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ROMANIAN ECONOMIC POLICY UNDER THE TRAP INNOCENCE

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1. The evolution of the main economic indicators in Romania during 1992-2009.
2. The forecast of the Romanian economic environment during 2010-2011.
3. Are we sure that IMF wants to reform the Romanian economy?
4. Conclusions.

Abstract

The project of a significant change in Romanian fiscal policy causes a lot of theoretical controversies and great movements of the labour unions.

The paper deals with the idea that Romania is far away from a "Greek situation" and the government fiscal measures are not the best ones.

We started with the analysis of the Romanian economy situation until 2009, in order to observe that it wasn't so bad compared to other Member States and the EU average.

The next step was to realise a comparative analysis of the economic forecast for Romania and the EU during 2010-2011.

A distinct part of the paper is to demonstrate the necessity to adopt other fiscal measures than those proposed by the government and to offer an alternative solution.

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1. Romania faced one of the greatest real GDP growth rate across the EU during 2004-2008. But this economic growth was followed by fiscal and external imbalance, which supported the present socio-economic situation in Romania, as well.

During 2006-2008, Romania achieved significant economic growth rates, greater than 6%, even than 7%. In 2009, the economic collapse led to a GDP's decrease by 7.1% (see Figure 1). Only five Member States had a decrease of their GDP greater than in Romania.

The economic growth in Romania was supported by consumption. During 1992-2008, the private consumption grew powerfully, as a result of the revenues' growth and consumption credits' facilities. In 2009, the situation became worst and the private consumption decreased by 10.5%. Only three other Member States had a worsen consumption rate in the same year. The public consumption had an insignificant growth rate during 1992-2005 and decreased in 2006 and 2009. In order to create an optimistic environment for the elections, the public consumption grew by 7.1% in 2008. As a result, it decreased to 0.8% in 2009. The government consumption expenditures change in 2009 was practically insignificant, even if the crisis was devastating.

The same evolution had the gross fixed capital formation, which achieved double-digit growth rates during 2006-2008. The crash of the investments in 2009 supported the gross fixed capital formation decrease by 25.3% and the equipment decrease by 32.7% as well. They were the result of the closing companies in Romania. They were some great companies' production capacities which were closed and thousands of SMEs, as well.

The Romanian foreign trade is chronically in the red. As a result, the imports' growth rates were greater than the exports' growth rates during 1992-2008. In 2009, Romania was forced to decrease the imports because it wasn't able to pay them. As a result, the imports decreased by 20.6% and the exports by 5.5% (see Figure 2).

This is why the net exports contribution to GDP growth was positive (7.3%) in 2009. It was for the first time when the net exports contribution to GDP growth was positive in Romania. On the other hand, the domestic demand and the inventories' contribution to GDP growth were negative in 2009.

The economic growth in Romania supported the decrease of the unemployment rate during 2006-2008. This rate grew by 6.9% in 2009 (see Figure 3). The unemployment rate grew as a result of the economic restructuration, especially in agriculture, steel industry and constructions. But the unemployment rate in Romania was smaller than the EU average.

Parallel to this, the compensation of employees/head grew very much during 1992-2008. This was doubled by a negative trend of the total employment in Romania, as in Figure 4. In this figure, we can observe that the total employment is approximately constant.

The problem appears when we analyse the labour productivity. During 1992-2008, the labour productivity growth rate was one of the greatest across the Member States. In 2009, this indicator marked a decrease by 6.2%, the highest decrease in the EU (see Figure 5).

The labour productivity decrease was accompanied by a dramatically breakdown of the total investment in 2009. During 1992-2008, the total investment growth rate had a positive trend, with a peak of 30.3% in 2007 (see Figure 6). Still in 2001, total investment growth rate was greater in Romania than in the EU until 2008. In 2009, the situation changed, because the decrease of the EU total investment rate was smaller than in Romania.

If we focus the analysis only on the public investment as percentage of GDP, we can observe that the Romanian ones are greater than the community ones during 2001-2009 (see Figure 7).

We have to use carefully this above mentioned information because the inflation rate in Romania was greater than in the EU during 1992-2009. The explosion of the inflation rate in Romania began in 1990 and continued to have two digit values until 2004. Even if this rate decreased by 5.6% in 2009, it remained high according to the EU average (see Figure 8). According to this figure, the prices explosion after 1990 was followed by a higher inflation rate in Romania than in the EU. As a result, the inflation rate was 4.6% greater in Romania than in the EU in 2009.

