

ECONOMIC POLICIES IN ROMANIAN TRANSITION TOWARDS THE MARKET ECONOMY

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Abstract

This paper underlines several positive and negative aspects generated by the public economic policies from Romania after 1989, when the communist era ended. The transition to the market economy brought major changes to the decision process, coordinated and implemented by the public authorities with many errors and delays, but also with the acceptance of the idea of changing and improving.

First of all, it is analyzed the complexity of elaboration an economic policy, under the pressure of rapid establishment of a political democracy, but without creating an institutional framework and without an experience of the economic democracy. The most serious aspect is the perception of a corrupt capitalism despite the potential of a free market economy.

Secondly, the economic policy components have different approaches and evolutions.

The concept of an economic policy in Economic and Monetary Union is based on three pillars: monetary, fiscal and structural. In Romania, the monetary pillar was the fastest adopted, the fiscal one is still in discussion, and the structural problems are difficult to be changed.

The most difficult aspect is linked to the issues of planning and democracies, as long as there are not settled up clear and correct directions and objectives. This equates to a chaos, favorable to corruption and to internal and external speculators.

On the third row, it is interesting to analyze the merger of the interest specific to the public sector with the private sector one, subordinated finally to the interest of civil society. To all of these are added the effects of the European integration and globalization. The experience of Romania was deeply affected by the overlap between transition and world financial instability, getting to the complex problems of the current international crisis.

The conclusion of this article refers to the fact that the development and effectiveness of economic policies depends on a combination of dynamic rules, actions, resources, incentives and behaviors that involve the public sector, the private sector, the civil society, but on an area extended internationally.

Key Words: Romania, transition, economic policy, correlations.

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1. Introduction

This article reviews some aspects of the economic policy during the process of gradual replacement of <super centralized> and <super socialist> economy with a market economy in Romania in the period 1990-2010.

The research is based on official statistics regarding the evolution of economic and social indicators for a period of 20 years, but they are related to permanent institutional changes.

The interpretation of these developments was made from several points of view, starting from economic theory and practice, but also with appreciations of socio-human nature.

Although there are references and some transition models, still cannot talk about a valid solution for Romania, as other states.

The paper underlines several positive and negative aspects generated by the public economic policies from Romania after 1989 when the communist era ended. The transition to the market economy brought major changes to the decision process, coordinated and implemented by the public authorities with many errors and delays, but also with the acceptance of the idea of changing and improving.

To all of these are added the effects of the European integration and globalization. The experience of Romania was deeply affected by the overlap between transition and world financial instability, getting into the complex problems of the current international crisis.

Finally, there is the idea that *transition* is not an easy transition to a model economy, as the financial crisis has highlighted many weaknesses even in those economies considered developed, and the globalization has contributed to the emergence of the real risk of contagion.

Visible consequence of the turmoil from the largest economies is the emergence of a syndrome of continuous global monitoring of the regional or international bodies, together with increasingly frequent meetings of policy-makers in almost all countries, with the hope to establish more democratic and transparent the conclusions and some ways to follow. But every time they were not acceptable for all economies and the economic, social and environmental crises manifest even greater.

In fact, the effectiveness of economic policies depends on a combination of dynamic rules, actions, resources, incentives and behaviors that involve the public sector, the private sector, the civil society, but taking into consideration the international context, too.

Surely, in the article is visible a perception of the authors who have gone through this transition not as politicians or rich of the transition, but as the ordinary people.

2. Economic policy under the pressure of rapid establishment of a political democracy in Romania

The transition process in Romania started suddenly after Ceausescu in December 1989.

First of all, there was a perception that the political transition was abrupt and relatively easy, but the economic transition was much slower and difficult. In reality, it was considered that the slow change was due to a lack of <political will>. So, there is the complexity for elaboration an economic policy, under the pressure of rapid establishment of a political democracy, but without creating an institutional framework and without an experience of the economic democracy.

From another point of view, both economic and democratic reforms have focused on decentralizing, privatizing, and downsizing government to create capacity for providing basic services and critical public goods effectively and equitably, and manage the marketplace transparently. In same time, the globalization and economic liberalization are moving governments forcefully in this direction [1].

