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Country Report Romania 2020

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COMMUNICATION FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT, THE EUROPEAN COUNCIL, THE COUNCIL, THE EUROPEAN CENTRAL BANK AND THE EUROGROUP

2020 European Semester: Assessment of progress on structural reforms, prevention and correction of macroeconomic imbalances, and results of in-depth reviews under Regulation (EU) No 1176/2011

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EXECUTIVE SUMMARY

In the absence of lasting reform efforts, growing fiscal and current account deficits are putting the sustainability of Romania's economic growth at risk. Strong domestic demand, stimulated by tax cuts and large wage increases, has been the economy's growth engine in recent years. This consumption-led growth model has pushed the country's current account and public finances into rising deficits. In addition, adverse demographic developments have led to significant labour and skill shortages, limiting the country's growth potential. Despite an average growth of around 5% in the past three years, inequality is increasing and poverty remains high, while regional disparities are deepening. Without a correction of the fiscal and external deficits and a firm commitment to implement structural reforms, Romania's convergence towards EU living standards is likely to suffer important set-backs ([1]).

The economy continues to grow, albeit at a slower pace. Real GDP growth remained robust in 2019 at 4.1% on the back of private consumption, with investment providing support. Growth is forecast to ease to 3.6% and 3.3% in 2020 and 2021 respectively, due to weaker industrial production and a softening external demand.

The fiscal-led boom in domestic demand continues, further widening the current account deficit. With strong private-consumption led import growth outpacing exports, the current account deficit is set to deteriorate to 5.1% in 2019 and is expected to increase to 5.4% in 2021.

The labour market continued to tighten, while significant challenges remain. A very low labour force participation rate and a decline of the active population, due to demographic changes, including emigration, have resulted in labour force and skill shortages and mismatches. Labour activation policies and adult learning programmes are not effective in responding to such needs. At the same time, skill mismatches are deepening, while technological development generates a shift in the demand for skills. Social dialogue remains limited. Wages remain low compared to the EU average but have been growing rapidly, supporting employees' purchasing power. The sustained wage growth, strongly outpacing productivity increases, may pose risks to competitiveness in the future.

The public deficit has risen sizably, driven by current expenditure. The public deficit continued to increase, above the 3% of GDP Treaty threshold in 2019, driven by current spending. It is projected to widen further, in particular due to a 40% pension indexation scheduled for September 2020. As in previous years, the rules of the national fiscal framework have not been respected. A high public deficit and increasing ageing costs result in high fiscal sustainability risks.

The banking sector has remained solid, but financial intermediation is low. Some damaging provisions to the financial sector in December 2018 were amended in 2019 and 2020, favouring banks' resilience and a stable capitalisation, above the EU average. However, banks only play a limited role in providing credit to corporates, which may be holding back the economy.

Insufficient investment hampers the potential of the economy to converge to EU levels. The quality and reliability of the road and rail networks is poor. Investment in sustainable transport, energy and environmental infrastructure (i.e. in waste, wastewater and air pollution) is lacking. The energy, waste, wastewater infrastructure continue to need an important investment push. Prioritisation, stabilisation and increases of public and private investment in research, development and innovation and in physical and digital infrastructure would contribute to reduce regional disparities and improve productivity and long-term growth.

Romania has made limited ([2]) progress in addressing the 2019 country-specific recommendations. There has been substantial progress in:

- Safeguarding financial stability and the robustness of the banking sector.

([1]) This report assesses Romania's economy in light of the European Commission's Annual Sustainable Growth Strategy published on 17 December 2019. In this document, the Commission sets out a new strategy on how to address not only the short-term economic challenges but also the economy's longer-term challenges. This new economic agenda of competitive sustainability rests on four dimensions: environmental sustainability, productivity gains, fairness and macroeconomic stability.

([2]) Information on the level of progress and actions taken to address the policy advice in each respective subpart of a country-specific recommendation is presented in Annex A.

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There has been some progress in the following areas:

- Ensuring the long-term viability of the second pension pillar;
- Implementing the national public procurement strategy.

There has been limited progress in the following areas:

- Efforts to strengthen tax compliance and collection;
- Improving the quality and inclusiveness of education;
- Increasing the coverage and quality of social services;
- Improving social dialogue;
- Developing a minimum wage setting mechanism based on objective criteria;
- Improving access and cost-efficiency of healthcare;
- Focusing investments on key policy areas and strengthening project prioritisation and preparation in public investment.

There has been no progress in the following areas:

- Ensuring that the national fiscal framework is implemented;
- Ensuring the sustainability of the public pension system;
- Improving skills by increasing the labour market relevance of vocational education and training and higher education;
- Completing the minimum inclusion income reform;
- Improving the predictability of decision making;
- Improving the corporate governance of state-owned enterprises.

The Social Scoreboard supporting the European Pillar of Social Rights points to a number of employment and social challenges. High economic growth has translated into improved social conditions. However, poverty and social exclusion, as well as in-work poverty, remain very high while income inequalities have increased. Social transfers have a limited impact on poverty reduction. Inequalities persist, in particular for people in rural and disadvantaged areas. The inactivity rate for women and early school leaving are also very high. The decentralisation of social services has not been accompanied by the provision of proper financial allocations, thus hampering the sustainability of service delivery. The coverage of public services remains low. The de-institutionalisation of children continues to show encouraging progress.

Romania recorded positive progress towards most of its national targets of the Europe 2020 strategy. Romania is performing well on employment rates, national greenhouse gas emissions, renewable-energy levels, energy efficiency and tertiary education. R&D investment and early school leaving remain some distance away from their respective targets.

In terms of the United Nations' Sustainable Development Goals (SDGs), Romania continues its progress towards EU levels ([3]). In climate action (SDG13) Romania is below EU-average levels in greenhouse gas emissions, energy and renewable-energy consumption. In quality education (SDG4) however, Romania is performing particularly poorly with respect to the EU-average levels, with high numbers of early school-leavers and young people neither in education, employment or training. However some improvement can be observed in terms of trends.

([3]) Within the scope of its legal basis, the European Semester can help drive national economic and employment policies towards the achievement of the United Nations Sustainable Development Goals (SDGs) by monitoring progress and ensuring closer coordination of national efforts. The present report contains reinforced analysis and monitoring on the SDGs. Annex E presents a statistical assessment of trends in relation to the SDGs during the past five years, based on Eurostat's EU SDG indicator set.

The main findings of the in-depth review contained in this report and the related policy challenges are as follows:

- **Romania's current account deficit continued to widen and its financing raises concerns.** The current account deficit is expected to continue increasing due to strong import dynamics rather than poor export performance. The composition of imports, tilted towards consumption goods, does not support long-term economic growth. The coverage of the growing current account deficit by foreign direct investments has been declining and past improvements in the net international investment position have recently started to show signs of reversal.

- **The risks to Romania's competitiveness come from both cost and non-cost factors.** Labour cost growth has eased but remains among the highest in the EU**.** Wage increases continue to outpace solid productivity growth, also in sectors integrated in global value chains and open to international trade. The labour cost based real effective exchange rate has appreciated, although at a slower pace. Furthermore, non-cost factors such as the poor quality of infrastructure, the economy's low innovative capacity and poor institutional quality hinder the country's ability to compete internationally.

- **Some of the main risks to the financial sector created by the December 2018 legislation have been averted, but some concerns remain.** The tax on banks' assets was eliminated. As regards the second pension pillar, the possibility to opt out was removed and the additional minimum capital requirements for fund management companies cancelled. However, the overall perception of legislative unpredictability affecting the financial sector persists.

- **Policy unpredictability continued in 2019, still some progress was made on executing the national public procurement strategy.** Persistent uncertainty about policy and legislative decisions contributed to an overall perception of unpredictability in public policymaking. Increased legislative stability and quality of legislative proposals, together with an improved communication on the country's reform direction would help businesses anchor investment decisions. Despite improved implementation, public-procurement efficiency remains an issue, and the irreversibility of certain measures should be further monitored.

Other key structural issues analysed in this report, which point to particular challenges for Romania's economy, are the following:

- **Adverse demographics and existing structural deficiencies require labour activation and upskilling measures.** The persistent negative population growth and the outward migration of skilled labour generated significant labour force shortages. Inactivity has declined but remains one of the highest in the EU especially for women. It also varies considerably across regions and social groups, which indicates a low adequacy and effectiveness of activation measures. Without targeted upskilling and re-skilling measures based on a comprehensive skills forecasting mechanism, the supply of certain skills might become scarce.

- **Poverty and inequality remain high, with limited access to services.** One in three Romanians is at risk of poverty or social exclusion, with vulnerable groups, including the Roma, being the most exposed. Child poverty and educational attainment are closely linked to parents' income. In-work poverty is among the highest in the EU while social benefits and minimum income are failing to reduce poverty. Despite a rapidly ageing population, active ageing measures are missing. Access to services still faces challenges, deepening the rural-urban divide, regional disparities and inequalities. The potential of the social economy to improve social conditions is insufficiently used.

- **The equity, inclusiveness and quality of education remain important challenges.** Education spending is amongst the lowest in the EU. Early school leaving is very high, in particular for pupils in rural areas, Roma children and children with disabilities. An

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integrated, nation-wide strategy targeting early school leaving is not yet in place. Educational outcomes, especially in rural and economically deprived areas, are not improving. The acquisition of digital skills is low, posing challenges for the future labour market integration of graduates. The labour market relevance of vocational education and training and higher education remains low, harming graduates' job perspectives.

- **The healthcare system is not effective in improving neither accessibility nor the health of the population.** Unmet medical needs have increased, with high urban-rural gaps and low coverage for low income groups and the elderly. Preventive, outpatient and community based care remain under-financed and not covered by sufficiently targeted public policy measures. The health status of the population remains below the EU average. Total healthcare spending is low and focused on inpatient care. Population ageing and migration are putting increasing pressure on the sustainability of the healthcare system.

- **Regional disparities in Romania are amongst the highest in the EU.** Significant gaps across regions persist in investment, productivity, competitiveness and employment. Addressing them and prioritising investment at a regional level would help increase the country's competitiveness and support long-term growth, development and modernisation.

- **Romania's weak research and innovation performance hampers the transition towards a knowledge-based economy.** The country continues to have one of the lowest levels of public and private expenditure on research and development in the EU, negatively affecting scientific quality and the diffusion of technology amongst firms. Increasing R&D investment and quality and supporting innovative firms remain important challenges.

- **The reform of the public administration is stalling, still some progress was made on executing the national public procurement strategy.** There has been little progress in decision-making and the quality and effective use of regulatory impact assessments. The development of an effective framework for strategic and budgetary planning has stalled. Red tape and an insufficient capacity to deliver quality services, including digital, are negatively impacting on citizens and businesses. Frequent reorganisations and overuse of temporary management hamper the independence of the administration. High fragmentation of competencies and resources continue to affect the delivery of public services, especially at local level and in poor communities. Public-procurement efficiency remains an issue, and the irreversibility of certain measures should be further monitored.

- **The implementation of corporate governance for state-owned enterprises has shown no significant progress.** There has been a deterioration in the operational and financial performance of state-owned enterprises in 2018 and the first half of 2019.

- **Corruption continues to be a major problem for the business environment in Romania.** While the government currently supports actions to prevent and sanction corruption, Romania is facing important challenges to restore progress in the fight against corruption following damages done in the past years through legislative amendments and continued pressure on judicial institutions.

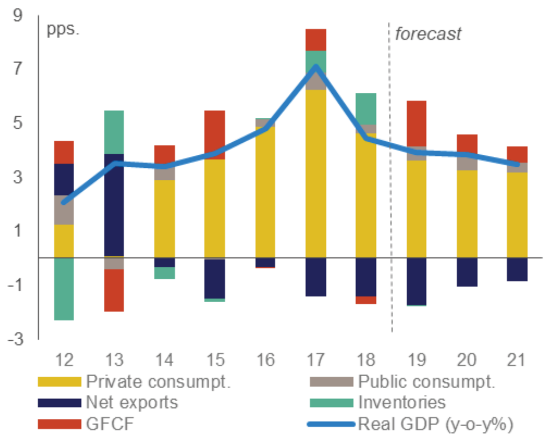
- **Substantial challenges remain regarding air pollution, climate change mitigation and adaptation.** Greenhouse-gas emissions not covered by the EU trading system are set to increase, deviating from the 2030 target. Curbing emissions from transport, buildings and agriculture will be key in reaching the target. Investment in green technologies and sustainable solutions, and securing adequate funding will be key to deliver on the climate and energy objectives and shape a new growth model. The Commission's proposal for a Just Transition Mechanism under the next multi-annual financial framework for the period 2021-2027, includes a Just Transition Fund, a dedicated just transition scheme under InvestEU, and a new public sector loan facility with the EIB. Designed to ensure a fair transition towards EU climate neutrality, it will help the most affected regions to address the social and economic consequences. Key priorities for support by the Just Transition Fund, set up as part of the Just Transition Mechanism, are identified in Annex D.

1. ECONOMIC SITUATION AND OUTLOOK

GDP and potential growth

Growth remained robust in 2019, close to the previous year's level. Real GDP is estimated to have increased by 3.9% in 2019, as a result of strong consumer spending and recovering investment (Graph 1.1). After a drop in 2018, gross fixed capital formation is expected to have contributed positively to growth in 2019, bolstered mainly by a booming construction sector. Net exports' contribution to growth is expected to have remained negative, as softer external demand slowed the dynamics of exports, while imports were still supported by resilient domestic demand.

Graph 1.1: **GDP growth and demand-side components**

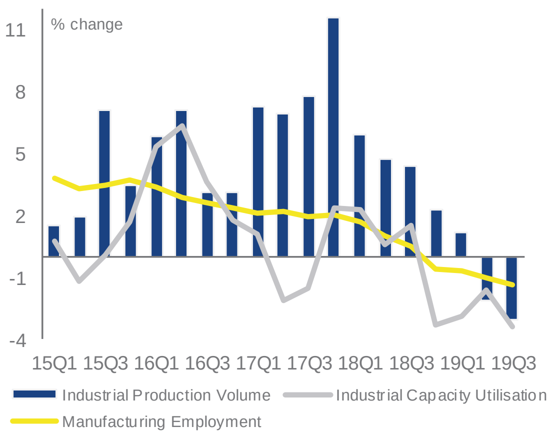


2019-2021: Winter forecast 2020 for real GDP growth, otherwise Autumn forecast 2019
Source: European Commission

Growth is expected to ease off progressively over the medium term. Real GDP growth is set to decelerate to 3.8% in 2020 and to 3.5% in 2021, with consumer spending as the main driver of growth. Net exports are forecast to remain a drag on growth, but slightly less so than in 2019. Lastly, the contribution of investment is expected to stay positive, albeit at lower levels, over the coming years, supported by construction and an acceleration in the absorption of EU funds.

Industrial production began to contract in 2019. Between the end of 2017 and the end of 2018, the growth rate of industrial production fell by almost 10 percentage points and turned negative in Q2-2019. Manufacturing declined by 1.6% over the first three quarters of 2019. The manufacturing of consumer goods has decreased every month since September 2018, while for capital goods production entered a contraction period in April 2019. At the end of Q3-2019, more than 70,000 jobs had been lost in the manufacturing sector compared to the corresponding quarter of 2018. The degree of capacity utilisation in manufacturing began to contract in Q4-2018 (Graph 1.2).

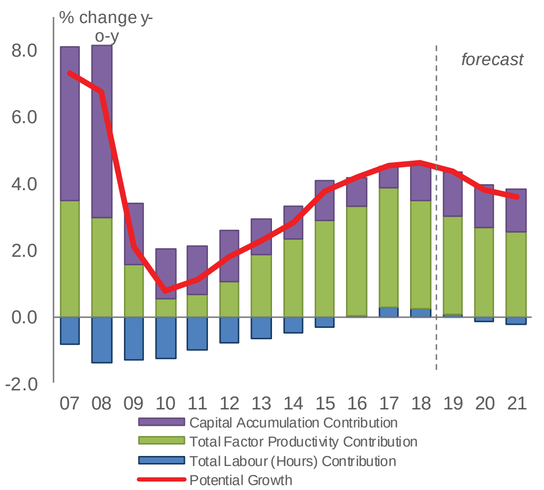
Graph 1.2: **Industrial production**



Source: European Commission

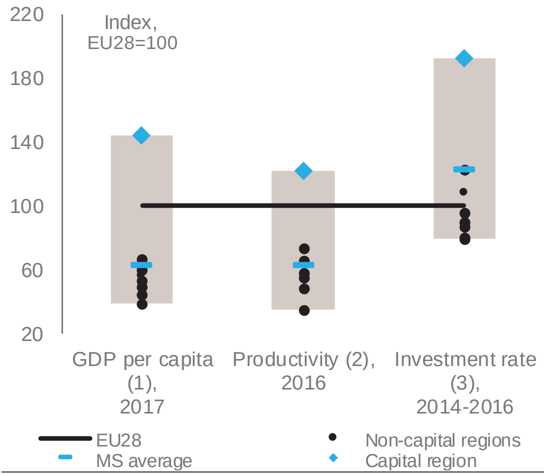
Potential growth is largely driven by total factor productivity and risks being hampered by demographic trends. Potential GDP growth is expected to have declined slightly in 2019 and continue to decrease thereafter. Total factor productivity is projected to decelerate, but remain the main growth contributor. The contribution of capital accumulation is projected to remain broadly stable. On the other hand, the already modest contribution of labour is forecast to turn increasingly negative, mainly due to the constant decrease in working age population (Graph 1.3).

Graph 1.3: **Contribution to potential growth**



Source: European Commission

Graph 1.4: **Disparities between Romanian regions**



Grey areas represent the range of disparities across regions.
(1) GDP per capita in purchasing power standard (PPS)
(2) Gross Value Added per person employed
(3) Percentage of GDP
Source: European Commission

Regional disparities

GDP per head continues to converge with the EU average but regional disparities persist. Income disparities are among the highest in the EU, mainly driven by the large gap between the capital region of Bucharest and the rest of the country. In five of the eight Romanian development regions (NUTS 2 regions), GDP per head grew faster than the EU average, while the three poorest regions saw their GDP per head shrink between 2011 and 2017. In the capital region, GDP per head corresponds to 144% of the EU average and has grown the fastest over the last six years. At 67% of the EU average, the Vest region has the second highest GDP per head in Romania. In the other Romanian regions, GDP per head ranges from 39% to 60% of the EU average (Graph 1.4).

Labour productivity differences between regions remain significant. Labour productivity in the capital region of Bucharest stands at 122% of the EU average, compared to just 73% in the Vest region, the second most productive (Graph 1.4). Differences in productivity growth rates are also significant. Between 2010 and 2016, real productivity grew fastest in the Vest (8.3%) and Sud-Est (6.5%) regions, followed by the capital region (6.4%). The other regions saw lower productivity growth, but still above the EU average (0.8%), with the exception of Nord-Est, where productivity shrunk by 1.4% per year.

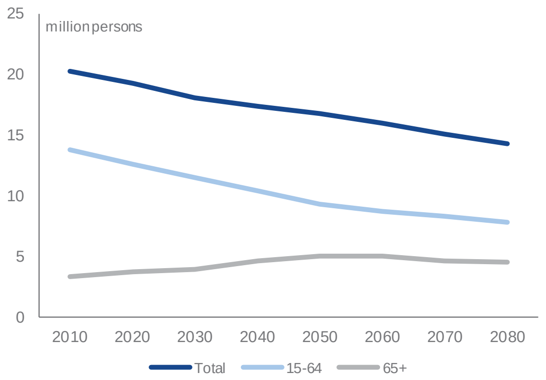
Investment levels are highly uneven. Less developed regions need a high level of public and private investment in order to catch up with the more developed regions. Between 2014 and 2016, investment in the Bucharest region, measured as gross fixed capital formation as a percentage of GDP, was almost twice the EU average, while in the other regions investment hovered around the EU average. Apart from the capital region, the level of investment was above the EU average in only two other regions, Nord-Vest and Centru.

Rural-urban disparities remain significant. Positive labour market developments are not benefitting all regions and population groups equally. The at-risk-of-poverty rate in rural areas is almost five times higher than in cities. Large regional disparities are detrimental to long-term sustainable growth. Regions with significant shares of the workforce concentrated in low-productivity sectors are characterised by relatively low salaries and high poverty rates, which have a negative impact on social cohesion.

Demography

Romania's population has decreased over recent decades and is projected to shrink further. It has fallen by 3.8 million since 1990 and is projected to fall to 15 million by 2070 (Graph 1.5), from the current level of 19.4 million, driven by demographic change, including emigration. As a consequence, the old-age dependency ratio, i.e. the ratio of people aged 65+ relative to people of working-age (15-64), is projected to double from 26.3% in 2016 to 52.8% in 2070. This implies that the number of working-age people for every person aged over 65 would fall from almost four to just two. Population ageing has a negative impact on the adequacy of pensions and on future spending on healthcare and the long-term sustainability of public finances.

Graph 1.5: **Demographic change in Romania**



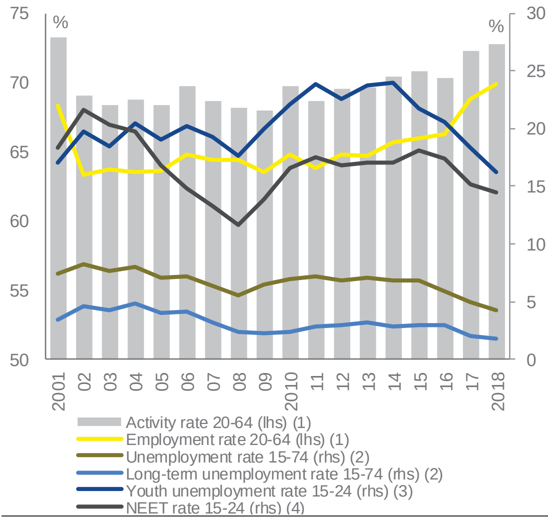
Source: European Commission

Labour market, poverty and social inclusion

On the back of positive economic developments, labour market conditions remain tight. Since 2017, there has been a general pick-up in employment, with an increase of 0.2% in 2018 (Graph 1.6), to a record employment rate of 70.8% in Q3-2019. This trend is expected to continue with employment growing further in 2019 and 2020. The unemployment rate fell to 3.9% in 2019, its lowest level since 1997.

Despite the overall positive labour market performance, a number of challenges remain. Romania has one of the lowest labour force participation rates in the EU and its working-age population has been declining steadily since 2008, while labour and skills shortages have been increasing. At the same time, the percentage of young people not in education, employment or training (NEET), standing at 14.5% in 2018, is one of the highest in the EU. The activity rate (for ages 15-64 years) is still among the lowest in the EU, in particular for women (58.7% in Q3 2019, compared to 77.9% for men) and people with low educational attainment (43.8% in Q3 2019 vs 88.8% among those with high educational attainment). Activation measures are not fully effective, especially in the case of vulnerable groups. The weak functioning of social dialogue does not adequately involve social partners in the design and implementation of reforms.

Graph 1.6: **Labour market overview**



(1)% of total population between 20-64
(2)% of total labour force between 15-74
(3)% of total labour force between 15-24
(4)% of total population between 15-24
Source: European Commission

Wages have increased significantly in Romania in recent years. Nominal wages continued to grow at a fast pace. As they grew more than inflation, real wages also increased, boosting employees' purchasing power. Wages remain low compared to the EU average and relatively high wage growth is to be expected from a catching-up economy. Public wages more than doubled between Q1-2015 and Q2-2019 and have significantly outpaced wages in the private sector, but they are expected to slow down in 2020. The minimum wage has also been increased markedly. While not yet directly visible, the sustained pace of wage growth may nonetheless pose risks to competitiveness in the future, if wages continue to increase ahead of productivity.

Poverty continued to decline but inequality has deepened. Despite higher wages and pensions, income inequality increased in 2018 following a two-year decline, while slightly decreasing in almost all Member States. The income share of the poorest 40% of the population, already one of the lowest in the EU, decreased. Despite a further decline in 2018, the percentage of people at risk of poverty or social exclusion was still among the highest in the EU, with one in three Romanians still at risk of poverty or social exclusion. In 2018, in-work poverty dropped, but it still stands at 15.3%. Poverty risks affect rural areas and vulnerable groups more strongly and tend to be associated with low educational attainment and unfavourable socio-economic status. Child poverty remains among the highest in the EU, affecting 38.1% of children compared to an EU average of 24.3%. Social transfers have a very low impact on poverty reduction (European Commission, 2019d).

Investment

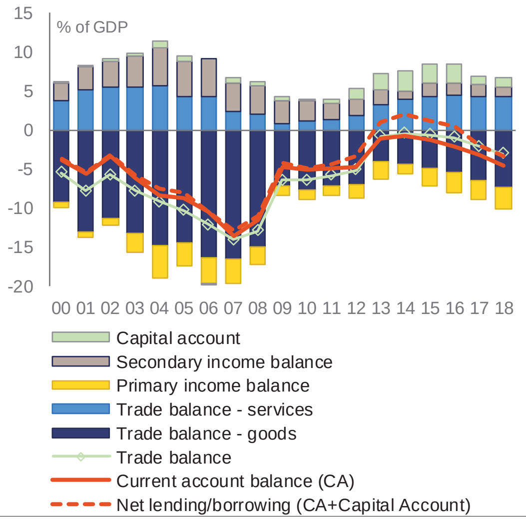
After a modest performance in 2018, total investment recovered in 2019, increasing by more than 18% in the first three quarters of the year. In 2018, total investment accounted for 21.0% of GDP, above the EU and peer countries' averages of 20.3% and 20.9% respectively. Private investment has dropped to 18.3% of GDP but remained above the averages for the rest of the EU and peer countries. Meanwhile, public investment slightly recovered from the post-EU accession low in 2017, increasing to 2.7% of GDP (see Section 4.4). However, it remained below the EU average and much below the average of the neighbouring countries. Total investment recovered in 2019, increasing by more than 17% in the first three quarters of the year. It is expected to remain relatively robust thanks to construction investment and an acceleration of spending on projects co-funded by the EU towards the end of the current programming period.

Investment could be negatively affected by persistent uncertainty. Continued unpredictability of public policies could hinder business confidence and investment decisions (see Section 4.4.5). Budgetary pressures resulting from the new pension law (see Box 4.1.1) also pose a downward risk to public investment.

External position

The current account deficit deteriorated further in 2019 on the back of strong domestic demand fuelling imports. Following a sharp increase in 2018 to -4.4% of GDP, the current account deficit is estimated to have further deteriorated to -5.1% of GDP in 2019 (Graph 1.7). The worsening of the goods trade balance was the main determinant of this evolution, with trade deficits in intermediate and consumer goods being the two main drivers. The deficits were the result of imports still advancing faster than exports. The slowdown in the growth of the surplus in services also contributed to this trend. Overall, export perform well and market shares increased. As in 2018, the current account balance continues to diverge from the values supported by the economy's fundamentals, which imply a balanced position ([4]).

Graph 1.7: **Current account breakdown and capital account**



Source: European Commission

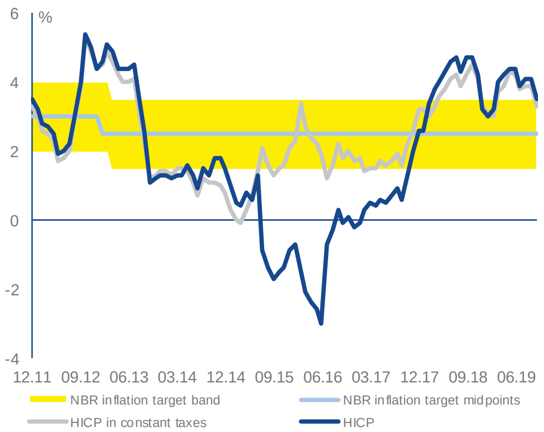
After years of improvement the net international investment position shows signs of setback. From a trough of some -68% of GDP in 2012 the net international investment position reached -43.7% of GDP in 2018 but slightly worsened to -44.3% in Q3-2019, following the deterioration of the current account balance. This evolution could continue as GDP growth slows and the current account deficit is expected to widen further. A positive capital account balance has partly mitigated, but not fully offset, the country's net borrowing as a whole. Past improvement was driven by a marked reduction of other investment (loans, currency and deposits, trade credit). More recently, portfolio investment picked up while the reserve assets declined somewhat (see Section 4.4.1).

([4]) For details regarding the estimation of current accounts' fundamentals, see Coutinho, Turrini and Zeugner (2018).

Inflation and monetary policy

Inflation edges down but remains among the highest in the EU. After a peak of 4.7% in September 2018, the harmonised index of consumer prices (HICP) started to ease and inched slightly below 3.9% in 2019, still among the highest in the EU (Graph 1.8). The decline in HICP inflation was largely due to the fall in energy prices, on account of international oil price developments. Despite the moderate decrease in headline inflation, core inflation (i.e. excluding energy and unprocessed food) remained high throughout 2019, at an average of 3.8%, supported by strong wage growth. In the medium term, headline inflation is expected to decrease moderately, to 3.4% in 2020 and 3.3% in 2021, thus re-entering the National Bank of Romania's (NBR) inflation target band (2.5% ± 1 pp.). The NBR maintained its policy rate at 2.5% throughout 2019 and at the beginning of 2020, while applying strict control over money market liquidity to counter inflationary pressures.

Graph 1.8: **Harmonised index of consumer prices (HICP)**

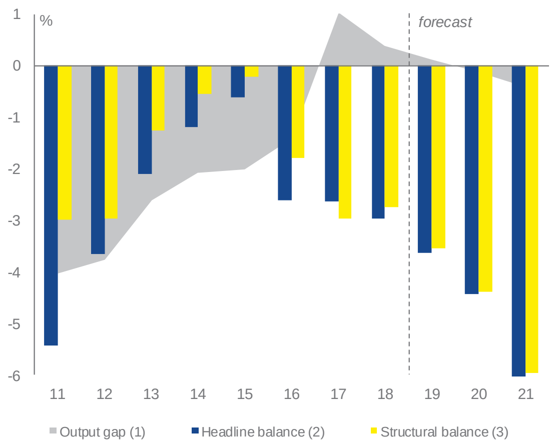


(1) HICP in constant taxes assumes a full pass-through of VAT changes to consumer prices.
(2) Inflation targets formulated in terms of annual change in the CPI and set as midpoints within a target band of +/- 1pp percentage points.
Source: European Commission, National Bank of Romania

Public finances

The public deficit has been widening, driven by higher current spending. The headline deficit is projected to have risen from 2.9% in 2018 to 3.6% of GDP in 2019, mostly driven by public wage expenditure. The headline deficit is set to continue widening, to 4.4% of GDP in 2020 and 6.1% of GDP in 2021, due to significant increases in old age pensions enacted in summer 2019 (see Box 4.1.1). The structural deficit ([5]) is projected to rise, to close to 6% of potential GDP in 2021 (Graph 1.9).

Graph 1.9: **General government balance and output gap**

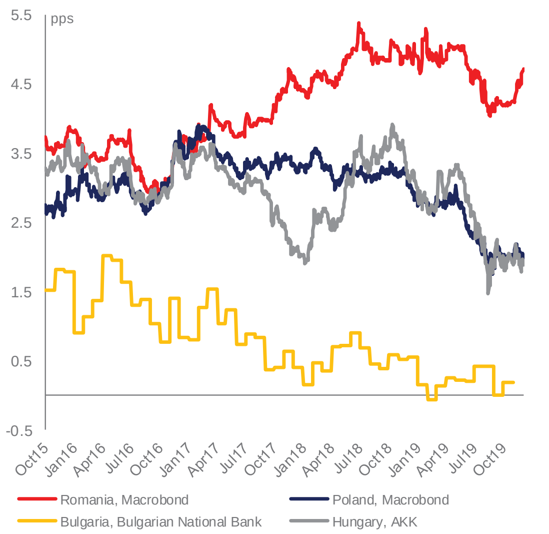


(1)% of potential GDP
(2)% of GDP
(3)% of potential GDP
Source: Eurostat, European Commission 2019 Autumn Economic Forecast

General government debt is projected to increase. Because of the widening of the public deficit, the general government debt is set to rise from 35% of GDP in 2018 to 40.6% of GDP in 2021. Assuming no policy change, the debt is set to increase above 90% of GDP by 2030. The financing cost of public debt is well above those observed for peer countries (Graph 1.10). Financial markets' perceptions of sovereign risk are at the lower limit of the investment grade, with a 'BBB-' or equivalent rating of the sovereign debt from the three major rating agencies. On 10 December 2019, S&P Global Ratings revised its outlook on Romania from stable to negative, due to its budgetary stance (Section 4.1.4).

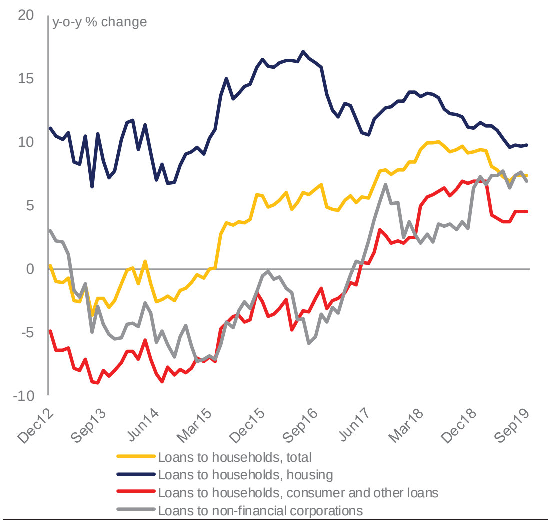
([5]) The deficit corrected for the business cycle and one-off operations.

Graph 1.10: **10 year government bond yield: Romania and peers**



Source: European Commission

Graph 1.11: **Loans to households and non-financial corporations**



Source: National Bank of Romania

Financial sector

The banking sector's capitalisation is above the EU average, but some vulnerabilities persist. While banking sector capitalisation and funding have remained robust, some signs of asset deterioration have resurfaced with increasing new non-performing loans (NPL), even though the gross NPL ratio at system-level further decreased. The bank-sovereign nexus has remained significant, as government bond holdings represent almost 18% of total assets in the banking sector, with a marked home bias, compared to a 3.2% average for euro area banks. The level of financial intermediation in 2018 was 25.6% of GDP, below the EU average, limited by legislative changes and weaknesses in the corporate sector.

Total credit continued growing in 2019 but at slower pace. Credit activity expanded more markedly from the end of 2017, when economic growth peaked in Romania. In terms of composition, around 75% of the credit went to the domestic private sector and around 20% were loans to non-residents in 2019. A decreasing share of 2.8% went to the public sector. In terms of private credit composition, households continued to account for the bulk of banks' credit allocation, despite a slow deceleration in 2019 (Graph 1.11). Loans to non-financial corporations remained broadly stable after an acceleration at the end of 2018 and beginning of 2019.

Private credit remained relatively steady in 2019 but growth performance was tilted towards foreign currencies. As a share, all types of currency loans remained broadly unchanged in 2019. However, the private sector seems to demand less credit denominated in domestic currency while loans denominated in foreign currencies, mainly in euro, accelerated in 2019, especially for non-financial corporations. Foreign-currency denominated loans to corporations grew at the beginning of 2019 for the first time since 2016 (NBR, 2019).