An important element of the analysis is the budget balance. The general government expenditures growth as a percentage of GDP was constant in Romania during 1992-2009. As a result, these expenditures achieved 40.4% of GDP in 2009. On the other hand, the general government revenues remained constant during the same period (approximately 32% of GDP). As a common conclusion, the general government expenditures as percentage of GDP are smaller in Romania than in the EU in 2009, while the general government revenues as percentage of GDP have the same evolution (see Figure 9).

At least, we analysed the gross debt as a percentage of GDP. This analysis leads us to a positive conclusion: Romania has a gross debt less than several other Member States, even in 2009 (see Figure 10).

According to the above analysis, the first important intermediary conclusion is that Romania had not a bad economic situation until 2008. Moreover, this situation was not too bad even in 2009.

2. In March 2010, the Romanian government approved the updated Convergence Program 2009-2010, which quantified the latest evolutions of the internal and international economic environment. The document was based on present legal framework and the 2010 budget provisions [1].

The convergence program maintains the undertaking of adopting euro on 1st of January 2015 and estimates an economic growth by 1.3% in 2010 and 3.7% in 2012. The inflation rate will decrease and the employment will grow, as well.

The average term economic strategy is focused on: the re-achievement of the economic growth, new jobs, public deficit adjustment, disinflation and population protection against the crisis' effects.

Other objectives are: the improvement of the fiscal policy performances on average term, the efficient use of the EU funds, the insurance of the public finances sustainability on long term, the public administration restructuration and efficiency, the implementation of the undertaking towards IMF, European Commission and World Bank.

Even if the Romanian government thinks about the euro adoption in 2015, the national currency will not be able to adhere to the exchange rate mechanism ERM II until 2012.

The Romanian government forecast a GDP growth rate by 1.3% in

2010, 2.4% in 2011 and 3.7% in 2011. The problem is that IMF forecast is for a GDP negative growth rate in 2010.

On the other hand, the budgetary deficit has to decrease to less than 3% of GDP until 2012, even if it was of 7.4% of GDP in 2009.

In 2010, the domestic demand will grow by 1.4%. Eurostat forecast talks about only 0.6% in 2010 and 4.1% in 2011. This growth will be based on the private consumption (+3.8%). Eurostat quantifies the same indicator by 0.7% in 2010 and 4.2% in 2011. The problem is that there are great disparities between the Romanian government optimistic forecasts, the Eurostat forecast and the IMF pessimistic forecasts, as well [2].

The evolution of the Romanian foreign trade will be supported by a greater foreign demand and a better domestic economic activity. The exports of goods and services will grow by 5.5% in 2010 and 6.5% in 2011. The contribution of the net exports to GDP growth will be of 0.3% in 2010 and -0.8% in 2011. As a result, the contribution of the trade deficit to GDP was -5.8% in 2009. The same contribution will achieve to -5.1% in 2010 and 2011.

The current account deficit will be maintained under the sustainable limits and will represent -4.4% of GDP in 2010 and -5.6% in 2011. The same indicator for the EU average will achieve -1.4% of GDP in 2010 and -1.3% of GDP in 2011.

The unemployment rate will grow spectacularly in 2010 and 2011, as a result of the latest economic measures engaged by the Romanian government to the IMF. As a result, the unemployment rate can achieve 10% in 2010.

At this moment, any forecast for the Romanian economy is very difficult. Nowadays, the Romanian economy is under chaos. The Romanian government doesn't have a real economic development strategy and it functions only in order to cover the current socio-economic problems.

On the other hand, the economic situation in Romania was not so bad at the beginning of 2010 and its evolution is better than the EU average during 2010-2011. We refer to general government gross debt as a percentage of GDP, general government balance, current account balance or unemployment rate (see Figures 11-12).

This is the second important intermediate conclusion, which supports the idea that Romania's economic situation is not the worst in the EU.

3. This is the situation of the Romanian economy. Within this framework, the Romanian government sends the message that the economy is down and we need a multiple financial support from IMF and EU. The main cause of this demand was the budgetary deficit caused by the budgetary expenditures. As a result, the Romanian government received 32.3 billion Euros from IMF and other financial institutions in 2009.

But only 9.4 billion Euros from this credit arrived to investment [3]. Romania made public investment three times less than the loans from IMF, EU and public bonds. IMF lent the Romanian government 9.16 billion Euros. 2.13 billion Euros were placed to the treasury and the rest to the national bank. The money from the national bank arrived indirectly to the Ministry of Finance, which borrowed massively from banks.

Moreover, the Romanian government chooses to scarify budget and retired persons. As a result, the public wages will be reduced by 25% and pensions and doles by 15%. These measures are the effect of the government incapacity to decrease the public expenditures and to use received money for investment, not for budgetary deficit financing.

