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COMMUNICATION FROM THE COMMISSION TO THE COUNCIL

Assessment of the action taken by Lithuania and Romania

in response to the Council Recommendations of 16 February 2010 with a view to bringing an end to the situation of excessive government deficit

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1. THE APPLICATION OF THE STABILITY AND GROWTH PACT IN THE CURRENT CRISIS SITUATION

The vast majority of EU Member States currently have general government deficits above the 3% of GDP reference value set in the Treaty on the Functioning of the European Union (TFEU). The origin of the often strong deterioration in the deficit as well as the debt positions must be seen in the context of the unprecedented global financial crisis and economic downturn in 2008/09. Several factors are at play. First, the economic downturn brought about declining tax revenue and rising social benefit expenditure (e.g. unemployment benefits). Second, recognising that budgetary policies have an important role to play in the current extraordinary economic situation, Member States implemented a European Economic Recovery Plan (EERP). The Plan stipulated that the stimulus should be differentiated across Member States to reflect their different positions in terms of public finance sustainability and competitiveness. Finally, several Member States took measures to stabilise the financial sector, some of which have impacted on the debt position or constitute a risk of higher deficits and debt in the future, although some of the costs of the government support could be recovered in the future.

In October 2009, capitalizing on first signs of a recovery in sight, the European Council endorsed a fiscal exit strategy based on the following principles: (i) The exit strategy should be coordinated across countries in the framework of consistent implementation of the Stability and Growth Pact. (ii) There is a need for timely withdrawal of the fiscal stimulus. Provided that the Commission forecasts continue to indicate that the recovery is strengthening and becoming self-sustaining, fiscal consolidation in all EU Member States should start in 2011 at the latest. Specificities of country situations should be taken into account, and a number of countries need to consolidate before then. (iii) In view of the challenges, the planned pace of the fiscal consolidation should be ambitious, and will have to go well beyond the benchmark of 0.5% of GDP per annum in structural terms in most Member States. (iv) Important flanking policies to the fiscal exit will include strengthened national budgetary frameworks for underpinning the credibility of consolidation strategies and measures to support long-term fiscal sustainability, as emphasised by the SGP. In addition, structural reform efforts should be strengthened to enhance productivity and to support long-term investment. These principles for fiscal exit have been put into operation in the recommendations issued in the context of the excessive deficit procedures as well as in the latest round of annual assessment of Stability and Convergence Programmes. The deadlines for correction and required structural efforts have been differentiated across Member States, taking into account country-specific circumstances.

The stimulus measures in the context of the EERP coupled with the measures taken to stabilise the financial sector have prevented an economic meltdown and laid the foundation for a recovery. The Commission services' spring 2010 forecast and in particular also the

September 2010 interim forecast confirm the outlook of gradual recovery consistent with withdrawal of fiscal stimulus.

On 16 February 2010, the Council addressed (revised) recommendations under Article 126(7) TFEU to Lithuania and Romania with a view to bringing the situation of an excessive deficit to an end by 2012[1]. These recommendations were based on the Commission services' autumn 2009 forecast and on the agreed principles of the fiscal exit strategy. The Council set the date of 16 August 2010 for taking effective action in response to the recommendations.

According to Regulation (EC) No 1467/97[2] and the revised Code of Conduct[3] a Member State should be considered to have taken effective action if it has acted in compliance with the Article 126(7) TFEU recommendation. The Code of Conduct states that the assessment of effective action should in particular take into account whether the Member State concerned has achieved the annual improvement of its cyclically adjusted balance, net of one-off and other temporary measures, initially recommended by the Council. In case the observed adjustment proves to be lower than recommended, a careful analysis of the reasons for the shortfall should be made. In case of a multi-annual adjustment, the Code of Conduct specifies that the assessment should mainly focus on the measures taken in order to ensure an adequate fiscal adjustment in the year following the identification of the excessive deficit.

Against this background, the Commission has made an assessment of action taken by Lithuania and Romania in response to the Council's recommendations[4].