All these processes have been particularly difficult, because until 1990, Romania had one of the most rigid economies in Eastern Europe, characterized by the super centralization of the political, economic or social decisions, concomitant with almost total collective property. Therefore, the politicians but also the population and managers do not have any experience in the market economy practices.

As in other transition economies, in Romania there were two scenarios:

- radical and rapid transformation, <the cut of dog's tail suddenly>, but this scenario was unacceptable socially and unsustainable financially;
- gradual transformation was chosen because it was better tolerated by the population, but this solution meant to combine populist measures with slow and incomplete measures of conversion to a market economy.

For example, the first major error of Romanian policymakers in 1990 was the launch of remedies to give satisfaction to all categories of population.

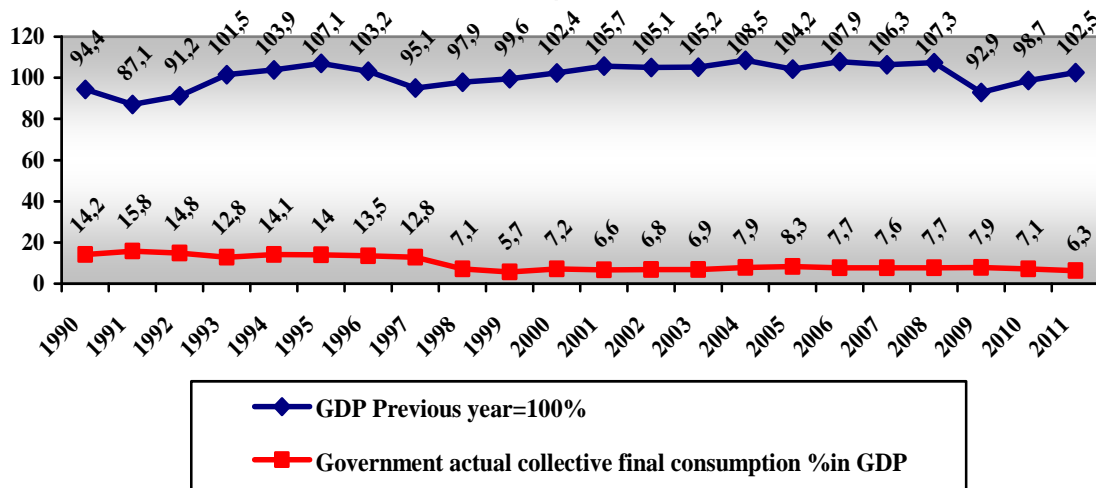
For 20 years, Romania oscillated between questionable actions and correct measures of social and economic policy, but the trend of change was maintained and totally there were still made progresses.

Specifically, it started institutional transformation on all levels, with the risk of mismatch and even mistakes in the economic and social legislation. The economic laws were approved sometimes in an unnatural order. For example, major privatizations took place without any clear legislation on public procurement.

It should be underlined that the process of improving the legislative and institutional framework in Romania was accelerated before and after EU accession in 2007. A lot of measures have been imposed under the slogan of alignment with European standards and requirements.

The institutional status in Romania can be reflected in some degree from statistical data about weight of the Government's actual collective final consumption in GDP, related also to the GDP evolution, as seen in Figure nr.1. Its evolution reflected both decentralization and moving expenses towards the private sector, but also a process of rationalization, especially under the impact of the crisis phenomenon.

Figure 1: Evolution of GDP and Government actual collective final consumption in GDP



Sources:

The National Institute of Statistics, *Romanian Yearbooks 1991-2011*.

The activity of national and local institutions is essential, but there is a contradiction between the role of institutions and the idea of bureaucracy, in fact the contradiction between efforts and effects of the national and local administration.

On the one hand, institutions must have better human resources and infrastructure, but all of these need money. Statistics indicate that budget of public institutions in Romania is directed predominant to staff costs and current expenses against the capital expenses, so the investment level is inappropriate.

On the other hand, the expansion of institutions and the existence of strict regulations are perceived as a growing bureaucracy. But the current crisis has highlighted the insufficient regulation and monitoring in various areas, including the financing one.

