

## **IMF calls for ‘aggressive’ restructuring of state companies**

*This is an excerpt of a Business Review interview with IMF Resident Representative Guillermo Tolosa, published on April 24, 2014. [Read the full interview on the Business Review website.](#)*

Guillermo Tolosa, resident representative in Romania and Bulgaria of the International Monetary Fund, says the government needs to step up its reforms of state-owned companies to reduce arrears, noting that the involvement of the private sector in the management of these firms has registered an “uneven performance”.

### **What are the areas in which Romania’s progress has been limited under the EUR 4 billion stand-by program with the IMF and European Commission?**

We should first note that major progress has been achieved. Our program with Romania is on track, and macroeconomic fundamentals strengthened further last year. Economic growth reached a post-crisis high. The current account deficit narrowed significantly in 2013. And inflation has fallen to historic lows. As a consequence, the government and private sector can now borrow at record low interest rates. It is also remarkable that for the first time Romanians now pay less for bank loans in lei than in foreign currencies. These strong macro fundamentals have also made Romania more resilient to external shocks, as proven by the country’s capacity to cope well during the recent volatilities in capital market flows.

There has also been some progress in terms of structural policies, which should put such growth on a more sustainable basis. The IPOs for the two energy companies last year and the implementation of the road map for liberalizing energy prices are important accomplishments.

Unfortunately, however, these achievements have not been matched in other areas. The end-December target for reducing the arrears of state-owned enterprises (SOEs) was missed by a substantial margin. While the authorities have taken some corrective actions to remedy this shortfall, a sustained effort is needed. This includes the aggressive restructuring of SOEs, in particular CFR Marfa, the attempt to privatize which has failed. Weak payment discipline or ability in the public sector needs to be overcome once and for all. Otherwise the public sector will hold back the prospects for sustainable, broad-based and shared economic growth.

### **How will Hidroelectrica’s reentry into insolvency impact the reform program in the energy sector? Aside from the energy sector, what fields are in dire need of reform?**

Let me step back a bit once again on the issue of the performance of SOEs. SOE reform is a crucial element of the economic program supported by this SBA (stand-by agreement). It is not an end in itself but a vital element to achieve the government’s growth ambitions.

In particular, the energy and transportation sectors can become motors of growth. But for that to happen they require upgrading and investment. Funds will only be attracted when these companies are run professionally and more efficiently. Many of the firms still deliver poor quality services, far below EU standards. The slow speed of trains is just one example. That's why the program seeks SOE reform in a number of ways. One is the involvement of the private sector in management. And here performance has been uneven.

We have seen too many changes on boards that coincide with changes in political leadership in line ministries. Another area is private involvement through IPOs. Here Romgaz was a major achievement and Hidroelectrica and Oltenia are set to follow.

The decision to put Hidroelectrica back into insolvency was out of the government's control. But we expect the IPO to happen as soon as possible after the renewed exit from insolvency. For Oltenia, we expect a potential delay for technical reasons (for assessing the coal reserves) to be strictly limited in time. In order to secure continued future successes, it is important that companies that have gone through IPOs are not engaged in new plans which can represent significant deviations from the roadmap for the companies originally presented to investors.

However, there is much more to the reform program agenda of SOEs than these two companies. The government has committed to continuously reduce arrears for all SOEs. This requires tackling the companies' underlying root problems. Many need to be restructured and made more efficient, in particular in the transport sector. Others need to receive sufficient budgetary transfers to cover their costs and avoid arrears. The SBA includes specific indicators for these targets. After a slippage regarding the SOE arrears target for end-December, there is no more room to delay difficult choices to achieve these targets in the future.

**Can we conclude that Romania has scrapped the deregulation of the gas market for industrial consumers after the government passed a draft bill last month allowing big industry to negotiate deals directly with gas producers? Were you consulted on this change?**

The energy regulator has so far fully implemented the agreed roadmap on energy price deregulation. The market for electricity for non-residents is already fully deregulated and important steps have also been taken for the gas market. It is important to continue this process, which will allow the full deregulation of gas prices for non-residents later this year.

Large consumers have been able to negotiate deals with gas producers in a free market, and there is no legislative change in this regard. Going forward, it is important that the government refrains from any type of interference in the free market.

**What role has the IMF played in the scheme designed to cut repayment rates for close to one million Romanians? The facility, dubbed Electorata, would grant income tax credits to those enrolling in this system. Has the IMF gauged the potential impact of this scheme on banks? Will it sustain gains in domestic consumption?**

This support scheme has been proposed by the government with the objective of supporting those households that have relatively low incomes and spend a large share of it on servicing their debt. Indeed, as a consequence of the crisis, households are still highly indebted. The government proposal would give certain households some breathing space and potentially increase their spending. How large the macroeconomic impact is, will depend on how many individuals and banks decide that this is an option that makes sense to them. Also, the government has committed to design the scheme in such a way that the future fiscal costs, which would be incurred as tax credits in 2016-17, would not exceed 0.1 percent of GDP.

A key positive feature of the scheme is that it is entirely voluntary. Therefore, banks do not have to make any decisions that would have a negative impact on their financial results. Against this background, and in the context of the still weak domestic demand, the scheme is not considered to go against the fundamental objectives of the IMF program.

**What is holding back bank lending in Romania?**

Our assessment is that the decline in credit in recent months is the result of tight supply and weak demand. Therefore efforts are needed in both areas to revive credit growth. On the supply side, steps to clean up banks' balance sheets are important and we're seeing some encouraging efforts. Some banks are in the process of putting NPLs (non-performing loans) up for sale after the tax treatment of such sales was finally clarified. Moreover, the National Bank of Romania is working on an action plan to reduce bad loans on banks' balance sheets. This is a new structural benchmark under the program.

At the same time, credit constraints for small and medium-sized enterprises are being addressed through an improved and expanded lending guarantee scheme. Also, in support of households, the authorities are continuing the guarantee scheme for first-time home buyers.

And very importantly, on the demand side credit is being supported by lending rates which are at historical lows. More generally, credit demand can be fostered by further strengthening the broad policy framework to secure a stable and predictable environment for investments.