in order to make a gradual passing from the investments financed entirely from national sources to investments co-financed from EU funds. Also, an important step in this policy is represented by the prioritization of significant public investment projects, in order to improve the absorption of EU funds.

3.2. EVOLUTION OF PUBLIC FINANCE IN 2016-2017

In 2016, the weight of total revenues in GDP in ESA terms was of 31.7%, i.e. 3.3 percentage points smaller compared to the previous year. In structure, the decrease of the weight of revenues is due mainly to the decrease of VAT collections by 9.6% compared to the previous year, when the standard VAT rate decreased as of January 1, 2016 from 24% to 20%.

The collections from corporate income tax increased by 11.7% compared to the previous year, and the collections from excises registered an increase of 3.6% compared to 2015. Both social contributions and the collections from the personal income tax and salary tax increased by 7.6% and 4.2%, respectively, compared to the previous year, representing 8.1% of GDP and 3.6% of GDP, respectively.

Chart 2 - Budget revenues (ESA 2010, %GDP)



Source: Ministry of Public Finance

Also, the weight of total expenses in GDP calculated in accordance with the ESA 2010 methodology was of 34.7%, i.e. 1.1 percentage points smaller compared to the previous year. This decrease is mainly due to the decrease of investment expenses by 1.6 percentage points, given the decrease of the expenses for projects financed from European funds.

Staff expenses increased by 14.9% in ESA terms compared to the previous year, reaching 8.2% of GDP, being mainly caused by the salary increases granted in the second part of 2015 and in 2016. Social assistance expenditures increased compared to the previous year by 0.1 p.p. (11.6% of GDP), increasing in terms of value compared to 2015 by 7.7%, being mainly influenced by the 5% increase of the pension point as of January 1, 2016 and by the doubling of the allowance for children as of June 1, 2015, as well as other measures that were approved in 2016. In exchange, expenses for goods and services decreased by 0.4 percentage points, down to 5.3% of GDP in 2016.

The budget deficit calculated in accordance with the European methodology was on the limit of the reference level of the Stability and Growth Pact, recording a level of 3.0% of GDP in 2016. The deficit increased by 2.3 p.p. compared to the previous year, mainly on the basis of the decrease of budgetary revenues as a result of fiscal relaxation measures, as well as of the salary and social assistance increases.

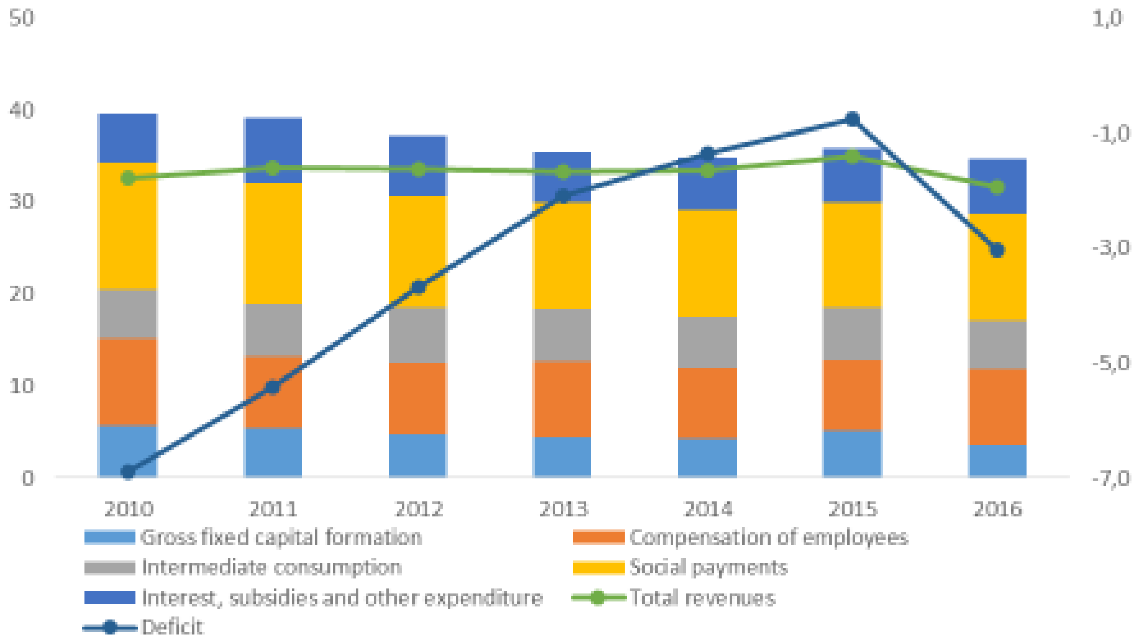
Also, a measure with impact of increase of the ESA deficit only in 2016 is represented by the State's obligation of reimbursing to the teachers their salary rights arising from the enforcement of Law no. 85/2016 on salary payments due to the teaching staff from the State education for the period of October 2008 - May 13, 2011.

At the same time, as of 2016, the National Authority of Return of Properties started implementing the regulations set through Laws no. 165/2013 and no. 164/2014, so that in 2016 it issued decisions for compensation of 2.1 billion Lei.

Considering the judgments rendered by the Court of Justice of the European Union with regard to the special charge for cars and motor vehicles, to the pollution charge for motor vehicles and the charge for pollutant emissions coming from motor vehicles, the Government approved through GEO no. 40/2015 the simplified administrative procedure of return of these charges. This measure had an impact of 0.4 billion Lei in 2016.

Also, State-owned companies reclassified in the public administration sector in accordance with ESA 2010 had a positive influence on the ESA deficit of 2016 of approximately 1.1 billion Lei.

Chart 3 - Consolidated budget position (ESA 2010, %GDP)



Source: Ministry of Public Finance

Table 7 - The main fiscal and budgetary measures taken into account when building the budget of 2017

Measures with impact in 2017	Estimated impact (million Lei)
Expenses	
Increase of salaries in the local administration by 20% as of February 1, 2017	843
Increase of salaries for the artists by 50% as of February 1, 2017	48
Increase of the pension point to Lei 1,000 as of July 1, 2017	2,502
Increase of the minimum pension to Lei 520 as of March 01, 2017	1,200
Free railway transportation for students	75
Increase of student scholarships	285
Revenues	
Main measure of the Fiscal Code:	**-6,118**
Reduction of the standard VAT rate from 20% to 19% as of January 1, 2017	-2,200
Elimination of the construction tax as of January 1, 2017	-1,000
Elimination of the excise of 7 Euro cents and increase of the excise from Lei 430.71/1000 cigarettes in 2016 to Lei 435.58/1000 cigarettes in 2017	-2,886
Additional measures	
Non-taxation of pensions:	
- exemption of pensions below 2000 Lei from the personal income tax	-1,200
- non-taxation with the CASS (health insurance contribution)	-900
Change of taxation of income from transfer of real estate properties from one's personal patrimony (personal income tax for the State and local budgets)	-300
Eliminating the maximum ceiling of 5 average gross salaries for the payment of the CAS (social insurance contribution)	1,100
Change of taxation share of microenterprises to 1% for those with one or several employees, setting the ceiling at EUR 500,000	-400
Distribution of a share of at least 90% of the net profit obtained in the form of dividends/payments to the State budget for national companies and companies with full or majority State-owned capital	800

Source: Ministry of Public Finance

Also, for 2017, by way of derogation from the provisions of art. 43 para. (3) in the Law no. 411/2004 on privately managed pension funds, as republished, as subsequently amended and supplemented, it was established that in 2017 the contribution share to these funds shall be maintained at the level provided for 2016, namely of 5.1%.

The preliminary evolution of the general consolidated budget in the first quarter of year 2017 indicates ca cash surplus of 0.2% of GDP. The total collected revenues increased by 7.1% compared with the first quarter of the previous year, while the total expenses made increased by 10.4%.[26]

Increases were registered compared to the previous year for the collections from the salaries and personal income tax (+15.8%), social contributions (+14.8%), foreign trade and international transactions tax (+18.2%), and capital revenues (+12.7%). The collections from other taxes and charges on goods and services increased by 60.2% compared to the same period of the previous year, the increase being mainly caused by the evolution of the collections that correspond to the contribution owed for

[26] The evolutions of budgetary revenues and expenses in Q1 are presented on the basis of cash data.

medicines, as well as for cost-volume/cost-volume-result agreements financed from the budget of the National Single Fund for Health Insurance.

With regard to VAT collections, they registered a decrease compared to the first three months of year 2016 by 9.1%, based on the decrease as of January 1, 2016 of the standard VAT rate from 24% to 20%, a measure which was reflected into the collections as of February 2016. At the same time, as of February 2017, the effects of the decrease of the standard VAT rate from 20% to 19% are also reflected into the collections. Nevertheless, VAT collections increased in February 2017 by 2.5% compared to February 2016, and by 8.9% in March 2017 compared with March 2016. The collections from excises were 7.4% smaller than during the same period of the previous year, being negatively influenced by the decrease of the level thereof for certain energy products as of January 1, 2017. Also, increases were registered compared to the previous year for taxes and charges on property in the local administrations of 50.1% and at the State budget they increased by 21.2%.

The amounts from the European Union on account of payments made for Q1 of 2017 are of 2.9 billion Lei, of which 2.7 billion Lei represent amounts that correspond to the projects in the field of agriculture.

Staff expenses increased by 16.4% compared to the same period of the previous year, being determined by the salary increased given in 2017, namely the increase by 15% of the salaries in the health and education fields as of January 1, 2017, of the salaries of staff paid from public funds from the public institutions and authorities of the local public administration who benefit of a 20% increase as of February 1, 2017, the increase of the gross minimum wage at national level from Lei 1250 to Lei 1450 as of February 1, 2017.

The expenses for goods and services decreased by 3.1% compared to the same period of the previous year, the decreases being registered at the State budget and the local administrations. Interests are 11.7% bigger compared to the same period of the previous year, remaining at the same level as percentage of the Gross Domestic Product, namely of 0.3%. Social assistance expenses increased compared to the previous year by 9.7%, being mainly influenced by the 5.25% increase of the pension point as of January 1, 2017, which reached Lei 917.5, as well as by other measures which were approved in 2016 and contributed to increasing social expenses.

Considering the monthly evolutions presented above and in order to ensure the observance of the approved annual budgetary provisions, the Government will implement the following measures:

Measures related to the increase of budget revenues

- Introduction as of June 1, 2017 of the payment obligation of the contributions owed by the employers at the level of the minimum gross salary guaranteed at national level for part-time employees with a salary or income under Lei 1450 who do not have paid full-time employment at the same time (an estimated impact of Lei 620 million in 2017 and Lei 1,330 million in 2018).

- The increase as of June 1, 2017 of the level of the excise for cigarettes by 1%, namely from Lei 435.58/1000 cigarettes to Lei 439.94/1000 cigarettes (estimated impact of 90 million Lei in 2017).
- The amendment of the provisions of the GEO no. 190/2000 on the regime of precious metals and precious stones in Romania - by applying the own guarantee mark exclusively by the ANPC, not by domestic producers, importers or retail sellers, in order to simplify and increase the efficiency of the control acts, as well as to guarantee the quality of the products traded to consumers (estimated impact of Lei 110 million in 2017).
- Continuance in 2018 of the distribution of a share of at least 90% of the net profit realized under the form of dividends/payments to the State budget, on occasion of approval of the financial statements of that year for the national companies, and fully or majority State-owned companies, as well as autonomous administrations, by mandating the State representatives in the General Meetings of Shareholders/Board of Directors, as applicable (estimated impact of Lei 870 million in 2018).
- The implementation as of July 1, 2017 of a mechanism of payments in installments of VAT, consisting of the payment by the public institutions and enterprises of the value-added tax that corresponds to the procurement of goods and services made directly from the account of the supplier/provider to the State budget (estimated impact of 180 million Lei in 2017 and 420 million Lei in 2018).