Over the last 10 years, the distribution of household credit between housing and consumer loans has inverted. In 2009, just 23% of such loans were for housing purposes. Since 2016, credit to households for housing loans has outweighed consumer loans. In 2019, this trend continued, fuelled by increases in disposable income and public support measures for mortgage lending such as the Prima casa (First Home) programme (see Section 4.2).

Housing market

Residential construction saw strong growth while house prices were quite stable. In the third quarter of 2019 residential construction activity recorded a 33.1% expansion in annual terms, in stark contrast to the loss of steam that characterised the sector in 2018. The development was supported by the rise in household income and by a cut in the VAT rate to 5% for second-home purchases. Growth in the sector is forecast also to continue in 2020, as indicated by positive consumers' intention. Following healthy growth rates in the first half of 2018, house prices stagnated in the second part of the year. Prices started picking up again in the first half of 2019.

Progress towards the SDGs ([6])

Romania is making progress towards achieving the United Nations' Sustainable Development Goals (SDGs). Areas where progress is more evident refer to SDG 17 "Partnership for the goals", with all its associated indicators showing an improving performance during the last five years. Relatively similar performances are found for SDG 1 "No poverty" and SDG 13 "Climate action". Notwithstanding this improving performance, current levels for some of these indicators are significantly lower than the EU average, particularly for SDG 4 "Quality education", where all indicators are below the EU average, and closely followed by SDG 1 "No poverty" and SDG 3 "Good health and well-being".

([6]) Annex E provides an overview of Romania's performance with regard to the broad range of the United Nations' Sustainable Development Goals.

Table 1.1: **Key economic and financial indicators**

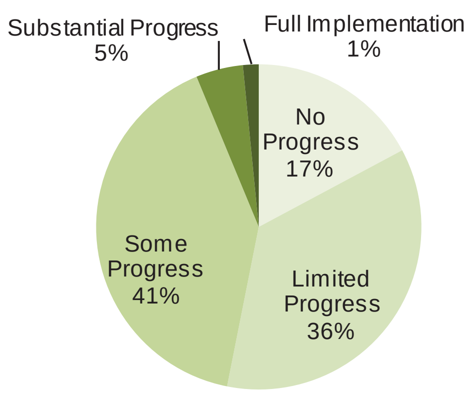
	2004-07	2008-12	2013-16	2017	2018	forecast 2019	2020	2021
Real GDP (y-o-y)	7.6	0.7	3.9	7.1	4.4	3.9	3.8	3.5
Potential growth (y-o-y)	6.1	2.5	3.3	4.5	4.6	4.4	3.8	3.6
Private consumption (y-o-y)	12.8	0.0	4.6	10.0	7.3	.	.	.
Public consumption (y-o-y)	1.9	1.2	0.6	4.2	2.1	.	.	.
Gross fixed capital formation (y-o-y)	23.6	-3.7	1.1	3.6	-1.2	.	.	.
Exports of goods and services (y-o-y)	13.9	7.0	12.0	7.6	6.2	.	.	.
Imports of goods and services (y-o-y)	27.9	1.4	10.5	10.8	9.1	.	.	.
Contribution to GDP growth:								
Domestic demand (y-o-y)	15.2	-1.1	3.2	7.7	4.7	.	.	.
Inventories (y-o-y)	-1.4	0.0	0.3	0.8	1.2	.	.	.
Net exports (y-o-y)	-6.4	1.3	0.4	-1.4	-1.4	.	.	.
Contribution to potential GDP growth:								
Total Labour (hours) (y-o-y)	-0.7	-1.2	-0.4	0.3	0.2	0.1	-0.1	-0.2
Capital accumulation (y-o-y)	2.1	2.3	1.0	0.6	1.1	1.3	1.3	1.3
Total factor productivity (y-o-y)	4.7	1.4	2.6	3.6	3.2	2.9	2.7	2.6
Output gap	4.6	-1.0	-2.0	1.0	0.4	0.1	-0.1	-0.4
Unemployment rate	7.2	6.6	6.7	4.9	4.2	3.9	4.2	4.3
GDP deflator (y-o-y)	13.4	6.2	2.5	4.7	6.3	7.3	4.5	4.4
Harmonised index of consumer prices (HICP, y-o-y)	8.1	5.7	0.8	1.1	4.1	3.9	3.4	3.3
Nominal compensation per employee (y-o-y)	15.8	8.0	6.9	14.8	13.4	13.0	9.2	7.1
Labour productivity (real, person employed, y-o-y)	7.8	2.5	4.5	4.6	4.2	.	.	.
Unit labour costs (ULC, whole economy, y-o-y)	7.4	5.3	2.2	9.8	8.8	8.8	5.6	3.8
Real unit labour costs (y-o-y)	-5.3	-0.9	-0.3	4.9	2.4	1.4	1.0	-0.5
Real effective exchange rate (ULC, y-o-y)	9.1	-3.0	1.2	7.9	5.9	3.5	2.4	1.8
Real effective exchange rate (HICP, y-o-y)	8.5	-2.9	0.3	-1.7	2.3	-0.2	0.6	1.3
Net savings rate of households (net saving as percentage of net disposable income)	-23.2	-21.1	-19.4	-15.4	-8.9	.	.	.
Private credit flow, consolidated (% of GDP)	14.0	3.0	-0.8	1.7	1.9	.	.	.
Private sector debt, consolidated (% of GDP)	43.7	70.6	60.1	50.9	47.4	.	.	.
of which household debt, consolidated (% of GDP)	12.0	21.4	17.8	16.1	15.8	.	.	.
of which non-financial corporate debt, consolidated (% of GDP)	31.8	49.3	42.3	34.8	31.6	.	.	.
Gross non-performing debt (% of total debt instruments and total loans and advances) (2)	1.4	.	13.0	5.1	4.1	.	.	.
Corporations, net lending (+) or net borrowing (-) (% of GDP)	-2.4	8.7	12.1	12.2	6.7	6.7	6.9	7.6
Corporations, gross operating surplus (% of GDP)	26.6	31.7	31.6	30.5	28.0	28.1	27.8	28.1
Households, net lending (+) or net borrowing (-) (% of GDP)	-5.6	-7.9	-9.1	-11.3	-6.9	-6.8	-6.4	-5.4
Deflated house price index (y-o-y)	.	.	0.7	3.3	1.3	.	.	.
Residential investment (% of GDP)	2.0	2.9	2.5	2.7	2.0	.	.	.
Current account balance (% of GDP), balance of payments	-10.3	-6.2	-0.7	-2.8	-4.4	-5.3	-5.5	-5.6
Trade balance (% of GDP), balance of payments	-11.4	-7.4	-0.6	-2.1	-3.1	.	.	.
Terms of trade of goods and services (y-o-y)	7.5	1.0	1.3	0.1	0.8	0.9	0.4	0.4
Capital account balance (% of GDP)	0.5	0.6	2.4	1.2	1.2	.	.	.
Net international investment position (% of GDP)	-37.4	-61.7	-56.0	-47.4	-43.7	.	.	.
NENDI - NIIP excluding non-defaultable instruments (% of GDP) (1)	-5.0	-22.2	-13.6	-5.5	-3.9	.	.	.
IIP liabilities excluding non-defaultable instruments (% of GDP) (1)	36.1	57.7	47.7	37.4	34.1	.	.	.
Export performance vs. advanced countries (% change over 5 years)	84.0	69.7	24.1	34.5	21.6	.	.	.
Export market share, goods and services (y-o-y)	13.9	2.3	7.7	3.0	4.0	2.5	0.5	0.0
Net FDI flows (% of GDP)	.	-2.8	.	-2.6	-2.4	.	.	.
General government balance (% of GDP)	-1.7	-6.1	-1.6	-2.6	-3.0	-3.6	-4.4	-6.1
Structural budget balance (% of GDP)	.	.	-1.0	-3.0	-2.7	-3.5	-4.4	-5.9
General government gross debt (% of GDP)	14.8	26.9	38.0	35.1	35.0	35.5	37.2	40.6
Tax-to-GDP ratio (%) (3)	28.8	27.3	27.3	25.8	27.1	27.3	27.5	27.6
Tax rate for a single person earning the average wage (%) (4)	.	28.5	25.5	25.6	36.9	.	.	.
Tax rate for a single person earning 50% of the average wage (%) (4)	.	25.4	22.7	22.5	34.6	.	.	.

(1) NIIP excluding direct investment and portfolio equity shares.
(2) Domestic banking groups and stand-alone banks, EU and non-EU foreign-controlled subsidiaries and EU and non-EU foreign-controlled branches.
(3) The tax-to-GDP indicator includes imputed social contributions and hence differs from the tax-to-GDP indicator used in the section on taxation.
(4) Defined as the income tax on gross wage earnings plus the employee's social security contributions less universal cash benefits, expressed as a percentage of gross wage earnings
Source: Eurostat and ECB as of 4-2-2020, where available; European Commission for forecast figures (Winter forecast 2020 for real GDP and HICP, Autumn forecast 2019 otherwise)

2. PROGRESS WITH COUNTRY-SPECIFIC RECOMMENDATIONS

Since the start of the European Semester in 2011, 47% of all country-specific recommendations addressed to Romania have recorded at least 'some progress'. 53% of country-specific recommendations recorded 'limited' or 'no progress' (Graph 2.1). Overall, Romania has advanced in implementing its country-specific recommendations since 2013. Even though efforts have been made, in several policy areas, action is slow and the country must endeavour to achieve tangible results on implementing reforms.

Graph 2.1: **Overall multiannual implementation of 2011-2019 CSRs to date**



(1) The overall assessment of the country-specific recommendations related to fiscal policy excludes compliance with the Stability and Growth Pact
(2) 2011 annual assessment: Different country-specific recommendation assessment categories
(3) The multiannual country-specific recommendations assessment looks at the implementation from the first year of adoption until the 2020 Country report
Source: European Commission

Since 2016, Romania has been pursuing an expansionary fiscal policy, not respecting its fiscal framework. Such policy led to a significant increase of the public deficit. Since 2016, the authorities have been systematically and repeatedly derogating from the national fiscal rules, thereby rendering them largely inoperable. Limited progress was made to strengthen tax compliance and tax collection. The VAT gap remains the highest in the EU although it is estimated to have decreased since 2017.

Risks to fiscal sustainability are high. Due to high public deficit and increasing ageing costs, in particular pensions and health care, the risks to fiscal sustainability are high. These risks worsened in 2019, due to the adoption of the new pension law. On the other hand, several legal provisions that threatened the long term viability of the second pension pillar were abrogated or amended at the beginning of 2020.

Substantial progress was achieved in safeguarding financial stability and the banking sector. The bank tax on total assets introduced by the Government Emergency Ordinance 114/2018 was completely removed at the beginning of 2020.

Access to quality and inclusive education remains insufficient and skills' improvement is lacking. Furthermore, consistently low educational outcomes and high rates of early school leaving also remain. Ensuring equal opportunities for students from poor households, particularly in rural areas, and the Roma community remains a challenge. The labour market relevance of vocational, training and higher education remains limited and damages job perspectives. The acquisition of basic and digital skills showed no progress, and would benefit from methods to forecast and anticipate future skill needs.

Progress on labour market reforms is limited. Few steps were taken to increase coverage and quality of social services and education, however effective results are not yet visible. The social reference index, used as a basis for most social benefits, has not been updated since its introduction in 2008. Social dialogue remains largely formalistic and modification of the legal framework stalled for a number of years. Even though no objective mechanism is yet in place, the minimum wage increase of January 2020 was based on certain economic indicators such as inflation or labour productivity. The implementation of the minimum inclusion income law, adopted in 2016, continues to be repeatedly postponed, thus no progress was recorded on this front.

The healthcare system faces multiple challenges. There has been limited progress in improving access to healthcare. Unmet needs for medical examination reported by patients are increasing again. A sustained policy of incentivising healthcare delivered outside of hospital inpatient settings by the National Insurance House may trigger a natural shift towards ambulatory care. The overall policy measures of the health system to facilitate this shift did not improve.

Limited progress was made on focusing investment in key policy areas. Railway infrastructure would benefit from feasibility studies for its upgrade and works are lagging. For road transport, European grants were allocated to develop a multi-standard open-access fast charging network along core-network corridors. Some progress was recorded on the acceleration of the implementation of environmental infrastructure projects, especially in waste water, towards the end of 2019. For other areas, there is either limited progress, for instance waste projects, or no progress, as in regard to air, biodiversity and R&I&D projects. For the latter, without a significant increase in public R&D plus improved regulatory measures to enhance quality, little progress is expected.

There has been no progress in improving the predictability of decision-making. Predictability of decision making remains a concern, with no tangible progress. Less than 30% of the annual government plan is respected and the number of emergency ordinances is still very high, with some having major socio-economic impact (e.g. GEO 114/2018). This type of legislation has no mandatory ex-ante impact assessment and no requirement for public consultations. Ex-ante regulatory impact assessment continues to be lacking, with no legal institutional framework. Moreover, although different formal structures exist, the quality of public consultations is deteriorating.

Overall, Romania made limited progress ([7]) in addressing the 2019 country-specific recommendations. There has been substantial progress on the financial and banking sectors; and some progress on the second-pillar pension-fund viability and public procurement. Limited progress was reached on tax compliance and collection, education, social services and dialogue, healthcare, minimum wage setting, investment and investment prioritisation. No progress was made on the fiscal framework and the public pension system, skills, minimum inclusion income, predictability of decision-making and the corporate governance of state-owned enterprises.

Upon request from a Member State, the Commission can provide tailor-made expertise via the Structural Reform Support Programme to help design and implement growth-enhancing reforms. Since 2017, such support has been provided more than 46 projects. In 2019, several projects were delivered on the ground, including support to the National Fiscal Agency on risk assessment, selection and auditing of large taxpayers and e-commerce transactions and to the Financial Supervisor on developing solutions for dormant accounts on the equity market, as well as consolidating risk based supervision across all sectors. Support was also provided to the National agency for Roma on monitoring and evaluating County Action Plans, to the Ministry of Labour on the development of an indexation mechanism and on piloting a new payment method for social assistance benefits, and to the Ministry of Tourism on the development of destination management organizations. New projects were initiated in late 2019-early 2020 to support the elaboration of the Strategy for Economic and Social Development of the Jiu Valley, the simplification of the licensing system and the adoption of quality management standards for primary care and ambulatory care providers outside hospital settings.

([7]) Information on the level of progress and actions taken to address the policy advice in each respective subpart of a country specific recommendation is presented in the overview table in Annex A.

Table 2.1: **Assessment of 2019 CSR implementation**

Romania	**Overall assessment of progress with 2019 CSRs: Limited progress**
CSR 1: *Ensure compliance with the Council Recommendation of 14 June 2019 with a view to correcting the significant deviation from the adjustment path towards the medium-term budgetary objective. Ensure the full application of the fiscal framework. Strengthen tax compliance and collection.*	**Limited progress** • No progress was made in ensuring that the national fiscal framework is implemented. • Limited progress was made in strengthening tax compliance and collection.
CSR 2: *Safeguard financial stability and the robustness of the banking sector. Ensure the sustainability of the public pension system and the long-term viability of the second-pillar pension funds.*	**Some progress** • Substantial progress was made in safeguarding financial stability and the robustness of the banking sector. • No progress was made on ensuring the sustainability of the public pension system. • Some progress was made on ensuring the long-term viability of the 2nd pension pillar.
CSR 3: *Improve the quality and inclusiveness of education, in particular for Roma and other disadvantaged groups. Improve skills, including digital, in particular by increasing the labour market relevance of vocational education and training and higher education. Increase the coverage and quality of social services and complete the minimum inclusion income reform. Improve the functioning of social dialogue. Ensure that the minimum wage is set based on objective criteria, consistent with job creation and competitiveness. Improve access to and cost-efficiency of healthcare, including through the shift to outpatient care.*	**Limited progress** • Limited progress was made on improving the quality and inclusiveness of education. • No progress was made on improving skills. • Limited progress was made on increasing the coverage and quality of social services. • No progress was made on completing the minimum inclusion income reform. • Limited progress was made on improving social dialogue. • Limited progress was made on minimum wage setting. • Limited progress was made on improving access and cost-efficiency of healthcare.
CSR 4: *Focus investment-related economic policy on transport, in particular on its sustainability, low-carbon energy and energy efficiency, environmental infrastructure as well as innovation, taking into account regional disparities. Improve the preparation and prioritisation of large projects and accelerate their implementation. Improve the efficiency of public procurement and ensure the full and sustainable implementation of the national public procurement strategy.*	**Limited progress** • Limited progress was made on focusing investments on key policy areas. • Limited progress was made on strengthening project prioritization and preparation in public investment. • Some progress was made on implementing the national public procurement strategy.
CSR 5: *Ensure that legislative initiatives do not undermine legal certainty by improving the quality and predictability of decision-making, including by appropriate stakeholder consultations, effective impact assessments and streamlined administrative procedures. Strengthen the corporate governance of State-owned enterprises.*	**No progress** • No progress was made on improving the predictability of decision-making. • No progress was made on improving the corporate governance of State owned enterprises.

(1) This does not include an assessment of compliance with the Stability and Growth Pact
Source: European Commission

For CSR 4: The regulatory framework underpinning the programming of the 2021-2027 EU cohesion policy funds has not yet been adopted by the co-legislators, pending inter alia an agreement on the multiannual financial framework (MFF

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Box 2.1: EU funds and programmes to address structural challenges and to foster growth and competitiveness in Romania

Romania is one of the countries benefiting most from EU support. The financial allocation from the EU Cohesion policy funds ([1]) for Romania amounts to €26.8 billion in the current Multiannual Financial Framework (2014-2020), equivalent to around 2% of the GDP annually. By the end of 2019, some €28.5 billion (more than the total amount planned) was allocated to specific projects and €7.2 billion was reported as spent by the selected projects ([2]), showing a level of implementation well below the EU average.

While bringing about a more harmonious development through reducing economic, social and territorial disparities, EU Cohesion policy funding already significantly supports structural challenges in Romania. The Cohesion policy programmes for Romania have allocated EU funding of €2.7 billion for smart growth, €13 billion for sustainable growth and sustainable transport and €6.2 billion for inclusive growth. In 2019, following a performance review ([3]), €888 million have been made available for Romania within performing priorities.

EU Cohesion policy funding is contributing to major transformations of the Romanian economy by promoting growth and employment via investments, among others, in research, technological development and innovation, competitiveness of enterprises, sustainable transport, employment and labour mobility. By 2019, investments driven by EU Funds led to the reconstruction of 318 km of TEN-T railway lines, to works on 4,364 km of new or reconstructed roads, out of which 692 km in the TEN-T network and to the reconstruction and modernisation of four airports. Moreover, support is to be provided for 2,708 micro, small and medium size enterprises as well as 178 social enterprises. Cohesion policy funding will contribute to increasing the additional waste recycling capacity by 1,308,262 tonnes/year and to ensure a better conservation status for 41,416 hectares of habitats. In addition, 4,207,040 persons are expected to benefit from flood protection measures. Approximately 350,000 persons benefited from active labour market measures and had access to integrated educational services. Some 6.34 million people received food support and about 15 million food packages were distributed.

Agricultural and fisheries funds and other EU programmes also contribute to addressing the investment needs. The European Agricultural Fund for Rural Development makes available €9.6 billion and the European Maritime and Fisheries Fund €223 million (including the national co-financing for both). Romania benefits also from other EU programmes, such as the Connecting Europe Facility, which allocated EU funding of €1.2 billion to specific projects on strategic transport networks, Horizon 2020, which allocated EU funding of €196 million (including 90 SMEs with about €21.2 million) and Erasmus+, which allocated €413 million so far.

EU funding contributes to mobilisation of important private investment. European Structural and Investment Funds ([4]) supported programmes alone mobilise additional capital by committing about €457.8 million via financial instruments in the form of loans, guarantees and equity. EU funds already invest substantial amounts on actions in line with the Sustainable Development Goals (SDGs). In Romania the European Structural and Investment Funds support 13 out the 17 SDGs and up to 95% of the expenditure is contributing to those.

([1]) European Regional Development Fund, Cohesion Fund, European Social Fund, Youth Employment Initiative.
([2]) https://cohesiondata.ec.europa.eu/countries/RO
([3]) The performance review is regulated by art 22 of Regulation (EU) No 1303/2013.
([4]) European Regional Development Fund, Cohesion Fund, European Social Fund, European Agricultural Fund for Rural Development Fund and European Maritime and Fisheries Fund.

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3. SUMMARY OF THE MAIN FINDINGS FROM THE MIP IN-DEPTH REVIEW

The 2020 Alert Mechanism Report concluded that a new in-depth review should be undertaken for Romania to assess the persistence or unwinding of imbalances (European Commission, 2019e). In February 2019, Romania was identified as experiencing macroeconomic imbalances (European Commission, 2019f). The imbalances identified related to risks of cost competitiveness losses and a widening current account deficit in the context of an expansionary fiscal policy and an unpredictable business environment. Moreover, risks to the functioning of the financial sector were also identified. This chapter summarises the analyses in the context of the Macroeconomic Imbalances Procedure (MIP) in-depth review that is contained in various sections of this report ([8]).

3.1. IMBALANCES AND THEIR GRAVITY

The current account deficit is large and has been widening since 2014. The current account balance reached a deficit of 4.4% of GDP in 2018 and is estimated to have deteriorated to 5.1% of GDP in 2019. This evolution implies an increasing divergence from the economy's fundamentals, which point to a close- to- balance current account. This is mainly the result of an increasing deficit in the trade in goods, spurred by a fiscal-led consumer spending boom in times of high GDP growth. Changes in composition are also a concern, as growth in imports has been substantially higher for consumer goods than for intermediate or capital goods, meaning that the consumption and import spree is not likely to support the growth potential of the economy or improving living standards in a sustainable way. The coverage of the growing current account deficit by foreign direct investment and the capital account has been declining; instead, portfolio investment has gained relevance. The net international investment position improved further to –43.7% of GDP in 2018, but started to deteriorate in 2019. Past improvements, of more than 20 percentage points since 2012, have been mainly due to the strong nominal GDP growth more than offsetting the current account deficit.

Unit labour cost growth remains among the highest in the EU although it started to moderate. Despite significant productivity gains, which are to some extent a catching-up effect from a low starting point, increases in compensation per employee have been significantly outpacing productivity growth since 2016, leading to a marked acceleration of unit labour costs. At the end of 2018, unit labour costs returned to single-digit growth rates, but their increase is nevertheless expected to remain above those of most Member States. The unit labour costs-based real effective exchange rate, which started to increase in 2016, continued to appreciate, albeit at a slower pace.

Public and minimum wages have been increasing rapidly, potentially affecting competitiveness. Public wages continued to increase at double-digit rates in 2018 and 2019, although the pace of these increases is expected to diminish as of 2020. Empirical evidence (Biea et al, 2019) shows that the public sector plays a leading role in wage determination in Romania which may lead to higher private sector wages, potentially undermining cost competitiveness. The government-set annual increases in the statutory minimum wage, since 2015, have added to wage pressures and reinforced the potential negative effect on competitiveness. Moreover, non-cost factors such as the quality of infrastructure or the perceived unpredictability of policymaking continue to pose risks to competitiveness.

Legislative unpredictability remains a concern. Government Emergency Ordinance 114/2018, adopted with no impact assessment or stakeholder consultation, introduced wide-ranging measures with a negative impact on the financial sector and investments. It was amended by three other emergency ordinances in 2019 and 2020. Although these more recent changes repealed almost entirely the most problematic provisions of the original ordinance of 2018, the quick succession of changes relating to the taxation of banks, energy and telecommunication companies and the functioning of the second pension pillar added to the perception of high legislative unpredictability.

([8]) Analyses relevant for the in-depth review can be found in the following sections: Public finances and taxation (Section 4.1); Financial sector (Section 4.2), Labour market (Section 4.3), Competitiveness, reforms and investment (Section 4.4).

3.2. EVOLUTION, PROSPECTS AND POLICY RESPONSES

The fiscal-driven current account deficit is forecast to remain on a deteriorating path. According to the Commission's 2019 Autumn Forecast, a further current account deterioration beyond 5% of GDP is expected in 2020 and 2021. At the same time, the fiscal deficit may widen to some 6% of GDP in 2021.

The net international investment position may worsen after years of improvements. GDP growth, while still robust, has slowed from its 2017 peak and is expected to decelerate further in 2020 and 2021, while the current account is forecast to continue to deteriorate. This in turn could reverse the substantial improvement in the net international investment position observed since 2012, although the small debt weight may mitigate risks. Overall, recent and prospective developments on the external side expose the economy to growing risks, especially in times of an uncertain world economy or in case of heightened risk aversion. The external financing of the economy is also a concern, with government bond yields among the highest in the region and the sovereign ratings just at investment grade.

A number of cost and non-cost factors could hurt competitiveness. Romania's export market shares continued to increase in 2018 supported by a gradual depreciation of the national currency. However, private sector wages continue to increase strongly due to a very tight labour market, repeated minimum wage increases, and possible spill-overs from strong public sector wage increases, potentially affecting the country's cost competitiveness. Non-cost factors such as the limited availability of infrastructure, the economy's low innovative capacity and a cumbersome business environment could also hamper competitiveness in the future.

The continued unpredictable policy-making weighs on investment. The uncertainty over policy and legislative decisions has contributed in recent years to the overall perception of unpredictability in the business environment. Public policymaking remained difficult to forecast. In early 2020, 25 Emergency Ordinances were adopted mostly without consultation or impact assessment. The persistent uncertainty about the future direction of reforms could negatively affect firms' investment and production decisions.

3.3. OVERALL ASSESSMENT

Romania continues to face risks in the form of an increasing current account deficit and marked cost competitiveness losses. The current account deficit has been widening since 2014, reflecting an expansionary fiscal policy stimulating domestic demand and import growth. Rapidly increasing wages have put unit labour costs under growing pressure as productivity gains, although significant, were not enough to compensate. Wage pressure translated into marked cost competitiveness losses. While export performance still holds, an economic slowdown among some of Romania's main trading partners could find the country's current account ill-prepared to accommodate a drop in exports.

Policy measures have contributed to the widening current account deficit and risks to cost competitiveness. The fiscal stance has remained highly expansionary, continuing to stimulate consumer spending. The 2020 budget might not ensure sufficient fiscal consolidation. Past decisions on public and minimum wage increases have played a major role in increasing risks to cost competitiveness. While public wages are not expected to increase significantly in 2020 and 2021, a new minimum wage increase of 7.2% was adopted for 2020. The persistence of a large discrepancy between a strong domestic demand, fuelled by an expansionary fiscal policy, and a weakening external demand resulting in a widening current account deficit, further increases the government's and the economy's external financing needs.

Risks to the financial sector have abated after end 2018 but regulatory uncertainty persists. In January 2020, the government amended the most damaging provisions of government emergency ordinance 114/2018. However, legislative uncertainty affecting the business environment, and in particular the financial sector, appears to persist and requires monitoring.

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Table 3.1: **MIP assessment matrix (*) - Romania 2020**

	Gravity of the challenge	Evolution and prospects	Policy response
	Imbalances (unsustainable trends, vulnerabilities and associated risks)		
Financial sector (see Section 4.2) **and business environment/investment** (see Section 4.4)	Legislative initiatives adopted in December 2018 by the Parliament and the government threatened to harm financial stability, international capital flows and private investment, and constrained the conduct of monetary policy. The frequent and significant legislative changes add to the overall perception of an unpredictable business environment and may affect firms' ability to make investment decisions. The banking sector remains nevertheless well capitalised. Its profitability declined somewhat from 16.3% in September 2018 to 13.2% in September 2019 but remained well above the EU average.	In 2019 and ealry 2020, risks to financial stability and investment abated as a series of legislative amendments initially modified and eventually cancelled the most damaging provisions of Government Emergency Ordinance 114/2018. The taxation of energy companies introduced by Government Emergency Ordinance 114/2018 was also revised in early 2020. Both the original and the amending regulations were adopted without an impact assessment and proper stakeholder consultation, reflecting the persistently unpredictable legislative environment.	Government Emergency Ordinance 19/2019 de-linked the tax on banks' assets from the interbank rate and replaced it with a flat-rate tax applicable to a reduced tax base. It also introduced provisions taking into account the banks' size and profitability. As regards the second pension pillar, the capital requirements that had been hiked in late 2018 were significantly reduced in May 2019, mitigating to a large extent the risk of market exit by pension fund management companies. Finally, in January 2020, the government repealed the tax on banks' assets, the possibility to opt out of the second pension pillar, the increased capital requirements for second pension pillar fund management companies and provisions on fees were revised.
External balance (see Section 4.4.1)	The current account deficit has persistently deteriorated, to an estimated 5.1% of GDP in 2019. The widening deficit has been driven mainly by a worsening trade deficit in goods, which rose from 4.3% of GDP in 2014, when the current account was close to balance, to an estimated 8.2% in 2019. The worsening of the trade balance was driven by a marked increase in imports while export market shares continued to grow. The trade balance in consumer goods shifted from a small surplus in 2014 to a deficit of 2.6% of GDP in 2018. Recent improvements of the NIIP show signs of reversal and could deteriorate further from levels that are worse than what fundamentals would suggest.	The deterioration of the external balance has taken place in a context of buoyant foreign demand and strong gains in export market shares. The trade deficit is expected to continue to widen, pushing the current account deficit to an estimated 5.3% of GDP in 2020 and 5.4% in 2021. Less favourable external conditions could lead to an even stronger than forecast worsening of the current account. The consumption-led widening of the current account deficit is not supportive of potential GDP growth. Romania's consumer spending expanded by 10% in 2017 and 7.3% in 2018. The change in the composition of imports is worrisome. Imports of consumer goods have generally been growing faster than other imports since 2016 and this pattern was confirmed in the first 10 months of 2019. The coverage of the growing current account deficit by foreign direct investment and the capital account continued to decline and relying more on portfolio investment.	The widening of the current account deficit is in large part linked to the consumption boom. A persistently expansionary fiscal policy in times of strong GDP growth has been fostering this consumption boom through successive indirect tax cuts and substantial public and minimum wage increases, which also impact wages in the private sector. The government deficit has deteriorated in recent years. It is estimated to have reached 3.6% of GDP in 2019 and is forecast to widen to 4.4% in 2020 and 6.1% in 2021, much reflecting the recent pension law. The financing cost of public debt has been steadily increasing since mid-2017 to levels well above those observed for peer countries. Romania's sovereign risk ratings are at the lower limit of the investment grade and are sensitive to the future direction of fiscal policy. The financing of the broader economy can be affected as the bank-sovereign nexus has remained significant.

(Continued on the next page)

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Table (continued)

	Gravity of the challenge	Evolution and prospects	Policy response
Competitiveness (see Section 4.4.1)	After a moderate evolution in the wake of the crisis, unit labour costs have grown markedly in recent years. In 2018, economy-wide unit labour costs grew by about 9%, one of the highest increase in the EU. As of 2019, unit labour costs are expected to decelerate to single digit figures, while remaining among the fastest growing in the EU. The marked unit-labour-cost growh has been driven entirely by wage growth, with productivity continuing to improve at significant rates. Nominal compensation per employee increased by an average of 14.4% between 2016 and 2018. As a result, the unit-labour-costs based real effective exchange rate has appreciated continuously since 2016. The impact of these cost and price competitiveness losses may be lagged and exacerbated in an environment of trade tensions and slowing external demand.	Compensation per employee increased by 8.9% in the first three quarters of 2019. The growth pace remained higher in the public sector (14%), surpassing industry (5%) and services (6.8%). The impact of increasing unit labour costs on price competitiveness has so far been limited. Export prices, however, resumed growth in 2017 and continued their progress in 2018 and 2019, while the corresponding real effective exchange rate started to appreciate in 2017. It continued appreciating in 2018, signalling risks to price competitiveness, but slowed down in 2019. In 2020 and 2021, unit labour costs are expected to decelerate visibly into single-digit figures, yet remaining clearly among the fastest growing in the EU. Non-cost factors such as deficient infrastructure, particularly in poorer regions, and a cumbersome business environment, fuelled by political and legislative uncertainty and unpredictability, leave only limited room to counteract cost-competitiveness developments.	Repeated ad-hoc public wage and minimum wage increases have driven the acceleration of wages in the overall economy. The gross minimum wage more than doubled between July 2015 and January 2020. Around 20% of people with a full-time contract were earning the minimum wage in 2018. Wages in the public sector grew by more than 75% between 2015 and 2018, significantly outpacing the private sector. However, public-sector wage increases are expected to moderate over the coming years.

Conclusions from the IDR analysis

- The current account balance continues to deteriorate on the back of fiscal-driven domestic demand that has led to a spree of consumption goods imports. Romania has continued to gain export market shares. However, cost competitiveness has been deteriorating on the back of strong wage growth well in excess of productivity. Past legislative initiatives threatened to hurt financial stability and investment, adding to the overall perception of unpredictability.

- The deterioration of the current account balance is expected to continue in the medium term, reflecting the ongoing fiscal-led private consumption boom. Strong wage growth, although decelerating, is putting further pressure on cost competitiveness. A deterioration of external conditions due to increasing trade tensions, heightened risk aversion or a slowdown in the economies of major trading partners could further trigger a significant worsening of the country's current account. The financing of the economy's increasing external borrowing needs could also become increasingly costly as suggested by the recent path for government borrowing costs. Despite recent policy action to mitigate the negative effects on the financial sector of legislative initiatives adopted in December 2018, recurrent legislative changes have continued contributing to an overall perception of unpredictability affecting the business environment.

- Policy action has contributed to the accumulation of vulnerabilities for the Romanian economy on several accounts. The expansionary fiscal policy, leading to large and widening government deficits, has repeatedly stimulated an already fast growing economy and led to the widening of the current account deficit. Increases in unit labour costs, triggered by successive public and minimum wage increases may compromise cost competitiveness. Legislative unpredictability continues to weigh on the broader business environment.

Source: European Commission

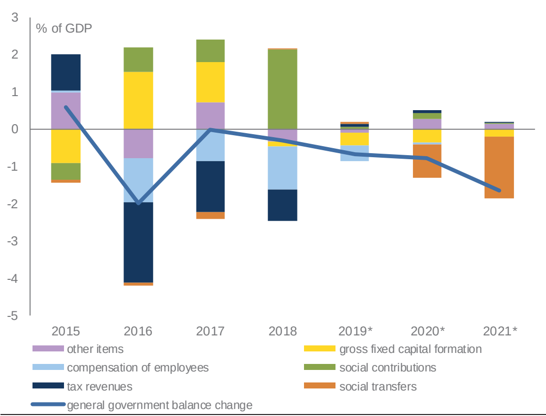
4. REFORM PRIORITIES

4.1. PUBLIC FINANCES AND TAXATION

4.1.1. FISCAL POLICY (*) (9)

The public deficit has been increasing, due to tax cuts and higher spending on public wages and old-age pensions. (Graph 4.1.1) Tax revenues dropped following cuts in consumption tax rates in 2016-2017 and a lower personal income tax rate as from 2018. On the expenditure side, public wages significantly increased since 2016. At the same time, public investment gradually fell to a post-EU accession low in 2017 and has increased only slightly since then. Therefore, the headline deficit increased from 0.6% of GDP in 2015 to 2.9% of GDP in 2018 and is projected to have risen to 3.6% of GDP in 2019. These policies boosted private consumption but may negatively affect long-term growth.

