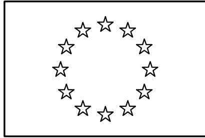

COMMISSION OF THE EUROPEAN COMMUNITIES

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REPORT FROM THE COMMISSION

Romania

Report prepared in accordance with Article 104(3) of the Treaty

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

Many EU countries are presently facing general government deficits above the 3% of GDP reference value set in the Treaty. 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. However, Romania pursued a pro-cyclical fiscal policy during the demand boom between 2005-2008, with headline deficits rising from 1.2% of GDP in 2005 to 5.4% of GDP in 2008, in a context of average real GDP growth of 6.5%. This implied a lack of fiscal consolidation efforts when economic conditions were favourable. Deficit developments were due to a large degree to overall weak budgetary planning and implementation. Initial budgets suffered from an over-estimation of revenues and frequent intra-year budgetary rectifications; no additional headroom was left for more difficult times. Weaknesses in the public administration also contributed to a recurrent under-execution of plans for capital expenditure and part of the resources budgeted for investment were subsequently shifted to current spending such as public wages and social transfers. Finally, large expenditure outlays are concentrated in the last weeks of the year, severely affecting budgetary credibility and predictability.

In its November 2008 European Economic Recovery Plan (EERP), endorsed by the European Council in December, the Commission called for a fiscal stimulus, which should be differentiated across Member States to reflect their different positions in terms of public finance sustainability and competitiveness and should be reversed when economic conditions improve. In an attempt to address its macroeconomic imbalances, the Romanian government undertook fiscal consolidation measures in the 2009 budget adopted in February 2009 and amended in April. Within this budget envelope Romania planned a set of measures aimed at relaunching and stimulating economic growth, notably by allocating a substantial part of spending to public investment. Several countries have taken measures to stabilise the financial sector, some of which impact 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 recouped in the future. Romania took limited financial sector measures of this kind, e.g. mainly a recapitalisation of the two state-owned banks (amounting to some 0.2% of GDP to be recorded below the line).

The Stability and Growth Pact requires the Commission to prepare a report such as the present one whenever the deficit of a Member State exceeds the 3% of GDP reference value. This report analyses the reasons for the breach of the reference value with due regard to the economic background and all other relevant factors. The amendments to the Stability and Growth Pact in 2005 aimed specifically at ensuring that in particular the economic and budgetary background was fully taken into account in all steps in the EDP. This means for instance that, if an “excessive deficit” is deemed to exist, adequate attention needs to be paid to the economic background and outlook when making recommendations on the pace of the

correction. In this way, the Stability and Growth Pact provides the framework supporting government policies for a prompt return to sound budgetary positions taking account of the economic situation.

2. LEGAL BACKGROUND

This report, which assesses recent and current budgetary developments in Romania and reviews the short- and medium-term prospects in the light of overall economic conditions and policy action taken by the government, is prepared according to Article 104(3) of the Treaty.

Article 104 of the Treaty lays down an excessive deficit procedure (EDP). This procedure is further specified in Council Regulation (EC) No 1467/97 "on speeding up and clarifying the implementation of the excessive deficit procedure"[1], which is part of the Stability and Growth Pact. According to Article 104(2) of the Treaty, the Commission has to monitor compliance with budgetary discipline on the basis of two criteria, namely: (a) whether the ratio of the planned or actual government deficit to gross domestic product (GDP) exceeds the reference value of 3% (unless either the ratio has declined substantially and continuously and reached a level that comes close to the reference value; or, alternatively, the excess over the reference value is only exceptional and temporary and the ratio remains close to the reference value); and (b) whether the ratio of government debt to GDP exceeds the reference value of 60% (unless the ratio is sufficiently diminishing and approaching the reference value at a satisfactory pace).

Article 104(3) stipulates that, if a Member State does not fulfil the requirements under one or both of these criteria, the Commission has to prepare a report. This report also has to "take into account whether the government deficit exceeds government investment expenditure and take into account all other relevant factors, including the medium-term economic and budgetary position of the Member State".

On 11 June 2008, the Commission addressed to Romania a Recommendation providing a policy advice[2] on the economic and budgetary policy in Romania. It recommended the country to: i) take urgent action to implement a binding medium-term fiscal framework; ii) implement rigorously the policy invitations of the Council issued on 12 February 2008 on the updated convergence programme of Romania for the period 2007 to 2010 so as to ensure that the general government deficit does not breach the 3% of GDP reference value and to help containing external imbalances and iii) accelerate structural reforms so as to increase Romania's growth potential and strengthening its external competitiveness.