Measures of reduction of public expenses and structural reforms for making expenses more efficient (estimated impact of 1 billion Lei in 2017 and 3 billion Lei in 2018).

- The incorporation by June 1, 2018 of a directorate in the General Secretariat of the Government which will seek to decrease the number of agencies and institutions subordinated to the Government.
- Elaboration of a Plan of rationalization of public expenses by July 1 of this year, with the following pillars: audit of governmental functions, accelerated computerization of the central and local administration, prioritization and acceleration of public investments, revision of the subsidies awarded to companies from the State budget. The subsidies from the budget to public companies will be conditioned on the improvement of financial performance, performance agreements will be introduced in all public institutions and State companies.
- Creation of the National public administration employment records - ANFP will collect directly the data necessary to populate the system from the public institutions and authorities.
- Improving corporate governance in State-owned companies: reform of the private management in State-owned companies from the strategic fields with standard agreements, performance criteria and payment according to performance.
- Reducing the operating expenses of the public institutions and authorities by 5-10%.

- Reducing by at least 35% the price of innovative medicines which lost their patent.
- The procurement made by the central authorities with regard to goods and services will be made in a centralized manner, by a central procurement unit. In this manner, the expenses for goods and services will be reduced by approximately 10 to 15% as soon as this unit becomes operational.
- Keeping special pensions at the level set at present.
- In order to efficiently use the budget resources allocated for social benefits, it would be opportune to set a ceiling for the child-raising allowance (CRA) at a maximum level comprised between Lei 5,000 and 10,000, as well as the introduction of the social benefits card.

3.3. MEDIUM TERM EVOLUTION OF PUBLIC FINANCE

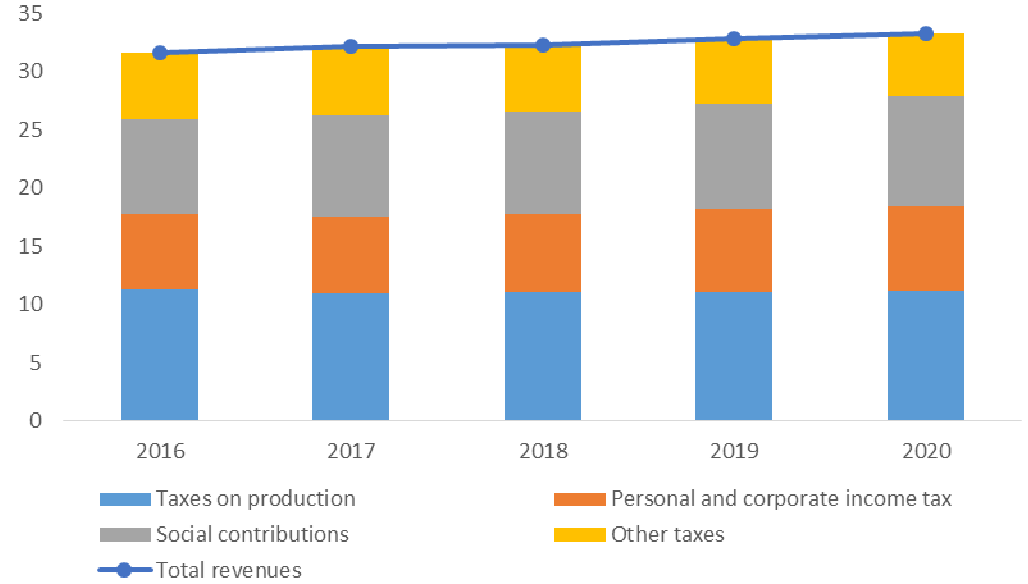
For 2018-2020, the budget estimates were built on the basis of the provisions of the Fiscal and budgetary strategy for 2017-2019 and on the additional measures that are to be implemented in 2017, under constant conditions in terms of fiscal policies.

For 2017 it is forecasted an increase of budget revenues calculated in accordance with the ESA methodology by 0.5 percentage points (32.2% of GDP), mainly due to the forecasted improvement of the absorption of European funds and of the positive trend for collections from social contribution revenues. This trend shall be maintained on an ascending direction on medium term, total revenues reaching a level of 33.3% of GDP in 2020. In structure, the revenues from current corporate income and personal income taxes will increase from 6.6% of GDP in 2017 to 7.1% in 2020, under the conditions of maintenance of a super-unitary elasticity of the collections from the corporate income tax. It is estimated that the revenues from taxes on production and import will decrease by 0.3 percentage points to 11.0% of GDP in 2017, as a result of the elimination of the over-excise for fuels and of the reduction of the standard VAT rate. On medium term, the collections from these taxes will be maintained as share of GDP (11.1% in 2020).

At the same time, the dynamics of the salary fund in the economy and the measures of extension of the taxation base of social contributions will lead to an increase of revenues from this source to 8.7% of GDP in 2017 and 9.4% by 2020.

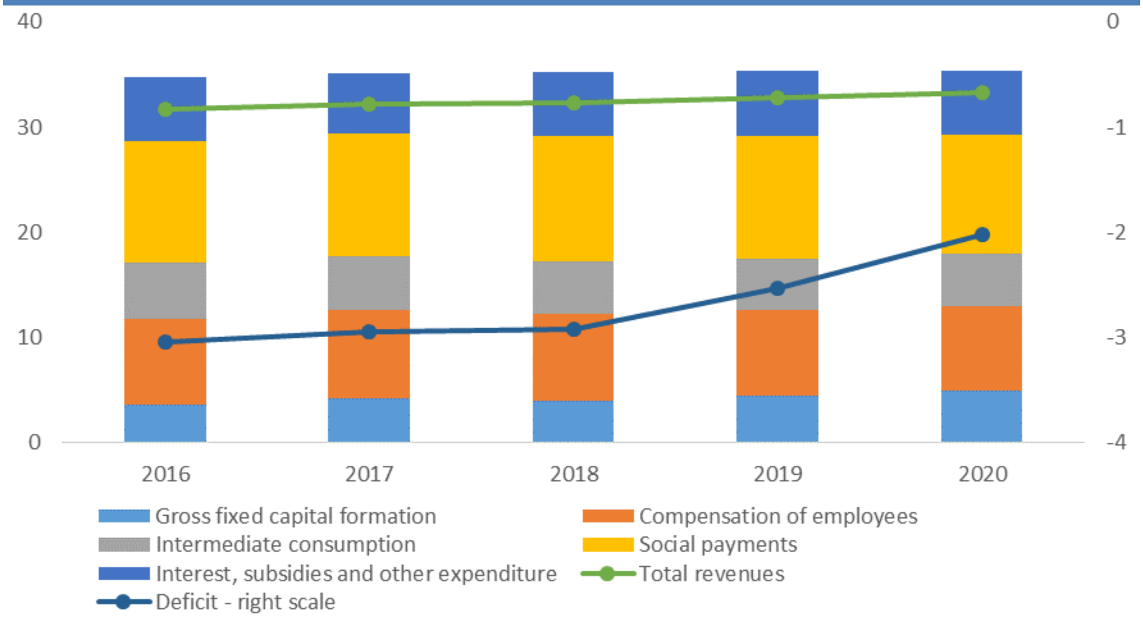
The total budget expenses are forecasted to increase in 2017, reaching 35.1% of GDP, and on medium term it is estimated a slight increase by 2020 (35.3% of GDP). Salary expenses will increase in 2017 by 0.2 percentage points compared to 2017, and in 2018-2020 a sufficient fiscal space will be maintained for the implementation of the provisions of the unitary salaries law in the budgetary sector. The expenses for interim consumption (goods and services) and social assistance will slightly decrease by 0.1 percentage points and 0.3 percentage points, respectively, in 2017-2020, while interest and subsidies expenses will remain relatively constant. Also, the gross fixed capital formation indicates the maintenance of an adequate allocation for medium-term investment expenses (from 4.3% of GDP in 2017 to 5.0% in 2020), which can ensure the improvement of the absorption of European funds compared to the previous financial year.

Chart 4 - Consolidated budget revenues (ESA 2010, %GDP)



Source: Ministry of Public Finance

Chart 5 - Consolidated budget position (ESA 2010, %GDP)



Source: Ministry of Public Finance

The estimates of the budget deficit for 2017 do not exceed the limit of 3% of GDP, and in 2018 it will remain constant, while as of 2019 it is estimated an adjustment trajectory thereof by approximately 1 p.p. by 2020. In structural terms, the deviation from the medium-term budgetary objective (MTO) will increase in 2017-2018 and as of 2019 it will enter an adjustment trajectory.

Table 8 - General consolidated budget balance (% of GDP)				
	2017 Estimates	2018 Estimates	2019 Estimates	2020 Estimates
ESA methodology balance	-2.9	-2.9	-2.5	-2.0
Structural balance	-2.9	-3.0	-2.8	-2.3

Source: Ministry of Public Finance

With regard to fiscal policy, for 2018 it is considered the amendment of the current taxation system of income obtained by private individuals, by waiving the current taxation rate of 16% and introducing a new differentiated tax of 0% or 10%, according to the global annual income per every household in Romania. The proposed system is considering passing from individual taxation of the income obtained by private individuals to the global taxation of the income obtained in one fiscal year in a household made up of the members who administer together a common patrimony. The global taxable income will consider a non-taxable ceiling and the extension of the current system of deductions. Also, families with children that register income below a certain ceiling will benefit of annual financial support for every child they support.

In the field of mandatory social contributions, the proposals refer to changing the tax burden of the obligations related to mandatory social contributions owed by the employee and the employer, by the employee taking over all contributions. Thus, the employer's burden will no longer include mandatory social contributions, and the employee will continue to pay social insurance contributions (CAS) and health insurance contribution (CASS). Also, the manner of establishment of the CAS and CASS in the case of private individuals who carry out independent activities will be revised.

Given that the parameters of these changes are not completed, the assessment of these measures is not included in the fiscal projections presented by this program. Nevertheless, it is expected that these proposals, corroborated with other measures contained in the Government program, will lead to a neutral impact in budgetary terms.

The draft Framework Law on salaries of the staff paid from public funds

As of January 1, 2011 entered into force the Framework law no. 284/2010 on unitary salaries for the staff paid from public funds, a law which sought to reform and simplify the salary system of public employees. In practice, this law was not entirely applied in 2011-2016 and through annual salary laws the salary rights of public employees were either maintained or punctual raises were given only for certain categories of staff. Also, through different legislative acts were approved salary increases for all the employees from certain public institutions, irrespective of the employment class they were part of, which exceeds the unitary nature of the salary system of public employees.

