Surveillance of budgetary positions and surveillance and coordination of economic policies

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The Commission presented a report to the Council on the enhanced monitoring mission carried out on 10 and 11 April 2018 in Romania pursuant to Article 11(2) of Regulation (EC) No 1466/97.

Background: as a consequence of the significant deviation from its medium-term budgetary objective (MTO) in 2016, a Significant Deviation Procedure (SDP) was launched for Romania in spring 2017.

On 22 May 2017, the Commission issued a warning to Romania and proposed to the Council to launch a SDP. In its SDP recommendation, of 16 June 2017, the Council asked Romania to take measures to ensure that the nominal growth rate of net primary government expenditure does not exceed 3.3% in 2017.

In December 2017, the Council concluded that no effective action had been taken by Romania and issued a **revised recommendation**. The Council asked Romania to take measures to ensure that the nominal growth rate of net primary government expenditure does not exceed 3.3% in 2018, corresponding to an annual structural adjustment of 0.8% of GDP in 2018. Romania reported to the Council on action taken on 20 April, after the 15 April deadline.

According to the Commission projections, both **the headline and structural deficit are likely to increase in 2018**. The expansionary fiscal policy is set to continue in the near future. The 2018 budget aims at a general government deficit of 3% of GDP, which implies a further increase of the structural deficit in the presence of an increasing output gap. However, the budget was built on an optimistic macroeconomic scenario and likely overestimates tax revenues. The Commission projects a headline deficit of **3.4% of GDP in 2018**.

Findings of the enhanced monitoring mission: the members of the Commission's enhanced monitoring mission, which took place on 10-11 April 2018, concluded that the **Romanian authorities did not intend to fact upon the SDP recommendation**. Minister Teodorovici, speaking on behalf of the Ministry of Finance and the Government, confirmed that the target for 2018 remains a headline deficit of just below 3% of GDP. Given a positive and widening output gap, this implies a deterioration of the underlying structural deficit, contrary to the Council recommendation.

The government is considering a further reversal of the 2008 systemic pension reform, which introduced the second pension pillar. The authorities have already reduced, as part of the 2018 budget, the share of social contributions transferred to the second pension pillar. According to public statements, the government is considering to make the transfers to the second pension pillar optional, and to make a decision by end-June 2018, after consultation with stakeholders. Those transfers amount to around RON 7 billion annually (around EUR 1.5 billion; 0.8% of GDP). Such a measure would decrease the fiscal deficit in the short term, as the second pension pillar is classified outside the general government under ESA. However, that fiscal gain would dissipate in the long term as the social contributions diverted from the second pillar would be accompanied by an obligation to pay old-age pensions in the future.

The National Bank of Romania (NBR) expressed concerns regarding the impact of the expansionary, pro-cyclical fiscal policy on the current policy-mix. Romania is in the middle of a large economic upswing while the fiscal position of Romania has been highly expansionary. As such, Romania's fiscal policy appears imprudent and strongly conditions monetary policy.

The Fiscal Council shared the Commission's concerns regarding the fiscal outlook. According to the Fiscal Council, the structural deficit will substantially deteriorate in 2018 and the headline deficit is projected to breach the 3% of GDP threshold in the absence of countervailing fiscal measures.