April 2011
IMF Country Report No. 11/80

Romania—Seventh Review Under the Stand-By Arrangement, Cancellation of Current Stand-By Arrangement, and Request for a New Stand-By Arrangement—Staff Report; Supplement on the Assessment of the Risks to the Fund and the Fund's Liquidity Position; Supplementary Information; Press Release on the Executive Board Discussion; Statement by the Executive Director and the Senior Advisor to the Executive Director for Romania

The following documents have been released and are included in this package:

- The staff report, prepared by a staff team of the IMF, following discussions that ended on February 8, 2011, with the officials of Romania on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on March 10, 2011. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.
- A staff supplement of March 11 on the assessment of the risks to the Fund and the Fund's liquidity position.
- A staff supplement of March 18, 2011 updating information on recent developments.
- Press Release summarizing the views of the Executive board as expressed during its March 25, 2011, discussion of the staff report that completed the review.
- A statement by the Executive Director and Advisor to the Executive Director for Romania

The documents listed below will be separately released.

- Letter of Intent sent to the IMF by the authorities of Romania*.
- Technical memorandum of Understanding*.

*Also included in Staff Report

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

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INTERNATIONAL MONETARY FUND

ROMANIA

Seventh Review Under the Stand-By Arrangement, Cancellation of Current Stand-By Arrangement, and Request for a New Stand-By Arrangement

Prepared by the European Department
(In Consultation with Other Departments)

Approved by Poul M. Thomsen and Aasim Husain

March 10, 2011

Stand-By Arrangement (SBA) and follow-up SBA: A 24-month, SDR 11.443 billion (€12.95 billion, US$17.07 billion, 1,110.77 percent of quota), SBA was approved by the Executive Board on May 4, 2009 (Country Report No.09/183). Seven tranches totaling SDR 10,569 million have been made so far. The authorities are considering treating as precautionary the eighth and final tranche of SDR 874 million, which will be made available subject to the completion of this review. In the attached letter of intent, the Romanian authorities requested to end the current SBA early and simultaneous approval of a new 24-month, SDR 3,090.6 million (€3.5 billion, US$4.9 billion, 300 percent of quota) SBA. The letter describes the new economic program for which they seek Fund financial support. Funds under the new program will also be provided by the European Union (on a precautionary basis) and the World Bank.

Status of the current program: The performance criteria for the seventh review have been met, with the exception of the criterion on general government arrears (for which a waiver was already granted January 7, 2011). Inflation remained within the inner band of the inflation consultation mechanism.

Key issues: The final SBA review and negotiations for the follow-up SBA focused on three issues: (i) measures to assure compliance with fiscal targets; (ii) progress on the structural reform agenda; and (iii) ensuring continued financial sector stability.

Discussions: Discussions were held in Bucharest, January 25–February 8, 2011. The mission met with President Basescu, Prime Minister Boc, Finance Minister Ialomiţianu, Central Bank Governor Isarescu, other senior officials, representatives of labor and business organizations, and financial institutions. The staff team comprised J. Franks (head), P. Mitra, M. Stierle, and L. Zhang (all EUR); F. Salman (SPR); F. Hasanov (FAD); and M. Dobler (MCM). T. Lybek (Resident Representative) assisted the mission. Discussions were held jointly with the EC, ECB, and World Bank staff.

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I. INTRODUCTION AND SUMMARY

1. **The economy has stabilized and growth is now resuming.** Data for Q4 2010 and recent indicators suggest that growth has restarted and will slowly gain momentum in 2011 to around 1½ percent. Growth is expected to accelerate in 2012, reaching 4–4½ percent. Inflation, driven by high food and fuel prices and the recent VAT hike, likely peaked at end-2010, and is expected to return to the central bank's target range (3 percent ± 1 ppt).

2. **The program will end broadly on track.** Performance criteria for the seventh review have been met except for the criterion on government arrears, (for which a waiver was already granted). While progress has been made in eliminating central government arrears, substantial arrears continue in local governments. The indicative targets on loss-making state-owned enterprises (SOEs) and current spending were missed. The structural benchmark regarding tax administration for high net wealth individuals was met, and that on parliamentary ratification of amendments to the bank resolution framework was partially met, as some amendments were ratified, but ratification is still pending in parliament for others. The structural benchmark for mid-March regarding integrating accounting reporting with the Treasury payment system was met, but there will be a delay in amending legislation to permit the use of the deposit guarantee fund to facilitate bank restructuring.

3. **The successor SBA will focus on boosting potential growth through structural reforms.** Structural deficiencies in key economic areas weigh heavily on economic growth. Improved efficiency of the public sector will reduce bureaucratic barriers to economic efficiency and will increase the absorption of EU structural funds to boost capital spending to improve the country's infrastructure. The new program also aims at deep-rooted reforms in the energy and transport sectors, including pricing reforms, improved regulation, and the restructuring and privatization of energy and transport SOEs. Fund and EU precautionary support will reassure private markets and provide a cushion against future shocks, should they materialize.

4. **Fiscal adjustment will continue.** The end-December fiscal balance target was met with a substantial margin, reflecting higher-than-expected tax revenues. The difficult fiscal measures enacted in 2010, complemented with continued prudent expenditure policies, put the fiscal cash deficit targets of 4.4 percent in 2011 and 3.0 percent in 2012 well within reach. However, continued efforts to improve tax collections, tackle expenditure pressures (particularly in the health sector), and reduce arrears will be crucial to sustained deficit reduction. As part of ongoing tax administration improvements, the government will pass an ordinance on indirect audit methods (¶17) as a prior action for the new SBA.

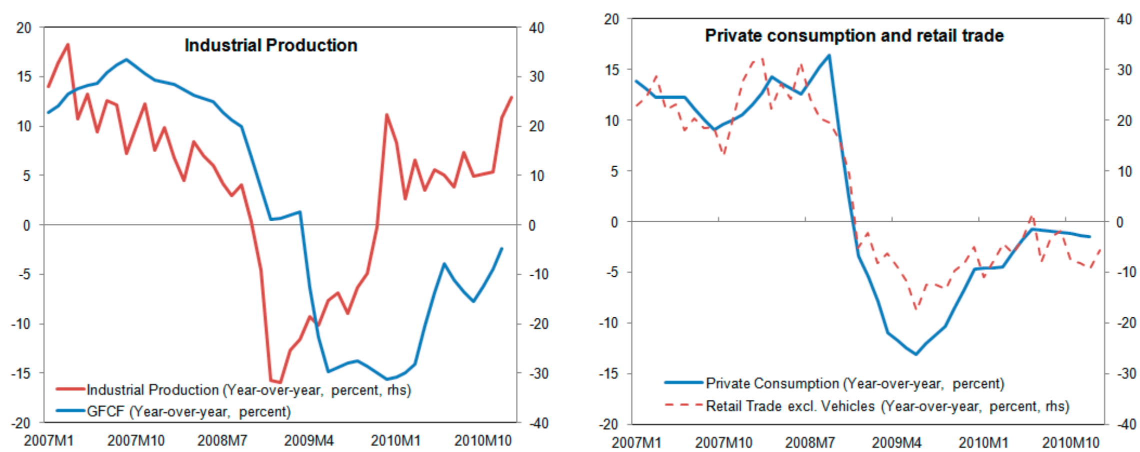
5. **The banking sector has weathered the crisis well, remaining well-capitalized and liquid.** Non-performing loans continue to increase, but at a declining pace and are expected to peak in mid-2011. Banks remain well-capitalized, with an average capital adequacy ratio of 14.7 percent and all banks above 11 percent at end-2010. However, the continued

6. vigilance is required, as performance will vary significantly across banks. In March, the authorities will discuss an extension of the European Bank Coordination Initiative (EBCI) with the largest foreign-owned banks, with a view toward continuing its stabilizing effects.

II. Recent Developments

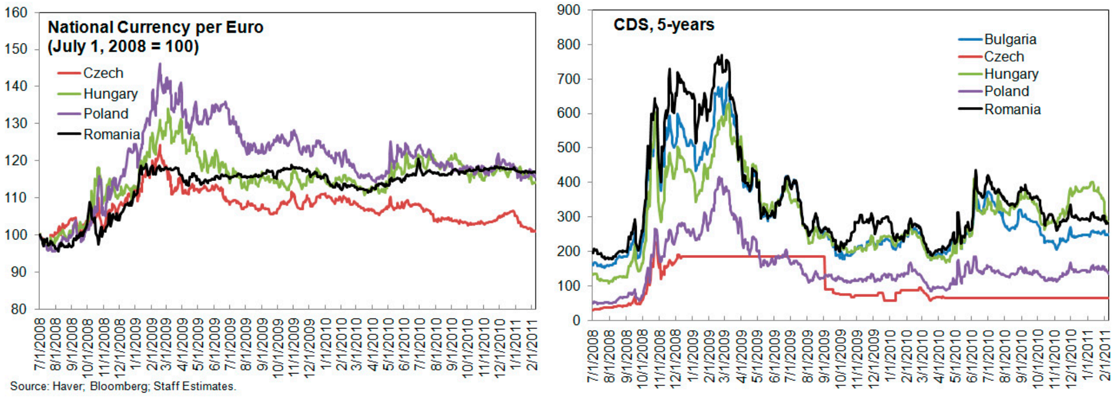
7. **The Romanian economy is beginning to recover.** Recent data show slight positive growth in Q4 2010, while revisions to previous quarters have produced a better outturn for the year than previously expected (-1.3 percent). Strong export growth continues and industrial production remains robust; however, weak retail sales persist. Registered unemployment has decreased, but mainly due to shrinking labor force participation rather than job creation.

8. **Inflation peaked in December 2010, and is now likely to decline.** Headline CPI inflation reached 8.0 percent in December before dropping to 7.0 percent in January. The initial pass-through of the 5 percentage points VAT hike in July 2010 was roughly as expected, but inflation was boosted by increased fuel and food prices (reflecting higher world prices).



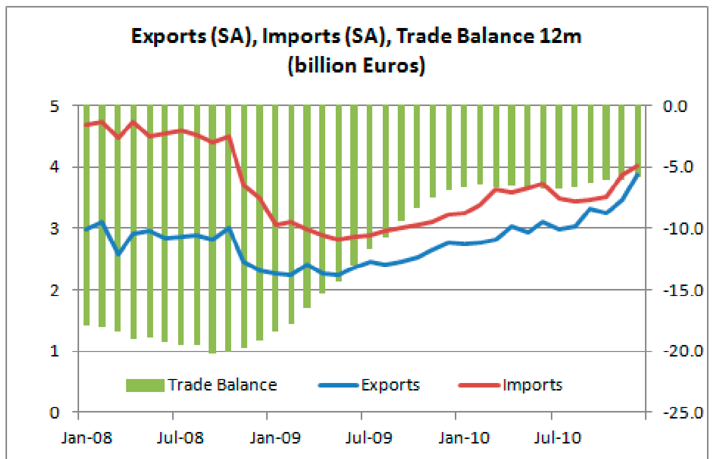
Source: Haver; Staff Estimates.

9. **Financial market stress has remained relatively low in recent months.** The CDS spread for sovereign debt has narrowed by around 100 basis points since September, now below several other EU countries. Romanian equity markets have recovered since their June trough. Thus far, the turbulence in the Euro area periphery has had little direct impact on Romania, though risks remain. Since summer 2010, the leu has remained relatively stable, obviating the need for significant central bank intervention.



Source: Haver; Bloomberg; Staff Estimates.

10. **Romania's external position continues to improve.** The current account deficit improved from 13½ percent of GDP in 2007 to around 4¼ percent of GDP in 2010, driven by a strong shrinking trade deficit. Exports are booming, driven by the manufacturing sector. On the transfers side, workers' remittances have shrunk due to the recession and high unemployment in host economies. Foreign direct investment (FDI) continued to be weak, financing less than half of the current account deficit, while official financing remained the major source of inflows. The depreciation of the leu experienced since mid-2007 has produced an improvement of roughly 15 percent in competitiveness, as measured by the Real Effective Exchange Rate.



Source: Haver; Staff Estimates.

III. Performance under the Current Program

11. **Significant progress has been made under the SBA in achieving fiscal consolidation and safeguarding the financial sector.** While the 2009–10 recession turned out to be deeper and more prolonged than originally anticipated, important adjustment efforts under the SBA have positioned Romania to generate sustainable growth in the coming years (Box 1). A structural fiscal deficit of almost 9 percent of GDP in 2008 was halved by 2010, and the government finances are broadly on track toward respecting the 3 percent of GDP Maastricht deficit limit in 2012. Financial sector measures helped maintain adequate capitalization of banks and liquidity in domestic markets, ensuring banking sector stability. Excessive capital outflows were avoided (in part reflecting the EBCI), and an orderly adjustment of the current account was made possible without undue exchange rate volatility. Structural reforms in tax administration, pensions, public wages and employment, and social

benefits will ease fiscal pressures in the medium-term, while improving public sector efficiency and setting the stage for more widespread improvements in the business climate.

12. **Most performance criteria and structural benchmarks were met throughout the program, including for the seventh and final review.** The performance criteria on government guarantees, external arrears, and net foreign assets were consistently met throughout the program, including for the seventh review. The fiscal deficit target was observed for all but the fourth program review, including by a significant margin for end-December 2010. In contrast, the general government arrears criterion was missed in all reviews.[1] While the central government and social security sector payment arrears have fallen significantly during the program (now under 0.05 percent of GDP), arrears from local governments continue to pose a challenge. Inflation has remained within the inner band of the inflation consultation mechanism throughout the program, though the band was adjusted after the VAT increase in mid-2010. Structural benchmarks, focused primarily on fiscal and financial sector reforms, have generally been met. For the seventh review, the indicative target on current spending was missed, as the authorities used some of the overperformance on revenues to allow for higher discretionary outlays. The indicative target on the operating balances of selected SOEs was also missed, which is symptomatic of the need for more profound SOE reforms under the new program.

[1] A waiver for the end-December arrears target was granted January 7, 2011.

Box 1. Major Measures Under the SBA, 2009–11

The adjustment in the structural fiscal deficit between 2008 and 2011 totaled some 7 percentage points of GDP, with additional savings expected in future years from public wage and pension reforms.

On the *expenditure* side, main measures included:

- Streamlined public employment (by over 100,000).
- A public sector wage cut of 25 percent (partly offset by 15 percent increase in 2011).
- Elimination of holiday bonuses and the 13th salary.
- Inefficient social benefits cut (15 percent) and reinforced social inspections.
- Central government arrears reduced to near zero.

On the *revenue* side, measures included:

- Broadening the tax base and improved tax collection.
- Hikes in VAT rates (from 19 to 24 percent) and excise tax rates.
- A rise in social security contribution rates (3 ppts.).

***Structural reforms* included:**

- A major pension reform was approved to increase retirement ages, move indexation from wages to inflation, and reduce incentives for early retirement, while continuing to build the second pension pillar.
- The public wage system was reformed, harmonizing wages across ministries and significantly reducing the role of bonuses in compensation.
- Social benefits were reformed—including unemployment insurance, social assistance programs, and maternity benefits—to improve efficiency while reducing costs.
- Major health sector reforms were begun to improve efficiency, cost recovery, and financial performance.
- Legislation was approved mitigating fiscal risks from local governments.
- A Fiscal Responsibility Law was introduced to improve medium term budget framework and budget execution.
- A Fiscal Council was established as an independent body to monitor fiscal policy.

In the *financial* sector:

- Support from parent banking groups was secured through the EBCI.
- Continued proactive and intensive supervision by the NBR helped to avoid significant bank difficulties.
- The bank resolution framework was significantly enhanced.
- The funding of the deposit guarantee scheme was strengthened.

IV. Elements of the New Program

A. Overall Program Objectives

13. **The proposed follow-up program aims to provide precautionary support against possible future economic shocks, while assisting Romania in continuing its economic adjustment.** Building on the achievements of the current SBA, the key objectives of the new program are to: (i) continue the fiscal adjustment process while attacking problems of revenue and expenditure efficiency, and arrears; (ii) boost growth potential through structural reforms and improved flexibility of the economy, which will allow for continued competitiveness as Romania prepares for eventual euro area entry; and (iii) continue fostering confidence, facilitating improved private capital flows, by improving policy stability and the business climate.

14. **Fiscal policy will be anchored on the authorities' commitment to reducing the deficit to within 3 percent of GDP by 2012.** Adjustment measures already taken should deliver the targeted 4.4 percent of GDP cash deficit by 2011, but further action may be needed in 2012. Fiscal reforms will concentrate on remaining problem areas, including health care and capital expenditure reforms, further efforts to tackle arrears, and improvements in tax administration and simplification. These reforms should also boost growth by reducing bureaucracy and boosting absorption of EU funds.

15. **Structural reforms aim to eliminate barriers to growth while boosting investment and job creation.** The new program will include a comprehensive SOE reform strategy focusing particularly on the energy and transport sectors, improving regulators' effectiveness, and opening markets (reforming administered prices), while protecting vulnerable members of society. The authorities will also pursue their efforts at labor market reforms and social benefits reforms, crucial to job creation and maintaining Romania's competitiveness.

B. Macroeconomic Framework and Risks

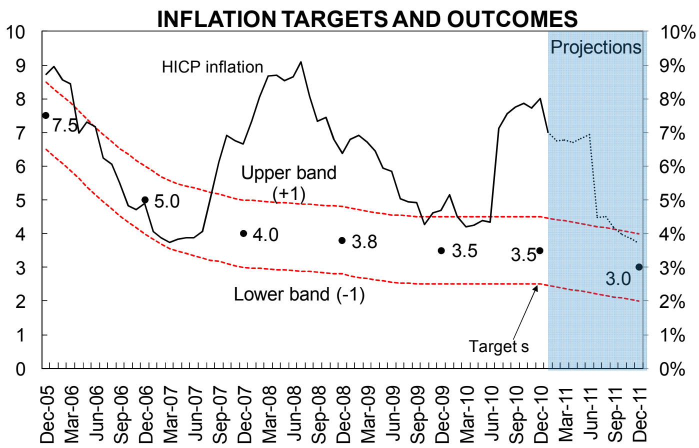
16. **The new program is based on a forecast of a gradual return to growth in 2011–12, abating inflationary pressures, and a stable current account.**

- ***Growth***. GDP growth is expected to pick up during 2011, reaching around 1½ percent as both incomes and employment gradually recover. Growth will accelerate to 4–4½ percent in 2012 and remain there in the medium-term, with domestic demand increasingly becoming the main driver, supported by improved EU funds absorption. The contribution from external demand will slow in line with moderate growth of export markets. Increased investor confidence, coupled with planned privatization under the program will bring renewed FDI and banking inflows.

Romania: Macroeconomic Outlook

	2007	2008	2009	2010	2011	2012	2013
			Baseline Scenario				
Real GDP growth	6.3	7.3	-7.1	-1.3	1.5	4.4	4.3
CPI inflation, average	4.8	7.9	5.6	6.1	5.4	3.4	3.0
CPI inflation, eop	6.6	6.3	4.7	8.0	3.7	3.0	3.0
Current account balance (percent of GDP)	-13.4	-11.6	-4.2	-4.2	-5.0	-5.1	-5.2
Gross international reserves (bn euros)	27.2	28.3	30.9	36.0	40.4	43.4	44.3
			Stress Scenario				
Real GDP growth	6.3	7.3	-7.1	-1.3	-0.5	3.5	4.5
Current account balance (percent of GDP)	-13.4	-11.6	-4.2	-4.2	-6.0	-5.9	-5.2
Gross international reserves (bn euros)	27.2	28.3	30.9	36.0	37.9	39.1	40.7

- ***Inflation***. Staff expects that CPI inflation will gradually return to the NBR's target band in the second half of 2011 as pressures from the recent VAT hike and rising food and fuel prices gradually subside. For 2012, further disinflation toward 3 percent is expected.



Source: Haver; Staff estimates.

- ***External position***. The current account deficit is projected to stabilize at around 4–5 percent of GDP in 2011–12. Export growth will moderate in 2011, leading to a slight worsening of the trade balance. Private capital inflows are expected to improve over the program period, with FDI rebounding from recession lows and portfolio inflows also recovering. Under staff's baseline scenario, no new financing gap is envisaged, consistent with the new program's precautionary nature.

- ***Risks.*** Growth and balance of payments risks are largely balanced, but inflation risks are tilted to the upside. On the downside, domestic political tensions could lead to policy reversals, dampening confidence, and weakening performance; a weaker-than-expected recovery in Western Europe or spillovers from the ongoing turbulence in the euro area periphery could dampen exports or raise risk premia and affect capital flows to Romania. On the upside, a faster-than-expected recovery of consumer confidence and domestic demand or improved EU funds absorption and rapid implementation of structural reforms could catalyze faster growth and prompt a higher current account deficit funded by greater capital inflows. Prospects of reaching the inflation target could be adversely affected by a continued resurgence in world food and energy prices, while needed increases in administered prices may also boost inflation.

C. Fiscal Policies

17. **Current fiscal policy is broadly appropriate for bringing the fiscal deficit to a sustainable level during the new program period.** The full-year effect of the July 2010 fiscal adjustment package along with continued expenditure restraint should help reach the agreed 2011 cash deficit target of 4.4 percent of GDP (from 7.3 percent of GDP in 2009). Key measures include an extension of the pension freeze, continued public employment reductions, elimination of *stimulente* funds (structural benchmark, end-June), expanding the base of healthcare contributions to more pensioners, and replacing heating subsidies with targeted assistance, and further savings expected from health sector (LOI ¶14–15) and education reforms. In the course of 2011, some loss-making SOEs will be brought under the definition of the general government annually adding around ½ percent of GDP to the deficit.[2] For 2012, renewed economic growth combined with prudent expenditure policies would bring the cash deficit to near 3 percent of GDP, though some additional measures may be needed. The cash deficit target may have to be modified in 2011 to partly accommodate the change in definition of the general government, however, in 2012 additional measures may be required to bring the accrual-based deficit within the Maastricht limit.

18. **Despite the progress achieved, there are still significant fiscal problems to be addressed in the follow-up arrangement.** On the revenue side, Romania's crisis stabilization has relied to a significant degree on raising tax rates to relatively high levels, while the efficiency of tax collection remains very low. The general VAT rate now stands at 24 percent and social contributions are over 40 percent of wages. The simplicity and ease of payment of the tax system are also substandard.[3] Under the new program, the authorities will continue tax administration reforms (advised by FAD) and will undertake a comprehensive review of the tax system with a view towards a revenue-neutral tax simplification. Following removal of multiple tax forms, options to reduce frequency of filing and create a unified tax declaration are being examined, as well as expansion of e-filing. A government decision on indirect audit methods will be passed (prior action) and a strategy and action plan developed for incorporating these methods into compliance functions.[4] Allocation of resources towards medium and large taxpayers will be improved by requesting the EU Council of Ministers for

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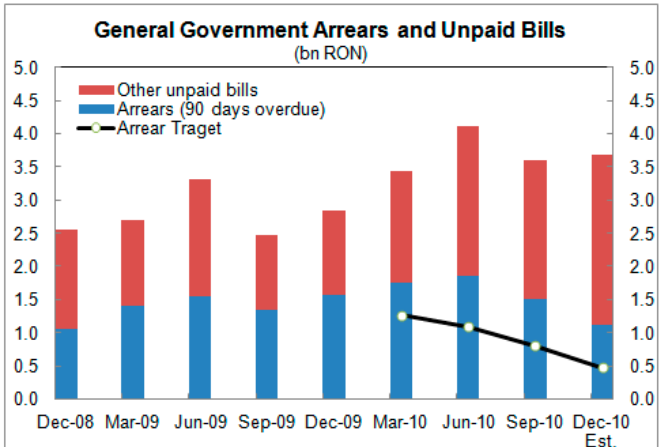
[2] Under Eurostat rules, an SOE must be included as part of the general government when more than half of its resources come from the state over a three year period. Several Romanian firms fall within this threshold and will be folded into the general government statistics in the course of 2011.

[3] According to a recent World Bank study conducted with PricewaterhouseCoopers, Romania ranks 151st out of 183 countries in terms of the ease of paying taxes, and 182nd in the number of payments required. See *Paying Taxes 2011: The Global Picture,* Washington, DC: The World Bank, 2010.

[4] Indirect audit methods are crucial step toward improving tax administration. Among other things, they should help with the new initiative on high net wealth individual taxation.

an increased VAT mandatory threshold of €50,000 while instituting simplified taxation for taxpayers under the threshold (structural benchmark, end-June 2011).

19. **On the expenditure side, improving expenditure efficiency and implementing a comprehensive solution to payments arrears are priorities**. By end-2010, central government and social security sector arrears had declined to near zero. On the local level, arrears have fallen below 0.2 percent of GDP and should continue declining with new legislation (effective January 2011) tightening local government financial management. To assess their full extent, a stocktaking of arrears and unpaid bills as of end-2010 will be conducted for the entire general government as well as SOEs and an action plan prepared by end-April 2011 (structural benchmark), after which payments will not be authorized for unregistered bills.[5] Central government and social security arrears will be fully eliminated during the program. To avoid future general government arrears, the authorities will also implement further health sector reforms (¶19) to reduce overdue payments and bring spending into line with budgetary allocations and complete on-going integration of accounting and Treasury payment systems (LOI ¶10) to better control expenditure commitments. During the new program, the deadline for payments will be reduced from the current 90 days to, in most cases, 30 days in line with new EU requirements. More broadly, the new program will make use of the recent functional expenditure reviews conducted by the World Bank (with EU support) to develop measures to improve expenditure efficiency. Beyond the general government, SOE reforms (¶24-25) will include comprehensive plans to reduce their arrears (via payments, liquidations, use of privatization proceeds, and/or debt restructuring).



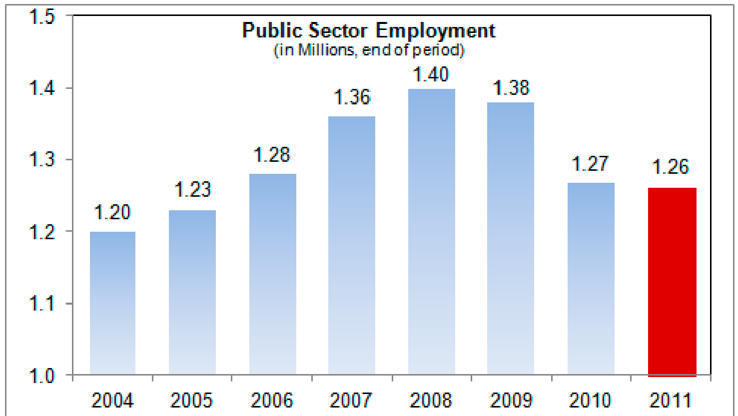
Source: Romania Authorities; Staff Estimates.

20. **Health care reforms will be critical to safeguarding fiscal consolidation.** Significant spending pressures have been generated in recent years by a fundamental mismatch between the entitlements for medical care and the resources available from the budget, contributing to arrears accumulation. Measures under the new program include: reforming the government-insured benefits package to exclude coverage of costly nonessential services; introducing a "money follows the patient" mechanism; using generic rather than brand drugs wherever possible; and reducing excess public sector hospital beds

[5] For local government SOEs, the stocktaking of arrears and unpaid bills as of end-December will be completed by end-June 2011.

with a view to reaching the EU average by 2013. The authorities are also advancing on the introduction of national health cards, electronic patient records, and electronic prescriptions.

21. **Despite significant public employment reforms under the current program, additional measures are needed.** Public employment shrank from 1.4 to 1.3 million people during 2010, with the largest declines in local governments and the education sector, as standard norms for local government personnel were implemented and student-teacher ratios moved closer to the EU average. However, further employment rationalization in the context of recent World Bank functional reviews is needed, especially given that the new unified wage scheme will only be fully effective over time.



Source: Ministry of Public Finanace; Staff Estimates.

22. **Public investment policies require significant reforms to increase efficiency and enhance the absorption of EU structural funds.** Romania spends a large share of its GDP on public investment (averaging over 6 percent of GDP in recent years), but capital spending has been plagued by inefficiency and under 3 percent of the €19 billion in available EU structural funds have been utilized. To better coordinate EU funds absorption, the EU funds unit will be moved from the Ministry of Public Finance (MOPF) to the Prime Minister's office. Measures to improve capital budgeting and project implementation (LOI ¶13) include comprehensive review, evaluation, and prioritization of projects within the existing investment portfolio; focusing on those where funding can be fully secured within a medium-term horizon (e.g., 3–5 years); and discontinuing low priority and non-performing projects. A final report and action plan will be produced by end-September 2011 (structural benchmark).

23. **The fiscal financing strategy will focus on moving away from multilateral budgetary support to full reliance on financial markets.** The recently prepared debt management strategy aims at extending the maturity of domestic debt, building the yield curve, and consolidating financial buffers. The authorities have made progress in recent months in building the domestic yield curve, and their euro medium-term notes program for regular debt financing in the Eurobond market is underway. Financing buffers will be brought to around four months of financing needs in 2011 and maintained at that level. A formal review of the government's debt management strategy, with the assistance of IMF staff, the EC, and the World Bank, will also be conducted in 2011.

D. Structural Reforms

State-Owned Enterprises

24. **SOEs constitute a significant fiscal burden and constrain private sector growth** (Box 2). Romania's post-communist privatization process has stalled in recent years, leaving inefficient state firms dominant in key economic sectors, such as energy and transportation. SOEs receive budgetary subsidies equivalent to around ½ percent of GDP annually and many generate considerable operating losses.[6] SOEs have accumulated arrears of around 4 percent of GDP to private sector firms and other public sector entities, damaging their financial health, reducing investment, and job creation. Moreover, inefficient operations and poor quality service of SOEs increase operating costs of private firms and create a barrier to augmenting exports and investments.

25. **To generate higher sustainable growth, the new program aims at deep-rooted SOE reform** (LOI ¶23). Action plans for key firms will classify them as in line for liquidation, privatization, or restructuring, and will contain concrete arrears-reducing strategies (structural benchmark, end-April 2011). Major financial and operational indicators of all SOEs (at central and local government levels) will be regularly reported to the MOPF. Governance issues will be addressed via regular independent external audits and by moving financial control of SOEs from line ministries to the MOPF.

