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POLICIES FOR THE EURO ADOPTION IN ROMANIA

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Abstract: *This paper analyses the policies for the euro adoption in Romania. For Romania, adopting euro as national currency seemed to be, at least until very recently, a priority objective, fact suggested by the rush in entering the EMS II system. A major regime change, as the monetary unification, is clearly made when there are strong motivations given by benefits, but such a change involves costs, risks and difficulties. The adoption of the unique currency in an unsuitable time can have more bad consequences than positive ones.*

Key words: *Monetary Union, convergence criteria, national target.*

1. Introduction

All Member States of the European Union, except Denmark and the United Kingdom, are required to adopt the euro and join the euro area. To do this, they must meet certain conditions known as 'convergence criteria'.

All EU Member States are part of the Economic and Monetary Union, which means they coordinate their economic policies for the benefit of the EU as a whole. However, not all EU Member States are in the euro area – only those having adopted the euro are members of the euro area.

Of the Member States outside the euro area, Denmark and the United Kingdom have 'opt-outs' from joining for reasons of economic sovereignty. These two countries can join in the future if they so wish.

Sweden is not yet in the euro area, as it has not made the necessary changes to its central bank legislation and it does not meet the convergence criterion related to participation in the Exchange Rate Mechanism (ERM II). However, under the Treaty, Sweden is required to adopt the euro.

The remaining non-participating Member States acceded to the Union in 2004 and 2007, after the euro was launched.

At the time of their accession, they did not meet the conditions for entry to the euro area, therefore their Treaties of Accession allow them time to make the necessary adjustments – they are Member States with a 'derogation', as is Sweden. These Member States have committed to joining the euro area as soon as they fulfil the entry conditions. When this is the case, the 'derogation' is 'abrogated' by a decision of the Council, and the Member State concerned adopts the euro. [1]

The fact that euro became a currency in its own right appear to have two implications. First, that it is a currency, the currency of particular countries. Secondly,

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that it no longer consists of a basket of currencies – in which form it could scarcely have an independent existence – but is now an independent currency having its own characteristics [2].

According to The Yearly Report of National Bank of Romania (2010), the fulfillment of the criteria foreseen in the Maastricht Treaty and the adoption of a sole European currency are a part of the European registration process of Romania. The entrance into the euro area implies the transfer of the development and leadership of monetary policies to the Central European Bank, institution whose actions are conducted in a unitary manner for the whole euro area, without taking into consideration the national economic particularities. In this context, in the primary period of the unique currency adoption, it takes a fundamental act in order for the national economy to cover the necessary adjustment in the euro area.

According to the Maastricht Treaty, a member state of the European Union benefits of a temporary derogation regarding the euro adoption. But it has the obligation to prepare itself for the entrance into the European mechanism and in the exchange rates ERM II, where it will stay for a period of at least two years, after the unique currency can be adopted.

2. The conditions for Romania to entry the euro area

The process of building Europe is one of progressive integration. The single market for goods, services, capital and labour, launched in 1986, was a major step in this direction.

Economic and Monetary Union and the euro take economic integration even further, and to join the euro area Member States must fulfil certain economic and legal conditions.

Adopting the single currency is a crucial step in a Member State's economy. Its exchange rate is irrevocably fixed and monetary policy is transferred to the hands of the European Central Bank, which conducts it independently for the entire euro area. The economic entry conditions are designed to ensure that a Member State's economy is sufficiently prepared for adoption of the single currency and can integrate smoothly into the monetary regime of the euro area without risk of disruption for the Member State or the euro area as a whole. In short, the economic entry criteria are intended to ensure economic convergence – they are known as the 'convergence criteria' (or 'Maastricht criteria') and were agreed by the EU Member States in 1991 as part of the preparations for introduction of the euro.

In addition to meeting the economic convergence criteria, Romania must make changes to national laws and rules, notably in the governing of its national central bank and in other monetary issues, in order to make them compatible with the Treaty. In particular, national central banks must be independent, such as the monetary policy decided by the European Central Bank is also independent [3].

The national target date for the adoption of the euro in Romania is 01.01.2015, which is a very ambitious goal, especially given to the effects of the global economic and financial crisis.

The Member States which were the first to adopt the euro in 1999 had to meet all these conditions. The same entry criteria apply to all countries which have adopted the euro since then and all those that will adopt it in the future. [4]

3. The convergence criteria

The convergence criteria are formally defined as a set of macroeconomic indicators which measure:

- Price stability, to show that inflation is controlled;

- Soundness and sustainability of public finances, through limits on government borrowing and national debt to avoid excessive deficit;
- Exchange-rate stability, through participation in the Exchange Rate Mechanism (ERM II) for at least two years without strong deviations from the ERM II central rate;
- Long-term interest rates, to assess the durability of the convergence achieved by fulfilling the other criteria.

The exchange-rate stability criterion is chosen to demonstrate that a Member State can manage its economy without recourse to excessive currency fluctuations, which mimics the conditions when the Member State joins the euro area and its control of monetary policy passes to the European Central Bank (ECB). It also provides an indication of the appropriate conversion rate that should be applied when the Member State qualifies and its currency is irrevocably fixed.

