

## SOME THEORETICAL AND PRACTICAL LESSONS TO BE LEARNT FROM THE ECONOMIC CRISIS CHALLENGES IN ROMANIA

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### Abstract

*The present article has as a main theme the complex mechanism regarding the evolution of world global economy crisis started back in 2008, and its present influence at the level of Romanian economy.*

*This paper herein will analyze, in short, a few of the theoretical, methodological, practical and implementation challenges brought about by the crisis in Romania, as well as the likely ways to prevent, mitigate impacts and resist to its shocks or to go back to the path of a sustainable economic growth.*

**Keywords:** *economic crisis, economic analyze, economic recovery process*

**JEL Classification:** E20, H12, G01

### Introduction

In contrast to the previous great depression, the current economic and financial crisis started in 2008 in the financial-banking sector due to the bankruptcy of Lehman Brothers Bank in the USA, and has had a very quick spill over impact at both national and international levels. Thus, in 2009, its **systemic nature** was evident **at an international scale**, where most countries were affected, directly or indirectly, by strong recession phenomena, imbalance and turbulent times.

Despite of a real and correct forecast based on pertinent causal analyses and accompanied by appropriate plans of measures and actions at all levels, the very-much-talked-about issue of exiting the crisis, also during the G-20 Summit meetings, has recently worsened due to the **spearhead of the sovereign debts crisis**, under the threat of a new crisis looming into the air; and this happens when a part of the world economy seemed to have partially recovered in 2010 and started going on a narrow but sure upwards road.

In September 2008, some decision-making factors in Romania were thinking that our economy would not be directly impacted by the crisis and that the decision to make a loan from the IMF, EU and World Bank in the amount of EUR 20 bns. was only a precautionary measure (the so-called 'protection umbrella' or 'safety belt'); later, such opinions, reassuring and comforting for the large public – uninformed – proved to be totally unrealistic!

The crisis in Romania has been even stronger and longer than in the other countries. Not even today, in 2012, the economy is not very promising, as the

specialists see the threat of the second wave of crisis, while many of the EURO zone countries are in danger of having the rating lowered from AAA, due to the pressure coming from the sovereign debts.

For the scientific economic research in general and in Romania, as a particular case, the current economic and financial crisis, firstly emerged in the financial-banking and then economic areas, followed by political and social circles, has triggered a series of new interpretations, paradigms and perspectives of economic thought and doctrines in terms of the causes, effects, fight and prevention against the systemic risk that economic phenomena and processes contain in a latent manner.

### **1. The fundamental cause of crisis – a deeper divide between the real and nominal economy**

Without the least intention to enter a scholastic dispute regarding the unequivocal or bi-unequivocal (!) relationships between the **real and nominal economy**, the top priority or importance of one or the other, I truly consider that the two facets of the same economic phenomenon should be linked in a **complex nexus of systemic and intrinsic connection**, where one cannot efficiently operate without the other; in other words, a consistent synchrony, relationship and compatibility in dynamics of the two interdependent manifestation types of economy represents a sine-qua-non requirement of the balance, sustainability, efficiency and profitability of the whole economic system at all levels of aggregation and operation.

As far as the literature in review is concerned, the expansion of the financial-banking system, with no support in the real economy and relying on a **pseudo-innovation of many of the financial-banking products**, in compliance with the desire and extreme greed, has made that the speculative vector, acceptable only within certain limits as a ‘must’ factor of economic growth, to have outgrown such limits long time ago and become ‘toxic’, thus affecting entire sectors and economies; likewise, it has accrued, obscurely and cynically, a major potential of imbalance, tensions and financial bubbles, via credits without warranties and coverage, subprime credits, by apparently favorable multiplications of the transactions on the secondary capital market and predominantly speculative financial placements (hedging, endorsements, etc.).

Certain famous **rating agencies** have also contributed to the above circumstances, unable to realistically evaluate and timely warn about the critical economic and financial situation of many banks and systemic institutions or of a major importance for the proper course of the national and international economies.

I truly consider that the momentum of the nominal, financial and monetary economy, with no direct and efficient support in the real economy, will always trigger phenomena of destabilization in economy and society, toxic spill over effects by generating negative externalities (external marginal costs) or diseconomies. The corrective taxes Pigou, made available by implementing the **polluter pays principle**, up to the integral compensation of the induced prejudice

to third parties, may constitute one of the remedies, similar with the Pigou mechanism that was initiated for and implemented in the environment economy. Unfortunately, the ‘polluters’ (guilty ones) in the nominal economy, whom have started the crisis, are hard to identify, let alone the high level of difficulty to establish the damage in time and space of their negative externalities, at both national and international scales. For this reason and for others targeting their economic and political force, they will not have to bear the crisis costs, but rather the taxpayer ‘at large’.

Up to now, an effective solution worldwide (and not only) seems to be a ‘goal’ that the suggested mix of economic policies, instruments and mechanisms of fighting and recovery has only managed to brush it lightly – in theory, methodology and intention – based on restructuring and partial debts exemption, budget austerity measures (transparent and careful), a higher efficiency of the systemic risk management, etc.

All these measures, mostly known and implemented, have not represented an antidote against crisis recurrence and recessions but they are rather ‘palliative’, which gave away when rare, difficult to forecast problems occurred (i.e. economic and financial crisis, earthquakes, flooding, epidemic diseases or other extreme meteorological phenomena), considered ‘black swans’.<sup>1</sup>

The pragmatic-applied challenges of solving the present crisis target the financial stability funds at the EU level and EURO zone, the financial aid from states, granted to the banks in difficulty, a series of micro and macro prudential measures of the banking systems, consolidation of the supervision means, control and monitoring of the financial sector inevitably generate a series of controversies related to the **losers and winners** of crisis, the operational behavior of implementing business ethics, responsibility and involvement of the rich ones, etc.