26. **Reforms will focus on the energy and transport sectors, where regulatory and pricing issues, combined with the dominance of SOEs, drag down economic growth.** The energy and transport sectors include most of the largest SOEs (including the largest loss-makers and those with the largest arrears). Moreover, these sectors constitute key bottlenecks for accelerating GDP growth and for EU funds absorption.

- ***In the energy sector***, the authorities will restore the energy regulator's full operational and financial autonomy, and will phase out regulated prices in electricity and gas, while protecting vulnerable groups. Minority and/or strategic private investors will be brought into key energy firms, including Transelectrica, Transgaz, Romgaz, and Petrom,[7] as well as firms slated to be included in the two "national champion" companies (whose creation, in staff's view would compromise the viability of "good" energy assets by combining them with undesirable ones).[8] Unprofitable coal companies will also continue to be

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[6] In 2010, the ten largest loss-making SOEs lost an estimated 1.1 percent of GDP in 2010.

[7] Petrom already has a private majority shareholder; the state would sell an additional tranche of some 10 percent.

[8] In 2010, the authorities launched a strategy to combine 21 existing state-owned energy production companies into two "national champion" firms. Among the concerns about such a strategy are the following: (i) it may

(continued)

downsized, with viable assets spun off. A similar strategy of separating viable assets will be followed for Termoelectrica.

- ***In the transport sector,*** passenger railway and infrastructure service will be restructured with reductions in coverage (closure of 1000 kms. of unfrequented railway lines by end-August), competitive tendering for public service and infrastructure maintenance, and a significant decrease in losses and arrears. Passenger railway and the Bucharest metro system are scheduled to improve cost recovery through higher tariffs. Strategic investors will be sought for the rail freight company (CFR Marfa) and the national air carrier (Tarom) (LOI ¶29).

create greater monopoly power within the Romanian market; (ii) the combination of profitable and loss-making firms may give rise to cross-subsidization, which is economically inefficient and may contravene EU regulations; and (iii) existing private minority shareholders in some energy firms have filed legal challenges to the mergers which may stall needed investment in the industry.

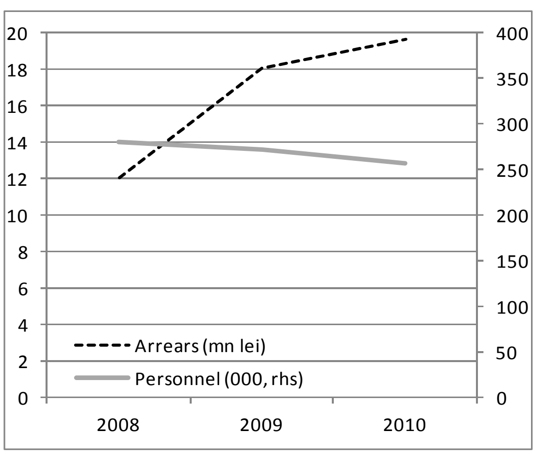
Box 2. State-Owned Enterprises in Romania: Taking Stock

The list of SOEs in Romania currently includes majority stakes in 154 companies, numerous minority stakes as well as around 25 autonomous institutions at the central government level alone. In addition, the portfolio of the privatization agency, AVAS, comprises 19 majority and about 350 minority stakes.

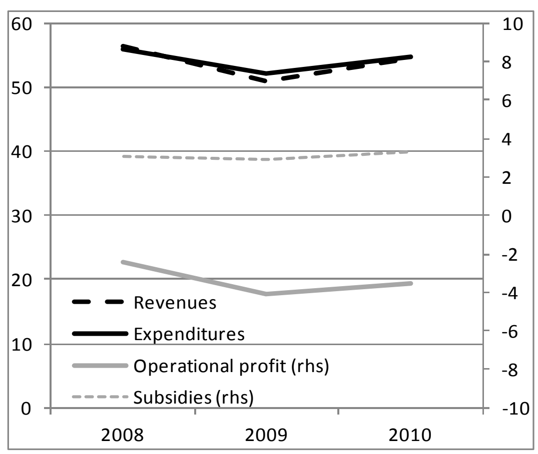
Detailed information is only available for the 154 companies. They employ more than 250,000 people, representing about 6 percent of all employees. The financial situation of these companies continues to deteriorate. Expenditures have fallen little despite cost-cutting measures, including a reduction of 28,000 employees since end-2008. In 2010, revenues increased, mainly based on increasing tariffs, including the installation of an electronic road toll system as well as higher tariffs for passenger rail. In the first three quarters of 2010, subsidies paid to these companies increased to around ½ percent of GDP. In addition, the stock of arrears has reached more than 4 percent of GDP.

Out of the 154 companies, 83 are held by the Ministry of Economy (especially in the energy sector) and 36 by the Ministry of Transport and Infrastructure. Operating losses are concentrated in the Ministry of Transport, Ministry of Agriculture, and Ministry of Communication. Subsidies are largely paid to companies under the control of the Ministry of Transport, Ministry of Economy, and Ministry of Agriculture. Basically, the entire stock of arrears has been accumulated by companies under the control of the Ministry of Economy (57 percent) and Ministry of Transport (42 percent).

154 SOEs:
Arrears and personnel, 2008–10



154 SOEs: Revenues, expenditures, subsidies & profit, 2008–10, bn. lei



Other reforms

27. **Social benefits and labor market reform will also play an important role in fiscal consolidation and improving growth.** Social benefits reforms (Box 1) have already yielded significant fiscal savings and are expected to improve incentives for work while providing support for the neediest. The authorities are nearing completing of a package of labor reforms to improve labor flexibility, increase labor force participation, and enhancing the representativity of collective bargaining while making the wage-setting process more flexible and allow for a better orientation of wage growth on productivity developments.

E. Financial Sector Policies

28. **Growth in non-performing loans slowed significantly in recent months and the banking sector remains liquid and well capitalized.** Non-performing loans, expected to peak in mid-2011, grew at a slower pace in the last quarter—rising to 11.9 percent[9] at end-December. Profitability turned negative by mid-2010, but the banking system retains adequate buffers with an average capital adequacy ratio of 14.7 percent at the end of 2010, while all banks remained above 11 percent (compared to the statutory minimum of 8 percent). As the economic recovery gains traction and loan loss provisions stabilize over the first half of 2011, the banking sector as a whole is expected to return to profitability. The parents of the largest foreign subsidiaries maintained aggregate exposures under the EBCI of 98 percent at end-January 2011, well above the July 2010 commitment of 95 percent.

Romanian Banking System - Core Indicators (in percent)

	Dec-08	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10
Capital adequacy						
Capital adequacy ratio	13.8	14.7	15.0	14.3	14.6	14.7
Leverage ratio[1/]	8.1	7.6	8.1	7.9	7.9	7.9
Asset quality						
Non-performing loan ratio[2/]	2.8	7.9	9.1	10.2	11.7	11.9
Loan loss ratio[3/]	6.5	15.3	17.2	17.8	20.2	20.8
Profitability						
Return on assets	1.6	0.2	0.5	-0.1	-0.2	-0.1
Return on equity	17.0	2.9	6.0	-1.6	-2.1	-1.0
Liquidity						
Loans to deposit ratio	122.0	112.8	113.2	117.5	116.3	113.5
Immediate liquidity ratio[4/]	34.4	35.3	37.1	35.9	36.7	37.9

Source: NBR.

1/Tier 1 capital/ total average net assets
2/Unadjusted exposure from loans and interest falling under "doubtful" and "loss" / total classified loans and interest, excluding off-balance sheet items.
3/Unadjusted exposure from loans classified as "loss" defined as past 90 days and/or initiation of legal preceeding/ total loans and interest, excluding off-balance sheet items.
4/ Cash, sight and term deposits with banks plus government securities free of pledge/ total liabilities

29. **Under the existing program, the authorities have undertaken significant reforms to strengthen the financial safety net.** However, there have been some delays in a reform to enable the Deposit Guarantee Fund (DGF) to finance the new bank resolution and

[9] Using the authorities preferred definition of non-performing loans based upon 90 days past due. The ratio based upon doubtful and loss which includes 60 days past due rose to 20.8 percent.

restructuring tools, which will be completed under the new program (now expected by end-June 2011). The NBR (in conjunction with the DGF) will also develop operating procedures and contingency plans for deploying the new resolution tools. The authorities will ensure that the DGF has ready access to liquidity to meet any potential shortfalls in funding and prepare joint procedures for deploying DGF funds in a bank resolution. The authorities will also review the DGF banking and the winding-up legislation to ensure their mutual consistency.

30. **Significant reform is also underway on the regulatory front.** Preparations have already begun to introduce International Financial Reporting Standards (IFRS) for the banking sector in 2012. By end-June 2011, the NBR will prepare proposals for prudential filters to allow for continued higher provisions to reflect the difficulties banks face in enforcing collateral in Romania. The NBR will continue to closely monitor credit conditions and assess the future evolution of NPLs and banks' profitability, to identify any potential further capital needs at individual institutions. It will also take action as needed to address the risks of lending in foreign exchange to un-hedged borrowers. The authorities are committed to refrain from promoting legislative initiatives (such as the current draft of the personal insolvency law or proposals for the debt collecting law) which could undermine debt or discipline. The authorities will also ensure that the prudential treatment of debt for equity swaps does not result in a weakening of banks' financial positions, such that the value of equity is fully deducted from their own funds of credit institutions and the revenues obtained by releasing loan-loss provisions due to these operations are not taxed.

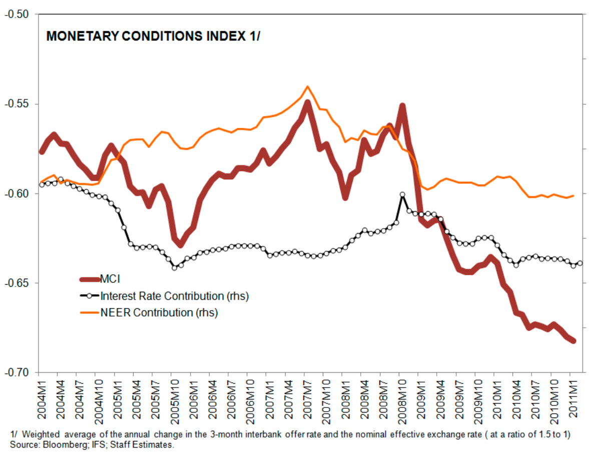
31. **The NBR will need to remain vigilant**. Some small- and medium-sized banks with high cost ratios, rising loan impairments and lower than average provisions, will continue to incur losses. Further capital injections may be required from existing shareholders or new investors in some cases, while losses could be absorbed from existing buffers in other cases. In March, the NBR will discuss an extension of the EBCI agreement with the largest foreign banks with a view toward continuing the stabilizing effects of the agreement.

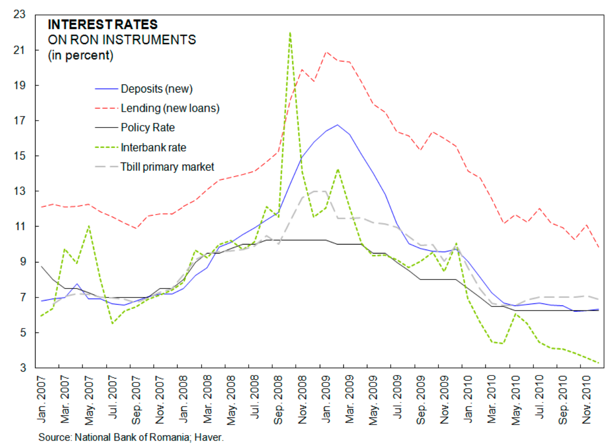
F. Monetary and Exchange Rate Policies

32. **The central bank has paused its monetary policy easing, pending a clear signal that inflationary pressures are easing.** After a 4 percentage point cumulative reduction in interest rates since early 2009, the NBR has left its key policy rate unchanged since July 2010 due to uncertainties associated with the VAT increase as well as food and fuel prices. The authorities believe that heightened vigilance will be needed to keep inflation expectations contained and stave off possible second-round inflationary effects. Reserve requirements have also remained unchanged since November 2009.[10]

[10] The reserve requirements are 25 percent for foreign currency liabilities and 15 percent for local currency liabilities, including both short-term and long-term (with clauses referring to early withdrawal, repayment and transfer).

33. **Despite the NBR's decision to pause further policy loosening, monetary conditions have moderated further, reflecting continued reductions in deposit and lending rates in the banking system.** Lending rates, however, did not fall by as much, as banks raised lending margins to cover increased provisioning due to continued increases in non-performing loans (NPLs). This policy easing was facilitated by the heavy reliance of the NBR on the overnight standing facility for absorbing liquidity at a rate well below the policy rate, though in recent weeks this excess liquidity seems to be disappearing.[11] The exchange rate has remained in a relatively narrow band (RON 4.1–4.3/€) in recent months, despite only modest NBR intervention in support of the currency. The real exchange rate assessment has not changed since the latest Article IV consultation (i.e., slight overvaluation).





34. **The program´s NFA target contemplates a gradual increase over 2011 parallel to augmenting gross reserves, mainly due to official inflows, and a relatively modest improvement in 2012.** This reserve accumulation should place the NBR in a position to effectively service the peak repayments to the Fund in 2013 while maintaining reserve coverage of at least 100 percent of annual short-term financial liabilities. A consultation clause is included in the program requiring that the authorities confer with staff if reserve losses exceed €2 billion in any 30 day period.[12]

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[11] Romania has a large spread for interbank market rates (400 basis points around the policy rate, where the upper bound is the Lombard rate and the lower bound is the overnight standing facility), allowing for greater fluctuations of the interbank rate. Heavy reliance on the overnight standing facility has allowed the interbank rate to come closer to the lower end of the band. In recent weeks, the gap between interbank rates and the policy rate has been narrowing, suggesting a tightening of liquidity conditions.

[12] The NFA target assumes the program is precautionary, and official inflows are represented accordingly.

Net Official Inflows (millions of Euro)

	2009	2010	2011	2012	2013
IMF	6,819	4,321	877	(1,530)	(4,766)
BOP	5,881	3,095	877	(1,530)	(4,766)
Budget	939	1,226	-	-	-
Non-IMF-Financing	2,100	3,650	3,246	-	-
EC	1,500	2,150	1,350	-	-
WB	300	-	700	-	-
EIB/EBRD/IFC	300	1,500	1,196	-	-

V. Program Modalities

A. Access

35. **Romania is not expected to face actual balance of payments financing needs in 2011 and 2012, though financing risks remain.** As described in ¶15, under staff's assumptions, private and non-program public flows should fully cover the current account deficit once multilateral disbursements under the existing program are completed. FDI should cover close to half of the current account deficit, with renewed private portfolio and banking inflows covering the rest.

36. **However, if downside financing and growth risks materialize, the authorities might need to draw under the new arrangement.** Under staff's stress scenario (Tables 7–8), higher perceived risks would reduce FDI and rollover rates on private sector external liabilities would drop below 100 percent as banks repatriate some resources (commitments under the EBCI will gradually decline) and corporations find less access to external financing.[13] A weaker euro area recovery would also dampen exports. Economic growth would fall by a cumulative 3 percentage points in 2011–12 compared to the baseline. Lower capital inflows would require additional external financing of €5 billion, which would be covered by disbursements from the Fund and the EU.

37. **The successor arrangement would begin on March 31, 2011, following completion of the seventh review and cancellation of the current SBA.** In order to provide a sufficient financing cushion against unforeseen shocks over the program period, the program is based on total support of €5.4 billion with precautionary support from the Fund (€3.6 billion), precautionary support from the European Union (€1.4 billion), and €0.4 billion from the World Bank. In addition, about €1.2 billion in incremental lending from the EBRD, EIB, and IFC is projected during the program period. Given Romania's cumulative use of Fund resources, the new program of SDR 3,090.6 million (300 percent of quota) entails exceptional access. Staff assesses that Romania meets the four criteria for

[13] Relative to the baseline, banks' and corporations' average rollover rates would decline by around 10 ppts.

exceptional access (Box 3) and considers that SBA terms are appropriate. Program resources would be made available at 131 percent of quota in 2011, 167 percent of quota in 2012 and 2 percent of quota in 2013. For the first year, disbursements would be 6 percent of quota at the approval of the program, followed by 3 equal installments (of 41.7 percent of quota) in the first three quarterly reviews.

Precautionary Financing (billion Euros)[1]

	2011	2012	2013
IMF	1.57	2.01	0.02
EC[2]	0.61	0.78	0.01
Total	2.18	2.79	0.03

[1] Under follow up arrangement.
[2] Exact EC financing amounts will be decided once a request for disbursement has been made.

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

38. **Romania's capacity to repay the Fund would remain strong.** Fund credit outstanding would peak in 2011 at 36.9 percent of gross reserves. Peak payments would be in 2013–14 at a still manageable 11.9 and 12.2 percent of gross reserves and around 9.0 and 8.4 percent of exports of goods and services (Table 13). While this exposure remains large, servicing risks are mitigated by the relatively low level of public debt. Direct public indebtedness is expected to remain under 37 percent of GDP, with public external debt peaking at around 16 percent of GDP in 2011 (Table 9). Total external debt is projected to increase to about 83 percent of GDP at end-2012, but the declining current account deficit and a return to economic growth would gradually reduce it to manageable levels in the medium term (Table 15). Romania's strong political commitment to the SBA program and its excellent track record servicing external obligations also provide comfort that it will fulfill its financial obligations to the Fund in a timely manner.

C. Program Monitoring and Conditionality

39. **The program will be monitored by quarterly reviews.** Table 3 sets out specific quarterly targets that are to be observed under the SBA for the overall general government balance, guarantees provided by the general government, the change in arrears for the central government and social security system, CPI inflation, and net foreign assets. In addition, there will be indicative targets on the current primary expenditure of the general government, and the operating balances and arrears of SOEs. One prior action and structural benchmarks are presented in Table 4. The first review should be completed by end-June 2011 (based on end-March 2011 targets), and the second review by end-September 2011 (based on end-June 2011 targets).

40. **Progress has been made by the NBR on the recommendations contained in the safeguards assessment performed under the May 2009 SBA**. To evaluate this progress, the National Bank's external auditors are authorized to provide IMF staff with all necessary information and to discuss directly any issues relevant to this process. The authorities also commit to receiving a safeguards mission and to provide that mission with all necessary information requested without delay. The safeguards assessment update should be completed by the time of the first review of the SBA (end-June, 2011).

Box 3. Exceptional Access Criteria

Staff's evaluation is that Romania continues to meet the four exceptional access criteria. Proposed access under the new SBA would equal €3.6 billion (SDR 3,090.6 million, 300 percent of quota). However, the overall access by Romania to the Fund's general resources (net of scheduled purchases) exceeds normal access, requiring evaluation under the exceptional access framework. In staff's view, Romania meets the four substantive exceptional access criteria:

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

  Romania does not face actual balance of payments pressures. However, it is exposed to risks of economic and financial disruptions in Europe. The realization of a stress scenario[14] could give rise to financing needs, which would imply cumulative access above the normal access limits.

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

  Public debt is low (33 percent of GDP) and is not expected to pose a risk under the program and in the medium term. Continued fiscal adjustment would set the public debt ratio firmly on a downward path, ensuring debt sustainability with a high probability. Barring unexpected events, potential contingent liabilities of the government would also be limited. Total external debt has risen to 75 percent of GDP in 2010 and is expected to peak at 79 percent in 2011. Starting from 2012, repayments to the Fund, a manageable current account deficit, and higher economic growth would gradually reduce the external debt in the medium-term.

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

  Romania has regained access to private capital markets and is expected to retain access while Fund resources are outstanding. Early in 2010, a €1 billion Eurobond issue was successfully placed and domestic issuance of euro-denominated instruments totaling €2.4 billion were placed in July and November. Starting from 2011, the government will initiate the medium-term notes (MTN) program which is expected to generate around €2 to €2.5 billion a year for the next four years. However, elevated risks in the euro area may hamper the projected inflows through the MTN program.

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

  The program has good prospects for success and will enhance Romania's economic sustainability. The authorities' performance during the current program lends confidence in their institutional and political capacity to continue implementing sound policies.

[14] The stress scenario involves reduced capitals inflows, and net exports resulting in lower growth, all of which together would create a financing gap in the balance of payments.

VI. Staff Appraisal

41. **Romania's economy has stabilized, and strong economic policies under the existing SBA have set the stage for renewed economic growth.** Exchange rate volatility has eased without significant NBR intervention and country risk (as measured by CDS spreads) has lessened significantly. The current account deficit has been reduced sharply and exports are booming. Banking sector difficulties have been largely avoided and massive capital outflows have been forestalled. After significant challenges early in the program, government revenues are now overperforming, putting the government on track to reach its 2011 fiscal deficit without significant additional measures. While the economic recovery was delayed by weak domestic demand (in part due to the needed fiscal consolidation), GDP growth has now resumed and should gain strength in the coming quarters.

42. **While fiscal adjustment measures already taken have placed Romania on a path toward its medium-term fiscal objectives, significant fiscal challenges remain:**

- The necessary revenue measures to address massive fiscal imbalances have left the country with high rates collected on a relatively narrow tax base, due to tax evasion, a large informal sector, and inefficiencies in tax administration. Over time, tax administration improvements must be implemented to allow for a gradual reduction in rates as the tax base expands.
- Temporary cuts in public sector wages and across-the-board cuts in public employment were essential components in the adjustment strategy, but they must give way in the medium-term to application of the new unified wage system, together with comprehensive efforts to improve government efficiency based on the recent functional reviews.
- Significant pressures remain in the health care sector, where further reforms are required to provide for efficient services within budget constraints and to avoid further arrears accumulation.
- Successful efforts to clear payments arrears in the central government and social security system must be expanded to tackling the persistent arrears problems in local governments and public enterprises.
- A large share of GDP is devoted to public investment in Romania, but the results are poor. Many projects are left uncompleted for years, completed projects are often overly expensive, and scarce domestic resources are used while grant money from the EU remains largely untapped.

These fiscal reforms are more complex than tax increases or broad expenditure cuts, making implementation of planned measures challenging but nonetheless essential.

43. **Sustainable economic growth will require reforms in key economic sectors that are currently plagued by underperforming state firms functioning in conditions where**

market forces are not fully operational. The new program includes urgently needed reforms in the energy market and transport sectors aimed at an improved pricing framework and providing more independent and transparent regulation. An enhanced market environment in these sectors is a precondition for attracting private investment and managerial know-how, including in the search for strategic investors for SOEs. Staff encourages the authorities to reconsider their plan to form two national energy "champions" (combining viable and less efficient companies) in favor of a more aggressive privatization strategy for current firms. The authorities should also forcefully re-launch their privatization strategy outside the energy sector as well, selling majority stakes where appropriate. For those firms remaining under state control, enhanced monitoring and strengthened governance are also key steps to reverse operating losses and mounting arrears, which are a major fiscal and economic drag. The staff supports the authorities' intention to reforms the labor market to ensure that the labor force is productive, flexible, and competitive while protecting workers and their collective bargaining rights.

44. **The authorities' strongly proactive stance in banking supervision has played a vital role in forestalling banking sector difficulties, but continued vigilance is needed.** With NPLs expected to continue to rise for at least several months more—risks remain. These may need to be watched particularly carefully in smaller locally-owned banks without the prospect of parent support. The authorities should continue to elaborate detailed contingency plans in case of difficulties, as well as to develop procedures to use their newly enhanced bank resolution powers so as to be fully prepared in the event a bank was to face problems. Staff supports the authorities' intention to extend the EBCI agreement while gradually reducing banks' exposure commitments. Both the authorities and the banks have noted benefits from the initiative begun in Vienna in March 2009.

45. **Monetary policy has appropriately balanced the need for a firm stance against inflation with the desire to support economic recovery.** However, unforeseen pressures in food and energy prices, as well as needed changes in administered prices, may put the 2011 inflation target at risk. The authorities should step-up open market operations to mop up excess liquidity and bring interbank interest rates more in line with the policy rate. Once interbank interest rates are more in line with the policy rate, the NBR may see room for some additional rate cuts or reductions in reserve requirements if second round inflation effects remain absent. However, some differential between reserve requirement in local currency and FX should be maintained to help discourage excessive FX credit growth. The NBR should also avoid letting considerations of its own balance sheet unduly affect its monetary policy decisions.

46. **On the basis of Romania's performance under the SBA, staff supports the authorities' requests for completion of the seventh review and for approval of a new arrangement.** All seventh review performance criteria were met, with the exception of the end-December 2010 criterion on the general government arrears, for which a waiver has already been approved in the context of the last review. Progress on structural benchmarks

has also been sufficient to merit completion of the review. Staff views the new SBA as an effective mechanism to insure against possible future shocks while aiding the authorities in maintaining policy discipline in their efforts to reach their fiscal consolidation objectives while undertaking deeper economic reforms. Given a normalization of Romania's access to external financing in private markets, in the absence of further shocks the authorities would not likely need to draw under the arrangement despite repayments under the existing arrangement which begin in 2012.

Box 4. The New Stand-By Arrangement

Access: SDR 3,090.6 million, 300 percent of quota.

Length: 24 months.

Phasing: Resources will be made available at 131 percent of quota in 2011 and 169 percent of quota in 2012 and 13. For the first year, disbursements would be 6 percent of quota upon approval of the arrangement followed by 3 equal installments (of 41.7 percent of quota) beginning with the first quarterly review (scheduled for June 2011).

Conditionality

- ***Quantitative Performance Criteria***
  - A floor on the change in net foreign assets
  - A ceiling on central government and social security domestic arrears
  - A floor on the overall general government cash balance
  - A ceiling on general government guarantees
  - Non-accumulation of external debt arrears

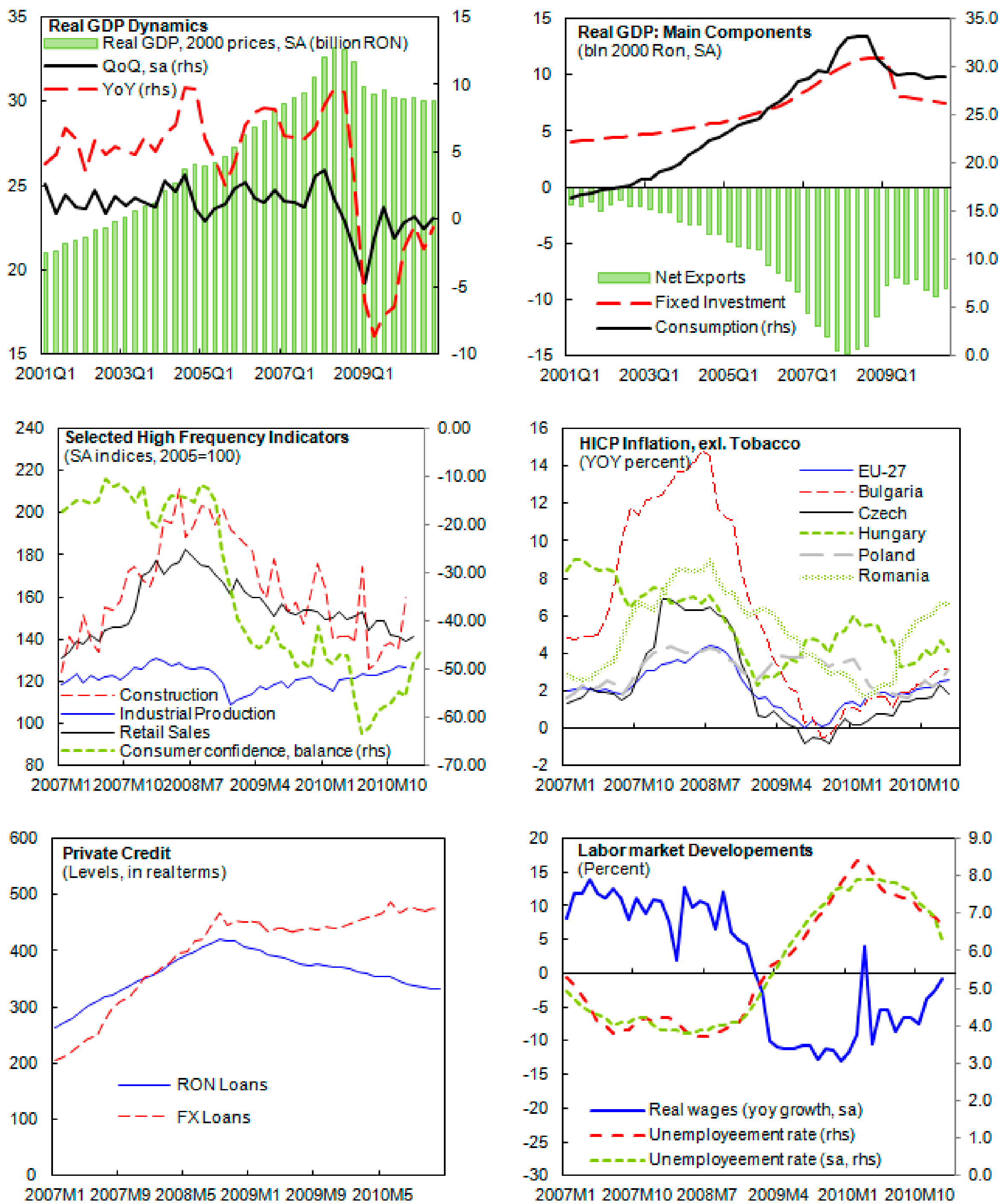
- ***Quantitative Indicative Targets***
  - A ceiling on general government current primary spending
  - A ceiling on local government domestic arrears
  - A floor on the operating balance and arrears of the key loss-making SOEs

- ***A consultation band around the 12-month rate of inflation of consumer prices***

