Fiscal Council of Romania

Fiscal Council's Opinion on the Third Budget Revision for 2020

Summary

- The economic shock of the pandemic is stronger than the one caused by the Great Recession. The Great Lockdown led to a dramatic double-digit decline in GDP in most European Union (EU) countries in the second quarter of this year. The third quarter showed a strong recovery in economic activity.

- Fighting the Pandemic and the induced economic crisis required exemplary resource mobilization. Public budgets have come to the forefront of the fight against the effects of the Pandemic and of the economic crisis, even as central banks have continued, or expanded unconventional policies - through quantitative easing (QE) and very low monetary policy rates (including negative ones, in nominal terms, in the case of the European Central Bank (ECB)).

- But the practices of developed economies (in which reserve currency is issued), including massive purchases of government bonds, cannot be replicated by emerging economies, which face currency constraints and have less robust economies, with significant deficits.

- The second wave of the Pandemic interrupts/slows the economic recovery in the fourth quarter of the current year. The evolution of the EU economy is appearing to follow a W pattern, due to a likely economic contraction in the fourth quarter of this year, as anticipated by the ECB and the European Commission (EC). A 7.4% decline in economic activity across the EU is forecasted for this year.

- The recovery of the GDP level is expected for 2022, but under the conditions of profound changes in economies, which are accelerated by new technologies (digitalization, robotics etc.) and the need to respond to climate change. The development of vaccines and therapies will support the recovery and will help changing the mood towards optimism in society.

- The Fiscal Council (FC) appreciates that the revised macroeconomic scenario of the Government which anticipates an economic contraction of 4.2%, although more adequate

compared to the previous one (which projected a 3.8% contraction of real GDP), seems more optimistic in comparison to the evolution of the economy and the Pandemic. FC considers that its previous range for economic growth in the current year, of a contraction between 4-6%, remains valid with an increasing probability that the GDP reduction will be situated in the second part of the range.

- The third budget revision increases the 2020 budget deficit projection to 9.1% of GDP, respectively by 0.5 pp above the level considered for the budget revision operated in August. The main causes of this development are: the unfavorable and large-scale impact on the budget revenues of the facility for deferring the payment of budget obligations by economic agents; the deterioration of the macroeconomic framework compared to the previous one; shortcomings of the budgetary construction.

- The key element for assessing the revenue projection from the third budget revision is the impact of the facility for deferring the payment of economic agents' obligations towards the general consolidated budget (GCB).

- FC considers as probable that fiscal revenues and social security contributions, together with other revenues, will exhibit a total negative gap of approximately 6.5-7.5 billion lei (about 0.65%-0.75% of GDP) in 2020. According to FC, this gap stems from NAFA's optimistic assessment of the amounts recoverable this year from the deferred obligations to be paid by economic agents, as well as from the high probability that the amounts related to renting 5G frequency bands will not be collected this year. It should be noted that this revenue gap, estimated by FC for 2020, is recoverable in the following year and will support the cash execution. From the perspective of the ESA methodology, the execution is not influenced by the elements identified by the FC that lead to this revenue gap for the current year.

- Regarding the new estimates for budget expenditures, FC has reserves only in the case of expenses with goods and services, but appreciates that additional funding needs may be covered by allocations from the reserve fund or may be offset by savings at the level of other expenditure aggregates.

- FC estimates a plausible level of the budget deficit for 2020, according to the cash methodology, at around 9.8% of GDP, by 0.7 pp above the MPF estimate as a result of identifying a probable revenue gap.

- Romania started the fight against Covid-19 with a large structural deficit, over 4% of GDP, the largest in the EU, as well as with the largest external deficit (of the current account) among emerging economies in the EU.

- The large structural deficit has reduced the Government's room for maneuver. The limited room for maneuver explains, to a large extent, why the recovery of the Romanian economy in the third quarter is inferior to many similar processes in the EU.

- In 2021, most EU countries will have substantially declining budget deficits through the reduction of non-permanent spending that has been induced by the Pandemic and the economic crisis. They will probably reach, as an arithmetic average, deficits around 5% of GDP and only Romania would remain at an almost double level of the deficit, if no adjustments were made and under the conditions of a 14% increase in the pension point. In 2022, the difference between Romania and the other EU states regarding the budget deficit would be even more striking. Markets would not finance deficits of more than 8-9% of GDP for years. By 2022, we would reach a public debt level of more than 55% of GDP and financing would be more and more problematic. Therefore, the macroeconomic correction should start in 2021.

- A macroeconomic correction imagined as being helped by a drastic decrease in interest rates on the Romanian money market, by substantial injections of liquidity by the NBR and operations with government securities on the domestic financial market, is counterproductive; confidence in the national currency would be lost, inflation would be greatly stimulated, it would be a disaster for financial and economic stability.

- Romania's macroeconomic problem must be addressed essentially by the credible, albeit gradual, reduction of the budget deficit.

- The position of public finances at the end of 2020 is important as it represents the starting point of the budgetary construction for 2021.

- Even if the 2020 budget execution includes one-off elements (estimated by the FC at about 1.5-2% of GDP, of which 0.4 pp financed by EU transfers), measures to combat the effects of the COVID-19 pandemic, a large part of the budget deficit is structural in nature and will continue in the future. Thus, considering the fiscal policy measures already adopted (increasing pensions, wages, child allowances according to the calendar announced by the Government) and eliminating one-off measures, the starting point of the budget deficit for 2021 will be about 8% of GDP. Given that the effects of the Pandemic will continue in 2021, at least some of the one-off measures are likely to be maintained, which would lead to a higher starting point for the 2021 budget deficit, possibly around 9% of GDP.

- Recent years have seen a sharp increase in personnel and social assistance expenditures as a percentage of GDP and tax revenues. This development, unfortunately, is also reflected by a sharp increase in the structural deficit of the public budget. In 2020, a peak was reached in this respect, personnel and social assistance expenditures representing 92.3% of tax revenues (including social security contributions). This situation is not sustainable in itself and is all the more to be judged from the perspective of the need for macroeconomic and budgetary correction.

- In this context, characterized by very high levels of the budget deficit, it is mandatory to implement a correction that will lead in the medium term to much lower levels of the budget deficit and that will anchor creditors' expectations towards a sustainable trajectory of the fiscal-budgetary policy.

- The announcement of a credible multi-annual fiscal/budgetary consolidation plan could provide the necessary time for a gradual approach that would affect the economic recovery as little as possible.
- The macroeconomic correction (reduction of the budget deficit) must take into account both the restructuring of expenditures and increasing fiscal/budgetary revenues. It is a false thesis that fiscal/budgetary revenues cannot be increased, especially by broadening the tax base. The tax system must be transparent and fair; all citizens and companies must pay - loopholes that make the tax regime unfair should be eliminated. Tax evasion should not be tolerated, as well as incorrect tax optimizations (tax avoidance) and undue rents.
- An intense absorption of European funds, which would capitalize on the almost double amount of resources allocated to Romania for the 2021-2027 period (due to the emergence of the European Recovery Plan *Next Generation EU* of 750 billion euros, of which Romania would benefit from 33.2 billion euros), could help substantially the macroeconomic correction efforts during the following 3-4 years.
- A successful macroeconomic correction would create the prerequisites for Romania to enter the Exchange Rate Mechanism 2 (ERM2) by 2025.

Fiscal Council's Opinion on the Third Budget Revision for 2020

On November 18th, 2020, the Ministry of Public Finance (MPF) sent to the Fiscal Council (FC), by address no. 476103 / 18.11.2020, the documents related to the third budget revision of this year, requesting, following art. 53, para. (2) of the Law on Fiscal-Budgetary Responsibility (no. 69/2010, republished, hereinafter referred to as FRL), the FC's opinion on them. Subsequently, the FC requested other relevant information from the Ministry of Public Finance, such as the scheduled dynamics of European funds, swap operations, as well as some explanations on the dynamics of fiscal-budgetary aggregates. All these data and explanations strictly necessary for the analysis were received on November 20th, 2020.

1. The global economic context created by the pandemic

The economic shock of the pandemic is stronger than the one caused by the Great Recession. The Great Lockdown led to a dramatic double-digit decline in GDP in most European Union (EU) countries in the second quarter of this year. The third quarter showed a strong recovery in economic activity.

The second wave of the Pandemic interrupts/slows the economic recovery in the fourth quarter of the current year. The evolution of the EU economy is appearing to follow a W pattern, due to a likely economic contraction in the fourth quarter of this year, as anticipated by the ECB and the European Commission (EC). A 7.4% decline in economic activity across the EU is forecasted for this year.

The recovery of the GDP level is expected for 2022, but under the conditions of profound changes in economies, which are accelerated by new technologies (digitization, robotics etc.), by the need to respond to climate change. The development of vaccines (Pfizer-BioNTech, Moderna etc.) and therapies will help changing the mood towards optimism in society.

Combating the pandemic and the induced economic crisis has called for exemplary resource mobilization. Public budgets are extremely tense, even in developed countries.

Public budgets have come to the forefront of the fight against the effects of the Pandemic and economic crisis, even as central banks have continued, or expanded unconventional operations - through quantitative easing (QE) and very low monetary policy rates (including negative ones, in nominal terms, in the case of ECB).

Budget deficits have increased a lot, through non-permanent expenditures - to support demand, companies, technical unemployment, etc. Thus, the decrease of the natural interest rates, of the monetary policy rates is capitalized, which would allow the stabilization of the public debts even in conditions of primary deficits.

But the practices of developed economies (in which reserve currency is issued), including massive purchasing of government bonds, cannot be replicated by emerging economies, which face currency constraints and have less robust economies, with significant deficits.

The outcome of the US presidential election is likely to stop dismantling multilateral arrangements in the system of international economic relations, the US return to the Paris Agreement (on climate change), the positive review of the status of the World Trade Organization (WTO), WHO etc. All this can change the overall global economic climate for the better.