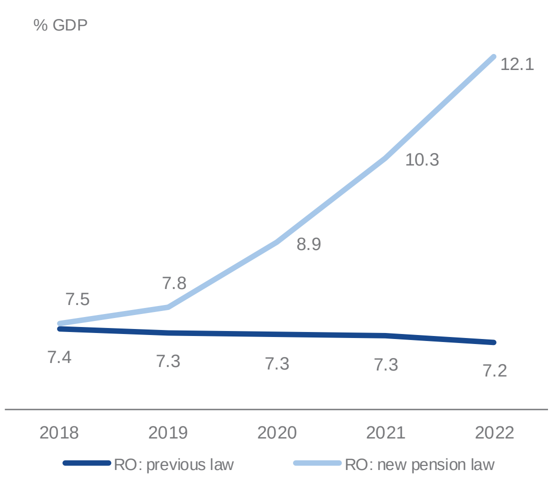
Graph 4.1.1: **Drivers of change of general government balance**



Source: Eurostat, European Commission 2019 Autumn forecast

The public deficit is projected to widen further due to significant increases to old-age pensions. Going forward, social expenditures (old-age pensions) are set to increase significantly due to a new pension law adopted in summer 2019 (see Graph 4.1.3 and Box 4.1.1). In particular, the law foresees an ad-hoc indexation of pensions by 40% in September 2020 and a further upward recalculation of pensions in 2021. The law is the main driver of the projected rapid increase of the general government deficit, to 6.1% of GDP in 2021, and of high fiscal sustainability risks (Section 4.1.2).

Graph 4.1.2: **Gross public pension expenditure in 2018-2022**



Source: European Commission (2019c)

4.1.2. DEBT SUSTAINABILITY ANALYSIS AND FISCAL RISKS (10)

Romania's sovereign risk ratings are at the lower limit of the investment grade and are sensitive to the future direction of fiscal policy. The value of the early-detection indicator of fiscal stress ('S0'), which assesses risk within one year, is below its critical threshold. Financial markets' perceptions of sovereign risk are at the lower limit of the investment grade, with a 'BBB-' or equivalent rating of the sovereign debt from the three major rating agencies. However, failure to put in place corrective fiscal measures, offsetting and/or modifying the scheduled significant pension increases, constitutes a key downside risk to Romania's ratings. In fact, on 10 December 2019, S&P Global Ratings revised its outlook on Romania from stable to negative precisely on these grounds.

The public debt is set to increase sharply, and the medium-term fiscal sustainability gap to expand, leading to high debt sustainability risks

(9) An asterisk indicates the analysis contributes to the in-depth review under the MIP (see Section 3).

(10) For an overview of fiscal sustainability assessment see European Commission (2020). See also Annex B of this Report.

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in the medium term. Due to a high structural primary deficit (which is driven by the enacted significant pension increases), and assuming no-policy change, the debt-to-GDP ratio is set on a steep upward path. It is projected to exceed 90% of GDP by 2030 (the end of the projection period). The debt path is sensitive to growth, fiscal and interest rate shocks. The structure of the government debt in terms of maturity longer than 1 year helps to mitigate vulnerabilities. However, the high share of government debt in foreign currency and the substantial debt holdings by non-residents could be aggravating factors, as could the negative net international investment position. Furthermore, the medium-term sustainability gap indicator ('S1') shows Romania would require a significant fiscal adjustment in order to achieve the debt target of 60% of GDP in 2034. This indicator nearly quadrupled with respect to last year and is now among the highest in the EU.

The high fiscal deficit and increasing ageing costs cause high fiscal sustainability risks over the long term. The relevant indicator ('S2'), points to a required fiscal adjustment of 8.8 pps of GDP in order to ensure that the public debt ratio stabilises over the long term. This value, among the highest in the EU, is driven by the initial budgetary position (a contribution of 5.1 pps of GDP) and ageing costs, in particular pensions and health care (a contribution of 3.7 pps of GDP). Both items are driven by the pension law, approved in summer 2019.

4.1.3. FISCAL FRAMEWORK

The Fiscal Responsibility Law sets national numerical fiscal rules, which should guide the budgetary process. It contains a structural deficit rule, which requires compliance with or convergence to the medium-term budgetary objective of a structural deficit not exceeding 1% of GDP ([11]). The national framework also contains several auxiliary rules on expenditure and revenue items. Furthermore, the government is required to prepare an update of the fiscal strategy - which sets out the macroeconomic assumptions, medium-term budget planning and expenditure ceilings that should guide the annual budget process - and send it to Parliament by 15 August of the preceding year.

Again, the national fiscal framework has not been respected. The fiscal rules laid down in the Fiscal Responsibility Law 'remained inoperable' with respect to the 2019 and 2020 budgetary laws, as the authorities continued its practice of derogating from them (Fiscal Council 2019a and 2019d). In particular, the 2019 budget target of a headline deficit of 2.76% of GDP was inconsistent with the structural deficit rule ([12]). Budget amendments adopted in August and November 2019 also derogated from a number of rules, in particular, in the latter case, by increasing the 2019 deficit target to 4.4% of GDP (Fiscal Council, 2019c). Moreover, as in previous years, the government did not send an update of the fiscal strategy to Parliament by the statutory August deadline, sending it in December 2019 instead. This again undermined the guiding role the fiscal strategy should have for the overall budgetary process. The 2020 budget and the fiscal strategy also derogated from several fiscal rules, in particular by targeting a headline deficit of 3.6% of GDP in 2020 (Fiscal Council, 2019d, 2019e and 2020).

4.1.4. TAXATION

The tax structure is characterised by low levels of revenues, with high reliance on consumption taxes. The tax-to-GDP ratio was 26.3% in 2018, well below the EU average of 39.2%. The tax structure is considered little detrimental to economic growth, as it largely relies on consumption taxes, while the tax burden on labour (including social contributions) is low (European Commission, 2019b). The limited use of recurrent taxes on immovable property and environmental taxes leaves scope to generate revenue in a growth-friendly manner.

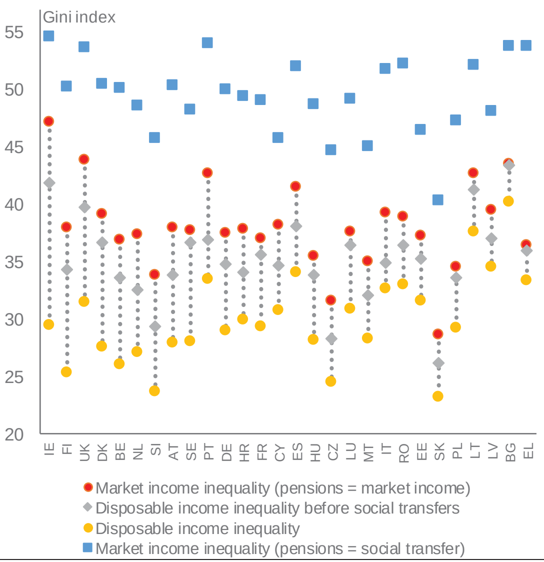
The impact of the tax system on reducing poverty and income inequality is limited.

([11]) The path of convergence is defined in agreement with the EU institutions, based on the rules of the Stability and Growth Pact.

([12]) The budget deficit target was increased after the submission of the draft 2019 budget to the parliament, in direct contradiction to the Public Finance Law (Fiscal Council 2019b). The original deficit target proposed by the government (2.55% of GDP) did not comply with the structural deficit rule neither.

Income inequality and poverty rates remain among the highest in the EU (see Section 4.3.4). The relatively low level of tax revenues limits Romania's ability to tackle these problems via either redistribution or through the provision of public goods and services (see Section 4.3). The design of labour taxation is among the least progressive in the EU, as measured by the difference between the relative tax burdens for low- and high-income earners (European Commission, 2019b). Such design contributes to the limited impact of the tax and benefit system in terms of reducing income inequality (Graph 4.1.3).

Graph 4.1.3: **Redistributive power of the tax and benefit systems in EU Member States, 2017**



(1) Income data adjusted for household size (equalisation).
(2) Income inequality measured by the Gini coefficient. The value 0 corresponds to perfect equality (same income to everybody) while 100 corresponds to maximum inequality (all income distributed to only one person and all the others have nothing.
(3) EU-SILC 2017 data are based on income generated in 2016.
Source: Commission services calculations based on Eurostat data

Environmental taxation remains at a relatively low level. Environmental taxes [13] amounted to 2.1% of GDP in 2018, below the EU average of 2.4%. Revenues from transport fuel taxes as a share of GDP are among the lowest in the EU. (European Commission, 2019b). The authorities lowered the excise duty on motor fuels from 1 January 2020. This means lower budgetary revenues and a negative impact in terms of the climate objectives. Moreover, the government dropped its plans to introduce a pollutants-dependent car registration tax in 2019.

The value added tax (VAT) gap decreased, but remains among the highest in the EU. The VAT gap is the difference between the VAT liability theoretically due and VAT actually collected. It thus represents lost revenue due to evasion, fraud, insolvencies, bankruptcies, administrative errors or legal tax optimisation. The VAT gap is estimated to have marginally dropped from 35.9% in 2016 to 35.5% in 2017 and, according to preliminary estimates, it lowered to 32% in 2018. However, it is still among the highest in the EU (CASE et al., 2019).

After repeated delays, there is a progress in the acquisition of electronic cash registers by the taxpayers. Out of an estimated total need of 750,000 cash registers for VAT purposes, approximately 580,000 taxpayers had them in place by December 2019. These registers are not yet connected to the servers of the National Agency for Fiscal Administration (NAFA). The NAFA is planning to develop the IT element of this initiative, i.e. the collection, safekeeping and archiving of the data, to be followed by risk analysis.

As of February 1st, 2020, the split VAT mechanism will no longer apply. A split VAT mechanism implies that the taxpayer has a separate, special bank account for cashing in and paying out the VAT. Taxpayers making payments to suppliers using the mechanism are obliged to pay the VAT into the supplier's special VAT account. The VAT split payment mechanism introduced by Romania in 2018 (mandatory for insolvent or VAT indebted companies) resulted in disproportionate burdens on taxpayers and did not prove efficient in fighting fraud. Starting in 2020, the provisions of the Government Ordinance 23/2017 regarding the split VAT mechanism were repealed, however this needs to be maintained by Parliament.

Undeclared work remains high. According to the Romania Fiscal Council, the value of the non-observed economy is 21.5% of GDP. The sectors

([13]) Taxes on energy products (including CO2 taxes), transport (excluding fuel, which is covered by the taxes on energy) and taxes on pollution and resources. See European Commission, 2019.

of high risk are mainly construction, services, and textile manufacturing. According to the NAFA, the compliance seems to have increased in the construction sector following recent tax exemptions (concerning social security contributions and personal income tax) for those working in the sector. However, there is no clear data available.

Coordination between the labour inspectorates and the tax authorities is improving. The two institutions sometimes carry joint inspections and have coordinated their risk analysis to a certain extent. In 2019, the two institutions stepped up the number of inspections at various private agencies for labour force/employment placement abroad. NAFA is still in the process of developing specific indicators for use in the risk analysis, including for under-declared earnings. In addition, the Labour Inspection remains relatively under-staffed, with shrinking number of labour inspectors.

The tax administration continues its internal reorganisation. NAFA intends to redistribute its human resources to reinforce the Large Taxpayers Office and the local tax administration in Bucharest-Ilfov. It also decided to centralise the risk assessment by creating a single directorate under the direct coordination of its president. The National Centre for Financial Information ([14]) is preparing the implement of several IT projects and the introduce SAFT-T files (audit files for tax conforming to OECD standards).

A tax amnesty was implemented in summer 2019. Romania does not have a voluntary compliance mechanism giving incentives for reporting and payment of overdue tax obligations. Instead, the authorities tend to enact ad hoc tax amnesties. The tax amnesty enacted in summer 2019 ([15]) had two components: tax restructuring and the cancellation of ancillary due amounts (fines and interest). By the beginning of December 2019, approximately 50,000 taxpayers had applied for the tax amnesty, most of them for the cancellation of ancillary obligations. The Fiscal Council (2019c) criticised the measure for the moral hazard it generated, amplified by the fact that only taxpayers who have accumulated a considerable volume of outstanding debt were eligible. In addition, the frequency of tax amnesties raises the problem of optimizing tax obligations over a longer period.

The authorities are planning to simplify procedures and reporting obligations to facilitate tax compliance. NAFA intends to introduce some pre-filling for the personal income tax annual declaration as of 2020, with the help of the Private Virtual Space. The authorities are also working on reducing the number of tax returns due from legal persons. Moreover, the authorities are analysing the possibility of extending the scope of electronic filling and submitting of tax returns.

([14]) This Centre was established at the end of 2017 as coordinator of the IT activities in the Ministry of Public Finance, the National Agency for Fiscal Administration, the National Agency for Public Procurement and the National Prognosis Commission.

([15]) Ordinance no. 6/2019.

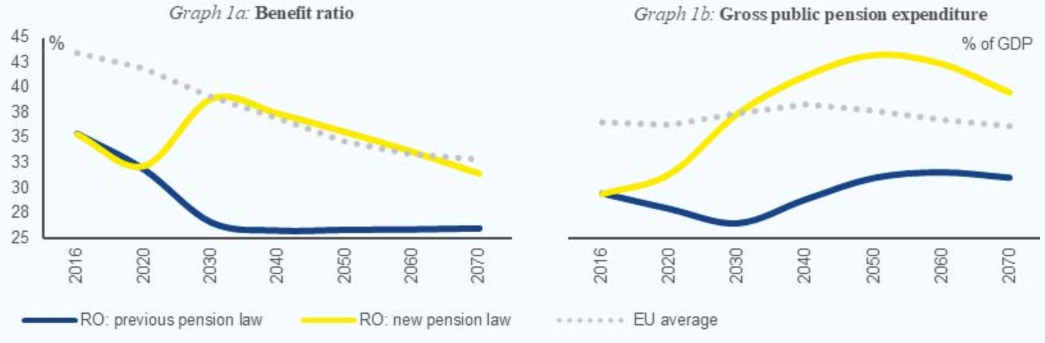
Box 4.1.1: **New pension law: pension adequacy and budgetary sustainability**

The pension system in Romania faces challenges connected to low average duration of working lives and to the aging of the population. Romania has one of the shortest average durations of working lives in the EU (33.5 years compared to the EU average of 36.2) and one of the lowest employment rates for older workers. This negatively affects the contributory period and thus the level of pensions. Moreover, projected aging of the population (see Section 1) poses a challenge to pension adequacy and sustainability in the future. The economic old-age dependency ratio, i.e. inactive population aged 65+ as a share of the employed population aged 15-64, is projected to double, from 39.1% in 2016 to 81.5% in 2070.

A new pension law, enacted in summer 2019, significantly changed several parameters of the public pension scheme. The pension system in Romania consists of three pillars. The first pillar is a mandatory, pay-as-you-go public point system. The second pillar is a partially mandatory, defined contribution scheme with a guarantee plan, based on individual accounts, while the third pillar is a voluntary, defined contribution scheme based on individual accounts. A new pension law, enacted in summer 2019, contains the following main changes to the first pension pillar: (i) ad hoc indexation of pensions until 2021: by 15% from September 2019 (already included in the 2019 budget law), 40% from September 2020 and 6% from September 2021; (ii) from 2022 onwards, the indexation of the pensions will be 100% of the inflation rate plus 50% of the real average gross wage growth; (iii) starting in 2021, the correction index which used to lift the first pension in line with wages will be abolished; (iv) new pensions will be calculated using at the denominator a fixed contributory period of 25 years, instead of 35 (M) / 31.9 in 2022, going up to 35 as from 2030 (F) years under the previous law; (v) existing pensions will be recalculated upwards to match this new formula. The law also contains some changes to the minimum pension, disability and survivor benefits, while pension, taxation as well as some provisions on pillar II, have also been modified in 2017 and 2018.

The new pension law improves pension adequacy, however it has significant budgetary costs in a very short period and causes high fiscal sustainability risks. A third of elderly in Romania were at risk of poverty and social exclusion in 2018, similar rate to the rest of Romanian population but much higher than the EU average (Section 4.3.4). Old-age pensions have been growing below the significant growth of wages of the last years. There are large pension adequacy gaps between different groups of pensioners. The benefit ratio (average public pension as a share of the average wage) amounted to 35.5% in 2016, much lower than the EU average of 43.5%. It is projected to decrease to 31% in 2070 under the new law (European Commission, 2019c), instead of a much lager fall to 26% in 2070 under the previous law. The benefit ratio for the EU as a whole is set to fall to 32.9% over the same period (European Commission, 2018b). Due to its implementation schedule, the law is set to significantly increase public spending on pensions in a short period. It is the main driver of the projected rapid increase of the general government deficit and of high fiscal sustainability risks (Section 4.1.2). Moreover, the law is not accompanied by measures aimed at increasing labour participation and duration of working lives beyond the statutory minimum, which are key to improve both pension adequacy and the sustainability of the pension system.

Graph 1a: **Benefit ratio** *Graph 1b:* **Gross public pension expenditure**



Source: European Commission (2018b and 2019c).

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4.2. FINANCIAL SECTOR

4.2.1. BANKING AND INSURANCE DEVELOPMENTS (*)

Despite several headwinds and some signs of asset quality deterioration, the banking sector has remained resilient. The highly criticised bank tax on total assets was recently abolished. Total banking sector capitalisation (19% at the end of June 2019) has been relatively stable for several years and above the EU average. The common equity Tier 1 (CET1) ratio rose to 17.1% in the first half of 2019, up from 18.4% at the same date last year. Even though non-performing loans (NPLs) declined, for unsecured consumer credit in local currency, the system-wide NPL ratio fell further, reaching 5% at the end of June 2019. The stock of legacy impaired assets decreased, albeit at slower pace than in previous years, mainly due to the decline in NPL sales. At the same time, the flow of new NPLs slightly increased.

Financial intermediation remains significantly below pre-crisis levels, hampered by a weak corporate sector and various legislative developments. Financial intermediation (measured as the ratio of total private sector credit to GDP) was 25.6% of GDP in 2018, some 11 pps below the 2009 level and roughly three times below the EU average. The main factors behind this low level are several legislative headwinds credit institutions have faced since 2016 and the financial situation of companies (very low or even negative capitalisation) and loose financial discipline, that has constrained their access to credit. Furthermore, the focus on retail lending in the business models of banks, the limited number of bank employees specialising in corporate lending and the low level of financial literacy in Romania have also contributed to the low and declining trend in financial intermediation since 2011.

The banking sector's exposure to the real estate market and government debt is still significant. Supported by the increase in disposable income and government measures, mortgage credit has expanded significantly in the post-crisis period, while consumer lending as a percentage of total lending to households has declined. At the end of March 2019, almost 70% of all loans to households constituted exposure to residential real estate. The mortgage loans granted under the government sponsored First Home (Prima Casa) programme continued to be significant, representing one third of the new housing loans in Q1 2019. However, the intended gradual reduction in the total guaranteed amounts coupled with a lower maximum level of indebtedness eligible in the new programme are expected to create a downward trend in new mortgages granted under this programme. Meanwhile, the attractiveness of mortgage products offered by banks outside the First Home programme is likely to increase. With government bond holdings of almost 18% of total banking sector assets in H1 2019 and a pronounced home bias, the government-bank nexus continues to remain strong. Given the current situation of public finances, (see Section 4.1) the banking sector is exposed to potential negative spill-overs stemming from increases in sovereign spreads and interest rates.

Some of the measures applicable to loans to households adopted in early 2019 would have benefitted from an impact assessment. Government Emergency Ordinance 19/2019 introduced the Consumer Credit Reference Index (IRCC), a new benchmark interest rate applicable to new and refinanced mortgage loans (including Prima Casa mortgages) and consumer loans, with variable interest rates. The IRCC is calculated as the arithmetic average of the daily interest rates on effective interbank transactions and is updated quarterly and applied by banks for the next quarter. While the IRCC was introduced with the aim of lowering the cost of credit for households, no proper impact assessment was done to ensure that its calibration and application do not raise concerns regarding an unwarranted adverse impact on the transmission mechanism and conduct of monetary policy ([16]).

The Parliament introduced several legislative initiatives, which could have negative impact on the banking sector. Four draft legislative proposals, which build on laws declared unconstitutional in early 2019, were submitted to the Senate in September 2019. The first draft proposal aims to protect consumers against excessive interest rate levels by capping interest rates for household loans (including mortgages). The second proposal intends to shield borrowers

([16]) Further details on the IRCC are included in the ECB opinion on the tax on banks' financial assets and the interest rate benchmark for consumer credit agreements https://www.ecb.europa.eu/ecb/legal/pdf/en_con_2019_18_f_sign.pdf from speculative debt-assignment agreements (i.e. sales of bank loans) by declaring the borrower debt-free in the event that the outstanding loan is transferred to a third party. A third proposal concerns the protection of borrowers against abusive or hasty foreclosures. The fourth proposal protects consumers against the foreign exchange risk embedded in credit contracts. Since the first three draft laws would also apply retroactively to outstanding loans, they are likely to induce moral hazard and weaken payment discipline in the banking sector.

The proposed amendments to the Statute of the Consumer Protection Authority may increase its competences in the banking sector. A draft legislative proposal already initiated in 2016 appeared to gather new momentum in Parliament in late 2019. It would give the National Consumer Protection Authority (ANPC) the right to supervise the financial and banking sector, by approving and endorsing financial products, to set fees for new financial products proposed by both financial and non-financial institutions, and to impose fines ranging from 0.5% to 10% of revenues at consolidated level (European Commission, 2017b). While enhancing consumer protection is important, some intended amendments to the ANPC Statute might interfere with the mandate of the Romanian Central Bank in the area of banking supervision, particularly in relation to the withdrawal of bank licences.

After several years of more benign developments, strain in the insurance sector is re-emerging. Insurance activity in Romania expanded further in 2018, as gross written premiums increased by roughly 4.5% compared to 2017. Insurance penetration (calculated as the share of gross written premiums in a country's GDP) has remained subdued and well below EU peers. While life insurance is underdeveloped, albeit increasing, the insurance sector is still highly dependent on non-life insurance (in particular compulsory car insurance), which generated 79% of the gross written premiums in 2018. Concentration in the compulsory car insurance business has increased, with two players underwriting the bulk of insurance premiums. The insurance sector has a combined ratio (calculated as losses and expenditures to earned premiums) for all business lines, which increased to 110% at the end of June 2019, while it stood at roughly 103% in 2018 and 98% in 2017. The combined ratio reached 122% for compulsory car at the end of June 2019, due to the increase in distribution costs, the higher costs charged by auto services companies and more accidents and casualties.

4.2.2. PENSIONS - SECOND PENSION PILLAR

The headwinds faced by the second pillar pension funds have subsided, but pockets of vulnerability remain. In January 2020, the government abolished several provisions targeting the second pillar pension funds, which were introduced by the former government in December 2018 and May 2019. The minimum capital requirements for pension fund management companies were restored to the level before the adoption of the Government Emergency Ordinance 114/2018. The provision whereby participants in the second pillar could switch to the Pay-As-You-Go pillar, after five years of contributing to the second pillar, was removed. The administration fees levied on gross contributions by the pension fund management companies, which were significantly cut in December 2018, were further modified in early 2020, but without prior in-depth analysis consulted with all relevant stakeholders.

The reduction in administration fees has had a negative impact on the results of pension funds management companies. Due to lower administration fees the revenues of pension funds management companies declined significantly in the first ten months of 2019. Thus, after seven successive profitable years, the sector registered an aggregate negative result as of October 2019. Since the industry is in its early years in Romania, detecting any unwarranted adverse effects on the performance and prudential situation of these pension fund management companies from the reduction in administration fees could be useful to allow for potential further fine-tuning and a sustainable second pillar for retirement.

4.2.3. CAPITAL MARKETS AND ACCESS TO FINANCE

Non-bank financing in Romania has continued to lag significantly behind bank credit to firms. Bank loans are the most important external financing source for firms in Romania, amounting

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to about 11.7% of GDP in 2018 (EU average of about 34% of GDP). Market based financing was with 6.2% of GDP also significantly below the EU average of 49.7% of GDP in 2018([17]). According to surveys by the National Bank of Romania, companies resort primarily to internal financing sources for their operational activity and investment projects. Firms' recourse to bank loans is relatively low, the main sources of external financing being overdrafts and credit lines. Companies using external financing face higher financing costs and loan application rejection rates, in particular due to low financial soundness ([18]) (NBR, 2019b). The microfinance sector has become the fifth most active microfinance sector in the EU, having good growth potential (OECD, 2018a).

Access to risk capital for innovative start-ups and scale-ups remains limited. Romanian firms operating in high tech knowledge-intensive services and manufacturing tend to be more finance constrained than firms active in less knowledge intensive sectors are (EIB, 2019a). This could be due to a lack of appropriate supply and financing instruments adapted to the needs of innovative start-ups and scale-ups. Romania was among the most attractive destinations in Central and Eastern Europe for private equity and venture capital funds (Invest Europe, 2018a) and venture capital investments have increased over the last four years. However, the size of the market and volumes are still relatively low and concentrated in few sectors, primarily in the Bucharest and Vest regions (Flachenecker et al., forthcoming). Efforts to support business creation with various financing options are initiated by national authorities, but lack a targeted approach and funds (OECD 2018b).

Various initiatives could support capital market development. With the support of the Financial Supervisory Commission (ASF), the process of setting up a central counterparty clearinghouse (CCP) in Romania has progressed further, which could contribute to the increase in derivative trading once operational in 2020. The ASF also aims to prepare a capital market strategy with the support of the Commission's Structural Reform Support Programme and is counting on the pro-active involvement of the government to ensure its success. After Romania's upgrade to Secondary Emerging market status by Financial Times Stock Exchange (FTSE) Russell and the inclusion in the CEEplus Index[19], these initiatives could further help boost the Romanian capital market and companies' access to non-bank financing. This should be complemented by several initiatives and a national strategy for financial literacy following a memorandum signed in 2018.

([17]) In this context, market based financing is calculated as ratio between the outstanding amounts of listed shares issued by non-financial corporations in Romania and GDP.

([18]) Romania has the second highest share of companies with negative equity in EU (EIB 2019)

([19]) The CEEplus Index, published since 4 September 2019, is calculated based on the value of the portfolio of the largest and liquid companies listed on stock exchanges from the central and eastern Europe region (Croatia, Czech Republic, Poland, Romania, Slovakia, Slovenia and Hungary).

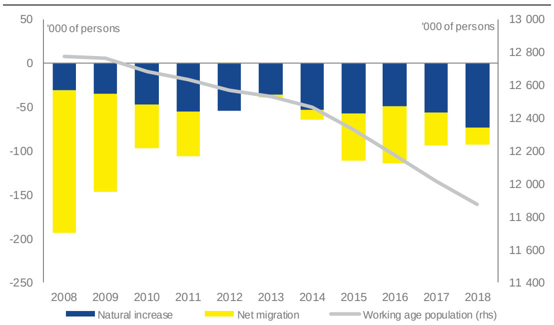
4.3. LABOUR MARKET, EDUCATION AND SOCIAL POLICIES

4.3.1. LABOUR MARKET

Positive labour market developments in Romania continue on the back of sustained economic growth but labour shortages persist. The labour market dynamics remain positive, with the employment at a record level of 70.8% in Q3-2019 ([20]), and the unemployment rate falling to 3.9%. However, differences in labour market outcomes remain between regions and population groups. On the back of the positive economic developments, labour market conditions remain tight, with labour and skills shortages. These are exacerbated by the decline in the labour force ([21]).

Demographic change and migration have a strong impact on labour market dynamics. The population continues to decrease due to a negative natural rate of population growth and outward migration. In 2018 Romanians were the largest group of EU citizens of working age (20-64) residing in other Member State (2,524,000 persons) ([22]). The emigration of working age Romanians increased by 7% compared to 2017, calling for continuous efforts to upskill and re-skill the labour force remaining in the country.

Graph 4.3.1: **Demographic growth and working age population**



Source: European Commission

Despite a slight improvement, inactivity remains high, with significant differences between age groups and across regions. The inactivity rate amounts to 31.6% (Q3 2019) of the overall population. Persistent high levels of inactivity are registered for women, young people aged 15-24 (71.17%), older people aged 55-64 (50.8%) and women aged 15-64 (41.7%) in Q3 2019. The inactivity gap between low- and high skilled youth remains high (43.3 pps). In the age group 20-64, family and caring responsibilities are often the main reasons for not seeking employment (23.6% of the inactive population). There are also regional disparities in inactivity rates (2018) between Centru (38.4%), Sud-Est (36.9%), and Vest (38%), compared to Nord-Est (26.3%) and the capital region (26%).

Active labour market policies, mainly employment subsidies, have little impact on reducing inactivity. In 2019, the number of apprenticeship contracts taken-up increased to more than 6,150 from around 430 contracts in 2017, as subsidies to employers were doubled in 2018 (from RON 1,125 to RON 2,250). In addition, subsidies for employing people from disadvantaged groups also increased. However, the share of employed persons in the total of participants in active measures was only around 40%, 6 months after participating in the measure. There remains significant scope to improve the effectiveness of activation measures, in particular for providing tailor-made services to vulnerable groups, such as low-skilled, old workers and persons with disabilities. While the employment rate for people with disabilities is below the EU average, 43.7% vs 50.6%, the legal framework does not effectively incentivise their employability and public employment support services are limited. Necessary reforms in the case management approach and relations with employers continue to stall, despite the European Social Fund funding (ESF) available.

Access to the labour market remains limited for certain groups. In 2018, the share of long-term unemployment within total unemployment increased to 44.1%, after declining from 50% in 2016 to 41.4% in 2017. Around 100,000 long-term unemployed are currently registered with the public employment services. Eighty eight per cent of them come from rural areas, around 9% are Roma and more than 90% are identified as having a low level of employability. Skills mismatches and lack of basic skills are obstacles to tackling these issues. Public employment services are not effectively tailored to individual needs and lack

([20]) Since 2017, there has been a general pick-up in employment, which is expected to continue in 2019 and 2020.
([21]) Since 2014, the population aged 20-64 has decreased by 5%.
([22]) EU citizens living in another Member State- statistical overview, Eurostat (2019).

integration with social services, despite substantial funding being available.

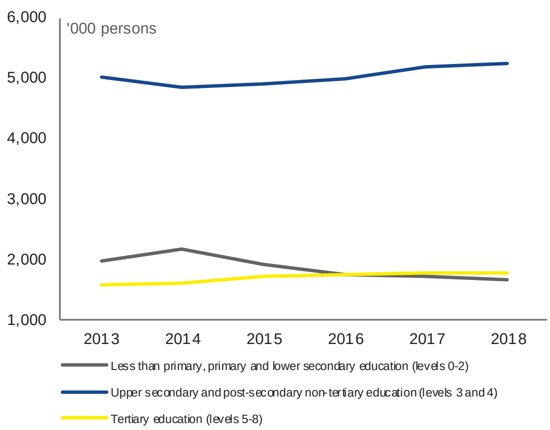
The percentage of young people neither in education nor in employment and training is among the highest in the EU. In 2018, 14.5% of young people (15-29 years) were neither in education nor in employment and training (NEET), compared to the EU average of 14.5%. More than a third of them were discouraged workers, short- and long-term unemployed ([23]). Despite the positive outcomes of some outreach measures, around 69% of NEETs remain inactive. In addition, a very high and increasing share of young people leave the country.

The gender gap in activity and employment remains high. At 19 pps in Q3 2019, the gender gap in activity increased further to above the EU average (10.7 pps). In 2018, the share of active women (15-64 years) was 58.7% (EU average 68.7%), compared to 7.9% for men (EU average 79.4%). The lowest activity rates were recorded among younger (aged 15-24) and older women (aged 55-64). Approximately 12% of women were inactive due to personal and family responsibilities. In 2018, the gender employment gap of people having one child below the age of six was as high as 29 pps. High early school leaving rates and insufficient childcare facilities and services negatively affect female labour market participation especially in rural areas (see Section 4.3.2).

In a context of increasing demand for labour and falling unemployment, labour shortages persist in some sectors. In the first three quarters of 2019, companies in the services sector (9.8%), construction (25.1%) and industry (13.7%) reported labour shortages as a factor hindering production (European Commission, 2019f), an increase compared to 2018. Future labour demand is expected to shift with a need for particular skills in some sectors and occupations (Cedefop, 2019). In 2018, job vacancies were reported mostly in the manufacturing sector (27%), followed by health and social work activities (11%), and public administration (13%) ([24]). By 2030, an increase in the demand for labour is expected for professional services, sales workers and associate professionals, while the demand for trade and agriculture workers is expected to decrease.

The skills mismatch has persisted over the recent years. The European Skills Index measuring the performance of EU skills systems shows that Romania is among the worst performers, especially in skills development and activation (Cedefop, 2019). In addition, the occurrence of vertical mismatches (over-qualification rate), while still below the EU average, almost doubled over the last decade. Thus, in 2018, 18% of workers with tertiary qualifications were employed in occupations that did not require that level of qualification while 28% of the employed people aged 25-34 with tertiary education were occupying a job that required tertiary education but their education or skills did not match the requirements of the job (Eurostat, Mismatch indicators). It points to a widening gap between education and work. Technological changes are expected to generate a shift in demand towards higher skills and qualifications, which might not be fully met by current labour supply, given the time necessary for the education and training system to adjust.

Graph 4.3.2: **Developments in hiring**



Source: European Commission, Labour Force Survey

The need for upskilling is high. In 2018, nearly 2.3 million people (21.5% of adults) only had low educational attainment**.** In 2018, only 0.9% of adults aged 25-64 had a recent learning experience (EU average 11.1%). This is particularly concerning given the low number of available jobs

([23]) Equally the same share of NEETs were in the category due to family responsibilities, illness or disability, and the rest reported other undeclared reasons.
([24]) INSSE, Average annual number of job vacancies 2017

requiring only a basic level of education. Recent attempts have been made to address the issue of upskilling and re-skilling. A new regulation for quality assurance in adult learning is also under development.

Wages in Romania continued to grow rapidly. In 2018, the nominal compensation per employee increased by 16.3%, also due to the rapid increases in public sector wages and rises in the minimum wage. In Q1-2019, wages still posted double-digit growth. Compensation per employee is expected to continue growing although at a gradually slower pace (13% in 2019 and 9% in 2020), following the expected slowdown in public wages. Real wages grew faster than productivity, increasing the share of national income that went to labour, as was also the case in a number of other Eastern European Member States with comparatively low labour shares in the past ([25]), contributing to further wages convergence in the EU.

