Aspen Dialogues Webinar: New Mechanisms for Financing the Economy
Webinar Report

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About the Webinar

The webinar, organized under the aegis of the **Aspen Dialogues** series and the **Aspen Economic Opportunities & Financing the Economy** public policy program, analyzed how Romania can benefit from the **new and complex mechanisms of financing the economy across Europe**. The workshop covered the debates at the EU level on the next **Multi-Annual Financial Framework and the EU Recovery Package**. The discussions focused on the need to direct public and private funds towards investments, looking into post-pandemic **challenges and opportunities for entrepreneurs, SMEs, and large companies**. The new economic instruments come on top an on-going process of developing the Green Deal in Europe, which implies significant costs of transition for newer member states like Romania. All these new mechanisms require a much heavier emphasis than before on the **public partnership with the private sector** and the financial sector in particular.

About the Aspen Economic Opportunities & Financing the Economy Program

The **Aspen Economic Opportunities & Financing the Economy Program** is a non-partisan platform for debate. Under the umbrella of the Program, a community was created comprising multiple stakeholders from the public, private, and non-governmental sectors, aiming to identifying key constraints and untapped opportunities facing the existing economic, investment, and development model of Romania and to formulate key public policy recommendations.

Speakers:

- **Cristina Buzaşu-Enache** – State Counsellor for European Affairs to the Prime Minister, Government of Romania
- **Csaba Bálint** – Member of the Board, National Bank of Romania
- **Prof. univ. dr. Cristian Păun** – President of the Board, National Credit Guarantee Fund for SMEs
- **Lara Tassan Zanin** – Head of the EIB Group Representation in Romania
- **Radu Ciocoiu** – Executive Director, Regional Corporate and Public Sector, Raiffeisen Bank Romania

Moderator: **Dr. Clara Volintiru** – Director, Aspen Economic Opportunities & Financing the Economy Program/ Associate Professor, Bucharest University of Economic Studies

Key Take-aways

The economic crisis caused by the SARS-COV-2 pandemic has shown that **promoting investments and reforms as well as taking adequate fiscal measures are essential steps in fostering sustainable economic growth**. To encourage member states to take such steps, the European Union (EU) brought about **new financing mechanisms to counter the multiple effects of the crisis**, offering member states significant opportunities to complement national budgets and make much-needed investments in priority areas.

An unprecedented amount of EU funding is available to member states through the new, **consolidated 2021 – 2027 Multiannual Financial Framework (MFF)** together with **new mechanisms such as the €750 billion NextGenerationEU**, aiming to help member states **recover from the crisis and increase resilience at the national and EU-level**. Together, these financial instruments sum up to almost **€1.8 trillion**. The key difference in the upcoming EU funding opportunities is their **focus on sustainability**, in line with the upcoming green transition at the EU level.

Romania can take advantage of the new MFF and the NextGenerationEU initiative, having managed to obtain a total allocation of almost **€80 billion**. This is a **unique opportunity for Romania to invest in projects in crucial areas** such as transport, energy, digital but also hospital and school infrastructure, health, R&D, education, agriculture. **Quality investments in these sectors are vital for increasing the country's productivity and competitiveness**.

Cohesion policy will remain a key part of the MFF, with an allocation of €28.2 billion for Romania. Following a consultation process, the Government has proposed 16 operational programs in key areas in order to benefit from this funding, as well as 8 regional programs which will be managed by the regional development agencies. Through the **common agricultural policy**, Romania was allocated approximately €19.3 billion for direct agricultural payments and rural development.

A large part of the €80 billion allocated to Romania, around €30.4 billion, come from the **Recovery and Resilience Facility**, which is the centerpiece of the NextGenerationEU initiative. However, to access funds from this plan, each member state must prepare a well-organized **National Recovery and Resilience Plan** outlining country priorities. The Romanian Government presented its Plan in November 2020 and started the public consultations process. The Plan outlines **both investment and reform priorities**, in line with the EU's country-specific recommendations in the European Semester. It is a **strategic plan**, aimed at setting out transformations which are much awaited by public and private sector and civil society alike.