However, a Brexit without an agreement between the United Kingdom and the EU would have further adverse effects on the European economy.

If we are now in a period of great vitreous (health crisis and economic crisis), in the coming years we will go through a great transition - induced by the need to combat global warming, "greening", structural transformation of economies, which will stress public and private budgets.

2. Considerations on the economic situation and the third budget revision for 2020

2.1. Analysis of the macroeconomic projection that substantiates the third budget revision

Similar to previous opinions, FC starts in its considerations regarding the third budget revision this year, from the extraordinary circumstances caused by the pandemic caused by the SARS-CoV-2 virus, as well as from its very severe economic and social impact.

The coordinates of the macroeconomic scenario that substantiates the projection of the Government's fiscal-budgetary aggregates envisages the new projection - from November 2020 - recently published by National Commission for Strategy and Prognosis (NCSP), as well as the accompanying note related to this forecast. FC starts in its analysis from the unprecedented uncertainty in recent history, induced by the evolution of the public health situation, regarding both the macroeconomic scenario and the dynamics of fiscal-budgetary aggregates, as well as the biunivocal interaction between them. The large uncertainties, which could widen the more probable intervals for real economic activity as well as for the evolution of other indicators, are contrasted, in the case of the current revision, by the relatively short interval until the end of 2020, which makes that the remaining few weeks of the current year may not be able to determine large variations from their average already recorded so far - which tends to narrow the probable intervals for macroeconomic variables, but also for fiscal-budgetary ones.

The high uncertainty of future economic developments stems from the combination of several relevant factors: (i) the fact that a new wave of the coronavirus pandemic is spreading at both European and national level, (ii) with effects on the dynamics of major partner economies (mainly European) trade in Romania, as a result of the re-establishment of local or even general restrictions in some of these states, which in turn influence both the course of these partner economies and that of the national economy, (iii) the reintroduction of local restrictions in Romania, which have a mitigating effect on the amplitude and speed of economic recovery, (iv) the fact that some uncertainties persist in the collection and aggregation of statistical data which makes their use induce the implicit incorporation of intervals increased confidence. In the opposite direction, the revitalization of activity and the reduction of uncertainty could act in particular (v) the change of expectations, and implicitly of consumption and investment behavior, related to households and firms in the economy, due to the relatively close prospect of vaccination of a relevant segment of the population, at national and European level as well as (vi) the relative resilience demonstrated by the Romanian labor market at an aggregated level, but with relatively important structural changes in the pandemic context.

In the analysis of the evolution of real GDP, which reflects the dynamics of the real economy, projected by NCSP to contract, this year, by 4.2%, in the data set underlying the current revision, we can start from the reality of a severe contraction, without a precedent given the size of the negative amplitude in the available data series, in the second quarter of this year, the annual and quarterly contraction of the activity being 10.3% and 11.9%, respectively. This contraction has as main determinants the reduction of the dynamics of domestic demand, especially of the consumption of the population, but also of the variation of stocks - stockpiling being a characteristic of the crisis periods - only partially counterbalanced by the gross fixed capital formation, as well as the consumption of public administration, which thus exercised an anti-cyclical impact, considering also the transition of the economy in the very probable situation of a significant demand deficit, as a result of the ample contraction of the economic activity. Subsequently, according to NIS[1] data, real GDP registered a significant recovery in the third quarter of this year, albeit considerably smaller in absolute terms than the previous contraction, which shows both a slower return to the previous level and a change in the structure, the unequal advance being concentrated at the level of retail sales, in contrast to the slower dynamics at the level of services provided to the population within the GDP. At the same time, agriculture has a poorer performance, with all the important advances in certain segments of it (for example the production of fruits and vegetables). Given these developments, as well as the dynamics of high frequency indicators in the economy, corroborated with the re-establishment of local restrictions in Romania, and some local and general at the level of the main partner economies in the EU, with definite influence at the level of the local economy, **we believe that the revised macroeconomic scenario of the Government, which predicts a contraction of GDP of 4.2%, although more adequate compared to the previous one (which projected a contraction of real GDP of 3.8%), seems more optimistic in relation to the evolution of the economy and the Pandemic**. At the same time, we note that the range proposed by FC for the economic dynamics this year, of a contraction between 4-6%, remains valid, being confirmed by the latest government projection, noting that recent data and trends shift the center of gravity of probabilities associated with projections towards the middle of the interval characterized by a larger magnitude of economic contraction. At the same time, in the structure of real GDP dynamics, we notice the lower emphasis, in the Government's projection, attributed to the contraction of domestic consumption offset by the dynamics of net exports. FC appreciates that this structure of GDP also induces risks regarding the dynamics of fiscal aggregates, because a contraction located mainly at the level of internal absorption, which seems relatively probable, will determine an economic contraction with a more severe impact on the level of taxes levied.

Regarding the dynamics of the GDP deflator, of the prices of goods and services included in GDP, considered in the current macroeconomic scenario of the Government, the advance of 3.4% for 2020 involves a series of risks determined mainly by the already registered evolution of the economy, but also deriving from the trends revealed by the data. Thus, if we consider that the GDP deflator can be approximated, from the point of view of the trend, by a combination of the dynamics of consumer prices and those related to industrial production, we notice that, regarding the first indicator, in October 2020, it decreased to 2.2% and seems to have been on a downward trajectory, towards the end of this year and the beginning of next year, mainly under the impact of significant base effects (higher levels of inflation in the fourth quarter of 2019 and the first

[1] Signal estimates on the evolution of GDP, in the third quarter of 2020 published on November 13th 2020.

quarter of 2020). Regarding industrial production prices - the second indicator considered relevant for assessing the dynamics of the GDP deflator - it has been in negative territory since the first quarter of 2020, and recent data from September 2020, published by the NIS, show the relative increase in his descendant dynamics. On the contrary, of a more consistent evolution of prices in the economy, we can consider that both the higher costs imposed by the pandemic at the firm level and the still high persistence of core inflation in the economy, as well as the still high level of expectations about the dynamics of prices at the level of households and companies. However, these influences seem to have dissipated their effects in the sense of rising prices recently, under the impact of both a large demand deficit that is beginning to weigh more heavily on consumption and saving / investment decisions in the economy, and new restrictions imposed related to the sanitary situation. For these reasons, the FC considers that the projection of the GDP deflator, in the revised macroeconomic scenario of the Government, could be more optimistic in relation to the actual evolution of the economy.

The risks of slight overestimation previously revealed, both in terms of real GDP dynamics and the related deflator, which combine their effects at the level of nominal GDP dynamics, highlight a possible overestimation, in the opinion of FC, at the level of this indicator. In addition, the structure of real GDP dynamics is more favorable, in the Government's projection, to the collection of higher taxes, likely to reduce the budgetary deficit.

Regarding the dynamics of the labor market, in assessing the Government's projection, we can start, on the one hand, from the resilience of the economy shown so far, especially due to the resumption of activity in many sectors after the lowering of restrictions related to physical mobility, but on the other hand we have to consider the impact that the re-imposition of some of these restrictions at the local level will have in the next period, as a result of the unfavorable evolution of the pandemic situation. We can also mention that the dynamics of the labor market is particularly important for the evolution of the personal income tax and SSC revenues as well as for some elements of expenditure such as unemployment benefits and social transfers - all with a significant aggregate impact on the level of fiscal deficit. In the Government's projection, the average number of employees in the economy is expected to decrease by 1.4% (respectively 1.7% according to the AMIGO methodology) in the current year, and the gross earnings to increase by 6.3%. Existing labor market[2] data show, on the one hand, a less pronounced negative dynamic (lower reduction in the number of employees and a resilient dynamic of the nominal wage), cumulated in the first three quarters of the year, but which can be corroborated with a more negative outlook in the last quarter of the year, due to the combined effect of re-imposing restrictions on physical mobility and triggering more unfavorable labor market dynamics as a result of increased pressures on production costs and capping price increases, affecting both the number of employees and the evolution of gross earnings. However, the result of these contrary

[2] Among which we can list those from the NIS on employment and unemployment in the second quarter, trends in the evolution of economic activity between October and December 2020 and the average gross earnings per economy in September 2020.

influences indicates the relative adequacy of the coordinates of the government scenario on the labor market, the risks being, in the FC's opinion, in the sense of a possible small overestimation, in the Government's projection, of labor market developments.

All the elements presented above regarding the evolution of the macroeconomic indicators projected in the third revision of the budget this year reveal, in the FC's opinion, a slightly more optimistic vision of the Government, in relation to the statistical data and short-term forecasts, regarding the labor market as well as the risk of a more relevant deviation in terms of the level of nominal GDP and its composition, relevant from a fiscal point of view. Moreover, this assessment is supported both by the EC projections (detailed in the autumn projection for 2020) and by the forecasts of other public and private institutions, Romanian and foreign, recently published.

2.2. The big trade-off: limited room for maneuver due to the large structural deficit

Romania started the fight against Covid-19 with a large structural deficit, over 4% of GDP, the largest in the EU, as well as with the largest external deficit (of the current account) among emerging economies in the EU.

The large structural deficit has reduced the Government's room for maneuver. The limited room for maneuver explains, to a large extent, why the recovery of the Romanian economy in the third quarter is inferior to many similar processes in the EU.

The budget deficit in 2020, over 9% of GDP, will be in line with deficits in emerging economies in the region, but starting from the handicap mentioned. The decline in GDP in 2020 will probably be around 5% given the second wave of the pandemic. FC estimated at the beginning of 2020 that the GDP decline will be in a range of 4-6%, noting that the evolution of the pandemic is important for the effective dynamics of the economy.

In 2021, most EU countries will have budget deficits declining considerably by reducing non-permanent spending that has been induced by the Pandemic and the economic crisis. It will probably reach, as an arithmetic average, deficits around 5% of GDP and only Romania would remain at an almost double level of the deficit if no adjustments were made, and in the conditions of increasing the pension point by 14%. In 2022, the difference between Romania and the other EU states regarding the budget deficit would be even more striking.