Thus, the current public salary system is facing a series of malfunctions and salary inequalities, like:

- different salary levels for people who hold the same position and have the same duties within the same institution or within institutions of the same kind from one sector;
- equal salaries for people who hold the same position and have the same duties, but with different seniority;
- smaller or equal salaries for people employed on positions which require higher education, compared to the people employed on positions requiring secondary education;
- small salaries which exist on the basis of the salary pyramid;
- unsatisfactory salaries for the medical staff, for the educational staff, cultural and military staff.

Considering the aforementioned aspects, it was necessary to elaborate a new legislative act, a more simplified and accessible one, which proposes:

- the ratio between the minimum basic salary and the maximum basic salary in the budgetary sector should be of 1 to 12, hierarchy of positions based on general criteria like: knowledge and experience, complexity, creativity and diversity of activities, judgment and impact of decisions, responsibility, coordination and supervision, social dialogue and communication, work conditions, incompatibilities and special regimes;
- the basic salaries from the appendices to the law are established in absolute amounts, which represent the salary level that corresponds to year 2022, when the salary grid will be applicable entirely, and as of 2023 the basic salaries will be determined in accordance with hierarchy coefficients of the positions from the budgetary system and the level of the minimum gross salary guaranteed at national level. thus, salary overlapping caused by the increase of the minimum basic salary guaranteed at national level will be eliminated, as well as the different levels of salaries for the same positions, and the equalization of salaries for people with different seniority;
- setting of the salaries on the basis of a single legislative act, thus eliminating the current provisions from different legislative acts which set salaries for certain staff categories;
- the ratio between the variable part (bonuses, indemnities, compensation) and the basic salary will be of 30% per total spending authority;
- the salary system of public employees will be based on the following principles:
    - the principle of legality, namely salary rights shall be set only through legal norms with power of law;
    - the principle of nondiscrimination, which states that any form of discrimination will be eliminated and equal treatment will be established for the public employees who carry out the same activity and have the same seniority on the labor market and on the job;
    - the principle of equality, by ensuring equal basic salaries for work of equal value;

- the principle of social importance of the work, meaning that the salaries of staff from the public sector are set relative to their responsibility, the complexity, the risks of the activity and the levels of studies thereof;
- the principle of stimulating public employees, in the framework of recognizing and rewarding their professional performance, based on the criteria set under the law and on own regulations;
- the principle of hierarchy, on the vertical axis as well as on the horizontal axis, within the same field, according to the complexity and importance of the activity performed;
- the principle of transparency of the mechanism of establishment of salary rights, within the meaning of ensuring salary predictability for public employees;
- the principle of financial sustainability, within the meaning of setting the salary level for the public employees so as to ensure the observance of the ceilings of staff expenses of the general consolidated budget established under the law (instead of the Framework law no. 284/2010).

Improving the collection of taxes and charges

ANAF's strategic objectives for 2018-2020 presuppose priority actions on the following directions: increasing the degree of voluntary compliance for payment, fighting tax evasion and reducing underground economy, as well as increasing collection efficiency.

In order to improve voluntary compliance, it is targeted the extension of the "Virtual Private Space" service to include legal entities and other entities without legal personality (SPV), which will determine the increase of communication efficiency, by ensuring real time communication of the documents issued by the administrative structures, guiding the taxpayers and tax audits. At the same time, the implementation of a unified system for management of waiting lines at tax administrations is a priority actions. In addition, it is promoted the payment of tax liabilities through the new payment modalities implemented by ANAF: payment by bank card at the POS installed in the territorial units of the State Treasury or using the facilities offered by the platform *ghiseul.ro.*

Apart from improving voluntary compliance, the priority actions of ANAF refer to increasing collection efficiency through the development of a complex professional training program dedicated to all the employees of the institution and the implementation of the "Revenue Administration Modernization Project" (RAMP), which presupposes the development of the management function, re-engineering and IT development and the development of taxpayer services.

With regard to fighting tax evasion and reducing underground economy, actions like the following are continued: the development of the risk analysis for tax audits and fighting VAT related tax fraud, introducing the random testing program of compliance, fighting customs fraud, etc.

3.4. EVOLUTIONS AND LEVEL OF GOVERNMENT DEBT[27]

GOVERNMENT DEBT AND GOVERNMENT PUBLIC DEBT MANAGEMENT STRATEGY

The government debt in accordance with the EU methodology was at 37.6% of GDP at the end of 2016, clearly inferior to the ceiling of 60% set through the Maastricht Treaty. At the end of February 2017, the government debt was of 37.5% of GDP, of which domestic debt was of 19.6% of GDP and foreign debt was of 17.9% of GDP.

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

- Cover the central government's funding needs and the payment obligations, while minimizing the cost on medium and long term;
- Limit the financial risks associated with the government public debt portfolio, and
- Develop the domestic market of government securities.

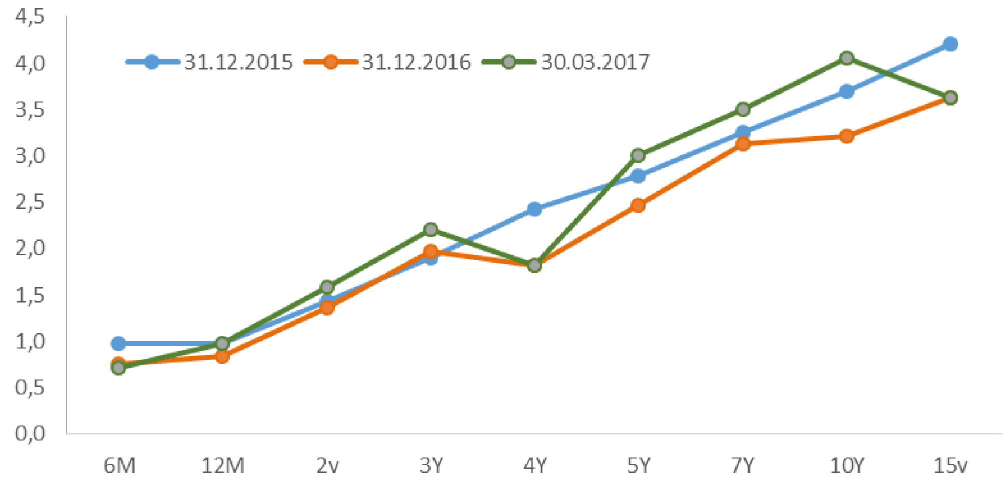
In 2016, the budget deficit and the refinancing of government public debt was financed mainly from domestic sources and in addition for external sources .

The yields of government securities followed a downward trend in the first three quarters of 2016, and then the increase thereof was marked mainly by a series of external events, like the results of the elections in the USA and the expectations of the investment environment that the Federal Reserve of the USA will raise the reference interest rate, which were materialized through the increase of the interest rate by 25 bps by the FED in December meeting.

The vote in Great Britain to exit the European Union in June 2016 did not `have a negative impact on the yields of government securities; on the contrary, they registered decreases, Romania being the only country in the region with the most pronounced decreases thereof. Even though the USA elections generated a series of increases of the yields as of November, they are below the level registered at the end of 2015, especially on maturities bigger than 3 years.

[27] All the indicators used in this chapter are compliant with the EU methodology.

Chart 6 – Yields of government securities on the primary market



Source: Ministry of Public Finance

In 2017, the budget deficit and the refinancing of government public debt will be financed mainly from domestic sources and in addition from external sources. The MPF will continue to maintain a flexible approach in performing the financing process, seeking to ensure the predictable and transparent nature of the offer of government securities, especially in order to be able to react promptly and adequately to the possible changes in market tendencies and the investors' behavior.

The financing strategy from domestic sources is mainly considering issuances of government securities denominated in lei, respectively T-bills with short-term maturities and benchmark bonds with medium and long-term maturities, according to the demand existing on the market and considering the objective of consolidation of the yield curve in lei. On the domestic market, in order to increase the liquidity of the secondary market, the MoPF intends to continue the policy of building a series of liquid benchmark bonds on the entire yield curve, at the same time as a transparent policy of issuance of government securities, until it reaches volumes per security with an equivalent value of up to 2 billion EUR, with prior information of the market with respect to the volumes, frequency of launching/reopening of certain categories of maturities. The issuances of government securities denominated in EUR on the domestic market can be made in the framework of an important demand for such instruments coming from the local investors, in the absence of alternative instruments, this creating the assumptions for an advantageous maturity/cost ratio.

Also, according to the completion of the procedural and operational framework related to the operations on the secondary market at the level of the NBR[28] it is considered the use of operations of the type of anticipated redemptions or exchanges of State securities in order to facilitate the process of refinancing of the series with large accumulated volumes, which become due and accelerating the process of

[28] The auctions that correspond to buy back operations and bond exchange operations shall be made by using the electronic platform developed by the NBR for the auctions that correspond to the primary market.

creation of series of State securities of liquid benchmark type. In a similar manner, it is intended to use reverse repo operations for an efficient management of liquidities, on the basis of prior consultation with the NBR, in order to coordinate the policies of financing and managing liquidities with monetary policies.

In order to increase the accessibility of the government securities among small investors and increase the degree of financial education thereof, it is also considered the continuance of the retail bond issuance Programme FIDELIS, through the issuance of retail bonds for theindividuals, according to the potential interest of the targeted investor category.

With regard to *external financing sources*, the MPF intends to maintain its presence on the international capital markets, mainly through issuances of bonds denominated in EUR. The issuances denominated in dollars from the external markets or in other currencies will be launched as financing alternative, under advantageous cost conditions, in the case of external events which might limit access to certain segments of maturity in financing on the European market, considering the advantages offered through the extension of the maturity, the increased capacity of the market of absorption of new issuances and the diversification of the investor base.

The first issuance on the external markets this year was launched on April 10, being attracted the amount of EUR 1.75 billion through an issuance of Eurobonds in EUR in two installments, of which EUR 1 billion through a new issuance with 10 year maturity, coupon of 2.375% and EUR 0.75 billion through the reopening of the issuance launched in October 2015, with an initial maturity of 20 years and a coupon of 3.875%. These two installments were made at decreasing costs for Romania. Thus, for the 10 year maturity a yield of 2.411% was obtained, the lowest historical level for this maturity, the equivalent of a margin of 170 base points over the mid swap reference quotations, decreasing compared to the similar issuance with 10 year maturity made in October 2015 (with a yield of 2.845% and which was reopened at a yield of 2.55% in February 2016). Also, the reopening of the issuance with maturity on October 29, 2035 attracted the attention of investors, being launched at a yield of 3.55%, which is a decrease compared to the level of 3.93% obtained on the initial launch thereof in October 2015.

The MPF will remain flexible with regard to the moment of accession of the international markets and the volume of external issuances, considering the associated costs, the risk considerations, the possible implications of the central bank’s policy, as well as the evolution of the local market.

At the same time, on medium term, the MPF intends to continue its partnership with the international financial institutions, in order to benefit of the financial advantages that correspond to the products thereof in limiting the costs and extending the maturity of the debt portfolio through the cost and maturity conditions offered, like the IBRD's development policy loans (DPL), as well as those contracted for the purpose of financing budget deficit and refinancing government public debt, the amounts being made available on the basis of the implementation of certain measures and/or other actions necessary in the field of sector reforms.