- ***Prior Action***
  - Passage of indirect audit methods

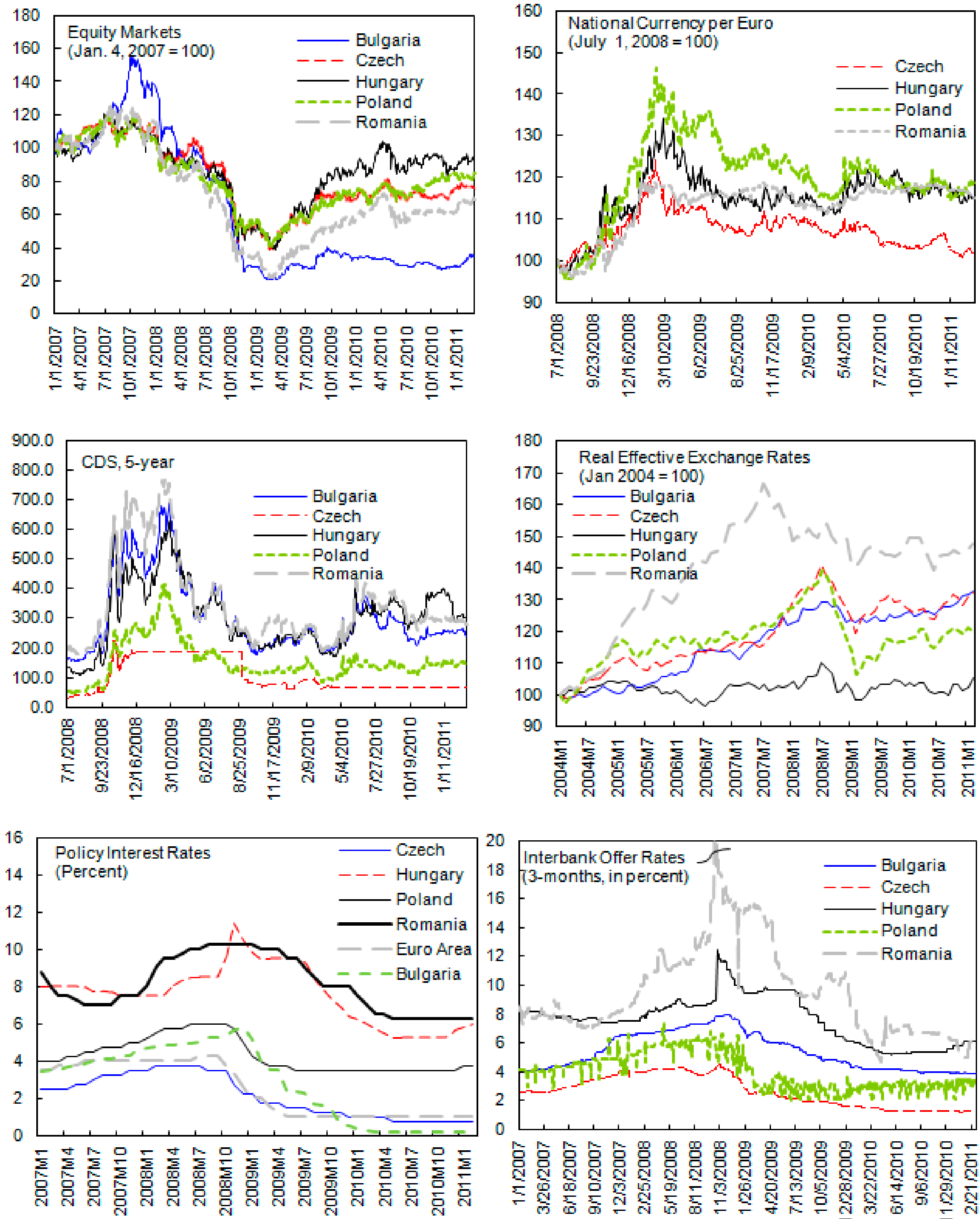
- ***Structural Benchmarks***
  - Completion of a stocktaking of arrears and unpaid bills as of end-December 2010 for the entire general government and SOEs *April 30, 2011*
  - Preparation of strategic action plans for key SOEs (as specified in TMU) *April 30, 2011*
  - Elimination of the legal basis of *stimulente* funds, effective January 1, 2012 *June 30, 2011*
  - Introduction of a simplified taxation system for smaller taxpayers under the threshold with help from the IMF and EC, while requesting a shift in the VAT mandatory threshold from the EU Council of Ministers to €50,000 *June 30, 2011*
  - Completion of a comprehensive review of the existing investment portfolio, which will prioritize and evaluate existing projects to focus on those where funding can be fully secured, examine the viability of old projects, with low priority and unviable ones discontinued, and production of a final report and an action plan *September 30, 2011*

Figure 1. Romania: Recent Economic Trends



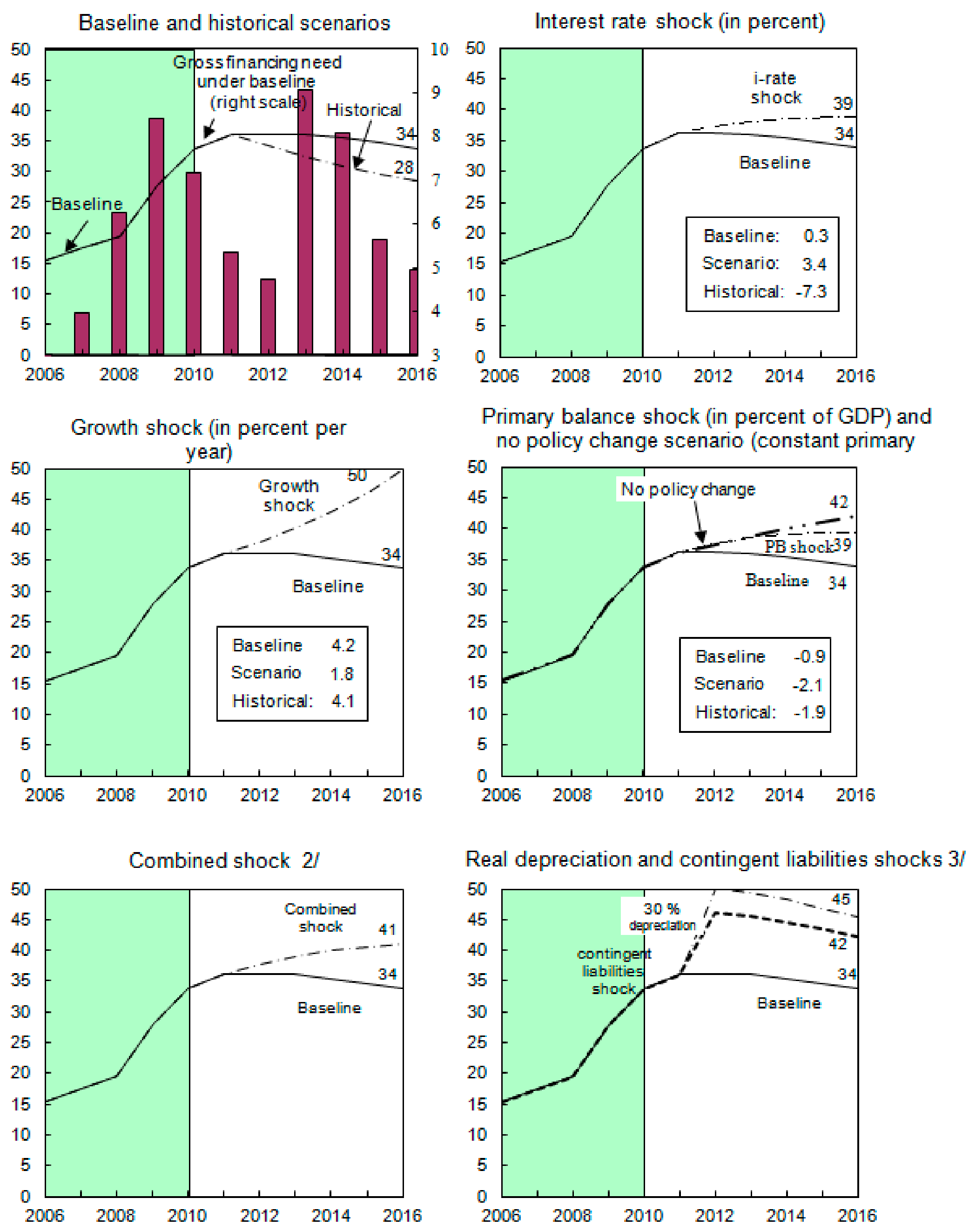
Source: Haver; Staff Estimates.

Figure 2. Romania: Financial Developments



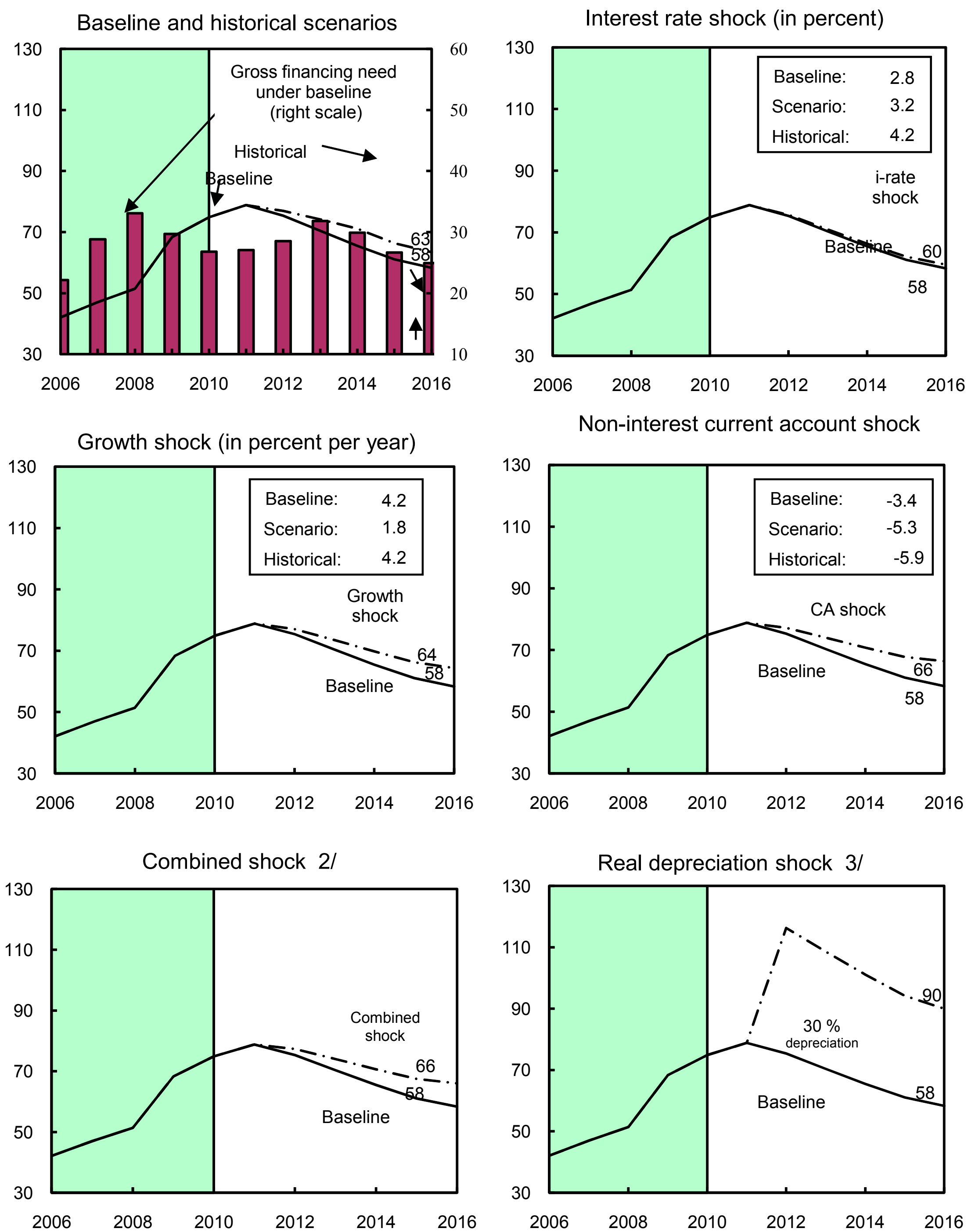
Source: Bloomberg; Haver.

Figure 3. Romania: Public Debt Sustainability: Bound Tests 1/
(Public debt in percent of GDP)



Sources: International Monetary Fund, country desk data, and staff estimates.
1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.
2/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and primary balance.
3/ One-time real depreciation of 30 percent and 10 percent of GDP shock to contingent liabilities occur in 2010, with real depreciation defined as nominal depreciation (measured by percentage fall in dollar value of local currency) minus domestic inflation (based on GDP deflator).

Figure 4. Romania: External Debt Sustainability: Bound Tests 1/
(External debt in percent of GDP)



Sources: International Monetary Fund, Country desk data, and staff estimates.
1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.
2/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.
3/ One-time real depreciation of 30 percent occurs in 2010.

Table 1. Romania: Quantitative Program Targets for Seventh Review

	2008	2009				2010					2011		
	Dec	March	June	Sept	Dec	March	June	Sept	Dec		January		March
	Actual	Actual	Actual	Actual	Actual	Actual	Actual	Actual	Prog.	Actual	Prog.	Actual	Indicative
I. Quantitative Performance Criteria													
1. Change in net foreign assets (mln euros) 1/ 2/	25,532	-3,468	-5,119	-4,566	-4,874	779	-509	-318	-2,000	-750	0	855	350
2. Floor on general government overall balance (mln lei) 3/ 4/ 5/	-24,655	-8,300	-14,456	-25,563	-36,101	-8,422	-18,015	23,732	-34,054	-33,621	…	…	-6,300
3. Stock in general government arrears (bn lei)	1.06	1.41	1.55	1.4	1.50	1.76	1.8	1.57	0.48	1.13	…	…	0
4. Ceiling on general government guarantees issued since start of program (face value, bn lei)	…	…	0.02	0.8	2.2	4.6	5.5	6.5	12.0	7.6	…	…	12.0
II. Continuous Performance Criterion													
5. Nonaccumulation of external debt arrears	0	0	0	0	0	0	0	0	0	0	0	0	0
III. Inflation Consultation													
6. 12-month rate of inflation in consumer prices													
Outer band (upper limit)	…	…	8.4	7.7	6.5	6.5	6.0	10.0	10.0	…	…	…	9.0
Inner band (upper limit)	…	…	7.4	6.7	5.5	5.5	5.0	9.0	9.0	…	…	…	8.0
Actual/*Center point*	6.3	6.7	5.9	4.8	4.7	4.2	4.4	7.8	8.0	8.0	…	…	*7.0*
Inner band (lower limit)	…	…	5.4	4.7	3.5	3.5	3.0	7.0	7.0	…	…	…	6.0
Outer band (lower limit)	…	…	4.4	3.7	2.5	2.5	2.0	6.0	6.0	…	…	…	5.0
IV. Indicative Target													
7. General government current primary spending (excl. EU funds and social assistance, mln lei) 3/	92,327	22,149	43,238	63,878	85,637	32,749	66,124	98,721	131,500	131,938	…	…	32,000
8. Operating balance (earnings before interest and tax) net of subsidies of 10 SOEs, defined in TMU (mln. lei) 3/						-1,081	-2,333	-3,801	-4,000	-5,542	…	…	-750
Memorandum Item:													
Revenue of general government, net of EU funds (mln. lei) 3/	…	…	…	…	151,508	36,355	74,669	116,091	157,950	159,141	…	…	40,100

1/ The December 2008 figure is a stock.
2/ Performance criterion for January 2011 and indicative target for March 2011 are relative to December 2010 target.
3/ Cumulative figure during calendar year (e.g. March 2011 figure is cumulative from January 1, 2011).
4/ In accordance with TMU, the end-September and end-December program targets were adjusted from the original target of -28,200 and -34,650 by one-half of the revenue over-performance.
5/ The target for March 2011 can be adjusted with higher or lower capital spending as defined in TMU.

Table 2. Romania: Performance for Seventh Review

Measure	Target Date	Comment
Quantitative performance criteria		
1. Floor on general government overall balance	December 31, 2010	Met
2. Ceiling on general government guarantees	December 31, 2010	Met
3. Ceiling on general government domestic arrears	December 31, 2010	Missed
4. Non-accumulation of external debt arrears	December 31, 2010	Met
5. Floor on net foreign assets	January 31, 2011	Met
Quantitative Indicative Target		
1. Ceiling on general government current primary spending	December 31, 2010	Missed
2. Floor on the operating balance of ten largest loss-making SOEs	December 31, 2010	Missed
3. Floor on net foreign assets	March 31, 2011	Likely to be met
Inflation consultation band		
Inner band	December 31, 2010	Met
Outer band	December 31, 2010	Met
Structural benchmarks		
1. Parliamentary ratification of amendments to the bank resolution framework	December 1, 2010	Partially met
2. Reform tax administration methodology for high net wealth individuals	December 31, 2010	Met
3. First phase to integrate the accounting reporting system with the Treasury payment system	March 15, 2011	Met
4. Amend legislation to allow the use of the deposit guarantee fund resources to facilitate bank restructuring, including purchase and assumption transactions	March 15, 2011	Likely to be missed, reset for July 31, 2011

Table 3. Romania: Quantitative Program Targets for New Program

	2010	2011			
	Dec	March	June	Sept	Dec
	Actual	Prog.	Prog.	Indicative	Indicative
I. Quantitative Performance Criteria					
1. Change in net foreign assets (mln euros) 1/ 2/	20,026	250	250	500	500
2. Floor on general government overall balance (mln lei) 3/ 4/	-33,621	-6,300	-12,600	-17,150	-23,953
3. Stock of central government and social security arrears (bn lei)	0.19	0.20	0.20	0.15	0.10
4. Ceiling on general government guarantees issued since end-2008 (face value, bn lei)	12.0	14.0	14.0	14.0	14.0
II. Continuous Performance Criterion					
5. Nonaccumulation of external debt arrears	0	0	0	0	0
III. Inflation Consultation					
6. 12-month rate of inflation in consumer prices					
Outer band (upper limit)	…	9.0	8.8	6.2	5.7
Inner band (upper limit)	…	8.0	7.8	5.2	4.7
Actual/*Center point*	8.0	*7.0*	*6.8*	*4.2*	*3.7*
Inner band (lower limit)	…	6.0	5.8	3.2	2.7
Outer band (lower limit)	…	5.0	4.8	2.2	1.7
IV. Indicative Target					
7. General government current primary spending (excl. EU funds and social assistance, mln lei) 3/	131,938	32,000	64,000	95,600	128,550
8. Operating balance (earnings before interest and tax) net of subsidies of key SOEs (as defined in TMU (bn. lei)) 3/	-6.5	-1.7	-2.7	-3.6	-4.0
9. Stock of arrears of key SOEs (as defined in TMU (bn. lei))	18.8	19.5	19.5	19.0	18.0
10. Stock of local government arrears (bn lei)	0.91	0.95	0.90	0.85	0.80
Memorandum Item:					
Revenue of general government, net of EU funds (mln. lei) 3/	159,141	40,100	82,250	127,000	171,575

1/ The end-December 2010 figure is a stock.
2/ Cumulative flows relative to end-December 2010 stock.
3/ Cumulative figure during calendar year (e.g. March 2011 figure is cumulative from January 1, 2011).
4/ The target for March 2011 can be adjusted with higher or lower capital spending as defined in TMU.

Table 4. Romania: Conditionality for New Program

Measure	Target Date	Comment
Prior action		
The government decision on indirect audit methods will be passed (¶12).		
Quantitative performance criteria		
1. Floor on general government overall balance	Quarterly	
2. Ceiling on general government guarantees	Quarterly	
3. Ceiling on central government and social security domestic arrears	Quarterly	
4. Non-accumulation of external debt arrears	Continuous	
5. Floor on net foreign assets	Quarterly	
Quantitative Indicative Target		
1. Ceiling on general government current primary spending	Quarterly	
2 Ceiling on local government domestic arrears	Quarterly	
3. Floor on the operating balance and arrears of key loss-making SOEs	Quarterly	
Inflation consultation band		
Inner band	Quarterly	
Outer band	Quarterly	
Structural benchmarks		
1. Completion of a stocktaking of arrears and unpaid bills as of end-December 2010 for the entire general government and SOEs (¶10).	April 30, 2011	
2. Preparation of strategic action plans for key SOEs (as specified in TMU) (¶23).	April 30, 2011	
3. Introduction of a simplified taxation system for smaller taxpayers under the threshold with help from the IMF and EC, while requesting a shift in the VAT mandatory threshold from the EU Council of Ministers to €50,000 (¶12).	June 30, 2011	
4. Eliminate by government ordinance the legal basis of *stimulente* funds, effective January 1, 2012 (¶8).	June 30, 2011	
5. Amend legislation to allow the use of the deposit guarantee fund resources to facilitate bank restructuring, including purchase and assumption transactions (¶4).	July 31, 2011	
6. Completion of a comprehensive review of the existing investment portfolio, which will prioritize and evaluate existing projects to focus on those where funding can be fully secured, examine the viability of old projects, with low priority and unviable ones discontinued, and production of a final report and an action plan (¶13).	September 30, 2011	

Table 5. Romania: Selected Economic and Social Indicators, 2007–12

	2007	2008	2009	2010 Prog.	2010 Est.	2011 Proj.	2012 Proj.
Output and prices			(Annual percentage change)				
Real GDP	6.3	7.3	-7.1	-1.9	-1.3	1.5	4.4
Domestic demand	14.2	7.3	-12.9	-3.9	-1.0	1.2	4.3
Net exports (contribution)	-9.6	-1.0	7.5	2.2	-0.2	0.2	-0.1
Consumer price index (CPI, average)	4.8	7.9	5.6	6.1	6.1	5.4	3.4
Consumer price index (CPI, end of period)	6.6	6.3	4.7	8.2	8.0	3.7	3.0
Unemployment rate (average)	4.3	4.0	6.3	7.8	7.6	6.6	5.8
Nominal wages	22.6	23.6	8.4	2.0	2.6	4.7	6.7
Saving and Investment			(In percent of GDP)				
Gross domestic investment	31.0	31.3	25.3	27.8	26.5	24.6	25.2
Gross national savings	17.6	19.7	21.1	22.3	22.2	19.5	20.1
General government finances							
Revenue	32.3	32.2	31.4	32.7	32.8	33.3	33.7
Expenditure	35.4	37.0	38.7	39.5	39.4	37.7	36.7
Fiscal balance	-3.1	-4.8	-7.3	-6.8	-6.5	-4.4	-3.0
Privatization proceeds	0.1	0.1	0.0	0.0	0.0	0.0	0.0
External financing	0.1	0.4	2.9	4.6	4.6	2.8	0.7
Domestic financing	2.9	4.3	4.5	2.2	1.9	1.6	2.3
Structural fiscal balance 1/	-5.8	-8.5	-7.0	-4.4	-4.9	-2.4	-1.6
Gross public debt (direct debt only)	17.5	19.5	27.4	33.9	33.2	36.1	36.2
Money and credit			(Annual percentage change)				
Broad money (M3)	33.7	17.5	9.0	4.3	6.9	10.3	14.1
Credit to private sector	60.4	33.7	0.9	4.1	4.7	7.7	8.7
Interest rates, eop			(In percent)				
Euribor, six-months	4.79	3.52	4.52	-	1.23	-	-
NBR policy rate	7.50	10.25	8.00	-	6.25	-	-
NBR lending rate (Lombard)	12.00	14.25	12.00	-	10.25	-	-
Interbank offer rate (1 week)	7.14	12.72	10.69	-	3.63	-	-
Balance of payments			(In percent of GDP)				
Current account balance	-13.4	-11.6	-4.2	-5.5	-4.2	-5.0	-5.1
Merchandise trade balance	-14.3	-13.7	-5.8	-5.4	-4.8	-5.1	-4.7
Capital and financial account balance	17.6	12.7	-2.5	2.1	1.1	5.3	8.4
Foreign direct investment balance	5.7	6.7	3.0	2.4	2.0	2.9	2.9
International investment position	-43.5	-49.4	-62.7	-61.3	-70.8	-75.3	-72.6
Gross official reserves	23.0	20.2	26.3	27.8	29.5	31.7	30.9
Gross external debt	47.0	51.4	68.3	73.9	74.5	78.9	75.4
Exchange rates							
Lei per euro (end of period)	3.5	4.0	4.2	-	4.3	-	-
Lei per euro (average)	3.3	3.7	4.2	-	4.2	-	-
Real effective exchange rate							
CPI based (percentage change)	8.4	-5.0	-7.5	-	1.8	-	-
GDP deflator based (percentage change)	17.3	1.5	-8.8	-	0.2	-	-
Memorandum Items:							
Nominal GDP (in bn RON)	416.0	514.7	498.0	511.6	513.6	542.0	590.2

Social and Other Indicators

GDP per capita (current US$, 2009): $7,500; **GDP per capita, PPP** (current international $, 2009): $14,198

Unemployment rate: 6.8% (December 2010)

Poverty rate: 5.7% (2008)

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

1/ Actual fiscal balance adjusted for the automatic effects of the business cycle.

Table 6: Romania: Macroeconomic Framework, Current Policies, 2008–2016

	2008	2009	2010 Est.	2011 Proj.	2012 Proj.	2013 Proj.	2014 Proj.	2015 Proj.	2016 Proj.
GDP and prices (annual percent change)									
Real GDP	7.3	-7.1	-1.3	1.5	4.4	4.3	4.2	4.1	4.0
Real domestic demand	7.3	-12.9	-1.0	1.2	4.3	4.5	4.4	4.2	4.1
GDP deflator	15.2	4.1	4.5	4.7	4.3	4.6	4.9	5.1	5.2
Domestic demand deflator	14.4	4.2	3.5	4.2	4.2	4.2	4.4	4.6	4.7
Consumer price index (CPI, average)	7.9	5.6	6.1	5.4	3.4	3.0	3.0	3.0	3.0
Consumer price index (CPI, end of period)	6.3	4.7	8.0	3.7	3.0	3.0	3.0	3.0	3.0
Nominal wages	23.6	8.4	2.6	4.7	6.7	6.9	7.0	8.0	8.0
Real effective exchange rate, CPI based	-5.0	-7.5	1.9	-0.2	3.3	3.0	3.2	2.5	2.6
Real effective exchange rate, GDP deflator based	1.5	-8.8	0.4	-0.9	4.1	4.5	5.1	4.8	4.9
Monetary aggregates (annual percent change)									
Broad money	17.5	9.0	6.9	10.3	14.1	14.5	14.9	16.0	16.0
Domestic credit	33.7	0.9	4.7	7.7	8.7	10.4	10.9	11.4	11.8
Saving and investment (in percent of GDP)									
Foreign saving	11.6	4.2	4.2	5.0	5.1	5.2	5.2	5.1	5.0
Gross national saving	19.7	21.1	22.2	19.5	20.1	20.8	21.5	22.0	22.7
Government	1.5	-0.8	0.8	2.7	4.5	5.4	6.0	5.6	5.2
Private	18.2	21.9	21.4	16.8	15.6	15.4	15.5	16.4	17.5
Gross domestic investment	31.3	25.3	26.4	24.6	25.2	26.0	26.7	27.1	27.6
Government	6.3	6.5	7.3	7.1	7.5	8.3	8.5	7.8	7.3
Private	25.0	18.8	19.1	17.4	17.7	17.8	18.2	19.3	20.4
General government (in percent of GDP)									
Revenue	32.2	31.4	32.8	33.3	33.7	33.5	33.2	32.4	31.7
Tax revenue	18.4	17.8	18.1	18.9	18.9	18.7	18.6	18.5	18.5
Non-Tax revenue	3.1	2.9	3.9	3.5	3.6	3.4	3.4	3.4	3.4
Grants	0.9	1.0	1.8	1.6	2.4	2.7	2.8	2.2	1.8
Expenditure	37.0	38.7	39.4	37.7	36.7	36.4	35.7	34.7	33.9
Fiscal balance	-4.8	-7.3	-6.5	-4.4	-3.0	-2.9	-2.5	-2.3	-2.1
Structural fiscal balance 1/	-8.5	-7.0	-4.9	-2.4	-1.6	-2.0	-2.0	-2.1	-2.1
Gross public debt (direct debt only)	19.5	27.4	33.2	36.1	36.2	36.0	35.5	34.7	33.8
Balance of payments (in percent of GDP)									
Current account	-11.6	-4.2	-4.2	-5.0	-5.1	-5.2	-5.2	-5.1	-5.0
Trade balance	-13.8	-5.8	-4.8	-5.0	-4.7	-4.6	-4.2	-3.7	-3.2
Services balance	0.5	-0.6	-0.6	-0.5	-0.5	-0.5	-0.4	-0.3	-0.2
Income balance	-2.7	-1.3	-1.6	-2.2	-2.3	-2.3	-2.4	-2.5	-2.6
Transfers balance	4.3	3.5	2.8	2.8	2.3	2.1	2.0	1.8	1.7
Capital and financial account balance	12.8	-1.9	1.1	5.3	8.4	8.6	8.3	5.6	6.1
Foreign direct investment, balance	6.7	3.0	2.0	2.9	2.9	2.9	3.0	3.0	3.0
Memorandum items:									
Gross international reserves (in billions of euros)	28.3	30.9	36.0	40.4	43.4	44.3	45.1	44.6	47.3
Gross international reserves (in months of next year's imports)	7.8	7.4	7.8	8.0	7.8	7.2	6.7	6.1	6.1
International investment position (in percent of GDP)	-49.4	-62.7	-70.8	-75.3	-72.6	-73.0	-74.2	-72.6	-69.5
External debt (in percent of GDP)	51.4	68.3	74.5	78.9	75.4	70.4	65.5	61.1	58.4
Short-term external debt (in percent of GDP)	14.7	12.4	15.4	15.9	15.3	14.8	14.2	13.7	13.3
Export volume (percent change)	8.3	-5.3	24.5	7.2	7.6	8.1	8.3	8.3	8.3
Import volume (percent change)	7.9	-20.9	9.0	6.7	7.5	8.5	8.4	8.3	8.3
Terms of trade (percent change)	2.8	-0.4	-1.8	-0.7	0.6	0.4	0.7	1.1	1.1
Nominal GDP (in millions of lei)	514,700	498,008	513,641	542,035	590,247	643,816	703,827	770,546	843,680
Nominal GDP (in millions of Euros)	139,666	117,558	122,062	127,237	140,658	156,307	174,317	194,107	216,339

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

1/ Actual fiscal balance adjusted for the automatic effects of internal imbalance (output gap) and external imbalance (absorption gap) on the fiscal position.