Markets would not finance deficits of more than 8-9% of GDP for years. We would reach over 55% of GDP in 2022 with public debt, and financing would be more and more problematic. Therefore, the macroeconomic correction should start in 2021.

A macroeconomic correction imagined as being helped by a drastic decrease in interest rates on the Romanian money market, by substantial injections of liquidity by the NBR and operations with government securities on the domestic financial market, is counterproductive; confidence in the national currency would be lost, inflation would be greatly stimulated, it would be a disaster for financial and economic stability.

An intense absorption of European funds, which would capitalize on the almost double amount of resources allocated to Romania for the period 2021-2027 (due to the emergence of the European Recovery Plan Next Generation EU of 750 billion euros, of which Romania would benefit from 33.2 billion euros[3]) could help substantially the macroeconomic correction efforts during the following 3-4 years.

The announcement of a credible multi-annual fiscal/budgetary consolidation plan could provide the necessary time for a gradual approach that would affect the economic recovery as little as possible.

The macroeconomic correction (reduction of the budget deficit) must take into account both the restructuring of expenditures and increasing fiscal/budgetary revenues. It is a false thesis that fiscal/budgetary revenues cannot be increased, especially by broadening the tax base. The tax system must be transparent and fair; all citizens and companies must pay - loopholes that make the tax regime unfair should be eliminated. Tax evasion should not be tolerated, as well as incorrect tax optimizations (tax avoidance) and undue rents.

A successful macroeconomic correction would create the prerequisites for Romania to enter the Exchange Rate Mechanism 2 (ERM2)[4] by 2025.

2.3. Romania's situation in relation to the fiscal rules of the European Union

Since June 2017, Romania has been on the preventive arm of the Stability and Growth Pact (SGP), being under the Incidence of the Significant Deviation Procedure (SDP) from the MTO[5]. The latest notification from the EC regarding the deviation from the MTO, in November 2019[6], stated that this was in addition to the foreseeable exceeding the 3% of GDP for the budget deficit threshold.

In the case of Romania, which ended the execution of the general consolidated budget in 2019 with a deficit of 4.6% of GDP, at the beginning of March 2020, the EC recommended to the Council

[3] In total, Romania can receive European funds worth 80 billion euros in the coming years through the "Next Generation EU" Recovery Plan and the Multiannual Budget of the European Union 2021-2027.

[4] Antechamber for the entrance in the euro area where a country stays for at least 2 years to check the robustness of the public budget and the soundness of the equilibria in the economy.

[5] Without following the repeated recommendations of the European Commission and the EU Council to undertake an annual fiscal adjustment effort to bring closer and convergence with the MTO target, namely a structural deficit of 1% of the potential GDP, in the period 2016-2019 the gap to this target has gradually and continuously increased from 1.6 pp to over 3.5 pp.

[6] Council Recommendation with a view to correcting the significant observed deviation from the adjustment path toward the medium-term budgetary objective in Romania (COM/2019/ 912 final), Brussels, 20.11.2019.

the initiation of the Excessive Deficit Procedure (EDP)[7]. Arguing that Romania's violation of fiscal rules precedes the onset of the COVID-19 pandemic, in early April 2020, the EU Council decided that, in accordance with Article 126 (6) TFEU, there is an excessive deficit in Romania and approved the start of the EDP[8][9]. Meanwhile, the special circumstances of the COVID-19 pandemic and its severe impact led, in the last decade of March 2020, to the activation of the general derogation clause of the SGP by the EC, by which the fiscal rules of the European budgetary framework were temporarily suspended in 2020, with an extension in 2021.

Given the global economic and budgetary impact of the pandemic, as well as the uncertain horizon of the post-COVID recovery, it became obvious that the budget deficit targets, set for Romania under the EDP[10], could not be achieved.

In November 2020, the EC updated its position regarding the fiscal situation in Romania[11], stating that, for the time being, it cannot take any decision on the EDP-related measures, including a credible projection for fiscal policy, given the exceptional uncertainty created by COVID-19 pandemic. Thus, Romania's budgetary situation, including fiscal risks, will be reassessed in the spring of 2021, based on the results of the 2020 budget execution, the 2021 budget and the Commission's spring forecast.

Under these circumstances, Romania is notified that sound economic and fiscal governance is an important premise for ensuring an environment conducive to public investment and attracting EU funds, including access to the Recovery and Resilience Facility (RRF). It is also necessary to take into account the established evaluation criteria that require Romania's Recovery and Resilience Plan to contain measures appropriate to the challenges identified in the country-specific recommendations, in particular those relating to structural reforms.

Both from the message that emerges from this EC communication, and from reasons to avoid the risk of major slippages of macroeconomic and financial balances, it results that it is vital for Romania that the fiscal consolidation process starts in 2021.

[7] Recommendation for a Council Recommendation with a view to bringing an end to the situation of an excessive government deficit in Romania (COM/2020/91 final), Brussels, 4.3.2020.
[8] Council Recommendation of 3 April 2020 with a view to bringing an end to the situation of an excessive government deficit in Romania (OJ C 116, 8.4.2020).
[9] In summary, corrective measures were recommended leading to targets of the budget deficit of 3.6% of GDP in 2020, 3.4% in 2021 and 2.8% in 2022. Obviously, given the Pandemic and the economic crisis, this calendar is no longer relevant.
[10] Council Recommendation of 20 July 2020 on the 2020 National Reform Programme of Romania and delivering a Council opinion on the 2020 Convergence Programme of Romania (OJ C 282, 26.8.2020).
[11] Communication from the Commission to the Council on Fiscal situation in Romania (COM/2020/752 final), Brussels, 18.11.2020.

3. Updated coordinates of budgetary revenue and expenditure related to the third budget revision

The third budget revision increases the budget deficit projection for 2020 to 9.1% of GDP, respectively by 0.5 pp above the level considered for the budget revision operated in August this year. This evolution has as main causes:

- the unfavorable and large-scale impact on the budgetary revenues of the facility regarding postponing the payment of budgetary obligations by the economic agents. It should also be noted that this facility was extended compared to what was considered at the time of the adoption of the draft budget revision in August this year;
- the deterioration of the macroeconomic framework compared to the previous one (projected decrease of real GDP of 4.2% compared to 3.8%), nonetheless this is smaller compared to its revisions from the first two budgetary amendments of this year;
- shortcomings in the budget construction.

In its opinion on the second budget revision in 2020, the FC predicted a likely level of the budgetary deficit for this year between 8.6% and 9.4% of GDP, mainly as a result of considering a more unfavorable macroeconomic scenario compared to that provided by the Government (economic decline between 4 and 6% compared to 3.8%). The FC also noted the risks to budget revenues associated with the uncertainty of the amounts recovered from economic agents on account of deferred budgetary obligations. The government announced at that time a level of about 7 billion lei, corresponding to a degree of outstanding amounts recovered of 70%.

Compared to the parameters approved by the second budget revision operated in August this year, the third budget revision significantly decreases the total estimated revenues of GCB by 4.2 billion lei, while the total budget expenditures are increased by 0.8 billion lei, the budget deficit being thus increased by about 5 billion lei. The third budget revision maintains the level envisaged in the second budget correction for the swap - chain compensation scheme of arrears - to the GCB, with a symmetrical impact on revenue and expenditure (and therefore neutral on the budget deficit). Therefore, swap schemes do not influence the assessment of changes in the projections of the budget aggregates contained in this draft budget revision.

The negative revision of the revenue projection in the amount of 4.2 billion lei has as main causes lower anticipated levels of receipts from fiscal revenues (-1.3 billion lei), from non-fiscal revenues (-0.9 billion lei) , as well as from the amounts received from the EU / other donors on account of the payments made and pre-financings related to the financial framework 2014-2020 (-2.2 billion lei).

In the FC's opinion, **the key element for assessing the projection of budget revenues from the third budget correction is the impact of the facility to defer the payment of obligations to GCB**

of the economic agents. In order to support companies in the context of the economic difficulties generated by the COVID-19 pandemic, the Government decided to allow the deferral of payments due to the GCB, initially for the period March-June (GEO no. 29/2020 of March 21, GEO no. 48/ 2020 in force from April 16th, 2020), subsequently extended until October 25th (GEO no. 99/2020 in force from June 25th, 2020). It should be noted that the facility had a wide applicability, not being limited to companies whose activity was severely affected by the COVID-19 pandemic, which is likely to generate adverse selection, respectively companies that can pay tax obligations choose not to do so, given the advantages of the scheme. However, given the initial deadline of 25th of October for the payment of outstanding amounts, the facility only had an impact from the perspective of the public finances' liquidity position. In fact, FC considered in the forecast of budget revenues for 2020, the amount of 7 billion lei estimated by NAFA as recoverable from the total deferred tax liabilities in the amount of about 10.3 billion lei in June 2020. In October this year the Government approved a new modification of this facility by GEO no. 181/2020 (in force since October 26th, this year), offering the possibility of staggering the outstanding fiscal obligations for 12 months by submitting an application until the end of the this year, but this time the facility also involves the payment of an interest of about 3.65% per year**. Given this latest change, the facility no longer has an impact only on the liquidity position of public finances in 2020, but also on the budget revenues for the current year and further on the cash budget deficit[12].**

According to NAFA, on September 30th this year, the total amount of obligations to GCB deferred to payment by economic agents was about 16 billion lei, of which the recovery of the amount of 5.3 billion lei is expected until the end of December 2020 (2.9 billion at the level of VAT, 0.5 billion at the level of the personal income tax, 1.9 billion lei at the level of social security contributions). The FC notes, on the one hand, the major impact of this scheme, of approximately the same magnitude as the budget expenditures intended to combat the effects of the COVID-19 pandemic, and, on the other hand, notes the very high uncertainties (higher than those existing at the second budgetary revision) regarding the recovery of these amounts in 2020 at the level estimated by NAFA. Thus, the payment of these obligations can be made in advantageous conditions, at a lower interest rate than in the market for lending to companies and it is therefore anticipated that a significant part of the economic agents that have resorted to deferring tax obligations to continue deferring the payment of the amounts over the next 12 months. Moreover, the amounts deferred for payment will probably increase even more compared to the level recorded on September 30 this year. Having in view of all above mentioned, the FC has reservations regarding the amounts anticipated to be recovered by the end of December 2020 from deferred tax liabilities and therefore on the level of current projections of revenue aggregates that include these amounts

[12] The statistical treatment from the perspective of the ESA 2010 methodology will probably involve considering, at least in part, the amounts deferred to be paid as budgetary revenues for 2020 even if the amounts will actually be collected in 2021.