In my opinion, such measures may be completed with others targeting the stock and extra stock markets, mainly by the stimulation of the **initial public offerings** (IPO), a market which is very low in Romania.

The initial public offerings make a direct connection between the real and the nominal markets – it is not about the predominance of the secondary capital market that relies on speculations ‘à la hausse’ and ‘à la baisse’, triggering transactions of the ‘securities’, with no positive effect upon increasing the real added value, but an impact on the nominal market that bring about higher inflationist pressure, beyond certain acceptable limits, necessary and sufficient, for a sustainable economic growth.

There cannot exist a ‘prosperous’ secondary market of capital in Romania with a very weak primary market, episodic, non-existent, as in other countries with an emergent or developing economy.

The volatility of the capital market, mainly the secondary one, was obviously marked by the activity crash of world stocks, including BVB (Bucharest Stock

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<sup>1</sup> See Taleb Nassim Nicholas (2007/2010), *The Black Swan. The Impact of the Highly Improbable*, New York, Ransom House and Penguin, completed with the essay ‘On Robustness and Fragility’ in second edition in 2010.

Exchange) in 2009-2011; the stock crash was so strong in Romania and other countries that the stock operation was suspended for certain intervals of time.

The issue of the secondary stock market, the speculative securities, is not a new one. The Romanian economists have been analyzing their negative impact upon economy and society since the 19<sup>th</sup> century – Mihai Eminescu, the great poet, was one of them. His ability to look into the economic, social and forecasting phenomena has been confirmed by famous names of the Romanian economic science, namely Mihail Manoilescu. M. Eminescu<sup>2</sup> was not at all against the primary capital markets (initial public offerings – IPO), which relied on ,naturally made-up’ prices and are proportionate with the ‘enterprise output’. On the other hand, he considered that ,the stock transactions on the secondary capital market are not lucrative but only for the people who hold important money funds and can influence the stock assessment to value as much as they want, even though the rate they impose is found in a total contradiction with the company economic condition (whose stocks are the object of transactions). Most frequently, when losses occur, this situation leaves their financial force intact or almost untouched<sup>3</sup>.

Now, in the context of the systemic crisis, a large part of the financial and banking system and of the secondary capital market had lost contact with the real economy and was expanding in virtue of an inertia of **undue enrichment** in the nominal economic world, eager to become rich quickly via artificial securities.

Currently, it is confirmed at large scale the Eminescu’s statement that the stock market is as much interested in spreading the taste for gaming, quick money at someone else expense, dirty transactions, contempt for the intrinsic value of business. The speculative stock activities withdraw the money from real merchandise transactions, from companies making real goods to throw them into future companies with a zero production<sup>4</sup>.

I consider that one of the measures required for recovering the economic situation is **to reduce the volume of speculative transactions on the financial capital market**, of the securities, complying with rigorously set criteria. Thus, these measures may target the discontinuation of the stock activity on the secondary market for a certain period of time, including by implementing certain limitations or forbidding the ‘**naked short-selling**’ transactions for an undetermined time, at some companies in the banking and financial sector.

The specialists in Germany, for instance, bring arguments and put pressure to **ban at the European level** the ‘naked short-selling’ share transactions, governmental shares and the ‘swap’ contracts on credit risk. For the short-selling operations, a share loan will take place, where the investors sell and hope that their prices will lower so that they will be able to purchase them at a smaller price and return them to the ones they borrowed them from. Practically, for this transaction, the investor bids on a lower share price. Even though many specialists believe that

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<sup>2</sup> Eminescu M., „Creditul mobilier și jocul de bursă”, *Opere*, vol. XII, Critical edition by Perpessicius, Romanian Academy Publishing House, Bucharest, 1986, p. 276-283.

<sup>3</sup> *Ibidem*, p. 275.

<sup>4</sup> *Ibidem*, p. 276.

such operations will not be able to stop the speculative market for too long and will maintain the share prices relatively constant for a short time, it is still a 'win' situation to distribute that money towards the sector of real economy, lucrative indeed.

Another issue to be taken into consideration by the decision makers in the real and nominal economy and the theoreticians is in regard to the order or viable measures, healthy, of an optimum balance between the **profit rate and economic growth** – as indicators that reflect the real economy and between the **interest rate and inflation rate** – as signals coming from the monetary and financial economy.

A normal, effective and healthy interposition of these indicators requires **the average interest rate be lower than the average profit rate and not vice versa**. How large should be the difference between the size of the two indicators represents a complex issue that depends on the level of economic and social development, specific features and condition of the national economies, the size of risks and vulnerabilities of the respective economy.

A wide research area for economists and not only, derived from the current crisis, is the one regarding the fight against the accumulated effects of the economic, financial crises, of environment, supply and energetic sectors, as an extended issue of interference between real and nominal, in economy and society, by paying a special attention to the importance of economic 'real', as a support for the nominal economy and, on the other hand, the positive feedback with growth force or negative with a force of cancellation, meant to flatten imbalance and tension in the nominal economy.

The multiplication of the adverse contagious effects of the negative externalities in the nominal economy that exceeded a certain threshold of tolerance has represented the main cause of crisis unlatching. Unfortunately, the multitude of the **early warnings** (clignotants) of various models and risk management schemes has not been successfully applied up to now, in order to have a more rigorous and clearer warning in due time, in connection with the imminence and extension of the procedure in recession and economic and financial crisis.