In particular, for Romania, the implementation of additional fiscal consolidation measures of around 5% of GDP on an annual basis has put Romania on track to achieve the 2010 government deficit target agreed in the context of the multilateral financial assistance programme. Large carry-overs from the 2010 consolidation measures and planned additional savings on the expenditure side should allow a further reduction of the deficit to below 5% of GDP in 2011. The measures taken are an important step towards restoring a sustainable fiscal position and macroeconomic stability. At the same time, significant risks exist. In particular, it will be crucial that fiscal consolidation measures remain in place and that their effects are not offset by other policies. Moreover, the authorities should continue to rigorously implement the reforms agreed in the context of the multilateral financial assistance programme.

Lithuania has implemented significant corrective fiscal measures as planned in the 2010 budget, estimated to generate savings of above 3% of GDP. The authorities also adopted several measures for 2011 and have outlined in some detail the consolidation strategy necessary for a correction of the excessive deficit by 2012, as recommended by the Council. However, considerable adjustment is still needed in the coming years. The 2011 budget should include further significant measures, thereby also replacing temporary measures with more lasting and structural measures. If economic and budgetary conditions turn out better

1 An overview of all past and ongoing EDP procedures is available at: http://ec.europa.eu/economy_finance/sgp/deficit/countries/index_en.htm

2 OJ L 209, 2.8.1997, p. 6.

3 "Specifications on the implementation of the Stability and Growth Pact and guidelines on the format and content of stability and convergence programmes", endorsed by the ECOFIN Council of 7 September 2010, available at: http://ec.europa.eu/economy_finance/sgp/deficit/legal_texts/index_en.htm.

4 For Malta, which also received recommendations under Article 126(7) TFEU on 16 February 2010, the assessment has been postponed until after the presentation 2011 budget, in view of the Council's recommendation to Malta to put an end to the excessive deficit situation by 2011.

than previously expected, it would be important to aim at accelerating the consolidation and overachieving the targets. Proposals to strengthen the enforceability of the medium-term fiscal framework and the budget execution monitoring, as well as structural reforms (especially of the social security system), are welcome, but the authorities are invited to step up their efforts in these areas.

In view of the above assessment, the Commission considers that no further steps in the excessive deficit procedure are needed at present.

2. LITHUANIA

2.1. The excessive deficit procedure and most recent recommendations

On 7 July 2009, the Council decided that an excessive deficit existed in Lithuania in accordance with Article 104(6) of the Treaty establishing the European Community (TEC). The most recent Council Recommendation under Article 126(7) TFEU was adopted on 16 February 2010[5].

The Council recommended Lithuania to put an end to the present excessive deficit situation by 2012. The Lithuanian authorities should bring the general government deficit below 3 % of GDP in a credible and sustainable manner by taking action in a medium-term framework. Specifically, to this end, the Lithuanian authorities should: (a) implement rigorously the corrective measures planned in the budget for 2010 and adopt additional measures, if necessary, to achieve the envisaged-consolidation; (b) ensure an average annual fiscal effort of at least 2¼% of GDP over the period 2010-2012, notably by containing primary current expenditure; (c) specify and adopt the additional measures necessary to achieve the correction of the excessive deficit by 2012, cyclical conditions permitting, and accelerate the reduction of the deficit if economic or budgetary conditions turn out better than currently expected; to this end adopt and swiftly implement the planned structural reforms entailing significant budgetary savings.

In addition, to limit risks to the adjustment, Lithuanian authorities should enhance the medium term budgetary framework, including by strengthening fiscal governance and transparency and reinforcing expenditure discipline, through enforceable ceilings, as well as improve the monitoring of the budget execution throughout the year. The medium term budgetary framework needs to be enhanced by introducing necessary forward-looking elements and mechanisms to avoid pro-cyclicality.

The Council established the deadline of 16 August 2010 for the Lithuanian government to take effective action to implement the recommended fiscal consolidation in 2010 as planned in the budget for 2010 and to outline the consolidation strategy that will be necessary to progress towards the correction of the excessive deficit. The assessment of effective action will take into account economic developments compared to the economic outlook in the Commission services' autumn 2009 forecast.

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5 All EDP-related documents for Lithuania can be found at the following website: http://ec.europa.eu/economy_finance/sgp/deficit/countries/index_en.htm.