There is still no objective mechanism to determine the minimum wage in Romania. The minimum wage increased from RON 975 (€210) to RON 2,080 (€442) between 2015 and 2019 and was raised further to RON 2,230 (€496) in January 2020. According to the authorities, this latest increase was based on a formula taking into account several economic indicators, such as the inflation rate and labour productivity. The decision was preceded by discussions with the trade unions and employers' organizations. However, an objective mechanism to determine the minimum wage is not yet in place. While being among the lowest in the EU, the gross minimum wage in Romania currently amounts to 43% of the average wage and 58% of the median wage. Approximately 20% of people under a full time contract receive the minimum wage, resulting in a highly compressed wage distribution. This indicates a high incidence of envelope wages that come as a complement (see Section 4.1).

Social partners are not sufficiently engaged in reforms addressing labour market challenges and other relevant policy issues. The established institutional framework for social partners' consultation is not adequately used to feed into the decision-making process. The limited capacity building of social partners and ineffective dialogue remain a concern. Social partners still do not enter into voluntary dialogue in order to address labour market challenges and their involvement and contribution in policymaking remains limited. The government plans to review the role of social dialogue committees in order to improve the involvement of social partners.

Discussions on changes to the social dialogue law and the revision of economic sectors have stalled. The draft changes to the law have been in parliamentary procedure since June 2018. In April 2018, the International Labour Organisation gave recommendations on the legislative project but the follow-up is uncertain. The delineation of sectors still does not allow for sufficient representation of workers or employers in most sectors, and there are no immediate plans for improvement ([26]). The authorities report higher rates of collective bargaining coverage 45%, which may be linked to collective bargaining becoming temporarily mandatory for all employers, following the shift in social security contributions from employers to employees at the end of 2017.

4.3.2. EDUCATION AND SKILLS

Underfunding and delayed reforms continue to hamper the equity, inclusiveness and quality of education. Spending on education remains one of the lowest in the EU (2.8% of GDP vs 4.6% EU average), particularly at pre-primary and primary level, which account for just 21.8% of the budget (EU average 32%). Persistent problems with the acquisition of basic skills at school ([27]) and the low digital literacy of the population ([28]) pose challenges for the labour market integration of future graduates. The enrolment rates at all

([25]) Compared to 2018 the nominal change in the monthly rate in Bulgaria (9.81%) and Croatia (9.48%), for instance, is similar to the change in Romania (9.36%). Romania together with Bulgaria and Lithuania, saw their minimum wages more than double in real terms since 2010 (Eurofund, 2019)

([26]) Both partners are present in only 6 out of 30 sectors. According to the government, a project for the revision of sectors has been prepared since 2018, in consultation with social partners, however the latter requested to wait until the social dialogue law was changed.

([27]) Romania ranks among the last countries in the EU in the 2018 PISA survey in terms of mean performance in mathematics, science and reading (OECD, 2019a)

([28]) Only 10.1% of the adult population has above basic digital skills, the lowest share in the EU (European Commission, 2019g) education levels remain significantly below the EU average. Despite recent improvement, early school leaving is still very high, with negative effects for labour market participation, poverty and social inclusion. Ideas for important reforms of the educational system have been put forward by both the Ministry of Education and the Presidential Administration but have not yet been pursued.

Delays in the rationalisation and modernisation of the school infrastructure may affect the quality of education. The school-age population is projected to fall by 10% by 2030. Between 2000 and 2016, Romania closed 25% of its schools and 17% of the satellite schools (World Bank, 2018). Yet, 58% of schools still have a surplus of building space, while 22% of students study in overcrowded schools, mostly in urban areas (MEN, 2018). In addition, equity challenges are not effectively addressed, with long walking distances to schools and kindergartens in rural areas and commuting costs posing barriers to access. A strategy for rationalising the school infrastructure was developed by the Ministry of Education but not yet adopted.

Low participation in early childhood education and care widens inequality of opportunities between pupils. Only 15.7% of children below the age of three are in formal childcare. For children aged between four and the compulsory school age participation increased to 89.6% in 2017, but remains below the EU average (95.4%). This rate is even lower for children in rural areas ([29]) and Roma ([30]). This has a detrimental effect on the acquisition of basic skills and on the social mobility of children from disadvantaged backgrounds or marginalised communities. The coverage of the kindergarten network improved but rural-urban disparities persist. Some steps are being taken to increase access and quality of services, including with EU structural funds support.

Despite recent improvements, early school leaving remains very high, deepening existing socio-economic disparities. The rate of early school leavers from education and training stood at 16.4% in 2018, almost 6 pps above the EU average. This rate is particularly high in rural areas (around 25%) ([31]), for Roma ([32]) and children with disabilities ([33]). Regional disparities persist, with the highest rates of early leavers being recorded in the South-East and North-East regions, which also face the highest poverty levels. The high rate of early leavers from education and training in some regions correlates with low degrees of urbanisation (e.g. North-East). Romania also has the highest rate of early school leavers for girls in the EU (16.1% vs. 8.9% EU average), posing challenges in terms of the likely future persistence of the already high employment gender gap. Comprehensive measures targeting early school leaving through tailor-made support for vulnerable pupils are not yet in place. Such measures would contribute to progressing toward SDGs 4, 5 and 10.

The education system continues to face significant challenges in terms of quality and inclusiveness. Romania is one of the countries with the highest share of low achievers among 15-year olds in all three areas tested under the OECD Programme for International Student Assessment (PISA) ([34]), and results have worsened since 2015. The mean score of pupils in all three domains is over 60 points below the EU average, the equivalent of one-and-a-half years of schooling. Persistent lower attainment levels are reported in rural and economically deprived areas ([35]), including those with a high Roma population. In general, poorer students are more likely to receive a lower quality education (World Bank, 2018). Similarly, only 4% of new university entrants have parents with low educational attainment (European Commission, 2018c). In 2016, the Ministry of Education issued a document banning school

([29]) Gross enrolment rates in kindergarten (age 3-6) was 85% in rural areas compared to 97.4% in urban areas (National Institute for Statistics).

([30]) Only 37% of Roma children are enrolled in preschool education (European Commission, 2019h)

([31]) The rate is 15% in towns and 4.2% in cities (European Commission, 2019i)

([32]) According to 2016 data, 53% of Roma had completed primary education only (FRA, 2016)

([33]) The early school-leaving rate for persons with disabilities is 41.4%, among the highest in the EU and more than double the EU average (19.6%) whereas the tertiary attainment rate (22.6%) is significantly below the EU average (32.4%)

([34]) 46.6% of 15-year-olds are underachievers in mathematics (EU average: 22.4%), 43.9% in science (EU average: 21.6%) and 40.8% in reading (EU average: 21.7%)

([35]) The difference in mean score in reading between pupils in urban schools and those in rural area schools is of 110 points, the equivalent of almost three years of schooling (OECD, 2019a) segregation, but adopted the methodology only in 2020, and the implementation of planned actions has been delayed. Such measures, if implemented, would contribute to progressing toward SDG 10.

The low labour market relevance of vocational education and training negatively affects graduates' job prospects. In 2018, the employment rate of vocational education and training (VET) graduates increased slightly to 69 % from 67.2% in 2017, but remains well below the EU average (79.5%). Students enrolled in VET programmes had limited exposure to work-based learning, with only 10% enrolled in dual programmes. The VET system also suffers from poor attainment, with 11% of pupils enrolled in professional schools in 2017-2018 not being promoted to the next school year (INS, 2019). Romania does not perform well in skills activation (a measure of the transition from education to work) and skills development (a measure of the investment in education and training) (Cedefop, 2018). Some efforts are being made to increase the relevance of VET education but a comprehensive reform is missing.

Participation in higher education is low and remains insufficiently aligned to labour market needs. Enrolment in university has been decreasing ([36]) and in 2018 tertiary attainment for the 30-34 age group declined further to 24.6% (EU average: 40.7%), with women having the lowest participation rate in the EU (28.1% vs 45.8%). Regional disparities are also high, with a tertiary attainment level of 38% in the capital region and between 13% and 15% in the other regions. For degrees in science, technology, engineering and mathematics (STEM), the number of graduates remains particularly low, leading to skills shortages in the labour market. While 89% of tertiary education graduates find employment, many are hired outside their area of specialisation (UEFISCDI, 2015). A national comprehensive skill forecasting mechanism, per sector and qualifications, is not yet in place.

Acquisition of digital skills remains limited. The percentage of young people aged 16-19 who assess their digital skills as low is among the highest in the EU (39% compared to the EU average of 15% in 2019). Existing curricula, programmes and infrastructure do not sufficiently reflect the need to increase the pupils'' digital skills. The number of highly digitally equipped and connected schools in Romania is significantly below the EU average. As part of the E-Education 2023 strategy, Romania launched two major projects, 'The computer system of Management of schooling' and 'The National Education Platform' that should contribute to the digitisation of education in over 4,500 schools.

Teacher shortages, particularly in rural areas, together with limited continuing professional development (CPD) opportunities, restrict the quality and inclusiveness of education. Teacher shortages persist, with a visible impact on educational outcomes. It remains necessary to redesign initial teacher education and strengthen CPD opportunities. Initial teacher education offers very little preparation and practical training, particularly in modern teaching techniques or inclusive pedagogy (OECD, 2017). Teachers reported high development needs in Information and Communications Technology (ICT) teaching skills (21.2%), individualised learning (21.5%) and in teaching students with special needs (35.1%). 70% of teachers report that participation in CPD is hindered by high costs (OECD, 2019b).

4.3.3. HEALTH AND LONG-TERM CARE

The health status of the Romanian population is improving, but remains below the EU average. Romania had one of the lowest life expectancies at birth in the EU in 2017. Ischaemic heart disease remains the main cause of death, although cancer mortality is on the rise. The preventable mortality rate ([37]) and the treatable mortality rate ([38]) are among the highest in the EU. Moreover, shortages for certain essential medicines are regularly reported, while access to novel medicines is limited.

([36]) The enrolment rate in the school year 2014/2015 was 11.6% of the 18-34 year olds, whereas it was 20.4% in 2008/2009 (European Commission, 2018).

([37]) A mortality is considered preventable if death below the age of 75 could have been avoided by public health interventions focusing on wider determinants of public health, such as behaviour and lifestyle factors, socioeconomic status and environmental factors.

([38]) A mortality is considered as treatable if death below the age of 75 could have been avoided through optimal quality healthcare.

Spending on healthcare in Romania remains very low. About 5.2% of Romania's GDP was spent on healthcare in 2017, compared to 9.8% in the EU. This is despite the fact that spending on healthcare as a share of total public spending has consistently increased in previous years. Provision of key diagnostic and therapeutic equipment such as medical scanners and radiotherapy facilities are among the lowest in the EU. This hints at the potential for tangible improvements through targeted investments, also fostering more efficient spending through faster diagnosis.

Preventive care is underfunded and its availability limited. Spending on preventive care is considerably below the EU average (1.8% ([39]) v. 3.1%). Romania faces challenges in preventing some infectious diseases, with the highest rate of tuberculosis cases in the EU (OECD, 2019b). Vaccination rates are dropping, particularly affecting children. In addition, health promotion measures may have a role to play in curbing the observed obesity rate, which has increased in particular among children in recent years (OECD 2019b). Such measures would contribute to progressing toward SDGs 2 and 3.

Romania faces considerable challenges in ensuring access to healthcare. Overall, about 11% of the population remains uninsured and has only access to a restricted basket of services. The percentage of population covered by a form of health insurance has been decreasing ([40]), with a significant urban-rural gap ([41]). A large share of self-employed workers in agriculture and of the rural Roma population is not covered by health insurance. Plans to expand primary care services under this restricted basked by 2023 are underway.

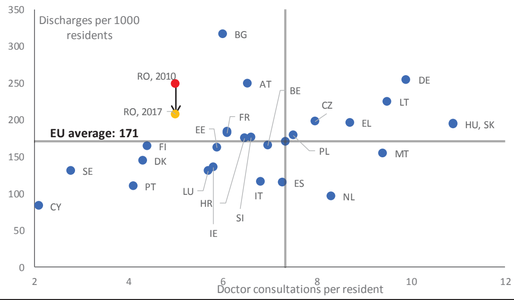
Unmet medical needs are high and increasing. Significant disparities in terms of reported unmet medical needs persist between the lowest (8%) and highest (2.3%) income groups. In 2017, Romania has the one of the highest levels of unmet medical needs for children in the EU. The level of unmet medical needs for retired people is twice as high as for the general population. In 2018, the country was among the worst performing in the EU in terms of affordability of healthcare and waiting times. Whereas most health spending is publicly financed (79%), the share of out-of-pocket expenditure represents a substantial cost for individual households. Most out-of-pocket spending is on pharmaceuticals. Furthermore, informal payments add to this financial burden.

Territorial imbalances in the provision of healthcare services are large and expanding. Reported unmet needs as a result of travelling distance are among the highest in the EU, reflecting an uneven distribution of healthcare facilities and physicians. In 2018, some municipalities had six time more physicians per inhabitant than others, a difference that has been growing since 2012. The level of unmet medical needs is some 28% higher in rural areas than in the country as a whole. The family physician network is mainly a private health service network, with low incentives for doctors in rural areas, which migrate to urban, more developed areas, leaving poor areas with less coverage ([42]).

Spending on healthcare remains skewed towards inpatient hospital care. This is despite a reduction in the number of hospital discharges. Associated inefficiencies include the high use of hospital beds, the low use of day surgery and lack of effective integration of health service delivery. The share of family physicians (approximately 20% of all physicians) has been steadily declining, raising questions as to the capacity to refocus healthcare delivery away from hospital inpatient care (Graph 4.3.3). Moreover, there is limited continuity and integration between different levels of care. This situation testifies to a lack in capacity to instil principles of comprehensive performance-based management into the health system (OECD 2019b).

([39]) Severe material deprivation rate for children by educational attainment level of their parent.
([40]) 77.02% in 2016, 86.1% in 2014
([41]) The percentage of insured rural population decreased to 65.6% in 2016 compared to 66.3% in 2015 and 75.8% in 2014
([42]) In 2017, there were 500 villages without any provider (National Society for Family Medicine).

Graph 4.3.3: **Outpatient use vs inpatient use**



(1) Data refer to 2017 or the closest year.
Source: Eurostat Database, OECD

Healthcare staff shortages remain considerable. The number of doctors and nurses is among the lowest in Europe. In 2018 salaries paid in public hospitals were substantially increased. In addition, investments on the ground targeting the upgrading of medical facilities are likely to contribute to better workforce retention.

Demographic change raises sustainability concerns for the Romanian healthcare system. This relates to population ageing as well as high migration. Projections indicate that these factors will imply an increase by one fifth in public spending on healthcare as a share of GDP (European Commission, 2018b). This is likely to contribute to increased pressures on health spending in Romania.

Romania lacks a unitary policy framework for long-term care and services adapted to demographic trends. Although the share of the population aged 80+ is expected to double by 2050, services for the elderly continue to be scarce. Long-term care falls under the larger umbrella of social and medical services. Responsibilities are further scattered among different institutional actors at different levels (European Commission, 2019j). The share of the elderly population is much higher in rural or remote areas, and less served by social services. The demand for residential long-term care services is largely unmet, due to the marginal amount of non-residential services provided ([43]) and an insufficient number of workers in the field (OECD, 2019c).

4.3.4. SOCIAL POLICIES

Social conditions continue to improve but vulnerable groups still face substantial challenges. The percentage of people at risk of poverty or social exclusion further decreased, to a historically low level ([44]) of 32.5% in 2018. However, one in three Romanians is still at risk of poverty or social exclusion, with families with children, the unemployed, inactive, atypical workers, Roma, elderly women and people with disabilities among the most exposed. This rate is still more than twice as high in rural areas than in cities. Once in poverty, overcoming it is increasingly difficult, due to the high level of intergenerational transmission of poverty and inefficient labour activation measures. Regional disparities remain high (see Section 4.4.3). Severe material and social deprivation is among the highest in the EU. Close to one Romanian in two is unable to face unexpected expenses. Access to essential services, such as energy, is also a challenge ([45]).

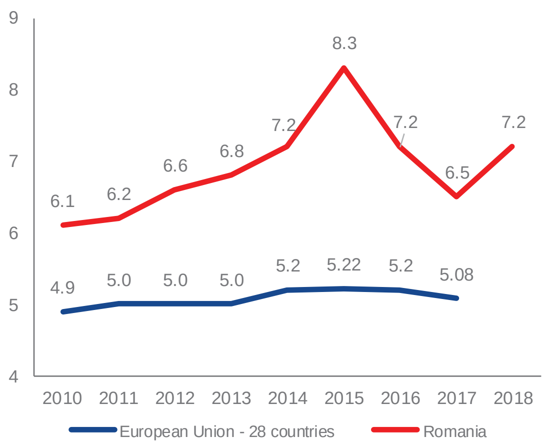
Rapid income growth has been accompanied by increasing income inequalities, while inequality of opportunity persists. Despite large increases in wages and pensions, income inequalities remain high and actually deepened in 2018 (Graph 4.3.4). This change is driven by both income increases for people in the highest income group and decreases for those in the lowest income group. High inequality is due both to high inequality of market incomes and to low redistributive impact of the tax and benefit system. In 2018, the income share of the poorest 40% of the population saw one of the greatest declines in the EU, remaining well below pre-crisis levels 17.6% compared to an EU average of 21.5%. Children of low-skilled parents continue to face a substantially higher risk of poverty than those of high-skilled parents; a gap of 70.7 percentage points in 2018, well above the EU average of 43.3pp.

([43]) Only 0.3% of elderly disabled people living with their families are covered by non-residential services

([44]) This indicator is available for Romania since 2007, when it amounted to 47.0%.

([45]) In 2018, 9.6% of the population was unable to keep home adequately warm (EU average 7.3%). The percentage of the population with arrears on utility bills is also above the EU average (14.4% vs 6.6%).

Graph 4.3.4: **Income inequality in Romania - S80/S20 income quintile share ratio**



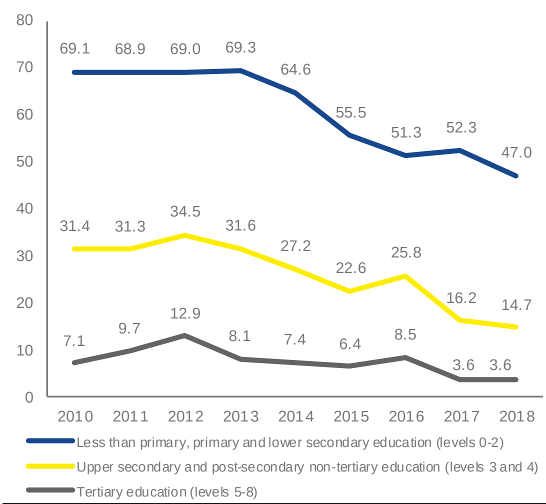
Source: European Commission

In-work poverty has been declining but remains among the highest in the EU. In 2018, in-work poverty declined but remained high at 15%. This is also related to a lack of quality jobs, especially in rural areas, and the precariousness of non-employees. There is a high rate of self-employment in rural areas and a high proportion of non-remunerated contributing family members (in small family businesses) among non-employees. In 2017, while only 45% of all employed persons were residing in rural areas, 82% of the self-employed and 94% of the contributing family members were living in rural areas. Most of the self-employed in Romania work in subsistence agriculture, some of them in construction and other small family businesses. The minimum wage increases have resulted in higher gaps between the income of employees and those of the self-employed, as incomes of the latter are growing at a slower pace.

Children's access to services is uneven, with higher costs for vulnerable groups. Monetary poverty of children has decreased but there has been no progress has been registered on access to services for children in vulnerable situations. Children in rural areas and vulnerable groups have limited access to (pre)school education, adequate nutrition, health care and housing. The implementation of measures to tackle the challenges herein would contribute to progressing toward SDGs 1, 4, 5 and 10. The consumption of low and high-risk drugs among children and young people is increasing, while preventive/support services are limited and their geographical distribution is uneven ([46]). One in every eight women giving birth for the first time in 2017 was a teenager. The deinstitutionalisation process for children shows good progress, with important steps being taken, including in terms of the relevant legislative framework. The residential care system for children does not yet ensure a successful transition to independent living.

High rates of child poverty signal inequalities of opportunity in the future. Children with low educated parents and those from households with very low work intensity are the most disadvantaged (Graph 4.3.5). Particularly affected are children in Roma communities, those living in rural areas and in marginalised urban communities, where access to education and social services is limited. The decrease in school enrolment and increase in the dropout rate for these groups point to a polarisation of education (Ministry of Education, 2019) which is likely to contribute to a higher poverty rate for the future adults (see Section 4.3.2).

Graph 4.3.5: **Severe material deprivation rate for children by educational attainment level of their parents**



Source: European Commission

Almost a quarter of elderly people face risks of poverty while the gender pension gap is high. In 2018, 17.4% of older people in Romania were exposed to severe material deprivation and 22.8%

([46]) Licensed social services distribution fiches at national, regional and county levels, 2018 were at risk of poverty. These figures are similar as for the rest of population in Romania andhigher than the rates for older people in the EU as a whole (4.7% and 17.1%). While the share of elderly exposed to severe material deprivation (which measures absolute poverty) has been falling, their at-risk-of-poverty rate has been increasing, as the significant growth of wages outpaced that of old-age pensions([47]).The new pension law enacted in summer 2019 is set to improve the future adequacy of pensions but has significant and unsustainable budgetary costs and is not accompanied by measures aimed at increasing the duration of working lives beyond the statutory minimum (see Box 4.1.1).

There are large gaps between pensions by gender, moment of retirement, type of work and special pensions. Statutory retirement ages and full contributory periods are not equal for both genders. This results in an average pension that is significantly lower for women than for men (a difference of 27.8% in 2017). The new pension law will equalise the full contributory period among genders and will decrease the difference in statutory retirement age by 2030. Convergence in this field would contribute to progressing toward SDG 5. The first pension also largely differs depending on the moment of the retirement for the persons with otherwise similar characteristics. The new pension law aims to resolve this issue (see Box 4.1.1.). There are also large gaps between pension revenues by type of work, in particular for workers in agriculture. Romania has one of the most complex special pension systems in the EU, as it has special schemes in virtually all special pension categories and they are hardly being streamlined (European Commission, 2018b). The minimum social allowance received by elderly with limited or without pension rights has not been increased in 2020, with potential adverse impact on income inequality among elderly.

People with disabilities have limited access to support services. The rate of persons with disabilities at risk of poverty or social exclusion in Romania is among the highest in the EU (37.6% vs an EU average of 28.7%). The lack of synergies and complementarity between educational, employment and social services further aggravates the situation of this group. Moreover, there are no licensed community services for adults with disabilities ([48]). The deinstitutionalisation of care of adults with disabilities is only being taken up slowly, while significant EU funds are available.

The integration of the Roma community remains a challenge. Roma people are much more affected by poor housing conditions (World Bank, 2014) ([49]), while discrimination in accessing social housing and forced evictions are still present. The Roma also continue to face obstacles in accessing health services due to lack of identification documents, low coverage of social security, stigma and discrimination. Enrolment of Roma children in education is still below the country's average. Despite some progress, early school leaving is high and educational segregation remains a challenge. The implementation of the National Roma Integration Strategy is lagging behind due to, among other factors, lack of coordination between stakeholders. Several Roma inclusion projects, co-financed by the European Social Fund, are being implemented, but results are not yet visible.

Homelessness and housing exclusion have increased. The determinants of homelessness in Romania have been shifting from individual reasons to structural weaknesses such as mass evictions, lack of housing support policies and insufficient social housing stock. Nine in ten affected people reside in large urban settlements. A quarter of the estimated homeless are children and young people. People living in marginalised communities as well as informal temporary houses or barracks represent a new form of housing exclusion. The number of people living in these settlements is higher than the number of people living on the streets. Approximately 200 000 people live in informal settlements. A new definition of homelessness and intervention approach would facilitate the development of services for such marginalised communities.

([47]) The at-risk-of-poverty rate is the share of people with an equivalised disposable income (after social transfers) below the at-risk-of-poverty threshold, which is set at 60 % of the national median equivalised disposable income after social transfers. Therefore, this is a relative indicator - it measures low income in comparison with other residents in that country.

([48]) Licensed social services distribution fiches at national, regional and county levels, 2018, p.15

([49]) Almost one third of the Roma population is living in slum dwellings and more than half in overcrowded dwellings.

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Social service provision remains largely insufficient, particularly in rural areas (see Section 4.4.3). Low salaries, lack of attractiveness of rural areas and strict conditions of access to the profession of social worker hamper the provision of social services. Recently, the government broadened the access of social work technicians) in the integrated teams at community level in order to cover the professionals' shortage. However, the social work technicians can only carry out their activity under the supervision by a social worker which creates other difficulties in delivering the social services at community level. Coordination between the local, county and national levels remains poor, also due to the fragmented distribution of powers and responsibilities (European Commission, 2019a). Misalignment between decentralisation of social services and financial means further deepened in 2019 and had a negative impact on the effectiveness of service delivery at the local level (see Section 4.4.5). The EU co-funded pilot project to introduce integrated teams at community level is under implementation with the first results expected shortly.

The tax and benefit system has a limited impact on reducing poverty and income inequality. Tax revenues are relatively low and tax structure has little progressivity (see Section 4.1.4). Government spending on social protection is much lower than the EU average. Social benefits have a very limited impact on reducing poverty. In 2018, social transfers reduced the at-risk-of-poverty rate by 16% and the poverty gap by 33% (compared to an EU average of 33% and 5% respectively). Family benefits have the largest effect on the poverty rate, followed by sickness and disability benefits. Unemployment benefits have very limited effect on the incidence and depth of poverty, possibly due to low coverage and short duration. Consequently, the power of the tax and benefit system (excluding pensions) to reduce income inequality is also limited (Graph 4.1.3).

The adequacy of social benefits is severely affected by a lack of indexation. The social reference index used as a basis for most social benefits has not been updated since its introduction in 2008. Thus, the level of many social benefits, while remaining constant in nominal terms, has been decreasing in real terms. The consumer price index has increased by 33% over the period 2008-2019, while average net wages have grown (in nominal terms) by 139%. Simulations show that, if the social reference index had been updated regularly in line with inflation, the at-risk-of-poverty rate in 2019 could have been reduced by 12% (or 2.6 percentage points). A more generous indexation in line with average net wage growth would have implied a reduction of 44% (or 9.3 percentage points).

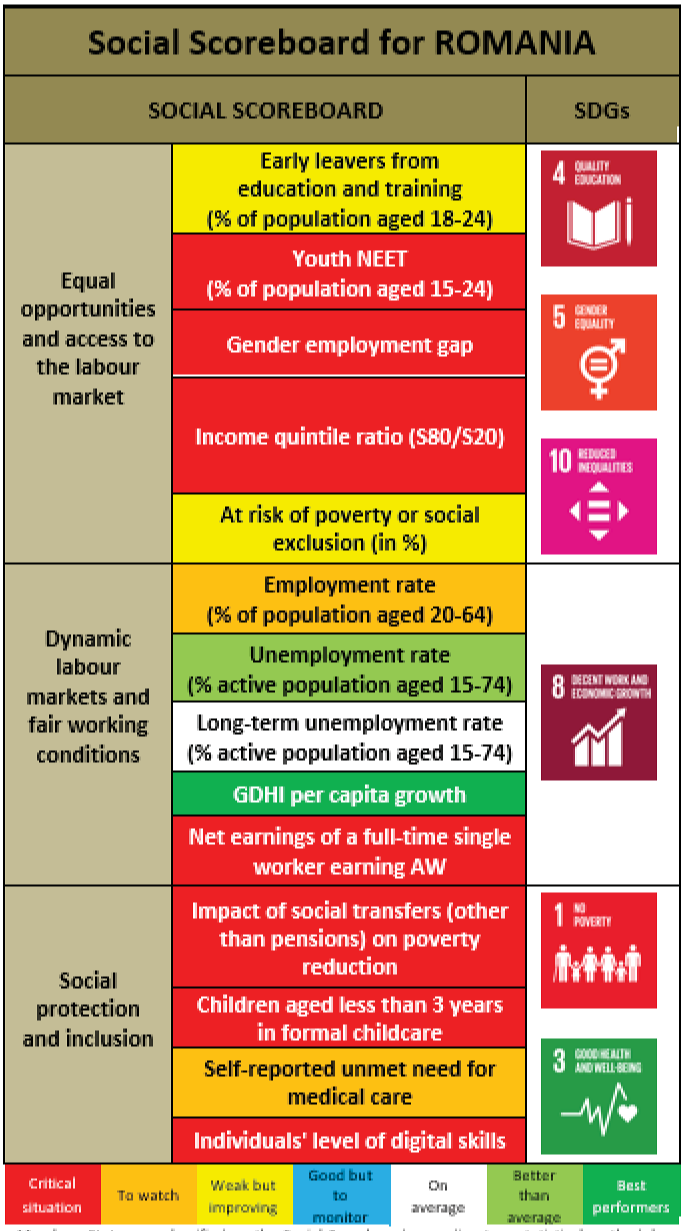
Romania lacks a minimum floor of social protection for all workers. Coverage of casual and seasonal workers for unemployment, sickness, maternity, accidents and occupational injuries is generally missing. Moreover seasonal workers do not have access to old-age/survivors' pensions.

The minimum inclusion income reform has again been postponed. Though adopted in 2016, the entry into force of the minimum inclusion income law is postponed to 2021, due to lack of capacity of the public administration. The social reference index used as a basis for most social benefits has not been updated since its introduction in 2008 (European Commission, 2019a). The adequacy of the minimum income support thus remains one of the lowest in the EU (European Commission, 2019d). The government is working on operationalising the payment model (prepaid card) and the revision of the indexation mechanism for social assistance benefits, with help from the EU.

The social economy is facing significant challenges. The economic impact of social enterprises remains marginal in Romania. An estimated 6,000 de facto social enterprises are active on the market and the number of paid employees they support stands at 19,065 (European Commission, 2019). Only a very small number of them have the official "social enterprise" label. Almost nine in ten social enterprises are associations or foundations, while the number of cooperatives, sheltered workshops and social insertion enterprises is very limited (12.6%). The framework is characterised by a narrow focus on social insertion enterprises, limited fiscal incentives and difficulties in accessing financial resources. There is no integration of social economy policies with active labour market policies for vulnerable groups. The current legal and policy frameworks do not harness the potential of social enterprises to innovate and contribute to environmental goals.

Box 4.3.1: **Monitoring performance in light of the European Pillar of Social Rights**

The European Pillar of Social Rights is a compass for a renewed process of upward convergence towards better working and living conditions in the European Union. It sets out twenty essential principles and rights in the areas of equal opportunities and access to the labour market; fair working conditions; and social protection and inclusion.



Social Scoreboard for ROMANIA		
SOCIAL SCOREBOARD		SDGs
Equal opportunities and access to the labour market	Early leavers from education and training (% of population aged 18-24)	4 Quality Education
	Youth NEET (% of population aged 15-24)	
	Gender employment gap	5 Gender Equality
	Income quintile ratio (S80/S20)	10 Reduced Inequalities
	At risk of poverty or social exclusion (in %)	
Dynamic labour markets and fair working conditions	Employment rate (% of population aged 20-64)	8 Decent Work and Economic Growth
	Unemployment rate (% active population aged 15-74)	
	Long-term unemployment rate (% active population aged 15-74)	
	GDHI per capita growth	
	Net earnings of a full-time single worker earning AW	
Social protection and inclusion	Impact of social transfers (other than pensions) on poverty reduction	1 No Poverty
	Children aged less than 3 years in formal childcare	
	Self-reported unmet need for medical care	3 Good Health and Well-Being
	Individuals' level of digital skills	

Critical situation	To watch	Weak but improving	Good but to monitor	On average	Better than average	Best performers

Members States are classified on the Social Scoreboard according to a statistical methodology agreed with the EMCO and SPC Committees. It looks jointly at levels and changes of the indicators in comparison with the respective EU averages and classifies Member States in seven categories. For methodological details, please consult the proposal for a Joint Employment Report 2020, COM(2019) 653 final; NEET: neither in employment nor in education and training; GDHI: gross disposable household income. Update of January 2020.

The Social Scoreboard supporting the European Pillar of Social Rights points to a number of employment and social challenges in Romania, while some indicators have improved. The levels of poverty, social exclusion and early school leaving are still among the highest in Europe. Income inequalities increased, and inequalities persist in access to quality education, healthcare and social services, with regional disparities and a deep urban-rural divide. Coverage of public services, including childcare and healthcare services, remains low in particular in rural areas and among marginalized communities. There is a misalignment between the decentralisation of social services and the allocation of financial means, which hampers the effectiveness of service delivery at local level. The impact of social transfers on poverty reduction is limited.

In spite of high economic growth and low unemployment rate, several labour market indicators remain a matter of concern. The gender employment gap and inactivity, especially among women, remain high, while activation measures are ineffective. Insufficient childcare facilities and services are among the factors affecting female labour market participation, especially in rural areas. Skills of the workforce are not keeping up with the evolution of the labour market, in particular with regard to digital and high-end technological skills. Social security for atypical workers remains inadequate. While wages are increasing at a fast pace, net earnings remain comparatively very low and the risk of in-work poverty is among the highest in the EU.

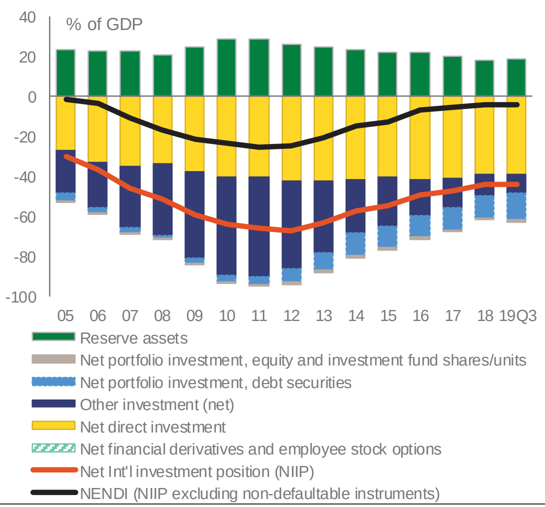
The de-institutionalisation of social and health services for children continues to show encouraging progress. Key to its success was the adequate mix between legislation, policy and delivery mechanisms, backed by a good level of administrative capacity of the stakeholders. Improvements are expected in the areas of integrated community services and consolidation of the social assistants' system, where the authorities are implementing two EU-funded strategic projects.

4.4. COMPETITIVENESS, REFORMS AND INVESTMENT

4.4.1. COMPETITIVENESS AND EXTERNAL POSITION (*)

The net international investment position (NIIP) has improved significantly but remains highly negative. The net international investment position reached -43.7% of GDP in 2018, improving by almost 24 pps compared to 2012 (Graph 4.4.1). In 2018 alone, the NIIP improved by 3.7 pps due to strong GDP growth and despite a widening current account deficit. However, this positive evolution is showing signs of reversal as the NIIP declined to -44.3% in Q3-2019. By components, net direct investment has remained broadly stable as a share of GDP, averaging -41% in the last eight years, but has steadily increased its share in the net international investment position. Portfolio investment has gained some weight over recent years, while other investment declined more visibly. Reserves have been somewhat trending down in terms of GDP.