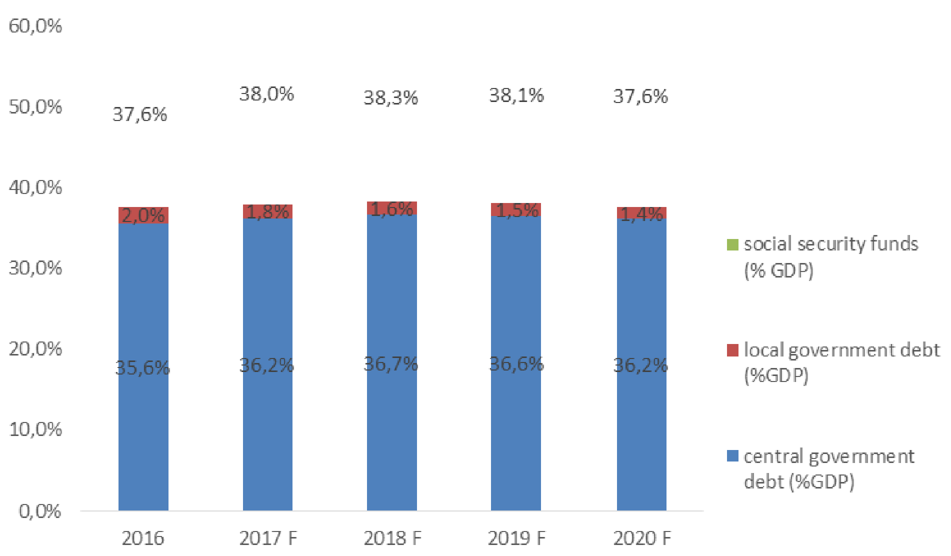
The necessary sources for refinancing the government public debt will be ensured from the markets where these debts were issued, as well as from the financial reserve in foreign currency at the State Treasury disposal . In order to improve public debt management and avoid seasonal pressure in ensuring the financing sources for the budget deficit and refinancing government public debt, it is considered to maintain the financial reserve (buffer) in foreign currency at the State Treasury disposal at a comfortable level, so as to reduce the risks that correspond to the periods characterized by high volatility of the financial markets. On medium term, the level of this buffer will continue to be consolidated so as to cover 4 months of gross financing needs.

In order to use the derivative financial instruments (currency swap and interest rate swap), for the creation of the legal, procedural and technical framework, the Ministry of Public Finance, acting through the General Directorate of Treasury and Public Debt, benefits of technical assistance from the World Bank Treasury, for a period of 18 months, within the project “Developing the capacity for government public debt management through the use of derivative financial instruments” code SIPOCA 10. The project is financed from the European Social Fund, within the Operational Program of Administrative Capacity for 2014-2020 and it is under implementation.

On the basis of the average annual economic growth of 5.5% of GDP and of deficits calculated in accordance with the EU methodology of up to 3% of GDP, in 2017-2020 we estimate that the ratio of gross government debt will not exceed 40% of GDP, as shown by the chart below.

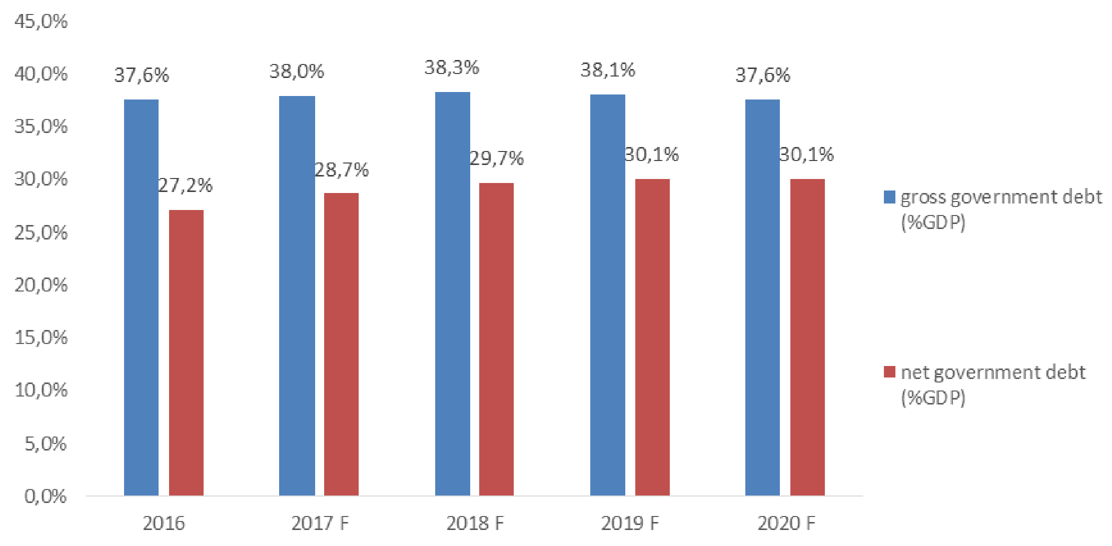
Chart 7 - Gross government debt according to the EU methodology (% of GDP)

Source: Ministry of Public Finance



If the liquid financial assets are considered[29], the level of net government debt (representing the gross government debt minus the liquid financial assets) during the period under analysis will not exceed 30.5% of GDP.

Chart 8 - Government debt according to the EU methodology (% of GDP)



Source: Ministry of Public Finance

The factors which influence the change in the government debt ratio in GDP in 2017-2020, including the stocks-flows adjustments, are presented in appendix 4.

[29] 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).

3.5. STRUCTURAL REFORMS

Structural reforms in the field of State-owned companies

The Ministry of Energy continues the implementation of the process of preparation for the privatization of Complexul Energetic Oltenia[30] and of Hidroelectrica[31], as well as the process of restructuring and rendering more efficient the activity of the companies where the State has holdings.

With regard to Complexul Energetic Oltenia, it was approved at the end of 2016 a restructuring plan for 2016-2020 which refers to rendering more efficient the activity in order to increase the company's attractiveness for investors. Also, the Government is considering to initiate a primary public offering for the sale of a package of 15% newly issued shares, through share capital increase both for Complexul Energetic Oltenia and for Hidroelectrica.

A program of restructuring of Complexul Energetic Hunedoara is being implemented as well, and discussions are being held in parallel with the European Commission for granting State aid of the SIEG - General Interest Service type to ensure the operation of two units of the complex in 2017-2024.

With regard to Compania Nationala a Uraniului (CNU - National Uranium Company), we make the mention that it is process of restructuring in order to make it more efficient, after the Ministry of Energy and the Competition Council took at the end of 2016 the measures necessary to notify the European Commission on the request for granting rescue aid to CNU. In parallel was elaborated a draft legislative act for granting rescue aid to CNU, the Ministry of Energy being authorized to grant to CNU S.A. a rescue aid under the form of a loan on 6 months.

Structural measures in the field of employment:

The Government intends to accelerate the process of reformation of policies, programs and interventions in the **social field** through an integrated, harmonized and coordinated approach thereof.

The Government's concerns, as initiator of social policies and promoter of social rights, refer to changes of mentality, of approaching the system, as well as transforming it into a proactive system. Such a measure can be realized by shifting the focus from assistance granted in a passive manner to the individual to building alternative measures, which means potentiating the role of the individual, of the family, decreasing the dependence of people in distress, as well as promotive active aging.

[30] Complexul Energetic Oltenia is an integrated producer of electricity based on lignite, which was incorporated through the merger of the three energy complexes in Craiova, Rovinari and Turceni with the National Company of Lignite in Oltenia.

[31] Hidroelectrica is the main producer of electricity and the main provider of system services in Romania.

For 2017 are planned a series of legislative measures and amendments, which refer mainly to the consolidation of 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:

- The amendment of the legislative framework of social assistance for the elderly:

- revision of the cost standards for care services given to the elderly at their domicile and in residential centers, in order to update the amounts thereof, as well as to elaborate the separate costs for care services in residential centers according to the dependence degree, through the amendment and supplementation of GD no. 978/2015;
- the amendment and supplementation of the laws related to social assistance services for the purpose of legislative harmonization, including with the law on local public finance, with that related to public-private partnerships, as well as in order to revise the sanctions in the field of social services;
- implementation of the measures from the Government Program related to strengthening public services of local social assistance and developing community teams of integrated intervention.

Legal provisions were introduced for **establishment of the profile of the person** in search of a job, in order to establish the level of employability, namely: “easily employable”, “medium employable”, “difficult to employ”, “very difficult to employ”, levels which indicate the degree of difficulty with regard to insertion on the labor market.

The people who were established the level of employability “difficult” and “very difficult” will benefit of guidance services during the process of social and professional integration at a job, for a term of at most 3 months, based on the employer’s consent. These services will be carried out by services suppliers from the public or private sector, who are accredited under the law.

The Government of Romania adopted measures **of stimulation of the labor force** which refer mainly to granting mobility premiums (employment premium and installation premium). Thus, three types of subsidies were regulated, meant to stimulate the use of employment opportunities from an area by the labor offer available in another area: the employment premium, the installation premium and the relocation premium. At the same time, the concern of the Government of Romania of setting certain targeted measures of activation includes the regulation of activation premiums of Lei 500, non-taxable.

Following the assessment of the data resulting from the implementation of the National employment program approved for 2015, it was considered that **the measures of stimulation of employers** who employ a series of special social categories are not sufficiently stimulative, because the amounts granted are not incentive. Thus, the Government of Romania increased the amount of the subsidies granted to employers. Also, it was established the equalization of the amount of the subsidy awarded to the employers who employ graduates of certain educational institutions, no matter the graduation level.

In order to support **internal mobility** was adopted the National Mobility Plan which established the administrative-territorial units eligible for the measures included in the mobility package - the employment premiums and the installation premiums. The integrated programs which will be elaborated for these disadvantaged areas, financed from European funds and the national budget, seek to encourage investments, local development and the demand for new jobs.

Between November 23 and December 9, 2016 was launched the project call Registration with the Public Employment Service (PES) of inactive NEET youth (financed from the ESF 2014-2020). The financial allocation of 50 million EUR is dedicated to identifying the inactive NEET youth who are not registered in the database of the PES, especially the persons with low qualifications, the Roma individuals and the youth from the rural areas, and those who failed to integrate, to ensure the counseling services and the profiling procedure; the awareness campaigns and the monitoring measures dedicated to NEET youth.

Measures in the field of education

The Government program for 2017-2020, the programmatic European and national documents in the field (the Europe 2020 Strategy, the ET 2020 Framework) substantiate the main strategic targets of the Ministry of National Education in the perspective of year 2020: i) the percentage of those who leave school early should be below 11.3%; ii) at least 26.7% of the people between 30 and 34 years old should have completed tertiary education; iii) at least 10% of the people between 25 and 64 years old should participate to lifelong learning.

The main objectives which are considered and for which a series of measures have been adopted are:

- Ensuring equal chances of access and participation to relevant and inclusive education - Implementation of the guaranteed social package for education, through actions performed both in 2016 and in 2017.
- Ensuring quality at all educational and professional training levels.
- Recapitalization of professional and technical education, within the project “Job Orientation Training in Businesses and Schools”, a project implemented in partnership with the MNE, CNDIPT and the Pedagogical University in Zürich. The Ministry of European Funds launched the project call “Practice strategies for pupils and students in the agricultural-food sector, industry and services” with a total allocation of over 47.8 million EUR from the Operational Program Human Capital (POCU).
- Introducing dual professional education.