2.2. Assessment of effective action taken

According to the Commission services' spring 2010 forecast, the outlook for real activity in Lithuania is more favourable than expected at the time the Council issued its recommendations in February 2010. After a very sharp recession in 2009, with real GDP falling by 14.8%, real GDP is expected to fall by 0.6% in 2010 and to grow by 3.2% in 2011, while in autumn 2009 the Commission services projected a fall of 3.9% and growth of 2.5%. The expected recovery of Lithuania's economy was recently confirmed, with annual growth turning positive in the second quarter of 2010 (+1.3%).

The government deficit reached 8.9% of GDP in 2009 due to a very severe downturn and despite substantial consolidation measures of around 8% of GDP adopted during 2009, which was still a better outcome than the 9.8% of GDP expected by the Commission services and the authorities in autumn 2009. This is explained by a lower expenditure ratio by almost 3 percentage points of GDP, partly offset by lower-than-expected revenue ratio by 2 percentage points.

Regarding 2010, the authorities broadly implemented the deficit-reducing measures planned in the budget for 2010 as recommended by the Council. The significant savings package of above 3% of GDP included in the 2010 budget was implemented by the authorities in the course of the year. Hence sizeable cuts in expenditure have been put in place as foreseen, particularly in government current spending (1.7% of GDP), including notably the public sector wage bill, and as regards social benefits, among them pensions and maternity benefits (1.3% of GDP). On the revenue side changes are limited to a full year effect of the VAT rate increase in September 2009 (0.7% of GDP), a reduction in the corporate income tax rate and some increases in non-tax revenues. Some other expenditure items such as interest payments and capital expenditure, due to national co-financing of EU funds, are set to increase. The deficit target for 2010 of 9.5% originally envisaged in the 2010 budget was changed to 8.1% of GDP in the February 2010 convergence programme, reflecting the clearly more favourable economic developments compared to what assumed in the budget. The Commission services' spring 2010 forecast projects a somewhat higher deficit of 8.4% of GDP. The difference with the new official target is largely due to lower nominal growth projected in the spring forecast. Overall, the budgetary results seem to be slightly better than planned and the budgetary target put forward by the Lithuanian authorities in the February 2010 convergence programme appears achievable.

The calculation of the fiscal effort undertaken by the Lithuanian authorities is strongly affected by the large revisions in potential growth following the strong growth of the Lithuanian economy before the crisis. The latest estimates using the standard methodologies are likely to significantly underestimate the structural effort in these exceptional circumstances, as they produce a relatively small deterioration in the output gap in 2010, and are unlikely to fully reflect the behaviour of budgetary components in this very extreme cycle. This implies that only a marginal part of the ongoing deterioration in the government revenues and expenditures is imputed to the cyclical component. Given the small improvement in the nominal budget balance expected in 2010, the effects described above result in a change in the structural balance in 2010 of just ⅓% of GDP. However, most recent estimates of revenue developments suggest a deterioration of close to 2% of GDP in 2010, in spite of the government taking a number of revenue-increasing discretionary measures in order to contain the shortfall. At the same time, the government managed to reduce total expenditure, in spite of the cyclical increase in unemployment expenditure. The above considerations and the estimated fiscal impact (using the bottom-up method) of the consolidation measures undertaken in the 2010 budget and currently under implementation suggest that the structural effort in 2010 could be close to if not higher than the 2¼% of GDP (on average over 2010-2012) recommended by the Council.

Despite the sizeable fiscal consolidation already implemented in 2009 and 2010, a significant further adjustment is needed in the coming years to achieve the correction of the excessive deficit by 2012. In this respect, the 2011 budget is an important step to deliver an essential part of the necessary consolidation. The authorities have already adopted several measures affecting 2011, ahead of the preparations of the 2011 budget, however, most of them are a continuation of existing measures, and some remain of temporary nature. The cuts in public employee wages, which have been decreased several times in 2009, reducing both the base and the coefficients, were extended to 2011, prolonging the estimated savings of 0.5% of GDP achieved in the previous year, but leaving doubts as to its continuation in the future if the economic conditions improve. Also, the reduction in transfers to the second-pillar pension funds, previously reduced only for the period of 2009-2010, was extended until the economic situation improves. This represents savings of around 0.6% of GDP in the short term, although it affects negatively the long-term sustainability of the public finances and being a temporary measure it does not contribute to the structural consolidation. The reduced sickness leave benefits have also been extended (0.1% of GDP). In addition to the prolongation of measures already decided in previous years, budgetary savings would be generated by some structural changes, which include reduced maternity benefits from July 2011. The full effect of this change is estimated to generate savings of around 0.35% of GDP in 2011 and of around 0.7% of GDP annually in the following years. As the above-mentioned measures extending the validity of earlier cuts were already included in the Commission services' spring forecast, except the reduction in the transfers to the second pillar pension funds, the deficit projections for 2011 by the Commission are not changed significantly by the measures taken so far, and additional measures of around 1⅔% of GDP appear still needed to achieve the required consolidation in 2011. Therefore, the 2011 budget should include further consolidation measures to reach a deficit of below 6% of GDP in line with the targets set out in the February 2010 convergence programme and to comply with the Council's recommendation.