(noting that these amounts are recoverable in 2021, at least in part, and will support the budget revenues in that year).

It should also be noted that more unfavorable developments in the economy compared to the most recent NCSP forecast are partially accommodated in the FC assessment below by taking into account the current budget execution that already incorporates the evolution of the economy so far.

By revenue categories, revisions of the previous estimates occur as follows:

- *Amounts received from the EU/other donors on account of payments made and pre-financing related to the 2014-2020 financial framework*: -2.2 billion lei. This revision occurs mainly as a result of the decrease of the amounts transiting the general consolidated budget intended for pre-financing of the projects of the non-governmental sector in case of temporary unavailability of European funds, based on art. 10 of GEO no. 40/2015 (-3 billion lei), while the amounts related to European funds for agriculture increase by 1.1 billion lei, and the amounts from structural and cohesion funds are decreased in planning by about 0.3 billion lei. As the FC showed in its opinion on the previous budget revision, the first two categories, which were not included in the cash budget execution before 2016, represent European funds whose beneficiary is the private sector and have a symmetrical impact on revenue and expenditure, only transiting the consolidated general budget and not being relevant in assessing the position of public finances *stricto sensu*. Therefore, there is no relevant change in this budgetary aggregate from the perspective of GCB's position. Given the up-to-date execution, FC notes the existence of risks regarding the materialization of the European funds revenue projection at the expected level taking into account the relatively high gap between it and the 9-month execution, even if traditionally the absorption of European funds accelerates strongly in the last part of the year. However, these risks appear to be lower than those existing in previous years at the time of the last budget revision of the year.

- *Fiscal revenues*: -1.3 billion lei, out of which:

    - *Corporate income tax*: -0.8 billion lei. The revision is explained by the decrease in the same amount of the amounts anticipated by NAFA to be recovered from the amounts deferred for payment related to this category. In the opinion of FC, the MPF' proposed level appears as plausible.
    - *Personal income tax*: +0.27 billion lei. The revision is compatible with the up-to-date budget execution and with the consideration of the amounts recovered from the deferred budgetary obligations according to the NAFA estimate. The FC has already expressed its reservations about the latter and, therefore, we consider as probable

the appearance of a negative gap at the level of personal income tax. FC evaluates in an aggregate manner, at the level of all categories of budget revenues, the size of the revenue gap having as source the evaluation, optimistic in the opinion of FC, of the amounts expected to be recovered in 2020 from the budgetary obligations deferred to payment by economic agents.

- *Property tax*: -0.3 billion lei. The revision appears in line with the up-to-date budget execution.
- *VAT*: +0.4 billion lei. The revision is compatible with the up-to-date budget execution and with the consideration of the amounts recovered from the budgetary obligations deferred to payment according to the NAFA estimate (approximately 2.9 billion lei). On the issue of recovering the amounts deferred, FC has already expressed its reservations and, therefore, we consider as probable the occurrence of a significant revenue gap at the level of VAT receipts.
- *Excise duties*: -0.6 billion lei. The revision appears as justified in the context of up-to-date budget execution.
- *Taxes on the use of goods, on authorizing the use of goods and on carrying activities*: -0.04 billion lei, given that the revenue estimate of about 2.5 billion lei from the sale of 5G licenses by ANCOM was maintained. Given the short period of time remaining until the end of the year, the FC considers that there is a significant risk that these amounts will not be found in the cash budget execution for 2020. It should also be noted that this likely failure to achieve these revenues will affect only to a small extent the budget execution for 2020 according to the European methodology as, according to it, the revenues associated with the rental of frequency bands are distributed over the entire duration of the contracts.

- *Social security contributions*: +0.3 billion lei. The revision is compatible with the up-to-date budget execution and with the consideration of the amounts to be recovered from the budgetary obligations deferred to payment according to the NAFA estimate (approximately 1.9 billion lei). On the issue of the recovery of deferred payments, FC has already expressed its reservations and, therefore, we consider as very likely a significant revenue gap in the collection of social security contributions.

- *Non-fiscal revenues*: -0.87 billion lei. The assessment appears as prudent in the context of the up-to-date budget execution.

Summarizing, on the budgetary revenues side, we note the downward revisions in the level of current revenues (fiscal and non-fiscal) by about 2 billion lei, to which is added a decrease in the amounts provided from European funds, but the latter refers to less relevant elements from the perspective of assessing the position of public finances. A central element of the revenue projection for 2020 is the consideration of the collection of significant amounts from the budgetary obligations deferred to payment by the economic agents (5.3 billion lei in the conditions of an existing stock on September 30 this year of about 16 billion lei). **It is also important to point out the substantial change in the provisions of the deferred payment scheme of the remaining budgetary obligations of economic agents compared to the variant considered on the occasion of the previous budgetary revision in August, which is likely to significantly change the FC assessments on the budget revenue projection for 2020.** Thus, considering the plausible increase of the deferred budgetary obligations in the circumstances in which this facility is currently in force, as well as of the advantageous conditions for deferring the payment of the remaining budgetary obligations during 2021, FC considers as probable the materialization of a revenue gap in 2020 of approximately 4-5 billion lei (about 0.4% -0.5% of GDP) at the level of fiscal revenues and those from social security contributions. In addition, given that the organization of the tender for the rental of 5G frequency bands is unlikely to be completed this year (resulting in a decrease in cash execution of 2.5 billion lei), **FC considers as probable a gap in total tax revenues and social contributions plus other revenues of about 6.5-7.5 billion lei (about 0.65% -0.75% of GDP) in 2020.**

The budget expenditures are increased, on the occasion of the third budget revision, by about 0.8 billion lei, this evolution being determined mainly by the supplementation of social assistance expenditures (+2.5 billion lei), other transfers (+2.1 billion lei) and expenditures on goods and services (+1 billion lei), partially offseted by the reduction of capital expenditures (-2.6 billion lei), expenditures related to projects financed from non-reimbursable external funds (-1.4 billion lei) and the amounts available at the level of the reserve fund (-1 billion lei).

By categories of expenditure, revisions of previous estimates are as follows:

- *Personnel expenses*: +0.2 billion lei. The supplementation of the wage bill is intended to ensure the necessary funds for the payment of salary differences established by court decisions and administrative acts as well as the payment of salary rights related to the activities of preparation, organization and conduct of elections for the Senate and Chamber of Deputies in 2020. Given the latest information related to the budgetary execution, the FC considers as probable achieving the proposed new personal spending' target.

- *Reserve funds*: -1 billion lei. Although the amounts available at the level of the reserve fund are lower compared to the second budget revision by about 1 billion lei, in fact the amounts related to the reserve fund were supplemented by 1.2 billion lei, provided that the amounts previously existing in the reserve fund have been already spent, being now located at the level of other categories of budgetary expenditure.

- *Goods and services*: +1 billion lei. The supplementation of this budget aggregate validates the FC's assessment in its opinion on the second budget revision which identified an under-estimation of these category of expenditure. Under the new circumstances, the budget envelope is placed at a level of 55.6 billion lei, respectively by about 5.3% above the nominal level of 2019. In the first 9 months of 2020, this category of expenditures recorded a rate of increase of about 12.7% compared to the same period last year. In this context, even given the increase decided at the second revision, most likely this budgetary aggregate is under-budgeted by about 0.15-0.25% of GDP, a share of this additional need being able to be covered by allocations from the reserve fund.

- *Other transfers*: +2.1 billion lei. According to the clarifications sent by the Ministry of Public Finance, the main cause of this review is the registration of the amounts obtained from the auctioning of greenhouse gas emission certificates assigned to Romania at EU level, according to GEO no. 115/2011, amended and supplemented by GEO no. 81/2019. These amounts amount to 331 million euros (about 1.5 billion lei) and are found on both the revenue side and the expenditure side, without affecting the GCB balance, and the unused amounts by the end of the year will be carried over to the following year. To these are added +0.6 billion lei to supplement Romania's contribution to the EU budget, an expense that normally should be included in the draft budget.

- *Other expenses*: +0.8 billion lei.

- *Social assistance:* +2.5 billion lei. The main sources of the change are:

  - +1.8 billion lei to the state social insurance budget, as a result of the budget execution for the first 9 months of the year, which reveals a need for additional allocations. In the FC opinion, it is necessary to investigate the causes that generated an increase in pension expenditures above the level justified by the increase of the pension point, especially since the differences are important, respectively of the order of billions of lei. A relevant part of this additional amount may come from the variability of the correction index used in determining the initial pension, which needs to be rigorously analyzed. It should also be noted that the estimated level of expenditure related to this chapter is consistent with the reversal by the end of this year of the decision to pay in advance the pensions distributed through the Romanian Post; otherwise there is an additional need to the proposed level of 1.4 billion lei.
  - +0.5 billion lei for the National Health Fund needed for increasing the funds necessary for the payment of medical leaves.

The FC considers as probable the materialization of the new level proposed for this budgetary aggregate, being possible even lower expenditures by about 3-400 million lei, but notes that this evolution reveals new weaknesses in the budgetary construction, respectively the disclosure of a necessary permanent additional expenditures, of the order of 1.5 billion lei.