Overlapping the two plans of institutional development must reach that standard to enable service to both private and public interest while respecting the laws and economic, social, ecological, measures etc.

3. Transition vs corruption, inflation and unemployment

The most serious aspect is the perception of a corrupt capitalism despite the potential of a free market economy.

In essence, citizens believe that the institutions defending the law, but there is a lack of trust in the state institutions.

In Romania, neither the transition, nor the EU accession has managed to restrain the capacity of the government to distribute benefits in a particular manner and there is a debate about four basic categories:

- public jobs, as the public sector is extremely politicized and each winning party fills with his own people not only the political jobs but many civil servant offices as well;
- public spending, for instance procurement, but also preferential bailouts, subsidies, government transfers to regional and local branches, loans from state banks;
- preferential concessions and privatizations from former state property;
- market advantages in the form of preferential regulation.[4]

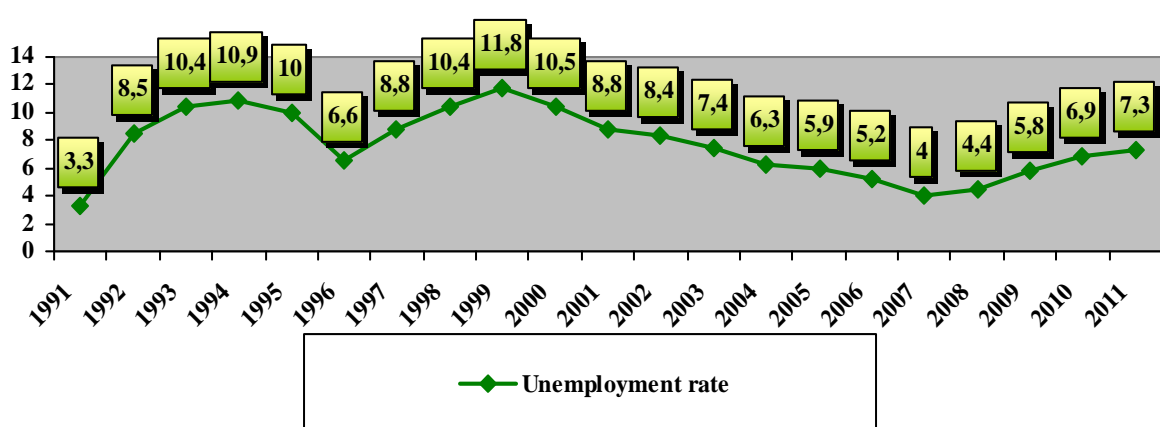
In reality, the market economy can not impose administrative, political, economic or social strategy, but practically it is done by arbitration between different types of objectives and instruments that seek guidance "ex ante" using three systems:

- an information system, - through mass media, communication infrastructure, especially IT;
- a system of incitement, - through legislation, promotion, taxation,
- a system of prohibition, - through law, institutions, feed back to laws and improving measures that combat and restrict black or gray market.

The massive transfer of legislation prompted by EU did not yield the expected results, but there is a trend to reduce the distance between the <real country> and the <legal country>.

The transition is associated with the phenomena of unemployment (figure 2) and inflation (figure 3), and statistics indicate that these problems were difficult to be managed. In fact, these problems are difficult to manage by all economies and the financial crisis has generated, on the one hand, a series of measures that aimed the financial stability, but on the other hand, unemployment increased and additional austerity measures appeared.