Graph 4.4.1: **Net international investment position**



(1) Merged BPM5/BPM6-ESA 2010 data
Source: European Commission

Further progress on improving NIIP could stall or even reverse. The expected widening of the current account deficit in the next years combined with a projected slowdown of GDP growth raise the prospect of some further worsening of Romania's NIIP. For instance, a 1 pp. lower than forecast real GDP growth in 2021 and onwards could result in the NIIP dropping below –60% of GDP by 2027. Alternatively, an increase in domestic government yields in 2021 and onwards could see the NIIP deteriorate even more significantly.

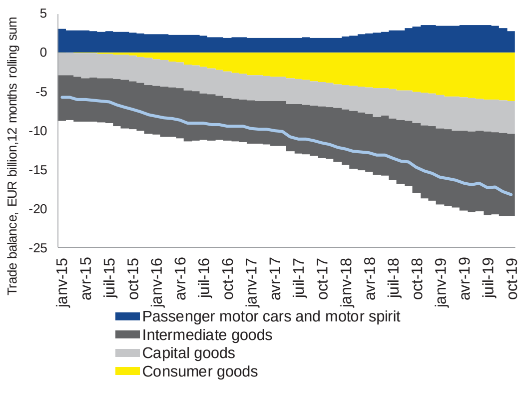
Foreign direct investment (FDI) flows remain volatile. In 2018, foreign direct investment inflows increased by about 18% compared to 2017. In the first 11 months of 2019 they increased slightly compared to the same period in 2018. This decline was attributable to debt instruments and reinvested earnings, while FDI in equity increased substantially. The main countries of origin for foreign direct investment in Romania are the Netherlands, Germany, Austria, Italy and Cyprus.

The current account deficit continued to worsen, reflecting strong domestic demand and imports growth. From an almost balanced position in 2014, the current account reached a deficit of 4.4% of GDP in 2018 and is estimated to have widened further to 5.1% in 2019. The trade balance in goods remains the main driver of the widening current account deficit. The deficit in the trade in goods gradually increased from 4.3% of GDP in 2014 to 7.3% in 2018 and is expected to have exceeded 8% in 2019. In the first 11 months of 2019, the current account balance deteriorated by 21% compared to the same period in 2018 mainly on the back of a 19% deterioration in the trade balance in goods. The surplus of the services balance, which increased by 1.8%, was not enough to compensate for the rapid deterioration of the trade in goods. The primary balance remained negative but improved by 13%. The secondary income balance, which consists mainly of remittances, increased its surplus by about 14% compared to January-November 2018.

The continued deterioration of the current account fuelled by an expansionary fiscal policy raises macro-stability concerns. The increase of the current account deficit in recent years has been acompanied by a decline of its coverage by foreign direct investments and the capital account from more than 130% in 2017 to less than 75% in the first 11 months of 2019. In the event of an economic slowdown or heightened risk aversion in the markets, a downward adjustment of the exchange rate could alleviate the current account deficit but at the same time could have other effects, e.g. on external liabilities. For instance, it could increase significantly the cost of the government debt and the affordability of such a measure would ultimately depend on the level and the structure of the public debt ([50]). The economy's net lending/borrowing position became negative already in 2017 when the current account deficit started to widen markedly. The net borrowing needs come mainly from households and the government, while corporations are net lenders.

Imports of consumer goods have grown significantly faster than other imports but are slowing down. The deterioration of the trade balance was accompanied by a change in the composition of imports, with consumer goods imports growing significantly faster than those of capital and intermediate goods (Graph 4.4.2). This evolution has been fostered by a fiscal policy directed at increasing disposable income, which in turn stimulated consumer spending. Between 2015 and 2018, consumer goods imports increased by an annual average of 11.9%. The corresponding figures for imports of intermediate goods and those of capital goods were 9.8% and 8.6% respectively. Although in 2018 imports of capital goods grew much faster than those of intermediate and consumer goods, in the first 10 months of 2019 consumer goods imports exceeded again by a significant margin the imports of other goods.

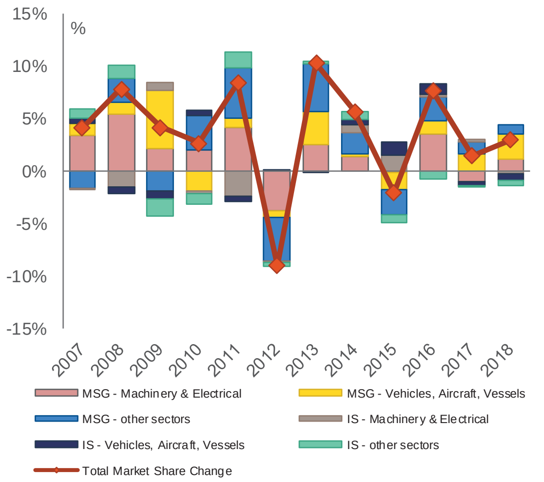
Graph 4.4.2: **Trade balance breakdown**



Source: European Commission

Export performance remained relatively strong in recent years. Romania's export market share for goods and services increased by 8.9% in 2016, 3% in 2017 and a further 4% in 2018. Over 2013-2018, it increased by 25%, fourth in the EU. In 2018, Romania gained most market shares in the vehicle industry and only lost market shares in the wood industry (Graph 4.4.3). Exports of services continued to be concentrated on transport and telecommunications.

Graph 4.4.3: **Export market share by industry**

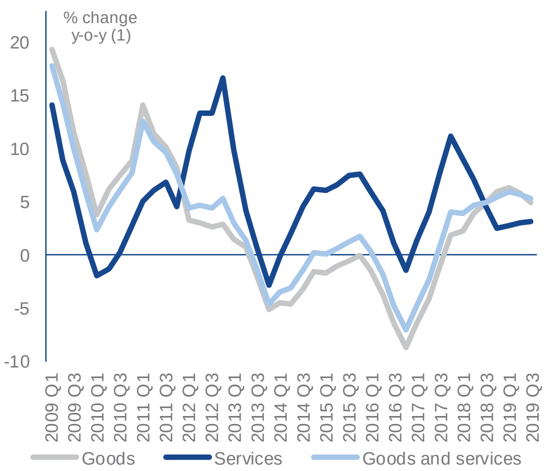


(1) IS stands for Romania's initial sectoral specialisation, while MSG (market share gain) captures how successful Romania has been in gaining market shares on average across export products.
Source: European Commission

Romania's price competitiveness could be hurt by increasing export prices. The price of exported goods in the domestic currency (as measured by the export of goods deflator), fell each year between 2013 and 2016 (Graph 4.4.4) and resumed growth in 2017. In 2018 export prices for goods increased on average by 6%, while in the first three quarters of 2019 the growth decelerated to 4% on average, raising concerns about the country's price competitiveness. Conversely, and also thanks to some nominal depreciation, the pace of appreciation of the real effective exchange rate deflated by export prices moderated in 2019 following an appreciation throughout 2018.

([50]) While private sector indebtedness is low (47.4% of GDP in 2018), similar risks apply in the event of a devaluation.

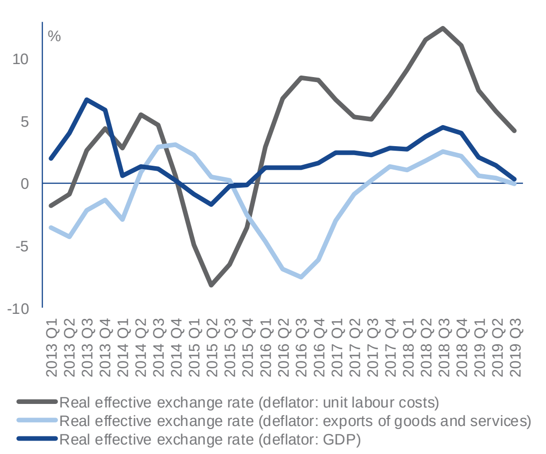
Graph 4.4.4: **RON-denominated export price evolution**



Source: European Commission

Rapidly increasing unit labour costs pose risks to competitiveness. The acceleration of unit labour costs has put pressure on the real effective exchange rate and Romania's cost competitiveness. As a result, the evolution of the unit-labour-cost-deflated real effective exchange rate, subdued until early 2016 moved into positive territory, putting pressure on cost competitiveness. (Graph 4.4.5).

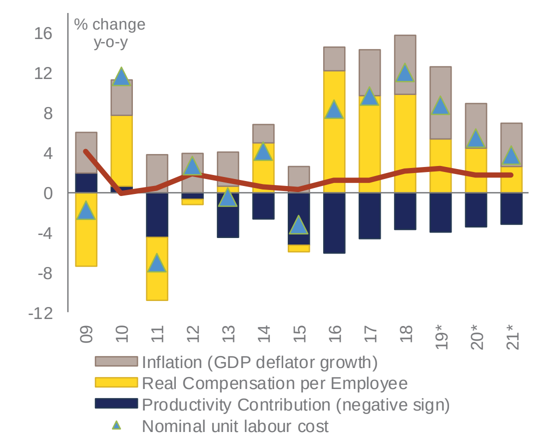
Graph 4.4.5: **Real effective exchange rate growth**



Source: European Commission

Labour cost dynamics have outpaced productivity developments but are set to moderate. Nominal unit labour costs started increasing strongly in 2016 (Graph 4.4.6), growing by 8.5% in 2016, by 9.8% in 2017 and 8.8% in 2018. This acceleration was driven entirely by compensation per employee, which increased by double digits in nominal terms between 2016 and 2018. However, in 2019 unit labour cost decelerated as compensation per employee slowed down. Labour productivity per person grew by 6% in 2016, 4.6% in 2017, 4.2% in 2018 and an estimated 3.9% in 2019.

Graph 4.4.6: **Nominal unit labour cost**



Source: European Commission

The public sector continued to be the main driver of nominal unit labour cost dynamics. Unit labour costs in the public sector increased by about 20% in 2017 and 2018 and by an average of 15% in the first three quarters of 2019. Unit labour costs in other sectors have seen milder increases, except for construction where growth was significant in 2017 and 2018. In industry, Romania's main exporting sector, unit labour costs expanded less, by 6.8% in 2017, 3.9% in 2018 and about 4% in the first three quarters of 2019.

A number of non-cost factors also affect Romania's competitiveness negatively. The poor state of infrastructure hinders businesses' effectiveness in moving goods and services across borders, limits labour force mobility and aggravates regional disparities. The economy's low innovative capability is another key factor limiting competitiveness (see Section 4.4.2). A cumbersome business environment, marked by frequent and unpredictable legislative changes, together with excessive red tape and persistent inefficiencies in the public administration undermines investment decisions and risks reducing the country's attractiveness to foreign investors (see Section 4.4.5).

Box 4.4.1: Investment challenges and reforms in Romania

Macroeconomic perspective

Despite the investment as a share of GDP being above the EU average, its evolution since the crisis has been volatile. Following a modest performance in 2018, characterised by a drop in the private investment ratio and a recovery in the public one, total investment picked up in 2019, increasing by over 18% in the first three quarters.

Assessment of barriers to investment and ongoing reforms

Public administration / Business environment	Regulatory/ administrative burden	CSR
	Public administration	CSR
	Public procurement /PPPs	CSR
	Judicial system	
	Insolvency framework	
	Competition and regulatory framework	CSR
Labour market/ Education	EPL & framework for labour contracts	
	Wages & wage setting	CSR
	Education	CSR

Financial Sector / Taxation	Taxation	
	Access to finance	CSR
R&D&I	Cooperation btw academia, research and business	
	Financing of R&D&I	CSR
Sector specific regulation	Business services / Regulated professions	
	Retail	
	Construction	
	Digital Economy / Telecom	
	Energy	CSR
	Transport	CSR

	No barrier to investment identified
CSR	Investment barriers that are also subject to a CSR
	No progress
	Limited progress
	Some progress
	Substantial progress
	Fully addressed

Investment could be hampered by persistent uncertainty, both in the form of unpredictable policymaking and of budgetary pressures on public investment stemming from the new pension law.

Selected barriers to investment and priority actions under way

1. The lack of skill improvement in the labour market hampers economic growth prospects and acts as a barrier to investment, the country ranking amongst the worst performers in the EU according to the European Skills Index. Overall, despite progress in the inclusiveness of education, no advancement was made in promoting digital literacy and increasing the relevance of higher and vocational education and training. Moreover, the over-qualification rate, despite below EU average, has almost doubled over the last decade. Given the already tight labour market and current demographic trends, such issues point to a further worsening of skilled-labour shortages.

2. In terms of research and development, the country is amongst the worst performers in the EU, spending just 0.5% of GDP in R&D activities in 2018 compared to the 2020 country target of 2%. All peer countries in the region invest substantially more in R&D than Romania.. This underinvestment has resulted in poor scientific quality and performance. Academia-business cooperation occurs mainly on an ad-hoc basis and its development is hampered by regulatory barriers. Without significant regulatory and budgetary changes, current measures are insufficient to tackle the underfinancing and structural problems affecting the research and innovation sector.

The EU supports investment via the European Fund for Strategic Investments (EFSI). By November 2019 total financing under the EFSI amounted to €722 million, intended to trigger €3 billion in additional investments. EFSI backing amounted to approximately €519 million for infrastructure and innovation projects approved and financed by the European Investment Bank, and to €203 million for agreements with small and medium enterprises financed by the European Investment Fund. By the end of 2020, EFSI and other EU financial instruments will come under the roof of the new, policy-driven InvestEU programme, guaranteeing a more coherent approach and greater choice of policy implementation options.

4.4.2. PRODUCTIVITY AND INVESTMENT

Productivity developments

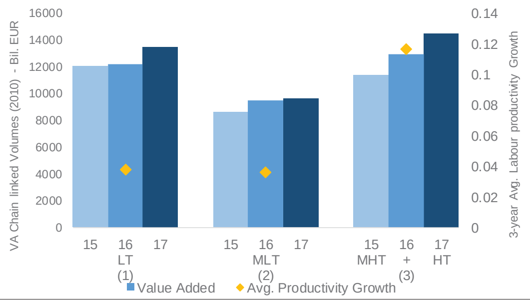
Productivity has been increasing since the early 2000s, but Romania has room to catch up. On average, real labour productivity per person increased by 4.8% per year between 2000 and 2019. Since 2012, this performance has been driven mainly by total factor productivity growth, but both labour composition and capital deepening have had a strong positive impact on the trend. Despite the improvements, Romania's productivity remains among the lowest in the EU and in 2019 stood at nearly 68% of the EU average nominal labour productivity.

Labour productivity dynamics vary significantly across firms. Domestic firms are on average smaller, less productive and less innovative than larger, and mostly foreign-owned, firms (NBR, 2018). Despite a recent shift of manufacturing jobs towards more productive firms and increased allocative efficiency, there is scope for improvement. While foreign-owned firms represented less than 10% of all firms, they accounted for almost half of gross value added and more than two-thirds of the country's exports in 2016 (NBR, 2018).

Firm size and characteristics largely account for the low level of technology uptake. On average, small firms tend to invest less in new technologies and innovation (EIB, 2019). Even in knowledge-intensive sectors such as medium and high-tech manufacturing, firms invest less in R&D than their peers in the region. In addition, Romania has one of the lowest robot densities in the region (IFR, 2017) and SMEs are five times less likely to use robots than large firms (European Commission, 2019a).

Performance in the manufacturing sector has been mixed across technology classes. Whilst the low and medium-low technology sectors grew moderately in value added and labour productivity, medium-high technology production has been the largest contributor to growth (Graph 4.4.7). The foreign-dominated automotive industry and related sectors such as rubber and plastics are the driving forces behind this development and have also improved export quality. However, despite the presence of FDIs in R&D activities, spill-overs from foreign to domestic firms remain limited at best, with a positive effect between foreign-owned firms and domestic suppliers but a negative one between horizontal competitors (NBR, 2018).

Graph 4.4.7: **Value added and average labour productivity growth by manufacturing technology class**



(1) LT: Low technology sector;
(2) MLT: Medium-low technology sector;
(3) MHT + HT: Medium-high and high technology sector (merged due the low overall share of HT)
Source: European Commission

In services, labour productivity increased in the knowledge intensive and the low-knowledge-intensive sectors. In terms of value added however, low-knowledge intensive sectors have a slightly higher growth rate (Bauer et al, 2020). The share of domestic firms in value added has also increased consistently since 2010. Amongst knowledge-intensive activities, the labour productivity gap between foreign and domestic firms has decreased in the ICT sector despite the smaller size of domestic firms on average. Labour market tightness and financial constraints may constitute an obstacle to the scaling up of these domestic firms.

Investment activity

Despite significant investment needs, investment remains subdued. The 2019 European Investment Bank Investment Survey (EIB, 2019) indicates that less Romanian firms invest than the EU average (71% vs 85%). SMEs and infrastructure firms are confident about expanding investment, but more service sector firms expect a decrease. Meanwhie the share of firms operating at or above capacity (57%) remains in line with that of the EU average (59%), especially in the service sector. Uncertainty about the future remains the most cited barrier to investment (81% vs 72% EU average).

Availability of adequate transport infrastructure, of staff with the right skills and labour market regulations are the next most relevant barriers (all around 73%). Finally, energy costs and availability of finance are also more likely to be cited as barriers compared to the corresponding EU averages.

More investment is also necessary to improve the low quality of digital and physical infrastructure. Digitalisation efforts have not yet led to sufficient reduction of the urban-rural divide and push forward the integration of digital technologies by firms. In addition, transport, energy and water infrastructure remain poor, posing an obstacle to territorial integration. Robust transport and energy networks would help companies connect with global markets and suppliers and boost their productivity. Countries with strong infrastructure are also more attractive to foreign direct investment, which can support an economy's shift to the production of higher value-added goods.

Research and innovation

Romania has yet to start its transition towards a knowledge-based economy. The country's innovation performance is poor, ranking last in the EU in the 2019 European Innovation Scoreboard (European Commission, 2019b). Investment in employee training and ICT solutions are lower than the EU average (EIB, 2019). R&D investment is very low, with an R&D intensity of 0.51% of GDP in 2018, well below the 2020 national target of 2% and the EU average of 2.12%. Public R&D investment was 0.2% of GDP in 2018. Private expenditure on R&D was only 0.30% of GDP, below the EU average of 1.41%

Scientific performance and academia-business links continue to be poor. The country still ranks at the bottom of the EU in terms of top scientific publications and international co-publications (European Commision, 2018a). Universities do not receive any institutional funding for R&D, despite their important role in producing relatively good research. Regulatory barriers (e.g. red tape, conflicting or unclear rules) hamper academia-business links, which tend to occur on an ad-hoc basis.

The ICT and automotive sectors show signs of innovation potential. Both sectors are predominantly export-oriented and well integrated into global value chains (ANIS 2018; NBR 2018), and are therefore exposed to competition and high technological standards. The ICT sector is leading in high growth enterprises ([51]) (Flachenecker et al, forthcoming), innovative start-ups and successful scales-ups (My-Gateway, 2019). The automotive sector accounts for some of the largest business R&D investment in the country. However, since foreign-owned firms operating in Romania tend to keep key R&D activities at their foreign headquarters (NBR, 2016), potential know-how or technology spill-overs remain limited (NBR, 2018). This is also visible in the R&D investment intensity of the ICT sector, which was among the lowest in the EU in 2016 (European Commission, 2019a), whilst in the automotive sector it is lower than in peer countries.

Policies supporting the transition towards a more knowledge-based economy remain limited. The economic competitiveness, research and innovation and smart specialisation strategies cannot achieve their stated objectives without a sufficient level of public R&D funding. Besides the tax exemption for ICT professionals, there are no targeted measures for innovative start-ups. The 'Start-up Nation' programme was not deemed well-tailored to the needs of innovative start-ups (World Bank, 2018). The scaling up of innovative domestic firms remains challenging due to the limited size of the local venture capital market (Invest Europe, 2018b). Most successful measures for start-ups and scales-ups (e.g. accelerators, business angels, venture capital) are bottom-up initiatives, with limited policy support (My-Gateway, 2019).

Regional initiatives to enhance growth exist, but risk being hampered by a lack of a robust national innovation and entrepreneurship ecosystem. The Romanian regions have developed and are currently updating Smart specialisation strategies (S3), identifying key innovative sectors and projects pipelines. In 2019 they continued to receive tailored expertise under the Commission's

([51]) Enterprises with an average annualised growth in the number of employees of more than 10% per year over a 3-year period and at least 10 employees when the growth began. 7.7% of firms in the Romanian IT sector are high growth enterprises.

Catching up Regions Initiative in order to facilitate the transfer and dissemination of new technology between research organisations and businesses, better commercialise research projects, build capacity for technology transfer and promote innovation in local small and medium-sized businesses and start-ups. In 2019 the initiative led to the reallocation of EU Funds to innovation projects in two regions (Nord-Est and Nord-Vest) and will be carried out until end 2020. However, though very promising in terms of capacity and knowledge-building, these regional initiatives cannot achieve full potential and increase the country's performance and competitiveness unless a functional and robust national innovation and entrepreneurship ecosystem is set up.

Digitalisation

Romania slightly improved in almost all of the Digital Economy and Society Index (DESI, 2019g) dimensions. Despite some stagnation, Romania performs best in the Connectivity dimension. Fixed broadband coverage of households remained at around 87% below most Member States. Broadband take-up stalled at 66% of households, well below the EU average of 77%. In general, Romania performs very well for ultrafast (of at least 100 Mbps download) broadband coverage and take-up (75% and 45% respectively). However, only 39% of rural areas are covered by ultrafast broadband, though still above the EU average of 29% (European Commission, 2019g).

Despite some efforts, digitisation of the economy is lagging behind. The country launched the Manifesto for Digital Romania in 2016. This set out objectives for a digital future, but a more comprehensive approach has not yet been developed. More than one fifth of Romanians never used the internet, and less than a third have basic digital skills. Public services lag behind other EU Member States, despite having one of the largest shares of e-government users (7th in the EU). Furthermore, Romanian businesses are well below the EU average in integration of digital technology. In 2018, only 11% of them used big data analysis, 9% social media and 7% cloud services (European Commission, 2019g).

Measures are in place to support investment in digital technologies. In terms of EU-coordinated programmes, Romania is a member of the EuroHPC73 Joint Undertaking, and signed the Declaration of the European Blockchain Partnership and the Declaration on Cooperation on Artificial Intelligence. During 2014 to 2020, under the European Regional Development Fund, Romania is also investing more than 75 million in the ICT innovation sector. The business sector showed a huge interest, responding to the calls for projects for five times higher than the available envelope. For the post-2020 EU Funds programming period, the intention is to put major emphasis on digitalisation and innovation.

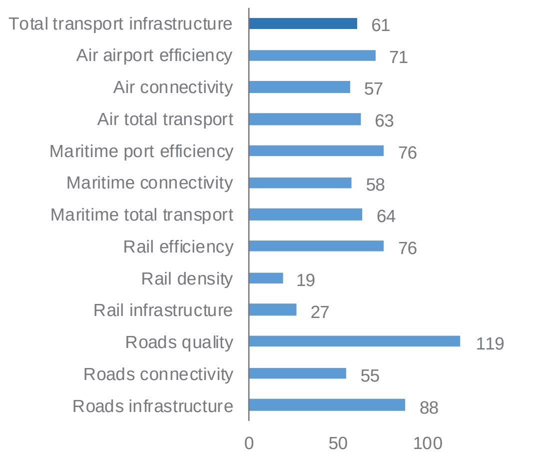
There are several initiatives in Romania in the field of cybersecurity, but there is a need for specialists in the field. The Government Decision 271/2013 on Cyber Security Strategy of Romania and the National Action Plan on the implementation of the National Cyber Security System address the development of the cyber-security knowledge of users. The National Cyber Security System facilitates the coordination of actions at national level between public authorities and the academic and business environment and professional associations. Public training centres and programmes have been developed. In the academic environment, a series of university programmes aim at increasing overall competences in the field. However, the main impediment in the development of cyber-security technology is the lack of specialized human resources. In early 2020 the Government adopted a new Emergency Ordinance for the operationalization of the Authority for the Digitalisation of Romania. It made the Secretary General of the Government in charge of policy implementation and strategy at national level.

Transport infrastructure

The condition and reliability of transport infrastructure remains poor, below peers and the EU average (European Commission, 2019m). Romania ranks low in infrastructure quality for road, rail efficiency, maritime and airport infrastructure (Graph 4.4.8) (Global Competitiveness Report, 2019). In road infrastructure, the TEN-T network has not yet been completed and is missing the cross-Carpathian connection. The lack of adequate transport endowment is an obstacle to territorial integration, leaving certain regions such as the Nord-Est and

Sud-Vest Oltenia isolated. Moreover, adequate multi-modal connection in many urban areas is still to be developed.

Graph 4.4.8: **World rank of Romanian transport infrastructure on 13 indicators**



(1) Rank amongst 141 World economies
Source: Global Competitiveness Report 2019, WEF

Regions in Romania are underperforming in terms of infrastructure compared to the EU average (European Commission, 2019m). The lack of sufficient and modern transport endowment is an obstacle to Romanian and European territorial integration, as it leaves certain regions, such as the Nord Est and Sud Vest Oltenia, isolated.

Insufficient upgrades and maintenance has reduced train speed and affected delivery times (OECD, 2016) (CNSDN, 2019). The reform of the railway sector is lagging behind. The recently established National Rail Reform Authority is set to complete a strategic review of the sector in order to bring down costs and eliminate redundant infrastructure. Completing the missing links in the cross-border rail sections with Hungary and Bulgaria, the upper railway section of the Rhine–Danube corridor, and advancing works on the Arad–Timisoara–Bucharest–Constanta line, as well as other major national connecting lines as listed in the General Transport Masterplan, should remain a priority. Despite recent investment in rail signalling, in the context of the European rail traffic management system, the systems are not yet operational.

Promoting public transport and shifting freight transport away from road could reduce external costs, including for the environment. Although the Romanian government aims to increase the share of rail compared to road transport (National Reform Programme 2019, p. 32), plans and their implementation are still in early stages. The Strategy for Railway Infrastructure Development 2019-2023 assessed future mobility needs. It analyses the actions needed to develop railway infrastructure and assesses the financing needs to be €12.8 billion over the next five years.

A reliable transport infrastructure strategy and investments would benefit from prioritisation and stabilisation. Investment gaps exist in sustainable transport, including efficient railways, digitalisation, and infrastructure for alternative fuel use, e.g. for electric vehicles. More efforts are necessary to upgrade significantly the administrative capacity of the road agency (CNAIR) and rail agency (CFR), notably through the enforcement of the performance-based contracts agreed with the European Commission in 2017 in the context of fulfilling the ex-ante conditionality on transport.

Romania has one the poorest road safety records in the EU. It registered double the EU-average number of fatalities per million inhabitants in 2018, despite a 4% reduction in fatalities since 2017. Contributing factors are underdeveloped infrastructure, especially for pedestrians and cyclists, excessive speed and weak enforcement. Investment in motorways as well as in maintenance and upgrades on existing roads would improve safety. Beyond infrastructure, Romania is part of a knowledge-sharing programme to the improve administrative capacity to tackle road safety in an integrated manner ([52]).

Energy

Links to neighbouring countries in the gas market still lack sufficient infrastructure. Investment in the gas-transmission infrastructure,

([52]) Romania benefits from the new “EU Road Safety Exchange Programme”, financed by the European Parliament, and from the “Safer Transport Platform”, an advisory facility created by the Commission and the EIB in 2019. EIB technical assistance is ongoing in developing a road safety investment programme.

particularly the completion in 2020 of the Romanian sections of the Bulgaria-Romania-Hungary-Austria (BRUA) pipeline corridor, would allow bi-directional flows and enhanced interconnectivity with Bulgaria and Hungary. In a second phase, BRUA is also crucial for the start of Black Sea offshore gas production. This would give consumers in Romania and in the broader Central and Southeast European region, access to a domestic gas source, improving security of supply and competition.

With improved infrastructure Romania could tap into its potential for renewable power generation. A well-developed and well-interconnected power grid is essential to exploiting this potential. In 2017, the electricity interconnection level was 7%, below the 2020 target of 10%. The implementation of the Planned Projects of Common Interest (PCI) in electricity will contribute to this goal. The Back Sea Corridor PCI cluster aims to relieve grid congestion in Southeast Romania and enable the integration of renewable power generation in both Romania and Bulgaria,creating a bridge to the energy markets of the Western Balkan countries.

Investment in energy efficiency remains low despite good incentives. To meet the EU 2030 target of 32.5% energy efficiency, private financing should be attracted to boost investment in energy efficiency. Although the country has allocated significant amounts from the European Structural and Investment Funds into energy efficiency in buildings (see Section 4.5), absorption is very low, pointing to the need for an improvement in this area.

Air quality

Supporting measures aimed to address the main sources of air pollution (e.g. domestic heating, transport, etc.) leading to air quality improvement and upgrading of the monitoring should be stepped up. It is necessary to ensure that key measures supported under specific sectoral policies (e.g. energy, transport) are fully aligned with/not detrimental to air quality objectives; The upgrade and improvement of the air quality monitoring network, and supporting timely reporting of air quality data are of paramount importance.

Water

Romania's water policy still shows deficiencies, in particular with regard to access to water and sanitation in rural areas, as well as quantity and quality of drinking water. Collection of wastewater and connection to public sanitation infrastructure is still incomplete. The distance to the target of collecting wastewater generated by agglomerations >2,000 population equivalent is 26%. Currently across the EU, on average 96% of citizens are connected to potable water supplies, only 67,5% in 2017 in Romania[53]. Affordability is the lowest in the EU with water supply and sanitation expenditures accounting for over 6% of households' expenditures in the poorest population group.

Investments in wastewater treatment could address these issues. The national regulator (ANRSC) needs to play a stronger role in asset management, business plan evaluation and monitoring. Efforts are needed for the extension and modernization of drinking water and wastewater infrastructure, for drinking water quality monitoring and the modernization of laboratories for better monitoring of substances discharged into the waters. In a recent study, the OECD([54]) estimates an investment need for water supply and sanitation of approximately €17.9 billion by 2030, while the additional costs for connecting vulnerable and marginalised people to public water supply systems are of around EUR 1.1 billion by 2030.

Waste

Waste management remains a key challenge for Romania. The country continues to be characterised by low recycling of municipal waste (14%) and high landfilling rates (70%). Moreover, recycling rates have been stagnated since 2013, while the incineration rate has increased slightly to

53

https://ec.europa.eu/eurostat/tgm/table.do?tab=table&plugin=1&language=en&pcode=ten00012

([54]) Source: OECD, *draft version:* Water-related investment needs and financing capabilities in EU Member States *Report not published to date*. *Publication planned by early 2020*

4%. In 2017, municipal waste generation per capita in Romania was still considerably below the EU average of around 487 kgs. The Early Warning Report for Romania identifies the country as being at risk of missing the 2020 preparation for re-use/recycling target for municipal waste.

Achieving ambitious targets of recycling and reducing landfilling will require policy action. New requirements arising from the revised Waste Framework Directive with more ambitious recycling targets for the period up to 2035, and a revised Landfill Directive with the obligation to ensure that the amount of municipal waste landfilled is reduced to 10% or less by 2035 necessitate concentrated efforts. Appropriate policy measures include in particular meaningful Pay-As-You-Throw schemes, functional separate collection, especially in the most populated areas, improvements of waste data reporting and capacity building for municipalities, and investment to waste prevention.

4.4.3. REGIONAL DISPARITIES

Regional disparities in Romania are among the highest in the EU, though they have decreased slightly over the last five years. GDP per head in the capital region was 144% of the EU average, while in the Nord-Est it was 39%. Nord-Est, Sud-Est and Sud-Vest have the lowest growth rate also being the poorest regions (see Section 1). Disparities are mainly driven by the significant investment and labour productivity gaps between the capital and the rest of the country. In addition, in all Romanian regions, except the Bucharest region, the road infrastructure and related public investment are not sufficiently developed (see Section 4.4.2). The lack of specific responsibilities at regional and county levels to provide inclusive public transport services increases the isolation of marginalised communities and reduces their access to essential services.

Regional competitiveness correlates with employment and productivity levels in important economic sectors. In 2019, the Bucharest region was the most competitive with a score of 55.9 (0-100) while the remaining regions with scores between 20.9 and 5.3 are lagging behind significantly (European Commission, 2019m). This correlates with the level of employment in certain key sectors with higher (e.g. industry) or lower (e.g. agriculture) productivity levels. The Vest region is a good example of increased competitiveness, with a score of 20.9 in 2019. The Vest also had the highest increase in the number of people employed in growth areas such as ICT (though starting from a low base) ([55]) or professional and administrative activities ([56]). This is despite the same region also having areas with predominantly high polluting industries and low productivity rates (such as agriculture), thereby reducing the regional competitiveness and increasing the share of population at risk of poverty.

The urban-rural disparities create very high income and opportunity inequality across the population. The risk of poverty decreased in cities but remained relatively constant in rural areas, almost five times higher compared to cities. The average overall disposable income for a household member in urban areas is 1.9 times higher than in rural ones. In 2018, the share of NEETs among the young rural resident population (15-24) is almost three times that of those living in cities (18.1% compared to 7%). In 2017, of the total of registered unemployed, 71% were from rural areas. The proportion of early leavers from education and training in 2018 was 10.5 pps higher in rural areas than in town and suburbs and six times higher than in cities. More than half of the rural employed population is not covered by pension, unemployment or health insurance, despite their compulsory nature. Access to health care is especially poor and self-reported unmet needs for medical examination was twice as high as in urban areas and four times higher than the EU average.

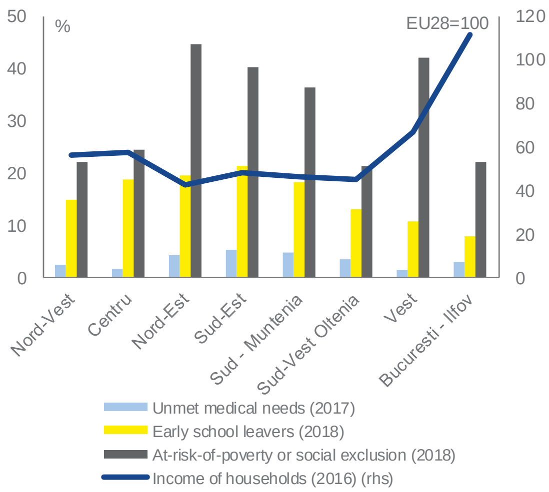
High regional and rural-urban disparities in social exclusion and poverty rates are not compensated for by the existing social services. While for the country as a whole 28% of the existing number of social services infrastructure units are currently provided for, the figure is only 26% for Sud-Est and 19% in Sud-Muntenia ([57]). The difference is even starker for certain types of social facilities, such as day centres for people with disabilities or addictions, where only 1% of

([55]) By 46% over the 2014-2018 period
([56]) By 21% over the 2014-2018 period
([57]) For visualisation and data, refer to local-social infrastructure map: https://portalgis.servicii-sociale.gov.ro/arcgis/home/

the required facilities exist in Sud-Vest Oltenia (compared to 56% in Bucuresti-Ilfov and 57% in Centru). Regions with the highest level of unmet medical needs (Sud-Est 5.3% and Sud-Muntenia 4.9%) also have below average levels of existing social services facilities.

