



The World Bank

Romania Second Programmatic Inclusive and Green Growth Development Policy Loan (P179297)

Program Information Document (PID)

Appraisal Stage | Date Prepared/Updated: 26-Apr-2023 | Report No: PIDA36054

**BASIC INFORMATION****A. Basic Project Data**

Country	Project ID	Project Name	Parent Project ID (if any)
Romania	P179297	Romania Second Programmatic Inclusive and Green Growth Development Policy Loan (P179297)	P178912
Region	Estimated Board Date	Practice Area (Lead)	Financing Instrument
EUROPE AND CENTRAL ASIA	30-Jun-2023	Macroeconomics, Trade and Investment	Development Policy Financing

Proposed Development Objective(s)

The Program Development Objective (PDO) of the proposed series is to support the Government of Romania's efforts to: 1) strengthen inclusion and fiscal management; and 2) foster decarbonization and climate resilience.

Financing (in US\$, Millions)**SUMMARY**

Total Financing	650.00
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DETAILS

Total World Bank Group Financing	650.00
World Bank Lending	650.00

Decision

The review did authorize the team to appraise and negotiate



B. Introduction and Context

Country Context

The proposed operation of US\$650 million is the second in a programmatic series of two operations to support the Government of Romania to enhance inclusion; strengthen fiscal management; and foster decarbonization and climate resilience. Following the first operation comprising a EUR 600 million IBRD loan (equivalent to US\$641.7 million) and a US\$24.2 million grant from the IBRD Fund for Innovative Global Public Goods Solutions, this second operation comprises a proposed US\$650 million IBRD loan. Romania continues to see substantial poverty and inclusion challenges, as reflected in the forthcoming Systematic Country Diagnostic (SCD) Update as well as the 2018 SCD. Regional income and service delivery disparities are wide, the impact of social transfers on reducing poverty and inequality is among the lowest among European Union (EU) countries. The population has the highest poverty rate and is among the most unequal in the EU, with 11.3 percent of the population estimated to be poor (using the international poverty line of \$6.85-a-day in 2017 Purchasing Power Parity terms) and with a Gini coefficient of equivalized disposable income of 34.3 in 2021, fourth highest in the EU and above the EU average of 30. Hence, the inclusion agenda is paramount in the country, gaining added significance with Russia's invasion of Ukraine and the unprecedented influx of forcibly displaced persons (FDPs) into Romania. The country has also been running a large structural fiscal deficit, averaging 3.5 percent of GDP during 2010-21, fueled by tax cuts and numerous exemptions, and untargeted permanent spending increases. With the economic and humanitarian spillovers of Russia's invasion of Ukraine (particularly support to households and firms in the face of elevated energy prices and accommodation of the refugees), fiscal pressures are on the rise. The war in Ukraine has also raised issues of energy security and independence, adding to the debate on the sector's role in achieving reduced greenhouse gas (GHG) emissions. As an EU member, Romania is signatory to the European Green Deal with its ambitious, timebound decarbonization targets of reaching the net zero emissions by 2050.

Romania's macroeconomic policy framework is adequate for this operation. Despite the economic shock of the Russia's invasion of Ukraine and its accompanying fiscal pressures, the government continues to implement a macroeconomic policy mix aimed at reducing the fiscal deficit while supporting vulnerable populations (including the forcibly displaced persons and host communities), stabilizing the public debt, and containing internal and external imbalances.

Relationship to CPF

This DPL series underpins all the three objectives of the Country Partnership Framework (FY2019-23). The inclusion actions – those on FDP, host community, the disabled, and the social protection reforms - map directly into the Focus Area I: 'Ensure Equal Opportunities for All', specifically, on improving access to modern health care and connecting the poor and vulnerable to jobs. The green agenda links to Focus Area III: 'Build Resilience for Shocks', specifically, on improving preparedness to natural disasters and climate change. The actions on renewables also link to the Focus Area II: 'Catalyze Private Sector Growth and Competitiveness'. In addition, the proposed operation benefits from the World Bank Group Green Resilient and Inclusive Development (GRID) approach; the Fragile Conflict and Violence (FCV) Strategy 2020-2025; the Global Crisis Response Framework (GCRF); and is private capital enabling (PCE).