In terms of investment priorities, the Plan is built on **3 pillars**, tailored to 12 specific areas:

1. **Green transition and climate change**: priority investments here include issues such as sustainable transport (improving connectivity and completing the TEN-T comprehensive network), renewable energy, green and smart technologies in the energy sector, electricity infrastructure, energy efficiency.

2. **Public services, urban development and heritage**: key priorities under this pillar are improving the health system and education (better access to public health, including oncology, dual education, better correlation of skills to the labor market).
3. **Economic competitiveness, digitalization and resilience**: focusing on improving the business environment, developing entrepreneurship and industrial ecosystems, upgrading the economic competitiveness of SMEs, research & innovation, digitalization of public services including health & education.

Together with these investment priorities, the Plan acknowledges the need for **wide-ranging reforms, both horizontal and sectoral**, in order to boost competitiveness and be able to use the available funds efficiently. Horizontal reforms that are prioritized refer to the **financial sustainability of public financing** and **increasing the flexibility of the labor market**. Key sectoral reforms needed are the **creation and support of an adequate legal framework** for the proposed investments, as well as increasing the **quality and accessibility of public services**.

The green transition and green finance will be on top of the EU agenda, as the Green Deal is paving the way for a new sustainable, carbon-neutral economic model. The EU has set the goal of becoming carbon-neutral by 2050 and the ambitious intermediary target of reducing greenhouse emissions tp 55% of the 1990 levels by 2030. Romania will face **significant transition costs**, as its greenhouse emissions are about 3 times higher than the EU average. Thus, meeting EU targets requires **complex and difficult adjustment measures for the economy and citizens**. The move to a low carbon economy does not just imply green energy production, but also less emission-intensive industries. Romania still has a **high dependence on both coal-based energy production (and a switch to natural gas would not be ambitious enough) and carbon-intensive industry**. Furthermore, green energy production can absorb very little employment (about 1 in 100 workers from carbon-intensive energy production), underlining a **clear need to upskill and reskill employees**.

The **Just Transition Fund** will provide much-needed support, with almost €2 billion available for Romania. The Fund is aimed at helping the reskilling workers from carbon-intensive energy producers and enterprises, as well as the **economic and social reconversion** of areas affected by the green transition. In addition to this, the **Modernisation Fund** will support 10 lower-income EU member states in their transition to climate neutrality by helping to update their energy systems and improve energy efficiency. Romania will be one of the beneficiary states, with an allocation of about €500 million/year for the next 10 years. Furthermore, the **European Investment Bank** (EIB) will have about €7 – 10 billion available to Romania in the next decade.

However, despite the unprecedented level of available opportunities, the **potential risk** to Romania is that all this EU funding comes with strings attached. This can provide **significant challenges** in terms of:

1. **Timeline:** The Recovery & Resilience Facility must be committed (meaning that projects must be agreed on and signed) by 2023, while the implementation stage is until 2026. This requires very **pragmatic and realistic project preparation** on behalf of member states, which Romania has sometimes lacked in the past.

2. The EU funding is available with a purpose, requiring **substantial structural reforms**, for instance in the case of the **EU-wide green and digital transitions**. To prepare quality projects that can be approved, Romania needs to **improve public policies** and be able to **carry out much-needed reforms**, such as those provided by the National Recovery and Resilience Plan. In addition to reforms related to the green and digital transitions, there is a clear need for the **structural reform of the education sector**, with an emphasis on skills for the future. Furthermore, to be able to respect implementation deadlines, Romania must **reform public procurement** in order to make procurement processes more effective. Romania has had disagreements with contractors which often ended up in court and sometimes led to cancelled contracts, creating a lose-lose scenario and making quality contractors avoiding the country on the long-term. Furthermore, to gain access to other types of funding, Romania should **reform its framework for PPP partnerships**.

In order to be able to deal with these challenges, future decision-makers will need **concerted political will and a strong, ambitious, consensus-oriented vision**. A more **team-oriented approach across Ministries and relevant agencies** is also needed for quality policy planning. To make the most of the available funds, investment plans should **focus on what is achievable in the imposed timeline** and should be **targeted at the appropriate financial instruments**. Long-term needs that require significant project preparations (e.g. new hospitals, large infrastructure projects) should be left for the MFF. Projects related to the green transition should be aimed at the Just Transition Fund and the Modernisation Fund. The EIB can provide technical assistance for such projects.