Replacing temporary measures with more lasting and structural measures, would contribute to strengthening the quality of the consolidation, thus supporting the long-term sustainability of public finances. Furthermore, considering the large adjustment in the coming years, it would be important for the government to aim at accelerating the consolidation and overachieving the targets to the extent that the economic and budgetary conditions turn out better than previously expected. The next convergence programme should provide essential details of the fiscal strategy underpinning the necessary consolidation until 2012.

The February 2010 convergence programme targets a gradual reduction of the deficit to 3% of GDP by 2012, the correction deadline set by the Council. To reach the targets, quantified consolidation efforts on both revenue and expenditure side of the budget are envisaged but still need to be backed up by specified measures as recommended by the Council.

Regarding the Council's recommendation to strengthen the budgetary medium-term framework, a new concept paper on the reform of the budget planning and execution framework has been prepared and is currently under discussion, aiming at its submission in autumn 2010. In particular, a number of measures to increase transparency and monitoring of the budgetary process by presenting and publishing government budget indicators based on the ESA 95 classifications are being discussed. Fiscal stance and fiscal impulse indicators are to be introduced in the budgetary preparation process. So as to improve enforcement, an automatic obligation to implement an anti-inflationary fiscal policy, based on the output gap indicators, is proposed. Implementation of these measures, especially as regards the monitoring of the budget execution, as well as a strengthening of the multi-annual budgetary framework needs to be stepped up in view of ensuring compliance with the Council recommendation over the next years.

As recommended, Lithuania is also further advancing with implementation of structural reforms. A concept paper on the social security reform was adopted in June 2010; the reform is to take place in two stages. The first stage is nearly completed and among other measures, it includes a gradual increase in retirement age as of 2012 to improve the long-term sustainability of public finances. The Parliament still has to vote on this measure in autumn.

On 27 August 2010, the Lithuanian authorities submitted a voluntary report on the action taken in response to the Council recommendation of February 2010. The report referred to the measures implemented in 2010, which would allow achieving the envisaged consolidation, outlined measures under preparation in view of adoption of the 2011 budget and reiterated the commitment to take further measures to correct the deficit by 2012. It also provided information about the progress on structural reforms and enhancing the medium-term budgetary framework.

2.3. Conclusions

On current information it appears that Lithuania has taken action representing adequate progress towards the correction of the excessive deficit within the time limits set by the Council. In particular, Lithuania has implemented in 2010 significant corrective fiscal measures as planned in the 2010 budget, estimated to generate savings of above 3% of GDP.

As considerable adjustment is still needed in the coming years in order to bring the deficit below 3% of GDP in 2012, further measures underpinning the envisaged consolidation will be needed in the outer years. The Lithuanian authorities already adopted several measures for 2011 and have outlined in some detail the consolidation strategy that is necessary to progress towards the correction of the excessive deficit by 2012, the deadline recommended by the Council. The 2011 budget to be adopted in autumn should include further significant and lasting measures necessary to reach the fiscal targets presented in the convergence programme. Replacing temporary measures with more lasting and structural measures, would contribute to strengthening the quality of the consolidation, thus supporting long-term sustainability of public finances.