- Increasing salaries in education, with the objective of attracting and retaining human capital in this field.

3.6. IMPACT OF EUROPEAN FUNDS ON PUBLIC FINANCE

In 2017-February 28, 2017, Romania benefited of European funds of 37.1 billion EUR, while the contributions to the EU budget were of 14.1 billion EUR, resulting a positive balance of 23 billion EUR.

For 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.

9 programs have been elaborated and are being implemented from European structural and investment funds within the Partnership Agreement for 2014-2020, as follows: a) the Operational Program of Competitiveness - 1.33 billion; b) the Operational Program of Human Capital - 4.22 billion; c) the Operational Program of Large Infrastructure - 9.41 billion; d) the Regional Operational Program - 6.7 billion; e) the Initiative for SMEs Program - 0.1 billion; f) the Operational Program of Administrative Capacity - 0.55 billion; g) the Operational Program of Technical Assistance - 0.21 billion; h) the National Rural Development Program - 8 billion; i) the Operational Program of Fishing - 0.17 billion.

Measures for improvement of the management and general coordination of the implementation of European structural and investment funds:

- Completion of the process of appointment, considering the different levels of intervention, like the institutional framework, the procedural framework, inter-institutional cooperation and the information system.
- Implementation of the monitoring mechanism of the action plans for fulfillment of the ex ante conditions.
- Monitoring the launch of project calls to identify delays from the proposed schedule and the impact of those delays on the implementation of every OP.
- Making more urgent the process of assessment by all management authorities, through completion within the shortest time possible of the procurement procedures of services of assessors/employment of specialized staff/etc.
- Observing the procedural terms of assessment, selection and contracting, as well as analysis of the possibility of reducing some of them.
- MDRAPFE is considering the improvement of the implementation of large infrastructure projects, so as to avoid any more blockages and delays.
- Implementation of the technical assistance supplied by the IFI in order to improve the management of the ESIF.

4. SENSITIVITY ANALYSIS AND COMPARISON WITH THE PREVIOUS VERSION OF THE CONVERGENCE PROGRAM

4.1. 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 trade partner countries.

In Europe, the main risks refer to the manner in which the exit of Great Britain from the EU will be made, as well as the results of the elections which will take place in 2017 in certain Member States. If for some Member States there is a high pre-electoral uncertainty with regard to future political lines and the maintenance of the pro-European commitment, concerns have arisen with regard to the possibility of a hard exit for Great Britain, accompanied by big costs for both parties. From Romania's perspective, the impact of Brexit will have a moderate amplitude, since the trade relationships between the two countries are of a low intensity. Romania's exports to Great Britain are of almost 2.5 billion EUR (4.3% of the total) and imports are of only 1.5 billion EUR (2.3% of total imports). In this framework, it can be considered that Brexit will not represent a significant obstacle in the performance of Romania's international trade activity. Although the procedure of starting the formal process of leaving the EU has already taken place, Brexit will be effectively completed in 2019. This time interval gives the space necessary to Romania to adapt in institutional terms, as well as with regard to the business environment, to the new arrangements that are to be established following the negotiations with the EU. Also, at European level the low profitability of the banking system, associated with a sudden and abrupt increase of the risk appetite at global level, might have negative effects on domestic demand, with a negative impact on Romanian exports.

At the same time, at national level persists the uncertainty from the electoral campaign and the period when the new US administration took over its duties, with regard to its attitude towards the international bodies, international trade and the regulation of the financial sector.

Geopolitical tensions keep the uncertainty at high levels and might become an obstacle for investments. More than that, the continued maintenance of the intensity of terrorist attacks on certain Member States of the EU (Great Britain, Sweden), as well in Turkey, the most important trade partner of Romania outside the EU, amplify the already existing geopolitical tensions. Under these circumstances, the risk aversion of the business environment can be intensified and thus affect a large spectrum of the economic activity.

But all of these threats to the stability climate of the West-European nucleus might represent an opportunity for Romania within the meaning of triggering the attention of the investors towards a space which represents an increased degree of security and a competitive level of taxation. Romania could attract significant flows of capital by offering to the business environment a favorable climate for performance of the economic activity.

On the internal plan, risks are generally balanced in terms of affecting domestic offer or demand. Domestic risks are counterbalanced by the measures from the Government program of fiscal relaxation and increasing the population's income. There is a risk for part of the additional domestic demand to be covered in an increased proportion through imports, with an impact on the external imbalances. From the perspective of inflation, the risks are associated with the rhythm of adjustment of the administered prices, as well as the uncertainties of the future evolutions of the prices for energy products.

4.2. SENSITIVITY OF THE BUDGET FORECASTS FOR DIFFERENT SCENARIOS AND ASSUMPTIONS

Given that collections from taxes and charges 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 collections from value-added tax and social insurance contributions.

Table 9 - Sensitivity of the budget forecasts for different scenarios and assumptions

Category of taxes and charges	Macroeconomic base	Changes of the macroeconomic base (percentage points)	Changes of the revenues (% of GDP) 2016
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

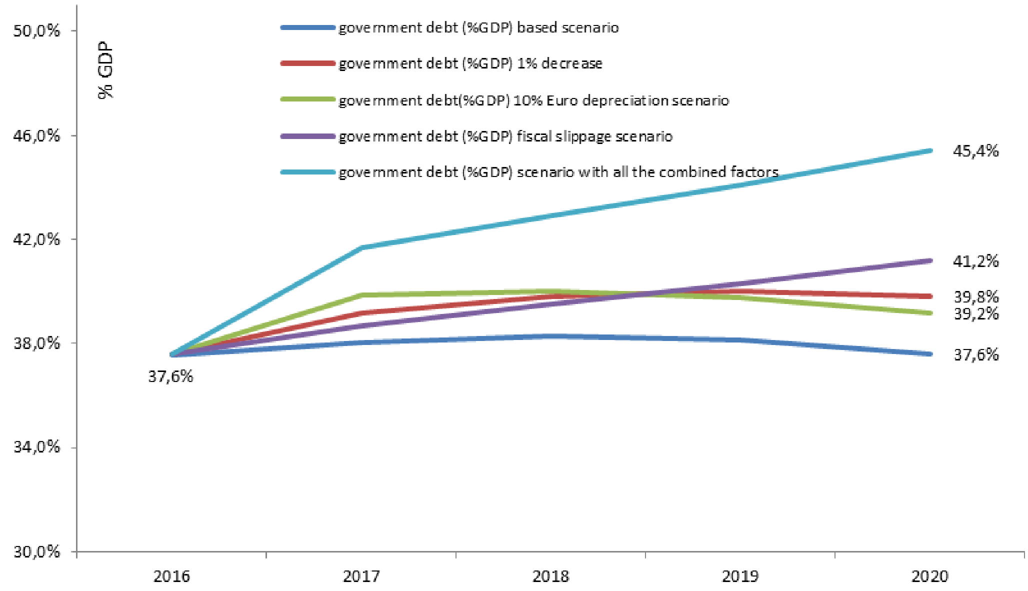
4.3. PUBLIC DEBT SENSITIVITY

Public debt sensitivity analysis[32]

1) the influence of economic growth, of the domestic currency depreciation, as well as of the fiscal slippage on the government debt outstanding , and

2) the influence of the domestic currency depreciation and of the interest rates changes on interest payments.

Chart 9 - Influencing factors of government debt



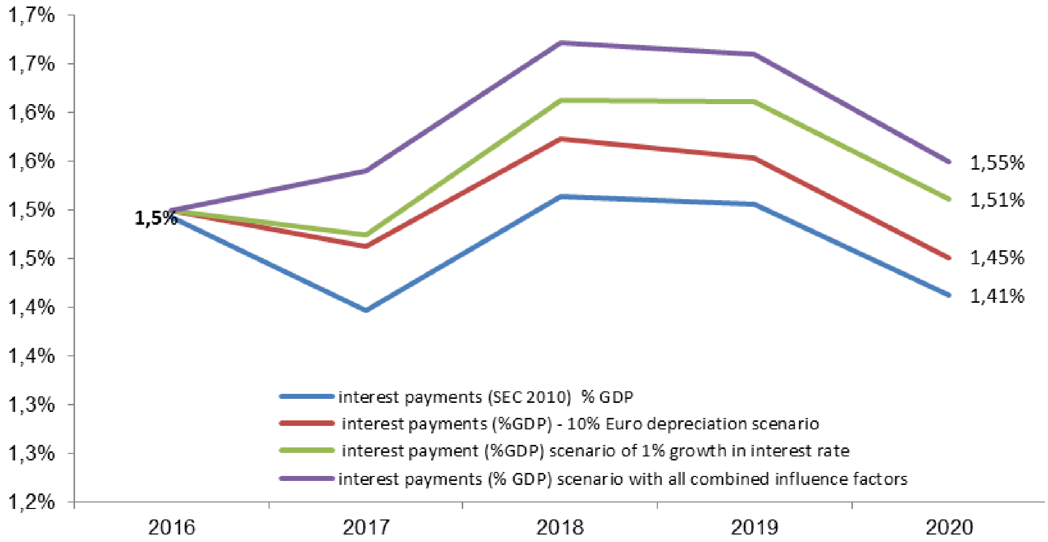
Source: Ministry of Public Finance

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 2.2% of GDP in 2020, 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 government debt ratio in GDP of up to 1.6% of GDP in 2020. A fiscal slippage transposed into a cash deficit to finance of 3.6%[33] of GDP in 2017-2020 would lead to a higher indebtedness ratio in GDP by up to 3.6% of GDP in 2020, while the combined influence of these factors on the government debt ratioin GDP determines an increase of this indicator by 7.8% of GDP in 2020.

[32] All the indicators used in this sub-chapter are compliant with the EU methodology.

[33] The determination of this indicator took into account the winter forecast of the EC, which estimates for 2017 an ESA2010 deficit of 3.6 of GDP

Chart 10 - Influencing factors of interest payments



Source: Ministry of Public Finance

In the chart above it can be noted that the depreciation of the national currency relative to EUR[34] would have a low negative impact on interest payments, within the meaning of increasing the ratio thereof in the GDP by up to 0.04% of GDP in 2020, while the increase of interest rates by 1% would lead to a more accentuated increase of the interest payments ratio in GDP by up to 0.10% in 2020. The combined influence of these factors on interest payments would cause an increase of these payments by 0.14% of GDP in 2020.

[34] The other foreign currencies in which debt is denominated follow the same tendency of appreciation

4.4. COMPARISON WITH THE PREVIOUS VERSION OF THE CONVERGENCE PROGRAM

The macroeconomic scenario of medium-term development presented in this program is significantly different from the scenario from the previous edition of the Convergence Program, namely the edition of April 2016, with regard to the evolution of the GDP and its components. The differences between the two programs are mainly caused by the revision of the statistical data for the period 2014-2015 and the publication of the provisional data for 2016, as well as by the implications of the measures provided in the Government Program.

Thus, in the previous edition of the Convergence Program it was estimated that GDP would increase by 4.2% in 2016. The economic results obtained by the economic sectors, namely the industry, the constructions and, especially, the services, led to an increase of the GDP by 4.8%.

