

INTERNATIONAL FINANCIAL CRISES - CHANCE FOR ROMANIA

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Abstract: *The international financial crisis can be a real chance for Romania. The international financial crisis has served to reveal the true and deep domestic economic crisis. Face to face with the real situation, using the European funds at full, the alternative financial support such as PPP, the particular natural and human potential, Romania could become the best in its historically traditional successful fields (such as agriculture) and position on innovative fields (such as high technologies of transport, new energy sources, research and development) by burning steps of development. This paper presents the present economic situation, what the unused tools are, what is the opportunity and what monetary and fiscal policies can do.*

Key words: *domestic economic crisis,; European fund absorption, PPP, restructure.*

1. Introduction

The current financial crisis brings out obvious adverse effects and is somewhat forced to find positive implications in this situation. There are positive implications but if we think of reducing consumption and environmental impact, of rethinking how the state intervenes in economies.

Beyond these general and universal issues, in Romania the chance that crisis can be beneficial, is related to class policy and government, to the fact that in a constraint situation they will find solutions for the national economic recovery and they may finally manage to start a sustainable development in the fields which have growth potential.

These areas with growth potential are recognized and affirmed both in economic analysis, political speeches and citizen's consciousness. It is about agriculture,

infrastructure and renewable resources also. The international financial crisis has served to reveal the true and deep domestic economic crisis, the fact that almost 45 % of internal consumption [6-7] was covered by imports and sustain by lending.

2. Objectives

We show in a more analytical step the reasons for our domestic crises, the real potential of growing in agriculture, infrastructure and renewable resources, the unused tools in these fields and what monetary and fiscal policy can do.

3. Domestic Crises

The economic growth we recorded between 2004 and 2008 only boosted sectors of lesser importance to the economy, such as real-estate, automotive

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sales and home appliance sales. The economy could not be fed, and once foreign financing stopped for these sectors, they began to collapse. Downturns of 60 to 70 percent could not be blamed on the crisis, as they were the result of anomalies that existed before the crisis began. These anomalies come from the fact that economic growth registered in Romania was unsustainable, relied exclusively on

the consumption of imported goods, financed by foreign money (Fig.1) through lending (Fig. 2). If we look in a mirror we can see that current account deficit, hand in hand with trade deficit, are covered by foreign investment. And the most important increasing factor of current account deficit financing is lending through commercial banks.

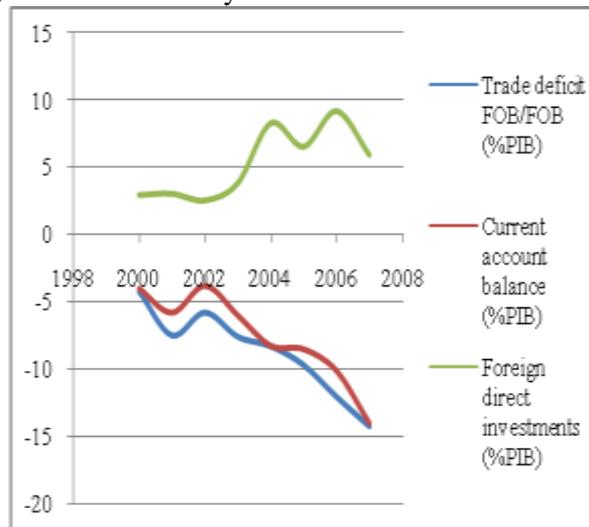


Fig. 1. *The current account deficit and foreign direct investment in Romania (% din PIB)*

Source: INSSE, BNR

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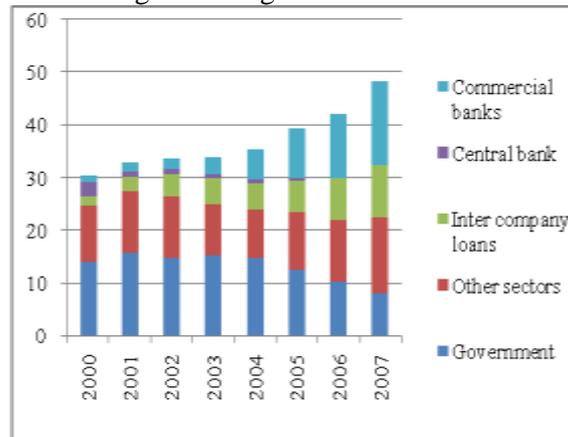


Fig. 2. *Current account deficit in Romania - sources of financing (% din PIB)*

Source: BNR

Sector as industry and agriculture dropped (Figure 3) although consumer demand was high. At this point we have to look to government. As we can see only services and construction increased in this period as contribution to GDP. If we have in mind the structure of services, that is

commerce, transport, tourism and others, we understand the impact of imports in increasing services.