Table 7. Romania: Balance of Payments, 2008–16

(In billions of euros, unless otherwise indicated)

	2008	2009	2010		2011		2012		2013	2014	2015	2016
	Act	Act	Prog	Est.	Proj.	Scen.	Proj.	Scen.	Proj.	Proj.	Proj.	Proj.
Current account balance	-16.2	-4.9	-6.7	-5.2	-6.4	-7.5	-7.2	-8.2	-8.2	-9.0	-9.9	-10.8
Merchandise trade balance	-19.1	-6.9	-6.5	-5.9	-6.4	-7.4	-6.6	-7.5	-7.2	-7.5	-7.4	-7.2
Exports (f.o.b.)	33.7	29.1	35.2	37.3	41.1	39.6	45.4	43.6	50.2	55.6	61.7	68.4
Imports (f.o.b.)	52.8	36.0	41.7	43.1	47.5	47.0	52.0	51.1	57.4	63.1	69.1	75.6
Services balance	0.7	-0.3	-0.8	-0.7	-0.8	-1.0	-0.8	-1.0	-0.9	-0.9	-0.8	-0.8
Exports of non-factor services	8.8	7.1	6.3	6.4	7.0	6.8	7.7	7.4	8.6	9.5	10.5	11.7
Imports of non-factor services	8.1	7.4	7.1	7.1	7.8	7.7	8.5	8.4	9.4	10.4	11.4	12.4
Income balance	-3.7	-1.9	-2.2	-2.0	-2.1	-2.1	-2.4	-2.4	-2.8	-3.2	-3.8	-4.4
Receipts	2.3	1.2	1.0	1.0	1.1	1.1	1.1	1.1	1.2	1.2	1.3	1.3
Payments	6.0	3.1	3.2	3.0	3.2	3.2	3.5	3.5	4.0	4.4	5.0	5.7
Current transfer balance	6.0	4.1	2.8	3.4	2.9	2.9	2.6	2.6	2.7	2.6	2.0	1.5
Capital and financial account balance	17.8	-2.9	2.5	1.3	6.7	3.3	11.8	8.0	13.8	14.9	11.4	13.6
Capital account balance	0.6	0.6	0.6	0.2	0.6	0.6	0.6	0.6	0.6	0.6	0.6	0.6
Foreign direct investment balance	9.3	3.6	2.9	2.4	3.7	2.4	4.1	2.7	4.6	5.2	5.8	6.6
Portfolio investment balance	-0.9	0.5	0.9	0.7	2.0	2.0	1.8	1.8	2.7	2.6	-1.0	-1.0
Other investment balance	8.7	-7.6	-1.9	-2.0	0.4	-1.7	5.3	2.9	6.0	6.5	6.0	8.5
General government 1/	0.2	-0.5	-0.2	-0.1	-0.3	-0.3	0.0	0.1	0.0	-0.2	-1.5	0.0
Domestic banks	3.0	-5.5	-0.3	0.6	0.0	-1.5	1.2	-0.3	1.4	1.5	1.7	1.9
Other private sector	5.5	-1.6	-1.4	-2.5	0.8	0.0	4.1	3.0	4.6	5.1	5.8	6.5
Errors and omissions	-1.7	-1.0	0.0	-0.7	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Prospective financing	...	2.1	2.9	3.7	3.2	3.8	0.0	0.8				
European Commission	...	1.5	2.2	2.2	1.4	1.9	0.0	0.8				
World Bank	...	0.3	0.0	0.0	0.7	0.7	0.0	0.0				
EIB/EBRD/IFC	...	0.3	0.7	1.5	1.2	1.2	0.0	0.0				
Overall balance	0.0	-6.7	-1.3	-0.8	3.5	-0.4	4.6	0.5	5.7	5.9	1.5	2.9
Financing	0.0	6.7	1.3	0.8	-3.5	0.4	-4.6	-0.5	-5.7	-5.9	-1.5	-2.9
Gross international reserves (increase: -)	0.0	-1.1	-3.0	-3.5	-4.4	-2.0	-3.1	-1.1	-0.9	-0.8	0.5	-2.7
Use of Fund credit, net	0.0	6.8	4.3	4.3	0.9	2.4	-1.5	0.6	-4.8	-5.1	-2.0	-0.1
Purchases 2/	0.0	6.8	4.3	4.3	0.9	2.4	0.0	2.1	0.0	0.0	0.0	0.0
Repurchases	0.0	0.0	0.0	0.0	0.0	0.0	-1.5	-1.5	-4.8	-5.1	-2.0	-0.1
Other liabilities, net	0.0	1.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:					(In percent of GDP)							
Current account balance	-11.6	-4.2	-5.5	-4.2	-5.0	-6.0	-5.1	-5.9	-5.2	-5.2	-5.1	-5.0
Foreign direct investment balance	6.7	3.0	2.4	2.0	2.9	1.9	2.9	2.0	2.9	3.0	3.0	3.0
Merchandise trade balance	-13.7	-5.8	-5.4	-4.8	-5.1	-5.9	-4.7	-5.4	-4.6	-4.3	-3.8	-3.3
Exports	24.1	24.7	28.9	30.5	32.3	31.5	32.2	31.3	32.1	31.9	31.8	31.7
Imports	37.8	30.6	34.3	35.3	37.4	37.3	37.0	36.7	36.7	36.2	35.6	35.0
Gross external financing requirement	33.1	29.7	27.9	26.6	26.9	28.6	28.4	29.3	31.6	29.7	26.5	24.8
					(Annual percentage change)							
Terms of trade (merchandise)	3.1	0.2	-5.2	-1.8	-0.7	-0.7	0.6	0.6	0.4	0.7	1.1	1.1
Merchandise export volume	3.8	-3.1	21.2	24.5	7.2	3.6	7.6	7.6	8.1	8.3	8.3	8.3
Merchandise import volume	4.7	-23.4	11.1	9.0	6.7	5.5	7.5	6.9	8.5	8.4	8.3	8.3
Merchandise export prices	20.9	2.8	-0.2	3.3	2.8	2.8	2.5	2.5	2.3	2.3	2.3	2.3
Merchandise import prices	17.2	2.6	5.1	5.0	3.6	3.6	1.9	1.9	1.9	1.6	1.2	1.2
					(In billions of euros)							
Gross international reserves 2/	28.3	30.9	33.9	36.0	40.4	37.9	43.4	39.1	44.3	45.1	44.6	47.3
GDP	139.7	117.6	121.9	122.1	127.2	126.0	140.7	139.4	156.3	174.3	194.1	216.1

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

1/ Includes IMF disbursement to the Treasury of €0.9 billion in 2009 and €1.2 billion in 2010, and issuance of €1 billion Eurobond included in the capital and financial account as noted in footnote 1.

2/ Operational defition. Reflects the allocation of SDR 908.8 million that was made avaialable in two tranches in August and September 2009.

Table 8. Romania: Gross Financing Requirements, 2010-12

(In billions of euros, unless otherwise indicated)

	2010					2011						2012		Total	
	Q1	Q2	Q3	Q4	Year	Q1	Q2	Q3	Q4	Year		Year		2011-12	
	Act	Act	Act	Est	Est	Proj	Proj	Proj	Proj	Proj.	**Scenario**	Proj.	**Scenario**	Proj.	**Scenario**
I. Total financing requirements	**9.8**	**8.3**	**9.7**	**9.4**	**37.3**	**8.3**	**8.6**	**8.9**	**9.6**	**35.4**	**36.6**	**37.4**	**38.4**	**72.8**	**75.1**
I.A. Current account deficit	1.5	2.1	0.5	1.0	5.2	1.8	1.4	1.8	1.3	6.3	7.5	7.2	8.2	13.5	15.8
I.B. Short-term debt	4.9	4.5	5.6	5.0	20.0	4.9	5.1	4.9	4.9	19.8	19.8	20.0	20.0	39.8	39.8
Public sector	1.4	0.7	1.4	1.1	4.6	0.6	0.6	0.6	0.6	2.4	2.4	2.2	2.2	4.6	4.6
Banks	2.5	2.9	2.8	2.8	11.0	3.1	3.0	3.1	3.0	12.2	12.2	12.2	12.2	24.4	24.4
Corporates	1.0	0.9	1.4	1.1	4.4	1.2	1.5	1.2	1.3	5.2	5.2	5.6	5.6	10.8	10.8
I.C. Maturing medium- and long-term debt	2.9	1.7	3.8	2.5	10.9	1.6	2.0	2.2	3.4	9.3	9.3	10.2	10.2	19.5	19.5
Public sector	0.2	0.3	0.9	0.4	1.8	0.2	0.2	0.2	0.2	0.9	0.9	1.0	1.0	1.9	1.9
Banks	1.1	0.4	1.0	0.4	2.9	0.4	0.7	0.7	0.7	2.5	2.5	2.8	2.8	5.3	5.3
Corporates	1.6	1.0	1.9	1.7	6.2	1.0	1.1	1.3	2.5	5.9	5.9	6.5	6.5	12.4	12.4
I.D. Other net capital outflows 1/	0.5	0.0	-0.2	0.9	1.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
II. Total financing sources	**8.9**	**8.2**	**8.6**	**8.6**	**34.2**	**8.5**	**8.4**	**9.6**	**9.3**	**35.8**	**32.4**	**42.0**	**38.1**	**77.8**	**70.5**
II.A. Foreign direct investment, net	0.5	0.7	1.0	0.3	2.4	0.7	1.0	1.4	0.5	3.7	2.4	4.1	2.7	7.8	5.2
II.B. Capital account inflows	0.0	0.1	0.0	0.0	0.1	0.1	0.1	0.2	0.2	0.6	0.6	0.5	0.5	1.1	1.1
II.C. Short-term debt	5.9	4.9	5.9	5.4	22.1	4.9	5.2	4.9	4.9	20.0	18.6	23.2	21.6	43.2	40.2
Public sector	1.7	0.8	1.6	1.1	5.2	0.6	0.6	0.6	0.6	2.2	2.4	2.2	2.5	4.5	4.9
Banks	3.0	2.6	3.1	3.0	11.7	3.1	3.0	3.1	3.0	12.2	11.0	13.4	12.2	25.6	23.2
Corporates	1.2	1.5	1.2	1.3	5.2	1.3	1.6	1.3	1.4	5.6	5.2	7.5	7.0	13.1	12.2
II.D. Medium- and long-term debt	2.5	2.5	1.7	2.9	9.6	2.7	2.1	3.1	3.7	11.5	10.8	14.2	13.2	25.8	24.0
Public sector	1.0	0.4	0.1	0.7	2.2	1.2	0.2	1.0	0.3	2.7	2.6	2.7	2.6	5.4	5.3
Banks	0.3	1.2	0.3	1.1	2.9	0.4	0.7	0.7	0.7	2.5	2.3	2.8	2.5	5.3	4.7
Corporates	1.2	0.9	1.3	1.1	4.5	1.1	1.2	1.4	2.7	6.3	5.9	8.8	8.1	15.1	14.0
III. Increase in gross reserves	2.9	-1.2	2.4	-0.7	3.5	2.8	0.3	1.4	0.0	4.5	2.0	3.1	1.0	7.6	3.0
IV. Financing Gap	**4.0**	**0.2**	**3.4**	**0.3**	**8.0**	**2.7**	**0.4**	**0.7**	**0.3**	**4.1**	**6.2**	**-1.5**	**1.4**	**2.6**	**7.6**
V. Program financing	**4.0**	**0.2**	**3.4**	**0.3**	**8.0**	**2.7**	**0.4**	**0.7**	**0.3**	**4.1**	**6.2**	**-1.5**	**1.4**	**2.6**	**7.6**
IMF 2/	2.5	0.0	1.9	0.0	4.3	0.9	0.0	0.0	0.0	0.9	2.4	-1.5	0.6	-0.7	3.0
Purchases	2.5	0.0	1.9	0.0	4.3	0.9	0.0	0.0	0.0	0.9	2.4	0.0	2.1	0.9	4.5
Repurchases												-1.5	-1.5	-1.5	-1.5
Others	1.6	0.2	1.5	0.3	3.7	1.8	0.4	0.7	0.3	3.2	3.8	0.0	0.8	3.2	4.6
European Commission	1.0	0.0	1.2	0.0	2.2	1.2	0.2	0.0	0.0	1.4	1.9	0.0	0.8	1.4	2.8
World Bank	0.0	0.0	0.0	0.0	0.0	0.3	0.0	0.4	0.0	0.7	0.7	0.0	0.0	0.7	0.7
EIB/EBRD/IFC	0.6	0.2	0.4	0.3	1.5	0.3	0.3	0.3	0.3	1.2	1.2	0.0	0.0	1.2	1.2
Memorandum items:															
Rollover rates for amortizing debt ST (in percent)															
Public sector	121	114	114	100	113	93	93	93	93	93	100	100	110	96	105
Banks	120	90	111	107	106	100	100	100	100	100	90	110	100	105	95
Corporates	120	167	86	118	118	107	107	107	107	107	100	135	125	121	113
Rollover rates for amortizing debt MLT (in percent)															
Public sector	500	133	11	175	122	588	88	458	129	307	297	280	270	293	283
Banks	27	300	30	275	100	100	100	100	100	100	90	100	90	100	90
Corporates	75	90	68	65	73	107	107	107	107	107	100	135	125	122	113
Gross international reserves 3/	34.8	35.0	35.8	36.0	36.0	…	…	…	…	40.4	37.9	43.4	39.1	…	…
Coverage of gross international reserves															
- Months of imports of GFNS (next year)	…	…	…	…	8.6	…	…	…	…	8.0	…	…	…	…	…
- Short-term external debt (in percent)	117.5	114.6	126.6	123.6	123.6	…	…	…	…	133.6	125.6	100.8	90.5	…	…

Source: IMF staff estimates.

1/ Includes includes portfolio equity, financial derivatives and other investments, assets position.

2/ Last disbursement of the current program is treated as precautionary

Table 9. Romania: General Government Operations, 2008–12
(In percent of GDP)

	2008	2009	2010 Prog.	2010 Est.	2011 Proj.	2012 Proj.
Revenue	32.2	31.4	32.7	32.8	33.3	33.7
Taxes	27.9	27.4	26.9	27.0	28.1	27.6
Taxes on profits	2.8	2.7	2.1	2.1	2.0	2.0
Taxes on income	3.6	3.7	3.5	3.5	3.5	3.5
Value-added taxes	7.9	6.9	7.6	7.6	8.5	8.5
Excises	2.7	3.1	3.4	3.4	3.4	3.4
Customs duties	0.2	0.1	0.1	0.1	0.1	0.1
Social security contributions	9.5	9.6	8.8	8.9	9.2	8.8
Other taxes	1.2	1.2	1.3	1.3	1.4	1.3
Nontax revenue	3.1	2.9	3.9	3.9	3.5	3.6
Capital revenue	0.2	0.1	0.1	0.1	0.1	0.1
Grants, including EU disbursements	0.9	1.0	1.7	1.8	1.6	2.4
Expenditure	37.0	38.7	39.5	39.4	37.7	36.7
Current expenditure	32.5	34.8	35.2	35.7	33.9	32.8
Compensation of employees	8.9	9.4	8.2	8.3	7.5	7.2
Maintenance and operations	6.2	5.6	5.7	5.8	5.4	5.1
Interest	0.7	1.2	1.5	1.4	1.8	1.7
Subsidies	1.5	1.4	1.3	1.3	1.1	0.9
Transfers 1/	15.1	16.7	18.0	18.5	17.8	17.7
Pensions 2/	6.4	8.0	8.2	8.2	8.7	8.5
Other social transfers	4.1	4.8	5.2	5.2	3.9	3.6
Other transfers 3/ 4/	3.4	3.4	4.1	4.6	4.7	5.0
o\w contribution to EU budget	0.9	1.1	1.0	1.0	1.1	1.0
o\w pre-accession EU funds	0.0	0.6	0.7	0.8	0.2	0.0
Other spending	1.2	0.5	0.6	0.6	0.4	0.5
Proj. with ext. credits	0.0	0.4	0.5	0.3	0.4	0.2
Capital expenditure 5/	4.6	4.4	3.9	3.8	3.7	3.9
Reserve fund	0.0	0.0	0.3	0.0	0.0	0.1
Net lending	-0.1	-0.5	0.0	-0.1	0.0	0.0
Fiscal balance	-4.8	-7.3	-6.8	-6.5	-4.4	-3.0
Primary balance	-4.1	-6.1	-5.3	-5.1	-2.7	-1.3
Financing	4.8	7.3	6.8	6.5	4.4	3.0
Privatization proceeds	0.1	0.0	0.0	0.0	0.0	0.0
External	0.4	2.9	4.6	4.6	2.8	0.7
Domestic	4.3	4.5	2.2	2.0	1.6	2.3
Financial liabilities						
Gross public debt 6/	21.3	29.5	35.5	35.2	37.7	37.6
Gross public debt excl. guarantees	19.5	27.8	33.9	33.2	36.1	36.2
External	6.9	10.0	14.4	14.3	16.3	15.7
Domestic	12.6	17.8	19.5	18.8	19.8	20.5
Memorandum items:						
Total capital spending	6.3	6.5	7.1	7.4	7.1	7.5
Fiscal balance (ESA95 basis)	-5.3	-8.3	...	...	...	...
Output gap 7/	10.0	-0.8	-6.1	-4.3	-5.3	-3.7
Conventional structural fiscal balance	-8.5	-7.0	-4.4	-4.9	-2.4	-1.6
Nominal GDP (in billions of RON)	514.7	498.0	511.6	513.6	542.0	590.2

Sources: Ministry of Finance; Eurostat; and Fund staff projections.

1/ Increase in 2009 mostly reflects higher EU-financed capital spending and budgeted rise in pensions.

2/ Projected increase in pensions in 2011 is due to a reclassification of some pensions from the state budget to the pension fund.

3/ Includes co-financing of EU projects.

4/ In 2011, projected increase is due to higher outlays in state aid and transfers to state agencies for investments.

5/ Does not include all capital spending.

6/ Total public debt, including government debt, local government debt, and guarantees.

7/ Percentage deviation of actual from potential GDP.

Table 9. Romania: General Government Operations, 2008–12 (concluded)
(In millions of RON)

	2008	2009	2010 Prog.	2010 Est.	2011 Proj	2012 Proj
Revenue	165,549	156,373	167,230	168,635	180,329	199,040
Taxes	143,855	136,350	137,867	138,667	152,124	163,028
Taxes on profits	14,426	13,466	10,920	10,969	10,850	11,815
Taxes on income	18,523	18,551	17,969	17,957	18,827	20,502
Value-added taxes	40,874	34,322	39,050	39,246	46,232	50,344
Excises	13,646	15,646	17,300	17,312	18,502	20,148
Customs duties	962	656	577	574	610	668
Social security contributions	49,008	47,829	45,246	45,704	49,739	51,714
Other taxes	6,416	5,879	6,805	6,905	7,364	7,838
Nontax revenue	15,892	14,487	19,854	19,796	18,971	21,452
Capital revenue	1,076	546	750	685	477	520
Grants	4,702	5,057	8,759	9,494	8,757	14,040
o/w EU pre-accession funds	…	2,959	3,808	4,054	951	1,322
Financial operations and other	25	-67	0	-6	…	…
Expenditure	190,407	192,782	201,871	202,256	204,282	216,669
Current expenditure	167,095	173,445	180,293	183,243	183,763	193,434
Compensation of employees	45,608	46,676	41,999	42,839	40,570	42,587
Maintenance and operations	32,012	28,028	29,028	29,541	29,143	30,149
Interest	3,776	6,063	7,742	7,275	9,500	10,031
Subsidies	7,899	7,215	6,777	6,735	5,780	5,367
Transfers 1/	77,800	83,407	92,155	95,060	96,627	104,337
Pensions	33,187	39,851	42,126	42,107	47,357	50,315
Other social transfers	20,973	24,101	26,379	26,505	21,150	21,412
Other transfers 2/	17,646	16,931	20,734	23,514	25,687	29,772
o\w contribution to EU budget	4,506	5,650	5,171	5,153	6,160	6,175
o\w pre-accession EU funds		2,959	3,808	4,054	951	
Other spending	5,993	2,523	2,916	2,933	2,433	2,838
Proj. with ext. credits	0	2,056	2,592	1,794	2,142	963
Capital expenditure 3/	23,794	21,837	19,812	19,660	20,313	22,828
Reserve fund	0	0	1,766	0	207	407
Net lending	-481	-2,500	0	-647	0	0
Fiscal balance	-24,858	-36,409	-34,641	-33,621	-23,953	-17,629
Primary balance	-21,082	-30,346	-26,898	-26,346	-14,453	-7,598
Financing	24,858	36,409	34,641	33,621	23,953	17,629
Privatization proceeds	371	0	0	0	0	0
External	2,284	14,233	23,474	23,474	15,123	4,196
Domestic	22,203	22,177	11,166	10,147	8,830	13,433
Financial liabilities						
Gross public debt 4/	109,752	146,938	181,579	180,950	204,184	221,813
Gross public debt excl. guarantees	100,435	138,598	173,239	170,283	195,843	213,473
External	35,733	49,966	73,440	73,467	88,563	92,759
Domestic	64,702	88,632	99,799	96,816	107,280	120,713

Sources: Ministry of Finance; Eurostat; and Fund staff projections.

1/ Increase in 2009 mostly reflects higher EU-financed capital spending and budgeted rise in pensions.

2/ Includes co-financing of EU projects.

3/ Does not include all capital spending.

4/ Total public debt, including government debt, local government debt, and guarantees.

Table 10. Romania: Monetary Survey, 2009–12

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

	Dec-09	Dec-10 2/	2011(Proj.) Q1	Q2	Q3	Q4	Dec-12 Proj.
			I. Banking System				
Net foreign assets	**17,684**	**18,776**	**30,867**	**31,697**	**36,470**	**33,223**	**52,627**
In million euros	4,182	4,382	7,140	7,359	8,498	7,770	12,158
o/w commercial banks	-19,708	-21,158	-21,158	-21,158	-21,158	-21,158	-21,158
Net domestic assets	**171,946**	**183,987**	**172,788**	**182,313**	**180,212**	**190,425**	**202,555**
Public sector credit	26,748	43,393	45,876	48,376	50,876	53,324	69,129
Private sector credit	199,887	209,298	210,022	221,936	219,281	225,412	244,941
Other	-54,688	-68,704	-83,110	-88,000	-89,945	-88,312	-111,515
Broad Money (M3)	**189,630**	**202,763**	**203,655**	**214,010**	**216,683**	**223,648**	**255,182**
Intermediate money (M2)	188,013	199,586	201,344	210,924	213,198	220,144	251,184
Money market instruments	1,617	3,177	2,312	3,085	3,485	3,504	3,998
Narrow money (M1)	79,361	81,605	72,726	91,614	95,911	101,189	114,130
Currency in circulation	23,968	26,793	23,280	28,287	27,218	32,685	36,865
Overnight deposits	55,394	54,812	49,447	63,327	68,694	68,504	77,265
			II. National Bank of Romania				
Net foreign assets	**101,015**	**109,433**	**122,339**	**122,833**	**127,270**	**123,689**	**144,212**
In million euros	23,891	25,540	28,298	28,517	29,656	28,928	33,316
Net domestic assets	**-49,354**	**-54,330**	**-73,231**	**-68,942**	**-72,464**	**-63,491**	**-76,316**
Public sector credit, net	-13,626	-12,795	-23,104	-23,204	-23,254	-16,795	-16,795
Credit to banks, net	-23,848	-26,148	-29,335	-30,335	-27,335	-28,335	-36,335
Other	-11,880	-15,387	-20,792	-15,403	-21,875	-18,360	-23,185
Reserve money	**51,662**	**55,103**	**49,108**	**53,891**	**54,807**	**60,198**	**67,896**
			(Annual percentage change)				
Broad money (M3)	9.0	6.9	7.2	9.7	10.7	10.3	14.1
NFA contribution	2.6	0.6	2.5	2.4	6.2	7.1	8.7
NDA contribution	6.4	6.3	4.7	7.3	4.5	3.2	5.4
Reserve money	2.4	6.7	7.3	9.7	10.8	9.2	12.8
NFA contribution	-18.4	16.3	31.1	10.0	33.4	25.9	34.1
NDA contribution	20.8	-9.6	-23.8	-0.3	-22.6	-16.6	-21.3
Domestic credit, real	5.5	3.2	8.4	4.4	8.5	6.3	9.4
Private sector, real	-3.7	-3.0	-1.4	-1.5	1.2	3.8	5.5
Public sector, real	159.7	21.9	18.4	18.3	22.7	11.9	18.5
Broad money (M3), in real terms	4.0	-1.0	0.4	2.6	6.3	6.3	10.8
Private deposits, at constant e/r	8.1	5.0	6.0	7.7	8.9	9.9	13.1
Memorandum items:							
CPI inflation, eop	4.8	8.0	6.8	6.9	4.2	3.7	3.0
Inflation target	2.5 - 4.5	2.5 - 4.5	2.0 - 4.0	2.0 - 4.0	2.0 - 4.0	2.0 - 4.0	2.0 - 4.0
Interest rates (percent):							
Policy interest rate	8.00	6.25	6.25	…	…	…	…
Interbank offer rate, 1 week	10.70	3.6	3.30	…	…	…	…
Corporate loans 1/	15.4	9.5	…	…	…	…	…
Household time deposits 1/	9.9	7.6	…	…	…	…	…
Share of foreign currency private deposit	38.8	36.1	…	…	…	…	…
Share of foreign currency private loans	60.1	63.0	…	…	…	…	…
M2 velocity	2.65	2.56	2.55	2.55	2.55	2.58	2.61
Money multiplier (M3/reserve money)	3.67	3.68	4.15	3.97	3.95	3.72	3.76

Sources: National Bank of Romania; and Fund staff estimates.

1/ Rates for new local currency denominated transactions.

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

Table 11. Romania: Financial Soundness Indicators, 2008–10

(In percent)

	2008 Dec	2009 Mar	2009 Jun	2009 Sep	2009 Dec	2010 Mar	2010 Jun	2010 Sep	2010 Dec
Core indicators									
Capital adequacy									
Capital to risk-weighted assets	13.8	13.16	13.51	13.73	14.7	15.0	14.3	14.6	14.7
Tier 1 capital to risk-weighted assets	11.8	11.4	11.9	12.0	13.4	14.2	13.4	13.8	13.8
Asset quality									
Nonperforming loans to total gross loans 1/	2.8	4.0	4.7	6.5	7.9	9.1	10.2	11.7	11.9
Nonperforming loans net of provisions to capital 1/	10.7	15.9	24.3	8.8	11.3	12.6	14.5	16.3	15.7
Earnings and profitability									
Return on assets	1.6	-0.3	0.1	0.3	0.2	0.5	-0.1	-0.2	-0.1
Return on equity 2/	17.0	-2.9	0.6	3.2	2.9	6.0	-1.6	-2.1	-1.0
Net interest income to operating income	44.8	38.9	38.4	41.8	44.1	55.7	58.2	58.7	58.2
Noninterest expense to operating income (cost to income)	55.7	57.1	67.2	65.4	63.9	56.5	59.2	58.6	64.1
Personnel expense to operating income	23.4	21.4	22.8	21.4	20.3	20.7	21.6	21.2	20.6
Liquidity									
Liquid assets (/3)to total assets	47.1	51.7	54.7	53.9	57.4	58.6	59.1	59.3	59.9
Liquid assets (/3) to short-term liabilities (/4)	230.5	226.3	261.9	136.3	132.0	150.0	146.7	148.7	144.6
Liquid assets (/3) to total attracted and borrowed sources	116.2	119.2	130.6	87.7	79.4	81.2	79.8	82.1	81.2
Foreign exchange risk									
Net open position in foreign exchange, in percent of capital	1.6	-2.3	-2.5	1.7	2.3	1.6	-3.2	1.4	1.3
Lending in foreign exchange, in percent of non-gov. credit	57.8	59	59.1	59.7	60.1	60.4	62.8	62.5	63
Foreign currency liabilities, in percent of total attracted and borrowed source	43.7	42.3	41.8	44.1	42.8	43.6	44.7	44.1	43.5
Deposits in foreign exchange, in percent of non-gov. dom. deposits	34.8	37.1	35.6	37.8	38.8	37	38	37.4	36
Encouraged indicators									
Deposit-taking institutions									
Leverage ratio 5/	8.1	6.8	6.9	7.0	7.6	8.1	7.9	7.9	7.9
Personnel expenses to noninterest expenses	41.9	37.5	33.9	32.7	31.8	36.6	36.4	36.1	32.2
Customer deposits to total (non-interbank) loans	81.9	80.2	83.9	85.1	88.7	88.3	85.1	86.0	88.1

Source: Romanian National Bank.

1/ NPLs for 2004-June 2009 include un-adjusted exposures of loans and related interests classified "loss" (overdue by more than 90 days, including the contaminated ones, and/or with for which legal proceedings were initiated) and from September 2009 the "NPLs ratio " represents un-adjusted exposures of loans and related interests classified "loss 2", meaning loans and related interests overdue for more than 90 days and/or for which legal proceedings were initiated.

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

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

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

5/ Tier 1 Capital to average assets

Table 12a. Romania: Schedule of Reviews and Purchases

Date	Amount of Purchase		Conditions
	Millions of SDRs	Percent of Quota	
May 4, 2009	4,370	424.19	Approval of arrangement
September 21, 2009	1,718	166.76	First review and end-June 2009 performance criteria
December 15, 2009 1/	1,409	136.77	Second review and end-September 2009 performance criteria
February 19, 2010	766	74.35	Third review and end-December 2009 performance criteria
July 2, 2010	768	74.55	Fourth review and end-March 2010 performance criteria
September 24, 2010	769	74.65	Fifth review and end-June 2010 performance criteria
January 7, 2011	769	74.65	Sixth review and end-December 2010 performance criteria
March 25, 2011	874	84.84	Seventh review and end-December 2010 & end-January 2011 performance criteria
Total	11,443	1110.76	

Source: IMF staff estimates.