## **2. The 'natural' rate of unemployment and the emergency level in youth unemployment**

It is well-known that the crisis phenomena mainly result into the reduction (contraction) of the activities in various economic and social sectors which trigger the increase in number of unemployed people, especially for youth up to 25 years of age.

The ideal criterion or principle of 'full employment' or of the 'natural' unemployment rate has been and still is a 'moving target' for the entire decision making in the market economy, relying on practical experience, without wasting human capital. What worries is the high unemployment among young people, as crisis has amplified this phenomenon which the competitive free market has not been able to face, as there is the need for an efficient partnership with the state.

**The unemployment rate in Romania versus other EU member states  
for June 2010 and June 2011**

Country	Young unemployed under 25 years of age		Total of unemployed people	
	June 2010	June 2011	June 2010	June 2011
<b>Romania</b>	<b>22.0</b>	<b>22.8</b>	<b>7.2</b>	<b>7.5</b>
Bulgaria	22.3	27.3	10.1	11.4
Czech Republic	18.6	16.7	7.2	6.5
Ireland	27.3	26.9	13.6	14.2
Greece	31.9	38.5	12.2	15.0
Germany	10.1	9.1	7.1	6.1
Spain	41.5	45.7	20.2	21.0
France	23.8	22.8	9.8	9.7
Italy	27.5	27.8	8.3	8.0
Hungary	27.7	24.8	11.3	9.9
Poland	23.8	23.6	9.6	9.9
Portugal	27.3	26.8	12.1	12.2

*Source:* Eurostat, Financiar newspaper, August 3, 2011, p. 10.

Even though in Romania the unemployment rate is lower for both total and young people in comparison with other countries, we consider that this rate is still high mainly for this category of population, which means not only a waste of human capital and poor living conditions, but also an additional factor of delinquency, social tensions, unemployment and leaving the country in search for a job (brain waste).

The fact that the young labor force leaves Romania, mainly talented graduates and young researchers, is an extraordinarily great “brain” loss for this country, which deepens the difference between the potential and real GDP here.

The big challenge of solving exiting crisis problems is not large, massive layoffs, but creating employment and new jobs that will counteract the temptation of such layoffs and the damaging phenomena of crisis.

The sharp and massive layoffs have turned into **overloading the existent staff**, so that their labor efficiency and work results have been less competitive.

A series of adverse effects emerged, due to the lack of coherence in lowering wages costs and discontinuation in the bonification system, less company cars and money spent for travelling abroad, training programs, less frequent attendance to conferences and international events or renegotiation for contracts and agreements.

To avoid as much as possible to cut down the salaries, mainly in the sectors less paid, the implementation of **as many as possible measures of non-financial incentives** in institutions and companies could be realized, which will increase the motivation of the employees, as such: improvement of the professional skills via at-work courses and seminars; job rotation; flexible schedules; a regular feedback concerning the employees performance; a nicer work environment,

encouraging rather than critical; internal competitions on non-professional topics; attracting employees in programs of social responsibility of companies; organizing ‘brainstorming’ meeting to debate on how to raise efficiency and exit crisis.

In this context, the measures and policies of inserting young people into labor market is one of the core topics that the decision making factors should take a good look at, in order to provide solid support to the sustainability of the economic growth and inter-generation cooperation.

Similarly, the positive effects that the **policy of promoting ‘active ageing’**, policy that involves work opportunities for the over-65 people, mainly the highly qualified, which has made the EU place it on top of its agenda and of other European countries’. Another reason is that the young employed segment does not interfere with the positions for the older segment, in point of view of the difference in job levels and skills.

Downsizing is one of the easy and shallow ways to increase, on short-term, the apparent labor productivity. This can entail serious long-term consequences, for economic take-off requires large and highly-qualified workforce. The unemployed, particularly the long-term ones, either fail to meet the requirements of an ever-demanding labor market or they find a job abroad; therefore, unemployment results in short, medium and long-term imbalances on the national job market. Another consequence of the crisis is hiring ill-qualified or non-qualified staff, to replace the highly trained workforce (see the medical staff shortage and the substitute teachers taking the place of the regular teaching staff in the rural areas). For the managers making lay-offs and dramatic pay deductions or cuts in the recruitment and training budgets, the post-crisis recovery process is rather slow, for it is easier to restart an engine working at its minimum capacity than a completely turned-off one.

According to the human resource specialists from multinational Romanian companies<sup>5</sup>, a new potential crisis wave hitting our country in 2012 is likely to follow the first one, outburst in 2008, when, as a result of emotional approaches, a general cost-reduction measure is implemented, **without having a clear strategic perspective on the medium and long-term consequences** of such a step.

### **3. Reconsideration of the convergence dynamics development and of the economic, social, technological and environmental gaps reduction**

The complex and concerning issue of convergence and of theoretically, methodologically and especially metrically reducing the interstate economic and social gaps is based on various economic and mathematical models, relevant for the ex-post analysis, yet less or non-reliable forecast instruments under the crisis or post-crisis circumstances. We are talking about the **time duration in which a business process recovers from a micro, mezzo and macroeconomic downturn**, the intensity and dynamics of the downturn and of the recovery process in various economic sectors, usually suggestively represented by the letters V, U, W and, in

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<sup>5</sup> See Ziarul Financiar, 15 of August 2011, page 9.

the least fortunate case, by L. Additionally, the economic growth theory takes the “J” or “U” shape rather at micro and mezzo than macro levels.

We present below the variations of some anti-crisis indicators and measures in order to see the effort / outcome ratio.