In 2009, Romania received a foreign financial package of 19.95 billion Euros: 12.95 billion Euros from IMF, 5 billion Euros from EU, 1 billion Euros from the World Bank and 1 billion Euros from ERDB, EIB and IFC. If this money had been used in investment, it would have covered the budgetary deficit.

At the beginning of May 2010, an IMF official delegation came to Romania and signed an agreement with the Romanian government in order to decrease the budgetary deficit. The Romanian government reaction was to declare that it tries to protect the country from becoming a "new Greece case". As a result, the government considered that the options for it were to grow taxes or to decrease the budgetary expenditures.

The problem is that the revenues decrease and the inflation will hardly affect the economic growth and the tax collection. The Romanian government is focused on the deficit decrease from 9% of GDP to 6.8% in 2010.

According to the official data from 2009, the decrease by 15% of the pensions, unemployment benefits and other financial rights would imply a decrease of the expenditures from 12.7% of GDP to 10.8% (-1.9% of GDP).

In 2009, the salary envelope was of 9.2% of GDP and the effective paid salaries covered 5.6%. If the Romanian government cuts 25% of these salaries, the budgetary saving will be of 1.4%.

Practically, the total budgetary saving will achieve 3.3% of GDP (1.9%+1.4%). On the other hand, the government will receive lower budgetary revenues as a result of the consumption decrease.

Another governmental measure will be focused on pensions. But the greatest part of the pensions is very little in Romania. As a result, the replacement coefficient (according to present pension system and average life is only of 39%, not of 80% as the right estimation is.

Moreover, the number of budget labour grew from 900000 to 1500000 in the last five years. This is why the government wants to reduce the wages and the employment from this sector. The problem is that the forecast wages decrease by 25% will affect all budget labour categories in the same way, even if the number of professors and doctors didn't grow in the last five years. Practically, the Romanian government has a plan to decrease the budget labour, even if it is efficient or not.

Another intermediary conclusion is that the Romanian government doesn't have to cut the pensions or to apply the same decrease for all budget labour categories.

Moreover, the government has an ambitious plan to cut the budget labour, including professors and physicians. During 1997-2008, the number of physicians grew in Romania, but it was still low compared to other Member States. Practically, only Poland had a lower number of physicians per 100000 inhabitants than Romania in 2008 (see Figure 13).

A bad situation appears in connection to the hospital beds per 100000 inhabitants. Here we don't speak only by of number; we must speak about conditions and facilities. In Romania, almost all hospitals have no medicines, including surgery instruments. This is why the government decision to cut the number of physicians is aberrant.

The situation of the professors is not better. This is the result of the public expenditures on education as percentage of GDP in Romania (3.48%). This is less than the EU average (5.04%) and is greater only than in Luxemburg (3.41%) (see Figure 14).

The sustainable solution for the government is to cut the public expenditures, which covered 5.7% of GDP in 2009. These expenditures are quantified to 7 billion Euros.

Moreover, the government has to focus on the underground economy. The underground economy covers 25-40% of GDP in Greece, Italy, Spain, Romania and Bulgaria. On the other hand, the underground economy in the Central and Northern Member States covers only 5-15% of GDP. The Romanian Tax and Customs Administration declared that it stopped fiscal rip-offs which covered 1.6% of total underground economy in 2009. The immediate solution would be to support the implementation of the Romanian dedicated laws.

4. The Romanian government assumes to cut budget labour revenues, pensions and unemployment benefits. On the one hand, the first amendment is that it is not a deadline to these measures and the people are not informed about the dimension of their financial sufferance.

On the other hand, the government has taken any measure connected to the economic growth, which would be able to improve the tax collection and to create new jobs. Practically, the government has no solutions to this crisis.

What can we do? We propose the decrease the social contributions (45% nowadays) and a more careful taxation of the revenues. These measures will be able to decrease the unit labour cost and will support companies to invest more and to move their plants from abroad to Romania.

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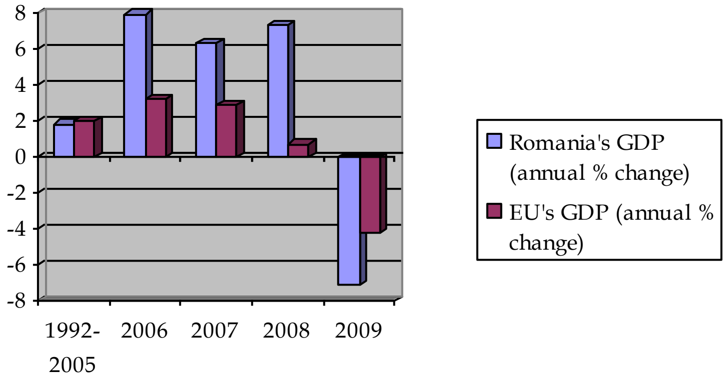

Figure no.1: The evolution of the Romania's GDP
Source: personal information processing according to European Commission, *European Economic Forecast,* Spring 2010, Brussels, p.134.