According to data notified by the authorities in April 2009[3] and validated by Eurostat[4], the general government deficit reached 5.4% of GDP in 2008, thus exceeding the 3% of GDP

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[1] OJ L 209, 2.8.1997, p. 6. The report also takes into account the "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 11 October 2005, available at http://ec.europa.eu/economy_finance/about/activities/sgp/main_en.htm.

[2] Commission Recommendation of 12 June 2008, providing a policy advice on the economic and budgetary policy in Romania

[3] According to Council Regulation (EC) No 3605/93, Member States have to report to the Commission, twice a year, their planned and actual government deficit and debt levels. The most recent notification of Romania can be found at:
http://epp.eurostat.ec.europa.eu/pls/portal/docs/PAGE/PGP_PRD_CAT_PREREL/PGE_CAT_PRERELYEAR_2009/PGE_CAT_PREREL_YEAR_2009_MONTH_04/2-22042009-EN-BP.PDF

reference value, while the general government debt stood at 13.6% of GDP in 2008, well below the 60% reference value, but on a growing trend.

Table 1: General government deficit and debt [a]

	2003	2004	2005	2006	2007	2008	2009	2010
General government balance	-1.5	-1.2	-1.2	-2.2	-2.5	-5.4	-5.1	-5.6
General government gross debt	21.5	18.7	15.8	12.4	12.7	13.6	18.2	22.7

Note:[a] In percent of GDP.
Source: Eurostat and Commission services' spring 2009 forecasts.

The figure for the 2008 deficit provides *prima facie* evidence on the existence of an excessive deficit in Romania in the sense of the Treaty and the Stability and Growth Pact. The Commission has therefore decided to initiate the excessive deficit procedure for Romania with the adoption of this report. Section 3 of the report examines the deficit criterion and section 5 deals with public investment and other relevant factors. The document takes into account the Commission services' spring 2009 forecast, released on 4 May 2009.

3. DEFICIT CRITERION

In 2008, the general government deficit reached 5.4% of GDP.

Well in excess of 3% of GDP, the estimated deficit is not close to the Treaty reference value.

The excess over the 3% of GDP reference value cannot be regarded as exceptional.

It does not result from an unusual event in the sense of the Treaty and the Stability and Growth Pact. This definition is to be applied narrowly to cover events such as wars or natural disasters.

It does not result from a severe economic downturn in 2008 in the sense of the Treaty and the Stability and Growth Pact. Despite growth slowing down in the final quarter of the year, overall GDP growth in 2008 accelerated to a rate of 7.1%, from 6% in 2007. This is significantly above the rate of potential growth, estimated to be around 5% in 2007-2008. As a consequence, the output gap increased from around 6½% in 2007 to 8½% in 2008. The economic slowdown is projected to continue over most of 2009, when real GDP is projected to contract by 4%.

The excess over the 3% threshold in 2008 is to a large extent a reflection of the fact that, since 2006, fiscal policy in Romania has been expansionary, not providing any safety margin to avoid an excessive deficit in a downturn. The structural balance also deteriorated sharply since 2006 and despite strong economic growth, the government did not plan any structural adjustment in the successive convergence programmes. Notwithstanding Council recommendations on those convergence programmes, as well as the Commission policy

4 Eurostat news release No 56/2009 of 22 April 2009.

advice of 12 June 2008, the necessary fiscal consolidation was not carried out. In addition, deficits were also driven by a weak budgetary planning and execution and a lack of predictability and discipline, which resulted in systematic budgetary slippages. In 2008, the deficit outturn was more than twice the official target and this significant deviation is mostly due to weak budgetary management with frequent ad-hoc budgetary amendments, using overly optimistic revenue projections to increase expenditure and shifting capital to current spending. This was compounded by a sudden drop in revenues at the end of the year due to the economic slowdown as mentioned above.