Furthermore, in line with the Council recommendation and considering the large adjustment in the coming years, it would be important for the government to aim at accelerating the consolidation and overachieving the targets to the extent that economic and budgetary conditions are turning out better than previously expected. The Lithuanian authorities have initiated work to strengthen the enforceability of the medium-term fiscal framework and the budget execution monitoring. The government also pursued structural reforms, especially of the social security system, which should improve long-term sustainability of public finances. These measures are welcome and the authorities are invited to step up their efforts in these areas.

In view of the above assessment, the Commission considers that no further steps in the excessive deficit procedure of Lithuania are needed at present. The Commission will continue to closely monitor budgetary developments in Lithuania in accordance with the Treaty and the SGP, in particular in the light of the fragile situation of public finances.

Comparison of key macroeconomic and budgetary projections

		2007	2008	2009	2010	2011	2012
Real GDP (% change)	COM	9.8	2.8	-15.0	-0.6	3.2	n.a.
	CP	n.a.	2.8	-15.0	1.6	3.2	1.2
Output gap[1] (% of potential GDP)	COM	10.1	9.0	-8.2	-8.6	-6.4	n.a.
	CP	n.a.	8.8	-7.7	-5.9	-2.9	-1.7
General government balance (% of GDP)	COM	-1.0	-3.3	-8.9	-8.4	-8.5	n.a.
	CP	n.a.	-3.2	-9.1	-8.1	-5.8	-3.0
Primary balance (% of GDP)	COM	-0.3	-2.6	-7.9	-6.8	-6.6	n.a.
	CP	n.a.	-2.6	-7.8	-6.2	-3.6	-0.6
Cyclically-adjusted balance[1] (% of GDP)	COM	-3.7	-5.7	-6.7	-6.1	-6.8	n.a.
	CP	n.a.	-5.6	-7.0	-6.5	-5.0	-2.6
Structural balance[2] (% of GDP)	COM	-3.1	-5.6	-7.1	-6.8	-6.8	n.a.
	CP	n.a.	-6.0	-7.2	-6.8	-4.8	-2.3
Government gross debt (% of GDP)	COM	16.9	15.6	29.3	38.6	45.4	n.a.
	CP	n.a.	15.6	29.5	36.6	39.8	41.0

Notes:

[1] Output gaps and cyclically-adjusted balances according to the programmes as recalculated by Commission services on the basis of the information in the programmes.
[2] Cyclically-adjusted balance excluding one-off and other temporary measures.

Source: Commission services' 2010 spring forecast (COM) and February 2010 convergence programme update (CP)

3. ROMANIA

3.1. Excessive deficit procedure and most recent recommendations

On 7 July 2009, the Council decided that an excessive deficit existed in Romania in accordance with Article 104(6) TEC. The most recent Council Recommendation under Article 126(7) of the TFEU was adopted on 16 February 2010[6].

The Council recommended Romania to put an end to the present excessive deficit situation by 2012. The Romanian authorities should bring the general government deficit below 3% of GDP in a credible and sustainable manner by taking action in a medium-term framework. Specifically, to this end, Romania should: (a) implement the fiscal measures in 2010 as planned in its budget law and continue consolidation in 2011 and 2012; (b) ensure an average annual fiscal effort of 1¾ % of GDP over the period 2010-2012; (c) specify the measures that are necessary to correct the excessive deficit by 2012, cyclical conditions permitting, and accelerate the reduction of the deficit if economic or budgetary conditions turn out better than currently expected.

To limit risks to the adjustment, the Council also recommended that the Romanian authorities continue implementing the measures to improve fiscal governance agreed in the framework of the multilateral financial assistance programme. In particular, the Council considered that

6 All EDP-related documents for Romania can be found at the following website: http://ec.europa.eu/economy_finance/sgp/deficit/countries/index_en.htm.

adoption and implementation of the Fiscal Responsibility Law would greatly enhance the credibility and predictability of public finances through, among others, the creation of a fiscal council, setting up a binding medium-term fiscal framework, ensuring more cautious revenue forecasts and establishing limits on budget revisions during the year. The Council recommended Romania to adopt and implement the draft pension reform to improve the long-term sustainability of public finances, while safeguarding adequate replacement rates.

The Council established the deadline of 16 August 2010 for Romania to take effective action to implement the fiscal consolidation measures in 2010, as planned in the 2010 budget, and to outline the consolidation strategy towards the correction of the excessive deficit. It specified that the assessment of effective action will take into account economic developments compared to the economic outlook in the Commission services' autumn 2009 forecast.