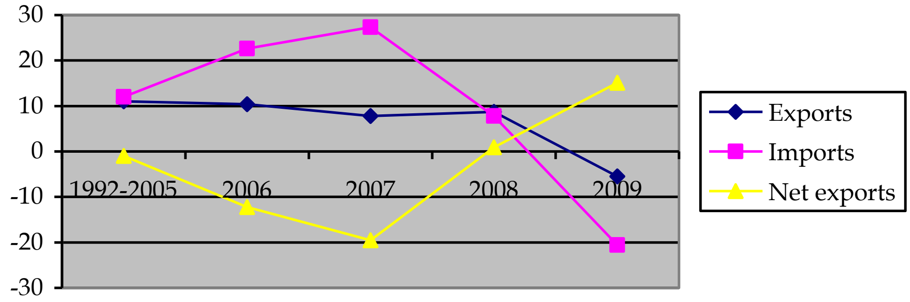

Figure no.2: The evolution of the Romania's foreign trade (%)
Source: personal information processing according to European Commission, *European Economic Forecast,* Spring 2010, Brussels, p.134.

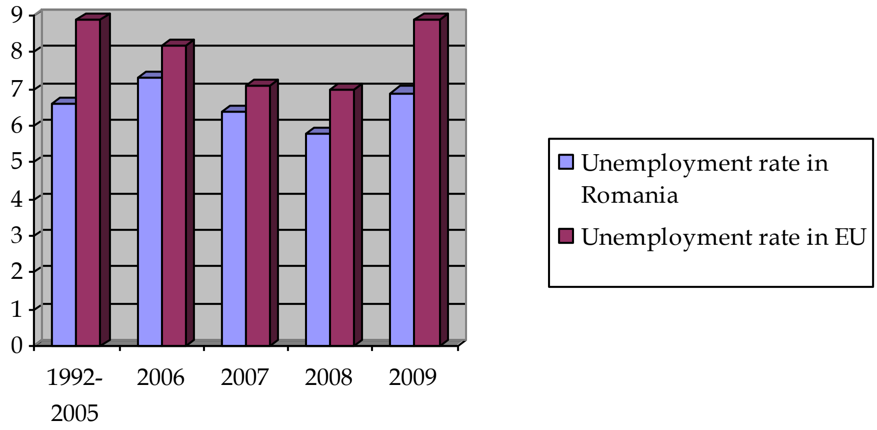

Figure no.3: The evolution of the unemployment rate (%)
Source: personal information processing according to European Commission, *European Economic Forecast,* Spring 2010, Brussels, p.134.

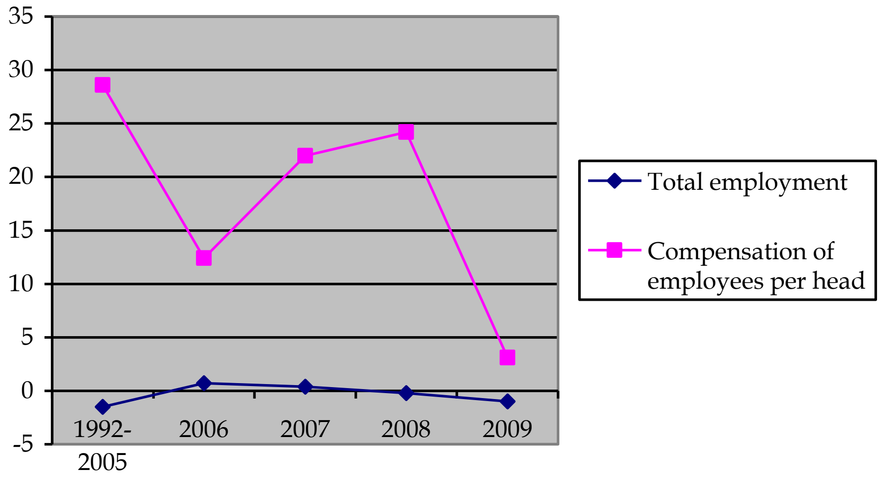

Figure no.4: The evolution of the total employment and compensation of employees (% of GDP)

Source: personal information processing according to European Commission, *European Economic Forecast,* Spring 2010, Brussels, p.192.