For year 2017 the forecast considered the positive impact of the measures provided in the Government Program on the business environment and on the population's purchasing power. As a result, it is provided that in 2017 the GDP would increase by 5.2% compared to the 4.3% increase forecasted in the previous version, being mainly supported by domestic demand. For 2018-2020 it is estimated that Romanian economy will resume its more sustained increase, with an average annual pace of 5.6%. The growth dynamics of gross fixed capital formation will register an acceleration, being supported by an improved accession of European funds, while those of private consumption will decrease as a result of the decrease of the impact of fiscal measures.

Chart 11 - Comparison between the GDP growth forecasts

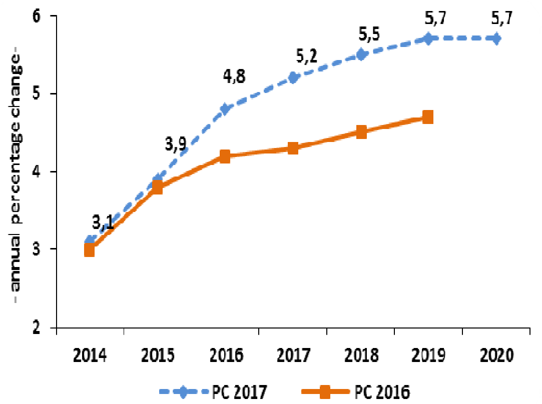
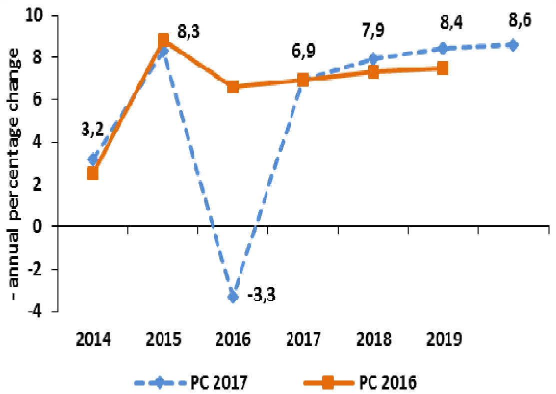


Chart 12 - Comparison between the GFCF increase forecasts



Source: National Commission of Prognosis

Chart 13 - Comparison between the private consumption increase forecasts

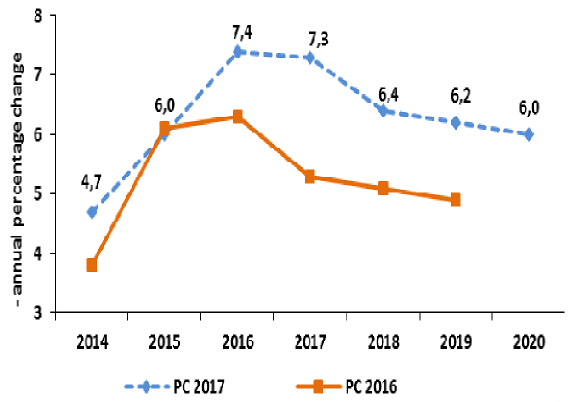
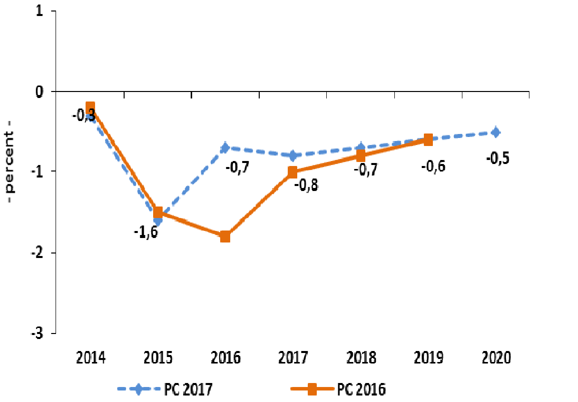


Chart 14 - Comparison between the contributions of net export to GDP increase



Source: National Commission of Prognosis

5. 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 Population Aging Report, which comprises economic and budgetary forecasts for the 28 Member States of the European Union until 2060. The update of the forecasts for the new financial year 2015 estimates for Romania that the share of pension expenses in the GDP will be maintained until the end of the forecast period 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 estimated to remain significantly below the reference value of 60% of GDP on medium-term.

It should be noted the positive evolution compared to the Report of 2009 on sustainability, when Romania was characterized by a high risk on long-term sustainability, due to the budgetary impact caused by the expenses related to the population's aging, which were much over the EU average. In this respect, the improvement of the forecasts in accordance with the Report of 2012 is also confirmed by the financial year 2015.

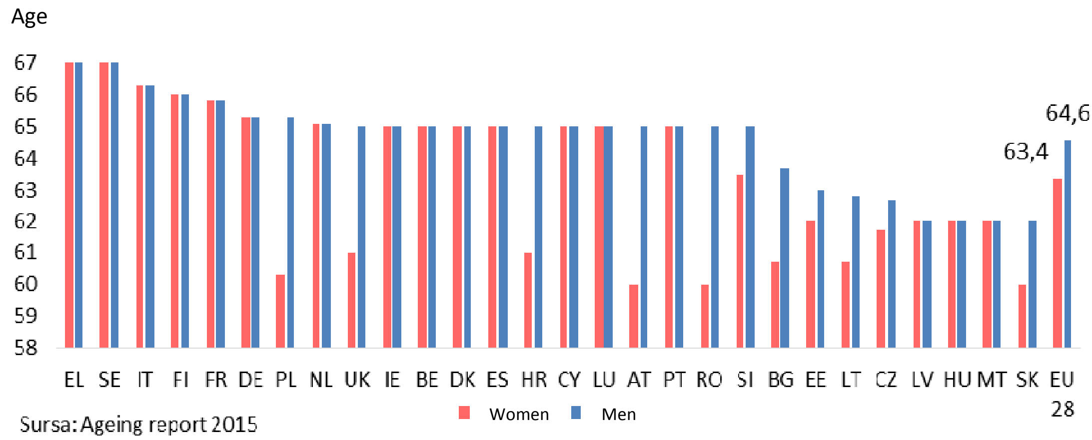
The updated forecast of increase of expenses strictly related to population aging indicates for Romania an increase of 2.2 percentage points of GDP for the period 2013-2060 (the European average being of 1.8 percentage points). On the main expenses components:

- 0.1 percentage points of GDP are represented by the decrease of pension expenses (the European average is of 0.2 percentage points);
- 1.9 percentage points of GDP are represented by the increase of health and long-term care expenses (the European average is of 2 percentage points);
- 0.4 percentage points of GDP are represented by the increase of educational expenses (the European average is of 0 percentage points).

Table 10 - Long-term forecast of total age related expenses[35], as percentage of GDP:						
2013	2014	2020	2030	2040	2050	2060
15.5	15.5	15.8	16.2	17.1	17.5	17.6

The average of standard retirement ages in the European Union is of 64.6 years for men and 63.4 years for women. Romania is close to the European average in the case of the retirement age of men, but has the lowest retirement age for women, together with PL, AT and SK.

Chart 15 - The standard retirement age

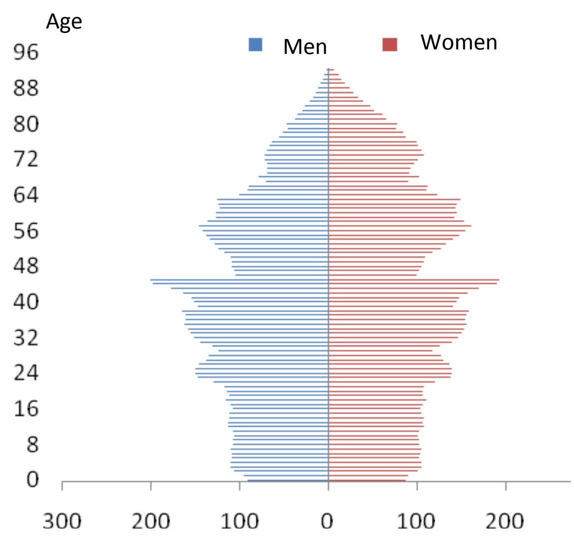


Sursa: Ageing report 2015

Compared to the evolutions at European level, the rhythm of increase of expenses related to population aging is marked in Romania by a more accentuated overturn of the age pyramid. It should be mentioned that the projections did not include the recommendation of the European Commission of equalizing the retirement age between men and women, to 65 years.

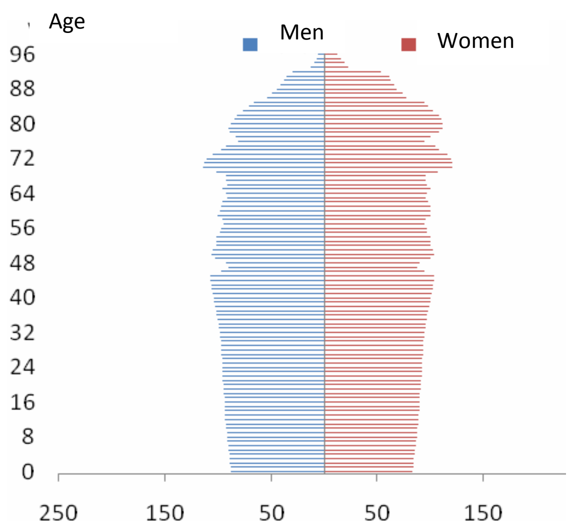
Chart 16 - Population structure: 2013-2060

Structural of Romania's population in 2013



Source: Eurostat-EUROPOP2015

Structure of Romania's population in 2060



Source: Eurostat-EUROPOP 2015

[35] Total expenses include unemployment aid.

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

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 aging.

Table 11 - Long-term forecast of pension expenses

	2013	2014	2020	2030	2040	2050	2060
Pension pillar 1	8.2	8.2	8.1	8.1	8.4	8.4	8.1
Pension pillar 2	-	-	-	0.1	0.4	0.7	0.8

Source: National Commission of Prognosis

The results estimated through the pension model "Pension Reform Options Software Toolkit (PROST)" for the Aging 2015 report indicate an increase of the weight of pension expenses from pillar 1, from 8.2% of GDP in 2013 to approximately 8.4% of GDP at the beginning of the 2040-50 decade, followed by a gradual decrease towards the end of the forecast period until below the level of the basic year.

Pension pillar 2 will have a more and more significant weight in the total pension expenses, reaching a weight of 0.8% of GDP at the end of the forecast horizon.

The PROST model takes into account the indexation of the pension point on a yearly basis with inflation and 50% of the increase of the average salary, the evolution of the population in accordance with the projections of Eurostat-EUROPOP, the assumptions of the European Commission on the evolution of macroeconomic variables. The model does not take into account the possibility of equalization of the retirement age between men and women or other changes of the retirement conditions which are at intention level.

The analysis from the perspective of the *Report of the European Commission on fiscal sustainability*, 2015 edition, confirms the absence of significant risks on the short term and on the long term these risks are considered to be of medium level and derive especially from the initial unfavorable budgetary condition, being increased the public expenses for population aging, especially those related to health care and long-term care.

6. PUBLIC FINANCE QUALITY

The structural measures for increase of public expenses 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.

Rendering budget expenses more efficient

One of the major concerns in the budgetary expenses policy is the **optimization of public investments**, 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 co-financed from EU funds.