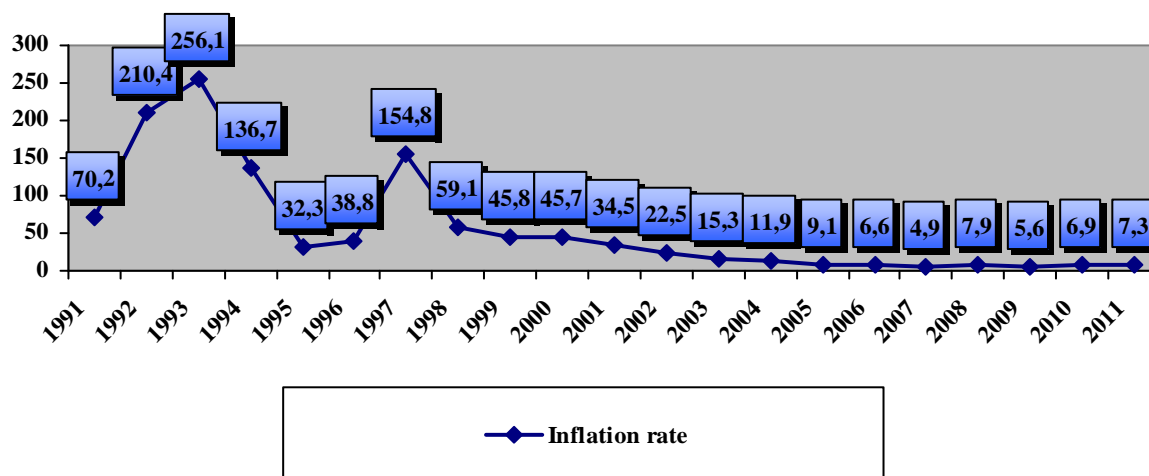
Figure 2: Evolution of unemployment rate (1991-2011)



Source: The National Institute of Statistics, *Romanian Yearbooks* 1991-2011.

Often, the inflation peaks are generated by election years, while taking many populist measures, which then must be corrected (figure 3).

Figure 3. Evolution of inflation rate (1991-2011)



Source: The National Institute of Statistics, *Romanian Yearbooks 1991-2011*.

4. Monetary policy - the engine of economic policies in Romania's transition to market economy

The concept of economic policy in Economic and Monetary Union are based on three pillars: monetary, fiscal and structural. The statistics from EU indicate that these components have different approaches and evolutions, thus even at present there are not models that can be applied to entire EU area.

The EU experience confirms that the economy is primarily driven discreetly, but with greater efficiency and speed through <money>, in fact by monetary policy measures and the creation of appropriate institutions. The EU has followed a strategy for creating and functioning of Euro, so that monetary policy can be considered an engine of management and control for other problems in all EU states, even in the states that have not adopted the single currency. As consequence, Romania and other countries are concerned about the economic, financial and social convergence allowing the transition to Euro.

In Romania, the monetary pillar was the fastest adopted, and the monetary statistics indicate a totally alignment to the terminology and practices of European monetary union.

Monetary policy is accompanied by financial stability, and the National Bank of Romania (NBR) and the Government took strong measures to safeguard the stability of financial markets, banks and weathered the stress well. Thus, The National Bank of Romania adopted some measures in order to promote the prices and financial stability such as [13]:

- transition to positive real interest;
- full liberalization of current account;
- start the restructuring of the banking system;
- liberalization of the capital account;
- adoption of inflation targeting strategy.

Now, the contagion effect in the financial sector is being mitigated in several ways, because Greek banks account for about a sixth of the assets in Romania's banking system.

But, the fiscal one is still in discussion, and the structural problems are difficult to be changed, because these depend on two main aspects.

The first aspect is the purity of economic policy (the extent to which economic aspects are taken into consideration, without political or social interference). In this regard, the parliament should be based both on high competence specialized committees, and on the attitude of the entire parliament, which must discern between political and business interests.

But the transition was seriously affected by political interference. For example, the large number of emergency ordinance shows some serious decision issues under the pressure of political interests, but on the other side, is about the weak competence of politicians in Romania, many of them having no knowledge of modern principles of corporate governance.

The degree of articulation between state and market has a great influence and this is reflected in compliance of those rational expectations of the economic agents, as measure of economic policy effectiveness. Although this is a fine mechanism it is difficult to be achieved even in traditional market economies, however, there must be followed some indicators, such as the relationship between public and private investments, financial intermediation and personal investments.

5. Personal finance and investment - the final result of transition

A person or a family interacts with money and with a series of real estate, movable or financial assets and together these represent a person property. Personal investments in essence refer to financial assets and non financial assets. More specifically there are: equities; fixed income; cash/deposits; real estate; alternative investments (structured products, hedge funds, derivatives, commodities, venture capital).