Differences in regional social indicators are dampening the perspectives for future upward convergence. There is a high correlation between low household income and existing poverty rates on the one hand and low attainment in education on the other. The poor availability of jobs for the low skilled workers and the positive effect of higher value-chain businesses in economic development means that advanced skills are needed for the labour population to make a positive contribution to the upward convergence of regional disparities. The high number of early school leavers in poorer areas such as Sud-Est (21.3%) or Nord-Est (19.5%) however, and the very low level of adult upskilling opportunities, remain a significant problem (Graph 4.4.9).

Graph 4.4.9: **Social needs - income distribution per region**



Source: European Commission

Investment in productivity improvement is needed to escape the low competitiveness trap. Regions with significant shares of the workforce concentrated in low-productivity sectors are characterised by relatively low dynamics of business environment, low salaries and high poverty rates, which have a negative impact on social cohesion. Poorer regions in the country therefore risk being trapped in a negative feedback loop. Existing industries therefore need to increase productivity and higher-growth economic sectors need to build capacity. Education and upskilling can also make a positive contribution to improved competitiveness if market relevance is increased.

Lack of digital connectivity and adequate infrastructure further deepens the disparities between and within regions. Within regions, counties with low connectivity experience a low level of economic growth, whereas the counties with good connectivity combined with significant investment in infrastructure and high rates of foreign direct investment show a high level of economic growth as well as high levels of average salaries. In terms of internet use and activities, six of the eight Romanian regions are at the bottom of the EU ranking, with fewer than 60% of adults making daily use of the internet in 2018. The lowest shares are recorded in Sud-Est (46%) and Nord-Est (45%) (Eurostat, 2019a). The same applies in the case of the share of adults making use of e-government services, where Romania scores particularly low, with four regions performing very poorly, Vest (9%), Sud-Vest Oltenia (also 9%), Nord-Est (7%) and Sud-Est (3%).

In addition, urban-rural disparities also affect the development of Romania's digital economy and society, restraining the country's competitiveness. In terms of digital connectivity, in 2018, only 68% (EU average 81%) of households in rural areas of Romania had broadband access, compared to 80% (EU average 86%) in towns and suburbs and 89% in cities (Eurostat, 2019b). The same sharp divide between rural areas and the two other types of areas (mainly cities) applies to the internet access indicator, where Romania also has a lower overall level of internet access than the EU-28 average (Eurostat, 2019b). As far as digital skills are concerned, Romania displays a stark gap between city-dwellers and people living in rural areas. In 2017, this digital divide in overall skills reached 23 pps while the EU average is 14 pps (Eurostat Regional Yearbook, 2019).

To address the regional digital divide, EU Funds have been provided under the 2014-2020 financial framework. The Romanian Operational Programme for Competitiveness has earmarked €100 million from the European Regional Development Fund (ERDF), while the 2014-2020

Rural Development Operational Programme had initially provided for an indicative amount of €25 million from the European Agricultural Fund for Rural Development (EAFRD) under LEADER, of which less than €2 million were effectively allocated to broadband infrastructure measures. Under ERDF, in addition to the delayed RoNet project, a new grant scheme for next-generation networks (NGN) deployment, with a total estimated budget of €55 million, was set up to provide support to private operators deploying access infrastructure for additional localities in under-served areas. The project started in the first half of 2019 and results will only be visible in the medium-long term.

4.4.4. SINGLE MARKET INTEGRATION

Single market for goods and services

Romania is increasingly integrated into EU production chains. Romania attracts an increasing share of trade relating to EU value chains, particularly in manufacturing and business services. This integration has enabled market share gains to be achieved in the largest western countries (Germany, Italy, France), and a strong export performance overall since 2010.

The automotive cluster is particularly well integrated into EU supply chains. It also benefits from having many suppliers and component manufacturers working in joint ventures with foreign partners. Romania is already among the top five EU countries in terms of car manufacturing jobs, employing over 185,000 people and contributing to almost half of Romania’s exports. At the same time, the automotive industry is technologically mature and will undergo major changes (e.g. automation, smart and green mobility, new production and business models). Given its degree of integration into global value chains, significant investment in intangible assets such as R&D, digitalisation and skills would be required in order to maintain the country’s attractiveness as an automotive hub.

Removing barriers for service providers could stimulate investment. Cumbersome administrative procedures for setting up businesses (see Section 4.4.6) as well as regulatory requirements imposed on service providers, including regulated professions, limit market development. The level of restrictiveness in Romania is higher compared to the single market average for civil engineers, architects, accountants, and tourist guides. Removing these barriers could stimulate competition and investment, including in innovation, within the services sector.

A reform of the licensing system for services has been launched in 2019. The project ‘Comprehensive redesign of the licensing system in Romania’ is helping Romania to modernise its licensing system, strengthen the capacity of its licensing institutions and align the licensing system with international best practices. The project is funded by the European Commission’s Structural Reform Support Programmeand implemented by the OECD.

Market surveillance of the single market for goods is essential in order to protect consumers and ensure a level playing field for businesses. Responsibility for market surveillance of non-food products is spread over more than a dozen authorities, posing coordination and prioritisation challenges. In order to reduce the volume of non-compliant products imported from outside the EU, cooperation between market surveillance authorities should be reinforced, as well as cooperation between market surveillance and customs authorities. Limited financial resources have an impact on the ability to carry out product testing. The number of non-compliance findings shared with other Member States is low.

The weak performance of the transport sector hampers the transport connectivity of businesses with the rest of the single market. Businesses take the quality of transport services into account when making strategic decisions. Romania has low scores in accessibility and performance of road transport.

Energy market

Romania's potential as a producer and hub for natural gas needs to be underpinned by an appropriate, stable and predictable legal framework in line with EU law. The legislative measures introduced by emergency ordinances issued recently (Government Emergency Ordinance 114/2018 (2018) and Government Emergency Ordinance 19/2019 (2019i)) have had a negative impact on market functioning and could hamper investment in offshore-gas development in the Black Sea, to the detriment of Romania's and the region's supply security.

The lack of electricity interconnectors affects Romania's ability to participate in EU cross-border electricity trade. Romania remains less connected than the EU average, and unlike peers such as the Baltic region, it has not made progress in developing new electricity interconnectors. Cross-border exchange of electricity and gas are important cost- and CO2-savings. Connecting to EU markets can avoid unnecessary investment in backup generation, thereby avoiding emissions and costs (European Commission, 2019).

Collaborative economy

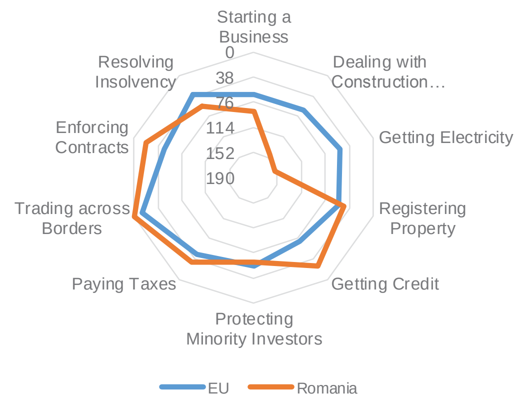
The collaborative economy has a strong growth potential. Romania has recently introduced requirements that are relevant to the collaborative economy in the field of accommodation and transport. The Tourism Act has been amended to introduce, inter alia, an obligation for providers of short-term rental accommodation to register with the competent local public administration, and to prohibit for platforms intermediating such services from publishing advertisements for unregistered accommodation structures. In the transport sector, an Emergency Ordinance (GEO 49/2019) establishing a licensing system for ride hailing transport services was adopted to regulate the use of alternative transport services. In 2018, the Romanian Competition Authority launched a study on the collaborative economy.

4.4.5. REGULATORY ENVIRONMENT AND INSTITUTIONAL QUALITY

Business environment

Romania's business environment could be further improved. Romania is ranked 55th in the World Bank's Doing Business 2020 report, indicating scope for further improvement particularly in electricity and construction permits, insolvency and protection of minority investors. However, performance is higher than the EU average for enforcing contracts, trading across borders and obtaining credit (Graph 4.4.10) but the performance varies significantly at sub-national level (World Bank, 2017).

Graph 4.4.10: **Ease of Doing Business (2019)**



Ranking: (1) easiest to (190) most difficult
Source: World Bank

Enhancing stability and predictability would help improve the business environment. The involvement of social partners, civil society organisations and other relevant stakeholders in public policy developments remains limited. A recent evaluation finalised by General Secretariat of the Government in 2019 the uneven application of the minimum rules for public consultations both at central and local level. Mandatory standardised procedures are to be developed, with the aim of increasing quality of public consultations (Government of Romania, 2018). The government adopted important initiatives with limited or no impact assessment and stakeholders' consultation. Impact assessments are not mandatory in the case of Emergency Ordinances, which reduces the legislative quality. The process and the criteria used for assessing the opportunity and quality of the Emergency Ordinances are not sufficient nor effective. The legislative agenda in Parliament is also very unpredictable. Despite efforts to improve the methodological guidelines of the Annual Working Government Plan, less than 30% of the Plan is implemented (Government of Romania, 2019a).

The lack of policy and legislative predictability has a negative effect on investment decisions. Survey data show that Romanian firms see uncertainty as regards policy and labour and business regulations as the main obstacles to long-term investment (EIB Investment Survey, 2019-

2020). An example is the change to the ex-ante control system performed by the National Agency for Public Procurement (ANAP) in 2019. The authorities unexpectedly reverted to the previous system and eliminated ex-ante controls for tenders co-financed by EU Funds launched since January 2019.

Protection of foreign investors has weakened in recent years. Several shortcomings regarding investor protection, in particular concerning the interactions between foreign investors and the state, have emerged in recent years. In this context, the lack of appropriate recognition of property rights (for instance, weaknesses regarding the enforcement of property rights on land) can have an unwarranted adverse impact on investor sentiment and cross-border investment projects.

Judicial reform and the fight against corruption

Concerns of negative impacts on the justice system and its capacity to investigate high-level corruption remain as long as Romania does not take corrective measures. Important legal modifications and political pressure on the judiciary in 2017, 2018 and in the largest part of 2019 have affected the efficiency, quality, independence of the justice system and its capacity to investigate and sanction high-level corruption. (CVM report 2019**).** The implementation of the amended justice laws since October 2018 confirmed the risks that a number of measures were damaging to the judiciary. Several Government Emergency Ordinances further amending the justice laws in 2019 have increased these concerns. The operation of the special prosecutor section for the investigation of offences committed by magistrates which was set up end of 2018 following the amendments of the justice laws has confirmed the concerns expressed by the Commission, the Venice Commission and GRECO that the section could be politically influenced to change the course of high-level corruption cases (European Commission, 2019l). In this context, on 27 of December 2019, the Government adopted a Memorandum, in which it supports the solution of abolishing the Special Section. The entry into force of provisions which would particularly affect the human resources of the justice system on early retirement, the initial training period and the number of judges on panels, was delayed for two more years to January 2022 and January 2021 respectively. While the current Government has stated its commitment to repair the damages to the justice system created by the amendments to the justice laws, further corrective legislative measures have not yet been adopted.

Romania continues to make efforts to improve the enforcement of court decisions. In April 2019, the Government approved a memorandum on ‘measures to ensure the execution of judgments against a public debtor, in accordance with the case law of the European Court of Human Rights regarding non-execution or execution with delay of the judgments handed down against a public debtor’. The IT application which will be used to identify the number of final court decisions in which public institutions are debtors or creditors is in its last stages of development.

Corruption continues to be major problem for the business environment in Romania. A 2019 business Eurobarometer survey shows that 88% of businesses consider corruption to be a serious problem for their company when doing business in Romania. Since 2013, the share of companies that perceive corruption as a problem increased in Romania by 23 pps, the largest increase in the EU and in stark contrast with the EU average which continued to decrease (now at 37%). Overall 97% of businesses think that corruption is widespread in Romania and 87% say it is widespread in public procurement managed by national authorities. On a more positive note, 50% of respondents think that those engaged in corruption would be caught by police and 43% think that those caught for bribing a senior official receive appropriate sanctions, both higher than the EU average. Romania’s scores on the control of corruption index of the World Governance Indicators and the Corruption Perception Index of Transparency international have also continued to decrease, from the 55th to the 52nd percentile rank in 2018 (World Bank, 2019) and from 47 to 44 points respectively.

The implementation of the national anti-corruption strategy is progressing at technical level, the credibility and impact of the process requires renewed political commitment. Corruption prevention measures such as the internal audits by each of the participating public institutions and the peer review evaluation missions planned in 2018 were put in motion, both in central institutions and at local level (90 municipalities and county councils were evaluated between April - November 2019). The inter-institutional cooperation platforms met in April, June and November 2019. The authorities also report continued corruption prevention measures and activities in central ministries and public institutions in priority areas.

Amendments to the legal framework for conflicts of interests and incompatibilities could affect the capacity of the National Integirty Agency to impose sanctions. In the last two and a half years five legislative proposals modifying the integrity laws have been adopted. In particular one amendment sets a prescription deadline of three years for the deeds that determine the existence of the state of conflict of interests or incompatibility. While a number of investigations had to be closed, it is unclear whether a sanction can still be applied after a final court decision, if it is only issued after the end of the three years prescription period. Another amendment modified the list of applicable administrative sanctions for locally elected officials found in conflict of interests. (European Commission, 2019f).

Corporate governance of state-owned enterprises

The performance of state-owned enterprises is deteriorating. The operational and financial results of state-owned enterprises declined substantially in 2018 and the first half of 2019. Aggregate profits, at RON 3.5 billion in 2018, decreased by 53% compared to 2017 (Government of Romania, 2019b), according to Ministry of Finance data. In particular, companies in the energy and transport sectors contribute to this situation. Arrears are also increasing again, having reached RON 4.4 billion (c. €932 million) at the end of 2018, 11% higher than in December 2017.

The deterioration of corporate governance contributes to poor performance. Romania has a very solid corporate governance framework for state-owned enterprises (European Commission, 2017a), but its implementation has been limited (European Commission 2018a, 2019a). Loss-making companies are not asked to restructure or modify their business plans. Debts to the State budget, social security or other state-owned enterprises amount to 90% of all arrears by state-owned enterprises, which represents a financial risk for the state but also demonstrates a permissive attitude from public sector suppliers and creditors. Interim boards and managers became a standard practice in most companies. The authorities applied 60 financial penalties for administrative offences under the corporate governance legislation, but the amounts tend to be symbolic. Furthermore, different Ministries and departments involved in overseeing state-owned enterprises seem to disagree increasingly on the respective responsibilities, despite clear allocations under the law.

The future of the Sovereign Development and Investment Fund is unclear. The creation of the Fund was announced in 2017 (European Commission, 2018a). It should receive the state's shares in some 30 state-owned enterprises to boost investment, but with unclear objectives or strategy. A first law was approved in spring 2018 but rejected by the Constitutional Court (European Commission, 2019a). In November 2018, the government addressed the Court's concerns and adopted framework legislation. It accelerated the assessment of how to create the Fund outside the budget perimeter but plans are unclear.

Public administration and quality of institutions

Results of the reform of the public administration system are not yet visible. Legislative and procedural steps in several areas will require time and active political involvement in order to produce the expected results. EU funded projects aim to reform human resource management, the regulatory impact assessment system and strategic planning of public institutions (see below). Legislation setting up the Council for Human Resources was adopted by Law 69/2019 (Parliament of Romania, 2019) and steps are being taken to make it operational as of January 2020. The relevant legal framework for reforming national competitions for civil servants and other areas of the central administration was adopted by Government of Romania Emergency Ordinance 57/2019.

Frequent reorganisations and overuse of temporary management positions hamper independence and trust in the administration. Since 2014, the number of civil service functions has been increasing both at central and local level, with no clear strategy and not in line with the decentralisation of competences to the local level. At the same time, the share of vacant positions remains high. Frequent reorganisations of public structures illustrate a significant degree of instability. Moreover, the sector faces significant ageing challenges, as 78.5% of all staff is more than 40 years old. The situation improved only marginally with the increase in public sector wages, showing that complementary measures or a more predictable career path is needed.

The quality of public consultations and regulatory impact assessments remain a challenge. The General Secretariat of the Government has started to monitor the quality of regulations. A public report should be available for the first time in spring 2020. The quality and effective use of regulatory impact assessments and public consultations vary significantly, with no legal institutional framework for quality control at governmental level. Options for setting-up an independent Regulatory Impact Assessment Board are currently being assessed. Several projects are ongoing to reinforce the methodology and tools for regulatory impact assessments and to increase expertise across the central public administration. Public consultations are generally perceived as formal and of low quality, and the involvement of social partners and other relevant stakeholders is limited. In March 2019, a new version of the online platform for public consultations was launched, which should facilitate interactions between authorities and relevant stakeholders.

Efforts continue to improve transparency of the public administration, with weaker results at the local level. Under the Open Government Partnership (OGP), Romania is implementing a new National Action Plan (2018-2020) (Government of Romania, 2018). The Romanian OGP website was re-launched in order to provide transparent monitoring. Further efforts to continue improving transparency both at central and local levels are partly supported by EU funds (Government of Romania, 2019a). In this context, eight briefing sessions were organised in various cities, attended by relevant stakeholders. A slightly positive trend can be observed in some central authorities, but progress by local authorities has been more limited. Better quality, transparency and access to information, would encourage citizens to become involved in the decision-making process and improve oversight of public policies.

The development of an effective framework for strategic and budgetary planning has stalled. The revision of the relevant legislative framework has stalled since 2017 (Government of Romania, 2019a). This framework would establish a stronger link between the Strategic Programmes of the central public institution and the annual budgetary allocations and would have the potential to increase the quality of public spending. The changes are also necessary in order to clarify the institutional coordination mechanism and responsibilities of relevant public institutions. Furthermore, the strategic management role of the General Secretariat of the Government is still to be consolidated. National Strategic Programmes in different sectors report a lack of funding of ongoing measures, also due to the lack of a multi-annual budgeting approach. EU funds continue to support the central and local administrations in strengthening their strategic planning capacity, but results remain fragmented.

Public service delivery

Decentralisation of public services hampers their availability and quality, especially at local level and for poor communities. Little progress has been achieved since the start of the decentralisation process. An updated calendar was discussed by the Government in June 2019 (Ministry of Regional Development and Public Administration, 2019) to speed up the adoption of sectoral legislations for decentralisation, and for the finalisation and adoption of the quality and cost standards developed for a number of public services. As cost and quality standards are not yet in place, these services are still under-financed, with very limited opportunities for further development.

Fragmentation of competencies and resources continue to affect the delivery of public services. National and regional strategies are not well translated into integrated measures at regional and local level. Funding of public services is uneven across regions and territorial administrative units and does not take into account regional disparities and local needs. Public and private social service providers continue to compete for very limited public funding.

The fiscal decentralisation process is slow. The revenue of local administrations continues to lack stability and predictability, in a context of increasing competencies and demand for services at local level. The capacity of local authorities to increase the share of their own resources remains limited. The adoption of the Code for Local Public Finances has repeatedly been postponed (Government of Romania, 2019a). The low level and unpredictability of the local administrations' budgets have contributed to the lack of services in some areas or their low-quality service delivery.

The limited capacity of the public administration hinders development. Insufficient administrative capacity to deliver quality public services (including digital) and red tape are an obstacle for business and citizens, and thus for social and economic development. The implementation of simplification measures for citizens is delayed due to bottlenecks at central level and to the low interest of local communities in addressing the situation. There is a low level of contracting and implementation of EU funds available for simplification measures for local level administration via the Administrative Capacity Operational Program.

eGovernment

Despite progress, there is considerable scope for improvement in digital public services. Overall, Romania still ranks low in this respect. There are low scores for pre-filled forms and online service completion, which could indicate a systemic problem with the quality and usability of the services offered (European Commission, 2019g).

The national administration's fragmented IT system represents an administrative burden for citizens and businesses. Interoperability between public administration services is generally low, as each public institution has developed its own digital public service. As a result, it is unclear how much information, once submitted, is then re-used by other institutions. The government decided to establish a National Interoperability Framework, based on the European Interoperability Framework, but work still needs to take off. A proposal for an Interoperability Law has been submitted to Parliament discussion in order to create a more mandatory framework for future public digitalisation projects and to provide for a body of expertise that will be made available in order to ensure effective interoperability.

As of 2018, the eDelivery Access Point is operational. This will contribute to achieving compliance with the Electronic Identification, Authentication and Trust Services (eIDAS) Regulation and will support the implementation of access points for other service, such as e-invoicing, transportation, environment, health, e-tendering or e-justice. The eIDAS node of Romania is still in the process of being built through an ERDF financed project (acronym 'SITUE'), expected to be finalised by the end of 2020.

A new Centre for Financial Information allows electronic interaction with taxpayers. The centre was redesigned and simplified in 2018 and is now available via the Single Contact Point. It allows the government to communicate electronically with taxpayers and tax declarations to be submitted online. The Virtual Private Space is the system for management of citizens' declarations and tax liabilities, where payment obligations are established, but it does not include a payment module.

Several central and local authorities provide simplified procedures via the Single Contact Point. The documentation is available online but not all procedures can be completed online. The Ministry of Health has simplified its procedures so that the approval and correction of medicine prices can be sent electronically and communication to operators can take place online. However, projects such as the Disease Registry Project have stalled. The National Office Trade Register has implemented the online registration process for new companies. The simplified registration has a response time of a maximum three working days. The National Office Trade Register now provides 30 digital public services.

Public procurement

The implementation of the national public procurement strategy is progressing. The new e-procurement system (i.e. SICAP) has laid the foundation for more transparency in the procurement process. Accurate maintenance and a further fine-tuning of its functionalities are essential for ensuring a continuous and full exploitation of the system. The adoption of an ambitious professionalisation plan is in line with the objectives of the National Public Procurement Strategy. However, duly prioritising and effectively addressing the main shortcomings of the public procurement system, including with respect to promoting green and socially responsible procurement, will be crucial for the successful implementation of the strategy set to start in early 2020.

Other reform commitments to improve public procurement were stopped or even reversed. Changes to the ex-ante control mechanism by reducing the sample and introducing voluntary checks, trigger significant risks in terms of the efficiency and the effective implementation of EU funds. Without prior public consultations or relevant impact assessments, these legislative changes confirm the persistent unpredictability and lack of confidence in the decision-making process. This is also reflected in the ambitious number of public-private partnership (PPP) projects included in the list of strategic investment projects, while contracting authorities clearly lack expertise in this field. The changes to the legal framework regulating institutional responsibilities for PPPs have added a further layer of uncertainty.

There is still a need to further enhance administrative capacity in public procurement. The newly functional Centralised Public Procurement Body (ONAC) is yet to build-up its human resources as well as technical and professional capacities. ONAC has only limited institutional experience in the centralised procurement of simple products subject to demand aggregation. A number of legislative changes will expand its competence to health sector products, thus adding further complex challenges to the efficient functioning of the newly set institution.

The National Integrity Agency investigates incompatibilities and administrative conflicts of interests. The PREVENT system for systematic ex-ante checks of conflicts of interests is now fully operational and the National Integrity Agency reported positive results. However, the stability of the legal framework on integrity continues to face challenges.

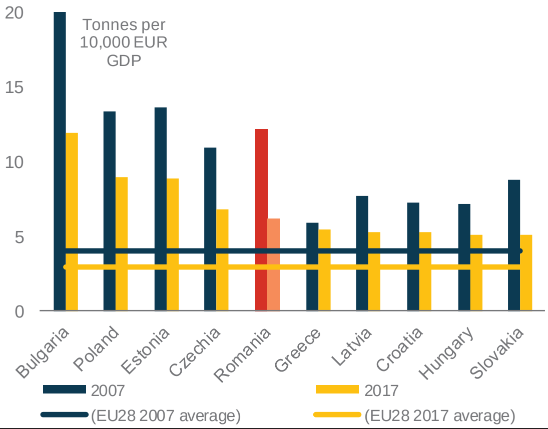
4.5. ENVIRONMENTAL SUSTAINABILITY

Combining economic prosperity with environmental sustainability is a key challenge for Romania. Since joining the EU, Romania has made substantial progress in raising living standards. However, further economic growth should help reduce the still significant gap with the EU average. At the same time, Romania, like the entire EU, is facing climate change and environmental degradation. Such dual challenges require coherent policies in order to ensure sustainable development.

The greater frequency of extreme weather events already caused material damage in recent times. Over the last two decades, Romania has been affected by severe inland and coastal floods and droughts possibly linked to climate change. Romania is amongst the EU countries most subject to large flooding events, and about 13% of the country lies in floodplains. Between 2002 and 2012, Romania had one of the highest number of fatalities in the EU due to flooding and the largest number of houses damaged, with an estimated total direct costs of €3.6 billion. Future floods management investments identified in the Flood Risks Management Plans are approximately €3.7 billion. In the absence of climate change policies, the climate is set to change considerably over the next 50 to 100 years leading to an estimated 8-10% loss in GDP per capita in Romania by 2100.

Meanwhile, the production of goods and services is carbon and energy intensive. Although Romania has among the lowest greenhouse gas emissions (GHG) per person in the EU, the country has some of the highest rates of carbon intensity (Graph 4.5.1). Without changing production patterns, economic growth is likely to result in continued, or possibly greater GHG emissions.

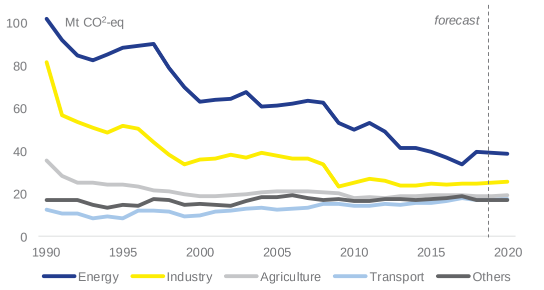
Graph 4.5.1: **EU highest GHG emissions per GDP in 2017**



Source: European Commission

Despite a high share of renewable energy, energy supply remains the most significant source of GHG emissions. Installed capacity for renewable energy sources (RES) has increased significantly over the last decade. In 2017, the share of RES in overall energy consumption was 24.5%, above the EU average. While this resulted in falling emissions from energy supply, the sector still accounted for 30% of all GHG emissions in 2017 (Graph 4.5.2).

Graph 4.5.2: **GHG emissions in Romania by sector**



(1) Mt CO2-eq = Metric tonnes of CO2 - equivalent
Source: European Commission

Moreover, several industrial sectors contribute significantly to emissions. Transport, agriculture and manufacturing show a somewhat rising trend (Graph 4.5.2). The agricultural sector accounts for 17% of total emissions. Transport in Romania produced 24.7% of total CO2 emissions and 16.6% of GHG emissions in 2017 (European Commission, 2019m), well below the EU average. In particular, road transport accounted for over 90% of total transport CO2 and GHG emissions in the country. The industry sector, in addition to

GHG, also contributes to water emissions and waste generation.

Energy remains also the main air-polluting sector. Restructuring energy and domestic heating systems (by facilitating district heating and pollution controls, switching to gas and integrating renewables) as well as traffic and other pollution and prevention control measures could help significantly in addressing air quality.

Air pollution continues to have significant health impacts. The latest data on the health impact of fine particulate matter (EEA 2019 Report on Air Quality in Europe) shows that, in Romania, around 1,8 years of life lost per 1,000 inhabitants in 2016 were attributable to exposure to fine particulate matter, the fourth highest in the EU. In 2017, the limit value for nitrogen dioxide was exceeded in five out of 54 air quality zones, of the limit value for particulate matter in four and of the limit value for fine particulate matter in two. Air quality data measured by the Romanian Monitoring Network also indicate serious and structural shortcomings.

Intensive illegal logging of Romanian forests is a recurrent problem, leading to a reduction of the natural carbon sink of forests, a significant loss of biodiversity, an increase in disaster risks, and an economic loss of around 6 billion EUR/year. Romanian forests and woodland have a substantial CO_2 uptake, estimated at 25,444,000 tonnes (on the basis of the LULUCF Inventory), which represents 6% of the total forest and woodland CO_2 uptake at EU level (JRC, 2019). Illegal logging amounted for about 20 million m3/year during the period 2013-2018, roughly the same volume of wood that is officially cut in Romania. These activities not only endanger biodiversity and jobs, they also remove a natural means for protecting against flooding and for capturing CO_2. A reform in the forestry sector needs to be carried out as soon as possible, starting with the update of SUMAL, the revision of the Forest Code in order to be full in line with the provision of the EU Nature laws, enhancing the administrative capacity of Romsilva, especially with regards to its control bodies and also transparency in relation to forests activities.

Romania is on track to meet its 2020 targets, but is set to miss the 2030 targets. Romania can increase GHG emissions not covered by the EU Emissions Trading System (ETS) by a maximum of 19% by 2020 compared to 2005 levels. According to preliminary estimates, these emissions decreased by 2% between 2005 and 2018 and are projected to increase by 1% between 2005 and 2020. The target is thus expected to be met by a margin of 18 pps. The 2030 target — a 2% decrease compared to 2005 levels — is set to be missed by a margin of 12%. Emissions are projected to increase above the base year: by 10% under current measures and by 6% with just the additional measures announced being implemented.

The targets for the draft National Energy and Climate Plan show a level of ambition which needs increasing if Romania is to meet its 2030 targets. At the end of 2018, Romania submitted its draft National Energy and Climate Plan (NECP)[58] to the European Commission. The document provides a comprehensive summary on the energy systems and sets national targets for 2030 for greenhouse gas reduction and RES. It is intended to reduce the GHG emissions of the agricultural sector mainly through knowledge transfer and advisory services and investment support for farm modernisation. The proposed RES target in 2030 is just 27.9%. This is far below the country's potential cost-efficient development of RES and also well below the collective EU target of 32% (Draft NECP, 2018).

Romania has a diverse energy mix, with a sizeable percentage of renewable energy. There are no subsidies/incentives for fossil fuels in transport and energy production. Starting with 2011, subsidies were granted for the closure of uncompetitive coal mines, according to Council Decision 787/2010 of 10 December 2010 on State aid to facilitate the closure of uncompetitive coal mines. However, authorities acknowledge the need for a better distribution between fossil and alternative fuels as well as the need to gradually reduce the share of coal and eliminate the subsidies for fossil fuels in energy production and transport.

Romanian power generation companies will still receive free allocation to comply with the Emissions Trading System for 2021-2030.

[58] Romania has not yet submitted the final National Energy and Climate Plan to the Commission

Following the ETS revision of 2017, the Romanian power generators are not under the same pressure as others in Europe to seek efficiency gains. It is however still unclear how this will be compensated by other pricing mechanisms to incentivise the decarbonisation of the power sector.

The building sector has a central role to play in achieving the energy efficiency and climate targets for 2030. The energy consumption in the household sector and the tertiary sector (offices, business premises and other non-residential buildings) represents 45% of the total final energy consumption in Romania (European Commission, 2017). About 53% of residential buildings were built before 1970 and over 90% before 1989, all with poor energy performance. However, an ambitious long-term renovation strategy and by strengthening the implementation of the existing provisions, would support the building sector. The National Programme on Increasing Energy Efficiency in Residential Blocks, which already resulted in over 70000 apartments for which the thermic rehabilitation has been finalised throughout the country, has been extended for the period 2019-2020 with a total allocated budget of €10.4 million for a three-year period. Further measures are still needed in order to address the low energy performance of buildings and stimulate old-building renovation.

New vehicle sales of passenger cars increased by over 22% between 2017 and 2018, and registrations of goods vehicles increased by over 10% (European Commission, 2019m). With more road vehicles used, alternative fuels have to play a greater role to reduce the sector's environmental footprint. In 2018, Romania submitted its National Policy Framework for Alternative Fuels to the European Commission. The country has established targets for most mandatory fuels and modes established targets, but the framework does not contain one for liquefied natural gas refuelling points to be put in place along the road TEN-T Core Network for heavy-duty vehicles.

Other measures are in place to support the uptake of alternative fuels, but there is still a long way to go. Two scrapping programmes will support the reduction of car emissions. Initial financial allocations for both were approximately of €65 million, later increased by €36 million, as a result of the high level of interest in the programmes. In 2018, a new programme was launched to expand the charging infrastructure for electric cars in municipalities. Further measures include battery and plug-in hybrid electric vehicle purchase subsidies, registration and ownership tax reductions and infrastructure incentives. European grants from the Connecting Europe Facility were also allocated to developing a multi-standard open-access fast-charging network along core network corridors. However, the high cost of alternative-fuel vehicles, which only represented 1.7% of the overall new car sales in 2018, and lack of appropriate infrastructure, hinders their growth.

A successful transition will require additional investments in energy infrastructure. The draft NECP points to an investment need of €22 billion in the period 2021-2030 in the energy sector alone. Investments in the period 2025-2030, based on planned measures, represent an increase of 47% compared to investments based on existing measures, and most of the investments (82%) need to be channelled to satisfy demand, which is forecast to grow significantly as a result of economic growth.

Given the challenge of achieving sustainable growth, a coherent and operational strategy could provide support. The shift to a low carbon economy might lead to an increase the unemployment rate especially in regions with low-productivity carbon-intensive industries. It would also boost labour market demand for medium and high-skilled workers in different sectors, including in the renewable energy sector. In the affected regions, the current lack of integrated social services together with weak re-skilling and upskilling delivery mechanisms is also likely to contribute to an increase the number of persons at risk of poverty as well as deepen regional disparities. Against this backdrop, a coherent strategy covering the different dimensions of this transition could identify the instruments needed to mitigate the negative effects, while also identifying opportunities and synergies.

The Just Transition Fund could support the diversification of the economy towards low-carbon intensive activities. Romania still relies heavily on coal for energy production. Coal mining and the respective power plants are mainly concentrated in the Hunedoara and Gorj counties.

Moreover, energy intensive manufacturing and heavy industries are present in the Dolj, Galați, Prahova and Mureş counties. Phasing out these sectors would have a significant negative socio-economic impact on the regions and local communities. Efforts are already under way: in 2018, the Jiu Valley became part of the Commission's Coal Regions in Transition initiative ([59]) and a strategy is under way for the transition away from coal, with technical support from the EU (pwc, 2019). By means of the Just Transition Fund these efforts can be extended to all regions and areas concerned and ultimately mitigate these transition shocks via the necessary reconversion and modernisation efforts. Dedicated investment guidance for the Just Transition Fund is provided in Annex D.

([59]) It led to a first stocktaking of needs and opportunities and the tentative flagging of possible further initiatives.