The global crisis has done nothing but create turmoil and raise costs; it is not the reason for the situation we are currently seeing in Romania.

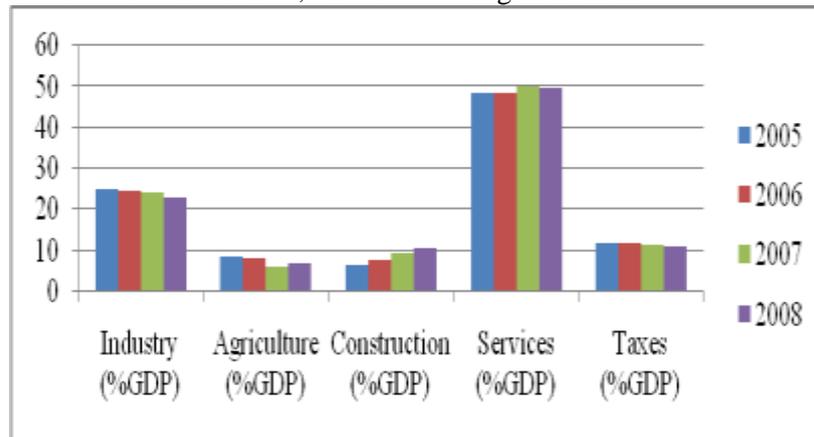


Fig. 3. Main contribution to Romania's -Gross Domestic Product (%)
Source: INSSE

4. Agriculture

This article starts from the belief that Romania can feed twice its population and somehow we all know that this could be true. The reality is that we have a trade deficit on segment of food, beverage and tobacco of around 1.8% of GDP, [6-7] despite the fact that Romania stands very comfortable in terms of agricultural resources. Arable land represents 39.5% of its total area and only 5 other countries in the world have a better position than Romania. [9]

Romania's agricultural sector is often referred to as a main potential beneficiary of EU membership. Opportunities stemming from increased budgetary transfers are expected, as the EU funds earmarked for Romania under the

Common Agricultural Policy amount to EUR 7.5 billion during 2007-2013.

Furthermore, opportunities are expected to arise from a more stable and predictable agricultural regulatory and market environment due to the EU seven-year programming cycles and, in particular, the market price stabilization effects of the interventions under the Common Market Organizations (CMOs).

Full integration into the EU could translate into increased market opportunities for the Romanian farmers, who, in principle, have the opportunity to supply a market of more than 500 million consumers.

Romania might become the third agricultural power in Europe after France and Germany given good absorption of EU funds until 2013, high FDIs directed

towards agriculture and strong governmental support.

The problems in Romania's agriculture and the opportunities too are self employment and low productivity, agriculture at the nature's mercy, highly fragmented land holdings and the market orientation. [1]

Self employment dominates the landscape and this structure of labor force along with low investments in agriculture results in a very low productivity. Average

yield per hectare for main crops is well below European standards (only 40% on average as compared to France). [8] Gross value added per employed person in agriculture is by far the lowest in the national economy.

Self employed people usually work for their own benefit. Actually, more than 33% of the total households' income in the rural area is "self consumption" (agricultural produce retained for consumption within the household).

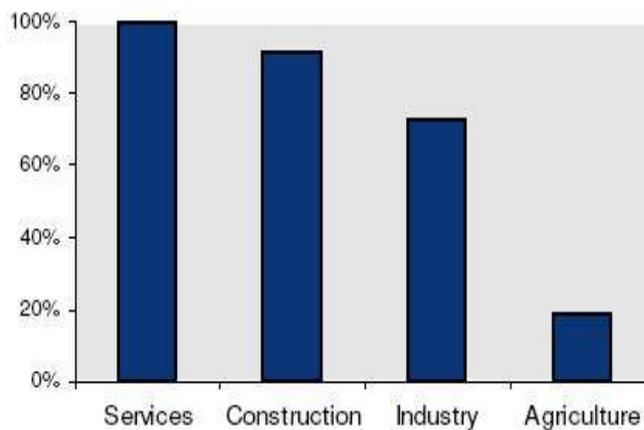


Fig. 4. *Gross value added per employed person (service = 100%)*
Source: *INSSE, BCR Research*

This problem goes hand in hand with highly fragmented land holdings that are an important setback for the local agriculture and the incapacity to sell their crop and animal production in modern hypermarkets and supermarkets. Agriculture in Romania may have the worst rural infrastructure in Europe, but for the bold, this only offers potential.