Another key lesson is that a **closer partnership between public and private sector** is needed. To foster investments and the development of the business sector, decision-makers need to provide **legal stability and predictability of regulations**. The **financial sector** can have a highly relevant role in the NextGenerationEU thanks to its ability to act as a **channelling agent**. One example of good practices in the financial sector is the Raiffeisen Sustainability Report which has been carried out for 11 years and is a useful tool in channelling funds to where they are most needed. Furthermore, to combat the effects of the pandemic, the financial sector has created partnerships with the state. For instance, Raiffeisen has worked closely with the National Credit Guarantee Fund for SMEs and Eximbank but also the European Investment Fund to adapt products to the new situation**. Such partnerships can unleash financing on the market by targeting projects focusing on sustainable development and adapting to a new reality**.

The SARS-COV-2-induced crisis has had a strong effect on SMEs because of their very **low capitalization**. Access to finance is a global problem for SMEs but in Romania the banking sector is financing the private sector in a particularly small proportion. In Romania, there is relatively **little interest from SMEs to access finance through the financial sector and financial institutions**. SMEs finance themselves to a high extent through commercial credit (relying to customers and suppliers), a fact which has led to a **big liquidity problem during the crisis**.

A solution could be **an extended program to facilitate access to investment capital** for such companies. There is a clear need to **diversify sources of financing**, in particular long-term financing. SMEs must be offered the option to look to the **capital market** for solutions, as an over-reliance on bank loans damages competitiveness. Thus, the creation of investment funds and venture capital funds must be promoted. Furthermore, a **guarantee scheme for leasing finances** is needed, as leasing is a very reliable, long-term financing scheme that shares the risk between the financial company and the SME. A **guarantee scheme for factoring and also discounting the bills of exchange** at the level of companies should also be considered.

While the government has, during the pandemic, offered public aid schemes such as grants to SMEs and large companies, **more ambitious programs in support of the business environment**, particularly SMEs and new investors, should be designed. An example of good practices is the implementation of the **IMM Invest** program, in which banks provided SMEs with credits which were guaranteed by the state. Thus, the **support of banks was crucial** in 2020, as IMM Invest facilitated access to capital for more than 22,000 companies, more than 60% of those being micro-companies. Around RON60 billion were granted, half of that for investments, and financing. IMM Invest showcased a **strong partnership between banks, SMEs, and the state (with its guarantee letter)**.

The Romanian economy faces the **dual pressure of a much-needed economic transition towards a model based on sustainability and digitalization, coupled with the need for a post-pandemic recovery**. While, during the first lockdown in Spring 2020, there was a deep and unprecedented economic contraction, recovery started since May, albeit not at the pace that could be expected. The initial shock was similar to the one suffered during the 2008 crisis, but, systemically, **financial conditions are better now**: the system is marked by less volatility, lower interest rates, stable exchange rates, and government deficits are being financed by markets. Central Banks played a helpful role in ensuring this. There is a need to fine tune some measures but measures such state guarantee for loans have been very important. The banking sector is recovering as lending activity is starting to increase again. Thus, **support of monetary and fiscal policies contributed to the recovery**.

The **short-term outlook** for the economy is influenced by the powerful second wave of the pandemic. Research suggests that the economic impact could be much lower than in the first wave, due to more targeted, less stringent measures. While the public and private sector gained experience in handling the crisis, **economic recovery will probably be asymmetric across the world**. Overall, the second wave seems to more of a **slow-burning crisis** compared to the first wave shock.

However, when looking at **long-term consequences**, the **costs of the crisis will be very high** as the damage to the system has been huge. There are higher and higher government deficits across the world, which is normal because the economy needs to be supported during the crisis. Nevertheless, **managing debt will be a big challenge**. Very well-designed policies will be needed domestically and externally. On the positive side, **the pandemic accelerated a series of structural changes in the economy** (e.g. work from home) and **accelerated the shift to a greener, digital economic model**. Overall, **EU funds may be a game changer** in helping overcome the effects of the crisis, but Romania requires quality policy-making and structural reforms to make the most of existing opportunities.