Personal finances and investments are, on one hand, an aspect of privacy of an individual (or family), but on the other hand, there is a feedback relationship between personal decisions and all economic and social system. The signals in the economic and political environment, but also the way they are perceived can engage population to ascending economic evolutions or by contrary can create bottlenecks and panic.

According to a report by Credit Suisse banking group [9], the average wealth of Romanian adult increased more than 4 times in the past decade, from 3,840 dollars per person in 2000 to 17,599 dollars in 2011, which places our country on 59 ranks from 160 countries.

The structure shows that Romanians continue to have a real estate fortune twice against the financial assets, and furthermore, their financial debt is related mostly to real estate loans.

Romania still has a poor population, so that our country's adult population is 0.37% from the total number of adults worldwide, but the Romanian property is only 0.13% of the world total. In addition, almost one quarter of Romania's adult population (24.5% of total) has an average wealth under 1,000\$, 44% are between 1,000 \$ and 10,000\$, 29.4% have between 10,000 and 100,000 dollars and only 2.1% of residents have an average wealth of 100,000\$.

Many theoreticians consider that economic progress is reflected by the evolution of rich wealth. In Romania, there were 16,528 millionaires in dollars in 2011, of which two are billionaires, which places Romania on a 47th rank in the world by number of rich people, as shown in the report of Credit Suisse banking group.

The crisis has led to increased capital (equities), the investment in fixed income instruments, but safer (bonds) and cash money. Real estate declined primarily due to falling prices.

Romania's population was touched by housing bubble, but is sensitive to other developments in the stock market and especially the currency market.

6. Planning and democracy

In transition, the most difficult aspect is linked to the issues of planning and democracy, as long as there is not settled up clear and correct directions and objectives. This equates to a chaos, favorable to corruption and to internal and external speculators.

The Romanians suffered greatly due to more extensive planning, which began with the establishment of economic targets through five years plans and ended with the establishment of

a total of 4 children for every family. Therefore, since 1990 the planning process has become taboo, considering that the market economy needs no plan.

Ideally, a new society could only be based on direct democracy and economic democracy and that may be defined as an economic structure and a process which, through direct citizen participation in the economic decision-taking and decision-implementing process, secures an equal distribution of economic power among citizens. But, in our time, the market economy system is dominated by the growth ideology and personal greed, and there is the idea of automatic functioning of the system itself. From another point of view, the essence of today's economic crisis lies in the hugely uneven control over incomes and productive resources that characterizes the world countries.[3]

Planning is important and useful process for a modern society, being a branch of economic science based on calculations and econometric models more and more complex.

Although not supported politically, the planning process took place directly through the development of annual and after this, bi-annual plans, as was the plan 2004-2006. Planning was done by developing national and local budgets, through the monetary and fiscal policy measures. Often, in transition these provisions have been established with a long delay and many corrections during the year.

The prediction and multi-annual planning was enforced by the EU.

First, accession to the EU is based on National Development Plan –NDP 2007-2013 [11], prepared by Romanian Government in December 2005 with six national development priorities:

- Increasing economic competitiveness and developing an economy based on knowledge;
- Developing and modernizing transport infrastructure;
- Protecting and improving the quality of the environment;
- Developing human resources, promoting employment and social inclusion and strengthening administrative capacity;
- Developing rural economy and increasing productivity in the farming sector;
- Diminishing development disparities between country regions.

After joining the EU in 2007, Romania has established a number of investment projects according to EU funding, which also set certain targets for economic and social development.

Secondly, in Romania, the financial difficulties gave rise to a series of reforms, with support from the international financial institutions in health, education, the financial sector, public financial management (such as treasury and debt management, macro forecasting capacity, strategic prioritization in the budget process), public administration, social insurance and social assistance. Some of these reforms address short-term responses to the crisis, while others are anchored in a coherent longer-term strategy.