Table 2: Macroeconomic and budgetary developments [a]

	2003	2004	2005	2006	2007	2008	2009	2010
Real GDP (% change)	5.2	8.5	4.2	7.9	6.2	7.1	-4.0	0.0
Potential GDP (% change)	3.8	4.1	4.3	4.6	5.1	5.1	3.8	3.1
Output gap (% of potential GDP)	-1.9	2.2	2.0	5.2	6.4	8.4	0.3	-3.0
General government balance	-1.5	-1.2	-1.2	-2.2	-2.5	-5.4	-5.1	-5.6
Primary balance	0.1	0.2	-0.1	-1.3	-1.8	-4.7	-3.6	-4.0
One-off and other temporary measures	0.0	0.0	0.0	-0.6	-0.1	0.0	0.0	0.0
Government gross fixed capital formation	3.5	3.0	3.9	5.1	5.7	5.4	6.3	6.7
Cyclically-adjusted balance	-0.9	-1.9	-1.8	-3.7	-4.4	-7.9	-5.2	-4.7
Cyclically-adjusted primary balance	0.7	-0.4	-0.7	-2.9	-3.7	-7.2	-3.7	-3.1
Structural balance [b]	-0.9	-1.9	-1.8	-3.1	-4.4	-7.9	-5.2	-4.7
Structural primary balance	0.7	-0.4	-0.7	-2.3	-3.6	-7.2	-3.7	-3.1

Notes: [a] In percent of GDP unless specified otherwise.
[b] Cyclically-adjusted balance excluding one-off and other temporary measures.
Source: Eurostat and Commission services' spring 2009 forecasts.

The excess over the 3% of GDP reference value is not temporary in the sense of the Treaty and the Stability and Growth Pact. According to the Commission services' spring 2009 forecast, the general government deficit is expected to reach 5.1% of GDP in 2009 and 5.6% in 2010. This projection is based on GDP growth of -4.0% in 2009 and 0% in 2010. The Commission services' forecast takes into account measures for the current year in the budget for 2009 approved in February 2009 and the additional measures adopted by the government in April 2009.

In view of the large domestic and external imbalances and the adverse effect of the global financial turmoil on the economic and financial situation in Romania, the authorities made a request for multilateral financial assistance in March 2009[5]. The 2009 fiscal measures

[5] The total multilateral financial assistance amounts to up to EUR 20 billion over the period to the first quarter of 2011. The EU provides a medium-term loan of up to EUR 5bn in conjunction with EUR12.95 billion from the International Monetary Fund. Additional multilateral support of €2 billion will be

mentioned above reflect the fiscal targets agreed in the framework of this multilateral financial assistance, i.e. a deficit target of 5.1% of GDP in 2009.

In sum, the deficit is not close to the 3% of GDP reference value and the excess over the reference value cannot be regarded as exceptional and it is not temporary in the sense of the Treaty and the Stability and Growth Pact. This analysis suggests that the deficit criterion in the Treaty is not fulfilled.

4. RELEVANT FACTORS

Article 104(3) of the Treaty provides that the Commission report "shall also take into account whether the government deficit exceeds government investment expenditure and take into account other relevant factors including the medium-term economic and budgetary position of the Member State". These factors are further clarified in Article 2(3) of Council Regulation (EC) No 1467/97, which also specifies that "any other factors which, in the opinion of the Member State concerned, are relevant in order to comprehensively assess in qualitative terms the excess over the reference value and which the Member State has put forward to the Commission and to the Council" need to be given due consideration. Finally, Article 2(5) of the Regulation provides that the implementation of pension reforms introducing a multi-pillar system that includes a mandatory, fully funded pillar should be considered in all assessments in the framework of the excessive deficit procedure. In 2008, Romania adopted such a reform which is implemented in stages, leading to a progressive increase in costs.

In view of the above provisions, the following three subsections consider in turn (1) the medium-term economic position; (2) the medium-term budgetary position (including public investment); (3) other factors put forward by the Member State; (4) other factors considered relevant by the Commission and (5) pension reforms as mentioned above.

4.1. Medium-term economic position

Cyclical conditions and potential growth

Between 2002 and 2008, Romania's GDP has grown on average by an impressive 6.2% year-on-year. This above-potential performance was primarily driven by high wage growth and a powerful credit expansion boosting private consumption and real estate investment. Yet, the domestic demand boom came at the expense of rising domestic and external imbalances and had fuelled concerns of overheating: between 2002 and 2007, the current account deficit widened from 3% of GDP to almost 14% of GDP, subsequently easing to 12.3% of GDP in 2008; widespread foreign currency lending increased households' and companies' balance sheet exposure to exchange rate risks; and high private sector dissaving was exacerbated by rising fiscal deficits. Furthermore, since 2007, core-inflation has been on the rise, after a long period of disinflation, reflecting strong domestic demand pressures and wages growing faster than productivity.