Table 2

**The impact of the economic crisis in October 2011**

Year	GDP	Budget deficit	Exports	Non-resident reimbursements	Foreign direct investments (FDI)
2008	137 bn Euros	5.4%	34 bn Euros	8.6 bn Euros	9 bn Euros
2011*	120 bn Euros	4.4%	43 bn Euros	4 bn Euros	1.5 bn Euros

\* Preliminary estimates.

- o Although at the end of 2011 the GDP value increases by +2.5% compared to the previous year (the final quarter of 2011 records a decrease by -0.2% in the GDP, as opposed to the third quarter), the fall in the GDP recorded in 2009 and 2010 – matching the 2005-2006 values – cannot be redressed. The catching up and leapfrogging-based **economic recovery process** remains a challenge which is not unfortunately taken into consideration, in Romania, in a satisfactory way.

**Romanians working abroad** financially provide for their families by approximately 50% less, compared to the 2007-2008 thriving interval, following the economic crisis hitting the countries where they work. We doubt that the above-mentioned level will be reached in the future, for most immigrants have settled abroad with their families, while the rest have returned home for not finding employment overseas. The amounts of money sent by those working abroad are on the decrease.

The **foreign direct investment rate** has dropped by almost 4 times following the unfavorable economic environment generated by the crisis hitting both the host countries and Romania. Having in view the situation in Romania and in other countries, we shouldn't overlook that in the target country the FDI rate **reaches a limit or saturation level**, to gradually drop in time, following either greater profit opportunities envisaging in other countries, or increasing competition from domestic capital<sup>6</sup>.

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<sup>6</sup> We don't want to minimize the obvious positive impact of FDI for the host country; however, we cannot overlook some negative aspects that must be considered when making strategic decisions.

Pursuant to Donato de Rosa, senior economist of the World Bank (Bursa, 20 October 2011), between 2003 and 2008, according to the Bank's statistics, the added value of foreign companies in Romania increases on average by only 2.8% / year, while the domestic companies record a 5.9% rise, which proves that the latter's contribution to the GDP increase is significantly higher than the former's. In some countries from Central and Eastern Europe, the foreign capital companies record various added value rates: 4.3% in the Czech Republic, 12.4 in Poland and 19.1 in Slovenia.



The only sector reaching, between 2010 and 2011, the value recorded in pre-crisis 2008 is export (43 bn Euros vs. 34 bn Euros); in this case too, we have to analyze to what extent this sector drives the economic sustainable development in Romania, given that increased exports do not reflect in an increased GDP (?!), since most of them derive from foreign capital companies seated in Romania. According to our statistics, between 2008 and 2011, the volume of goods and services exported by foreign capital companies is lower than the volume of imported goods and services, therefore yielding in a trade deficit. This doesn't lead to an increased favorable **external balance and to the national sustainable development**.

In Romania, the crisis leads to a fall in the GDP per capita to a greater extent than in most EU member states, which hinders the **nominal convergence process**, although the GDP value vs. the EU-27 average is 26% in 1999 and 42% in 2008, being on the increase in that interval.

Romania overcoming the economic crisis in 2012 remains an arguable issue, for some partner EU member states seem to experience a slowdown in the economic growth process. Through the spillover effect, the EU member states cooperating with these countries are threatened to face bankruptcy.

According to the estimations of some specialized institutions, in the past two years, the credit risk indicator goes up, yet the situation is still stable. A shallow approach of or neglecting the government debt issue in Romania can entail serious consequences, given that the dynamics of this indicator progresses at a rapid pace under the unforeseeable influence of the domestic and foreign economic environment. If in early 2011 the credit-default swap (CDS) for the Romanian state bonds is 2.0-2.5%, in the September-October interval, the CDS quota rises to 4.5% in Romania, 1.5% in Bulgaria, 3% in Poland and 5% in Hungary. Although we have relatively sufficient foreign-exchange reserves, we mustn't overlook the low capacity to pay the foreign debt on medium and long term. This national trend is not very auspicious, especially if the increasing burden of short run external debt is taken into account.

The crisis entails significant gaps between Romania and the developed countries; this requires a well-defined **economic recovery and convergence strategy**, in terms of both nominal and **real convergence terms**. Focusing on real convergence contributes to a more efficient real/nominal economy correlation<sup>7</sup>. A comparative analysis between Romania and the other EU member states reveals deeper economic and social gaps rather than their relative and absolute reduction.

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<sup>7</sup> Moreover, we need to pay more attention to this aspect, for the nominal convergence indicators between Romania and the EU-27 average rate indicate a favorable climate for our country until 2008, to face the crisis one year later.

#### 4. The protection of new industries (infant industries)

One of the oldest theoretical, methodological and practical debates on the industry-related strategy covers the ways to stimulate **new, young or emerging industries**, known as “infant industries”. Despite of correlating this term with the “life cycle” concept, the national industry-related strategy is not analyzed in the context of a “life cycle” model. More precisely, the potential of new business entities, especially of those activating in top scientific and technological fields, to bring significant changes is overlooked.

Industrial development in Romania has been a long-addressed issue ever since the 19<sup>th</sup> century in the works of prestigious economists of our country, such as:

- P.S. Aurelian<sup>8</sup>, who sees development as a system of the small and medium-sized industry in Romania, without ruling out the possibility of establishing large enterprises as well;
- A.D. Xenopol<sup>9</sup>, who promotes the large industry as “a system, from the beginning” and, additionally, he fosters the development of small enterprises;
- D.P. Marțial<sup>10</sup>, who encourages the development of large and small enterprises simultaneously.