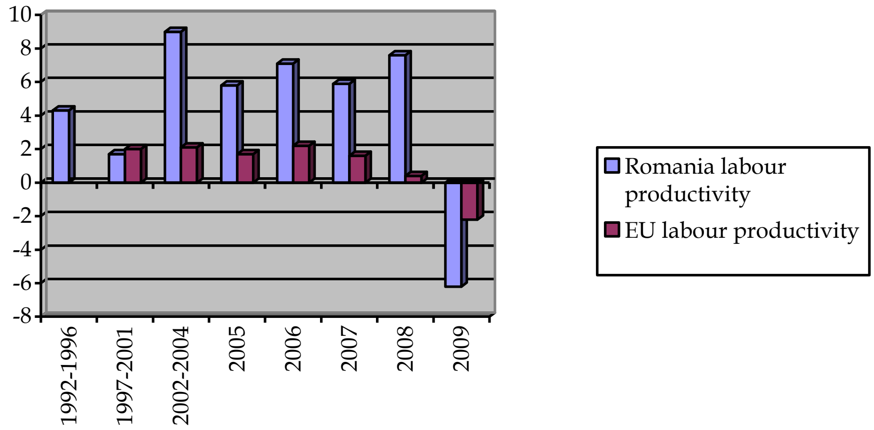

Figure no.5: The evolution of the labour productivity (%)
Source: personal information processing according to European Commission, *European Economic Forecast,* Spring 2010, Brussels, p.194.

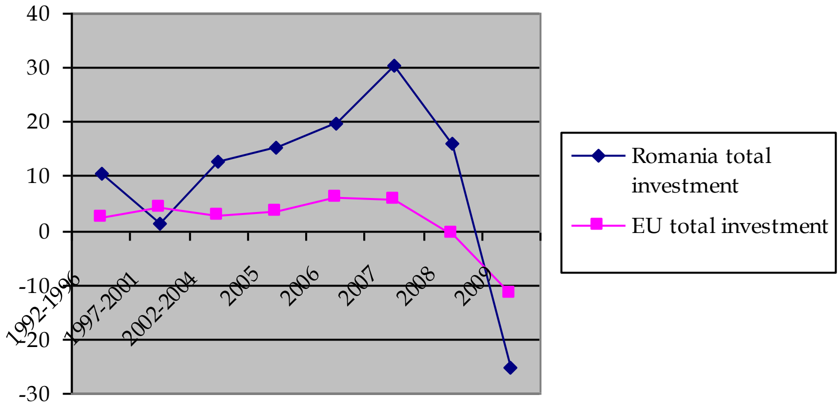

Figure no.6: The evolution of the total investment (% of GDP)
Source: personal information processing according to European Commission, *European Economic Forecast,* Spring 2010, Brussels, p.186.

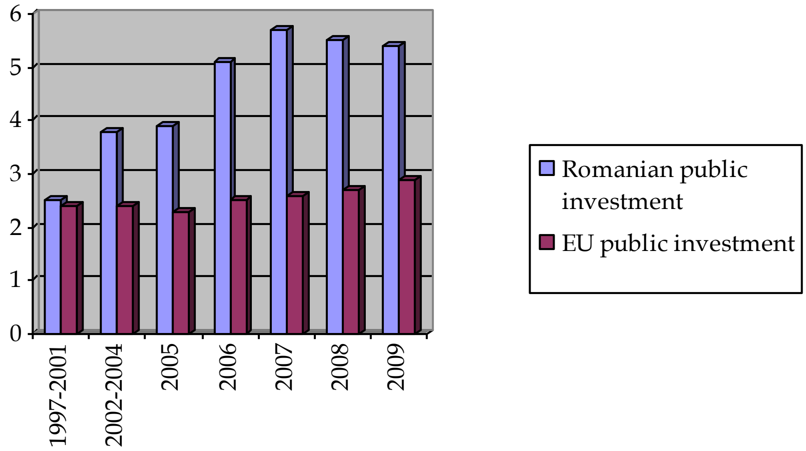

Figure no.7: The evolution of the public investment (% of GDP)

Source: personal information processing according to European Commission, *European Economic Forecast,* Spring 2010, Brussels, p.187.