These conditions have significantly increased Romania's vulnerability to the present global economic downturn, with declining capital inflows and falling external demand. Moreover, investor risk-aversion to home-grown vulnerabilities has significantly increased. This has

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provided by the World Bank (€1 billion), the European Investment Bank and the European Bank of Reconstruction and Development (€1 billion together) on top of their general lending activities.

been reflected in the depreciation of the RON, which has lost more than 30% since August 2007. Furthermore, the domestic demand boom has come to an abrupt end since Q4-2008, with real GDP growth falling to 2.9% yoy, from an average of 8.9% in the previous three quarters. According to the Commission services' spring 2009 forecast, GDP is expected to contract by 4% in 2009 and to record zero growth in 2010. On the back of a sharp contraction in domestic demand, net external borrowing is anticipated to ease significantly from 11.8% of GDP in 2008 to roughly 6½% in 2009 and just above 5% in 2010. Inflation is projected to moderate from 7.9% in 2008 to 5.8% in 2009 and 3.5% in 2010 following lower wage growth and still low international commodity prices.

Commission services' calculations according to the commonly agreed methodology show a marked deceleration in the rate of potential growth, from an average of 4.7% in the period 2005-2007 to 3.8% in 2009 and further weakening in 2010. Output gap estimates confirm the scale of the adjustment, with the high positive gap in 2008 (+8.4% of potential output) turning negative by 2010 (-3%)[6]. The multilateral financial assistance will be conditional on the implementation of a comprehensive economic policy programme, encompassing fiscal, financial sector and structural reform measures, which should have beneficial effects on the growth potential in the medium run.

Recent structural reforms

The government implemented several structural reforms, which could have a positive impact on the potential growth of the economy and, therefore, on public finances. In the area of pensions, measures have been taken to increase the long-term financial sustainability of the pension system. These include setting up a voluntary third pension pillar as of 2007 as well as a second pension pillar as of 2008, the gradual increase of the statutory retirement age (to 60 for women and 65 for men by 2014) and of the minimum contribution period (from 10 to 15 years also by 2014). However pension expenditure will come under increased pressure, notably given the impact of ageing on expenditure. In the area of health, reforms aiming notably at improving the quality and efficiency of the health services are planned. With respect to labour markets, measures to boost employment and combat undeclared work included *inter alia* a comprehensive tax reform introduced in 2005 and successive cuts in social contributions over 2006-2008. As set out in the Council's country-specific recommendations on the implementation of the Lisbon strategy[7], further urgent measures are needed to strengthen the efficiency, effectiveness and independence of the public administration, at both central and local level, by building up effective regulatory control and enforcement capacity, as well as to substantially streamline administrative procedures in order to improve the business environment. Substantially increasing energy efficiency could also help tackle Romania's external imbalances in the long run.

4.2. Medium-term budgetary position

Structural deficit and fiscal consolidation in good times

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[6] Output gap figures in general must be interpreted with special caution in the case of an economy such as Romania's, as potential growth is difficult to determine for an economy subject to rapid structural change.

[7] As laid down in the draft report No 6638/09 from the ECOFIN Council to the European Council.

The fiscal stance appears expansionary since 2006 despite economic good times. The structural deficit (cyclically-adjusted deficit net of one-offs)[8] increased from some 3¼% of GDP in 2006 to around 4½% of GDP in 2007 and deteriorated further to just below 8% of GDP in 2008. This has to be seen against an increasingly positive output gap (from 5.2% in 2006 to 8.4% in 2008). Looking forward, the Commission services' spring 2009 forecast projects the structural deficit to fall by around 2¾ percentage points of GDP to around 5¼% of GDP in 2009 and to continue to decline somewhat in 2010[9]. This mirrors the fiscal consolidation measures taken in the budget adopted in February 2009 as well as the additional measures included in the April 2009 budgetary rectification. The rectification reflects the fiscal targets agreed in the framework of the multilateral financial assistance, i.e. a deficit target of 5.1% of GDP in 2009.