In terms of supporting the development of new industries, we need to focus on how to succeed in doing that. Considering that “the national output cannot keep up or even exist without protectionist measures”<sup>11</sup>, Eminescu outlines: “The fruit of the national industry must be raised first, protected from the fight with the cruel outlandish industry and not until he grows up and becomes strong, will we let him compete under the free trade regime”<sup>12</sup>.

We reproduce a fragment from the economic prose of our great poet to show his visionary and rational capacity, confirmed so far by the economic practice on the principles and criteria of industry-intended subsidies.

According to Eminescu, the funds are meant for young industries, as a temporary protection means, and as soon as they reach their development stage, they can freely face the competition on the national and international markets. This truth is still fully valid to date and implemented in new ways more or less transparent by the major part of developed countries.

On the current crisis background, some companies receive funds not only in their early stage, but also in crucial situations, if they hold an important weight in

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<sup>8</sup> Aurelian P.S., *Cum se poate fonda industria română față cu libertatea comerțului de importațiune*, in Oe-A, p. 214-217.

<sup>9</sup> Xenopol A.D., *Studii economice*, Oe-X, p. 85-86.

<sup>10</sup> Marțial D.P., *Oe-M*, Studiu introductiv de Costin Murgescu.

<sup>11</sup> Eminescu M., „Alexandria, confessing...”, *Timpul*, 30 iulie 1882, in *Opere*, vol. XIII, Edit.cit., p. 155.

<sup>12</sup> Eminescu M., „Influența austriacă asupra românilor din Principate”. *Convorbiri literare*, 1 august 1876, *Opere cit.*, vol. IX, p. 167.

the social and economic picture, according to the “too big to fail”<sup>13</sup> principle. Unfortunately, in Romania’s transition economy such a principle fails to be implemented for large, systemic national enterprises – most of them foreign capital companies – subject to division and useless privatization with so-called foreign strategic investors. The failure to understand and, consequently, to implement the industry-intended funding strategy lies with the stakeholders, who are either ignorant, or ill-intentioned and serve the interests of foreigners aimed at eliminating the potential competition for their goods exported to the Romanian or other markets.

The economic protectionism, in general, and the trade and industry-related protectionism, in particular, gain new dimensions on the crisis background, having in view that the free trade promoted by the World Trade Organization is basically accepted in every state.

Presently, protectionism does not primarily result in tariff-based restrictions or state aid funds, but in non-tariff restrictions covering quality, technological and environmental standards or dumping practices. To the best of my knowledge, Romania hasn’t initiated an antidumping procedure, although we would have had all the reasons to do that, with respect to many competitive imported goods seriously affecting our domestic goods and services of various economic branches.

Most specialized studies show the way in which the industry-related strategies obviously depend on the **input and output dynamics**. Practically, a technology adoption model, in which the companies make forecasts on the technological decisions protection, is developed. Without promoting the permanent industry protection which may **induce an early technology adoption**, yet may result in the firms unlikely to adopt a new technology, we cannot overlook the motivation for temporary protection and funding within certain sectors and enterprises promoting innovation and scientific progress, generators of positive externalities. Experts state that temporary protection results in a faster technology adoption, unlike permanent protection which reduces the likelihood of the companies adopting technologies.

In case of industries characterized by a greater number of firms, the protection strategy does not change the technology adoption rates; it increases the net output likelihood.

With respect to the new industries, we emphasize the need to **elaborate a national reindustrialization strategy**, having in view that according to the latest statistics, industry, in general, and **manufacturing industry**, in particular, have experienced a rapid recovery potential, contributing to an increased GDP and to Romania coming out of the crisis. The expansion of the services sector in transitional Romania, under the post-industrial development thesis, translates, to a great extent, in an exacerbated services “pseudotertialization”, in the development of the super-nominal economy *per se*, characterized by speculative and inflationary pressures, failing to meet the real needs of the primary and secondary sectors. According to the statistics, between 2009 and 2011, only a minor part of the

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<sup>13</sup> Too large to go bankrupt.

tertiary sector contributes, to some extent, to Romania overcoming the crisis, while some of its major components have a negative impact. High wages and profits in some branches of this sector contrast with its contribution to the added value of the goods and services of real economy. In many cases, the selling price is a few times higher than the manufacturing cost, both on domestic and international markets (in the case of so-called transfer pricing), because of some speculative agents following the “profit searching” principle.

### 5. Inefficient shock dimensions of anti-crisis measures

During the crisis, all states turn to **austerity measures** resulting in wage freeze or cut, downsizing in both public and private sectors, fiscal facilities concurrently with income tax, wealth tax and the like.

A comparative analysis between Romania and the other EU member states in terms of the anti-crisis measures reveals the following:

- Romania implements **drastic steps**<sup>14</sup> to cope with the crisis: considerable wage cuts in the public sector (by 25%) along with cutting some benefits and bonuses (premiums, food vouchers, PhD-related compensation and the like), the value added tax rising from 19% to 24%, tax on pensions by 16%, increased price for drugs and the like; all of the above hinder the economic sustainable development, even if the budget deficit is, to some extent, temporarily redressed;
- wage cut and increased duties and taxes are applied equally, undifferentiated, linear for all employees or taxpayers, without assessing the social and economic contribution of the persons from various professional categories in terms of sustainable development, of affecting the quality of life and of solvency; such a pattern, reminding us of the “flat taxation myth” – relatively high for the small producers – hits especially the purchasing power of most low and middle-income earners, entailing increased poverty, tax avoidance, social tensions and discontent, in a nutshell, social polarization.

At least until now, the effects of the politicians’ shock measures of the anti-crisis policies undertaken by the Romanian decision makers did not have as result the wanted effect, on the contrary, they prolonged the turbulences and the economic and financial imbalances and they reduced the standard of living, they disrupted the base of the durable economic growth.