The Ministry of Public Finance shall carry out a pilot exercise in collaboration with the Ministry of Transportation, to identify the projects with weak performances, as well as those under-financed, and shall implement a settlement strategy.

In the prioritization process, as per GEO no. 88/2013, the Ministry of Public Finance shall present to the Government the prioritization results on a yearly basis, in order to approve through memorandum the list of priority projects. In 2016, 9 main spending authorities sent significant public investment projects with a total of 119 projects.

Following the analysis of the Law no. 233/2016 on **public-private partnership**, it was decided to start the measures for amendment of the legislation in force and then to elaborate methodological norms which will be approved through Government decision. In this respect, measures were taken to set up a work group, including ministries/institutions, and requesting the support of the International Financial Institutions (EIB, EBRD, and WB).

In order to increase **public spending efficiency** on medium term, the Ministry of Public Finance shall institutionalize the spending review process. Thus, a directorate was created within the ministry, which is responsible for performing these reviews.

Pilot public spending reviews were started in three fields considered priority fields (transportation, health, and education). An Initial report for the transportation sector identifies inefficiency spending areas and proposes savings measures.

For 2017, the Ministry of Public Finance requested to the European Commission - Structural Reform Support Service (EC-SRSS) to facilitate the granting of technical assistance for consolidation of the capacity of performance of spending reviews.

Through Law no. 98/2016 on public procurement Romania implemented in the national legislation Directive 2014/24/EU of the European Parliament and of the Council of February 26, 2014 on public procurement and repealing Directive 2004/18/EC. Therefore, the procurement made by the central authorities shall be made by a central procurement unit; therefore, expenses will decrease by approximately 10-15%, immediately when this unit becomes operational.

Revenue structure and efficiency

Consumption taxation

Romania registered in 2015 revenues collected from VAT of 8.1% of GDP, being 1.1 p.p. over the EU28 average (7%).[36] VAT receipts (in ESA standards/by the standards of ESA 2010) registered a decrease in 2016, compared to 2015, the weight thereof in GDP reducing by 1.5 p.p. to 6.6% of GDP, below the impact of reduction of the standard VAT rate from 24% to 20% and the extension of the application scope of reduced VAT rates to more than half the consumption basket.

With regard to VAT collection performance, the implicit collection rate[37] registered a continuous improvement after 2014, reaching the value of 73% in 2016[38], given the reduction of the weighted average VAT rate to 14.5%. Nevertheless, compared to the EEC countries, Romania had in 2015 an implicit collection rate inferior to that registered in the countries with similar weighted average rates of VAT (the Czech Republic, Estonia).

The level of revenue collected from excise duties in Romania reached 3.7% of GDP in 2015 (and 3.5% in 2016), being similar to that registered in the EEC countries. Nevertheless, the high energy intensity in Romania (almost double than the EU28 average)[39] and the average level of excises for petroleum products (close to the EU average) suggest that the implicit rate of excise collection is inferior to the EU 28 average.

Labor taxation

Romania has one of the lowest taxation rates on the income from salaries from the EU (16%), but this rate is higher than the rates of comparable countries from the Central and Eastern Europe (CEE) area, which leads to the reduction of this competitive advantage. Fiscal revenues from direct taxes paid by private individuals and households represented 3.7% of GDP in 2015, a level below the EU28 average, but similar to the level registered in the countries with similar rates of personal income

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[36] In the Central and Eastern European Area (CEE), Romania is in the middle of the classification, the lowest share being registered in Poland (7%), and the biggest in Hungary (9.7%) and Croatia (13%). Compared to the countries from the Euro area, bigger shares than Romania are only registered by the Northern countries and Portugal.

[37] The index is estimated as ration between the implicit taxation rate (represented by the ratio between the collected revenues and the relevant macroeconomic taxation base) and the weighted average taxation rate.

[38] The estimated value of the implicit VAT collection rate for year 2014 is consistent with the assessment of the European Commission on the level of the VAT gap in Romania of 37.9% (the highest in the EU28).

[39] http://ec.europa.eu/eurostat/tgm/table.do?tab=table&init=1&language=en&pcode=tsdec360&plugin=1

tax. The implicit collection rate of this tax has been constantly improved after 2008, reaching 81.6% in 2015[40].

The shares of social contributions of the employers are of 22.8% and of the employees of 16.5%. Although the shares of social contributions were reduced in Q of 2014, total contributions (employee and employer) are of 39.3%, over the EU28 average. The revenues from social contributions represent a low proportion of the GDP (8.1%), below the EU average of 13.2% and below most EEC countries, including the countries with a lower share of social contributions (Estonia, Poland, and Latvia). The collection efficiency of the total social contributions was of 83.2%[41] in 2015.

Another important indicator is the fiscal burden for different revenue installments. It affects labor cost and the participation to the labor market, with a negative impact on work demand and offer. Fiscal burden for the employees with low salaries (below 50% of the average salary) in Romania is very high, the seventh highest in EU28 and the third highest in the EEC countries. For the employees with salaries below 67% of the average salary, the fiscal burden is close to the EU average, and for the employees with average salaries and over the fiscal burden is below the EU average. Compared to 2008, the fiscal burden decreased for the employees with low salaries by 2.6 - 2.7 percentage points. For the employees with average and high salaries, the fiscal burden decreased by 3.1 - 4 percentage points. In conclusion, the fiscal burden for the employees with low salaries is disproportionate and together with the low level of the salaries it has a negative effect on the motivation to participate to the labor market for these employees.

Profit taxation

Romania registered revenues from the corporate income tax of 2.3% of GDP in 2015, the weight being slightly reduced than the one registered, on average, in the European Union (2.5% of GDP). Also, Romania collects higher revenues from corporate income tax compared to the countries which have similar taxation rates, namely Latvia, Lithuania (both with a 15% rate and weights of profit in the GDP of 1.6% and 1.5%, respectively, in 2015) and Slovenia (rate of 17% and 1.5% of GDP collection).

With regard to the implicit collection rate of corporate income tax, calculated on the basis of the implicit taxation index[42], it is noted a constant improvement in the interval 2013-2015, this evolution confirming the direct relationship between this index and the cyclical position of economy. In Romania, the implicit collection rate advanced to 0.26 in 2015, as a result of the increase of the implicit taxation rate, due to a higher

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[40] The calculation of this rate used as taxation base the gross salaries and did not take into account the exemption from payment of personal income tax for the private individual with serious or accentuated disability and for the income obtained as a result of the performance of the activity of creation of computer software and certain agricultural, forestry and fish breeding activities. Thus, the indicator is an underestimate of the real collection efficiency.

[41] The calculation of this rate did not take into account the exemption from payment of contributions for meal vouchers, gift vouchers, the ceiling of social contributions to at most 5 average salaries, etc.

[42] The implicit taxation rate for the corporate income tax is calculated relative to the corporate income tax paid by enterprises (code ESA D51B_C2) to the gross surplus from exploitation and mixed revenue (code ESA B2G_B3G)

growth rate of corporate income tax revenue compared to that of the tax base. By comparison with the EEC countries, it is noted that Romania has an implicit collection rate of corporate income tax lower than Bulgaria (0.46, with the lowest tax rate of 10%), the Czech Republic (0.36) and Slovakia (0.33), but higher than Poland and Hungary (both with 0.19), Slovenia (0.23), and Lithuania (0.21).

Property taxation

The fiscal revenues from property taxes represented 0.8% of GDP and 2.9% of the total fiscal revenues in 2015. These weights remained relatively constant as of 2008. Fiscal revenues from property taxes as percentage of the GDP and from total taxation are well below the EU average, of 2.5% of GDP and 6.4%. Although reduced by comparison with the EU average, they are comparable with those registered in other countries of the EEC area, but below the level registered in Poland, Hungary and Latvia.

APPENDICES

Table no. 1 a – Macroeconomic projections

	Code Sec	2016	2016	2017	2018	2019	2020
		Level 1) Billion Lei	Percentage change				
1. Real GDP	B1*g	745.4	4.8	5.2	5.5	5.7	5.7
2. Nominal GDP	B1*g	761.5	7.1	7.2	7.7	7.6	7.1
Real GDP components							
3. Private consumption expenditure	P3	473.3	7.4	7.3	6.4	6.2	6.0
4. Public consumption expenditure	P3	101.9	4.5	1.8	2.8	2.7	2.8
5. Gross fixed capital formation	P51	170.2	-3.3	6.9	7.9	8.4	8.6
6. Change of stocks and net securities procurement (% of GDP)	P52+ P53	9.3	1.1	-0.3	0.0	0.0	0.0
7. Export of goods and services	P6	316.6	8.3	6.8	6.3	6.9	7.0
8. Import of goods and services	P7	325.9	9.8	8.5	7.9	8.1	8.0
Contributions to GDP growth							
9. Final domestic demand			4.4	6.3	6.2	6.2	6.2
10. Change of stocks and net securities procurement	P52+ P53		1.1	-0.3	0.0	0.0	0.0
11. Net export	B11		-0.7	-0.8	-0.7	-0.6	-0.5

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

Table no. 1 b – Price evolution

	2016	2017	2018	2019	2020
	Percentage change				
1. GDP deflator	2.2	2.0	2.1	1.9	1.4
2. Private consumption deflator	-0.5	1.4	1.8	1.5	0.9
3. Harmonized consumer price index	-1.1	1.2	2.5	2.3	2.2
4. Public consumption deflator	5.3	1.9	2.1	2.1	1.0
5. Investments deflator	1.4	0.8	1.0	0.8	0.7
6. Export deflator (goods and services)	-0.5	-0.6	0.1	0.5	0.4
7. Import deflator (goods and services)	-1.1	-1.5	-0.8	-0.7	-0.7

Table no. 1 c - **Labor force market evolution**

	CODE SEC	2016	2016	2017	2018	2019	2020
		LEVEL THOUSAN D PERSONS	PERCENTAGE CHANGE				
1. Total employment[1]		8477.2	-0.9	0.7	0.9	1.0	1.0
2Employment thousand hours worked[2]		15303368	-0.7	0.8	1.0	1.0	1.0
3. Unemployment rate -%[3]			5.9	5.7	5.5	5.4	5.3
4. Labor productivity[4]			5.8	4.4	4.5	4.6	4.6
5. Hourly labour productivity[5]			5.6	4.3	4.4	4.6	4.6
6. Compensation of employees million Lei	D1	260692.1	13.8	8.6	8.5	8.3	8.0
7. Compensation per employee - Lei		41254	11.6	5.8	5.9	6.0	5.8

[1] Compensation, 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 employed person
[5] Real GDP per hour worked

Table no. 1 d – Sector balances

% of GDP	CODE SEC	2016	2017	2018	2019	2020
1. Net balance, compared to the rest of the world	B9	0.2	0.4	0.8	0.9	0.9
Of which:						
- the balance of goods and services		-0.9	-1.2	-1.4	-1.3	-1.2
- the balance of primary income and secondary income		-1.4	-1.2	-1.0	-0.8	-0.8
- capital account		2.5	2.8	3.2	3.1	2.9
2. Net private sector balance	B.9	3.2	3.3	3.7	3.4	2.9
3. Net government sector balance	EDP B.9	-3.0	-2.9	-2.9	-2.5	-2.0
4. Statistical discrepancy						