The solution is to reduce the number of individual farms, while increasing the average crop areas per one farm to meet the performance criteria set by the European Union because there are more than 4.2 million agricultural holdings, while the percentage of individual farms is predominant. [10]

Out of the total number of agricultural holdings, 99.6% were individual agricultural holdings, while companies and associations had an insignificant share of 0.4%. [10] There is plenty of room for future strong concentration of agricultural holdings with positive impact upon profitability.

The tool is an adequate legislation for Land Consolidation which is not yet approved in Romania. There were concerns, studies, financial support through Phare Program, pilot schemes likely to be assisted by the World Bank

But nothing materialized unless an adequate legislation is implemented before the land reform can start.

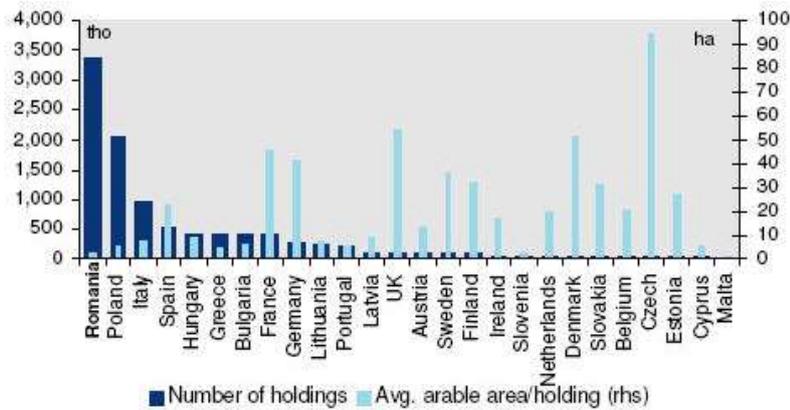


Fig. 5. *Strong imbalance between no. of holdings and arable area per holding in Romania*
 Source: Eurostat, BCR Research

It is hard for authorities to persuade farmers to consolidate their land without invoking the ghost of forced collectivization but they have to find ways to convince Romanians to understand that this is in their own. Joining is very important for farmers to become competitive, maybe not for the mutual property - but at least for mutual agriculture exploitation.

This is a solution of regulation that is an unused tool and is a premise for foreign investors who are pretty active. Usually,

most foreign investors who came to Romania to invest in agriculture were keen to buy large plots of land but, again, the high land fragmentation as well as the important red tape in merging several land plots could be an important setback for further investments. Foreign companies hold now more than 300,000 hectares (over 3% of total arable land) [1].

Agriculture in Romania may have the smallest FDIs in agriculture sector through eastern EU member but for the bold, this only offers potential.

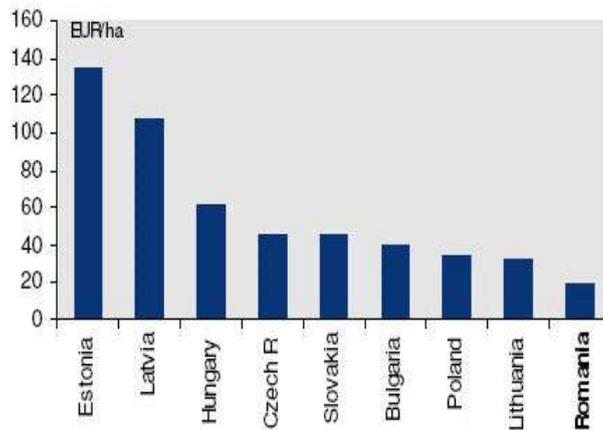


Fig. 6. *FDIs / ha in agricultural sector, stock 2006 (EUR)*
 Source: Central banks, statistical offices, BCR Research

Other unused tools due to some legislation drawbacks and dialog difficulties with EU institutions are EU funds. Romania couldn't absorb EU funds in the first year of accession. Actually, agriculture was by far the last performer in terms of EU funds absorption (only 1%), total funds that came in standing at a mere EUR 10 million out of 740 million earmarked for 2007.

In conclusion, if government will turn the face to this golden mine, agriculture, that is a real opportunity and viable solution.