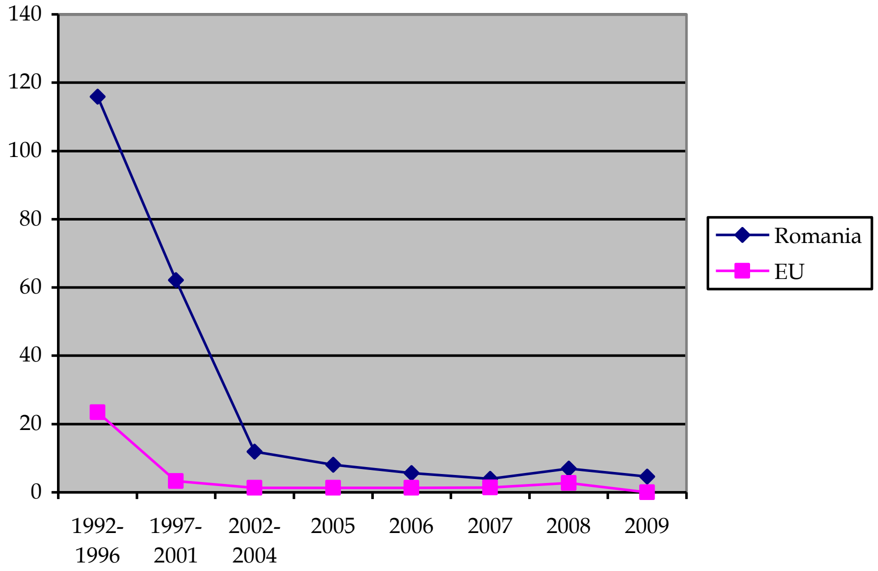

Figure no.8: The evolution of the inflation rate (%)
Source: personal information processing according to European Commission, *European Economic Forecast*, Spring 2010, Brussels, p.189.

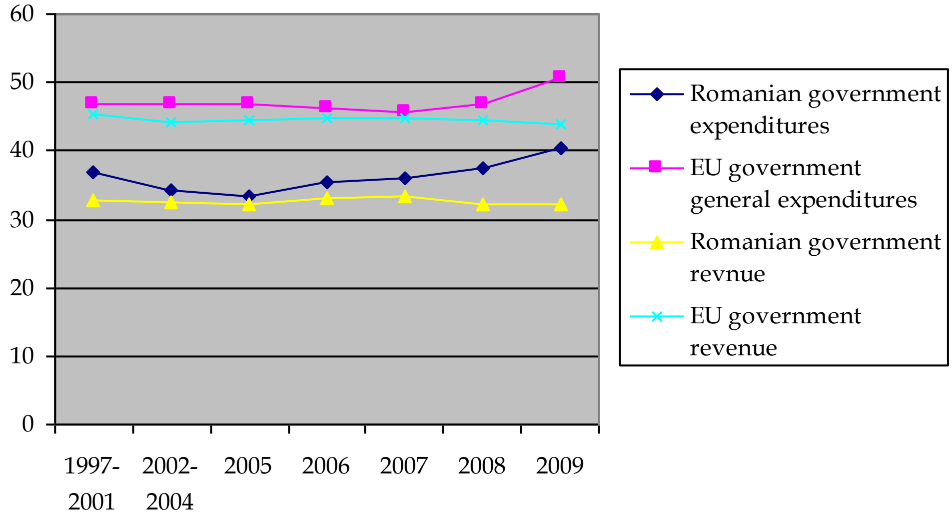

Figure no.9: The evolution of government expenditure and revenue (% of GDP)

Source: personal information processing according to European Commission, *European Economic Forecast,* Spring 2010, Brussels, p.199.

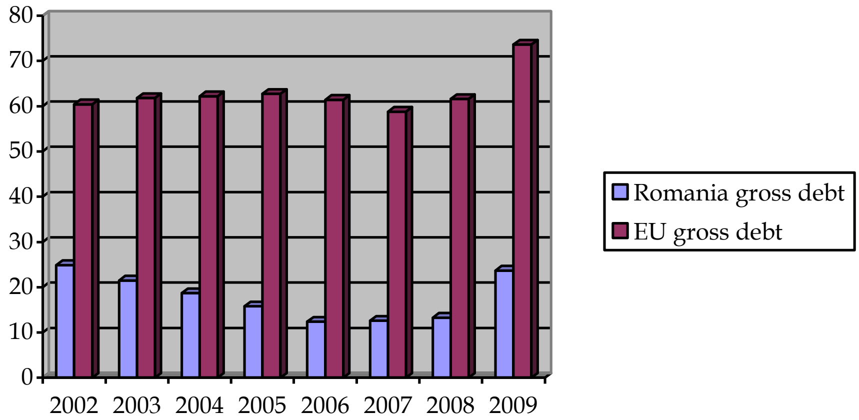

Figure no.10: The evolution of gross debt (% of GDP)

Source: personal information processing according to European Commission, *European Economic Forecast,* Spring 2010, Brussels, p.199.