Table no. 2 a– Consolidated budget projection

	CODE SEC	2016	2016	2017	2018	2019	2020
		LEVEL MILLION LEI	% OF GDP				
Bet balance (EDP B9), per sub-sectors							
1. Consolidated budget	S.13	-23,127.8	-3.0	-2.9	-2.9	-2.5	-2.0
2. Central administration	S.1311	-25,121.9	-3.3	-3.6	-3.4	-2.8	-2.3
3. State administration	S.1321	M	M	M	M	M	M
4. Local administration	S.1313	1,252.4	0.2	0.3	0.2	0.1	0.1
5. Social insurance fund	S.1314	741.7	0.1	0.3	0.2	0.2	0.2
Consolidated budget (S13)							
6. Total collections	TR	241,215.0	31.7	32.2	32.3	32.8	33.3
7. Total expenses	TE[1]	264,342.8	34.7	35.1	35.2	35.4	35.3
8. Net balance	EDP B.9	-23,127.8	-3.0	-2.9	-2.9	-2.5	-2.0
9. Interests	EDP D.41	11,373.4	1.5	1.4	1.5	1.5	1.4
10. Primary balance[2]		-11,754.4	-1.5	-1.6	-1.4	-1.0	-0.6
11. One-off and other temporary measures[3]		-3,200	-0.4	0.0	0.0	0.0	0.0
Selected revenue components							
12. Total taxes (12=12a+12b+12c)		135,122.7	17.7	17.6	17.8	18.0	18.2
12a. Production and import taxes	D.2	85,930.9	11.3	11.0	11.0	11.0	11.1
12b. Current taxes on income, fortune, etc.	D.5	49,191.8	6.5	6.6	6.8	7.0	7.1
12c. Taxes on capital	D.91						
13. Social contributions	D.61	61,973.5	8.1	8.7	8.7	9.0	9.4
14. Property taxes	D.4	7,379.9	1.0	0.9	0.9	1.0	1.0
15. Others[4]		36,738.9	4.8	5.0	4.8	4.8	4.6
16=6. Total revenues	TR	241,215.0	31.7	32.2	32.3	32.8	33.3
Selected expenses components							
17. Employee payment + interim consumption	D.1+P.2	103,130.1	13.5	13.5	13.3	12.8	12.4
17a. Employee payment	D.1	62,758.5	8.2	8.4	8.3	8.1	8.0
17b. Interim consumption	P.2	40,371.6	5.3	5.1	5.0	5.0	5.0
18. Social contributions (18=18a+18b)		87,975.3	11.6	11.7	12.0	11.7	11.4
of which Unemployment aid[5]		635.8	0.1	0.1	0.1	0.1	0.1
18a. Social contributions in kind	D.6311, D.6312, D.63131	6,600.7	0.9	0.9	0.9	0.9	0.9
18b. Social contributions, others	D62	81,374.6	10.7	10.8	11.1	10.8	10.5
19=9. Interests	EDP D.41	11,373.4	1.5	1.4	1.5	1.5	1.4
20. Subsidies	D.3	3,010.8	0.4	0.4	0.5	0.5	0.5
21. Gross fixed capital formation	P.51	27,190.9	3.6	4.3	4.0	4.5	5.0
22. Capital transfers	D.9	12,416.5	1.6	1.3	1.6	1.6	1.6
23. Others [6]		19,245.8	2.5	2.6	2.5	2.6	2.5
24=7. Total expenses	TE1	264,342.8	34.7	35.1	35.2	35.4	35.3

[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 policies[1]

	2016	2016	2017	2018	2019	2020
	Level	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP
1. Total revenues in case of preservation of current policies	241,215.0	31.7	32.1	32.0	32.5	33.0
2. Total expenses in case of preservation of current policies	264,342.8	34.7	35.2	35.6	35.7	35.6

1) The projections must start at the time when the Stability or convergence program 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. 2c – Amounts which must be excluded from the reference value of expenses

	2016	2017	2018	2018	2019	2020
	Level (million Lei)	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP
1.Expenses from EU programs covered completely from EU funds	3,875.2	0.5	1.2	2.0	2.3	1.8
2. Cyclical expenses for unemployment aid [1]	-27.7	-0.0036	-0.0012	-0.0006	0.0000	-0.0008
3. Effect of discretionary measures related to revenues[2]	0.4	0	0	0	0	0
4. Increase of the revenues imposed by law	0	0.1	0.1	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

The following formula was used: $E_t^{UC} = E_t^U \cdot \frac{u_t - NAWRU_t}{u_t}$ 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 expenses, by function

% of GDP

	CODE COFOG	2016	2019
1. General public services	1	4.8	n.a.
2. Defense	2	1.0	n.a.
3. Public order and national safety	3	2.2	n.a.
4. Economic relations	4	5.1	n.a.
5. Environmental protection	5	0.7	n.a.
6. Domiciliary and community services	6	1.0	n.a.
7. Health	7	4.1	n.a.
8. Recreation, culture, and religion	8	1.0	n.a.
9. Education	9	3.4	n.a.
10. Social protection	10	11.4	n.a.
11. Total expenses (=point 7=24 in Table 2a)	TE	34.7	35.4

*) the data for 2016 are semi-final

Table no. 4 – General government debt developments

% OF GDP	SEC CODE	2016	2017	2018	2019	2020
1. Gross government debt [1]		37.6	38.0	38.3	38.1	37.6
2. Change in gross government debt		-0.4	0.4	0.3	-0.2	-0.5
Contribution to changes in gross debt						
3. Primary balance[2]		-1.5	-1.6	-1.4	-1.0	-0.6
4. Interest [3]	EDP D.41	1.5	1.4	1.5	1.5	1.4
5. Stock-flow adjustments		-3.4	-2.6	-2.6	-2.7	-2.5
Of which: - Differences between interests paid and accrual[4]		-0.1	-0.1	-0.1	-0.1	-0.1
- Net accumulation of financial assets[5]		2.0	-0.4	0	0	0
of which: - privatization proceeds		0	0	0	0	0
- Valuation effects and others[6]		- 5.3	-2.1	-2.5	-2.6	-2.4
p.m. Implicit interest rate on debt[7]		4.2	4.0	4.3	4.2	4.0
Other relevant variables						
6. Liquid financial assets[8]	% of GDP	10.4	9.3	8.6	8.0	7.5
7. Net financial debt (7=1-6)	% of GDP	27.2	28.7	29.7	30.1	30.1
8. Debt amortization (existing obligations) since the end of the previous year[9]	% of GDP	6.8	4.6	3.9	3.8	2.8
9. Percent of the debt denominated in foreign currency	% of debt	52.4	50.0	47.4	44.2	42.7
10. Average maturity[10]	years	5.7	5.8	-	-	-

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 could be distinguished when they are relevant or in casethe debt - to -GDP ratio 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 could be distinguished when they are relevant or in case the debt- to- GDP ratio is over the reference value;
6) Changes due to exchange rates mouvements and to operation on the secondary market could be distinguished when they are relevant or in case the debt- to- GDP ratio is over the reference value;
7) The associated proxy variable is represented in the report between the annual interest payments and the debt stock 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 debt outstanding at December 31, 2016;
10) Average remaining maturity

Table no. 5 – Cyclical evolutions

% OF GDP	SEC CODE	2016	2017	2018	2019	2020
1. Real GDP growth (%)		4.8	5.2	5.5	5.7	5.7
2. Net consolidated balance	EDP B.9	-3.0	-2.9	-2.9	-2.5	-2.0
3. Interest expenses	EDP D.41	1.5	1.4	1.5	1.5	1.4
4. Temporary and one-off measures [1]		-0.4	0.0	0.0	0.0	0.0
5. Potential GDP growth (%)		3.9	4.5	5.0	5.3	5.4
Contributions:						
- labor		0.0	0.2	0.3	0.3	0.2
- capital		0.8	1.0	1.2	1.4	1.6
- total factor productivity		3.1	3.3	3.4	3.6	3.6
6. Output Gap		-0.8	-0.1	0.4	0.7	1.0
7. Cyclical component		-0.3	0.0	0.1	0.2	0.3
8. Cyclically adjusted balance (2-7)		-2.8	-2.9	-3.0	-2.8	-2.3
9. Cyclically adjusted primary balance (8+3)		-1.3	-1.5	-1.5	-1.3	-0.9
10. Structural balance (8-4)		-2.4	-2.9	-3.0	-2.8	-2.3

[1] A plus sign means one-off measures of deficit reduction

Table no. 6 - Differences from the previous version

	SEC CODE	2016	2017	2018	2019	2020
GDP growth **(%)**						
Previous version		4.2	4.3	4.5	4.7	
Updated version		4.8	5.2	5.5	5.7	5.7
Difference		0.6	0.9	1.0	1.0	
Budget balance (% of GDP)						
Previous version	EDP B.9	-2.9	-2.9	-2.3	-1.6	
Updated version	EDP B.9	-3.0	-3.0	-2.9	-2.5	-2.0
Difference		-0.1	-0.1	-0.6	-0.9	
Gross general government debt (% of GDP)						
Previous version		39.1	39.8	39.9	39.3	
Updated version		37.6	38.0	38.3	38.1	37.6
Difference		-1.5	-1.8	-1.6	-1.2	

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

% OF GDP	2007	2010	2020	2030	2040	2050	2060
Total expenses							
Of which: Age related expenses	13.2	17.2	15.6	16.1	17.0	17.4	17.4
- Pension expenses	6.3	9.4	8.1	8.1	8.4	8.4	8.1
- Social insurance expenses							
Pensions for age and anticipated pensions	5.2	7.8	7.0	6.8	7.2	7.2	7.0
Other pensions (disability, survivorship)	1.1	1.6	1.1	1.3	1.2	1.2	1.1
Occupational pensions (if related to the central administration)							
- Health care	3.5	3.7	4.1	4.3	4.6	4.7	4.8
- Long-term care (previously included under "health care")	0.5	0.6	0.8	1.0	1.2	1.4	1.6
- Education expenses	4.2	3.5	2.6	2.7	2.8	2.9	3.0
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	5.9	6.1	6.1	6.1	6.3	6.5
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 reforms[1)]							
Social contributions directed towards the mandatory private pension system[2)]	0	0.4	1.5	2.1	2.4	2.5	2.7
Expenses for pensions paid by the mandatory private pension system[3)]	0	0	0	0.1	0.4	0.7	0.8
Assumptions							
			- average paces -				
Labor productivity increase rate (by hour)	2.7	1.1	2.1	2.3	2.1	1.9	1.8
Real GDP growth	6.9	0.0	3.9	1.8	1.4	1.5	1.3
Participation rate among men (20-64 years)	76.4	77.3	81.0	78.5	76.7	76.5	77.0
Participation rate among women (20-64 years)	61.2	60.0	61.1	59.5	57.5	57.4	58.0
Total participation rate (20-64 years)	68.7	68.6	71.1	69.1	67.2	67.1	67.7
Unemployment rate - BIM	6.4	6.3	6.3	6.7	6.5	6.5	6.5
Population aged 65 and more out of the total population	14.7	15.9	17.3	21.1	24.3	28.7	30.8

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 obligations

	2016	2017
Public guarantees*)	2.3%	2.3%
Of which: related to the financial sector	0.02%	0.0%

*) corresponding to thegeneral government sector, excluding the guarantees issued between entities of the general government sector