1/ The amount of purchase for the second review was available from December 15, 2009, but was made together with the amount for the third review on February 19, 2010 given the delay in completing the second review.

Table 12b. Romania: Schedule of Reviews and Purchases

Date	Amount of Purchase: Millions of SDRs	Amount of Purchase: Percent of Quota	Conditions
March 31, 2011	60.0	5.82	Arrangement effective March 31, 2011, after approval March 25, 2011
June 15, 2011	430.0	41.74	First review and end-March 2011 performance criteria
September 15, 2011	430.0	41.74	Second review and end-June 2011 performance criteria
December 15, 2011	430.0	41.74	Third review and end-September 2011 performance criteria
March 15, 2012	430.0	41.74	Fourth review and end-December 2011 performance criteria
June 15, 2012	430.0	41.74	Fifth review and end-March 2012 performance criteria
September 15, 2012	430.0	41.74	Sixth review and end-June 2012 performance criteria
December 15, 2012	430.0	41.74	Seventh review and end-September 2012 performance criteria
March 15, 2013	20.6	2.00	Eigth review and end-December 2012 performance criteria
Total	3090.6	300	

Source: IMF staff estimates.

Table 13. Romania: Indicators of Fund Credit, 2011–16 1/

(In millions of SDR)

	2011	2012	2013	2014	2015	2016
Existing Fund Credit						
Stock 2/	10,569	9,262	5,210	1,329	96	0
Obligations 3/	111	1,454	4,166	3,933	1,244	98
Repurchase	0	1307	4052	3881	1233	96
Charges	111	147	114	52	12	2
Prospective Fund Credit under Stand-By Arrangement						
Disbursement	2,224	1,720	21	0	0	0
Stock 2/	2,224	3,944	3,965	3,453	2,019	550
Obligations 3/	22	46	54	566	1,478	1,490
Repurchase	0	0	0	512	1,435	1,468
Charges	22	46	54	54	43	22
Stock of existing and prospective Fund credit						
In millions of SDR	12,793	13,206	9,175	4,782	2,115	550
In percent of quota	1,242	1,282	891	464	205	53
In percent of GDP	11.7	11.0	6.9	3.2	1.3	0.3
In percent of exports of goods and services	30.9	29.1	18.4	8.7	3.5	0.8
In percent of gross reserves	36.9	35.5	24.3	12.6	5.7	1.4
Obligations to the Fund from existing and prospective Fund arrangements						
In millions of SDR	262	1,726	4,487	4,633	2,748	1,588
In percent of quota	25.4	167.5	435.5	449.7	266.7	154.1
In percent of GDP	0.2	1.4	3.4	3.1	1.7	0.9
In percent of exports of goods and services	0.6	3.8	9.0	8.4	4.5	2.4
In percent of gross reserves	0.8	4.6	11.9	12.2	7.4	4.0

Source: IMF staff estimates.

1/ Using IMF actual disbursements, SDR interest rate as well as exchange rate of SDR/US$ and US$/€ of March 2, 2011.

2/ End of period.

3/ Repayment schedule based on repurchase obligations.

Table 14. Romania: Public Sector Debt Sustainability Framework, 2006-2016
(In percent of GDP, unless otherwise indicated)

	Actual					Projections						
	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	**Debt-stabilizing primary balance 9/**
Baseline: Public sector debt 1/	15.4	17.5	19.5	27.4	33.2	**36.1**	**36.2**	**36.0**	**35.5**	**34.7**	**33.8**	**-1.4**
o/w foreign-currency denominated	7.1	6.6	6.4	15.0	20.4	24.0	21.9	18.4	15.0	11.7	10.0	
Change in public sector debt	-0.3	2.1	2.0	7.9	5.7	2.9	0.0	-0.1	-0.6	-0.8	-0.9	
Identified debt-creating flows (4+7+12)	-3.0	-0.1	2.7	7.9	7.8	2.4	0.0	-0.1	-0.6	-0.8	-0.9	
Primary deficit	0.6	2.4	4.1	6.1	5.1	2.7	1.3	1.2	0.8	0.6	0.4	
Revenue and grants	32.3	32.3	32.2	31.4	32.8	33.3	33.7	33.5	33.2	32.4	31.7	
Primary (noninterest) expenditure	32.9	34.6	36.3	37.5	38.0	35.9	35.0	34.7	34.0	33.0	32.2	
Automatic debt dynamics 2/	-3.1	-2.3	-1.3	1.8	2.7	-0.2	-1.3	-1.3	-1.4	-1.4	-1.3	
Contribution from interest rate/growth differential 3/	-1.7	-1.9	-2.6	1.9	0.6	-0.2	-1.3	-1.3	-1.4	-1.4	-1.3	
Of which contribution from real interest rate	-0.7	-1.1	-1.6	0.4	0.2	0.2	0.2	0.1	0.0	-0.1	-0.1	
Of which contribution from real GDP growth	-1.0	-0.8	-1.0	1.4	0.3	-0.5	-1.5	-1.4	-1.4	-1.3	-1.3	
Contribution from exchange rate depreciation 4/	-1.4	-0.4	1.3	0.0	2.1	...	...	...	...	...	...	
Other identified debt-creating flows	-0.4	-0.1	-0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Privatization receipts (negative)	-0.4	-0.1	-0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Other (specify, e.g. bank recapitalization)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Residual, including asset changes (2-3) 5/	2.8	2.2	-0.7	0.0	-2.1	0.0	0.0	0.0	0.0	0.0	0.0	
Public sector debt-to-revenue ratio 1/	47.6	54.2	60.7	87.4	101.0	108.6	107.3	107.7	106.9	107.0	106.4	
Gross financing need 6/	1.8	3.9	6.3	8.4	7.2	5.4	4.7	9.1	8.1	5.6	5.0	
in billions of U.S. dollars	2.2	6.7	12.8	13.8	11.6	9.0	8.7	18.5	18.2	14.0	13.6	
Scenario with key variables at their historical averages 7/						**36.1**	**34.2**	**32.5**	**31.0**	**29.6**	**28.4**	**-3.1**
Scenario with no policy change (constant primary balance) in 2011-2016						**36.1**	**37.5**	**38.8**	**39.9**	**41.0**	**42.1**	**-1.8**
Key Macroeconomic and Fiscal Assumptions Underlying Baseline												
Real GDP growth (in percent)	7.9	6.3	7.3	-7.1	-1.3	1.5	4.4	4.2	4.2	4.1	4.0	
Average nominal interest rate on public debt (in percent) 8/	6.1	5.8	5.2	6.0	5.3	5.5	5.1	5.1	5.0	5.2	5.3	
Average real interest rate (nominal rate minus change in GDP deflator, in percent)	-4.5	-7.7	-10.1	1.9	0.8	0.8	0.9	0.5	0.1	0.1	0.0	
Nominal appreciation (increase in US dollar value of local currency, in percent)	19.4	6.5	-16.5	0.3	-10.7	...	...	...	...	...	...	
Inflation rate (GDP deflator, in percent)	10.6	13.5	15.2	4.1	4.5	4.8	4.3	4.6	4.9	5.2	5.2	
Growth of real primary spending (deflated by GDP deflator, in percent)	14.8	12.0	12.4	-3.9	-0.1	-4.5	1.8	3.3	2.2	1.0	1.5	
Primary deficit	0.6	2.4	4.1	6.1	5.1	2.7	1.3	1.2	0.8	0.6	0.4	

1/ Coverage: General government gross debt, excluding guarantees.
2/ Derived as [(r - π(1+g) - g + $\alpha\varepsilon$(1+r)]/(1+g+π+gπ)) times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; α = share of foreign-currency denominated debt; and ε = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).
3/ The real interest rate contribution is derived from the denominator in footnote 2/ as r - π (1+g) and the real growth contribution as -g.
4/ The exchange rate contribution is derived from the numerator in footnote 2/ as $\alpha\varepsilon$(1+r).
5/ For projections, this line includes exchange rate changes.
6/ Defined as public sector deficit, plus amortization of medium and long-term public sector debt, plus short-term debt at end of previous period.
7/ The key variables include real GDP growth; real interest rate; and primary balance in percent of GDP.
8/ Derived as nominal interest expenditure divided by previous period debt stock.
9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Table 15. Romania: External Debt Sustainability Framework, 2006-2016
(In percent of GDP, unless otherwise indicated)

	Actual					Projections						
	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	**Debt-stabilizing non-interest current account 6/**
Baseline: External debt	42.1	47.0	51.4	68.3	74.5	**78.9**	**75.4**	**70.4**	**65.5**	**61.1**	**58.3**	**-7.2**
Change in external debt	3.3	4.9	4.4	16.9	6.2	4.4	-3.5	-5.0	-4.9	-4.4	-2.7	
Identified external debt-creating flows (4+8+9)	-5.4	-1.4	0.5	10.4	-0.4	-0.5	-2.2	-2.3	-1.9	0.2	0.2	
Current account deficit, excluding interest payments	9.2	12.2	10.1	2.4	1.8	2.7	3.0	3.3	3.4	3.6	3.6	
Deficit in balance of goods and services	12.0	14.0	13.2	6.1	5.5	5.7	5.3	5.2	4.8	4.2	3.7	
Exports	32.1	29.2	30.4	30.7	36.0	37.8	37.7	37.6	37.4	37.2	37.0	
Imports	44.2	43.2	43.6	36.8	41.4	43.5	43.0	42.7	42.1	41.4	40.7	
Net non-debt creating capital inflows (negative)	-8.6	-5.8	-6.1	-3.4	-2.6	-4.4	-4.2	-4.7	-4.4	-2.5	-2.6	
Automatic debt dynamics 1/	-6.0	-7.8	-3.6	11.4	0.4	1.2	-1.0	-0.9	-0.9	-0.9	-0.8	
Contribution from nominal interest rate	1.2	1.2	1.5	1.8	2.5	2.3	2.1	2.0	1.8	1.5	1.4	
Contribution from real GDP growth	-2.5	-2.1	-3.1	4.3	0.8	-1.1	-3.1	-2.9	-2.7	-2.4	-2.2	
Contribution from price and exchange rate changes 2/	-4.7	-7.0	-2.0	5.3	-2.9	...	...	...	...	...	...	
Residual, incl. change in gross foreign assets (2-3) 3/	8.8	6.3	4.0	6.5	6.5	4.5	-1.4	-2.6	-2.9	-4.6	-2.9	
External debt-to-exports ratio (in percent)	131.0	160.7	169.0	222.2	207.1	208.6	199.6	187.3	175.3	164.1	157.5	
Gross external financing need (in billions of Euros) 4/	21.7	35.9	46.2	34.9	32.5	34.4	40.2	49.8	52.1	51.8	53.9	
in percent of GDP	22.2	28.8	33.1	29.7	26.6	26.9	28.4	31.6	29.7	26.5	24.8	
Scenario with key variables at their historical averages 5/						**78.9**	**77.0**	**74.1**	**71.2**	**66.4**	**63.4**	**-9.8**
Key Macroeconomic Assumptions Underlying Baseline												
Real GDP growth (in percent)	7.9	6.3	7.3	-7.1	-1.2	1.5	4.4	4.3	4.2	4.1	4.0	
GDP deflator in Euros (change in percent)	13.8	19.8	4.4	-9.4	4.4	3.4	5.9	6.6	7.0	6.9	7.1	
Nominal external interest rate (in percent)	3.8	3.7	3.6	2.9	3.7	3.3	3.0	2.9	2.8	2.6	2.5	
Growth of exports (Euro terms, in percent)	19.3	15.9	16.6	-14.9	20.6	10.3	10.4	10.6	10.9	10.9	10.9	
Growth of imports (Euro terms, in percent)	25.2	24.7	13.2	-28.9	15.9	10.2	9.4	10.4	10.0	9.5	9.5	
Current account balance, excluding interest payments	-9.2	-12.2	-10.1	-2.4	-1.8	-2.7	-3.0	-3.3	-3.4	-3.6	-3.6	
Net non-debt creating capital inflows	8.6	5.8	6.1	3.4	2.6	4.4	4.2	4.7	4.4	2.5	2.6	

e = nominal appreciation (increase in dollar value of domestic currency), and a = share of domestic-currency denominated debt in total external debt.

1/ Derived as $[r - g - \rho(1+g) + \varepsilon\alpha(1+r)]/(1+g+\rho+g\rho)$ times previous period debt stock, with r = nominal effective interest rate on external debt; ρ = change in domestic GDP deflator in uro terms, g = real GDP growth rate,

ε = nominal appreciation (increase in dollar value of domestic currency), and α = share of domestic-currency denominated debt in total external debt.

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

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

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

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

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

APPENDIX I: ROMANIA: LETTER OF INTENT

Bucharest, March 10, 2011

Mr. Dominique Strauss-Kahn
Managing Director
International Monetary Fund
Washington, DC 20431

Dear Mr. Strauss-Kahn:

1. Our anti-crisis program, supported by the International Monetary Fund (IMF), the European Union (EU), and the World Bank (WB), has continued to play a crucial role in stabilizing the Romanian economy, reversing imbalances, rebuilding confidence of international financial markets, and setting the stage for future sustainable economic growth. The economy has stabilized and is expected to recover in 2011 with around 1½ percent growth, due to continued strong exports, supported by gradually improving domestic demand, underpinned by planned improvements in absorption of EU funds. Inflation, driven by the recent VAT rate hike and high food and fuel prices, peaked at 8.0 percent at end-2010. During the course of 2011, inflation is expected to return to the NBR's target band. The current account deficit has shrunk considerably from 11.6 percent in 2008 to around 4.5 percent in 2010. Despite these improvements, recovery remains vulnerable to adverse developments in international financial markets, via rising risk premia and lower capital inflows, and downside risks to euro area recovery.

2. In view of our strong performance under the macroeconomic program supported by the Stand-By Arrangement (SBA), the Government of Romania and the National Bank of Romania (NBR) request completion of the seventh review under the SBA. We are considering treating as precautionary the final purchase available upon completion of this review. Given that the current SBA with the IMF (approved on May 4, 2009) has been successful in achieving its broad objective of realizing macroeconomic stability in the face of crisis, we would also like to end the current SBA – and request the simultaneous approval of a new 24-month SBA totaling SDR 3,090.6 million (€3.5 billion, 300 percent of quota). The new SBA will support our comprehensive economic program for 2011-12 to boost sustainable economic growth, continue adjustment, and cushion the effects of future shocks, should they materialize. Since Romania's international reserves position is comfortable and access to external financing is improving, our intention is to treat the new arrangement as precautionary. In conjunction with WB commitments of €400 million, and precautionary support of €1.4 billion under the EU's balance of payment financing facility, this arrangement will signal the international community's continued support for our policies.

3. We believe that the policies and measures set forth in this Letter are adequate to achieve the objectives of our macroeconomic program supported by the next SBA, but the Government and NBR stand ready to take additional measures as appropriate to ensure the achievement of its objectives. Romania will consult with the Fund on the adoption of measures that may become appropriate to achieve the objectives of the program, and in advance of revisions to the policies contained in this Letter, in accordance with the Fund's policies on such consultation. We will also provide the IMF and the European Commission (EC) with the necessary information for program monitoring.

I. PERFORMANCE UNDER THE CURRENT SBA

Seventh Review

4. Our performance for the seventh review of the SBA has been strong (Tables 1 and 2).

- *Quantitative performance criteria and indicative targets.* The end-2010 fiscal deficit target was met with a margin of ¼ percent of GDP, reflecting higher revenues than anticipated. The NFA targets for end-December and end-January were also met with significant margins. All other remaining end-December 2010 quantitative performance criteria were observed, with the exception of that on general government arrears for which a waiver was already granted on January 7, 2011. The indicative targets on loss-making state-owned enterprises and current spending were missed. Inflation remained within the inner band of the inflation consultation mechanism throughout the period.
- *Structural benchmarks.* The ordinance on high net wealth individuals was approved by end-December, as programmed. A full project plan to implement the integration of the accounting reporting system with the Treasury payment system is in place. We will shortly secure parliamentary ratification of the remaining amendments to the bank resolution framework, slightly delayed from the December 1, 2010. We will amend by ordinance the Deposit Guarantee Fund (DGF) law by end-July 2011 to allow for the use of resources administered by the DGF (including through guarantees) to facilitate restructuring measures authorized by the National Bank of Romania regarding the transfer of deposits, including purchase and assumption transactions, if such use would be less costly than the direct payment of deposit guarantees (structural benchmark reset from March).

Review of Existing Program

5. Significant progress has been made under the existing program in achieving fiscal consolidation and safeguarding the financial sector. A structural fiscal deficit of almost 9 percent of GDP in 2008, which aggravated the initial impact of the global financial crisis, was halved by 2010. Measures taken in 2010 have also put the government finances firmly on path to reach the Maastricht deficit target in 2012. Financial sector measures ensured

adequate capitalization of banks and liquidity in domestic markets, securing banking sector stability. Excessive capital outflows were avoided, in part reflecting the European Bank Coordination Initiative, and an orderly adjustment of the current account was made possible without excessive exchange rate volatility. Structural reforms in tax administration, pensions, public wages and employment, and social benefits have placed public finances on a more sustainable medium-term path and have set the stage for more widespread improvements in the business climate.

II. Objectives and Policies for The New SBA

6. Romania is poised to reap the benefits of the difficult adjustment measures implemented under the existing program. The new economic program aims to boost potential growth with a focus on structural reforms, while consolidating fiscal and financial stability. In this context, building on the significant achievements of the current SBA, the key objectives of the new program are to: (i) continue the fiscal adjustment process while extending its scope to attack problems of revenue and expenditure efficiency and arrears; (ii) continue fostering confidence, facilitating improved private capital flows and generating sustainable growth; (iii) boost growth potential through structural reforms and improved flexibility of the economy, which will also allow for continued competitiveness as Romania prepares to eventually join the Euro area.

Macroeconomic Framework for 2011–12

7. After suffering a severe downturn in 2009-10, there are signs that economic activity is picking up. From around 1½ percent in 2011, growth is expected to gain momentum in 2012, reaching 4 to 4½ percent. Domestic demand will gradually become the main growth engine, supported by better absorption of EU funds. Growth in net external demand will slow in line with moderate growth of export markets, stabilizing the current account balance at around 5 percent of GDP. Increased investor confidence, coupled with planned privatization under the program, will bring renewed FDI and banking inflows.

Fiscal Policy

8. For 2011, we are committed to the previously agreed cash fiscal deficit target of 4.4 percent of GDP (or within 5 percent in ESA terms). We have passed the 2011 budget in line with our previous commitments. On the revenue side, the main components of the tax system will remain unchanged. We will request technical assistance from the IMF and WB to provide us with a comprehensive review of the tax system with a view toward revenue-neutral tax simplification. Should the economic recovery create sufficient fiscal space, we will consider a gradual reduction in social contributions, the high incidence of which weighs heavily on competitiveness, employment creation, and labor market practices. On the spending side, the wage bill will be kept within the agreed limit, as a nominal wage increase is balanced by elimination of the thirteenth salary and the holiday bonus. We have also maintained a freeze in the pension point. Public employment reductions will continue with

the policy of replacing only 1 of 7 departing workers on average across the public sector. We remain committed to the implementation of the recently approved wage and pension reform legislation, which will generate significant savings in the coming years, while at the same time protecting the viability of the second pension pillar. Following recent action to incorporate *stimulente* into base wage, we will eliminate by government ordinance the legal basis of *stimulente* funds effective January 1, 2012 (structural benchmark end-June). To encourage tax collection efforts, performance bonuses may be granted to tax collectors within the 30 percent bonus limit (as defined in the implementing legislation) for sustained improvements in revenues. Further savings have been secured through the overhaul of the social assistance system. By end-July, we will improve the legislation to provide heating allowances to target the most vulnerable members of society, while generating significant savings for the budget. Health (¶14 and 15) and education reforms will continue to improve quality and generate savings. Within the budget envelope, we have allocated additional resources to investment in the first half of the year, so as to improve absorption of EU funds. If absorption improves sufficiently, we will work on solutions to create greater fiscal space for investment from mid-2011. In addition, we will implement a reporting system for the state-owned enterprises (SOEs) that have been recently added (or will be added in 2011) to the ESA definition of the general government.[1] Once we start receiving timely information, at the time of the next review, we will request that the performance criterion on general government overall balance be amended to add the deficit of these entities.

9. For 2012, we aim to bring the deficit down to within 3 percent of GDP (in both cash and ESA terms). This will require compliance with the fiscal responsibility law and continued expenditure restraint, including on the wage bill. We will strictly limit further *ad hoc* changes to the tax system to ensure predictability and stability. We have started preparing the medium-term Fiscal Strategy for 2012–14, an important step in implementing the Fiscal Responsibility legislation, and will use this process to improve budget planning and solidify our commitment to the Maastricht targets. We will strengthen the recently established Fiscal Council, by providing it with adequate funding, so as to ensure that it is fully staffed with appropriately skilled people.

10. We will conduct a stocktaking of arrears and unpaid bills as of end-December 2010 for the entire general government and SOEs (structural benchmark, end-April 2011[2]). This exercise will ensure that they provide the Ministry of Public Finance (MOPF) with details of

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[1] Specifically, we will require monthly cash revenues, expenditures, and overdue payment bills statements as well as final quarterly fiscal statements as provided by other general government entities within the same deadline.

[2] For local government SOEs, the stocktaking of arrears and unpaid bills as of end-December will be completed by end-June 2011.

all arrears and unpaid bills incurred as of end-2010[3], with no payments subsequently authorized for any bills not registered in this exercise. We will also develop an action plan by end-April 2011, including an improved commitment control mechanism and enforcement measures, to eliminate existing arrears and prevent the accumulation of new ones at both the general government level and SOEs. Over the next two years the period for paying bills after submission will be reduced. A forthcoming EU directive in this area will be transposed into Romanian law on a timely basis. At the central level, we have recently reduced arrears substantially and will keep state and social security sector arrears near zero as agreed previously (performance criterion). New legislation on local government finance that took effect on January 1, 2011 will also allow for greater control of local government arrears, for which an indicative target will be established. The first phase in the integration of the accounting reporting system with the Treasury payment system is complete (structural benchmark, March 15, 2011). The next phase, the design of the system, including the commitment control and reporting module for all levels of government, will be completed by end-September 2011.

11. We have improved our financing strategy and will continue to focus on extending the maturity of our domestic debt, building the yield curve, and consolidating the financial buffers, guided by the recently prepared debt management strategy, which will be updated and published annually. We are launching a "euro medium-term notes" program that will maintain our presence in the external markets under more flexible issuance procedures and will help us balance the financing between the domestic and external markets. We are firmly committed to raising financial buffers to around four months of financing needs during 2011 and maintaining them there. To enhance our capabilities, in 2011 we will conduct a formal review of our debt management strategy with the assistance of IMF, EC, and WB experts. We will also improve treasury information technology (IT) systems and strengthen senior staffing.

12. We will continue our efforts to improve tax administration and fight tax evasion. The ordinance relating to high net wealth individuals was approved by end-December 2010, meeting the structural benchmark. An IMF expert has assisted in its subsequent implementation. We will staff the newly created Individual Analysis Office by end-March and develop and implement a compliance risk strategy in accordance with best practices by August 2011. Separately, the government decision on indirect audit methods will be passed (prior action), and we will develop an organizational strategy and implementation plan for incorporating these methods into our compliance functions by June 2011. As agreed with the IMF and EC, we will institute simplified taxation for smaller taxpayers under the threshold with help from the IMF and EC, while requesting a shift in the VAT mandatory threshold from the EU Council of Ministers to EUR 50,000 (structural benchmark, end-June 2011). We

[3] If required, the data will be verified with the help of external audit teams.

have unified several tax forms on social contributions starting this year. We are planning further simplification of tax forms and the number of payments required with a view to providing a one-stop shop for tax payments and expansion of e-filing. We will continue our efforts to introduce IT systems and consolidate the IT department in ANAF to improve tax administration. We have also started preparing the ANAF restructuring plan and will have a draft submitted to Parliament by end-April 2011. We will also provide a central point for screening and referral of potential cases of tax fraud and strengthen guidelines for identification of tax fraud.

13. The accelerated absorption of EU funds remains a focal objective of the government. Over the coming year, we will focus on strengthening the administrative capacity of units managing the funds; modernizing and consolidating the legislative and regulatory framework for public investment and other fields relevant for EU fund absorption; and prioritizing investment to assure sufficient financing for key projects. The government will also move the EU structural funds coordination unit from the MOPF to the Prime Minister's office and strengthen its authority and staffing. We will conduct a comprehensive review of the existing investment portfolio (including EU and non-EU funded projects), which will prioritize and evaluate the existing portfolio of projects to focus on those where funding can be fully secured within a medium-term horizon (e.g., 3-5 years), examine the viability of old projects, with low priority and non-performing ones discontinued, and will produce a database by June and a final report and an action plan by end-September 2011 (structural benchmark). We will create facilities for reallocating the capital budget during the year to those ministries with the best EU funds absorption performance and a track record of efficient project implementation.

14. The government will continue restructuring the health sector to ensure the quality functioning of the health care system within budgetary allocations going forward. We have reduced health payment arrears by end-December 2010 and continue implementing measures in line with our previous commitments. To achieve an appropriate balance between the need to preserve adequate healthcare services and to control costs, we have submitted legislation establishing a copayment system to Parliament; limited the number of contracted hospital in-patients by 10 percent relative to the 2010 levels; reduced the price markup paid by the government for drugs in the national programs (list C2); reduced the share of per-capita reimbursement of doctors from 70 to 50 percent. We are implementing a transparent and integrated IT system in the health sector to monitor and increase efficiency of health spending, where a significant number of questionable claims have already been uncovered. We have also asked the Court of Accounts to audit registrations of patients in primary care.

15. The following health sector measures agreed previously are currently under preparation: (i) clarifying the legislative framework for the claw back tax on drug suppliers; (ii) restructuring the hospital system; (iii) eliminating mandatory contracting with all hospitals, allowing competitive contracting with selected hospitals while ensuring transparency and oversight; (iv) providing indicative caps for quarterly services contracted with hospitals and physicians with the development of incentives for physicians who remain

within the ceilings; and (v) reforming, with assistance from the WB, the package of benefits insured by the government to exclude coverage of costly nonessential health services. We will also analyze and revise, with the assistance of the WB, the formula for the National Health House by the introduction of a mechanism whereby "money follows the patient." We will revise the list of compensated and free drugs approved by government decision 720/08, with a view toward modifying the list of these drugs and wherever possible moving to generics. For 2012, pharmaceutical costs of the most expensive drugs will be further controlled by applying strict drug use protocols and a new electronic prescription module for the National Health Information System, following strict procedures. Lastly, we will review hospital budgets and start implementing the hospital rationalization strategy with the objective of reducing the number of financed hospital beds (currently 135,200) to the EU per capita average by 2013, while also adapting acute beds accordingly. To reach this objective, by end-June 2011 we will reduce the number of beds to 133,000, and 129,500 by end-December 2011.

Financial Sector

16. The rise in non-performing loans slowed significantly during the final quarter of 2010, reaching 11.9 percent of total loans of the banking sector. As the economic recovery gains ground, and loan loss provisions stabilize over the first half of 2011, the banking sector as a whole is expected to return to profitability. The banks remain well capitalized, at 14.7percent, with all banks posting a solvency ratio above 11 percent at the end of 2010. The parents of the largest foreign subsidiaries maintained aggregate exposures under the European Bank Coordination Initiative (EBCI) at 98 percent at end-January 2011, well above the new target of 95 percent of end-March 2009 exposure. We intend to pursue discussions on an extension of the EBCI agreement, with a view toward gradually easing exposure commitments from banks as international market conditions improve.

17. We will maintain close vigilance over developments in the banking sector and continue to strengthen the financial safety net. The NBR, in conjunction with the DGF, will develop procedures for deploying the new restructuring powers, and will prepare contingency plans. We will also ensure that the DGF has ready access to liquidity to meet any potential shortfalls in funding, and to develop joint procedures, as agreed with the MOPF, for accessing the funds if necessary to help preserve depositor confidence and financial stability. The authorities will take the necessary measures to ensure that consolidation in the banking sector will deliver strong and well capitalized institutions with a shareholder base that can support them. The authorities will review the DGF, banking and the winding-up legislation to ensure their mutual consistency. To facilitate better bank access to NBR liquidity, the NBR will widen the range of assets acceptable as collateral for its refinancing operations to bonds issued locally by international financial institutions which are listed at the Bucharest Stock Exchange, as well as Eurobonds issued by the Government.

18. The NBR will prepare and release for consultation by end-June 2011 proposals for prudential filters that would preserve prudent bank solvency, provisions, and reserves, and enable the timely introduction of IFRS at the beginning of 2012. The authorities will ensure that the prudential treatment of debt-for-equity swaps does not result in a weakening of banks' financial positions[4] and impose requirements for banks to have in place methodologies for valuing the equity at the lowest value applicable according to the accounting treatment. We will monitor developments in foreign currency lending and take steps as needed to ensure that foreign currency credit is appropriately priced in order to reflect the risk of lending in foreign exchange to un-hedged borrowers. We will continue to consult with the IMF and EC staff before introducing or amending other aspects of the regulatory framework and make efforts to avoid adopting legislative initiatives, such as the current draft of the personal insolvency law or proposals for the debt collecting law, which could undermine debtor discipline. The current in-house banking executors shall have the possibility to join the liberal profession of public judicial executors without any formal restrictions and entry barriers such as professional admission licensing and/or exams as well as admission fees or taxes of any kind, and they shall become members of the above profession with full professional guarantees, rights, and obligations.

Monetary and Exchange Rate Policy

19. The NBR remains committed to bring inflation down to within the official target band of 3 percent ± 1 percentage point in 2011 and 2012. As under the existing program, progress towards these goals will be monitored using an inflation consultation clause (see TMU). The effects of last July's VAT rate increase on inflation have been roughly as expected. However, inflation in recent months was further boosted by food and fuel price pressures. After peaking around 8 percent, headline inflation is expected to gradually return to the NBR's target band in the second half of 2011. While existing slack in the economy would foster disinflation, risks are tilted to the upside, as food and energy prices may rise by more than expected and forthcoming SOE reforms may require increases in administered prices. Monetary policy easing may be resumed during 2011 provided major risks do not materialize and inflation remains close to the projected path.