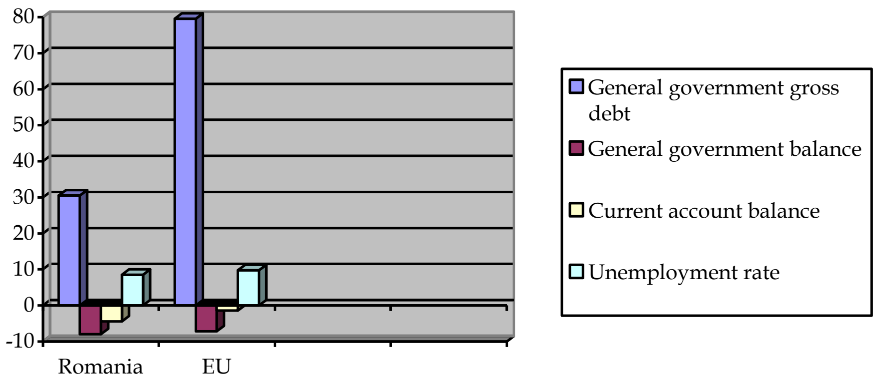

Figure no.11: The situation of main economic indicators in 2010 (% of GDP and %)

Source: personal information processing according to European Commission, *European Economic Forecast,* Spring 2010, Brussels, p.15.

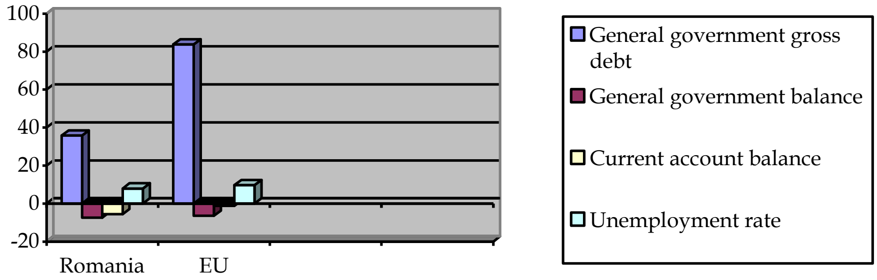

Figure no.12: The situation of main economic indicators in 2011 (% of GDP and %)

Source: personal information processing according to European Commission, *European Economic Forecast*, Spring 2010, Brussels, p.15.