3.2. Assessment of effective action taken

In July 2010 the Commission services updated their macroeconomic forecast for Romania in the context of the implementation of the multilateral (EU/IMF/WB) financial assistance programme. The new forecast projects real GDP to contract by 1.9% this year, which is a substantial downward revision compared to the 0.5% GDP increase projected in the Autumn 2009 Commission services' forecast and the 1.3% increase expected at the time of the Council Recommendation under Article 126(7) TFEU in February 2010. The worse than expected economic conditions reflect the negative impact of financial turbulences in the region in the first two quarters of 2010, the floods in the northern part of Romania in the spring, and the expected short term demand effects of the additional fiscal consolidation measures implemented by the government in July 2010. In July 2010, the Commission services have also revised the growth projection for 2011 downward to 1.5% from 2.6% at the time of the Article 126(7) recommendation.

The fiscal consolidation measures included in the 2010 budget law were implemented as planned. However, these measures did not deliver the expected savings and, with the worsening of economic conditions, the fiscal situation continued to deteriorate. During the multilateral financial assistance mission in May 2010, it appeared that under unchanged policies the 2010 government deficit target of 6.4% of GDP would be missed by a large margin (about 3 percentage points of GDP), mostly due to substantial revenue underperformance. The 2010 government deficit target was revised upward to 7.3% of GDP. To reach the revised target, the authorities took additional consolidation measures including a 25% reduction in public wages, a 15% reduction in social spending excluding pensions and an increase in the main VAT rate from 19% to 24%. In addition, the authorities decided to cut spending on goods and services by 10% and early retirements were frozen from 1st June 2010 until after the pension reform is in effect (1 January 2011). Social contributions and personal income tax bases were broadened, and a turnover tax on medical suppliers and distributors was introduced. The authorities also committed to further reduce personnel in the coming months, on top of cuts in the first half of 2010 exceeding 25000 jobs. The consolidation measures agreed since the adoption of the Council Recommendation in February 2010 add up to about 5% of GDP on an annual basis and, assuming continued rigorous budgetary execution, place the country on track to reach the revised 2010 government deficit target.

The authorities aim to further reduce the general government deficit in 2011 to below 5% of GDP. Provided that the fiscal austerity package implemented in 2010 remains fully in place the carryover from the 2010 fiscal consolidation measures (about 2½% of GDP) and planned additional savings on the expenditure side (in 2011 the authorities plan to reform the social assistance system, reduce energy subsidies, freeze pensions in nominal terms, and further reduce public employment) should be sufficient to reach this target, assuming rigorous budgetary execution. Overall, under unchanged policies the consolidation measures adopted and planned by the authorities should lead to improvements in the structural balance by some 3% of GDP in both 2010 and 2011, above the average of 1¾% recommended by the Council.

The authorities' Medium Term Budgetary Strategy for 2011-13 targets a deficit of 3% of GDP in 2012, in line with the Council Recommendation. Assuming that the fiscal consolidation package for 2010-11 is fully implemented and moderate expenditure restraint in 2012, this objective appears attainable. A fiscal effort – as measured by the improvement in the structural balance – of about 1% of GDP would be needed in 2012, under the assumptions made above, to reduce the headline government deficit to 3% of GDP.

In parallel with fiscal consolidation, Romania has made progress with the implementation of structural reforms. A Fiscal Responsibility Law was adopted by Parliament on 30 March 2010. A Fiscal Council has been created and is now operational – it examined the 2011-13 medium term budgetary strategy during the summer. A draft pension reform had been adopted by the government and is planned to be passed in Parliament by mid-September. The reform would strongly improve the long term sustainability of government finances, while preserving minimum social standards. Progress has also been made regarding the wage reform in the public sector, but important follow-up legislation remains to be adopted.

Finally, the authorities have placed increasing the absorption of EU Funds at the top of their priorities' list in order to address the exceptionally low absorption rate (around 1.5%). Measures have been taken to strengthen the administrative capacity of the relevant structures, streamline administrative procedures, increase the effectiveness of public procurements, and facilitate access to project co-financing through special guarantee facilities. The effectiveness of these measures remains however to be verified.