For example, the recent sectorial development, developed by the World Bank for Romanian crisis refers to four areas which are presented in the table nr.1. [15]:

Table 1: Areas and priorities for Romanian economy

<i>Areas</i>	<i>Sustainable Development</i>	<i>Human Development</i>	<i>Public Sector Reform</i>	<i>Private sector development</i>
<i>Priorities</i>	i) Agriculture (ii) Environment (iii) Infrastructure	(i) Health (ii) Education (iii) Poverty and Social Protection	(i) Reform of the Public Administration (ii) Governance/ Institutional Development	(i) Reform of the Public Administration (ii) Governance/ Institutional Development

However, the transition in Romania was more prolonged and many resources were wasted due to lack of long term planning strategies. This fact was extended to attract structural funds, because there were no institutions and best practices to launch projects of real interest for Romania, but in accordance with the EU's cohesion strategy.

7. Public and private sector in transition

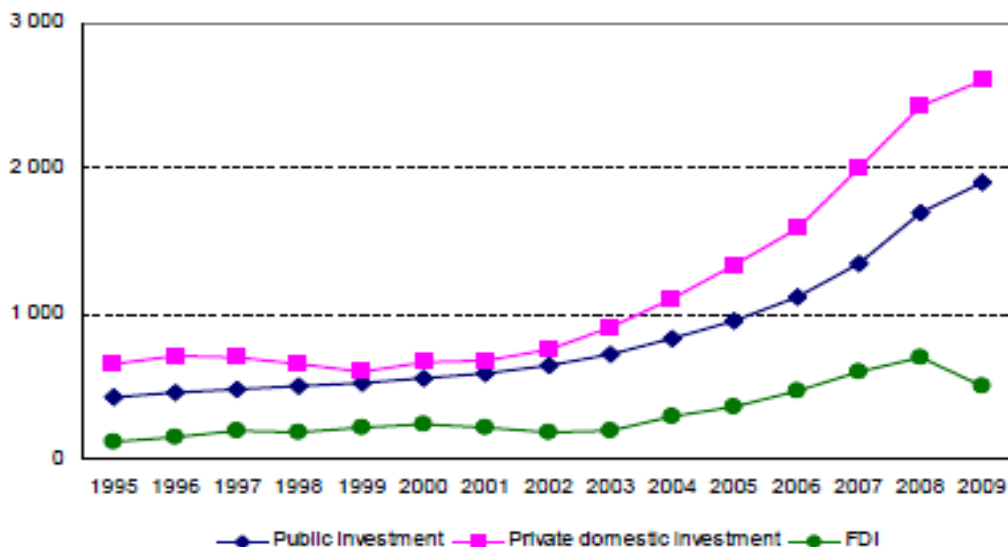
Another problem of transition is an analysis regarding the merger of the interest specific the public sector with the private sector one, subordinated finally to the interest of civil society.

At the beginning of transition following trends emerged:

- public sector received the most investment, although many units with state capital were then privatized or have been closed;
- the private sector did not benefit by consistent financial support and it was not rigorous included in the development plans;
- foreign investment were considered essential and had many facilities;
- there was not a public private partnership.

In all transition economies, the report was clearly in favor of public investment, as is shown in figure 4.

Figure 4: Public and private investment in developing and transition economies, 1995-2009 [8] - (Billions USA Dollars)



Classically, in all states there are developed and implemented public investment projects considered so because they are viewed as follows:

- on the one hand, they serve to the general public;
- on the other hand, they are financed by public money.

Transition governments forced Romania to solve two problems.

It was necessary the regulation of the public procurement. Public procurement is one of the main feeding sources for the ongoing process of economic and social development of Member States, exceeding 16% of the average GDP in the European Union. Although there are many critics, Romania has made progress in the public procurement activity, especially after EU accession. Thus, the share of public procurement increased to 10-12% in total GDP by electronic

system of public procurement (ESPP), which is considered the most transparent, as shown in Table 2.

Table 2: Public procurement to ensure transparency by ESPP relative to GDP [10]

	2007	2008	2009	2010	2011
GDP - billion lei	404.7	503.9	491.3	513.6	578.6
The total value of procurement published in the ESPP - billion lei	22.35	53.7	62.5	46.3	62.3
%	5.5	10.7	12.7	9.0	10.77

Also, the share of open public procurement increased and they are regarded as more transparent and with equal opportunity for participants.