Public investment

The general government gross fixed investment to GDP ratio has exceeded the general government deficit ratio since 2002. In 2008, the general government gross fixed capital formation, at 5.4% of GDP was identical to the deficit outturn. According to the Commission services' spring 2009 forecast, public investment should increase significantly in 2009 and the ratio (6.3% of GDP) would be above the general government deficit ratio in 2009 as well as in 2010.

Quality of public finances

General government expenditure rose from 33.5% of GDP in 2004 to 38.5% of GDP in 2008. Compensation of employees, social benefits and government intermediate consumption, represents more than 70% of the total expenditure. In particular, compensation of employees has been growing very rapidly, nominally doubling between 2004 and 2008. Public sector wage growth has become a driver of private sector wage increases, contributing to economic overheating. Public investment as a share of GDP has increased by more than 2½ percentage points of GDP between 2004 and 2008, boosted also by contributions from EU-funds. Nevertheless, relatively high current spending has put an increasing burden on public resources and has left less room for growth-enhancing investments. In addition, in recent years the composition of spending has been regularly modified in the course of the year compared to plans, with more resources devoted to current spending compared to what was initially foreseen in the budget.

The suboptimal composition of spending is also due to weaknesses in the area of budgetary planning and execution. Firstly, initial budgets suffer from an over-estimation of revenues. Secondly, there are several in-year budgetary rectifications, increasing current expenditure levels and shifting capital to current spending. The under execution of capital spending is partly linked to weak administrative capacity to plan and execute public investment projects, while slippages with respect to current spending are also due to the lack of a long-term strategy on public sector wage and pension policy, making spending prone to frequent ad-hoc adjustments. As a result, revenue and capital spending are recurrently lower than initially projected, while current spending, in particular wages and social benefits are higher than

[8] Estimated by the Commission services, applying the common methodology on estimating output gaps.

[9] Structural balance calculations are dependent on calculated output gaps and thus also subject to particular uncertainty for an economy such as Romania – see footnote 6 above.

planned. Finally, there is a high degree of uncertainty and policy discretion and large expenditure outlays are operated in the last few months of the year.

In the economic programme committed to by the authorities in the context of the multilateral financial assistance, measures are foreseen to improve budgetary strategy and process, in particular the adoption and implementation of a binding medium-term fiscal framework, establishing limits on budget revisions during the year, including fiscal rules and the creation of a fiscal council to provide independent and expert scrutiny.

Long-term sustainability of public finances

In the absence of long-term projections of age-related expenditures, based on the common macroeconomic assumptions as carried out by the EPC/Commission, it is not possible to assess the impact of population ageing in Romania on a comparable and robust basis as it is currently done for the other Member States. While a significant impact of ageing on expenditure cannot be excluded given the current demographic structure, the 2008 budgetary position in the programme, with a large structural deficit, is not sufficient to stabilise debt even before considering the long-term budgetary impact of ageing. Improving the structural budgetary position over the medium-term would thus contribute to containing risks to the sustainability of public finances.

4.3. Other factors put forward by the Member State

The authorities of Romania have not submitted a list of relevant factors according to Article 2(3) of Council Regulation (EC) No 1467/97.

4.4. Other factors considered relevant by the Commission

The government 2009 budget includes measures to limit the effect of the economic crisis and stimulate economic growth. The financial cost of this set of measures is at first sight high at 9% of GDP, but this includes some 7% of GDP for public investment and 1.4% for unpaid bills from 2008, which the government committed to pay out gradually in the first three months of 2009. The remaining 0.6% of GDP corresponds to the following main measures: i) a recapitalisation of the two state-owned banks (around 0.2% of GDP, but no direct impact on the 2009 deficit as it is a below-the-line operation); ii) non-taxation of reinvested profits as of second quarter 2009 (0.1% of GDP); iii) funds for export promotion (0.05% of GDP); iv) state subsidies for replacement of old cars (0.04% of GDP); v) prolonging by 3 months the period for which unemployment benefits will be paid (0.03% of GDP); vi) instituting a minimum "social" pension (0.1% of GDP).