20. Under the program, we anticipate increases in Gross International Reserves in 2011 (mostly reflecting multilateral disbursements) and 2012. They will provide improved confidence in the economy and allow for greater reserve coverage of short-term foreign

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[4] The prudential treatment of debt-for-equity swaps should guarantee that: (i) the involvement of credit institutions in such operations unfolds on the basis of a prudent decision making process; (ii) the value of equity is fully deducted from the own funds of credit institutions to avoid an artificial improvement in prudential indicators; and (iii) the revenues obtained by releasing loan-loss provisions due to these operations are not taxed.

liabilities. A performance criterion will be established on Net Foreign Assets that is consistent with this projection for gross reserves accumulation. Reserve losses exceeding €2 billion in any 30-day period during the program will trigger consultation with IMF staff.

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

Growth and Flexibility Enhancing Structural Reforms

State-Owned Enterprises

22. We are committed to deep-rooted reform of state-owned enterprises (SOEs), especially in critical growth generating sectors such as energy and transport. In recent years, many SOEs have become an increasingly substantial fiscal burden. In addition to requiring subsidies to cover considerable losses, they have accumulated arrears of more than 4 percent of GDP. The quality of service in many sectors is in need of significant improvements and weighs on growth by hindering further private sector development.

23. Implementing a comprehensive strategy addressing the viability of SOEs and reforming their governance will be vital. We will develop strategic action plans[5] by end-April 2011 for key firms (as specified in ¶20 of the TMU, structural benchmark) and end-July 2011 for all other firms that: (i) provides up-to-date information on the financial viability of each SOE with majority government ownership, and each *regii autonome* (autonomous institution, AI); (ii) classifies each as being in line for either liquidation, privatization, or retention (with restructuring as needed), (iii) outlines the steps to achieve closure, viability, or privatization; and (iv) lays out concrete plans to substantially reduce arrears (e.g. through payback, securitizations, swaps, etc.). We will implement a system to report main financial and economic indicators of all SOEs and AIs to the MOPF on a monthly basis. We will also amend ordinance 79/2008 to require that AIs and enterprises subordinated to local governments submit quarterly key financial and operational indicators to the MOPF. For key privatizations (¶25, 26)[6], an internationally recognized transaction advisor will be appointed by end-August 2011, proposals submitted by end-2011, and tenders made by mid-2012. To address problems in SOE governance, we will develop (in consultation with the WB) and approve legislation to improve governance in these firms, to require regular independent

[5] The strategic action plans will be reviewed by the WB.

[6] In addition to those listed below, we will begin analysis for privatization of the government's remaining stake in Oltchim.

external audits, and to move financial control of SOEs from line ministries to the MOPF by end-September 2011.

24. Securing efficient energy provision is crucial for sustainable growth. The energy sector suffers from underinvestment due to the effects of the economic downturn, the dominance of undercapitalized state-owned firms with room for efficiency improvements, and the fact that adjustments have not been fully applied in regulated prices and tariffs (due to concerns about effects on consumers). To address pricing and regulatory deficiencies, we will: (i) take the necessary steps to restore the energy regulator's (ANRE) operational and financial autonomy in accordance with EU legislation (third energy package); (ii) present a roadmap for phasing out regulated prices in electricity and gas by September 2011; (iii) define the vulnerable consumers by end-2011 according to EU legislation and develop mechanisms to protect them (in conjunction with the Ministries of Finance and Labor); (iv) complete removal, according to EU directives, of regulated prices for non-households in electricity and gas before end 2013[7] and complete the process by end-2015; and (v) assure that new bilateral contracts signed by state-owned gas and electricity generators be made transparently and non-discriminately through OPCOM (electricity) and other competitive procedures (gas), and that prices in existing contracts will be adjusted to prevailing market rates as quickly as legally permissible.

25. Much needed capital and managerial know-how will be brought to the energy sector through minority private investors (via IPOs or sales of stakes to strategic partners) in the following firms, with government approval: (i) Petrom (sale of a 10 percent stake is already underway); (ii) Transelectrica (15 percent stake by end-2011); (iii) Transgaz (15 percent stake by end-2011); and (iv) Romgaz (15 percent stake by spring 2012). If we succeed with our strategy to form the two national champion companies we will introduce appropriate mechanisms to ensure there is no cross-subsidization, in conjunction with recommendations of the Competition Council. If the national champion strategy is not successful by end-2011, we will look for an alternative solution, including by privatizing majority stakes in some energy firms. In the meantime, to bring investment into the sector we will move ahead to prepare sales of minority or strategic stakes in individual firms slated to be included in the national champion companies (which could later be converted to stakes in the combined firms).[8] The tax administration, ANAF, will use continued enforcement procedures on the tax arrears of CNH, which will ultimately lead to the selling of viable assets, possibly applying insolvency procedures. Remaining coal assets will be liquidated in line with EU stated rules. In Termoelectrica, viable assets will be separated and the remaining operations closed.

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[7] By April 1, 2011 a calendar will be established for adjustments to reach the full Unitary Gas Cost (CUG) price formula by end-2011 for non-residential consumers.

[8] Among the firms slated to be included in the national champions where strategic investments will be sought are the energy complexes in Craiova, Turceni, and Rovinari.

26. Private sector growth is severely constrained by inadequate transportation infrastructure. Addressing this weakness will lower production costs, improve export possibilities, and make Romania a more attractive destination for investment. Full execution of Ministry of Transport investment plans (particularly those with EU co-financing) will be crucial (¶13). Following EU rules on state aid, state-owned transport firms must also be privatized or restructured to provide needed service improvements. Actions will include the following:

Roads

- CNADNR will boost its revenues in 2011 while eliminating or renegotiating non-performing contracts.
- The Ministry of Transport will seek to balance road and rail transportation by reducing road transport.

Railways

- We will extend the policy of standard costs in the railway system, particularly for railway infrastructure procurement and for repairing rolling stock. We will develop multi-annual plans for public procurement and investments in CFR Calatori and CFR Marfa, in line with transport and necessities programs and in connection with market evolution. In CFR Infrastructura, CFR Calatori and CFR Marfa we will continue to use fully depreciated assets. Restructured personnel will be provided with reintegration and training services.
- *Cargo*- A minority stake in CFR Marfa will be offered in order to attract a strategic investor by end-2011 with a view toward a full privatization when market conditions permit.
- *Passenger*- Efficiency of the passenger rail service will be increased through restructuring of CFR Calatori, including by modifying its passenger service contracts, better cost recovery (including allowing for higher tariffs), and significant reductions in its scope of service. A strategic plan will aim at a 15 percent reduction in losses and no accumulation of new arrears in 2011.
- *Infrastructure*- Service reductions will also significantly improve the financial outlook for CFR Infrastructura. We will close 1000 kilometers of railway lines by end-August and will develop plans for competitive tendering of public service obligations and infrastructure maintenance on lines for another 20 percent of the system or close them. A strategic plan will aim at a 25 percent reduction in losses and no accumulation of new arrears in 2011.

Metropolitan transit

- We will pass legislation to establish a new metropolitan transit authority that will oversee Metrorex together with the above ground public transport system in Bucharest (RATB). The law will also allow for greater tariff adjustments (beyond inflation-indexing) in line with the strategic plan of covering current expenditures through revenues and capital expenditures through subsidies. Metrorex will diminish maintenance costs by 30 percent by end 2011.

Air transport

- We will complete an analysis for Tarom by end-April 2011, with a view toward seeking a strategic investor.

Labor Markets

27. We are making important legislative changes to increase the flexibility of the labor market, improve the efficiency of collective bargaining (while protecting the rights of workers and employers), and increasing labor force participation. We have finalized a draft law on amending the labor code and are processing the social dialogue code, which will consolidate the laws on trade unions, labor conflict resolution, employer association, collective labor contract, and Economic and Social Council. Both the amended labor code and the social dialogue code are expected to be approved by Parliament in the coming months. In addition, we will request that the International Labor Organization conduct a review of labor inspections to improve enforcement and address the large informal labor market in Romania. Improving the efficiency of social protection will remain a priority, especially in the area of social inspection.

Business Climate

28. Designed to improve the business climate, structural reforms in this program are growth-promoting. Infrastructure investment and efficiency will be boosted both from greater absorption of EU structural funds (¶13) and the restructuring, closing, or privatization of SOEs, especially in energy and transport (¶22–26). More broadly, steps to reduce tax compliance costs (¶12) and improve governance, as well as public procurement and contracting reforms, will reduce bureaucratic costs and impediments for the private sector. We will also undertake reforms in the agriculture sector—including by speeding up the surveying and registration of agricultural land—to improve food security and increase export prospects. We will work together with the EU to address concerns regarding the new public private partnership law.

Program Monitoring

29. The program will be monitored through quantitative performance criteria and indicative targets, structural benchmarks and consultation clauses, during quarterly reviews. Table 3 sets out specific quarterly targets that are to be observed under the SBA for the overall general government balance, guarantees provided by the general government, the change in arrears for the central government and social security system, CPI inflation, and net foreign assets. In addition, there will be indicative targets on the current primary expenditure of the general government, the operating balances and arrears of SOEs. We have also agreed with Fund staff on a prior action and structural benchmarks in Table 4. The first review should be completed by end-June, 2011, and the second review by end-September, 2011.

Safeguards

30. Progress has been made by the NBR on the recommendations contained in the safeguards assessment performed under the May 2009 SBA. To evaluate this progress, we will authorize the National Bank's external auditors to provide IMF staff with all necessary information and to discuss directly with them any issues relevant to this process. We also commit to receiving a safeguards mission, and to provide that mission with all necessary information requested without delay. The safeguards assessment update should be completed by the time of the first review of the SBA end-June, 2011.

/s

Gheorghe Ialomiţianu
Minister of Public Finance

/s

Mugur Isarescu
Governor of the National Bank of Romania

Attachments

Table 1. Romania: Quantitative Program Targets for Seventh Review

	2008	2009				2010					2011		
	Dec	March	June	Sept	Dec	March	June	Sept	Dec		January		March
	Actual	Actual	Actual	Actual	Actual	Actual	Actual	Actual	Prog.	Actual	Prog.	Actual	Indicative
I. Quantitative Performance Criteria													
1. Change in net foreign assets (mln euros) 1/ 2/	25,532	-3,468	-5,119	-4,566	-4,874	779	-509	-318	-2,000	-750	0	855	350
2. Floor on general government overall balance (mln lei) 3/ 4/ 5/	-24,655	-8,300	-14,456	-25,563	-36,101	-8,422	-18,015	23,732	-34,054	-33,621	…	…	-6,300
3. Stock in general government arrears (bn lei)	1.06	1.41	1.55	1.4	1.50	1.76	1.8	1.57	0.48	1.13	…	…	0
4. Ceiling on general government guarantees issued since start of program (face value, bn lei)	…	…	0.02	0.8	2.2	4.6	5.5	6.5	12.0	7.6	…	…	12.0
II. Continuous Performance Criterion													
5. Nonaccumulation of external debt arrears	0	0	0	0	0	0	0	0	0	0	0	0	0
III. Inflation Consultation													
6. 12-month rate of inflation in consumer prices													
Outer band (upper limit)	…	…	8.4	7.7	6.5	6.5	6.0	10.0	10.0	…	…	…	9.0
Inner band (upper limit)	…	…	7.4	6.7	5.5	5.5	5.0	9.0	9.0	…	…	…	8.0
Actual/*Center point*	6.3	6.7	5.9	4.8	4.7	4.2	4.4	7.8	8.0	8.0	…	…	*7.0*
Inner band (lower limit)	…	…	5.4	4.7	3.5	3.5	3.0	7.0	7.0	…	…	…	6.0
Outer band (lower limit)	…	…	4.4	3.7	2.5	2.5	2.0	6.0	6.0	…	…	…	5.0
IV. Indicative Target													
7. General government current primary spending (excl. EU funds and social assistance, mln lei) 3/	92,327	22,149	43,238	63,878	85,637	32,749	66,124	98,721	131,500	131,938	…	…	32,000
8. Operating balance (earnings before interest and tax) net of subsidies of 10 SOEs, defined in TMU (mln. lei) 3/						-1,081	-2,333	-3,801	-4,000	-5,542	…	…	-750
Memorandum Item:													
Revenue of general government, net of EU funds (mln. lei) 3/	…	…	…	…	151,508	36,355	74,669	116,091	157,950	159,141	…	…	40,100

1/ The December 2008 figure is a stock.
2/ Performance criterion for January 2011 and indicative target for March 2011 are relative to December 2010 target.
3/ Cumulative figure during calendar year (e.g. March 2011 figure is cumulative from January 1, 2011).
4/ In accordance with TMU, the end-September and end-December program targets were adjusted from the original target of -28,200 and -34,650 by one-half of the revenue over-performance.
5/ The target for March 2011 can be adjusted with higher or lower capital spending as defined in TMU.

Table 2. Romania: Performance for Seventh Review

Measure	Target Date	Comment
Quantitative performance criteria		
1. Floor on general government overall balance	December 31, 2010	Met
2. Ceiling on general government guarantees	December 31, 2010	Met
3. Ceiling on general government domestic arrears	December 31, 2010	Missed
4. Non-accumulation of external debt arrears	December 31, 2010	Met
5. Floor on net foreign assets	January 31, 2011	Met
Quantitative Indicative Target		
1. Ceiling on general government current primary spending	December 31, 2010	Missed
2. Floor on the operating balance of ten largest loss-making SOEs	December 31, 2010	Missed
3. Floor on net foreign assets	March 31, 2011	Likely to be met
Inflation consultation band		
Inner band	December 31, 2010	Met
Outer band	December 31, 2010	Met
Structural benchmarks		
1. Parliamentary ratification of amendments to the bank resolution framework	December 1, 2010	Partially met
2. Reform tax administration methodology for high net wealth individuals	December 31, 2010	Met
3. First phase to integrate the accounting reporting system with the Treasury payment system	March 15, 2011	Met
4. Amend legislation to allow the use of the deposit guarantee fund resources to facilitate bank restructuring, including purchase and assumption transactions	March 15, 2011	Likely to be missed, reset for July 31, 2011

Table 3. Romania: Quantitative Program Targets for New Program

	2010	2011			
	Dec	March	June	Sept	Dec
	Actual	Prog.	Prog.	Indicative	Indicative
I. Quantitative Performance Criteria					
1. Change in net foreign assets (mln euros) 1/ 2/	20,026	250	250	500	500
2. Floor on general government overall balance (mln lei) 3/ 4/	-33,621	-6,300	-12,600	-17,150	-23,953
3. Stock of central government and social security arrears (bn lei)	0.19	0.20	0.20	0.15	0.10
4. Ceiling on general government guarantees issued since end-2008 (face value, bn lei)	12.0	14.0	14.0	14.0	14.0
II. Continuous Performance Criterion					
5. Nonaccumulation of external debt arrears	0	0	0	0	0
III. Inflation Consultation					
6. 12-month rate of inflation in consumer prices					
Outer band (upper limit)	…	9.0	8.8	6.2	5.7
Inner band (upper limit)	…	8.0	7.8	5.2	4.7
Actual/*Center point*	8.0	*7.0*	*6.8*	*4.2*	*3.7*
Inner band (lower limit)	…	6.0	5.8	3.2	2.7
Outer band (lower limit)	…	5.0	4.8	2.2	1.7
IV. Indicative Target					
7. General government current primary spending (excl. EU funds and social assistance, mln lei) 3/	131,938	32,000	64,000	95,600	128,550
8. Operating balance (earnings before interest and tax) net of subsidies of key SOEs (as defined in TMU (bn. lei)) 3/	-6.5	-1.7	-2.7	-3.6	-4.0
9. Stock of arrears of key SOEs (as defined in TMU (bn. lei))	18.8	19.5	19.5	19.0	18.0
10. Stock of local government arrears (bn lei)	0.91	0.95	0.90	0.85	0.80
Memorandum Item:					
Revenue of general government, net of EU funds (mln. lei) 3/	159,141	40,100	82,250	127,000	171,575

1/ The end-December 2010 figure is a stock.
2/ Cumulative flows relative to end-December 2010 stock.
3/ Cumulative figure during calendar year (e.g. March 2011 figure is cumulative from January 1, 2011).
4/ The target for March 2011 can be adjusted with higher or lower capital spending as defined in TMU.

Table 4. Romania: Conditionality for New Program

Measure	Target Date	Comment
Prior action		
The government decision on indirect audit methods will be passed (¶12).		
Quantitative performance criteria		
1. Floor on general government overall balance	Quarterly	
2. Ceiling on general government guarantees	Quarterly	
3. Ceiling on central government and social security domestic arrears	Quarterly	
4. Non-accumulation of external debt arrears	Continuous	
5. Floor on net foreign assets	Quarterly	
Quantitative Indicative Target		
1. Ceiling on general government current primary spending	Quarterly	
2 Ceiling on local government domestic arrears	Quarterly	
3. Floor on the operating balance and arrears of key loss-making SOEs	Quarterly	
Inflation consultation band		
Inner band	Quarterly	
Outer band	Quarterly	
Structural benchmarks		
1. Completion of a stocktaking of arrears and unpaid bills as of end-December 2010 for the entire general government and SOEs (¶10).	April 30, 2011	
2. Preparation of strategic action plans for key SOEs (as specified in TMU) (¶23).	April 30, 2011	
3. Introduction of a simplified taxation system for smaller taxpayers under the threshold with help from the IMF and EC, while requesting a shift in the VAT mandatory threshold from the EU Council of Ministers to €50,000 (¶12).	June 30, 2011	
4. Eliminate by government ordinance the legal basis of *stimulente* funds, effective January 1, 2012 (¶8).	June 30, 2011	
5. Amend legislation to allow the use of the deposit guarantee fund resources to facilitate bank restructuring, including purchase and assumption transactions (¶4).	July 31, 2011	
6. Completion of a comprehensive review of the existing investment portfolio, which will prioritize and evaluate existing projects to focus on those where funding can be fully secured, examine the viability of old projects, with low priority and unviable ones discontinued, and production of a final report and an action plan (¶13).	September 30, 2011	

APPENDIX II. ROMANIA: TECHNICAL MEMORANDUM OF UNDERSTANDING (TMU)

March 10, 2011

31. This Technical Memorandum of Understanding (TMU) defines the variables included in the quantitative performance criteria and indicative targets set out in the letter of intent (LOI), the key assumptions, methods to be applied in assessing program performance, and the reporting requirements to ensure adequate monitoring of economic and financial developments. The quantitative performance criteria and indicative targets, and structural benchmarks for 2011 are listed in Tables 3 and 4 of the LOI, respectively.

2. For the purposes of the program, *the exchange rates* of the Romanian Leu (RON) to the euro is set at RON 4.2848 = €1, to the U.S. dollar at RON 3.2045 = $1, to the Japanese yen at RON 3.9400 = ¥100, and to the pound sterling at RON 4.9673 = £1, the rates as shown on the National Bank of Romania's (NBR's) website as of December 31, 2010. The exchange rates to other currencies, where applicable, will also be the ones shown on the NBR's website as of December 31, 2010.

3. For the purposes of the program, the *general government* includes the entitie*s as defined in the* 2011 budget. These are: the central government (state budget, treasury, self-financed state entities included in the budget, etc.), local governments, social security funds (pension, health, and unemployment), road fund company, and administration of the property fund. This definition of general government also includes any new funds, or other special budgetary and extra budgetary programs that may be created during the program period to carry out operations of a fiscal nature as defined in the IMF's *Manual on Government Finance Statistics 2001*. The authorities will inform IMF staff of the creation of any such new funds or programs immediately. As mentioned in the LOI (¶8), this definition will be expanded at the time of the first review under the SBA to cover state-owned enterprises incorporated into the general government accounts under ESA.

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

A. Floor on the Change in Net Foreign Assets

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

5. NFA of the NBR are defined as the euro value of gross foreign assets of the NBR (including reserve requirements of the commercial banking system held at the NBR) minus gross foreign liabilities of the NBR; and will be measured on the basis of the NBR's operational rather than accounting definitions. Non-euro denominated foreign assets and liabilities will be converted into euro at the program exchange rates.

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

7. Gross foreign liabilities of the NBR are defined as all foreign exchange liabilities to residents and nonresidents, including commitments to sell foreign exchange arising from derivatives (such as futures, forwards, swaps, and options), and all credit outstanding from the IMF, but excluding (i) banks' foreign currency deposits against reserve requirements; and (ii) government foreign currency deposits at the NBR. This definition is meant to bring the concept of foreign liabilities closer to the balance of payment definition, on which the targets are based.

Floor on cumulative change in NFA from the beginning of the year (in mln. euros)[1]

	2010	2011			
	December (stock)	March PC	June PC	September indicative	December indicative
Cumulative change in NFA	20,026	250	250	500	500
Memorandum Item: Gross Foreign Assets	32,432	1000	1000	1000	1000

[1]PC = performance criterion; data for end-month. Flows in 2011 are cumulative from the beginning of the calendar year (e.g., March 2011 figure is cumulative from January 1, 2011). The 2011 stocks are obtained by adding 2011 flows to end-2010 stock.

8. NFA targets will be adjusted upward (downward) by the surplus (shortfall) in program disbursements relative to the baseline projection. Program disbursements are defined as external disbursements from official creditors (World Bank and the EC) that are usable for the financing of the overall central government budget. The NFA targets will also be adjusted upward by the increase in commercial bank reserve requirements held with the NBR relative to end-December, 2010 (€6,797 million), measured at program exchange rates.

External program disbursements–Baseline projections (in mln. euros)

	2011			
	March	June	September	December
Cumulative flows from end of previous year	1,500	1,650	2,050	2,050

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

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

	2010	2011			
	December (actual)	March (target)	June (target)	September (indicative)	December (indicative)
Outer band (upper limit)		9.0	8.8	6.2	5.7
Inner band (upper limit)		8.0	7.8	5.2	4.7
Actual / *Center point*	8.0	*7.0*	*6.8*	*4.2*	*3.7*
Inner band (lower limit)		6.0	5.8	5.2	2.7
Outer band (lower limit)		5.0	4.8	4.2	1.7

C. Performance Criterion on General Government Balance

10. The budget deficit will be monitored quarterly through the cash balance of the general government. The authorities will consult with IMF staff on corrective measures in the event of shortfalls in government revenue and financing.

Cumulative floor on general government balance[1]

	(In millions of lei)
End-December 2010 (actual)	-33,621
End-March 2011 (performance criterion)	-6,300
End-June 2011 (performance criterion)	-12,600
End-September 2011 (indicative)	-17,150
End-December 2011 (indicative)	-23,953

[1] Cumulative figure during calendar year (e.g., March 2011 figure is cumulative from January 1, 2011).

11. The budget deficit will be measured from above the line using the budget execution data. At the time of the first review the calculation of the 2011 budget deficit will be modified to be in line with the expanded definition of the general government which will include the following SOEs (the data is expected to become available at the end of 2011Q1)[1]: Compania Nationala a Huilei S.A., Compania Nationala de Atostrazi si Drumari Nationale, Fondul Proprietatea, Metrorex S.A., Regia Autonoma Administratia Fluviala a Dunarii de Jos Galati, Societatea Nationala a Carbunelui S.A., Societatea Nationala de Transport Feroviar de Calatori, Compania Nationala de Radiocomunicatii Navale Radio Constanta, Societatea Nationala de Transport Feroviar de Infrastructura, Termoelectrica S.A., Acvavalor S.A., Aeroportul Arad S.A., Aeroportul Iasi RA, Aeroportul International Baia Mare R.A., Aeroportul Satu Mare R.A., Aeroportul Stefan Cel Mare Suceava R.A., Aeroportul Transilvania – Tirgu Mures R.A., Aeroportul Tulcea, Aqua Calor S.A., Centrala Electrica de Termoficare Brasov S.A., Citadin S.A. Hundedoara, Dalkia Romania S.R.L., Edil Therma Hunedoara, Goscomloc S.A., Gospodarie Oraseneasca S.A., Rominservices Therm S.A., Societatea Nationala "Aeroportul International Mihail Kogalniceanu", T.S.P Ecoterm S.A., Termica S.A., Termloc S.A., Uzina Termica Comanesti S.A.

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

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

13. If the difference between the general government deficit measured from above the line and from below the line is larger than lei 200 million each quarter during 2011, the MOPF will consult with IMF staff.

14. In the event that non-grant revenues exceed those projected under the program, the deficit target will be adjusted downward by one half of the surplus to allow for additional capital spending while reducing the deficit further. The following table shows the

[1] The list of SOEs to be included in the definition of general government will be determined by Eurostat at end-March, including possible revisions to those SOEs already incorporated.

accumulated projected non-grant revenue for 2011, to which the actual non-grant revenue will be compared.

Cumulative projected revenue of general government, net of EU funds[1]	(In millions of lei)
End-December 2010 (actual)	159,141
End-March 2011 (projection)	40,100
End-June 2011 (projection)	82,250
End-September 2011 (projection)	127,000
End-December 2011 (projection)	171,575

[1]Cumulative figure during calendar year (e.g., March 2011 figure is cumulative from January 1, 2011).

15. The performance criterion for the general government balance for the first quarter of 2011 will be adjusted downward from -6,300 by the amount that capital spending (including EU funds-related spending) exceeds 5,740 million lei, up to a limit of -8,000 million. Likewise, the target will be adjusted upward by the amount that capital spending undershoots 5,740 million lei in the first quarter of 2011.

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

16. The issuance of general government guarantees to the non-financial private sector and public enterprises will be limited during the program period. This ceiling is set at RON 14 billion but may be adjusted upward by up to RON 9.6 billion for guarantees for financing the Nabucco project. Revision to targets will be renegotiated during future missions to allow for reasonable public guarantees in the context of privatization of majority stakes in state-owned enterprises and securitization of domestic payment arrears.

Ceiling on new general government guarantees issued from end-2008 until:	(In billions of lei)
End-December 2010 (actual)	7.6
End-March 2011 (performance criterion)	14
End-June 2011 (performance criterion)	14
End-September 2011 (indicative)	14
End-December 2011 (indicative)	14

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

17. The performance criterion established on the stock in domestic payments arrears of the central government and social security sector (as defined in ¶3 above) contemplates their elimination during the program period. The stock will be measured net of intergovernmental arrears, but both gross and net arrears will be reported by the government. In case of need,

the government will take corrective measures to prevent the accumulation of new spending arrears. For the purpose of the program, arrears mean accounts payable past due date by 90 days (in line with ESA95 definitions for expenditures).

Stock of central government and social security arrears	(In billions of lei)
End-December 2010 (stock, actual)	0.19
End-March 2011 (performance criterion)	0.20
End-June 2011 (performance criterion)	0.20
End-September 2011 (indicative)	0.15
End-December 2011 (indicative)	0.10

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

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

G. Indicative Target on General Government Current Primary Spending

19. The indicative target on current primary expenditure of the general government is defined as spending on personnel, goods and services excluding EU funds (specified under external grant category), subsidies, transfers to public entities, pensions (social security budget in social assistance category), state aid and other spending in other transfers category, Reserve Fund, and other expenditure as classified in the monthly reporting tables. The current spending target will be adjusted for the extra spending due to swap arrangement between local governments and public enterprises by an amount spent in the respective quarter.[1]

[1] The swap arrangement would involve mutually cancelling overdue tax obligations of public enterprises with arrears owed to those enterprises by the general government (local administration).

Cumulative change in general government current primary expenditures[1]	(In millions of lei)
End-December 2010 (actual)	131,938
End-March 2011 (indicative)	32,000
End-June 2011 (indicative)	64,000
End-September 2011 (indicative)	95,600
End-December 2011 (indicative)	128,550

[1] Cumulative figure during calendar year (e.g., March 2011 figure is cumulative from January 1, 2011).

H. Indicative Target on Local Government Arrears

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

Stock in local government arrears	(In billions of lei)
End-December 2010 (stock, actual)	0.91
End-March 2011 (indicative)	0.95
End-June 2011 (indicative)	0.90
End-September 2011 (indicative)	0.85
End-December 2011 (indicative)	0.80

I. Monitoring of Public Enterprises

21. A quarterly indicative target for 2011 is set on the aggregate operating balance (earnings before interest and tax) net of subsidies, accumulated per calendar year, of the following public enterprises: C.N. Căi Ferate CFR S.A., C.N. de Autostrãzi de Drumuri Naționale din România S.A., C.N. a Huilei S.A., C.N. Poşta Românã S.A., S.C. Complexul Energetic Turceni S.A., S.C. Filiala de Intreținere și Servicii Energetice "Electrica Serv" - S.A., S.C. Metrorex S.A., S.N. de Transport Feroviar de Marfã ”CFR Marfã” S.A., S.N. Transport Feroviar de Călători ”CFR Călători” S.A., C.N. Tarom S.A., S.C. Electrocentrale București S.A., S.C. Electrica Furnizare Transilvania Nord S.A., S.C. Oltchim S.A., S.C. Termoelectrica S.A., SNa Lignitului Oltenia S.A., S.C. Electrificare CFR S.A., S. C. Intervenții Feroviare S.A., S. C. Telecomunicații C.F.R. S.A. The data shall be reported with operating results by firm. The targets will be as follows:

Cumulative operating balance[1]	(In billions of lei)
End-December 2010 (actual)	-6.5
End-March 2011 (indicative)	-1.7
End-June 2011 (indicative)	-2.7
End-September 2011 (indicative)	-3.6
End-December 2011 (indicative)	-4.0

[1] Cumulative figure during calendar year (e.g., March 2011 figure is cumulative from January 1, 2011).

22. A quarterly indicative target for 2011 is set on the stock of arrears of the public enterprises listed in ¶21 above. The data shall be reported at the firm level. The targets will be as follows:

Stock of arrears	(In billions of lei)
End-December 2010 (actual)	18.8
End-March 2011 (indicative)	19.5
End-June 2011 (indicative)	19.5
End-September 2011 (indicative)	19.0
End-December 2011 (indicative)	18.0

23. The quarterly indicative targets for the aggregate operating balance (¶21) and stock of arrears (¶22) for the public enterprises listed in ¶21 above will be revised at the time of the first review in accordance with the actions plans and audited end-2010 data (both of which will be available at that time).