A lot more justified and efficient would have been the differentiation of the measures in the field of the fiscal and salary policies, in the sense of their **adequacy to the specific of each social, professional and income policy, taking into consideration the positive effects of the labour tax reduction and the**

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<sup>14</sup> As a rule, any wage cut or tax increase measure is based on factors generally entailing 5%-7% deductions, at the most, not impacting upon the demand as a wage cut by 25% would, on one hand, and is implemented to test the population’s bear ability, on the other.

**increase of the wealth tax and Eco tax.** There is also an interesting and realistic measure in the field of the wage system: the increase of the minimum wage to 500 Euro/month, with the purpose to increase the consumption and investment savings and, therefore, the products and services demand. The financial insurance of such a measure could be found in the margin reductions of unjustified profits or in a more rigorous differentiation of the income taxes, as an answer to the stereotype objection “there is no money”!

The international experience regarding fiscal policy has shown that the great majority of the countries apply the differentiated, progressive tax and not the flat taxation<sup>15</sup> for the simple reason that the first offers greater possibilities of adjusting the taxes to the promotion of certain sectors and branches with strategic importance for the security and insurance of goods and services of vital importance for the population or with a strong propagation effect for the modernization and efficiency of the economy, as well as for the increase of the welfare. Taking into consideration that Romania will adopt the provisions of the EU “Fiscal Pact”, which anticipate a target of 0.5% structural deficit of the GDP, the need to overcome the recession is directly linked with the dimension (power) of the automated stabilizers, which depend on the tax system and share of the governmental sector within the GDP. The stabilizers initiated in Romania are weaker in comparison with other EU countries, such as Denmark, the Netherlands, Sweden and Finland, where taxation has a strong differentiated progressive character.

Therefore, the much-praised flat taxation in Romania proves to be contradictory with the budget imbalance reduction measures envisaged by the fiscal pact.

On the other hand, the tax installments must be underlain both from the point of view of their optimal dimension and from a social and economic point of view. It seems obvious and justified that those economic agents or those persons who **use or deteriorate more the environment factors**<sup>16</sup> and who generate marginal external costs (insufficiently analyzed within the Romanian theory and practice), must pay higher corrective taxes. Such taxes try to use the market mechanisms, making compatible the **private optimality or that of the competing market with the social optimality**, in order to promote equity, solidarity, inclusion and social equity.

The end of the crisis needs a better use of the **mechanism, of the so-called subsidies or the support of the positive externalities** (the marginal benefits

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<sup>15</sup> Without considering that one or the other tax method is a panacea (or that it would be perfect!), the progressive tax offers more promotion possibilities of the durable development policies from the economic, social and environmental points of view, as well as of structural budget deficit recently imposed by Fiscal Treaty signed by EU countries at the beginning of March 2012.

<sup>16</sup> By environment factors, we do not understand only its basic components (air, water, soil, subsoil), but also the anthropic capital, meaning the local, regional and national public infrastructure goods, the environment being the most comprehensive public good.

disseminated to third parties), in the case of the economic agents with positive externalities (environment, RDI, health, education etc.). The subsidies generally represent an economic policy instrument practiced currently within the western economy, under the condition that these are **affordable from the point of view of the financial resources, rigorously targeted and efficient (with a high probability** for the desired effect) and granted for a limited period of time (temporary). As an example of subsidies inefficiently granted, we mention the type of financial aid the farmers have benefited from, without any established conditions, commitments, correct production schedules. The state aids and the facilities granted to certain Romanian and foreign investors fall into this same category, in the case of the privatization of the state companies (some of which of great dimensions), which by post-privatization investment programmes committed themselves to respect the achievement of certain investment, production, personnel, environmental indicators. In reality, a lot of the commitments and provisions have not been accomplished and, consequently, the state aid or the advantages (which, in some cases, consisted in hundreds of millions of Euros) were inefficient!

The cancellation of the privatization contracts, their renegotiation during several rounds meant to Romania's economy a huge loss by the marginal external costs generated, including the law expenses for establishing the ownership. To these costs, we add the ones with the foreign consultancy companies for the privatization process or other specialists involved in the process. The increase in the efficiency of the institutional capacity of the timeliness and the specialization of the Romanian justice still is a major issue for Romania, with new peaks during the crisis periods.

One of the major flaws of the laws on many levels is exactly the lack of adequate preparation, solid bases, and careful analysis of the impact of different policies over the economy during different periods. It is exactly what the Nobel laureates in economy have approached in their studies; in 2011, J. Sargent and C. Sims talk about the means to determine the effects regarding the shocks of the market and other political factors upon the macro-economic process.

## **6. The public-private partnerships**

The current economic and financial crisis demonstrated once more, one on hand, the inconsistency and the unilateral character of the theories regarding the infallibility of the free market mechanisms and of those regarding the "walk-on" economic role of the state. The contemporary economists with international authority express it even tougher, in the sense that the current crisis threw to the history bin the neo-liberal monetarist theses, which, for a period of time, were accredited without reserves, with panacea abilities within the market economy.

I do not wish to make an analysis of the relations established between the state and the private sector, between 2008 and 2011, when many of the developed countries made major capital investments in order to try to save banks and other financial institutions in functional difficulty or when the state performed some sort of temporary "nationalizations" in the case of certain banks. I wish, nevertheless, to

highlight the fact that during the economic crisis, the economic role and intervention of the state must intensify. We are talking about a state with professional decision makers and performers and not about one affected by corruption and the incapacity to manage the crisis within the financial and banking system and the production and distribution system of public goods and services or private ones with strategic importance (food security, health, education, occupancy, etc.).