Recent years have seen a sharp rise in personal and social assistance spending as a percentage of GDP and of tax revenue. This development, unfortunately, is also reflected in the sharp increase in the structural deficit of the public budget. In 2020, a peak was reached in this respect, with personal and social assistance expenditures representing 92.3% of tax revenues (including SSC). This situation is not sustainable by itself and further more have to be judged from the perspective of the need for macroeconomic and budgetary correction (see figure in *Annex V*).

- *Capital expenditures*: -2.6 billion lei, mainly due to the decrease of the amounts allocated to this category at the level of the state budget (-1.6 billion lei at the Ministry of National Defense), respectively in the budget of fully or partly funded institutions from own revenues/activities (-1.6 billion lei). These reductions are partially offset by the supplementation of the amounts related to the National Local Development Program (NLDP) by 1 billion lei.

- *Projects financed from non-reimbursable external funds related to the 2014-2020 financial framework*: -1.4 billion lei. This revision occurs mainly as a result of the decrease in the need to refinance non-governmental sector projects in case of temporary unavailability of European funds, according to art. 10 of GEO no. 40/2015 (-3 billion lei), while the expenditures related to the European funds for agriculture increase by 1.1 billion lei. Expenditures related to projects financed from structural funds increase by almost 0.4 billion lei, but, as a result of the decrease in revenues from structural and cohesion funds in planning by about 0.3 billion lei, this increase in expenditures can be justified by appropriate supplementation of national co-financing, suggesting an underestimation of this aggregate in previous budgetary constructions. Given that the first two categories mentioned above (which also have a decisive impact on the revision of this aggregate) represent European funds for the private sector and have a symmetrical impact on revenue and expenditure, the data in the draft revision show that does not operate a major change in this budgetary aggregate from the perspective of the GCB's position.

Total public investment expenditures, from internal and external sources, decrease in planning by 2.4 billion lei, having as main source the reduction of capital expenditures by 2.6 billion lei, marginally offseted by the advance of expenditures related to projects financed from structural funds by almost 0.4 billion lei. The materialization of investment expenditures at the planned level can provide a stimulus to economic activity in the context of the difficult period we are going through. **Even with the reduction operated in this revision, the investment expenditures estimated by the current draft budget revision are about 24% higher in nominal terms than in the previous year, respectively their share in GDP is by 0.6 pp higher**[13]**.**

Summarizing, on the side of budgetary expenditures, from the perspective of GCB's position, the relevant changes refer to the increase of social assistance expenditures (+2.5 billion lei), goods and services (+1 billion lei), and also to the reduction in investment expenditures (-2.4 billion lei). In essence, additional weaknesses in budget construction are revealed, and these are offset by decreasing investment spending. **From the perspective of the plausibility of the new estimates for budget expenditures, FC has reservations only at the level of the aggregate of goods and services, but considers that the additional needs can be provided through allocations from the reserve fund or can be offset by some savings at other spending categories.**

Under these conditions, the FC estimates a probable level of the budget deficit according to the cash methodology of around 9.8% of GDP[14] **in 2020, with 0.7 pp above the MPF' estimate as a result of identifying a probable revenue gap.** This is attributable to the optimistic forecast of the Ministry of Public Finance regarding the amount of outstanding budget obligations to be paid by economic agents by the end of the year, as well as to the inclusion in the budget construction of the amounts from the tender for renting 5G frequency bands that seems very unlikely at this moment to be organized in 2020**.** It should be noted that this revenue gap identified by FC in 2020 is recoverable in the following year supporting the cash execution. **From the perspective of the execution according to the ESA methodology, it is not influenced by the elements identified by the FC that lead to this revenue gap for the current year.**

4. Compliance with fiscal rules

The draft of the third budget revision of the current year was elaborated based on GEO no. 181/2020, which at art. 23 stipulates that, by derogation from the provisions of art. 23 para. (2) of the FRL (which establishes the prohibition to approve more than two budget corrections in a budget year), in 2020 more than two budget revision may be approved. In the context of the exceptional situation generated by the COVID-19 pandemic, which also led to the successive unfavorable revision of the forecast of macroeconomic indicators, FC appreciates as justified the Government's decision to operate the third budget revision of this year.

[13] This estimate starts from the increase in the absorption of European funds this year compared to previous years.
[14] If we consider an economic decline according to the FC forecast, the cash budget deficit would be at the level of 9.9% of GDP.

The draft of the third budget revision provides for an increase in the ceilings of most of the indicators specified in the budgetary framework for 2020 (initially established by Law no. 238/2019 and then amended on the occasion of the first budget amendment by GEO no. 50/2020, amended subsequently, on the occasion of the second budget revision, by GEO no. 135/2020) as follows:

- the nominal ceiling of the GCB primary deficit is increased by 4.9 billion lei up to the level of 80.2 billion lei;
- the GCB deficit ceiling, expressed as a percentage of GDP, is increased by 0.5 pp up to 9.1%;
- the nominal ceiling of the GCB deficit is increased by 5.1 billion lei to the level of 96.1 billion lei;
- the nominal ceiling of the total expenditures of GCB, excluding financial assistance from the EU and other donors, is increased by 3 billion lei to the level of 394.3 billion lei;
- the public debt ceiling, expressed as a percentage of GDP, is increased by 3 pp up to the level of 47%;
- as regards the GCB personal expenditure in the revision proposal, it falls within both the ceiling set for the nominal level and the ceiling expressed as a percentage of GDP.

Having in view of the above, the draft of the GEO on the revision of the state budget for 2020 stipulates the necessary derogations from the fiscal rules established by the FRL and redefines the ceilings of the respective budgetary aggregates in accordance with the levels stipulated in the budget revision proposal.

5. Conclusions

The economic shock of the pandemic is stronger than the one caused by the Great Recession. The Great Lockdown led to a dramatic double-digit decline in GDP in most European Union (EU) countries in the second quarter of this year. The third quarter showed a strong recovery in economic activity.

Fighting the Pandemic and the induced economic crisis required exemplary resource mobilization. Public budgets have come to the forefront of the fight against the effects of the Pandemic and of the economic crisis, even as central banks have continued, or expanded unconventional policies - through quantitative easing and very low monetary policy rates (including negative ones, in nominal terms, in the case of the ECB).

However, the practices of developed economies (in which reserve currency is issued), including massive purchases of government bonds, cannot be replicated by emerging economies, which face currency constraints and have less robust economies, with significant deficits.

The second wave of the Pandemic interrupts/slows the economic recovery in the fourth quarter of the current year. The evolution of the EU economy is appearing to follow a W pattern, due to a likely economic contraction in the fourth quarter of this year, as anticipated by the ECB and the European Commission (EC). A 7.4% decline in economic activity across the EU is forecasted for this year.

The recovery of the GDP level is expected for 2022, but under the conditions of profound changes in economies, which are accelerated by new technologies (digitalization, robotics etc.) and the need to respond to climate change. The development of vaccines and therapies will support the recovery and will help changing the mood towards optimism in society.

The draft of the third budget revision increases the 2020 budget deficit projection by 0.5 pp of GDP up to a level of 9.1% mainly due to the unfavorable and large-scale impact on the budget revenues of the facility for deferring the payment of budget obligations by economic agents, the deterioration of the macroeconomic framework compared to the previous one, as well as due to shortcomings of the budgetary construction.

On the revenue side, FC considers as probable that fiscal revenues and social security contributions, together with other revenues, will exhibit a total negative gap of approximately 6.5-7.5 billion lei (about 0.65%-0.75% of GDP) in 2020. According to FC, this gap stems from NAFA's optimistic assessment of the amounts recoverable this year from the deferred obligations to be paid by economic agents, as well as from the high probability that the amounts related to renting 5G frequency bands will not be collected this year. Under these conditions, FC estimates a plausible level of the budget deficit for 2020, according to the cash methodology, around 9.8% of GDP, by 0.7 pp above the MPF estimate. It should be noted that this revenue gap, estimated by FC for 2020, is recoverable in the following year and will support the cash execution. From the perspective of the ESA methodology, the execution is not influenced by the elements identified by the FC that lead to this revenue gap for the current year.

Beyond the extremely high level of the budget deficit for the current year, which will lead to a corresponding increase in public debt, the position of public finances at the end of 2020 is important as it represents the starting point of the budgetary construction for 2021.

Even if the 2020 budget execution includes one-off elements (estimated by the FC at about 1.5-2% of GDP, of which 0.4 pp financed by EU transfers), measures to combat the effects of the COVID-19 pandemic, a large part of the budget deficit is structural in nature and will continue in the future. Thus, considering the fiscal policy measures already adopted (increasing pensions, wages, child allowances according to the calendar announced by the Government) and eliminating one-off measures, the starting point of the budget deficit for 2021 will be about 8% of GDP. Moreover, given that the effects of the Pandemic will continue in 2021, at least some of the one-off measures are likely to be maintained, which would lead to a higher starting point for the 2021 budget deficit, possibly around 9% of GDP.

Recent years have seen a sharp increase in personnel and social assistance expenditures as a percentage of GDP and tax revenues. This development, unfortunately, is also reflected by a sharp increase in the structural deficit of the public budget. In 2020, a peak was reached in this respect, personnel and social assistance expenditures representing 92.3% of tax revenues (including social security contributions). This situation is not sustainable in itself and is all the more to be judged from the perspective of the need for macroeconomic and budgetary correction.

In this context, characterized by very high levels of the budget deficit, it is mandatory to implement a correction that will lead in the medium term to much lower levels of the budget deficit and that will anchor creditors' expectations towards a sustainable trajectory of the fiscal-budgetary policy.

A macroeconomic correction imagined as being helped by a drastic decrease in interest rates on the Romanian money market, by substantial injections of liquidity by the NBR and operations with government securities on the domestic financial market, is counterproductive; confidence in the national currency would be lost, inflation would be greatly stimulated, it would be a disaster for financial and economic stability.