J. Reporting Requirements

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

Romania: Data Provision to the IMF

Item	Periodicity
To be provided by the Ministry of Finance	
Preliminary monthly data on general government accounts, including public enterprises as defined by ESA95	Monthly, on the 25th day of the following month
Quarterly final data on general government accounts, including public enterprises as defined by ESA95	Quarterly cash data, on the 35th day past the test date; Quarterly accrual data, on the 55th day past test date
The budget deficit of the general government using ESA95 definition	Quarterly, with a lag of three months
Preliminary data on below-the-line financing for the general government	Monthly, with a lag of no more than 35 days past the test date
Final quarterly data on below-the-line financing for the general government	Quarterly, no later than 45 days past the test date
Total accounts payable and arrears of the general government, including local governments	Preliminary monthly, within the next month. Quarterly, within 55 days
Stock of the central government external arrears	Daily, with a lag of not more than seven days
Public debt and new guarantees issued by the general government	Monthly, within one month
Preliminary monthly data on general government primary spending, net of EU disbursements	Preliminary monthly data will be reported to IMF staff within 25 days
Final quarterly data on general government primary spending, net of EU disbursements	Quarterly, within 35 days from the test date
The operating balance, profits, stock of arrears, and personnel expenditures of key public enterprises (as defined in ¶21 and 22) by total expenditures	Quarterly, within 30 days
Data on EU project grants (reimbursements and advances), capital expenditures and subsidies covered by EU advances or eligible for EU reimbursement on EU supported projects specifically agreed with the EU	Monthly, within three weeks of the end of each month
The balance of the privatization receipts registered in the account of the State Treasury, details on any claims on these receipts and projected net outflows.	Monthly, within two weeks of the end of each month

To be provided by the National Bank of Romania	
NFA data, by components, in both program and actual exchange rates	Weekly, each Monday succeeding the reporting week and with a 3 working day lag in the case of end-quarter data
Monetary survey data in the format agreed with IMF staff	Monthly, within 30 days of the end of the month
The schedule of contractual external payments of the *banking sector* falling due in the next four quarters, interest and amortization (for medium and long-term loans)	Monthly, 45 days after the end of each month
The schedule of contractual external payments of the *corporate sector* falling due in the next four quarters interest and amortization (for medium and long-term loans)	Monthly, 45 days after the end of each month
The stock of short-term external debt of banks and corporate	Monthly, 45 days after the end of each month
Balance of payments in the IMF format currently used to report	Monthly, 45 days after the end of each month
Exposure (deposits, loans, subordinated loans) of (i) foreign parent banks to their subsidiaries in Romania; (ii) IFI and (iii) other creditors to banks in Romania (by national and foreign currency).	Monthly, 20 days after the end of each month

INTERNATIONAL MONETARY FUND

Romania—Assessment of the Risks to the Fund and the Fund's Liquidity Position

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

(In consultation with other Departments)

Approved by Thomas Krueger and Aasim Husain

March 11, 2011

1. **This note assesses the risks to the Fund arising from the proposed Stand-By Arrangement (SBA) for Romania and its effects on the Fund's liquidity, in accordance with the policy on exceptional access.**[1] The authorities are requesting a 24-month SBA with access of SDR 3,090.6 million (300 percent of quota). Disbursements are largely evenly phased with SDR 60 million (5.8 percent of quota) available upon approval, SDR 430 million (41.7 percent of quota) available once the first review is completed, followed by six equal quarterly disbursements of SDR 430 million each, and a small final disbursement (Table 1). The authorities intend to treat the proposed SBA as precautionary. It would succeed the existing SBA arrangement in the amount of SDR 11,443 million.

Table 1. Romania: Proposed SBA—Access and Phasing

			Percent of quota	
Availability	Date 1/	SDR mn	Purchase	Cumulative
2011	March (approval)	60.0	5.8	5.8
	June	430.0	41.7	47.6
	September	430.0	41.7	89.3
	December	430.0	41.7	131.0
2012	March	430.0	41.7	172.8
	June	430.0	41.7	214.5
	September	430.0	41.7	256.3
	December	430.0	41.7	298.0
2013	March	20.6	2.0	300.0
	Total	3,090.6	300.0	300.0

Source: Finance Department.
1/ Starting in June 2011, purchases will depend on the completion of a review.

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

I. BACKGROUND

2. **Romania has had an extensive financial relationship with the Fund (Table 2).** Romania is currently the largest Fund borrower, with credit outstanding at a historic peak of SDR 10,569 million as of end February 2011. Since 1991, a total of eight SBAs have been approved, of which the 2009 SBA with access of SDR 11,443 million (1,111 percent of quota) has been the largest so far. It aimed at supporting confidence during a period of large external adjustment and facilitated reducing external and fiscal imbalances, while ensuring financial stability by maintaining adequate capitalization and liquidity in the financial sector, with a view to bringing Romania back to a path of strong and balanced growth over the medium term. At the time of the seventh review, the SBA remains broadly on track and significant progress has been made in achieving fiscal consolidation and safeguarding the financial sector. All obligations to the Fund under previous arrangements have been met in a timely manner.

Table 2. Romania: IMF Financial Arrangements, 1991–2015
(In millions of SDRs)

Year	Type of Arrangement	Date of Arrangement	Date of Expiration or Cancellation	Amount of New Arrangement	Arrangement as a Percent of Quota	Amount Drawn	Purchases	Repurchases	Fund Exposure 1/
1991	SBA	11-Apr-91	10-Apr-92	380.5	72.7	318.1	565.8		565.8
1992	SBA	29-May-92	28-Mar-93	314.0	41.6	261.7	338.5	153.4	750.9
1993									750.9
1994	SBA	11-May-94	22-Apr-97	320.5	42.5	94.3	245.1	89.6	906.4
1995							37.7	245.8	698.3
1996								245.4	453.0
1997	SBA	22-Apr-97	21-May-98	301.5	40.0	120.6	120.6	98.4	475.2
1998								92.3	382.8
1999	SBA	05-Aug-99	28-Feb-01	400.0	38.8	139.8	53.0	102.0	333.8
2000							86.8	72.9	347.7
2001	SBA	31-Oct-01	15-Oct-03	300.0	29.1	300.0	52.0	91.7	308.0
2002							82.7	75.7	314.9
2003							165.3	79.6	400.6
2004	SBA	07-Jul-04	06-Jul-06	250.0	24.3	0.0		115.3	285.4
2005								102.8	182.6
2006								113.7	68.9
2007								68.9	
2008									
2009	SBA	04-May-09	03-May-11	11,443.0	1,110.8		6088.0		6088.0
2010							3712.0		9800.0
2011 2/	*SBA*	*25-Mar-11*	*15-Mar-2013*	*3,090.6*	*300.0*		*2993.0*		*12793.0*
2012 2/							*1720.0*	*-1307.3*	*13205.8*
2013 2/							*20.6*	*-4051.8*	*9174.6*
2014 2/								*-4392.6*	*4782.0*
2015 2/								*-2667.3*	*2114.7*

Source: Finance Department.

1/ As of end-December.
2/ Figures under the proposed Stand-By arrangement in italics. Assumes repurchases on an obligations basis.

3. **Romania's public sector external debt remains moderate and is owed mainly to multilateral institutions (Table 3, Figure 1).** Total external debt has been growing rapidly over the last five years and stood at 75 percent of GDP at end 2010. About three quarters of total external debt was owed by the private sector—mainly to non-monetary institutions. Public sector external debt remains at moderate levels—despite having more than doubled to 23 percent of GDP at end 2010. The majority of the external debt is long-term debt.

Romania's total and public external debt are in the medium range compared to recent exceptional access cases (Figure 2).[2]

4. **Romania's external debt service burden is high, but only a small fraction is borne by the public sector.** A debt service ratio of about 70 percent of exports of goods and services places Romania towards the higher end relative to most recent exceptional access cases (Figure 2, Panel C). The debt service ratio is also significantly higher than the corresponding one for the 2009 SBA. Less than 10 percent of external debt service is borne by the public sector.

Table 3. Romania: Total External Debt, 2005–2010 1/

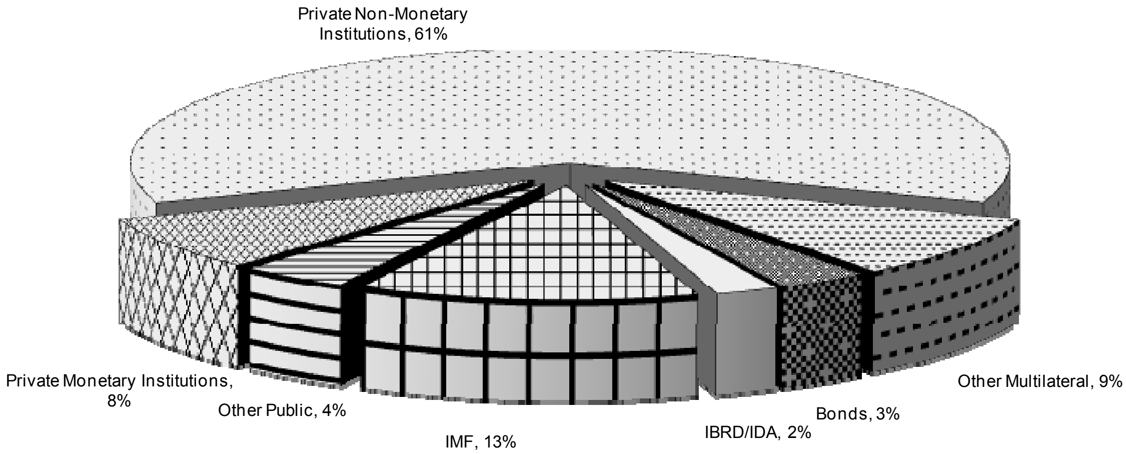
	2005	2006	2007	2008	2009	2010
	(In Millions of U.S. Dollars)					
Total External Debt	38,511	51,727	80,234	105,654	111,846	120,436
of which:						
Public	14,054	13,442	14,372	16,359	27,778	37,295
Loans	6,198	6,048	6,389	7,938	19,690	28,730
Multilateral	6,068	5,932	6,280	7,834	19,612	28,650
Bilateral	130	115	109	104	78	81
Bonds	3,307	3,226	3,343	3,885	3,863	3,847
Other 2/	4,549	4,168	4,640	4,536	4,225	4,718
Private	23,341	37,022	64,823	88,954	83,822	82,977
Short-term	7,789	15,764	26,785	29,708	19,275	22,867
Long-term	15,552	21,258	38,038	59,247	64,547	60,110
	(In Percent of GDP)					
Total External Debt	38.8	42.1	47.0	51.4	68.3	74.9
of which:						
Public	14.2	10.9	8.4	8.0	17.0	23.2
Loans	6.2	4.9	3.7	3.9	12.0	17.9
Multilateral	6.1	4.8	3.7	3.8	12.0	17.8
Bilateral	0.1	0.1	0.1	0.1	0.0	0.1
Bonds	3.3	2.6	2.0	1.9	2.4	2.4
Other	4.6	3.4	2.7	2.2	2.6	2.9
Private	23.5	30.1	38.0	43.3	51.2	51.6
Short-term	7.8	12.8	15.7	14.5	11.8	14.2
Long-term	15.7	17.3	22.3	28.8	39.4	37.4

Source: Romanian authorities and IMF staff estimates.

1/ End of year unless otherwise indicated.
2/ It includes debt with private banks, debt included after Public Debt Law Amendment, and other public debt.

[2] The exceptional access cases used as comparators in this paper are the SBAs approved since September 2008.

Figure 1. Romania: Composition of Total External Debt, 2010
(In percent)



Source: Romanian authorities and IMF staff estimates.

II. The New Stand-By Arrangement—Risks and Impact on Fund's Finances

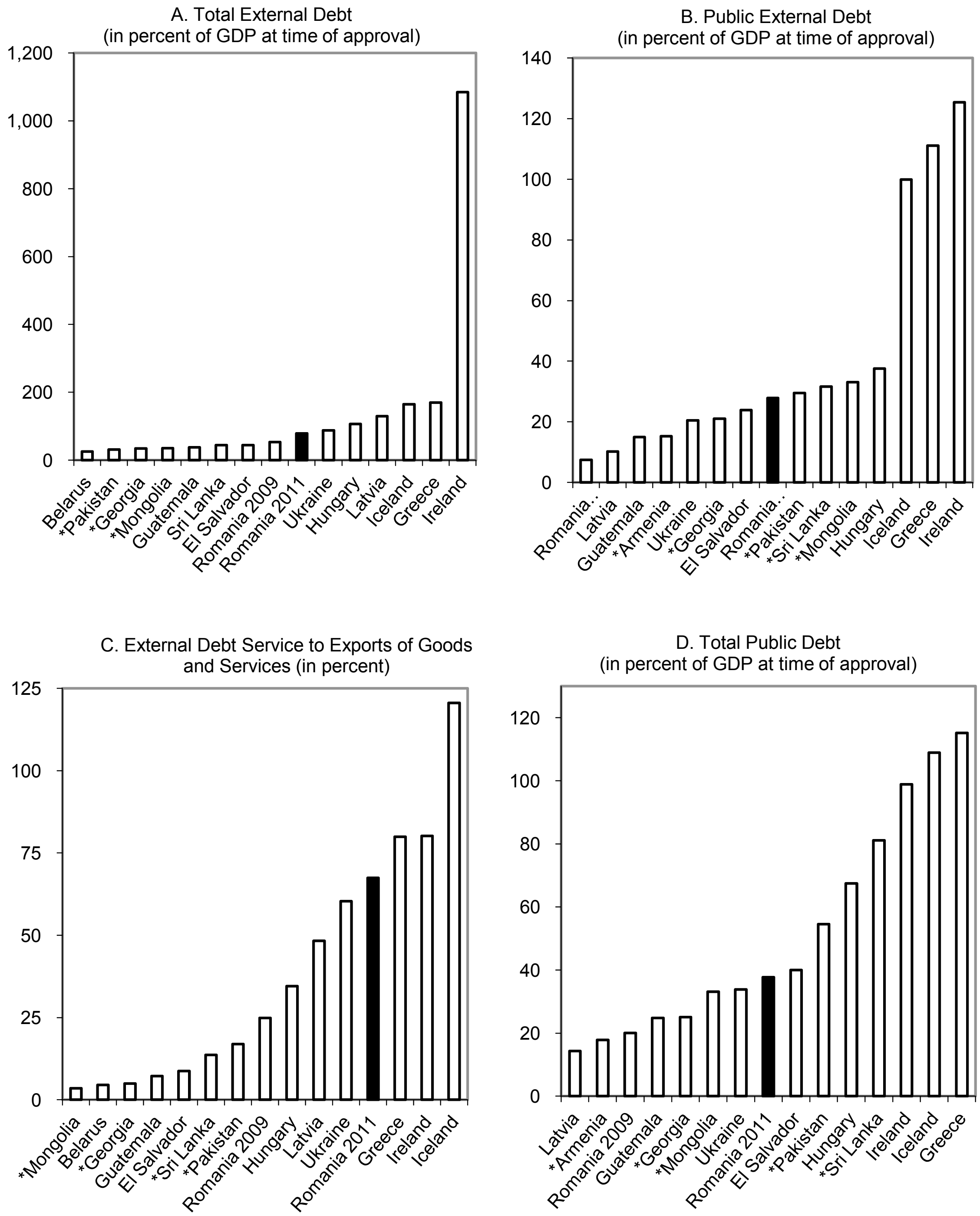
A. Risks to the Fund

5. **Access under the proposed arrangement is 300 percent of quota; cumulative access for Romania would exceed the cumulative access limit and would be high on a number of indicators.**[3]

- Access of SDR 3,090.6 million under the proposed arrangement would be moderate compared to recent exceptional access cases. Romania's combined access under the 2009 and the proposed SBA is the third highest among recent exceptional access cases (Figure 5, Panel A).

[3] For risk assessment purposes it is assumed that Romania makes a final purchase under the current arrangement equivalent to SDR 874 million (85 percent of quota) after completing the seventh review and before the arrangement is cancelled. The Romanian authorities have indicated that they are considering treating this last purchase under the current arrangement as precautionary.

Figure 2. Debt Ratios for Recent Exceptional Access Arrangements 1/



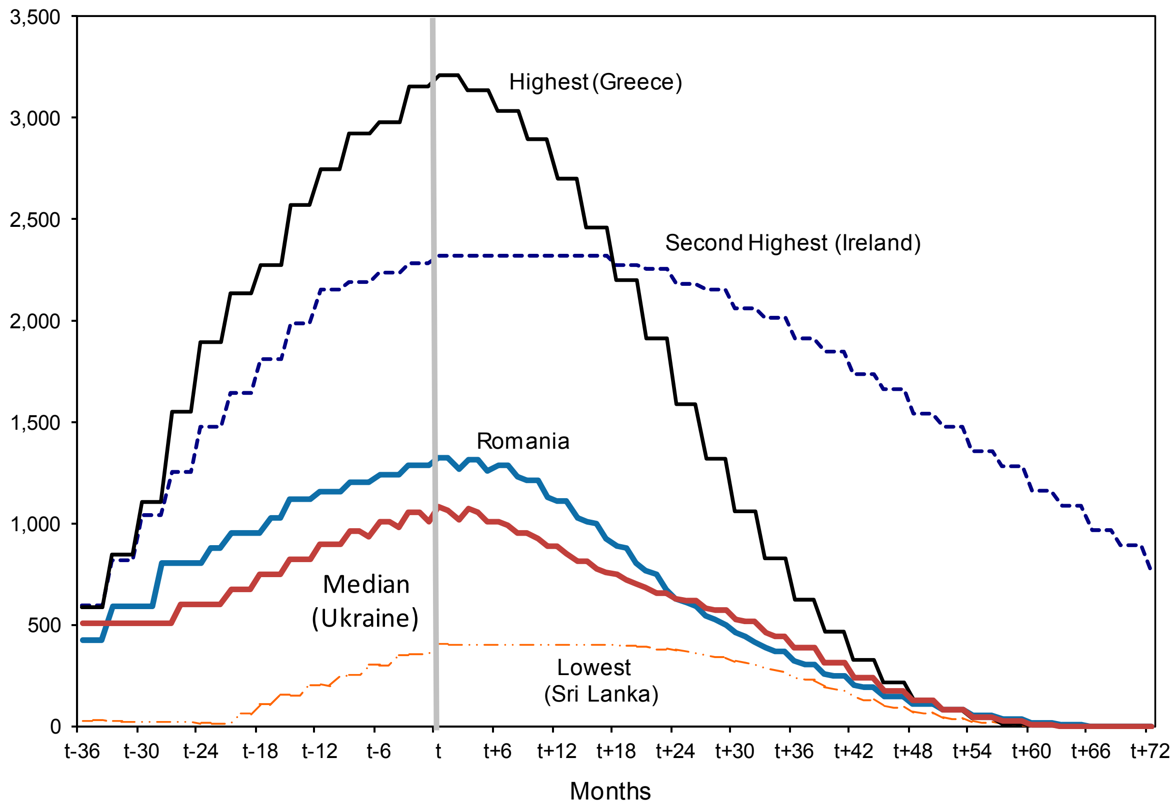
Source: Romanian Authorities, IMF staff estimates, and World Economic Outlook.

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

- If all purchases were made as scheduled, including the last purchase under the existing arrangement, Romania's outstanding use of GRA resources would rise to 1,116 percent of quota after the first purchase and peak at about 1,320 percent of quota in mid-2012. In terms of quota, this projected peak exposure would be the third highest after Ireland and noticeably higher than the median case (Figure 3).

- If all purchases were made as scheduled, the Fund's peak exposure to Romania in terms of GDP and total external debt would be in the medium to high range compared to recent exceptional access cases (Figure 4). Exposure in terms of gross international reserves would be more modest. The Fund's exposure under the proposed SBA would be very similar to the exposure under the 2009 SBA.

Figure 3. Fund Credit Outstanding in the GRA around Peak Borrowing 1/
(In percent of quota)
Approved Exceptional Access Cases since September 2008 2/



Source: IFS, Finance Department, and IMF staff estimates.
1/ Peak borrowing 't' is defined as the highest level of credit outstanding for a member. Repurchases are assumed to be on an obligations basis.
2/ Median credit outstanding at peak is 1,099 percent of quota; average is 1,190 percent of quota.

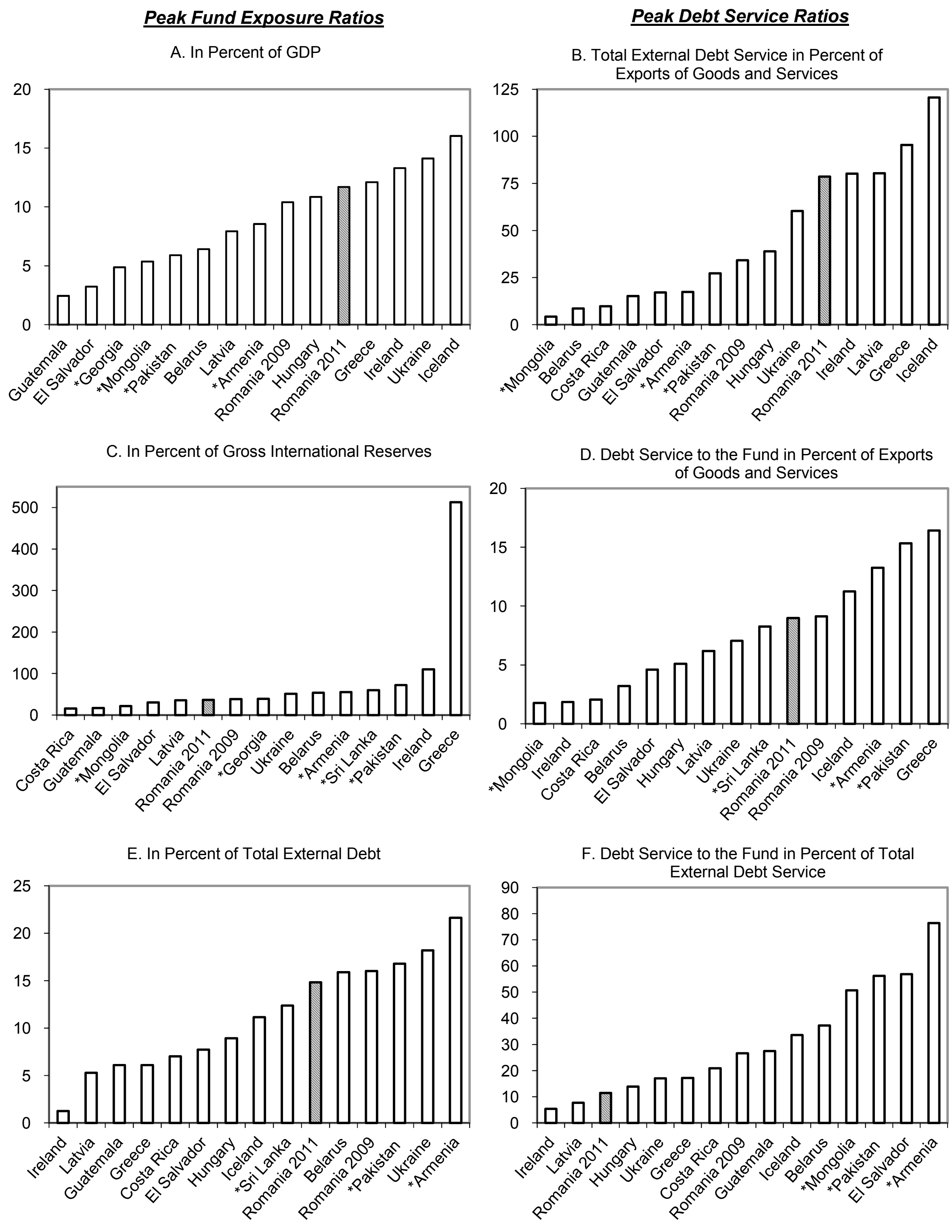
Table 4. Romania—Capacity to Repay Indicators 1/

	2011	2012	2013	2014	2015	2016	2017	2018
Exposure and Repayments (In SDR millions)								
GRA credit to Romania 2/	12,793.0	13,205.8	9,174.6	4,782.0	2,114.7	550.4	2.6	0.0
(In percent of quota)	(1,241.8)	(1,281.9)	(890.6)	(464.2)	(205.3)	(53.4)	(0.3)	(0.0)
Charges due on GRA credit 3/	261.6	418.3	435.1	240.3	80.3	23.6	6.6	1.6
Debt service due on GRA credit 4/	261.6	1,725.6	4,486.8	4,633.0	2,747.6	1,588.0	554.4	4.1
Debt and Debt Service Ratios 5/								
In percent of GDP								
Total external debt	78.9	75.4	70.4	65.5	61.1	58.4	55.8	53.3
External debt, public	27.8	25.4	21.5	17.8	14.2	12.3	11.8	11.3
GRA credit to Romania	11.7	11.0	6.9	3.2	1.3	0.3	0.0	0.0
Total external debt service	25.5	26.5	29.5	27.5	24.1	22.3	20.7	19.1
Public external debt service	1.4	2.6	5.5	5.0	2.9	2.3	2.1	2.0
Debt service due on GRA credit	0.2	1.4	3.4	3.1	1.7	0.9	0.3	0.0
In percent of Gross International Reserves								
Total external debt	248.9	242.7	245.0	248.0	258.1	257.4	256.7	256.0
External debt, public	87.9	81.6	74.8	67.2	60.2	54.4	54.2	54.1
GRA credit to Romania	36.9	35.3	24.0	12.3	5.5	1.3	0.0	0.0
In percent of Exports of Goods and Services								
Total external debt service	67.4	70.2	78.5	73.5	64.7	60.2	55.9	52.0
Public external debt service	3.8	6.9	14.7	13.3	7.8	6.1	5.7	5.3
Debt service due on GRA credit	0.6	3.8	9.0	8.4	4.5	2.4	0.8	0.0
In percent of Total External Debt								
GRA credit to Romania	14.8	14.6	9.8	5.0	2.1	0.5	0.0	0.0
In percent of Total External Debt Service								
Debt service due on GRA credit	0.9	5.4	11.4	11.5	7.0	4.0	1.3	0.0
In percent of Total Public External Debt								
GRA credit to Romania	42.0	43.3	32.1	18.3	9.1	2.5	0.0	0.0
In percent of Total Public External Debt Service								
Debt service due on GRA credit	16.6	55.2	61.0	63.2	58.5	38.7	13.2	0.1

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

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

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

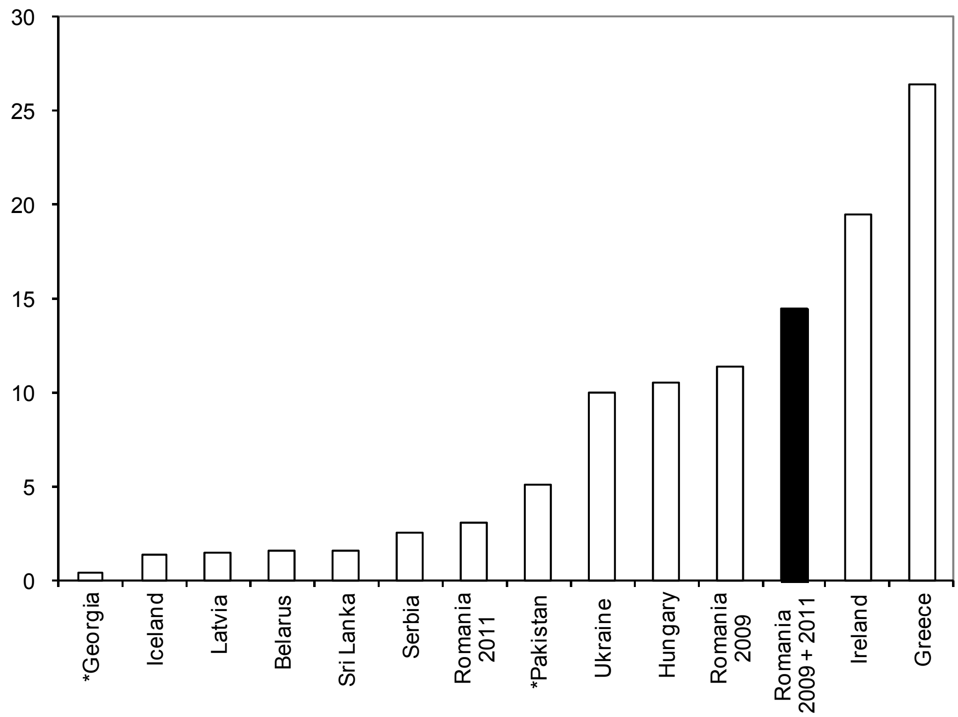


Source: Romanian authorities, IMF staff estimates, and World Economic Outlook.

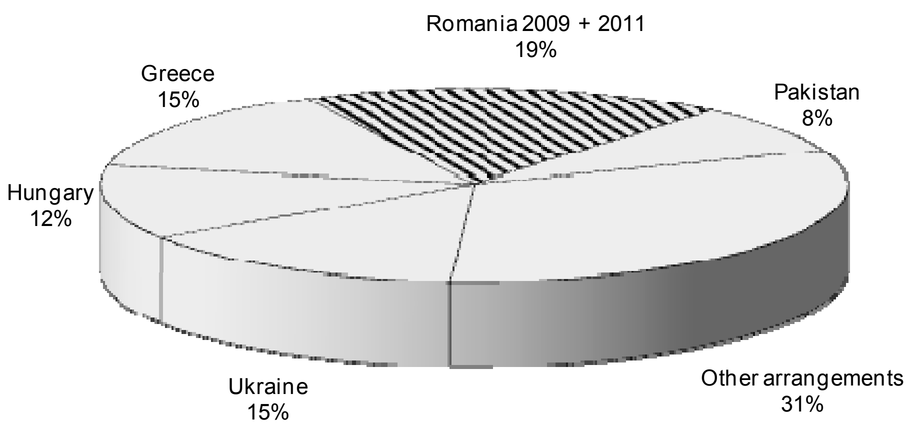
1/ Asterisks indicate PRGT eligible countries.