The crisis brought into attention the fact that it is very important to carefully analyze, in the case of the Romanian economy, the sense and opportunity of the financial aid given by the state to the banks in virtue of the statement: “too big to fail”. In such cases, it was possible and justified to defy the sacrosanct law of the functional market economy regarding the subsistence of only the profit-making firms. As mentioned before, during the transition period, the big state companies and banks which were, at that time too big to fail did not benefit from such treatments in Romania. Systemic entities were destroyed by insolvency, bankruptcy, division, partial privatization with national and foreign strategic investors, some of whom proved to be broke or incapable of redressing the bought from the state companies.

In many situations, the Romanian state invested amounts a few times bigger than the ones gained after the privatization in certain companies in the public sector in order to bring them back afloat, which we cannot consider to be a profitable business. The motivations of an “extra-economic nature” invoked by the decision makers, more or less transparently, directly or indirectly, in such cases did not generate compensations and equivalencies valid qualitatively, or in terms of value, money, for the economy and the people’s welfare, therefore the measures or pressures of other nature than the economic-financial one represented some sort of opaque “black box” that served other purposes and not Romania’s.

The crisis should also bring into discussion the issue of the bankruptcy effects quantification or that of rescuing a bank in difficulty, comparative with the same bankruptcy situation of a big company of national importance in the industrial field or other sector. Is it always true that the bank is more important than a big company within the production sector?! Obviously, it is necessary to perform a cost/benefit analysis both in the financial-banking intermediaries sector and the material production sector. I doubt that the bankruptcy of an automobile factory with a weight of 24% within the export of a country, for example, is less important or harmful than the bankruptcy of a bank, regardless of its size. Consequently, it is necessary to decide bankruptcies and company rescues, during the crisis periods, considering serious analysis and not temporary interests, personal interests or group interests imposed extra-economically by power within or outside the country. Many specialists wonder why banks receive so much attention from the state during crisis periods, while other companies from the industrial sectors do not benefit from the same treatment. Is a financial intermediary more important than a large industrial producer?! The answer must be well argued.

It is often neglected that the crisis imposes a tight collaboration between the state and the economy within the **public-private partnerships**, but also within the private-private and public-public ones. Reality proved that, during the crisis

periods, the state must have the capacity to propose solutions for the exit from the crisis, following the Schumpeterian process of “creative destruction”, which is not valid only for the technological progress, but for other activity fields as well, including the institutional one.

The shrinking of the state from the economy during the “quasi-normality” periods of Romania’s transition towards the market economy was a measure imposed due to the fact that, practically, a private sector did not exist in the country’s economy and it had to be created. The quasi-total backing of the state from the economy, under conditions of crisis, seems to be a totally uninspired measure. The crisis period needs the institutional capacity and the public information at superior quantitative parameters, in order to contribute directly to the exit from the crisis, through appropriate policies.

Regarding the relation between the public and private economic sectors, we consider completely inadequate the use of the term privatization when a “systemic” asset of the Romanian state is sold to another state, leaving the public Romanian sector for the public sector from another country.

There are, however, abnormal situations in my opinion, which have practically proved the **incapacity recognition of the Romanian state to manage certain companies it had to manage and, implicitly, the capacity of other states**. The natural question is: to what extent can we talk about a privatization or a transfer from Romania’s public sector towards the public sector of another country?!

On the other hand, the experience of other states showed that the state is, in certain cases, a good manager, guarding for specific needs of certain entities within the banking system or other sectors delivering public goods or systemic importance ones.

The sale of the minority stock package of the state from companies mainly private in Romania, when the crisis affects the level of the prices, cannot be justified in terms of durable development, because the low prices the state obtains by selling minority packages erase the possibilities to earn state incomes on the long term, and the state would need this kind of incomes. This manner to think and act under pressure, with short-term visions, for the betterment of a critical situation is totally detrimental to the insurance or permanent income sources of the state on the medium and long terms.

Another field where the tight cooperation between the state and the private sector is needed would be **the external balance of payments, of the public and private debt, internal and external on the short, medium and long term**. The crisis demonstrated that the thesis according to which the debt in the private sector has nothing to do with the public debt is wrong and injurious. There is no situation in which the public sector works fine because it has a small debt, when the private sector is almost bankrupt and vice versa. There is a bi-univoque connection between the public and the private debts, taking into consideration the fact that any private activity, by its positive or negative externalities, interferes on the long term with the public sector and the other way around.



Moreover, the private debts guaranteed by the state involve the state directly. If the private company granted by the state goes bankrupt, the state has to pay! The partnerships should function on the short, medium and long term, especially regarding the debt financing sources, the real payment capacity. The debts that are huge and unclear from the efficiency point of view, made during a political mandate of 4 years must be paid by others in the future. We are talking about the lack of inter-generation ethics, the ignorance of the economic and social development sustainability, but also about lack of accountability and social responsibility of decision makers.

## 7. The relation between FDI and the durable economic growth of Romania

According to recent statistical data, in 2011, FDI reduced to half in comparison with the same period of 2010 and in 2010, the reductions of FDI were of 50% in comparison with 2009, after a sensible decline in 2009 in comparison with 2008. This unfavorable trend is a consequence of the negative impact of the crisis, externally and internally, and it obviously imposes a reassessment of the means to attract foreign investors and of the reduction of their “volatility”, as it is a known fact that, for many reasons, they can leave the country looking for higher profit in other countries, leaving very negative effects upon the economy of the country of assignment.