The second problem is financing through public-private partnership (PPP). Practically any type of public investment should be private, with the condition that there are no suspicion of subjectivism, corruption and inefficiency. Romania has established a law for PPP, but some provisions are contested; the practice shows quite a reduced number of investment projects made by PPP. In the EU there is a standard partnership system, even if it is modeled in recent years more and more under the Anglo-Saxon influence in function of two major objectives: employment and local development to ensure economic and social cohesion, especially environmental protection.

PPP involves complicated arrangements that require a great deal of expertise and flexibility.

In emerging markets, international partners must address not only the project risk and country risk, but also the risks posed by the lack of local managerial skills, inadequacy of institutions, corruption, lack of transparency, and others [5].

8. Transition on the Globalization and Crisis

To all of these transition problems are added the effects of the European integration and globalization.

These phenomena should provide an infusion of foreign capital and best practices from the experience of developed countries, the emerging states offering several advantages for foreign investors.

Evolution of foreign investment as the structural funds show an increase until the crisis, accelerating the transition process, but they are reduced or even relocate during the crisis, with the same negative effects.

The experience of Romania was deeply affected by the overlap between transition and world financial instability, getting to the complex problems of the current international crisis.

Less developed financial market in Romania has contradictory effects:

- does not attract capital stock capitalization and evolution;
- no risk of massive and rapid departures of capital from banks.

Romania must notify various situations, given that foreign capital flows have profound social and political implications, but appreciated as contradictory, because it generates both positive effects (technical, economic, social progress, and best practices), and negative effects (loss of total control over economic policy, export of financial crisis, rising unemployment, the gap between wages and profits, expanding black economy, etc.)

After 20 years of transition, a World Bank report analyzed the weak points of Romania facing the globalization and crisis:

- high share of state loans with short maturity, 60% of total debt, or about 8 billion Euros;
- 80% of banking assets held by EU banks. The high percentage makes Romania vulnerable to the credit lines of the bank from other countries. Share of the foreign bank assets in Hungary and Poland is below 40%.

- high ratio of report loans/deposits, respectively 127%, less than Latvia (240%) and more than Russia (121%).
- high dependence of EU exports, respectively 75% from total exports;
- considerable degradation of Credit Default Swap index (CDS), with 231 basis points in comparison with 114 points average growth recorded by the developing countries. Index is high due because the increased dependence of local subsidiaries by the EU parent banks.

9. Conclusions

Modern economic policy aims to get continuity in balance, meaning that should be avoided the big "break", the major discontinuities. But the transition is just a radical change and evolutions in this period confirms once more that the rapid and radical discontinuities create the danger of serious disturbances, difficult to be solved as time and required resources.

Despite the lack of basic institutions 20 years ago, Romania has made considerable progress since then in developing institutions compatible with a market economy. But the country lagged behind other Central and Eastern European countries in policy reform and institutional development, until the prospect of EU membership became a driving force for reform and modernization.

In recent years, in all countries, not only in the countries considered in transitions, the crisis phenomena have forced major changes. Many people are asking how to "fix" capitalism without affecting the core system of market economy based on creation, development and democracy. Free economy needs a public sector, regulations that take into account the imperfections of markets, social and environmental imperatives. But these solutions are at a first hand analysis by institutions and into the depth are about the quality of governing in a democracy [2]. To these must be added the influence of globalization, such as at the decision table are placed nations with different degrees of development, but also with different cultures.

The result of the government is a modern economic policy that changes continuously through a system of arbitration, while solving the problems of aggregate demand (total), aggregate supply (total) and the problems of unemployment and inflation, in order to achieve a normal economic growth. The resultant should be measured through a normal rate of growth.

The current crisis has created a transition phenomenon of the entire world and the Eastern European experience shows that although there is not a model of change, yet in history there are many theories and practices of economics, political, social sciences that should be well known and used by policy makers able to convince the population of their good intentions, but also of their skills. Otherwise, democracy, in the context of general discontent and a background of education or information deficiencies can propel dangerous people and ideas. <Sleep of reason can born monsters>.

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