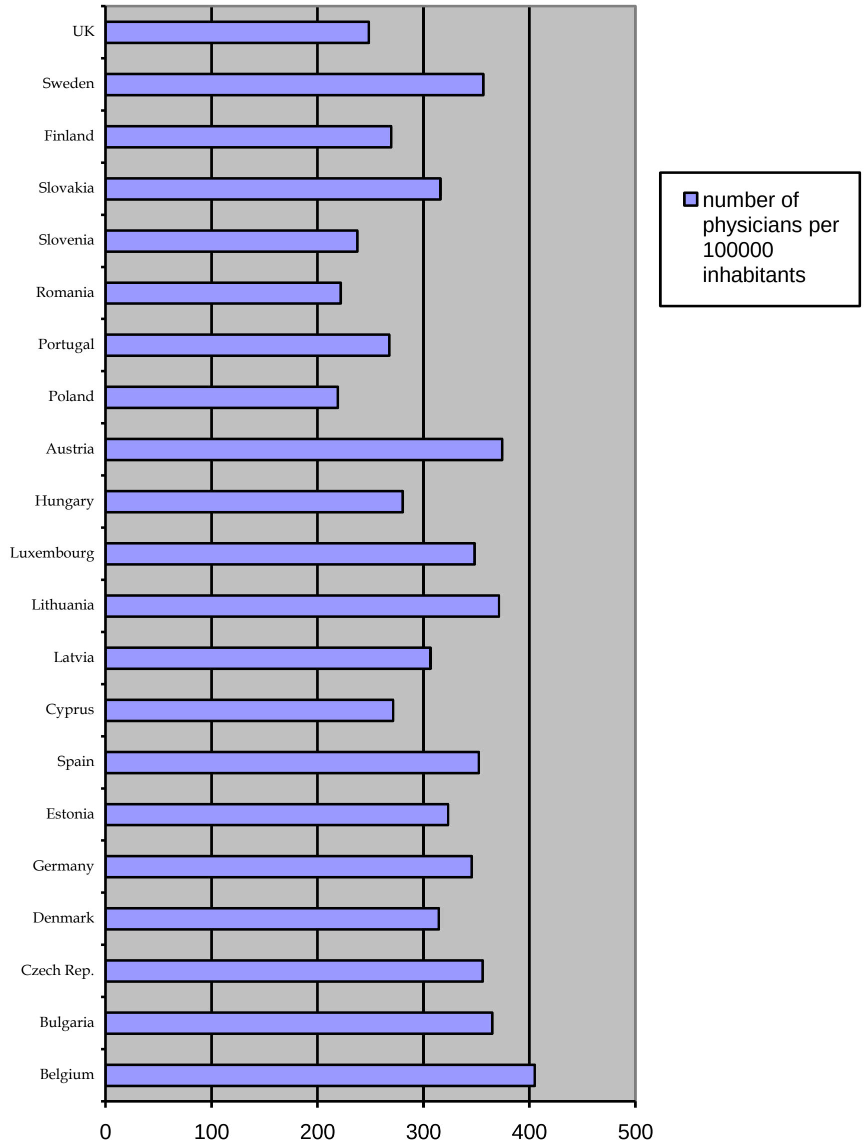

Figure no.13: Number of physicians per 100000 inhabitants
Source: personal information processing according to Eurostat.

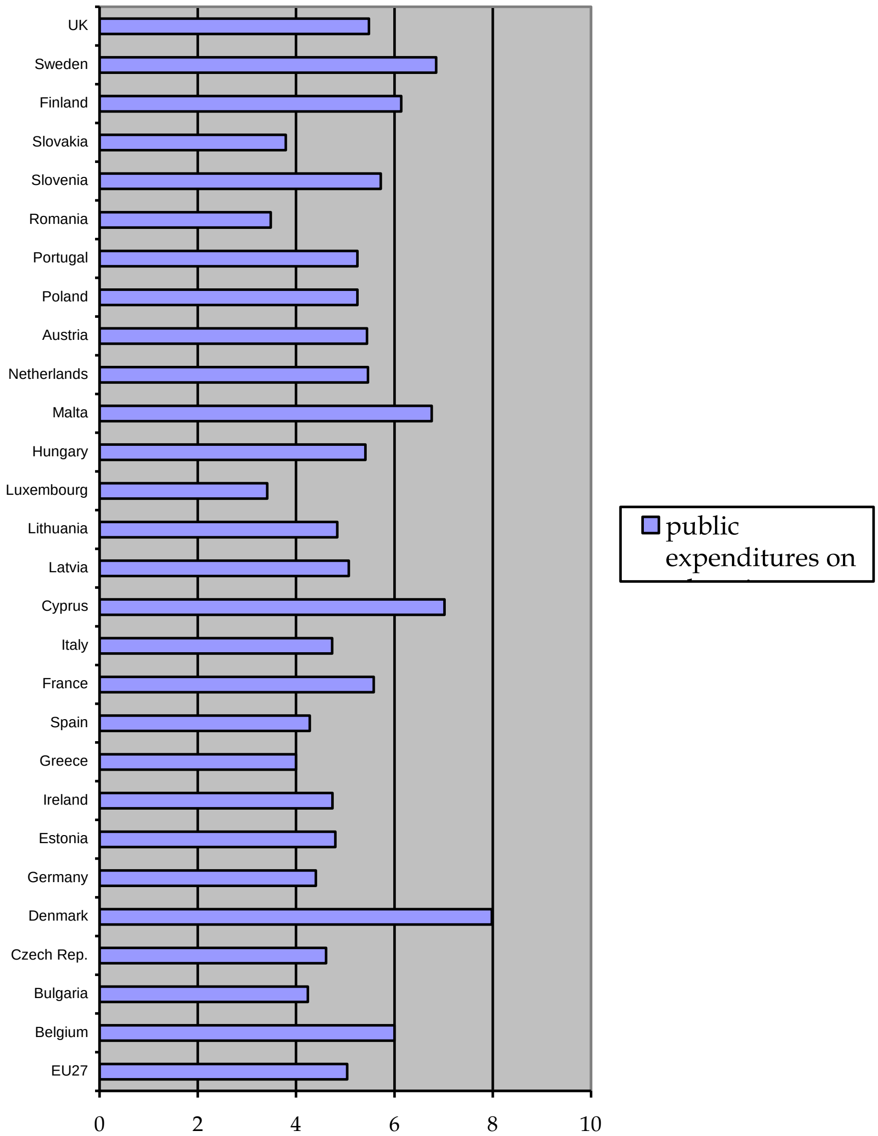

Figure no.14: Public expenditures on education as percent of GDP
Source: personal information processing according to Eurostat.