Currently, Romania has an open economy, FDI hold a **key position, dominant in most of the economic sectors, reaching over 90% in the banking system** and over 70% in the industrial field and the import-export one.

Under certain limitations and conditions, the foreign direct investments are a factor whose contribution to the development of the country is important, especially due to the efficient management, the economic and financial performances and technology transfer, the know-how, etc. The crisis proved that in spite of the foreign investors’ performances in Romania, **their favorable impact on the economy was not enough to lead to the end of the crisis!** Moreover, some of the important foreign investors have left or intend to leave.

According to the analyses upon the FDI firms in Romania<sup>17</sup>, the following aspects relevant for the challenges generated by the economic and financial crisis have resulted:

- **the biggest weight (over 43%) of the total FDI** amount was held, in 2010, **by the financial intermediary services, the trade and the services for the companies**, that is the tertiary sector whose contribution to the GDP is mainly based on speculative activities with volatile features, on the short and medium terms and that make financial profit without an equivalent in the real economy;
- in 2011, the total FDI amount in Romania was 1.92 billion Euro, 13.6% less than in 2010, close to the level of 2003, when the value amount of FDI

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<sup>17</sup> See: Zaman Gh et. al (2011), *Impactul ISD din România asupra exporturilor și dezvoltarea durabilă*, „Romanian Economic Journal”, Volume 33, issue 2 (42), pp. 1-60.

was 1.94 billion Euro. This descendent trend of the FDI during the last years was caused by the vulnerabilities caused by the international economic and financial crisis;

- the processing industry had a weight of approximately 32%, especially in the branches with a low technological level, the high-tech branches were holding a weight of approximately 4.5% of the total FDI within the industry;
- The agriculture had a weight of 1.4%-2.0%, which highlights the low interest of the foreign investors for this sector, also due to the relatively low profit, the seasonal character of the activity and the instability of the agricultural production level generated by the climatic factors.

Analyzing realistically the role of FDI in the Romanian economy, more careful attention must be paid to the manner in which their impact is manifested on the Romanian economy, and if they answer to the economic and social interest of the country. The acceptance without reserves of the thesis regarding the general healthy effect of the FDI upon the development of the national economy is a unilateral and partial approach. FDI can also have a negative effect upon the national economy, connected, for example, with the leasing of the foreign investors, the full expatriation of profits or the unfavorable impact of certain exports made by FDI firms, based mainly on products with a high consumption of natural capital and cheap labor force or by the so called “transfer pricing”<sup>18</sup>. In other words, it is necessary to analyze to what extent is the thesis according to which the lack of capital “transformed us” in an outlet, a cheap labor force source and staples, right for Romania.

### Conclusions

In the next lines we will point out some of the conclusions regarding the above analysis of the complex phenomena regarding worldwide economic crisis.

Firstly, as we stated above, the momentum of the nominal, financial and monetary economy, with no direct and efficient support in the real economy, will always trigger phenomena of destabilization in economy and society. So this lack of correlations between the two dimensions of an economy was the main factor causing the crisis and subsequent evolutions.

Related to this I consider that one of the measures required for recovering the economic situation is **to reduce the volume of speculative transactions on the financial capital market**, of the securities, complying with rigorously set criteria.

Thus, these measures may target the discontinuation of the stock activity on the secondary market for a certain period of time, including by implementing

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<sup>18</sup> The transfer pricing is specific to the export of the goods and services from the country of assignment of a parent-company at a relatively low price; these goods and services are resold at a price a few times higher after the brand or the package have been changed.

certain limitations or forbidding the **‘naked short-selling’** transactions for an undetermined time, at some companies in the banking and financial sector.

All this kind of financial speculative operations tend to produce more nominal economy effects and are not a truly efficient instrument fighting against the crisis effects. From the point of view of financial institutions, the crisis should also bring into discussion the issue of the bankruptcy effects quantification or that of rescuing a bank in difficulty, comparative with the same bankruptcy situation of a big company of national importance in the industrial field or other sector. We consider that if most of the resources should be directed towards improving the production sector emulation at the level of economic efficiency, the situations of helping financial institutions without a clear recovery from the consequences of the crisis will be no longer on the current agenda.

Consequently, it is necessary to decide bankruptcies and company rescues, during the crisis periods, considering serious analysis and not temporary interests, personal interests or group interests imposed extra-economically by power within or outside the country.

With respect to the new industries, we emphasize the need to **elaborate a national reindustrialization strategy**, having in view that according to the latest statistics, industry, in general, and **manufacturing industry**, in particular, have experienced a rapid recovery potential, contributing to an increased GDP and to Romania coming out of the crisis. In support of this conclusion are the statistics showing that between 2009 and 2011, only a minor part of the tertiary sector contributes, to some extent, to Romania overcoming the crisis, while some of its major components have a negative impact. So the opinion credited not long time ago that the tertiary sector of economy can bring most of the economic development is out-dated in the context of the actual crisis in Romanian economy.

Another conclusion of our study is related to the fact that analyzing realistically the role of FDI in the Romanian economy, more careful attention must be paid to the manner in which their impact is manifested on the Romanian economy, and if they answer to the economic and social interests of the country. Not every kind of FDI and any occasion represent an effective instrument for the development of Romanian economy, many of these companies having developed a highly efficient export mechanism of profits made at the level of our economy.

At the end of the conclusions I want to emphasize again the fact that during the economic crisis, the economic role and intervention of the state must intensify.

We are talking about a state with professional decision makers and performers and not about one affected by corruption and the incapacity to manage the crisis within the financial and banking system and the production and distribution system of public goods and services or private ones with strategic importance (food security, health, education, occupancy, etc.).

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