This operation supports progress towards the WBG's twin goals in Romania. Increased support to and integration of FDPs from Ukraine into the Romanian society will help them become self-reliant and enable them to get employed. This will help them sustain themselves and provide for their families. The implementation of the Law on the Minimum Inclusion Income (also referred to as VMI Law - or Venitul Minim de Incluziune (VMI) and the law on deinstitutionalization will help address the inclusion agenda more broadly, particularly supporting those in the bottom 40 of the income distribution. Fiscal reforms will enable efficient use of fiscal resources and increased fiscal space. This will help the government increase fiscal buffers and improve public spending which will be beneficial for the poor and those in the bottom 40 percent of



income distribution. Efforts aimed at decarbonization and increased forest cover will help Romania advance on its climate objectives and will support a reduction in extreme weather events which typically impact the poor and vulnerable to a larger extent. Finally, increased private sector participation in renewables and building renovations will provide jobs while also supporting the transition to net zero emissions.

C. Proposed Development Objective(s)

The Program Development Objective (PDO) of the proposed series is to support the Government of Romania's efforts to: 1) strengthen inclusion and fiscal management; and 2) foster decarbonization and climate resilience. The government seeks to: improve fiscal management, as fiscal balances were significantly impacted by the COVID-19 pandemic; protect and improve efficiency of critical social spending amid rising spending pressures associated with the war in Ukraine; and advance its green transition objectives. The proposed Inclusive and Green Growth DPL will support the government of Romania in addressing some of the key structural challenges faced by the country.

Key Results

The reforms supported by pillar 1 of the programmatic DPL series will help achieve the following results: (i) increased access to FDPs to healthcare and education services and (ii) to the Romanian labor markets; (iii) increased access of the poor to social assistance programs; (iv) better integration of adults with disabilities; (v) improvement in the fiscal position of the government through improved budgeting and higher tax collection. The reforms supported by pillar 2 of the programmatic DPL series will help achieve the following results (vi) increase in the share of buildings renovated with increase in energy efficiency; (vii) Increase in renewable energy and storage capacity contracted; (viii) reduction of coal-fired generation capacity; and (ix) increased area under afforestation and reforestation works.

D. Project Description

Under the inclusion objective, the first pillar includes the response to accommodate and help integrate the FDPs from Ukraine and increase the impact of social protection on reducing poverty. To further assist the FDPs and host communities, DPL2 will support the provision to FDPs of public employment services and Romanian language training and ensure that FDP and host community students benefit equally from resources provided to FDP hosting schools. To enhance inclusion, DPL2 aims to support measures that will strengthen the adequacy of social assistance, enable implementation of the Minimum Inclusion Income Program and the deinstitutionalization of persons with disabilities.

The first pillar also addresses structural inefficiencies that have contributed to Romania's fiscal imbalances. The DPL supports measures articulated in the government's medium-term reform program aiming to implement the reforms included in the National Program of Recovery and Resilience (NRRP), which is part of the European Resilience and Recovery Facility. The Bank has been providing support to the government of Romania in many of these key reform areas, prior to the formulation of the NRRP. To strengthen fiscal management, DPL2 supports measures that will enhance tax collections by reducing tax expenditures.

The second pillar fosters decarbonization by tackling key gaps in the legislative framework with respect to renewables and its storage, the inclusive transition from coal, the strengthening of energy efficiency in buildings and deepening of carbon sinks. In line with the European Green Deal, the government of Romania is taking steps to achieve climate neutrality by 2050. The second pillar of this DPL series supports the government's efforts in this direction through policy and institutional reforms that will help the country decarbonize and mobilize private sector capital in relevant areas like renewables, battery storage and energy efficient building renovation and industrial activities. The operation will also



support Romania's energy independence and security via increased investments in renewables and other fuels like green hydrogen and by optimizing energy consumption through energy efficiency measures. Particularly, this second operation builds on energy efficiency measures in hard-to-abate sectors, supports the development of low carbon fuels and storage capacity for renewables and the transition out of coal and further strengthens afforestation and reforestation efforts.

E. Implementation

Institutional and Implementation Arrangements

The Ministry of Public Finance (MoF) leads the effort in coordinating the overall implementation of the DPL. The MoF has experience and is conversant with World Bank policies and procedures through lending, Reimbursable Advisory Services (RAS) and Technical Assistance (TA) operations. Given the history of budget lending operations in Romania, some institutional capacity has been built up on data requirements and overall monitoring arrangements. Romania is a subscriber to the Fund's Special Data Dissemination Standard Plus (SDDS Plus) since November 2019. In addition, data is generally available through the MoF and the central bank's website. The World Bank team will continue to provide support to the government in monitoring the reform progress and results.

The World Bank team works closely with relevant ministries and agencies to monitor progress. This includes the MoF, the National Bank of Romania (NBR), the Chancellery of the Prime Minister, Ministry of Labor and Social Solidarity, Ministry of Education, Ministry of Energy, Ministry of Environment, Water and Forests and other relevant ministries.