3.3. Conclusions

On current information it appears that Romania has taken action representing adequate progress towards the correction of the excessive deficit within the time limits set by the Council.

In particular, the implementation of additional fiscal consolidation measures of around 5% of GDP on an annual basis (including a 25% cut in public wages, a 15% cut in social benefits excluding pensions and an increase in the VAT rate from 19% to 24%) has put Romania on track to achieve the 2010 government deficit target agreed in the context of the multilateral financial assistance programme (7.3% of GDP). In addition, the large carry-overs from the 2010 fiscal consolidation measures and the planned additional savings on the expenditure side should allow a further reduction of the deficit to below 5% of GDP in 2011. Moreover, Romania remains committed to reducing its deficit below 3% of GDP in 2012, and this objective appears attainable.

The measures taken by Romania following the Council Recommendation are an important step towards restoring a sustainable fiscal position and macroeconomic stability. At the same time, significant risks exist. In particular, it will be crucial going forward to ensure that the implemented fiscal consolidation measures remain in force and that their effects are not offset by other policies. Moreover, the authorities should continue to rigorously implement the reforms agreed in the context of the multilateral financial assistance programme.Declarations about new costly policy initiatives and changes to the consolidation package should be avoided. These tend to fuel uncertainty, at a time when Romania needs to reassure investors regarding the predictability of its policies.

In view of the above assessment, the Commission considers that no further steps in the excessive deficit procedure of Romania are needed at present. The Commission will continue to closely monitor budgetary developments in Romania in accordance with the Treaty and the SGP, in particular in the light of the fragile situation of public finances.

Comparison of key macroeconomic and budgetary projections

		2007	2008	2009	2010	2011	2012
Real GDP (% change)	COM Spring 2010	6.3	7.3	-7.1	0.8	3.5	n.a.
	Update COM forecast[1]	6.3	7.3	-7.1	-1.9	1.5	4.4
	CP	6.3	7.3	-7.0	1.3	2.4	3.7
Output gap[2] (% of potential GDP)	COM Spring 2010	7.4	9.3	-1.8	-3.9	-3.4	n.a.
	Update COM forecast	7.4	9.2	-1.2	-6.2	-7.6	-6.4
	CP	7.4	9.5	-1.7	-3.3	-3.7	-2.7
General government balance (% of GDP)	COM Spring 2010	-2.5	-5.4	-8.3	-8.0	-7.4	n.a.
	Update COM forecast	-2.5	-5.4	-8.3	-6.9	-4.4	-3.0
	CP	-2.5	-5.5	-8.0	-6.3	-4.4	-3.0
Primary balance (% of GDP)	COM Spring 2010	-1.8	-4.7	-6.8	-6.2	-5.4	n.a.
	Update COM forecast	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
	CP	-1.8	-4.8	-6.5	-4.5	-2.6	-1.6
Cyclically-adjusted balance[2] (% of GDP)	COM Spring 2010	-4.7	-8.2	-7.8	-6.9	-6.4	n.a.
	Update COM forecast	-4.7	-8.2	-7.9	-5.0	-2.1	-1.0
	CP	-4.7	-8.5	-7.5	-5.2	-3.2	-2.1
Structural balance[3] (% of GDP)	COM Spring 2010	-4.7	-7.7	-8.3	-7.1	-6.4	n.a.
	Update COM forecast	-4.7	-7.7	-8.4	-5.2	-2.1	-1.0
	CP	-4.7	-8.5	-7.5	-5.2	-3.2	-2.1
Government gross debt (% of GDP)	COM Spring 2010	12.6	13.3	23.7	30.5	35.8	n.a.
	Update COM forecast	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
	CP	12.6	13.6	23.0	28.3	29.4	29.7

Note:

[1] Updated forecast prepared in July 2010 by the Commission services in the framework of the multilateral financial assistance programme to Romania.

[2] Output gaps and cyclically-adjusted balances calculated by Commission services.

[3] Cyclically-adjusted balance excluding one-off and other temporary measures.

Sources: Commission services' forecast from July 2010 in the context of the Balance of Payment assistance programme, Commission services' 2010 spring forecast (COM) and March 2010 convergence programme update (CP)