Box 10. Structural vulnerabilities of the non-financial corporations sector in Romania

The structural vulnerabilities of the non-financial corporations sector are: (A) the large number of undercapitalised companies, (B) loose payment discipline, (C) the significant share of high-climate risk companies and (D) the small share of high-tech or high-knowledge industries. These vulnerabilities are likely to amplify the negative effects of the current crisis and depress the post-crisis recovery of the sector. Moreover, they put a damper on the development opportunities of the economy and the implementation of economic reforms.

A. Large number of undercapitalised companies

The non-financial corporations sector in Romania is characterised by a large number of companies with considerable capitalisation deficiencies. In 2019, there were 244.1 thousand firms with equity below the regulatory threshold, accounting for 35.4 percent of the total number of non-financial corporations. The capitalisation needs of these companies were estimated at lei 154.6 billion. Most of undercapitalised companies, i.e. 97 percent, reported negative equity. This vulnerability has significant implications for payment discipline (many of these firms recording substantial overdue payments in relation to their trading partners and/or the government budget) and for the access to finance.

B. Loose payment discipline

Loose payment discipline and poor corporate governance are another important vulnerability. This is a direct result of the large number of undercapitalised companies. Before the pandemic outbreak, the ratio of overdue trade debt stood at 15.2 percent and 16.1 percent respectively for SMEs (at end-2019). Companies with equity below the regulatory threshold made up approximately 55 percent of the volume of overdue payments in 2019. Another relevant aspect of payment discipline is the large share of trade credit in corporate financing (17.3 percent of firms' liabilities and owners' equity). Companies' payment discipline can be improved through a more efficient enforcement of Law No. 72/2013, which stipulates, *inter alia*, that the maximum payment period, currently standing at 120 days on average, cannot exceed 60 calendar days. In addition, better informing companies, especially SMEs, about the negative impact across the economy of the late payment and the rights granted by Law No. 72/2013 can contribute to improving payment discipline.

For financing their daily activity, apart from the wide resort to trade debt, companies also use to a significant extent the loans from shareholders and their affiliates, which amounted to lei 206.6 billion at end-2019, holding 12 percent of enterprises' liabilities and owners' equity.

C. Significant share of high-climate risk companies

The domestic economy is particularly based on energy-intensive sectors, which places Romania among top five European countries with a high intensity of greenhouse gas emissions. The measures that can contribute to increasing energy efficiency at national level could be aimed at: (i) promoting energy efficiency and developing less energy-intensive services sectors or (ii) energy policies, particularly by reducing the reliance on fossil fuels.

D. Small share of high-tech or high-knowledge industries

The small number of high-tech or high-knowledge industries also counts among the vulnerabilities of the Romanian economy. Moreover, research and development activities are very poorly represented. In 2018, research and development or innovation expenditure accounted for 0.5 percent of GDP (one of the lowest levels EU-wide). The digitalisation of economy is also limited, with Romania ranking third among the worst performing countries in this area.

The risks generated by the COVID-19 pandemic reiterate the need to solve these structural problems with a view to increasing the resilience of Romania's economy in periods of distress and facilitating economic recovery.