ANNEX A: OVERVIEW TABLE

Commitments	**Summary assessment** ([1])
2019 country-specific recommendations (CSRs)	
CSR 1: Ensure compliance with the Council recommendation of 14 June 2019 with a view to correcting the significant deviation from the adjustment path toward the medium-term budgetary objective. Ensure the full application of the fiscal framework. Strengthen tax compliance and collection.	Romania has made **limited progress** in addressing CSR 1
Ensure compliance with the Council recommendation of 14 June 2019 with a view to correcting the significant deviation from the adjustment path toward the medium-term budgetary objective.	Compliance with the Stability and Growth Pact is outside the scope of assessment of the Country Specific Recommendations in the Country Report.
Ensure the full application of the fiscal framework.	**No progress**. As in previous years, the national fiscal framework has not been respected. The fiscal rules laid down in the Fiscal Responsibility Law “remained inoperable” with respect to the 2019 and 2020 budgetary laws, as the authorities continued its practice of derogating from them (Fiscal Council 2019a and 2019d). In particular, the 2019 budget target of a headline deficit of 2.76% of GDP was inconsistent with the structural deficit rule. Budget amendments adopted in August and November 2019 also derogated from a number of rules, in particular, in the latter case, by increasing the 2019 deficit target to 4.4% of GDP (Fiscal Council, 2019c). Moreover, as in previous years, the authorities did not send an update of the medium-term fiscal strategy to Parliament by the statutory August deadline, thereby undermining its guiding role. The 2020 budget and the accompanying fiscal strategy also derogated from several fiscal rules, in particular by targeting a headline deficit of 3.6% of GDP (Fiscal Council, 2019d and 2019e).
Strengthen tax compliance and collection.	**Limited progress**. Compliance ratios for filing tax declarations have remained relatively stable. The VAT gap is estimated to have dropped marginally from 35.9% in 2016 to 35.5% in 2017 and, according to preliminary estimates, to have fallen to 32% in 2018. However, it still is among the highest in the EU. The National Agency for Fiscal Administration did not meet its revenue collection targets for 2019, partially because of an over-optimistic prognosis of these targets.

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CSR 2: Safeguard financial stability and the robustness of the banking sector. Ensure the sustainability of the public pension system and the long-term viability of the second pillar pension funds.	Romania has made **some progress** in addressing CSR 2
Safeguard financial stability and the robustness of the banking sector.	**Substantial progress.** The bank tax on total assets introduced by Government Emergency Ordinance 114/2018 was removed starting from the beginning of 2020.
Ensure the sustainability of the public pension system and	**No progress.** Fiscal sustainability indicators point to high risks. Due to a high structural primary deficit (which is driven by the significant pension increases contained in the new pension law of summer 2019), and assuming no-policy change, the debt-to-GDP ratio is set on a fast increasing and upward path. It is projected to rise from 35% in 2018 to beyond the 90% of GDP by 2030. The medium-term sustainability gap indicator ('S1') nearly quadrupled with respect to last year and is now among the highest in the EU. This means that Romania would require a significant fiscal adjustment to achieve the debt target of 60% of GDP in 2034. The long-term fiscal sustainability indicator ('S2'), points to a required fiscal adjustment of 8.8 pps of GDP in order to ensure that the public debt ratio stabilises over the long term. This value, one of the highest among EU countries, is driven by the initial budgetary position (a contribution of 5.1 pps of GDP) and ageing costs, in particular pensions and health care (a contribution of 3.7 pps of GDP). Both items are driven by the new pension law.
the long-term viability of the second pillar pension funds.	**Some progress.** Several provisions of GEO 114/2018 that threatened the long term viability of the second pension pillar were repealed or amended at the beginning of 2020. Thus, the possibility of opting out of the second pension pillar after a contributory period of 5 years was eliminated and the increased minimum capital requirements were eliminated. Also, the significant reduction of the administrative fees that second pension pillar fund management companies can charge was reversed. These administration fees were even further modified, but without prior impact assessment consulted with all relevant stakeholders.

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CSR 3: Improve the quality and inclusiveness of education, in particular for Roma and other disadvantaged groups. Improve skills, including digital, notably by increasing the labour market relevance of vocational education and training and higher education. Increase the coverage and quality of social services and complete the minimum inclusion income reform. Improve the functioning of social dialogue. Ensure minimum wage setting based on objective criteria, consistent with job creation and competitiveness. Improve access to and cost-efficiency of healthcare, including through the shift to outpatient care.	Romania has made **limited progress** in addressing CSR 3
Improve the quality and inclusiveness of education, in particular for Roma and other disadvantaged groups.	**Limited progress.** Challenges of quality and inclusiveness of education persist, in particular , in particular in rural areas and for Roma and other disadvantaged groups, with consistent low educational outcomes and high rates of early school leaving. Some reforms are underway but their implementation is delayed and results are yet to be seen.
Improve skills, including digital, notably by increasing the labour market relevance of vocational education and training and higher education.	**No progress**. Urgent measures are needed to address problems with the acquisition of basic skills at school and improve the digital literacy of the population. The percentage of young people who assess their digital skills as low is the highest in the EU (41% vs 14% EU average). Students enrolled in VET programs have limited exposure to work-based learning. The low labour market relevance of vocational education and training and higher education has a negative impact on graduates' job prospects (69% of VET graduates are employed vs 79.5% EU average). The ESF is supporting efforts to increase the relevance of VET, but a comprehensive reform is lacking.
Increase the coverage and quality of social services	Limited **p**rogress. The social reference index, used as a basis for most social benefits, has not been updated since its introduction in 2008. Progress in the provision of social services remains insufficient, in particular in rural areas. Misalignment between decentralization of social services and financial means increased further in 2019, with a negative impact on the effectiveness and quality of service delivery at local level and for poor communities. The EU co-funded pilot project to introduce integrated teams at community level is under implementation with the first visible results expected in 2020.

Complete the minimum inclusion income reform.	**No progress.** The implementation of the minimum inclusion income has been again postponed to 2021.
Improve the functioning of social dialogue.	**Limited progress.** The involvement of social partners in policymaking remains limited. Despite the established framework, this remains rather a procedural requirement than a genuine dialogue. The authorities report increased rates of collective bargaining coverage (45% in 2019). This could result from collective bargaining becoming temporarily mandatory for all employers, following the shift of social security contributions in 2017. However, the situation of collective bargaining at sector level has not changed. Discussions on changes to the legislative framework and the revision of sectors have stalled.
Ensure minimum wage setting based on objective criteria, consistent with job creation and competitiveness.	**Limited progress.** According to the authorities, the increase in the minimum wage as of 1 January 2020 was based on a formula taking several economic indicators into account, such as the inflation rate and labour productivity. The decision was preceded by discussions with the trade unions and employers' organisations. However, an objective mechanism is not yet in place.
Improve access to and cost-efficiency of healthcare, including through the shift to outpatient care.	**Limited progress.** There has been limited progress in improving access to healthcare. Unmet needs for medical examination reported by patients are high and increasing again. A sustained policy of incentivising healthcare delivered outside of hospital inpatient settings by the National Insurance House may trigger a natural shift towards ambulatory care. The overall policy measures of the Romanian health system to facilitate this shift did not improve.
CSR 4: Focus investment-related economic policy on transport, notably on its sustainability, low carbon energy and energy efficiency, environmental infrastructure as well as innovation, taking into account regional disparities. Improve preparation and prioritisation of large projects and accelerate their implementation. Improve the efficiency of public procurement and ensure full and sustainable implementation of the national public procurement strategy.	Romania has made **limited progress** in addressing CSR 4

Focus investment-related economic policy on transport, notably on its sustainability, low carbon energy and energy efficiency, environmental infrastructure as well as innovation, taking into account regional disparities.	**Limited progress.** Limited progress was made in drafting feasibility studies for upgrading railway infrastructure, and work is lagging considerably behind. This is mostly due to a lack of administrative capacity and inefficient procurement procedures. European grants have been allocated to develop a multi-standard open-access fast charging network along the TEN-T core network corridors. However, no projects are planned so far to ensure alternative clean fuel supply facilities in ports. There has been some progress in environmental infrastructure investment, especially in waste water projects, and the implementation of projects accelerated towards the end of 2019. In other areas, progress is more limited, particularly for waste projects. With regard to nature/biodiversity and air projects there has been no real progress, even though funds are available. No progress was made on research and innovation. Reported official measures are insufficient to address both the under-financing of R&I and the structural problems in the public science base and R&D private sector. Without a significant increase in the public R&D budget plus related regulatory measures to increase R&D quality and innovation, little progress is expected.
Improve preparation and prioritisation of large projects and accelerate their implementation.	**Limited progress.** In the twin context of the current EU cohesion policy funds implementation and the preparation of the next programming period (2021-2027), the Romanian authorities have started to speed up the implementation of large projects and have submitted to the Commission a number of projects in fields such as transport, health and wastewater management. However, the Fiscal Strategy 2020-2022 adopted in December 2019 contains low levels of planned capital expenditure and of planned spending on projects co-financed by the EU.

Improve the efficiency of public procurement and ensure full and sustainable implementation of the national public procurement strategy.	**Some progress.** While some progress in the implementation of certain commitments under the national public procurement strategy has been made, others were stopped or even reversed. The new e-procurement system, the adoption of an ambitious national professionalisation strategy as well as the newly functional centralised public procurement body (ONAC) are positive examples. However, the changes to the ex-ante control mechanism create significant risks in terms of the efficiency and implementation of EU funds. Moreover, the persistent unpredictability of the legislative changes in the public procurement field, made without prior public consultations and relevant impact assessments, reinforces the lack of confidence in the public procurement system and ultimately affects its efficiency.
CSR 5: Ensure that legislative initiatives do not undermine legal certainty by improving the quality and predictability of decision-making, including by appropriate stakeholder consultations, effective impact assessments and streamlined administrative procedures. Strengthen the corporate governance of state-owned enterprises.	Romania has made **no progress** in addressing CSR 5
Ensure that legislative initiatives do not undermine legal certainty by improving the quality and predictability of decision-making, including by appropriate stakeholder consultations, effective impact assessments and streamlined administrative procedures.	**No progress.** Predictability of decision making remains a concern, with no tangible progress. Less than 30% of the annual government plan is respected and the number of emergency ordinances is still very high, with some having major socio-economic impact (Ex. GEO 114/2018). There is no mandatory ex-ante impact assessment for emergency ordinances and no requirement for public consultations. The quality and effective use of ex-ante regulatory impact assessments continue to vary significantly, with no legal institutional framework for a quality control function at governmental level. Moreover, although different formal structures exist, the quality of public consultations is deteriorating. Public consultations are generally perceived as formal and of low quality, and the involvement of social partners and other relevant stakeholders is limited. Social partners and other relevant stakeholders report not being adequately consulted. However, several EU funded projects are ongoing to reinforce the methodology and tools for regulatory impact assessments and to increase know-how across the central public administration. In March 2019, a new version of the online platform for public consultations was launched to facilitate interactions between authorities and relevant stakeholders. Important legislation amending

	government emergency ordinance 114/2018 was adopted in the first half of the year without impact assessment and proper stakeholder consultation.
Strengthen the corporate governance of state-owned enterprises.	**No progress.** The corporate governance law is still only loosely applied. The appointment of interim boards has become a standard practice. The financial penalties applied for administrative offences are symbolic and do not have the power to change the overall behaviour. The operational and financial results of most state-owned enterprises deteriorated in 2019.

Europe 2020 (national targets and progress)	
Employment rate target set in the NRP: 70 %.	The national target is considered to have been already achieved, as the employment rate in the age group 20-64 is at 70.5% in Q2-2019, showing a steady increase over recent years.
R&D target set in the NRP: 2 % of GDP	Romania will not achieve the R&D intensity target by 2020. The country's R&D intensity in 2018 was only 0.51% of GDP, thus ranking last in the EU. The country has consistently ranked at the bottom of the EU in recent years. Public expenditure on R&D has continuously fallen since 2011 from 0.32% of GDP to 0.20% in 2018. On the other hand, business enterprise expenditure on R&D (BERD) has increased from 0.12% of GDP in 2013 to 0.30% in 2018. EU-funded investments in R&D infrastructure are slowly taking off, but they are unlikely to address the chronic under-funding of the research and innovation system.
National greenhouse gas (GHG) emissions target: - 19 % in 2020 compared with 2005 (in sectors not included in the EU emissions trading scheme)	Romania is on track to meet its target. According to preliminary estimates, GHG emissions decreased by 2% between 2005 and 2018 and are projected to increase by 1% between 2005 and 2020. The target is thus expected to be met with a margin of 18 pps.
2020 renewable energy target: 24 %	With 24.8% renewable energy share in gross final consumption, Romania is on track in attaining its renewable energy target for 2020. Emergency Ordinance No 24/2017 was approved by Law 184/2018, and introduced amendments to the renewable energy support scheme, providing support to promoting renewable energy in a sustainable manner while ensuring a reasonable consumer impact. This approach aims to bring the much needed

	stability and predictability to the Romanian renewable energy sector.
Energy efficiency, 2020 energy consumption targets: Romania's 2020 energy efficiency target is 43 Mtoe expressed in primary energy consumption (30.3 Mtoe expressed in final energy consumption)	In 2017, Romania has achieved only 53% of its required end-use energy savings obligation for the period 2014-2020 under the Energy Efficiency Directive, which puts at risk its ability to fulfil the obligation by 2020. The energy consumption continued to increase, in all the sectors.
Early school/training leaving target: 11.3 %.	The rate of early school leaving decreased to 16.4% in 2018, but the target is still far from being achieved. Albeit the decrease from 2017 was significant (1.7 points), the rate has stagnated overall since 2009 and Romania still has one of the highest early school leaving rates in the EU.
Tertiary education target: 26.7 % of population aged 30-34.	In 2018, the progress made on tertiary attainment in the past decade has been reversed, and the rate has decreased compared to 2017 from 26.3% to 24.6%, remaining the lowest rate in the EU.
Target for reducing the number of people at risk of poverty or social exclusion, expressed as an absolute number of people: 580,000 (base year 2010: 8.4 million).	The national target is considered to have already been achieved. In absolute terms, the number of people no longer at risk of poverty or social exclusion since 2008 had already hit 2,755,000 in 2018.

([1]) The following categories are used to assess progress in implementing the country-specific recommendations (CSRs):

No progress: The Member State has not credibly announced nor adopted any measures to address the CSR. This category covers a number of typical situations to be interpreted on a case by case basis taking into account country-specific conditions. They include the following:

no legal, administrative, or budgetary measures have been announced

in the national reform programme,

in any other official communication to the national Parliament/relevant parliamentary committees or the European Commission,

publicly (e.g. in a press statement or on the government's website);

no non-legislative acts have been presented by the governing or legislative body;

the Member State has taken initial steps in addressing the CSR, such as commissioning a study or setting up a study group to analyse possible measures to be taken (unless the CSR explicitly asks for orientations or exploratory actions). However, it has not proposed any clearly-specified measure(s) to address the CSR.

Limited progress: The Member State has:

announced certain measures but these address the CSR only to a limited extent; and/or

presented legislative acts in the governing or legislative body but these have not been adopted yet and substantial further, non-legislative work is needed before the CSR is implemented;

presented non-legislative acts, but has not followed these up with the implementation needed to address the CSR.

Some progress: The Member State has adopted measures that partly address the CSR; and/or that address the CSR, but a fair amount of work is still needed to fully address the CSR fully as only a few of the measures have been implemented. For instance, a measure or measures have been adopted by the national Parliament or by ministerial decision but no implementing decisions are in place.

Substantial progress: The Member State has adopted measures that go a long way towards addressing the CSR and most of them have been implemented.

Full implementation: The Member State has implemented all measures needed to address the CSR appropriately.

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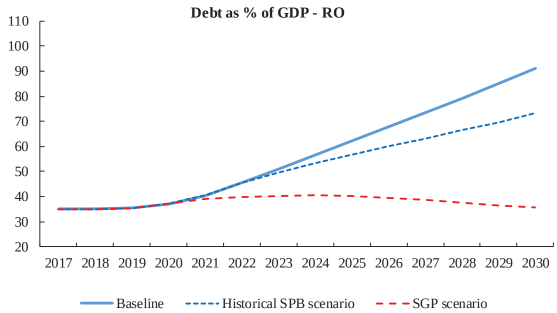
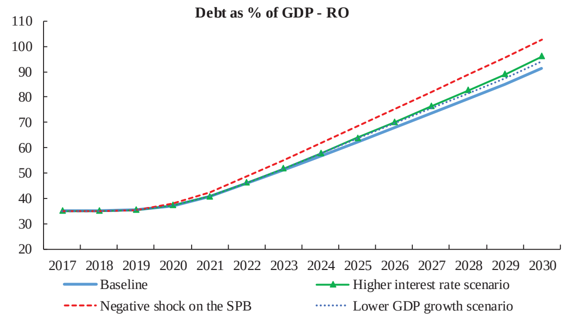
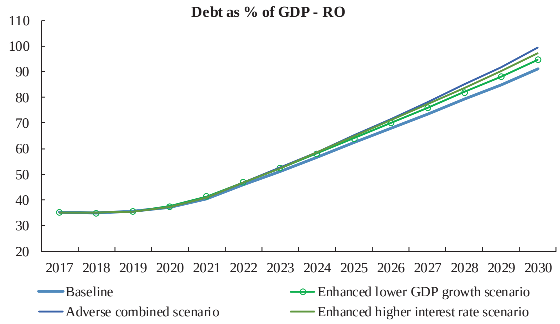
ANNEX B: COMMISSION DEBT SUSTAINABILITY ANALYSIS AND FISCAL RISKS

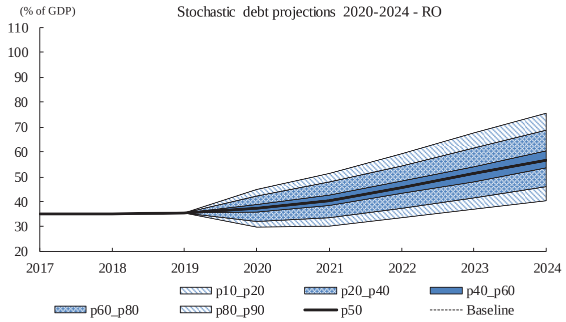
General government debt projections under baseline, alternative scenarios and sensitivity tests

RO - Debt projections baseline scenario	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030
Gross debt ratio	**35.0**	**35.5**	**37.2**	**40.6**	**45.8**	**51.1**	**56.7**	**62.3**	**68.0**	**73.6**	**79.3**	**85.1**	**91.2**
Changes in the ratio (-1+2+3)	*-0.1*	*0.5*	*1.7*	*3.4*	*5.2*	*5.3*	*5.6*	*5.7*	*5.6*	*5.7*	*5.7*	*5.7*	*6.2*
of which													
(1) Primary balance (1.1+1.2+1.3)	**-1.8**	**-2.4**	**-3.2**	**-4.8**	**-6.5**	**-6.4**	**-6.3**	**-6.2**	**-6.3**	**-6.3**	**-6.3**	**-6.4**	**-6.4**
(1.1) Structural primary balance *(1.1.1-1.1.2+1.1.3)*	***-1.6***	***-2.3***	***-3.1***	***-4.6***	***-6.4***	***-6.3***	***-6.3***	***-6.2***	***-6.3***	***-6.3***	***-6.3***	***-6.4***	***-6.4***
(1.1.1) Structural primary balance (bef. CoA)	*-1.6*	*-2.3*	*-3.1*	*-4.6*	*-4.6*	*-4.6*	*-4.6*	*-4.6*	*-4.6*	*-4.6*	*-4.6*	*-4.6*	*-4.6*
(1.1.2) Cost of ageing					*1.8*	*1.7*	*1.6*	*1.6*	*1.6*	*1.6*	*1.6*	*1.7*	*1.7*
(1.1.3) Others (taxes and property incomes)					*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	*-0.1*	*-0.1*	*-0.1*
(1.2) Cyclical component	***0.1***	***0.0***	***0.0***	***-0.1***	***-0.1***	***0.0***	***0.0***	***0.0***	***0.0***	***0.0***	***0.0***	***0.0***	***0.0***
(1.3) One-off and other temporary measures	***-0.3***	***-0.1***	***0.0***	***0.0***	***0.0***	***0.0***	***0.0***	***0.0***	***0.0***	***0.0***	***0.0***	***0.0***	***0.0***
(2) Snowball effect (2.1+2.2+2.3)	**-2.0**	**-2.5**	**-1.5**	**-1.4**	**-1.3**	**-1.0**	**-0.7**	**-0.6**	**-0.6**	**-0.6**	**-0.6**	**-0.6**	**-0.2**
(2.1) Interest expenditure	*1.2*	*1.2*	*1.2*	*1.3*	*1.5*	*1.8*	*2.1*	*2.4*	*2.7*	*3.0*	*3.4*	*3.7*	*4.0*
(2.2) Growth effect	*-1.3*	*-1.3*	*-1.2*	*-1.1*	*-1.3*	*-1.5*	*-1.6*	*-1.6*	*-1.8*	*-2.0*	*-2.2*	*-2.3*	*-2.2*
(2.3) Inflation effect	*-1.9*	*-2.4*	*-1.5*	*-1.6*	*-1.5*	*-1.4*	*-1.2*	*-1.4*	*-1.5*	*-1.7*	*-1.8*	*-1.9*	*-2.1*
(3) Stock-flow adjustments	**0.1**	**0.5**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**









Short term	Medium term	S1	Debt sustainability analysis (detail)	Baseline	Historical SPB	Lower GDP growth	Higher interest rate	Negative shock on SPB	Stochastic projections	DSA	S2	Long term
LOW (S0 = 0.4)	HIGH	HIGH (S1 = 5.7)	Risk category	HIGH	MEDIUM	HIGH	HIGH	HIGH	MEDIUM	HIGH	HIGH (S2 = 8.8)	HIGH
			Debt level (2030)	91.2	73.4	94.2	96.1	102.9				
			Debt peak year	2030	2030	2030	2030	2030				
			Percentile rank	96.0%	88.0%							
			Probability debt higher						96.2%			
			Dif. between percentiles						35.0			

Note: For further information, see the European Commission Debt Sustainability Monitor (DSM) 2019.

[1] The first table presents the baseline no-fiscal policy change scenario projections. It shows the projected government debt dynamics and its decomposition between the primary balance, snowball effects and stock-flow adjustments. Snowball effects measure the net impact of the counteracting effects of interest rates, inflation, real GDP growth (and exchange rates in some countries). Stock-flow adjustments include differences in cash and accrual accounting, net accumulation of assets, as well as valuation and other residual effects.

[2] The charts present a series of sensitivity tests around the baseline scenario, as well as alternative policy scenarios, in particular: the historical structural primary balance (SPB) scenario (where the SPB is set at its historical average), the Stability and Growth Pact (SGP) scenario (where fiscal policy is assumed to evolve in line with the main provisions of the SGP), a higher interest rate scenario (+1 pp. compared to the baseline), a lower GDP growth scenario (-0.5 pp. compared to the baseline) and a negative shock on the SPB (calibrated on the basis of the forecasted change). An adverse combined scenario and enhanced sensitivity tests (on the interest rate and growth) are also included, as well as stochastic projections. Detailed information on the design of these projections can be found in the FSR 2018 and the DSM 2019.

[3] The second table presents the overall fiscal risk classification over the short, medium and long term.

a. For the short-term, the risk category (low/high) is based on the S0 indicator. S0 is an early-detection indicator of fiscal stress in the upcoming year, based on 25 fiscal and financial-competitiveness variables that have proven in the past to be leading indicators of fiscal stress. The critical threshold beyond which fiscal distress is signalled is 0.46.

b. For the medium term, the risk category (low/medium/high) is based on the joint use of the S1 indicator and of the DSA results. The S1 indicator measures the fiscal adjustment required (cumulated over the 5 years following the forecast horizon and sustained after that) to bring the debt-to-GDP ratio to 60 % by 2034. The critical values used are 0 and 2.5 pps of GDP. The DSA classification is based on the results of five deterministic scenarios (baseline, historical SPB, higher interest rate, lower GDP growth and negative shock on the SPB scenarios) and the stochastic projections. Different criteria are used such as the projected debt level, the debt path, the realism of fiscal assumptions, the probability of debt stabilisation, and the size of uncertainties.

c. For the long term, the risk category (low/medium/high) is based on the joint use of the S2 indicator and the DSA results. The S2 indicator measures the upfront and permanent fiscal adjustment required to stabilise the debt-to-GDP ratio over the infinite horizon, including the costs of ageing. The critical values used are 2 and 6 pps of GDP. The DSA results are used to further qualify the long term risk classification, in particular in cases when debt vulnerabilities are identified (a medium / high DSA risk category).

ANNEX C: STANDARD TABLES

Table C.1: **Financial market indicators**

	2014	2015	2016	2017	2018	2019
Total assets of the banking sector (% of GDP)(1)	60.1	57.6	55.5	52.6	51.4	48.4
Share of assets of the five largest banks (% of total assets)	54.2	57.4	59.1	59.5	61.6	-
Foreign ownership of banking system (% of total assets)(2)	90.0	90.5	91.4	77.3	74.9	74.5
Financial soundness indicators:(2)						
- non-performing loans (% of total loans)	20.7	13.4	9.7	6.6	5.3	5.0
- capital adequacy ratio (%)	17.7	18.9	19.2	19.4	19.7	19.0
- return on equity (%)(3)	-15.2	11.3	10.6	11.7	13.6	13.0
Bank loans to the private sector (year-on-year % change)(1)	-1.3	4.5	3.3	7.1	9.9	9.6
Lending for house purchase (year-on-year % change)(1)	9.2	15.5	13.4	13.2	12.9	10.8
Loan-to-deposit ratio(2)	67.2	67.6	68.2	69.2	71.7	73.6
Central bank liquidity as % of liabilities(1)	-	-	-	-	0.0	0.0
Private debt (% of GDP)	62.1	58.0	53.7	50.9	47.4	-
Gross external debt (% of GDP)(2) - public	21.8	19.6	19.0	18.0	17.3	17.2
- private	28.9	26.8	28.2	27.9	27.0	26.0
Long-term interest rate spread versus Bund (basis points)*	333.1	297.8	322.9	364.1	429.0	478.2
Credit default swap spreads for sovereign securities (5-year)*	137.4	110.0	105.9	92.5	83.5	85.2

(1) Latest data Q3 2019. Includes not only banks but all monetary financial institutions excluding central banks.
(2) Latest data Q2 2019.
(3) Quarterly values are annualised.
* Measured in basis points.
Sources: European Commission (long-term interest rates); World Bank (gross external debt); Eurostat (private debt); ECB (all other indicators).

Table C.2: **Headline Social Scoreboard indicators**

	2014	2015	2016	2017	2018	2019 [5]
Equal opportunities and access to the labour market						
Early leavers from education and training (% of population aged 18-24)	18.1	19.1	18.5	18.1	16.4	:
Gender employment gap (pps)	16.7	17.5	17.6	17.1	18.3	18.8
Income inequality, measured as quintile share ratio (S80/S20)	7.2	8.3	7.2	6.5	7.2	:
At-risk-of-poverty or social exclusion rate(1) (AROPE)	40.3	37.4	38.8	35.7	32.5	:
Young people neither in employment nor in education and training (% of population aged 15-24)	17.0	18.1	17.4	15.2	14.5	:
Dynamic labour markets and fair working conditions						
Employment rate (20-64 years)	65.7	66.0	66.3	68.8	69.9	70.9
Unemployment rate(2) (15-74 years)	6.8	6.8	5.9	4.9	4.2	3.9
Long-term unemployment rate (as % of active population)	2.8	3.0	3.0	2.0	1.8	1.8
Gross disposable income of households in real terms per capita(3) (Index 2008=100)	99.3	106.0	116.4	131.1	145.5	:
Annual net earnings of a full-time single worker without children earning an average wage (levels in PPS, three-year average)	8621	8987	9609	:	:	:
Annual net earnings of a full-time single worker without children earning an average wage (percentage change, real terms, three-year average)	0.33	5.00	8.51	:	:	:
Public support / Social protection and inclusion						
Impact of social transfers (excluding pensions) on poverty reduction(4)	12.8	13.3	14.2	16.6	16.1	:
Children aged less than 3 years in formal childcare	2.6	9.4	17.4	15.7	13.2	:
Self-reported unmet need for medical care	9.8	9.4	6.5	4.7	4.9	:
Individuals who have basic or above basic overall digital skills (% of population aged 16-74)	:	26.0	28.0	29.0	:	:

(1) People at risk of poverty or social exclusion (AROPE): individuals who are at risk of poverty (AROP) and/or suffering from severe material deprivation (SMD) and/or living in households with zero or very low work intensity (LWI).
(2) Unemployed persons are all those who were not employed but had actively sought work and were ready to begin working immediately or within two weeks.
(3) Gross disposable household income is defined in unadjusted terms, according to the draft Joint Employment Report 2019.
(4) Reduction in percentage of the risk of poverty rate, due to social transfers (calculated comparing at-risk-of poverty rates before social transfers with those after transfers; pensions are not considered as social transfers in the calculation).
(5) Average of first three quarters of 2019 for the employment rate, unemployment rate and gender employment gap.
Source: Eurostat

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Table C.3: **Labour market and education indicators**

Labour market indicators	**2014**	**2015**	**2016**	**2017**	**2018**	**2019 [5]**
Activity rate (15-64)	65.7	66.1	65.6	67.3	67.8	68.5
Employment in current job by duration						
From 0 to 11 months	5.0	6.2	4.9	5.8	4.9	:
From 12 to 23 months	6.0	7.4	6.4	6.7	6.8	:
From 24 to 59 months	20.0	19.5	20.5	19.8	23.4	:
60 months or over	69.0	66.8	68.2	67.7	64.9	:
Employment growth* (% change from previous year)	0.8	-0.9	-1.0	2.6	0.2	-0.4
Employment rate of women (% of female population aged 20-64)	57.3	57.2	57.4	60.2	60.6	61.3
Employment rate of men (% of male population aged 20-64)	74.0	74.7	75.0	77.3	78.9	80.1
Employment rate of older workers* (% of population aged 55-64)	43.1	41.1	42.8	44.5	46.3	47.7
Part-time employment* (% of total employment, aged 15-64)	8.7	8.8	7.4	6.8	6.5	6.3
Fixed-term employment* (% of employees with a fixed term contract, aged 15-64)	1.5	1.4	1.4	1.2	1.1	1.4
Transition rate from temporary to permanent employment (3-year average)	57.8	56.5	56.1	56.9	62.7	:
Youth unemployment rate (% active population aged 15-24)	24.0	21.7	20.6	18.3	16.2	16.3
Gender gap in part-time employment	1.2	0.6	0.4	0.2	0.6	0.6
Gender pay gap[(2)] (in undadjusted form)	4.5	5.8	5.2	3.5	:	:
Education and training indicators	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**
Adult participation in learning (% of people aged 25-64 participating in education and training)	1.5	1.3	1.2	1.1	0.9	:
Underachievement in education[(3)]	:	39.9	:	:	:	:
Tertiary educational attainment (% of population aged 30-34 having successfully completed tertiary education)	25.0	25.6	25.6	26.3	24.6	:
Variation in performance explained by students' socio-economic status[(4)]	:	13.8	:	:	:	:

* Non-scoreboard indicator
(1) Long-term unemployed are people who have been unemployed for at least 12 months.
(2) Difference between the average gross hourly earnings of male paid employees and of female paid employees as a percentage of average gross hourly earnings of male paid employees. It is defined as "unadjusted", as it does not correct for the distribution of individual characteristics (and thus gives an overall picture of gender inequalities in terms of pay). All employees working in firms with ten or more employees, without restrictions for age and hours worked, are included.
(3) PISA (OECD) results for low achievement in mathematics for 15 year-olds.
(4) Impact of socio-economic and cultural status on PISA (OECD) scores.
(5) Average of first three quarters of 2019. Data for youth unemployment rate is seasonally adjusted.
Sources: Eurostat, OECD

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Table C.4: **Social inclusion and health indicators**

	2013	2014	2015	2016	2017	2018
Expenditure on social protection benefits* (% of GDP)						
Sickness/healthcare	3.9	3.9	3.8	3.9	3.9	:
Disability	1.1	1.1	1.1	1.0	0.9	:
Old age and survivors	8.0	8.0	7.9	7.9	7.9	:
Family/children	1.2	1.2	1.3	1.4	1.1	:
Unemployment	0.2	0.1	0.1	0.1	0.1	:
Housing	0.0	0.0	0.0	0.0	0.0	:
Social exclusion n.e.c.	0.2	0.2	0.2	0.2	0.1	:
Total	14.6	14.4	14.3	14.4	14.1	:
of which: means-tested benefits	0.6	0.6	0.6	0.5	0.6	:
General government expenditure by function (% of GDP)						
Social protection	11.5	11.4	11.4	11.5	11.7	:
Health	4.0	4.0	4.2	4.0	4.3	:
Education	2.8	3.0	3.1	3.3	2.8	:
Out-of-pocket expenditure on healthcare	20.2	20.3	21.3	20.8	20.5	:
Children at risk of poverty or social exclusion (% of people aged 0-17)*	51.4	50.7	46.8	49.2	41.7	38.1
At-risk-of-poverty rate(1) (% of total population)	23.0	25.1	25.4	25.3	23.6	23.5
In-work at-risk-of-poverty rate (% of persons employed)	18.4	19.8	18.8	18.9	17.4	15.3
Severe material deprivation rate(2) (% of total population)	29.8	25.9	22.7	23.8	19.7	16.8
Severe housing deprivation rate(3), by tenure status						
Owner, with mortgage or loan	16.1	4.9	1.6	1.4	1.2	0.0
Tenant, rent at market price	21.2	32.8	53.0	46.0	27.2	23.8
Proportion of people living in low work intensity households(4) (% of people aged 0-59)	7.6	7.2	7.9	8.2	6.9	7.4
Poverty thresholds, expressed in national currency at constant prices*	3888	3991	4253	4518	5167	6228
Healthy life years						
Females	5.2	5.7	5.7	5.6	5.1	:
Males	5.8	5.9	6.3	6.2	5.9	:
Aggregate replacement ratio for pensions(5)	0.7	0.7	0.6	0.7	0.6	0.5
Connectivity dimension of the Digital Economy and Society Index (DESI)(6)	:	43.9	46.2	49.8	54.1	:
GINI coefficient before taxes and transfers*	51.8	52.1	54.1	54.4	52.3	:
GINI coefficient after taxes and transfers*	34.0	34.7	37.4	34.7	33.1	35.1

* Non-scoreboard indicator
(1) At-risk-of-poverty rate (AROP): proportion of people with an equivalised disposable income below 60 % of the national equivalised median income.
(2) Proportion of people who experience at least four of the following forms of deprivation: not being able to afford to i) pay their rent or utility bills, ii) keep their home adequately warm, iii) face unexpected expenses, iv) eat meat, fish or a protein equivalent every second day, v) enjoy a week of holiday away from home once a year, vi) have a car, vii) have a washing machine, viii) have a colour TV, or ix) have a telephone.
(3) Percentage of total population living in overcrowded dwellings and exhibiting housing deprivation.
(4) People living in households with very low work intensity: proportion of people aged 0-59 living in households where the adults (excluding dependent children) worked less than 20 % of their total work-time potential in the previous 12 months.
(5) Ratio of the median individual gross pensions of people aged 65-74 relative to the median individual gross earnings of people aged 50-59.
(6) Fixed broadband take up (33%), mobile broadband take up (22%), speed (33%) and affordability (11%), from the Digital Scoreboard.
Sources: Eurostat, OECD

Table C.5: **Product market performance and policy indicators**

Performance indicators	2013	2014	2015	2016	2017	2018
Labour productivity per person[1] growth (t/t-1) in %						
Labour productivity growth in industry	3.98	0.19	8.52	2.17	5.16	3.27
Labour productivity growth in construction	4.72	2.70	6.84	5.37	-10.85	4.86
Labour productivity growth in market services	3.85	0.64	3.10	3.59	5.51	-0.04
Unit Labour Cost (ULC) index[2] growth (t/t-1) in %						
ULC growth in industry	-3.55	0.59	-0.06	7.24	6.60	10.74
ULC growth in construction	-3.96	-12.10	4.96	-2.90	21.33	19.21
ULC growth in market services	3.01	5.72	-0.17	10.65	7.00	13.06
Business environment	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**
Time needed to enforce contracts[3] (days)	512	512	512	512	512	512
Time needed to start a business[3] (days)	8.0	8.0	8.0	12.0	12.0	35.0
Outcome of applications by SMEs for bank loans[4]	0.99	0.94	0.46	0.36	0.69	0.75
Research and innovation	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**
R&D intensity	0.39	0.38	0.49	0.48	0.50	0.51
General government expenditure on education as % of GDP	2.80	3.00	3.10	3.30	2.80	:
Employed people with tertiary education and/or people employed in S&T as % of total employment	24	24	26	27	27	27
Population having completed tertiary education[5]	14	14	15	15	15	16
Young people with upper secondary education[6]	80	80	80	80	80	82
Trade balance of high technology products as % of GDP	-1.96	-1.66	-1.75	-1.60	-1.88	-1.78
Product and service markets and competition	**2003**	**2008**	**2013**			**2018***
OECD product market regulation (PMR)[7], overall	:	:	1.69			1.86
OECD PMR[7], retail	:	:	1.80			1.35
OECD PMR[7], professional services[8]	:	:	:			2.57
OECD PMR[7], network industries[9]	:	:	1.97			1.73

*While the indicator values from 2003 to 2013 are comparable, the methodology has considerably changed in 2018. As a result, past vintages cannot be compared with the 2018 PMR indicators.
1 Value added in constant prices divided by the number of persons employed.
2 Compensation of employees in current prices divided by value added in constant prices.
3 The methodologies, including the assumptions, for this indicator are shown in detail here: http://www.doingbusiness.org/methodology.
4 Average of the answer to question Q7B_a. "[Bank loan]: If you applied and tried to negotiate for this type of financing over the past six months, what was the outcome?". Answers were codified as follows: zero if received everything, one if received 75% and above, two if received below 75%, three if refused or rejected and treated as missing values if the application is still pending or don't know.
5 Percentage population aged 15-64 having completed tertiary education.
6 Percentage population aged 20-24 having attained at least upper secondary education.
7 Index: 0 = not regulated; 6 = most regulated. The methodologies of the OECD product market regulation indicators are shown in detail here: http://www.oecd.org/competition/reform/indicatorsofproductmarketregulationhomepage.htm.
8 Simple average of the indicators of regulation for lawyers, accountants, architects and engineers.
9 Aggregate OECD indicators of regulation in energy, transport and communications (ETCR).
Sources: European Commission; World Bank — Doing Business (for enforcing contracts and time to start a business); OECD (for the product market regulation indicators); SAFE (for outcome of SMEs' applications for bank loans).