Opportunities offered by agriculture: plenty of room for future strong concentration of agricultural holdings with positive impact upon profitability.

Opportunities offered by crises: pressure to adopt valid solutions.

Unused tools: legislation for Land Consolidation.

5. Infrastructure

Beginning with Aschauer (1989), [2] there has been resurgence in the debate about the productivity effects of infrastructure. This debate is reviewed in the World Bank's World Development Report (1994) [11] which finds a large range of empirical results on the importance of infrastructure for economic growth, with estimates ranging from no effect, to rates of return in excess of 100% per annum.

There has been also generate models, Baro models, of economic growth proving that the impact of infrastructure on GDP growth turns out to be substantial. Another models shows that is an optimal level of infrastructure which maximizes the growth rate; if infrastructure levels are set too high they divert investment away from other capital to the point where income growth is reduced.

Considering the long run positive impact of infrastructure on GDP per capita as a fact and the very poor infrastructure in a country like Romania, about 200 km of highway, investments in infrastructure are obviously unused tools and, at the same time, viable tools due to financial support offered by EU (about four-billion) and the resources that can be mobilized from international institutions such as EBRD, EIB and World Bank and that is not all. Today, the private sector is a significant participant in many infrastructure industries globally, and its role is likely to increase further because of the huge investment, technology, skills and management needs in developed and developing countries alike.

The lack of resources for infrastructure is not in that circumstances an excuse for governments for the poor development in this field but corruption is. So the crises can be an opportunity for Romanian economy because, at the pressure of the electors, with a lot of more vigilant eyes on government acts, corruption should be diminished and correct infrastructure contracts are signed. A consciously unused tool is the law of public procurement, adopted indeed but avoided many times.

Opportunities offered by infrastructure: positive impact of infrastructure on GDP per capita.

Opportunities offered by crises: diminishing of corruption.

Unused tools: correct application of public procurement law.

6. New Source of Energy

Investment in new source of energy is an anticrisis solution embraced of all nations.

We find the reasons for spending anticrisis budget to encourage production

of green energy in the new model of sustainable growing.

Another reason is that there are many energy sources today that are extremely limited in supply. Some of these sources include oil, natural gas, and coal. It is a matter of time before they will be exhausted.

Estimates are that they can only meet our energy demands for another fifty to seventy years. So in an effort to find alternative forms of energy, the world has turned to renewable energy sources as the solution.

There are many advantages to the use of renewable energy sources. There are also some disadvantages. The fact is energy demands will continue to increase. Through research and development, as well as new technologies, the hope is many of the disadvantages of renewable sources of energy can be eliminated and we can successfully incorporate it into our energy supplies.

Under these circumstances, the Government has to invest in the future but they also have to face the opposition of business leaders and the population. Business leaders have long argued that they cannot do better by the environment without adverse consequences for the economy. It seems that hardly a new environmental regulation is considered or passed into law without industry executives complaining that it will render them uncompetitive, force them to close plants, or compel them to delay or cancel planned projects. The public has to choose between the goals of protecting the environment or jobs.

We find interesting articles that show the fact that working for the environment is a growing source of jobs [5] but others that show a very small job impact. [8]

With or without job impact this investment has to be done and financial crises is a chance in this respect, because states have another type of support under crisis conditions.

For Romania the financial crisis is a chance in this field too because, at the same time, important sacrifices, the government can make important changes in the structure of energy production.

Unused tools in this respect are the fiscal tools.

Current tax and subsidy systems discourage job creation even as they encourage resource consumption. A key ingredient in shifting the economy to a more sustainable footing is phasing out current subsidies favoring polluting industries that use natural and financial resources inefficiently. [5] Even more important is restructuring the tax system. Raising taxes on resource consumption, pollution, and waste generation would make resource efficiency, renewable and "clean" production methods more attractive propositions. Deploying these tax revenues to finance national health or social security funds that are now typically funded through payroll taxes would help lower indirect labor costs and could boost job creation without hurting workers' interests.

A new economy that provides sufficient employment without exacting massive environmental damage is possible.

Opportunities offered by new sources of energy: future opportunities.

Opportunities offered by crises: voters' support.

Unused tools: Raising taxes on resource consumption, pollution, and waste generation.

7. Conclusions

Romania's economy has a strong pool of growth covered by real sources of financing that request government attention.

The chance will be translated as hope that our authorities will not waste this favourable context for restructuring.

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