4.5. Systemic pension reforms

In 2008, Romania started a pension reform introducing a fully funded second-pillar (mandatory for those aged 35 and below and voluntary for the 35-45 years old). The initial rate of social contribution accruing into the state funded pension scheme was 2% of the gross wage of participants and is set to increase gradually by 0.5 p.p. every year until reaching a contribution rate of 6% in 2016. However, in the context of the 2009 budget, the government decided to postpone to 2010 the increase in the pension contributions to the second pillar to 2.5%, implying a freeze in the contribution at 2% in 2009. This measure is aimed at safeguarding budget revenues.

According to the Romanian authorities, the budgetary impact of the implementation of the second pillar will remain limited. The estimated value of the contributions was around 0.2% of GDP in 2008 and is projected to increase to 0.3% of GDP in 2010, reaching 1% of GDP in 2016.

Table 3: Illustration of the impact of the net cost of system pension reform in Romania

	2007	2008	2009	2010	2011	2012
Government Balance*	-2.5	-5.4	-5.1	-5.6	N.A.	N.A.
Cost or pension reform (total)**	--	0.18	0.33	0.42	0.47	N.A.
Cost (stage1)	--	0.18	0.18	0.18	0.18	0.18
Cost (stage2)	--	--	0.15	0.15	0.15	0.15
Cost (stage3)	--	--	--	0.09	0.09	0.09
Cost (stage4)	--	--	--	--	N.A.	N.A.
Degressive scale (stage 1)	--	100%	80%	60%	40%	20%
Degressive scale (stage 2)	--	--	100%	80%	60%	40%
Degressive scale (stage 3)	--	--	--	100%	80%	60%
Degressive scale (stage 4)	--	--	--	--	100%	80%
Cost to be considered (stage 1)	--	0.18	0.14	0.11	0.07	0.04
Cost to be considered (stage 2)	--	--	0.15	0.12	0.09	0.06
Cost to be considered (stage 3)	--	--	--	0.09	0.07	0.05
Cost to be considered (stage 4)	--	--	--	--	N.A.	N.A.
Cost to be considered (total)	--	0.18	0.29	0.32	0.23	0.15
Adjusted government balance***	-2.5	-5.2	-4.8	-5.3	N.A.	N.A.

* according to Commission services' spring 2009 forecast
** estimates by the Member State
*** government balance adjusted for the pension reform costs to be considered
Source: Commission services

However, the cost of the systemic pension reform according to the Pact[10] should only be considered for adjusting the government balance in the case where the deficit exceeds the reference value, while remaining close to it, which is not the case[11]. In any event, the government deficit adjusted for the pension reform cost in 2008 would be well above 3% of GDP.

5. CONCLUSIONS

The general government deficit in Romania has reached 5.4% of GDP in 2008, above and not close to the 3% of GDP reference value. The breach of the threshold mainly reflects significant slippages with respect to current spending, notably on public wages and social benefits as well as overly optimistic revenue projections and, to a lesser extent, a sudden drop in revenue collection in the last quarter of 2008 owing to the economic slowdown. From 2009, in view of the significant external and internal imbalances and in line with the authorities' economic programme adopted in April 2009 in response to the international financial assistance extended to Romania, fiscal policy is more clearly aiming at correcting such imbalances. Nevertheless, the Commission services' spring 2009 forecast still projects the general government deficit to reach 5.1% of GDP in 2009 and 5.6% of GDP in 2010

[10] EC No 1467/97, Article 2(7), see also the 2007 Public Finance Report (pages 124-129).
[11] In this sense, table 3 is only illustrative as the degressive scale clause is not applicable when the deficit is not close to 3% of GDP.

against a background of a significant economic slowdown. These deficit developments also reflect a lack of fiscal consolidation efforts when economic conditions were favourable.

The excess over the reference value cannot be qualified as exceptional within the meaning of the Treaty and the Stability and Growth Pact, neither can it be considered temporary. This suggests that the deficit criterion in the Treaty is not fulfilled.

In line with the Treaty, this report has also examined "relevant factors". Given that the deficit in 2008 does not satisfy the double condition of closeness and temporariness, these factors cannot, according to the Stability and Growth Pact be taken into account in the steps leading to the decision on the existence of a excessive deficit. Considered on their own merit, the relevant factors in the current case on balance present a mixed picture.

The existence of a severe economic downturn, with potential public finance implications, increases the need to undertake enhanced surveillance under the EDP.