Figure 5. Exceptional Access Levels and Credit Concentration

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



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



Source: Finance Department.

1/ Does not include FCL arrangements. Asterisks indicate PRGT eligible countries.
2/ Credit outstanding as of February 22, 2011 plus last purchase under the existing arrangement and first purchase under the proposed arrangement with Romania.

- If all purchases were made as scheduled, GRA credit outstanding to Romania would be equivalent to 11 percent of GDP by end-2012 and over 35 percent of gross international reserves (Table 4). Outstanding use of GRA resources would represent about 15 percent of total external debt, and about 43 percent of public external debt.

6. **If all purchases were made as scheduled, Romania's peak debt service burden to the Fund would be relatively high.** Romania's projected debt service to the Fund would peak at about SDR 4,650 million in 2014. Peak debt service to the Fund as a share of exports of goods and services, at 9 percent, would be above the median share for most recent exceptional access cases, but comparable to the burden under the 2009 SBA (see Figure 4).[4] Peak total external debt service in percent of exports of goods and services of close to 80 percent in 2013 would place Romania toward the higher end relative to most recent exceptional access cases.

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

7. **The impact of the proposed arrangement on the Fund's liquidity would be modest, but more significant on the Fund's credit risk exposure.**

- **The proposed arrangement would reduce Fund liquidity by about 3 percent (Table 5)**. Commitments under the proposed arrangement would reduce the one-year forward commitment capacity (FCC), which currently stands at SDR 105 billion,[5] by about SDR 3.1 billion.[6] [7]

- **Potential GRA exposure to Romania would exceed the Fund's current level of precautionary balances (Table 5)**. The GRA commitment to Romania under the proposed arrangement represents 42 percent of the Fund's current level of precautionary balances. However, given the already high level of credit outstanding

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

[5] This figure refers to the FCC before the effectiveness of the expanded NAB and assumes that bilateral credit lines remain open. It does not take into account the possible activation of the expanded NAB.

[6] The FCC is the principal measure of Fund liquidity. The (one-year) FCC indicates the amount of GRA resources available for new financing over the next 12 months.

[7] The FCC is defined as the Fund's stock of usable resources less undrawn balances under existing arrangements, plus projected repurchases during the coming 12 months, less repayments of borrowing due one year forward, less a prudential balance.

to Romania, Fund exposure to Romania (assuming all purchases are made as scheduled) will exceed the current level of precautionary balances through 2013 and will peak at 180 percent of the current level of precautionary balances in 2012.

Table 5. Romania —Impact on GRA Finances
(millions of SDR unless otherwise noted)

	As of 3/7/2011
Liquidity measures	
Current one-year Forward Commitment Capacity (FCC) 1/	104,550.8
Impact on FCC on approval 2/	3,090.6
Prudential measures	
Fund GRA credit outstanding to Romania 4/	
In percent of current precautionary balances 3/	198.5
In percent of total GRA credit outstanding	22.2
Fund GRA credit outstanding to top five borrowers	
In percent of total GRA credit outstanding	68.0
In percent of total GRA credit outstanding including first Romanian purchase	68.1
Romania's annual GRA charges in percent of Fund's residual burden sharing capacity for 2011	510.5
Memorandum items	
Fund's precautionary balances (FY 2010) 3/	7,320.3
Fund's residual burden sharing capacity 5/	51.2

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

1/ The FCC is defined as the Fund's stock of usable resources less undrawn balances under existing arrangements, plus projected repurchases during the coming 12 months, less repayments of borrowing due one year forward, less a prudential balance.
2/ A single country's negative impact on the FCC is defined as the country's sum of Fund credit and undrawn commitments minus repurchases one-year forward.
3/ Precautionary balances exclude amounts in Special Reserves attributable to pofits on gold sales in FY2010.
4/ Credit outstanding assumes full drawing by Romania.
5/ Burden-sharing capacity is calculated based on the floor for remuneration at 85 percent of the SDR interest rate. Residual burden-sharing capacity is equal to the total burden-sharing capacity minus the portion being utilized to offset deferred charges and takes into account the loss in capacity due to nonpayment of burden sharing adjustments by members in arrears.

- **Were Romania to accrue arrears on charges under the proposed arrangement, the Fund's burden sharing capacity would be severely strained (Table 5).**[8] Charges on the GRA obligations would equal about SDR 260 million in 2011, about

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

five times the current estimated residual burden-sharing capacity of the Fund.[9] Charges would peak at about SDR 4.7 billion in 2014 if purchases were made as scheduled.

- **If the first purchase is made, Fund credit to Romania would represent 19 percent of total GRA credit outstanding**, making Romania the largest user of Fund resources (Figure 5). In terms of size, the proposed arrangement would be moderate, but it would come on top of already high exposure. The share of the top five users of Fund resources of total outstanding credit would increase only marginally since Romania is already part of this group of borrowers (see Table 5).[10]

III. Assessment

8. **The proposed arrangement aims to support further fiscal consolidation while undertaking deeper economic reforms.** Building on the achievements of the current arrangement, the proposed arrangement can be seen as an effective mechanism to insure against possible future shocks while aiding the authorities in maintaining policy discipline. It aims to boost growth potential through structural reforms, and to foster confidence and facilitate private capital flows by improving policy stability and business climate.

9. **There are significant financial risks associated with the proposed arrangement for Romania.** Romania will be the Fund's largest creditor and debt service to the Fund will be substantial. Potential risks to the program that could affect Romania's capacity to repay the Fund include:

- Domestic political tensions could lead to policy reversals, which could put the attainment of program objectives at risk.
- Weaker than expected recovery in Western Europe which would dampen exports.
- Spillovers from the turbulence in the periphery of the euro area would raise risk premia and affect capital flows to Romania. In such circumstances, there would also be a risk that foreign banks will be unable to maintain their exposure to Romania despite their commitment to do so, along with a risk of capital flight.

10. **These risks are mitigated by the authorities' strong commitment to the program and Romania's sound track record under the 2009 SBA.** The authorities are committed to the program which will in turn assist in maintaining policy discipline. Performance under the

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

[10] It is assumed that the last purchase under the existing arrangement is made.

2009 SBA was strong and the proposed arrangement will help to safeguard the gains made. In addition, Romania's excellent track record of servicing external obligations provides comfort that financial obligations to the Fund will be met in a timely manner.

INTERNATIONAL MONETARY FUND

ROMANIA

Seventh Review Under the Stand-By Arrangement, Cancellation of the Current Stand-By Arrangement, and Request for a New Stand-By Arrangement— Supplementary Information

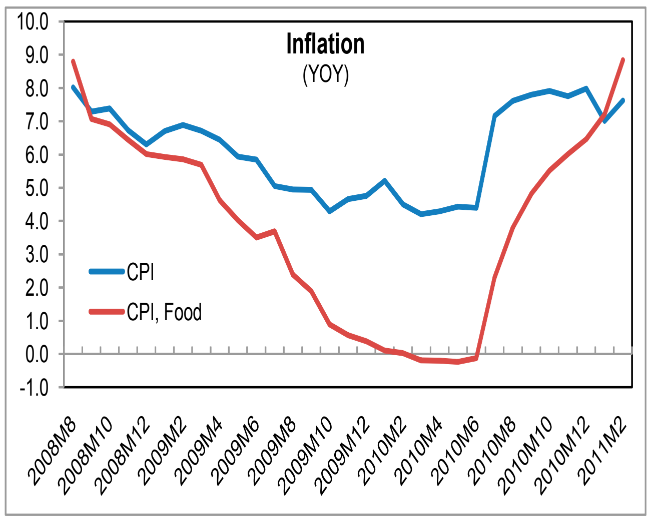
Prepared by the European Department
(In Consultation with Other Departments)

Approved by Poul M. Thomsen and Jan Kees Martijn

March 18, 2011

1. **This supplement provides an update on economic and policy developments since the issuance of the staff report on March 11, 2011 (EBS/11/37)**. The additional information does not change the thrust of the staff appraisal.

2. **Recent indicators confirm the nascent economic recovery, while showing increased inflation.** Trade data for January show continued strong export growth and industrial production remains robust. Economic sentiment indicators have improved, which may portend some recovery in domestic demand. February inflation was significantly higher than expected, mainly driven by higher food prices. Continued pressure on food and energy prices in the coming months will hinder prospects for future monetary easing and may compromise the NBR's end-year inflation target.



3. **The government met the prior action on adopting the norms on indirect audits at the cabinet meeting on March 17.** As noted in the staff report, the structural benchmark to amend the legislation of the Deposit Guarantee Fund has been reset to July 31, to allow additional time for consultation with the EU.

4. **On March 16, parliament approved the authorities' proposed reform to the labor code in a vote of confidence**. Use of the confidence vote mechanism means that no amendments were possible, so the legislation was unchanged from the text submitted by the government. The opposition is appealing aspects of the reform in the Constitutional Court.

5. **In a meeting on March 16 with participants in the European Bank Coordination Initiative for Romania, banks reiterated their strong commitment to maintaining adequate capitalization and to continued lending activity in the country.** However, given the economic recovery and the end of current SBA, it was decided that there was no need to continue with specific exposure and capital commitments under the EBCI. While some banks may reduce exposures upon expiration on the formal commitment, in staff's view aggregate exposure is unlikely to fall significantly, as most banks were already voluntarily maintaining exposures above the previous minimum and some have announced their intention to increase lending activity.

Table 1 (Revising table 2 of the staff report). Romania: Performance for Seventh Review

Measure	Target Date	Comment
Quantitative performance criteria		
1. Floor on general government overall balance	December 31, 2010	Met
2. Ceiling on general government guarantees	December 31, 2010	Met
3. Ceiling on general government domestic arrears	December 31, 2010	Missed
4. Non-accumulation of external debt arrears	December 31, 2010	Met
5. Floor on net foreign assets	January 31, 2011	Met
Quantitative Indicative Target		
1. Ceiling on general government current primary spending	December 31, 2010	Missed
2. Floor on the operating balance of ten largest loss-making SOEs	December 31, 2010	Missed
3. Floor on net foreign assets	March 31, 2011	Likely to be met
Inflation consultation band		
Inner band	December 31, 2010	Met
Outer band	December 31, 2010	Met
Structural benchmarks		
1. Parliamentary ratification of amendments to the bank resolution framework	December 1, 2010	Partially met
2. Reform tax administration methodology for high net wealth individuals	December 31, 2010	Met
3. First phase to integrate the accounting reporting system with the Treasury payment system	March 15, 2011	Met
4. Amend legislation to allow the use of the deposit guarantee fund resources to facilitate bank restructuring, including purchase and assumption transactions	March 15, 2011	Missed, reset for July 31, 2011

Table 2 (Revising table 4 of the staff report). Romania: Conditionality for New Program

Measure	Target Date	Comment
Prior action		
The government decision on indirect audit methods will be passed (¶12).		Met
Quantitative performance criteria		
1. Floor on general government overall balance	Quarterly	
2. Ceiling on general government guarantees	Quarterly	
3. Ceiling on central government and social security domestic arrears	Quarterly	
4. Non-accumulation of external debt arrears	Continuous	
5. Floor on net foreign assets	Quarterly	
Quantitative Indicative Target		
1. Ceiling on general government current primary spending	Quarterly	
2 Ceiling on local government domestic arrears	Quarterly	
3. Floor on the operating balance and arrears of key loss-making SOEs	Quarterly	
Inflation consultation band		
Inner band	Quarterly	
Outer band	Quarterly	
Structural benchmarks		
1. Completion of a stocktaking of arrears and unpaid bills as of end-December 2010 for the entire general government and SOEs (¶10).	April 30, 2011	
2. Preparation of strategic action plans for key SOEs (as specified in TMU) (¶23).	April 30, 2011	
3. Introduction of a simplified taxation system for smaller taxpayers under the threshold with help from the IMF and EC, while requesting a shift in the VAT mandatory threshold from the EU Council of Ministers to €50,000 (¶12).	June 30, 2011	
4. Eliminate by government ordinance the legal basis of *stimulente* funds, effective January 1, 2012 (¶8).	June 30, 2011	
5. Amend legislation to allow the use of the deposit guarantee fund resources to facilitate bank restructuring, including purchase and assumption transactions (¶4).	July 31, 2011	
6. Completion of a comprehensive review of the existing investment portfolio, which will prioritize and evaluate existing projects to focus on those where funding can be fully secured, examine the viability of old projects, with low priority and unviable ones discontinued, and production of a final report and an action plan (¶13).	September 30, 2011	

Press Release No. 11/101
FOR IMMEDIATE RELEASE
March 25, 2011

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Approves New €3.5 Billion Precautionary Stand-By Arrangement for Romania, Completes Seventh and Final Review Under the Current Stand-By Arrangement and Approves €1 Billion Disbursement

The Executive Board of the International Monetary Fund (IMF) today approved a new 24-month precautionary Stand-By Arrangement (SBA) in the amount equivalent to SDR 3,090.6 million (about €3.5 billion, 300 percent of quota), with the SBA coming into effect on March 31, 2011. The authorities have informed the IMF that they intend to treat the new arrangement as precautionary and therefore do not plan to draw under it. The SBA will be in conjunction with precautionary support from the European Union of €1.4 billion and a loan from the World Bank of €0.4 billion.

The Executive Board has also completed the seventh and final review of Romania's economic performance under an SDR 11.443 billion (about €12.95 billion or US$17.07 billion) 24-month SBA that was approved on May 4, 2009 (Press Release No 09/148) and will end effective March 30, 2011 at the authorities' request. The completion of the final review enables the immediate disbursement of SDR 874 million (about €1 billion or US$ 1.4 billion). The authorities have informed the IMF that they also intend to treat this final disbursement as precautionary.

Following the Executive Board's discussion on Romania, Mr. John Lipsky, First Deputy Managing Director and Acting Chair, stated:

"Policy implementation under the Fund-supported program has remained strong and the authorities are seeking a follow-up precautionary arrangement to signal their commitment to continued reform. The fiscal and structural measures already implemented are yielding results. The economy has stabilized and growth is resuming. The new program appropriately focuses on building on achievements to date with additional fiscal consolidation and structural reforms to boost growth and improve private sector participation in the economy.

"The authorities' planned fiscal adjustment should help reduce the budgetary deficit to within 3 percent of GDP in 2012. Going forward, efforts should focus on reforming social health care and public investment, tackling persistent domestic arrears, and improving the tax system. Priority should also be given to institutional changes that would facilitate the absorption of EU funds.

"Improved governance, regulation, and pricing at state-owned enterprises, particularly in the energy and transport sectors, are essential to bolster economic efficiency as would a reactivation of the privatization program. The authorities are also pursuing labor market and social benefits reforms, with a view to fostering job creation and productivity growth. These reforms should be mindful of the need to protect the most vulnerable groups and workers' rights.

"Monetary and financial sector policies have been prudent and proactive, helping preserve financial stability during the crisis. Monetary policy should continue to strike a balance between the need to address inflation risks and the need to support the recovery. The banking system is liquid and well-capitalized, but vigilance remains warranted, in light of rising non-performing loans and the potential for adverse regional spillovers".

ANNEX

Recent Economic Developments

The Romanian economy is beginning to recover. Recent data show slight positive growth in the last quarter of 2010, while revisions to previous quarters have produced a better outturn for the year than previously expected (-1.3 percent). Strong export growth continues and industrial production remains robust, however, weak retail sales persist. Registered unemployment has decreased, but mainly due to shrinking labor force participation rather than job creation.

Headline CPI inflation peaked at 8.0 percent in December 2010, and has since eased to 7.6 percent in February 2011. The CDS spread for sovereign debt has narrowed by around 125 basis points since September, and is now below several other EU countries. Romanian equity markets have recovered since their June trough. Thus far, the turbulence in the Euro area periphery has had little direct impact on Romania, though risks remain. Since January 2011, the leu has appreciated against the euro, obviating the need for significant central bank intervention in support of the currency.

The current account deficit improved from 13½ percent of GDP in 2007 to around 4¼ percent of GDP in 2010, driven by a strong shrinking trade deficit. Exports are booming, driven by the manufacturing sector. On the transfers side, workers' remittances have shrunk due to the recession and high unemployment in host economies.

Program Summary

The successor SBA will focus on boosting potential growth through structural reforms. Structural deficiencies in key economic areas weigh heavily on economic growth. Improved efficiency of the public sector will reduce bureaucratic barriers to economic efficiency and will increase the absorption of EU structural funds to boost capital spending to improve the country's infrastructure. The new program also aims at deep-rooted reforms in the energy and transport sectors, including pricing reforms, improved regulation, and the restructuring and privatization of energy and transport state owned enterprises. Fund and EU precautionary support will reassure private markets and provide a cushion against future shocks, should they materialize.

Fiscal adjustment will continue. The difficult fiscal measures enacted in 2010, complemented with continued prudent expenditure policies, put the fiscal cash deficit targets of 4.4 percent in 2011 and 3.0 percent in 2012 well within reach. However, continued efforts to improve tax collections, tackle expenditure pressures (particularly in the health sector), and reduce arrears will be crucial to sustained deficit reduction.

The banking sector has weathered the crisis well, remaining well-capitalized and liquid. Non-performing loans continue to increase, but at a declining pace and are expected to peak in mid-

2011. Banks remain well-capitalized, with an average capital adequacy ratio of 14.7 percent and all banks above 11 percent at end-2010.

Romania joined the IMF on December 15, 1972, and its quota is SDR 1.03 billion (about €1.2 billion or US$1.6 billion).

Table 1. Romania: Selected Economic and Social Indicators, 2007–12

	2007	2008	2009	2010		2011	2012
				Prog.	Est.	Proj.	Proj.
Output and prices							
Real GDP	6.3	7.3	-7.1	-1.9	-1.3	1.5	4.4
Domestic demand	14.2	7.3	-12.9	-3.9	-1.0	1.2	4.3
Net exports (contribution)	-9.6	-1.0	7.5	2.2	-0.2	0.2	-0.1
Consumer price index (CPI, average)	4.8	7.9	5.6	6.1	6.1	5.4	3.4
Consumer price index (CPI, end of period)	6.6	6.3	4.7	8.2	8.0	3.7	3.0
Unemployment rate (average)	4.3	4.0	6.3	7.8	7.6	6.6	5.8
Nominal wages	22.6	23.6	8.4	2.0	2.6	4.7	6.7
Saving and Investment							
Gross domestic investment	31.0	31.3	25.3	27.8	26.5	24.6	25.2
Gross national savings	17.6	19.7	21.1	22.3	22.2	19.5	20.1
General government finances							
Revenue	32.3	32.2	31.4	32.7	32.8	33.3	33.7
Expenditure	35.4	37.0	38.7	39.5	39.4	37.7	36.7
Fiscal balance	-3.1	-4.8	-7.3	-6.8	-6.5	-4.4	-3.0
Privatization proceeds	0.1	0.1	0.0	0.0	0.0	0.0	0.0
External financing	0.1	0.4	2.9	4.6	4.6	2.8	0.7
Domestic financing	2.9	4.3	4.5	2.2	1.9	1.6	2.3
Structural fiscal balance 1/	-5.8	-8.5	-7.0	-4.4	-4.9	-2.4	-1.6
Gross public debt (direct debt only)	17.5	19.5	27.4	33.9	33.2	36.1	36.2
Money and credit							
Broad money (M3)	33.7	17.5	9.0	4.3	6.9	10.3	14.1
Credit to private sector	60.4	33.7	0.9	4.1	4.7	7.7	8.7
Interest rates, eop							
Euribor, six-months	4.79	3.52	4.52	-	1.23	-	-
NBR policy rate	7.50	10.25	8.00	-	6.25	-	-
NBR lending rate (Lombard)	12.00	14.25	12.00	-	10.25	-	-
Interbank offer rate (1 week)	7.14	12.72	10.69	-	3.63	-	-
Balance of payments							
Current account balance	-13.4	-11.6	-4.2	-5.5	-4.2	-5.0	-5.1
Merchandise trade balance	-14.3	-13.7	-5.8	-5.4	-4.8	-5.1	-4.7
Capital and financial account balance	17.6	12.7	-2.5	2.1	1.1	5.3	8.4
Foreign direct investment balance	5.7	6.7	3.0	2.4	2.0	2.9	2.9
International investment position	-43.5	-49.4	-62.7	-61.3	-70.8	-75.3	-72.6
Gross official reserves	23.0	20.2	26.3	27.8	29.5	31.7	30.9
Gross external debt	47.0	51.4	68.3	73.9	74.5	78.9	75.4
Exchange rates							
Lei per euro (end of period)	3.5	4.0	4.2	-	4.3	-	-
Lei per euro (average)	3.3	3.7	4.2	-	4.2	-	-
Real effective exchange rate							
CPI based (percentage change)	8.4	-5.0	-7.5	-	1.8	-	-
GDP deflator based (percentage change)	17.3	1.5	-8.8	-	0.2	-	-
Memorandum Items:							
Nominal GDP (in bn RON)	416.0	514.7	498.0	511.6	513.6	542.0	590.2
Nominal GDP (in bn euros)	124.6	139.7	117.6		122.1	127.2	140.7

Social and Other Indicators

GDP per capita (current US$, 2009): $7,500; **GDP per capita, PPP** (current international $, 2009): $14,198

Unemployment rate: 6.8% (December 2010)

Poverty rate: 5.7% (2008)

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

1/ Actual fiscal balance adjusted for the automatic effects of the business cycle.

Statement by Age Bakker, Executive Director for Romania and
Mihai Nicolae Tanasescu, Senior Advisor to the Executive Director
March 25, 2011

The anti-crisis program supported by the Fund, the European Union, and the World Bank has continued to play an important role in stabilizing the Romanian economy, reversing imbalances, rebuilding confidence of international markets, and setting the stage for future sustainable economic growth. The authorities have requested a new program which will build further on the substantial progress made in macroeconomic policies and financial stability and focus on accelerating structural reforms with a view to eliminate barriers to growth while boosting investment and job creation.

Romania is on track with the implementation of quantitative targets. All end-December performance criteria for the seventh review have been met, with the exception of the criterion on general government arrears, for which a waiver was already granted January 7, 2011. While progress has been made in eliminating central government arrears, arrears from local governments continue to pose a challenge. My authorities are committed to taking further measures to reduce arrears, and with the implementation of the new local public finance law, arrears will start a downward trend during 2011.

Recent economic developments

After a severe downturn in 2009 and 2010, there are signs that economic activity is picking up. Data for the last quarter of 2010 and recent indicators suggest that growth has restarted and will gain momentum in 2011. Industrial production continued to grow and rose by 1 percent in January, driven mainly by manufacturing, and by 11.8 percent since January 2010. For 2011 GDP growth is expected to reach around 1.5 percent and to further accelerate in 2012 reaching 4-4.5 percent. Although an export-led recovery appears to be underway and is warranted as an exit out of the recession, it should be gradually complemented by a recovery in domestic demand. Domestic demand will gradually become the main engine of sustainable economic growth, supported by better absorption of EU funds.

The inflation rate is expected to peak in the coming months, due to the first-round effects of last year's increase in the VAT rate, and pressures from food and fuel prices. February inflation was 0.77 percent and accelerated to 7.6 percent yoy, but will gradually return to the Central Bank's target band in the second half of 2011.

The external position improved significantly, and the current account deficit narrowed by 86 percent yoy in January 2011, driven by strong export evolution. For the first time in the last ten years, the FOB-FOB trade balance reached a small surplus in January 2011. Exports reached EUR 3.4 billion, registering a remarkable increase of 47.8 percent yoy, mainly driven by exports to the EU, which increased by 40 percent. Looking at the components, machinery and transport equipment had the highest weight in exports.

Financial market stress has eased further in the last months, and the CDS spread for sovereign debt narrowed, leaving it well below several other EU member countries, including countries from the euro-area periphery.

Despite the progress achieved, the recovery remains vulnerable to risks of adverse developments in international financial markets, and a weaker-than-expected recovery in Western Europe or spillovers from the ongoing turbulence in the euro-area periphery could dampen exports and affect capital flows to Romania. The objectives and policies under the new Stand-By-Arrangement, which would be treated as precautionary, will boost potential growth with a focus on structural reforms, while consolidating fiscal and financial stability. The key objectives of this new program will further fiscal consolidation, attacking problems of revenue and expenditures efficiency and arrears, and will accelerate structural reforms, including in state owned enterprises, which will allow for continued competitiveness as Romania prepares to eventually join the Euro area.

Fiscal policy

The fiscal package implemented since the beginning of the program has produced the targeted adjustment. As a result, the end-December deficit target has been met, and the 2011 budget will help to reach the agreed cash fiscal deficit target of 4.4 percent of GDP at the end of the year. For 2012, renewed economic growth combined with prudent fiscal policy should bring the fiscal deficit to below 3 percent of GDP in ESA terms. This will require compliance with the fiscal responsibility law and continued expenditure restraint, including on the wage bill.

On the revenue side, tax policies will remain largely unchanged, including the VAT rate, which will be kept at 24 percent. Under the new program, improving tax administration and fighting against tax evasion will be important areas for increasing tax collection. Legislation relating to high net wealth individuals was approved by end-December 2010, and a government decision on indirect audit methods has been passed last week. The authorities will institute simplified taxation for smaller taxpayers requesting a shift in the VAT mandatory threshold from the EU Council of Ministers to EUR 50,000.

On the expenditure side, the government will keep the wage bill within the agreed limit and take additional measures to secure the 2011 deficit target, including further health care reforms, and continuing public employment reductions. On the health care reforms, the authorities will take measures to safeguard fiscal consolidation by reforming the government-insured benefits package, reducing excess public sector hospital beds with a view to reaching the EU average by 2013, and introducing national health cards, electronic patient records, and electronic prescriptions. The government will broaden the base for health contributions, improve revenues and control expenditures.

The accelerated absorption of EU funds remains a focal objective of the government. Under the new program the authorities will focus on strengthening the administrative capacity of units managing the funds, will modernize and consolidate the legislative regulatory framework for public investment, and will prioritize investment in order to assure sufficient financing for key projects. To better coordinate EU fund absorption, the EU funds unit will be moved to the Prime Minister's office.

Monetary and financial sector policies

The monetary authorities responded well to the contraction in economic activity, and the Central Bank has taken crucial measures to bring down inflation levels. However, inflation in recent months was boosted by the first-round effects of the last July's VAT rate increase, and continued food and fuel prices pressures. The Central Bank has paused its monetary policy easing and believes that further vigilance is needed to keep inflation expectations contained and stave off possible second-round inflationary effects from risks relating to supply-side shocks. The Central Bank remains committed to bringing inflation down to within the official target band of 3 percent +/-1 percentage points in 2011 and 2012.

The Romanian financial system so far has weathered well the impact of the economic contraction. The rise in non-performing loans slowed significantly during the final quarter of 2010, and as the economic recovery gaining ground, the banking sector as a whole is expected to return to profitability. The banks remain well capitalized, at 14.7 percent, with all banks posting a solvency ratio above 11 percent at the end of 2010. All parent banks of the nine largest foreign banks have in aggregate complied with their commitment to maintaining exposures under the European coordination Initiative, as had been agreed for the past two years. Recently, in the European Bank Coordination Initiative meeting between the IMF, the EC, the Romanian authorities and the nine largest foreign banks active in Romania, banks reiterated their strong commitment to maintaining adequate capitalization and collectively expressed interest in appropriately maintaining or expanding their exposures to Romania. Most banks expressed voluntarily maintaining exposures above the previous minimum and some have announced their intention to increase lending activity.

Under the existing program, the authorities have undertaken significant reforms to strengthen the financial safety net, including approving amendments to the banking law that enable the special administrator to promptly implement a broad range of restructuring measures. The Central Bank - together with the Deposit Guarantee Fund (DGF) - will develop operating procedures and contingency plans for deploying the new resolution tools, and will ensure that DGF has ready access to liquidity to meet any potential shortfalls in funding and prepare joint procedures for deploying DGF funds in a bank resolution. Moreover, the authorities are working to introduce International Financial Reporting Standards for the banking sector in 2012 , with a view to devising, in consultation with the Romanian Banking Association, prudential filters that would enable a smooth transition between RAS and IFRS in the sense of consolidating existing effective capitalization levels in individual credit institutions.

Structural reforms

Under the current program, the authorities have made significant progress on the structural side. However, sustainable economic growth will require further structural reforms in key economic sectors. The new program will include needed reforms in the energy market and transport sectors, which in recent years have increasingly become a fiscal burden and constrain private sector growth. Implementing a comprehensive strategy addressing the viability of key firms in these sectors and reforming their governance will be vital. Moreover, action plans will classify them as in line for liquidation, privatization, or restructuring, and will contain concrete arrears-reducing strategies. Major financial and operational indicators of all state-owned enterprises will be regularly reported to the Minister of Public Finance.

In the energy sector, the authorities will take necessary steps to restore the energy regulator's operational and financial autonomy in accordance with EU legislation, and will design a roadmap for phasing out regulated prices in electricity and gas. Much needed capital and managerial know-how will be brought to the energy sector through minority and /or strategic private investors into key energy firms, including Petrom, Transelectrica, and Romgaz. The authorities are committed to bringing investment into the sector by moving ahead to prepare sales of minority or strategic stakes in individual firms slated to be included in the national champion companies. The coal companies will also continue to be downsized, with viable assets spun off.

In the transport sector, passenger railway and infrastructure service will be restructured, including by modifying its passenger service contracts, better cost recovery, competitive tendering for public services and infrastructure maintenance, and a decrease in losses and arrears.

In the labor market, the authorities made important legislative changes to increase the flexibility of the labor market, and recently the parliament approved the proposed reform to the labor code in a vote of confidence. A reform of social benefits has been submitted to parliament, and will improve efficiency of protecting the poorest and most vulnerable, and will consolidate the guaranteed minimum income, heating benefits and family allowances into one new scheme.

In conclusion, my authorities acknowledge that the new Stand-By Arrangement will maintain the reform momentum, will provide additional security against unforeseen shocks, and will build on the considerable progress achieved over the past two years, setting the stage for strong and sustainable economic development while maintaining external and internal stability.