The announcement of a credible multi-annual fiscal/budgetary consolidation plan could provide the necessary time for a gradual approach that would affect the economic recovery as little as possible.

The macroeconomic correction (reduction of the budget deficit) must take into account both the restructuring of expenditures and increasing fiscal/budgetary revenues. It is a false thesis that fiscal/budgetary revenues cannot be increased, especially by broadening the tax base. The tax system must be transparent and fair; all citizens and companies must pay - loopholes that make the tax regime unfair should be eliminated. Tax evasion should not be tolerated, as well as incorrect tax optimizations (tax avoidance) and undue rents.

An intense absorption of European funds, which would capitalize on the almost double amount of resources allocated to Romania for the 2021-2027 period (due to the emergence of the European Recovery Plan Next Generation EU of 750 billion euros, of which Romania would benefit from 33.2 billion euros), could help substantially the macroeconomic correction efforts during the following 3-4 years.

The opinions and recommendations formulated above by the Fiscal Council were approved by the Chairman of the Fiscal Council, according to the provisions of art. 56, para (2), letter d) of Law no.

69/2010 republished, following their approval by the Council members, through vote, in the meeting of November 23rd, 2020.

23rd November 2020

Chairman of the Fiscal Council

Professor Daniel Dăianu

ANNEX I – Budgetary revisions vs. initial budget

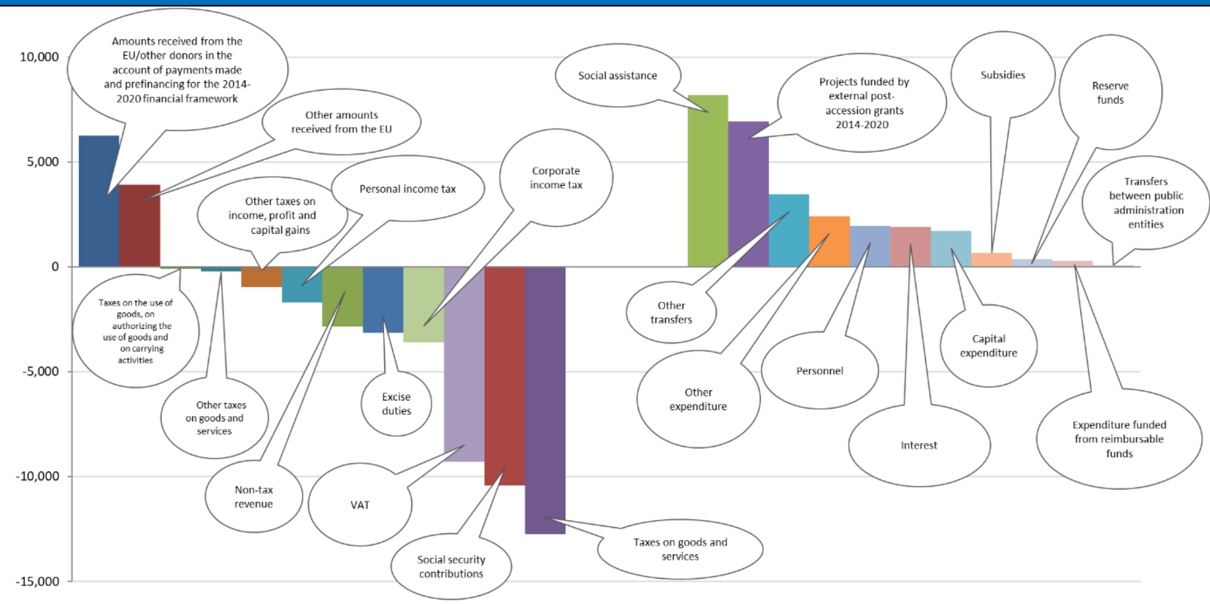
ANNEX I	Initial budget 2020	Swap program 2020	Initial budget 2020 without swap	Second budget revision (R2)	Swap R2	R2 without swap	Third budget revision (R3)	Swap R3	R3 without swap	R2 - initial budget	R3 - initial budget	R3 – R2
										Without swap		
	1	2	3=1-2	4	5	6=4-5	7	8	9=7-8	10=6-3	11=9-3	12=9-6
TOTAL REVENUE	**360,148.5**	**850.0**	**359,298.5**	**342,016.1**	**1,951.4**	**340,064.7**	**337,772.9**	**1,951.4**	**335,821.5**	**-19,233.8**	**-23,477.0**	**-4,243.2**
Current revenue	329,820.7	850.0	328,970.7	299,395.6	1,951.4	297,444.2	297,487.3	1,951.4	295,535.9	-31,526.4	-33,434.8	-1,908.3
Tax revenue	177,017.6	850.0	176,167.6	158,203.1	850.0	157,353.1	156,856.8	850.0	156,006.8	-18,814.5	-20,160.7	-1,346.3
Taxes on profit, wages, income and capital gains	49,883.7	0.0	49,883.7	44,431.2	116.0	44,315.2	43,736.8	116.0	43,620.8	-5,568.4	-6,262.9	-694.5
Corporate income tax	19,471.8	0.0	19,471.8	16,656.3	8.0	16,648.3	15,875.7	8.0	15,867.7	-2,823.5	-3,604.1	-780.5
Personal income tax	26,315.2	0.0	26,315.2	24,463.4	108.0	24,355.4	24,733.9	108.0	24,625.9	-1,959.8	-1,689.3	270.5
Other taxes on income, profit and capital gains	4,096.7	0.0	4,096.7	3,311.6	0.0	3,311.6	3,127.2	0.0	3,127.2	-785.1	-969.5	-184.4
Property tax	7,105.7	0.0	7,105.7	6,267.1	0.0	6,267.1	5,978.4	0.0	5,978.4	-838.6	-1,127.3	-288.7
Taxes on goods and services	117,974.8	850.0	117,124.8	105,504.1	699.0	104,805.1	105,073.8	699.0	104,374.8	-12,319.6	-12,750.0	-430.4
VAT	72,720.5	850.0	71,870.5	62,868.0	668.5	62,199.5	63,248.7	668.5	62,580.2	-9,671.0	-9,290.3	380.7
Excise duties	33,658.1	0.0	33,658.1	31,129.2	30.5	31,098.7	30,530.2	30.5	30,499.7	-2,559.4	-3,158.4	-599.0
Other taxes on goods and services	4,903.1	0.0	4,903.1	4,865.4	0.0	4,865.4	4,693.2	0.0	4,693.2	-37.7	-209.9	-172.2
Taxes on the use of goods, on authorizing the use of goods and on carrying activities	6,693.1	0.0	6,693.1	6,641.6	0.0	6,641.6	6,601.7	0.0	6,601.7	-51.5	-91.4	-39.9
Taxes on foreign trade and international transactions (custom duty)	1,253.9	0.0	1,253.9	1,125.9	0.0	1,125.9	1,125.9	0.0	1,125.9	-128.1	-128.1	0.0
Other tax revenue	799.5	0.0	799.5	874.7	35.0	839.7	942.0	35.0	907.0	40.2	107.5	67.3
Social security contributions	124,026.8	0.0	124,026.8	114,389.1	1,101.4	113,287.7	114,698.3	1,101.4	113,596.9	-10,739.1	-10,429.9	309.2
Non-tax revenue	28,776.3	0.0	28,776.3	26,803.5	0.0	26,803.5	25,932.2	0.0	25,932.2	-1,972.8	-2,844.1	-871.3
Capital revenue	1,000.8	0.0	1,000.8	951.9	0.0	951.9	792.3	0.0	792.3	-48.8	-208.4	-159.6
Grants	8.5	0.0	8.5	8.7	0.0	8.7	8.7	0.0	8.7	0.2	0.2	0.0
Amounts received from the EU in the account of payments made and prefinancing	7.7	0.0	7.7	7.7	0.0	7.7	4.7	0.0	4.7	0.0	-3.0	-3.0
Financial operations	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Amounts collected in the single account	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other amounts received from the EU	0.0	0.0	0.0	3,920.4	0.0	3,920.4	3,920.4	0.0	3,920.4	3,920.4	3,920.4	0.0
Amounts received from the EU/other donors in the account of payments made and prefinancing for the 2014-2020 financial framework	29,310.9	0.0	29,310.9	37,731.6	0.0	37,731.6	35,559.4	0.0	35,559.4	8,420.8	6,248.5	-2,172.2