Table C.6: **Green growth**

Green growth performance		2013	2014	2015	2016	2017	2018
Macroeconomic							
Energy intensity	kgoe / €	0.24	0.23	0.22	0.21	0.21	0.20
Carbon intensity	kg / €	0.86	0.83	0.80	0.75	0.70	-
Resource intensity (reciprocal of resource productivity)	kg / €	2.66	2.68	3.07	2.97	2.55	2.47
Waste intensity	kg / €	-	1.26	-	1.17	-	-
Energy balance of trade	% GDP	-1.9	-1.4	-0.9	-0.9	-1.3	-1.6
Weighting of energy in HICP	%	12.45	12.21	12.25	11.94	12.08	11.79
Difference between energy price change and inflation	p.p.	5.0	0.1	2.8	-1.0	1.6	7.0
Real unit of energy cost	% of value added	27.6	26.5	26.6	26.7	-	-
Ratio of environmental taxes to labour taxes	ratio	0.20	0.21	0.24	0.26	0.24	-
Environmental taxes	% GDP	2.1	2.4	2.5	2.4	2.0	2.1
Sectoral							
Industry energy intensity	kgoe / €	0.15	0.14	0.14	0.13	0.12	0.12
Real unit energy cost for manufacturing industry excl. refining	% of value added	21.2	20.6	20.4	20.3	-	-
Share of energy-intensive industries in the economy	% GDP	11.42	12.03	12.34	12.39	12.40	12.33
Electricity prices for medium-sized industrial users	€ / kWh	0.09	0.08	0.08	0.08	0.08	0.08
Gas prices for medium-sized industrial users	€ / kWh	0.03	0.03	0.03	0.03	0.03	0.03
Public R&D for energy	% GDP	0.01	0.02	0.01	0.02	0.01	0.01
Public R&D for environmental protection	% GDP	0.02	0.01	0.01	0.02	0.01	0.01
Municipal waste recycling rate	%	13.2	13.1	13.2	13.3	14.0	11.1
Share of GHG emissions covered by ETS*	%	36.8	37.0	36.3	35.2	35.0	34.8
Transport energy intensity	kgoe / €	0.54	0.53	0.48	0.43	0.43	0.41
Transport carbon intensity	kg / €	0.70	0.68	0.70	0.68	0.70	0.68
Security of energy supply							
Energy import dependency	%	18.1	16.4	16.4	21.6	23.1	-
Aggregated supplier concentration index	HHI	18.8	16.4	21.5	29.2	26.1	-
Diversification of energy mix	HHI	22.9	23.1	23.0	23.1	23.2	23.3

All macro intensity indicators are expressed as a ratio of a physical quantity to GDP (in 2010 prices)
Energy intensity: gross inland energy consumption (in kgoe) divided by GDP (in EUR)
Carbon intensity: greenhouse gas emissions (in kg CO2 equivalents) divided by GDP (in EUR)
Resource intensity: domestic material consumption (in kg) divided by GDP (in EUR)
Waste intensity: waste (in kg) divided by GDP (in EUR)
Energy balance of trade: the balance of energy exports and imports, expressed as % of GDP.
Weighting of energy in HICP: the proportion of 'energy' items in the consumption basket used for the construction of the HICP.
Difference between energy price change and inflation: energy component of HICP, and total HICP inflation (annual % change).
Real unit energy cost: real energy costs as % of total value added for the economy.
Industry energy intensity: final energy consumption of industry (in kgoe) divided by gross value added of industry (in 2010 EUR).
Real unit energy costs for manufacturing industry excluding refining: real costs as % of value added for manufacturing sectors.
Share of energy-intensive industries in the economy: share of gross value added of the energy-intensive industries in GDP.
Electricity and gas prices for medium-sized industrial users: consumption band 500–20 00MWh and 10 000 -100 000 GJ; figures excl. VAT.
Recycling rate of municipal waste: ratio of recycled and composted municipal waste to total municipal waste.
Public R&D for energy or for the environment: government spending on R&D for these categories as % of GDP.
Proportion of GHG emissions covered by EU emissions trading system (ETS) (excluding aviation): based on GHG emissions. (excl. land use, land use change and forestry) as reported by Member States to the European Environment Agency.
Transport energy intensity: final energy consumption of transport activity including international aviation (kgoe) divided by gross value added in transportation and storage sector (in 2010 EUR).
Transport carbon intensity: GHG emissions in transportation and storage sector divided by gross value added in transportation and storage sector (in 2010 EUR).
Energy import dependency: net energy imports divided by gross inland energy consumption incl. consumption of international bunker fuels.
Aggregated supplier concentration index: Herfindahl index covering oil, gas and coal. Smaller values indicate larger diversification and hence lower risk.
Diversification of the energy mix: Herfindahl index covering natural gas, total petrol products, nuclear heat, renewable energies and solid fuels. Smaller values indicate larger diversification.
* European Commission and European Environment Agency - 2018 provisional data.
Sources: European Commission and European Environment Agency (Share of GHG emissions covered by ETS); European Commission (Environmental taxes over labour taxes and GDP); Eurostat (all other indicators).

ANNEX D: INVESTMENT GUIDANCE ON JUST TRANSITION FUND 2021-2027 FOR ROMANIA

Building on the Commission proposal, this Annex ([60]) presents the preliminary Commission services' views on priority investment areas and framework conditions for effective delivery for the 2021-2027 Just Transition Fund investments in Romania. These priority investment areas are derived from the broader analysis of territories facing serious socio-economic challenges deriving from the transition process towards a climate-neutral economy of the Union by 2050 in Romania, assessed in the report. This Annex provides the basis for a dialogue between Romania and the Commission services as well as the relevant guidance for the Member States in preparing their territorial just transition plans, which will form the basis for programming the Just Transition Fund. The Just Transition Fund investments complement those under Cohesion Policy funding for which guidance in the form of Annex D was given in the 2019 Country Report for Romania ([61]).

Coal mining in Romania is concentrated within the two sub-regions of Jiu Valley and Rovinari/Turceni, which are situated in the counties of Hunedoara and Gorj.

The two counties employ 90% of the entire Romanian mining work force, and the total number of jobs depending directly on coal extraction or coal fired energy production represents 18 600, with another 10 000 indirectly depending on coal. Hunedoara and Gorj represent some 90% of greenhouse gas (GHG) emissions caused by Romania's coal fired power plants, or approximately 30% of all Romanian GHG emissions stemming from mining and manufacturing. Moving away from fossil fuel extraction and use is likely to put these jobs at risk.

Moreover, both counties have a number of carbon intensive industrial facilities, which adds to the decarbonisation challenge, as many of these companies are expected to undergo restructuring before 2030, which could also negatively influence employment. Based on this preliminary assessment, it appears warranted that the Just Transition Fund concentrates its intervention on these geographical areas.

In order to tackle the related transition challenges, high priority investment needs have been identified to alleviate the socio-economic costs of the transition. Key actions of the Just Transition Fund could target in particular:

- investment in regeneration and decontamination of sites, land restoration and repurposing projects;
- investment in the deployment of technology and infrastructures for affordable clean energy, greenhouse gas emission reduction, energy efficiency and renewable energy;
- productive investments in SMEs, including start-ups, leading to economic diversification and reconversion;
- investment in the creation of new firms, including through business incubators and consulting services;
- investment in research and innovation activities and fostering transfer of advanced technologies
- upskilling and reskilling of workers;
- job-search assistance to jobseekers;

([60]) This Annex is to be considered in conjunction with the EC proposal for a Regulation of the European Parliament and of the Council on the Just Transition Fund 2021-2027 (COM (2020) 22) and the EC proposal for a Regulation of the European Parliament and of the Council laying down common provisions on the European Regional Development Fund, the European Social Fund Plus, the Cohesion Fund, and the European Maritime and Fisheries Fund and financial rules for those and for the Asylum and Migration Fund, the Internal Security Fund and the Border Management and Visa Instrument (COM (2020) 23).
([61]) SWD(2019) 1022 final

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- active inclusion of jobseekers;

- technical assistance.

These counties are expected to suffer from substantial job losses, which might not be entirely offset by the creation and development of SMEs. Exceptionally, and where necessary for the implementation of the territorial just transition plan, support to productive investments in large enterprises could therefore be considered.

Furthermore, industrial sites in these counties, performing activities listed in Annex I to Directive 2003/87/EC, employ a substantial number of workers and their activity is at risk due to their high greenhouse gas emissions. Support to investments to reduce the emissions could be considered, provided that they achieve a substantial reduction of emissions (going substantially below the relevant benchmarks used for free allocation under Directive 2003/87/EC) and on the condition that the investments are compatible with the European Green Deal.

Within the counties of Dolj, Galați, Prahova and Mureş a significant number of the work force is employed in fossil fuel power and heat generation or energy intensive manufacturing and heavy industry (chemicals, metal processing cement, fertilisers, etc.). These counties represent approximately 35% of Romanian's GHG emission stemming from mining and manufacturing.

As the sectors identified are expected to undergo significant changes related to the necessary energy transition, it appears warranted that the Just Transition Fund also intervenes in these geographical areas to accompany them in their reconversion.

In order to tackle these challenges, high priority investment needs have also been identified to alleviate the socio-economic costs of the transition. Key actions of the Just Transition Fund could target in particular:

- productive investments in SMEs, including start-ups, leading to economic diversification and reconversion;

- investment in the creation of new firms, including through business incubators and consulting services;

- investment in research and innovation activities and fostering transfer of advanced technologies;

- investment in the deployment of technology and infrastructures for affordable clean energy, energy efficiency and renewable energy;

- investment in digitalization;

- investment in regeneration and decontamination of sites, land restoration and repurposing projects;

- investment in enhancing the circular economy, including through waste prevention, reduction, and resource efficiency, reuse repair and recycling;

- upskilling- and reskilling of workers;

- active inclusion of jobseekers;

- technical assistance.

These four counties are expected to experience substantial job losses, which might not be entirely offset by the creation and development of SMEs; support to productive investments in large enterprises could therefore be considered.

Furthermore, industrial sites in these counties, performing activities listed in Annex I to Directive 2003/87/EC, employ a substantial number of workers and their activity is at risk due to their high greenhouse gas emissions; support to investments to reduce the emissions could be considered, provided that they achieve a substantial reduction of emissions (going substantially below the relevant benchmarks used for free allocation under Directive 2003/87/EC) and on the condition that the investments are compatible with the European Green Deal.

ANNEX E: PROGRESS TOWARDS THE SUSTAINABLE DEVELOPMENT GOALS

Assessment of Romania's short-term progress towards the SDGs ([62])

Table E.1 shows the data for Romania and the EU-28 for the indicators included in the EU SDG indicator set used by Eurostat for monitoring progress towards the SDGs in an EU context ([63]). As the short-term trend at EU-level is assessed over a 5-year period, both the value at the beginning of the period and the latest available value is presented. The indicators are regularly updated on the SDI dedicated section of the Eurostat website.

Table E.1: **Indicators measuring Romania's progress towards the SDGs**

SDG / Sub-theme	Indicator	Unit	Romania				EU-28			
			Starting		Latest		Starting		Latest	
			year	value	year	value	year	value	year	value
SDG 1 – No poverty										
Multidimensional poverty	People at risk of poverty or social exclusion	% of population	2013	41.9	2018	32.5	2013	24.6	2018	21.9
	People at risk of income poverty after social transfers	% of population	2013	23.0	2018	23.5	2013	16.7	2018	17.1
	Severely materially deprived people	% of population	2013	29.8	2018	16.8	2013	9.6	2018	5.8
	People living in households with very low work intensity	% of population aged 0 to 59	2013	7.6	2018	7.4	2013	11.0	2018	8.8
	In-work at-risk-of-poverty rate	% of population aged 18 or over	2013	18.4	2018	15.3	2013	9.0	2018	9.5
Basic needs	Population living in a dwelling with a leaking roof, damp walls, floors or foundation or rot in window frames or floor	% of population	2013	16.2	2018	10.1	2013	15.6	2018	13.9
	Self-reported unmet need for medical care	% of population aged 16 or over	2013	10.9	2018	4.9	2013	3.7	2018	2.0
	Population having neither a bath, nor a shower, nor indoor flushing toilet in their household	% of population	2013	33.7	2018	25.6	2013	2.2	2018	1.7
	Population unable to keep home adequately warm	% of population	2013	14.7	2018	9.6	2013	10.7	2018	7.3
	Overcrowding rate	% of population	2013	50.6	2018	46.3	2013	17.0	2018	15.5
SDG 2 – Zero hunger										
Malnutrition	Obesity rate	% of population aged 18 or over	2014	9.4	2017	10.4	2014	15.9	2017	15.2
Sustainable agricultural production	Agricultural factor income per annual work unit (AWU)	EUR, chain linked volumes (2010)	2012	3 074	2017	4 380	2012	14 865	2017	17 304
	Government support to agricultural research and development	million EUR	2013	14.6	2018	14.3	2013	3 048.6	2018	3 242.5
	Area under organic farming	% of utilised agricultural area	2013	2.1	2018	2.4	2013	5.7	2018	7.5
	Gross nitrogen balance on agricultural land	kg per hectare	2012	16	2017	-12	2010	49	2015	51
Environmental impacts of agricultural production	Ammonia emissions from agriculture	kg per ha of utilised agricultural area	2012	10.8	2017	10.8	2011	19.7	2016	20.3
	Nitrate in groundwater	mg NO_3 per litre	N/A	:	N/A	:	2012	19.2	2017	19.1
	Estimated soil erosion by water	km^2	2010	16 159.3	2016	15 695.7	2010	207 232.2	2016	205 294.5
	Common farmland bird index	index 2000 = 100	N/A	:	N/A	:	2013	83.9	2018	80.7
SDG 3 – Good health and well-being										
Healthy lives	Life expectancy at birth	years	2012	74.4	2017	75.3	2012	80.3	2017	80.9
	Share of people with good or very good perceived health	% of population aged 16 or over	2013	68.8	2018	70.6	2013	67.3	2018	69.2
Health determinants	Smoking prevalence	% of population aged 15 or over	2012	30	2017	28	2014	26	2017	26
	Obesity rate	% of population aged 18 or over	2014	9.4	2017	10.4	2014	15.9	2017	15.2
	Population living in households considering that they suffer from noise	% of population	2013	26.4	2018	20.1	2013	18.8	2018	18.3
	Exposure to air pollution by particulate matter ($PM_{2.5}$)	$\mu g/m^3$	2012	19.4	2017	20.4	2012	16.8	2017	14.1
Causes of death	Death rate due to chronic diseases	number per 100 000 persons aged less than 65	2011	246.9	2016	229.6	2011	132.5	2016	119.0
	Death rate due to tuberculosis, HIV and hepatitis	number per 100 000 persons	2011	7.8	2016	6.6	2011	3.4	2016	2.6
	People killed in accidents at work	number per 100 000 employed persons	2012	5.78	2017	4.49	2012	1.91	2017	1.65
	People killed in road accidents	number of killed people	2012	2 042	2017	1 951	2012	28 231	2017	25 257
Access to health care	Self-reported unmet need for medical care	% of population aged 16 or over	2013	10.9	2018	4.9	2013	3.7	2018	2.0

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([62]) Data extracted on 9 February 2020 from the Eurostat database (official EU SDG indicator set; see https://ec.europa.eu/eurostat/web/sdi/main-tables).

([63]) The EU SDG indicator set is aligned as far as appropriate with the UN list of global indicators, noting that the UN indicators are selected for global level reporting and are therefore not always relevant in an EU context. The EU SDG indicators have strong links with EU policy initiatives.

Table (continued)

SDG / Sub-theme	Indicator	Unit	Romania				EU-28			
			Starting		Latest		Starting		Latest	
			year	value	year	value	year	value	year	value
SDG 4 – Quality education										
Basic education	Early leavers from education and training	% of the population aged 18 to 24	2013	17.3	2018	16.4	2013	11.9	2018	10.6
	Participation in early childhood education	% of the age group between 4-years-old and the starting age of compulsory education	2012	85.5	2017	89.6	2012	94.0	2017	95.4
	Underachievement in reading	% of 15-year-old students	2015	38.7	2018	40.8	2015	19.7	2018	21.7
	Young people neither in employment nor in education and training	% of population aged 15 to 29	2013	19.6	2018	17.0	2013	15.9	2018	12.9
Tertiary education	Tertiary educational attainment	% of the population aged 30 to 34	2013	22.9	2018	24.6	2013	37.1	2018	40.7
	Employment rate of recent graduates	% of population aged 20 to 34	2013	67.2	2018	77.4	2013	75.4	2018	81.7
Adult education	Adult participation in learning	% of population aged 25 to 64	2013	2.0	2018	0.9	2013	10.7	2018	11.1
SDG 5 – Gender equality										
Gender-based violence	Physical and sexual violence to women experienced within 12 months prior to the interview	% of women	N/A	:	2012	7	N/A	:	2012	8
Education	Gender gap for early leavers from education and training	percentage points, persons aged 18–24	2013	2.8	2018	0.6	2013	3.4	2018	3.3
	Gender gap for tertiary educational attainment	percentage points, persons aged 30–34	2013	2.6	2018	6.7	2013	8.5	2018	10.1
	Gender gap for employment rate of recent graduates	percentage points, persons aged 20–34	2013	4.5	2018	10.5	2013	4.4	2018	3.4
Employment	Gender pay gap in unadjusted form	% of average gross hourly earnings of men	2012	6.9	2017	3.5	2012	17.4	2017	16.0
	Gender employment gap	percentage points, persons aged 20–64	2013	16.3	2018	18.3	2013	11.7	2018	11.6
	Gender gap in inactive population due to caring responsibilities	percentage points, persons aged 20–64	2013	28.7	2018	31.7	2013	25.5	2018	27.1
Leadership positions	Seats held by women in national parliaments and governments	% of seats	2014	11.9	2019	19.8	2014	27.2	2019	31.5
	Positions held by women in senior management	% of board members	2014	11.0	2019	13.0	2014	20.2	2019	27.8
SDG 6 – Clean water and sanitation										
Sanitation	Population having neither a bath, nor a shower, nor indoor flushing toilet in their household	% of population	2013	33.7	2018	25.6	2013	2.2	2018	1.7
	Population connected to at least secondary wastewater treatment	% of population	2012	35.3	2017	46.5	N/A	:	N/A	:
Water quality	Biochemical oxygen demand in rivers	mg O_2 per litre	2012	3.33	2017	3.22	2012	2.06	2017	2.00
	Nitrate in groundwater	mg NO_3 per litre	N/A	:	N/A	:	2012	19.2	2017	19.1
	Phosphate in rivers	mg PO_4 per litre	2012	0.096	2017	0.098	2012	0.096	2017	0.093
	Inland water bathing sites with excellent water quality	% of bathing sites with excellent water quality	2013	0.0	2018	0.0	2013	76.5	2018	80.8
Water use efficiency	Water exploitation index	% of long term average available water (LTAA)	2012	16.4	2017	17.1	N/A	:	N/A	:
SDG 7 – Affordable and clean energy										
Energy consumption	Primary energy consumption	million tonnes of oil equivalent (Mtoe)	2013	30.4	2018	32.5	2013	1 577.4	2018	1 551.9
	Final energy consumption	million tonnes of oil equivalent (Mtoe)	2013	21.8	2018	23.5	2013	1 115.5	2018	1 124.1
	Final energy consumption in households per capita	kgoe	2013	386	2018	398	2013	605	2018	552
	Energy productivity	EUR per kgoe	2013	4.2	2018	5.1	2013	7.6	2018	8.5
	Greenhouse gas emissions intensity of energy consumption	index 2000 = 100	2012	93.1	2017	83.1	2012	91.5	2017	86.5
Energy supply	Share of renewable energy in gross final energy consumption	%	2013	23.9	2018	23.9	2013	15.4	2018	18.0
	Energy import dependency	% of imports in gross available energy	2013	18.1	2018	24.1	2013	53.2	2018	55.7
Access to affordable energy	Population unable to keep home adequately warm	% of population	2013	14.7	2018	9.6	2013	10.7	2018	7.3

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Table (continued)

SDG / Sub-theme	Indicator	Unit	Romania Starting year	Romania Starting value	Romania Latest year	Romania Latest value	EU-28 Starting year	EU-28 Starting value	EU-28 Latest year	EU-28 Latest value
SDG 8 – Decent work and economic growth										
Sustainable economic growth	Real GDP per capita	EUR per capita, chain-linked volumes (2010)	2013	6 760	2018	8 740	2013	25 750	2018	28 280
	Investment share of GDP	% of GDP	2013	24.8	2018	21.0	2013	19.5	2018	20.9
	Resource productivity	EUR per kg, chain-linked volumes (2010)	2013	0.38	2018	0.40	2013	1.98	2018	2.04
Employment	Young people neither in employment nor in education and training	% of population aged 15 to 29	2013	19.6	2018	17.0	2013	15.9	2018	12.9
	Employment rate	% of population aged 20 to 64	2013	64.7	2018	69.9	2013	68.4	2018	73.2
	Long-term unemployment rate	% of active population	2013	3.2	2018	1.8	2013	5.1	2018	2.9
	Gender gap in inactive population due to caring responsibilities	percentage points, persons aged 20–64	2013	28.7	2018	31.7	2013	25.5	2018	27.1
Decent work	People killed in accidents at work	number per 100 000 employed persons	2012	5.78	2017	4.49	2012	1.91	2017	1.65
	In-work at-risk-of-poverty rate	% of population	2013	18.4	2018	15.3	2013	9	2018	9.5
SDG 9 – Industry, innovation and infrastructure										
R&D and innovation	Gross domestic expenditure on R&D	% of GDP	2013	0.39	2018	0.51	2013	2.01	2018	2.12
	Employment in high- and medium-high technology manufacturing and knowledge-intensive services	% of total employment	2013	24.9	2018	28.5	2013	45.0	2018	46.1
	R&D personnel	% of active population	2013	0.37	2018	0.36	2013	1.15	2018	1.36
	Patent applications to the European Patent Office (EPO)	number	2012	72	2017	100	2012	56 772	2017	54 649
Sustainable transport	Share of buses and trains in total passenger transport	% of total inland passenger-km	2012	21.8	2017	19.7	2012	17.2	2017	16.7
	Share of rail and inland waterways in total freight transport	% of total inland freight tonne-km	2012	60.6	2017	57.6	2012	25.4	2017	23.3
	Average CO2 emissions per km from new passenger cars	g CO_2 per km	2013	132.1	2018	121.5	2014	123.4	2018	120.4
SDG 10 – Reduced inequalities										
Inequalities within countries	Relative median at-risk-of-poverty gap	% distance to poverty threshold	2013	33.6	2018	35.2	2013	23.8	2018	24.6
	Income distribution	income quintile share ratio	2013	6.8	2018	7.2	2013	5.0	2018	5.2
	Income share of the bottom 40 % of the population	% of income	2013	18.1	2018	17.6	2013	21.1	2018	21.0
	People at risk of income poverty after social transfers	% of population	2013	23.0	2018	23.5	2013	16.7	2018	17.1
Inequalities between countries	Purchasing power adjusted GDP per capita	Real expenditure per capita (in PPS)	2013	14 500	2018	20 100	2013	26 800	2018	31 000
	Adjusted gross disposable income of households per capita	Purchasing power standard (PPS) per inhabitant	2013	10 463	2018	15 377	2013	20 392	2018	22 824
	Financing to developing countries	million EUR, current prices	2012	:	N/A	:	2012	147 962	2017	155 224
	Imports from developing countries	million EUR, current prices	2013	8 669	2018	15 024	2013	817 475	2018	1 013 981
Migration and social inclusion	Asylum applications	Positive first instance decisions, per million inhabitants	2013	46	2018	31	2013	213	2018	424
SDG 11 – Sustainable cities and communities										
Quality of life in cities and communities	Overcrowding rate	% of population	2013	50.6	2018	46.3	2013	17.0	2018	15.5
	Population living in households considering that they suffer from noise	% of population	2013	26.4	2018	20.1	2013	18.8	2018	18.3
	Exposure to air pollution by particulate matter ($PM_{2.5}$)	µg/m^3	2012	19.4	2017	20.4	2012	16.8	2017	14.1
	Population living in a dwelling with a leaking roof, damp walls, floors or foundation or rot in window frames or floor	% of population	2013	16.2	2018	10.1	2013	15.6	2018	13.9
	Population reporting occurrence of crime, violence or vandalism in their area	% of population	2013	15.7	2018	11.5	2013	14.5	2018	12.7
Sustainable mobility	People killed in road accidents	number of killed people	2012	2 042	2017	1 951	2012	28 231	2017	25 257
	Share of buses and trains in total passenger transport	% of total inland passenger-km	2012	21.8	2017	19.7	2012	17.2	2017	16.7
Adverse environmental impacts	Settlement area per capita	m^2	2012	355.2	2015	364.8	2012	625.0	2015	653.7
	Recycling rate of municipal waste	% of total waste generated	2013	13.2	2018	11.1	2013	41.7	2018	47.0
	Population connected to at least secondary wastewater treatment	% of population	2012	35.3	2017	46.5	N/A	:	N/A	:

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Table (continued)

SDG / Sub-theme	Indicator	Unit	Romania Starting year	Romania Starting value	Romania Latest year	Romania Latest value	EU-28 Starting year	EU-28 Starting value	EU-28 Latest year	EU-28 Latest value
SDG 12 – Responsible consumption and production										
Decoupling environmental impacts from economic growth	Consumption of toxic chemicals	million tonnes	N/A	:	N/A	:	2013	300.3	2018	313.9
	Resource productivity	EUR per kg, chain-linked volumes (2010)	2013	0.38	2018	0.40	2013	1.98	2018	2.04
	Average CO2 emissions per km from new passenger cars	g CO_2 per km	2013	132.1	2018	121.5	2014	123.4	2018	120.4
	Energy productivity	EUR per kgoe	2013	4.2	2018	5.1	2013	7.6	2018	8.5
Energy consumption	Primary energy consumption	million tonnes of oil equivalent (Mtoe)	2013	30.4	2018	32.5	2013	1 577.4	2018	1 551.9
	Final energy consumption	million tonnes of oil equivalent (Mtoe)	2013	21.8	2018	23.5	2013	1 115.5	2018	1 124.1
	Share of renewable energy in gross final energy consumption	%	2013	23.9	2018	23.9	2013	15.4	2018	18.0
Waste generation and management	Circular material use rate	% of material input for domestic use	2012	2.6	2017	1.8	2012	11.5	2017	11.7
	Generation of waste excluding major mineral wastes	kg per capita	2012	1 162	2016	1 084	2012	1 716	2016	1 772
	Recycling rate of waste excluding major mineral wastes	% of total waste treated	2012	28	2016	30	2012	55	2016	57
SDG 13 – Climate action										
Climate mitigation	Greenhouse gas emissions	index 1990 = 100	2012	50.8	2017	46.1	2012	82.1	2017	78.3
	Greenhouse gas emissions intensity of energy consumption	index 2000 = 100	2012	93.1	2017	83.1	2012	91.5	2017	86.5
	Primary energy consumption	million tonnes of oil equivalent (Mtoe)	2013	30.4	2018	32.5	2013	1 577.4	2018	1 551.9
	Final energy consumption	million tonnes of oil equivalent (Mtoe)	2013	21.8	2018	23.5	2013	1 115.5	2018	1 124.1
	Share of renewable energy in gross final energy consumption	%	2013	23.9	2018	23.9	2013	15.4	2018	18.0
	Average CO2 emissions per km from new passenger cars	g CO_2 per km	2013	132.1	2018	121.5	2014	123.4	2018	120.4
Climate impacts	European mean near surface temperature deviation	temperature deviation in °C, compared with the 1850–1899 average	N/A	:	N/A	:	2013	1.4	2018	2.1
	Climate-related economic losses	EUR billion, in 2017 values	N/A	:	N/A	:	2012	2 719	2017	2 649
	Mean ocean acidity	pH value	N/A	:	N/A	:	2013	8.06	2018	8.06
Support to climate action	Contribution to the international 100bn USD commitment on climate related expending	EUR million, current prices	N/A	:	2017	0.9	N/A	:	2017	20 388.7
SDG 14 – Life below water										
Ocean health	Coastal water bathing sites with excellent water quality	% of bathing sites with excellent water quality	2013	34.7	2018	57.1	2013	85.5	2018	87.1
	Mean ocean acidity	pH value	N/A	:	N/A	:	2013	8.06	2018	8.06
Marine conservation	Surface of marine sites designated under NATURA 2000	km^2	2013	1 888	2018	6 362	2013	251 566	2018	551 899
Sustainable fisheries	Estimated trends in fish stock biomass	index 2003 = 100	N/A	:	N/A	:	2012	110.0	2017	136.0
	Assessed fish stocks exceeding fishing mortality at maximum sustainable yield (Fmsy)	% of stocks exceeding fishing mortality at maximum sustainable yield ($F>F_{MSY}$)	N/A	:	N/A	:	2012	52.9	2017	42.7
SDG 15 – Life on land										
Ecosystems status	Share of forest area	% of total land area	2012	32.5	2015	34.1	2012	40.3	2015	41.6
	Biochemical oxygen demand in rivers	mg O_2 per litre	2012	3.33	2017	3.22	2012	2.06	2017	2.00
	Nitrate in groundwater	mg NO_3 per litre	N/A	:	N/A	:	2012	19.2	2017	19.1
	Phosphate in rivers	mg PO_4 per litre	2012	0.096	2017	0.098	2012	0.096	2017	0.093
Land degradation	Soil sealing index	index 2006 = 100	2009	101.5	2015	106.0	2009	101.7	2015	104.2
	Estimated soil erosion by water	km^2	2010	16 159.3	2016	15 695.7	2010	207 232.2	2016	205 294.5
	Settlement area per capita	m^2	2012	355.2	2015	364.8	2012	625.0	2015	653.7
Biodiversity	Surface of terrestrial sites designated under NATURA 2000	km^2	2013	53 788	2018	54 214	2013	787 766	2018	784 252
	Common bird index	index 2000 = 100	N/A	:	N/A	:	2013	94.7	2018	93.5
	Grassland butterfly index	index 2000 = 100	N/A	:	N/A	:	2012	72.2	2017	74.1

(Continued on the next page)

Table (continued)

SDG / Sub-theme	Indicator	Unit	Romania Starting year	Romania Starting value	Romania Latest year	Romania Latest value	EU-28 Starting year	EU-28 Starting value	EU-28 Latest year	EU-28 Latest value
SDG 16 – Peace, justice and strong institutions										
Peace and personal security	Death rate due to homicide	number per 100 000 persons	2011	2.2	2016	1.6	2011	0.9	2016	0.6
	Population reporting occurrence of crime, violence or vandalism in their area	% of population	2013	15.7	2018	11.5	2013	14.5	2018	12.7
	Physical and sexual violence to women experienced within 12 months prior to the interview	% of women	N/A	:	2012	7	N/A	:	2012	8
Access to justice	General government total expenditure on law courts	million EUR	2012	459	2017	897	2012	48 381	2017	51 027
	Perceived independence of the justice system	% of population	2016	51	2019	40	2016	52	2019	56
Trust in institutions	Corruption Perceptions Index	score scale of 0 (highly corrupt) to 100 (very clean)	2013	43	2018	47	N/A	:	N/A	:
	Population with confidence in the EU Parliament	% of population	2013	49	2018	60	2013	39	2018	48
SDG 17 – Partnerships for the goals										
Global partnership	Official development assistance as share of gross national income	% of GNI	2013	0.07	2018	0.11	2013	0.43	2018	0.48
	EU financing to developing countries	million EUR, current prices	2012	:	N/A	:	2012	147 962	2017	155 224
	EU imports from developing countries	million EUR, current prices	2013	8 669	2018	15 024	2013	817 475	2018	1 013 981
Financial governance within the EU	General government gross debt	% of GDP	2013	37.6	2018	35.0	2013	86.3	2018	80.4
	Shares of environmental and labour taxes in total tax revenues	% of total tax revenues	2013	7.5	2018	8.0	2013	6.4	2018	6.1

Source: Eurostat

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