F. Poverty and Social Impacts, and Environmental, Forests, and Other Natural Resource Aspects

Poverty and Social Impacts

Overall, the policy reforms supported by this operation are expected to have mostly positive or neutral effects on the well-being of Romanian households in the long run, with some short-term costs associated with some of the actions under both Pillar I and Pillar II. In the medium term, most actions are expected to have positive impacts. Most prior actions under Pillar 1 are expected to bring positive or neutral poverty and social impacts, except for measures reducing tax exemptions, which can have negative short-term impacts but positive medium-term welfare impacts. Most prior actions under Pillar 2 are expected to bring positive or neutral poverty and social impacts, provided the potential unintended short-term effects on the poor and vulnerable are mitigated properly. This is especially true for the actions related to the phase out of coal and increased afforestation and reforestation efforts. Nevertheless, the actions supported by this operation include several mitigating plans such as upskilling affected workers, reinforcing the social safety nets in local communities, and revitalizing economic programs in affected regions. Several prior actions provide strong support to women and marginalized groups.

Environmental, Forests, and Other Natural Resource Aspects

The prior actions supported by this DPL have positive or neutral environmental impacts. The Pillar I prior actions of this operation are expected to have neutral or positive effects on the environment, forests, and other natural resources. Actions to ensure the right for FDPs to access social services help mitigate the potential adverse environmental effects associated with FDP-affected areas such as subsistence use of the environment to meet basic needs and unregulated waste disposal or water use. The access of FDPs to services and assistance reduces the risk of establishment of unregulated FDP camps or informal settlements. The remaining actions under this pillar are expected to have neutral effects. The Pillar



All policy and institutional reforms have significant positive effects while the implementation related potential negative environmental effects in the medium- to long-term can be dealt with by Romania given its existing legal framework. Actions aiming to promote renewable hydrogen and low-carbon gases have several potential positive environmental effects, as they are expected to lead to decreased reliance on fossil fuels, leading to reduced greenhouse gas emissions while also reducing some types of air pollution. These measures will not only have environmental benefits but will also have positive effects on health and human capital. The Decarbonization Law and actions to accelerate the energy efficiency in the industrial sector in Romania primarily aim to have positive environmental impacts by phasing out coal-fired electricity generation and coal extraction, as well as improving energy efficiency, thus reducing greenhouse gas emissions and pollution. Increased storage capacity for renewables will also have similar positive environmental benefits with existing legislation capable of dealing with potential negative effects related to battery production and disposal. Laying down binding rules for afforestation and reforestation will contribute to both climate change mitigation and adaptation. It will increase long-term carbon storage within forests and will help balance the overall national GHG emissions. It will further help to restore ecosystem integrity and enhance forest cover in Romania. Despite these notable positive benefits it is advisable that, during implementation, investments in these areas ensure that land use and waste is adequately managed by the existing legislative framework, including Environmental Impact Assessments (EIA). Notably, Romania's Environmental Impact Assessment (EIA) regulatory system (to which these investments would be subject) already mandates appropriate mitigation measures such as landscape impact assessment, implementation of adequate waste management protocols and supervision, ex-ante identification of indigenous protected fauna and flora and impact mitigation plans during construction and operation.

G. Risks and Mitigation

The overall risk rating for this operation is Moderate. Among the risk categories, political and governance risk and implementation risk is deemed to be substantial, technical design risk is low, while all other risk categories are rated as moderate, including 'other risks' related to the spillovers from the war in Ukraine. The political and governance risk is substantial as, in recent years, there have been frequent changes in political leadership because of unstable ruling coalitions. Nevertheless, the current ruling coalition has brought stability to policy making in Romania through a power sharing agreement which is expected to hold through to 2024, the year of elections for all levels of government. Risk mitigation includes strong government ownership and the backing of the European Commission for the reforms, supplemented with financing through the Recovery and Resilience Facility, as well as the Bank's strong policy dialogue with the government of Romania. In terms of other risks, there is considerable uncertainty related to the ongoing war in Ukraine which could potentially get prolonged. These events could have substantial implications on FDP arrivals, energy costs and supply, the green transition and other broader repercussions, including impacts on growth, fiscal needs, and security concerns. The government is taking measures to shield consumers and firms from excessive price hikes, including support from the EU. On implementation risks, while the legislative and regulatory framework of the country is fairly strong, the relatively weaker implementation capacity risks reducing the impact of reforms. This risk is mitigated by the fact that Romania receives significant assistance from the World Bank, the European Commission and other development partners for institutional capacity strengthening. On the reforms supported by this DPL, the World Bank will continue to provide technical assistance; and capacity building efforts will also be undertaken for many of the reforms. Close supervision of this operation will help address the challenges related to institutional capacity. The World Bank's existing and planned engagements will support reform implementation.

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APPROVAL

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