TOTAL EXPENDITURE	**400,694.5**	**850.0**	**399,844.5**	**433,012.8**	**1,951.4**	**431,061.4**	**433,831.3**	**1,951.4**	**431,879.9**	**31,216.9**	**32,035.4**	**818.5**
Current expenditure	373,441.7	850.0	372,591.7	401,424.8	1,350.0	400,074.8	404,863.4	1,350.0	403,513.4	27,483.1	30,921.7	3,438.6
Personnel	109,160.4	0.0	109,160.4	110,911.6	0.0	110,911.6	111,106.8	0.0	111,106.8	1,751.2	1,946.3	195.1
Goods and services	51,046.4	0.0	51,046.4	55,093.8	500.0	54,593.8	56,080.2	500.0	55,580.2	3,547.4	4,533.8	986.4
Interest	13,950.6	0.0	13,950.6	15,716.9	0.0	15,716.9	15,841.9	0.0	15,841.9	1,766.3	1,891.3	125.0
Subsidies	7,398.8	0.0	7,398.8	8,125.2	0.0	8,125.2	8,054.2	0.0	8,054.2	726.4	655.4	-71.0
Total transfers	190,364.5	850.0	189,514.5	208,135.8	850.0	207,285.8	211,610.1	850.0	210,760.1	17,771.3	21,245.6	3,474.3
Transfers between public administration entities	2,169.7	850.0	1,319.7	2,702.7	850.0	1,852.7	2,244.6	850.0	1,394.6	533.0	74.9	-458.0
Other transfers	17,090.5	0.0	17,090.5	18,437.9	0.0	18,437.9	20,544.6	0.0	20,544.6	1,347.4	3,454.1	2,106.7
Projects funded by external grants	199.3	0.0	199.3	391.3	0.0	391.3	398.5	0.0	398.5	192.0	199.2	7.2
Social assistance	131,220.5	0.0	131,220.5	136,944.9	0.0	136,944.9	139,409.9	0.0	139,409.9	5,724.4	8,189.4	2,465.0
Projects funded by external post-accession grants 2014-2020	32,958.6	0.0	32,958.6	41,280.5	0.0	41,280.5	39,877.4	0.0	39,877.4	8,321.9	6,918.8	-1,403.1
Other expenditure	6,725.9	0.0	6,725.9	8,378.5	0.0	8,378.5	9,135.1	0.0	9,135.1	1,652.6	2,409.2	756.6
Reserve funds	951.2	0.0	951.2	2,288.7	0.0	2,288.7	1,316.7	0.0	1,316.7	1,337.5	365.5	-972.0
Expenditure funded from reimbursable funds	569.8	0.0	569.8	1,152.8	0.0	1,152.8	853.5	0.0	853.5	583.0	283.8	-299.2
Capital expenditure	27,252.8	0.0	27,252.8	31,588.0	0.0	31,588.0	28,967.9	0.0	28,967.9	4,335.2	1,715.1	-2,620.1
Financial operations	0.0	0.0	0.0	0.0	601.4	-601.4	0.0	601.4	-601.4	-601.4	-601.4	0.0
Payments made in previous years and recovered in the current year	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
EXCEDENT(+) / DEFICIT(-)	**-40,546.0**	**0.0**	**-40,546.0**	**-90,996.8**	**0.0**	**-90,996.8**	**-96,058.5**	**0.0**	**-96,058.5**	**-50,450.7**	**-55,512.4**	**-5,061.7**

Source: Ministry of Public Finance, Fiscal Council's calculations

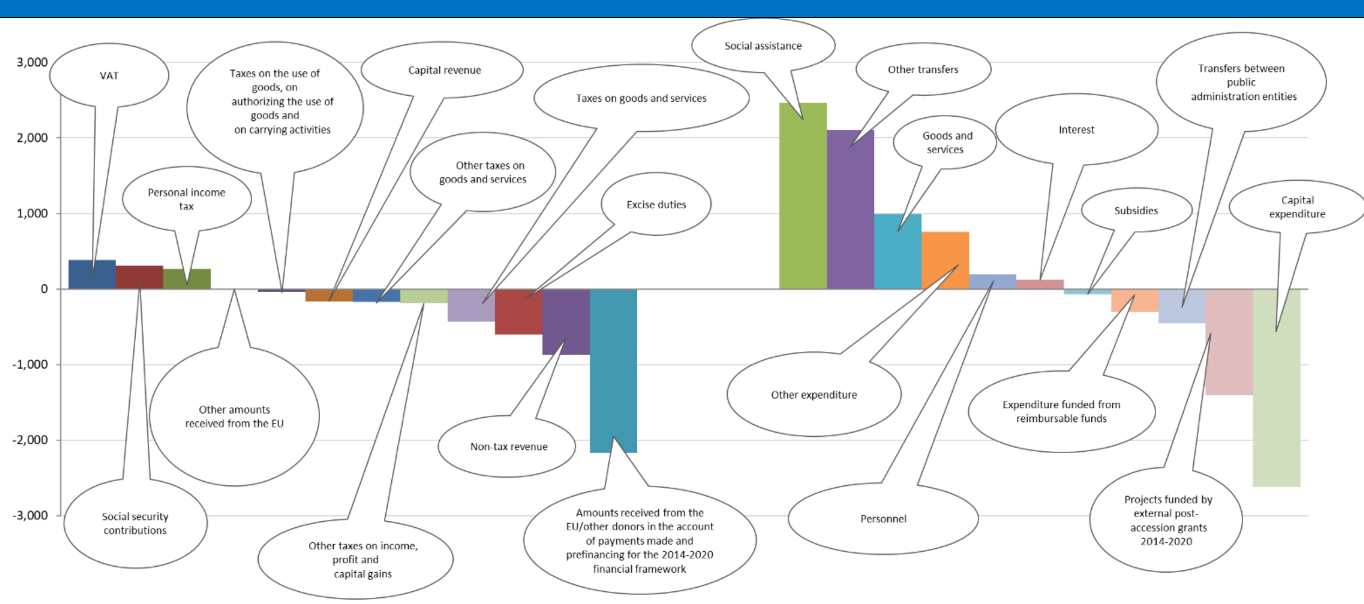
ANNEX II

Figure 1: Main changes in budgetary expenditures and revenues compared to the initial 2020 budget (without swap compensation schemes, mil. lei)



Source: Ministry of Public Finance, Fiscal Council's calculations

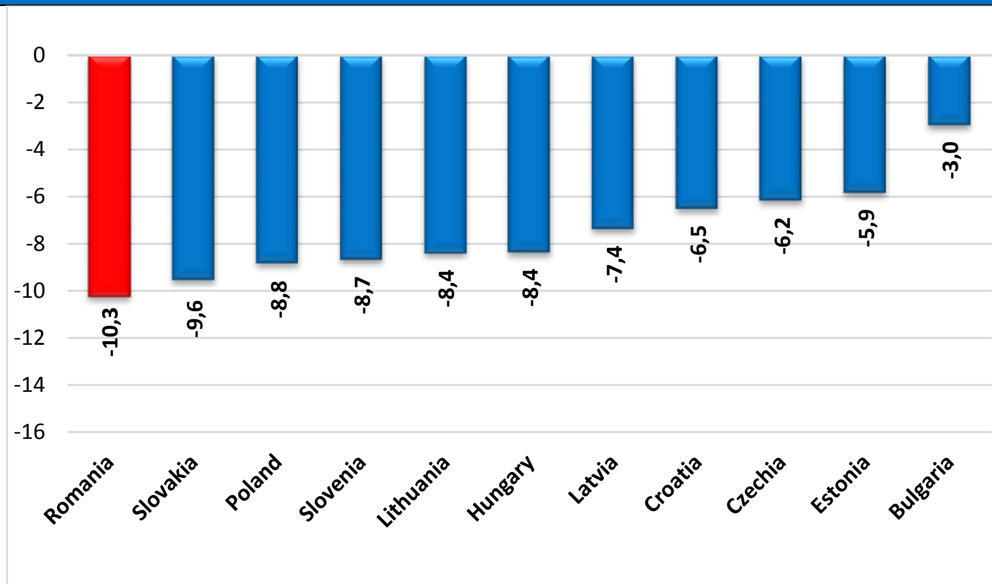
Figure 2: Main changes in budgetary expenditures and revenues compared to the second 2020 budget revision (without swap compensation schemes, mil. lei)



Source: Ministry of Public Finance, Fiscal Council's calculations

ANNEX III

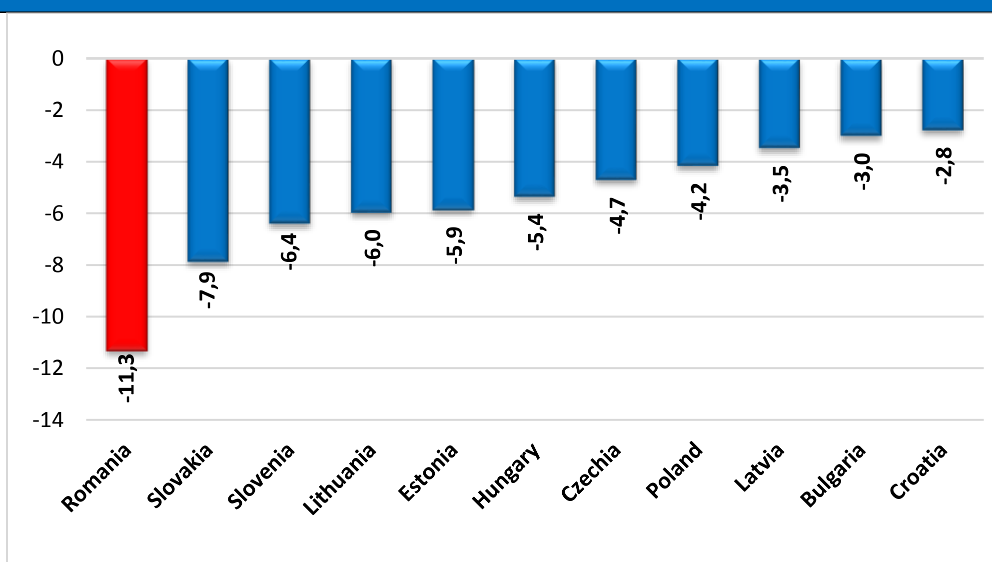
Figure 3: Estimated 2020 budget balance for new EU member states (% of GDP, ESA 2010)



Source: AMECO

Note: The estimated budget deficit for Romania includes the 40% increase of the pension point and the doubling of child allowances (Autumn 2020 Economic Forecast, EC, pg. 137)