The five convergence criteria Table 1

What is measured:	Price stability	Sound public finances	Sustainable public finances	Durability of convergence	Exchange rate stability
How it is measured:	Consumer price inflation rate	Government deficit as % of GDP	Government debt as % of GDP	Long-term interest rate	Deviation from a central rate
Convergence criteria:	Not more than 1.5 percentage points above the rate of the three best performing Member States	Reference value: not more than 3%	Reference value: not more than 60%	Not more than 2 percentage points above the rate of the three best performing Member States in terms of price stability	Participation in ERM II for at least 2 years without severe tensions

According to the Treaty, at least once every two years, or at the request of a Member State with a derogation, the Commission and the European Central Bank assess the progress made by the euro-area candidate countries and publish their conclusions in respective convergence reports.

On the basis of its assessment, the European Commission submits a proposal to the Council of the EU which, having consulted the European Parliament, and after discussion in the Council, a meeting of the heads of state or government decides whether the country fulfils the necessary conditions for adopting the euro currency. If the decision is favourable, the Council abrogates the derogation and, based on an European Commission proposal, having consulted the ECB, adopts the conversion rate at which the national currency will be replaced by the euro, which thereby becomes irrevocably fixed.[5]

4. Prospects and Threats for the Euro Adoption in Romania

- Romania's situation is similar to Hungary's: Most people support euro adoption and all mainstream political parties back it.
- The recently updated convergence plan sent to Brussels sets the target date for euro entry at 2015. This may be feasible, but it is increasingly likely that

the country will have to delay it. The government won political cover from IMF chief Dominique Strauss-Kahn, who said Romania should not insist on a 2015 entry date because the country could use an extra year or two. The European Commission (EC) reacted cautiously to Romania's updated convergence plan and pointed out several inherent risks. First and foremost, the EC criticized the lack of measures to bring down the budget deficit in 2011 and 2012. Romania will have to present deficit-lowering proposals to EU officials by mid-May. Romania also received negative comments for its failure to enact a fiscal responsibility law, which lowers the credibility of the government's pledges to consolidate state finances, in the EC's opinion.

- Inflation remains relatively high, registering 4.56 % in November 2012. But while consumer price increases are expected to cool off, the budget deficit is expected to top 4.3% this year. Given Romania's track record, skepticism is justified when it comes to Romania's ability to reduce its deficit.
- Political factors could also hinder the introduction of the euro. The Romanian government's efforts in bringing down the budget deficit may not be strong enough. Many of the conditions of its IMF loan remain unfulfilled a year after the contract was signed. The government should have made sizeable reductions in the state workforce by now. The administration is also still debating IMF-mandated laws that should have been passed already, including the fiscal responsibility law, pension reform and the unitary wage law. The government has reaffirmed its commitment to passing these painful measures on multiple occasions, but has always failed to follow up. The political outlook does not favour a multi-year consolidation plan, as we had again election in 2012, making it almost impossible for the administration to follow a prudent fiscal policy. 2015 is therefore not a realistic entry date. 2016 is more reasonable if we take the political reality into account.[7]

5. Advantages and disadvantages of the euro adoption

The euro adoption brings a series of advantages which can be grouped directly and indirectly, but also disadvantages.

The direct advantages are:

- Removal of currency risk from the euro;
- Reduction of volatility of the exchange rate from the currency of other commercial partners;
- Reduction of transaction costs;
- Reduction of administrative costs;
- Reduction of capital cost.

The indirect advantages:

- Growth of the exterior commerce;
- Growth of the direct foreign investments (DFI);
- GDP growth/habitant due to the increase of exterior commerce and DFI;
- Increase of competition and transparency;
- Increase of the standard of living in the long term.

Disadvantages:

- Technical and organizational costs referred to the conversion in euro;
- Specific costs in the bank sector and reduction of bank income sources;
- Loss of monetary independence policy and the exchange rate;
- Risk of asymmetric shocks;
- Possibility of a greater inflation on long term.

Regarding the benefits due to the adoption of the euro, they are absolutely sure. The most important from them is the one referred to the removal of the exchange rate risk and the stimulation of exterior commerce.[6]

Analysing the disadvantages of the euro currency adoption it is found that the Romanian economy is completely different than the euro area. After the adherence to the euro area, Romania cannot use the exchange rate as an adjusting instrument. The exchange rate facilitates the shock absorbance and the impossibility to use the exchange rate as a cushion for the economic shocks imposes a stable, solid, competitive economy. Otherwise the effects which will occur can be dramatic. The major disadvantage of the adherence is the loss of monetary policy tools, and this can lead to the appearance of the so called asymmetric shocks.

6. Conclusions

To adhere to the euro area, we should concentrate firstly on the increase of competitiveness, on public coherent policies and on an agenda of structural reforms.

At enterprise level, the competitiveness is the capacity to maintain the firm on the market through products with equal characteristics or superior ones than the competitive similar products.

At nation's level, to be competitive means taking a series of indicators (employment, productivity, foreign trade, financial stability, business environment) over the average and close to the most performing states from the euro area.

The moment of the euro adoption is not only a decision of Romania, through the efforts which need to be taken to achieve that level of development which can allow the adoption of the sole currency. Even if the criteria are the same for all the states which want to integrate from the economic and monetary point of view, each country needs to create its own strategy of monetary policy of transaction according to the needs and individual circumstances.[3]

Likewise, it is to be remarked that the passing to the euro area does not need acceleration in useless way, but the adoption of the unique currency does not need to be treated as a sole purpose. Besides the achievement of nominal convergence goals, the accomplishment in the shortest time of the real convergence represents the goal to which would be indicated to subsume the policies followed by the Romanian authorities.

It is obvious that Romania has a long way ahead in terms of convergence, especially the real one, but also the nominal convergence. What needs to be assured is, however, the sustainability of the convergence process.

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