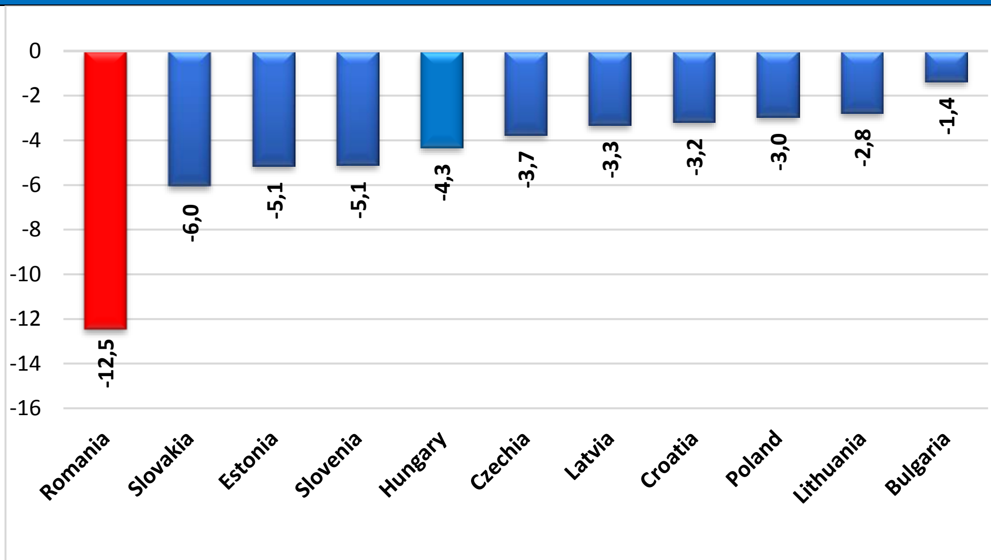
Figure 4: Estimated 2021 budget balance for new EU member states (% of GDP, ESA 2010)



Source: AMECO

Note: The estimated budget deficit for Romania includes the 40% increase of the pension point and the doubling of child allowances (Autumn 2020 Economic Forecast, EC, pg. 137)

Figure 5: Estimated 2022 budget balance for new EU member states (% of GDP, ESA 2010)

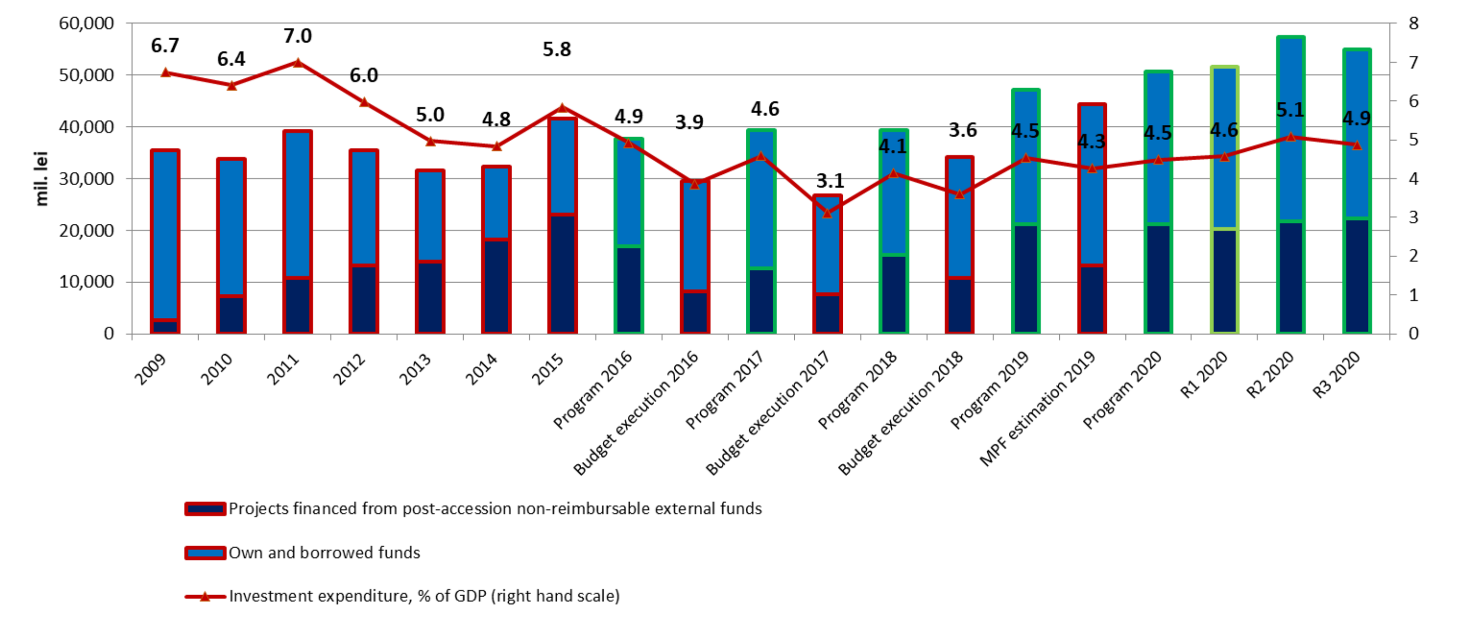


Source: AMECO

Note: The estimated budget deficit for Romania includes the 40% increase of the pension point and the doubling of child allowances (Autumn 2020 Economic Forecast, EC, pg. 137)

ANNEX IV

Figure 6: The evolution of public investment expenditures between 2009-2020 – planned level vs. realized (mil. lei)



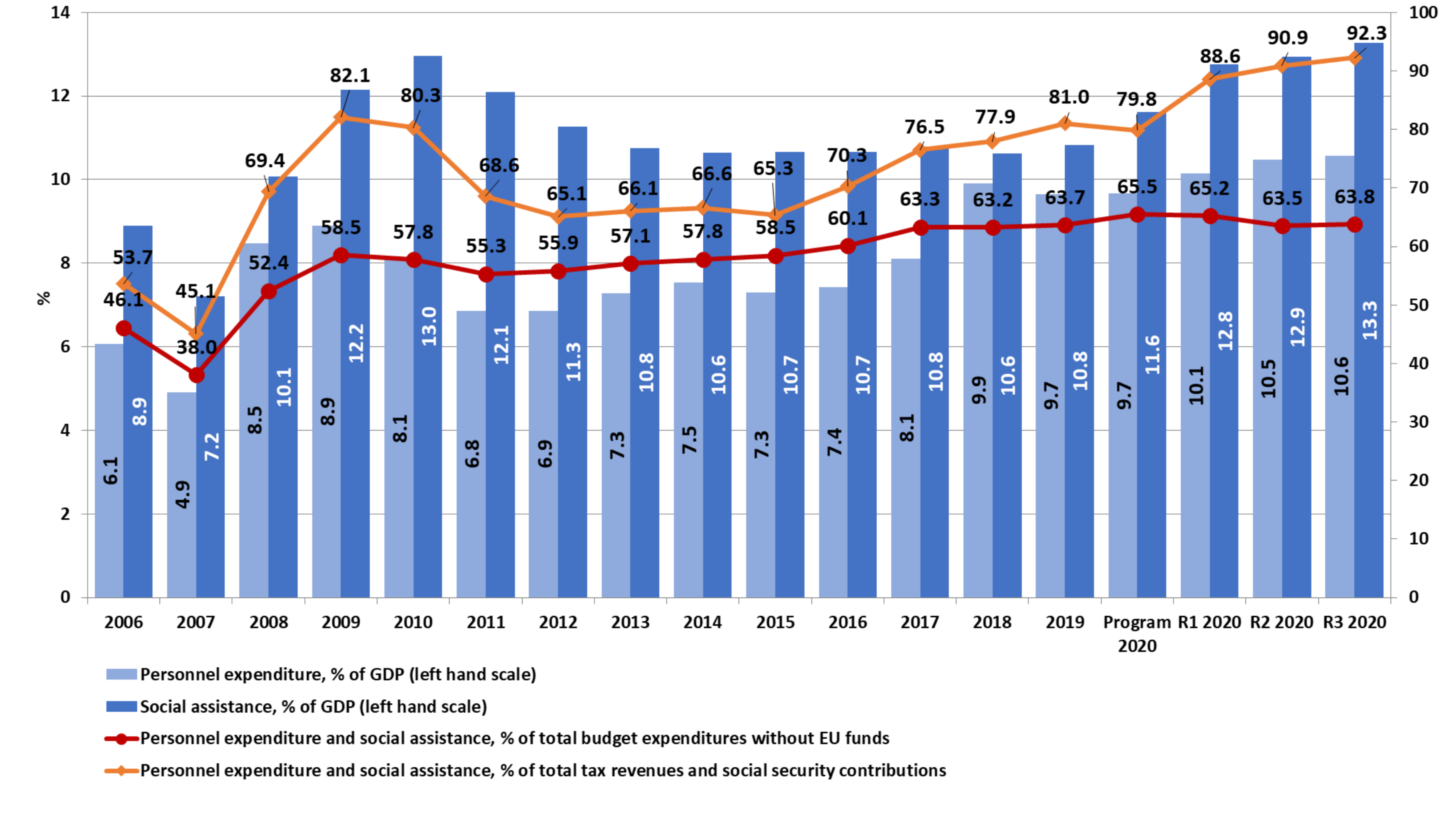
Source: Ministry of Public Finance, Fiscal Council's calculations

ANNEX IV – EU FUNDS	Initial budget 2020 (mil. lei)			Second budget revision (mil. lei)			Third budget revision (mil. lei)		
	Structural	Agriculture	Amounts according to art.10 letter a) of GEO no. 40/2015	Structural	Agriculture	Amounts according to art.10 letter a) of GEO no. 40/2015	Structural	Agriculture	Amounts according to art.10 letter a) of GEO no. 40/2015
EU funds inflows	16,557.0	12,753.9	72.4	17,904.9	19,826.8	5,228.5	17,642.3	17,917.1	2,195.1
EU funds expenditure	25,893.3	12,753.9	72.4	26,511.0	19,826.8	5,228.5	26,888.6	17,917.1	2,195.1
National cofinancing and ineligible expenses	9,336.3	0.0	0.0	8,606.1	0.0	0.0	9,246.3	0.0	0.0

Source: Ministry of Public Finance, Fiscal Council's calculations

ANNEX V

Figure 7: Personnel and social assistance expenditure evolution between 2006-2020



Source: Ministry of Public Finance, Fiscal Council's calculations