

## The Romanian economy may be on the slope?

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Romania is a complex country with diverse problems and complex possibilities. The seventh biggest country of the European Union has political, economic and social, cultural diversity. Romania can have benefits, advantages from this situation but disadvantages too. However the practice has showed us, that until the Romanian transformation there were rather more drawbacks for Bucharest, and there were just few years in the middle of the first decade of the new century, when Romania could leave on the way of the real development. If the global crisis didn't intervene, the emerging way of Romania could be other towards the evolution, but it has already stayed a theory.

Why did the economic processes proceed like this? What kind of invisible problems did the crisis bring up, what Romania must face up to them? What kind of changes can Romania have to make for the sustainable develop in the future?

Key words: Romania, economy, labour market, competitiveness, foreign direct investment, labour outflow

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As I wrote at the introduction, Romania has got many problems on many areas of life, while it has been thought since 2004-2005 and even having got the membership of the EU, that Romania could make a sustainable and long term economic boom (Momete, 2007, p. 2052-2056. & European Commission, 2007, p. 6.).

First of all, I will write about depression after leaving communism and the later recovery that let us know a starting point of recent process, what hits our eastern neighbours.

Then I will detail the affects of the crisis, why and how did it happen in Romania, what kind of economic processes have met and how they can weaken the possibility of recovery. Finally I would like to contribute with two alternatives as possible solutions to some Romanian problems.

Romania didn't seem a country by the end of the communism in the other countries to be able to follow the neighbours (Hungary) or the further countries, which belonged to Eastern Bloc (Poland, Czechslovakia)<sup>1</sup> (Zahorán, 2010, p.3.). The Romanian communism was a state-system as Joseph Stalin imagined it. A terrible dictator, called Nicolae Ceausescu headed it, his heritage is able to poison the political, social and economical life, even the ability of the cooperation among nations. Because while he was able to create a total shortage economy with mindless investments in the heavy industry, on side of the social policy he mixed the theory of communism with brutal nationalism. Its first target was the Hungarian minority in Transylvania. But he didn't forget the special German minority, the Saxon either (Hajdú, 2006, p.9.). The number of Saxons had been halved until 1989, and then a few years later they disappeared fully with their 850 years-old culture.

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<sup>1</sup> Hungary became a republic officially on 23 October 1989. Czechoslovakia became a republic after Velvet Revolution on 29 November 1989. The Polish transition started earlier, but it's difficult to say a divide day, because there are more ones. It was longer, but the first "half-free" elections were organized on 5 and 18 June 1989. If we compare the Romanian Revolution in Temesvár (Timisoara, Temeschwar) with László Tőkés's head, that started on 16 December 1989, and just after that the countryside movements and revolution in Bucharest began in the second half of December. Struggle to the power can suggest many unexplained questions eg. so called "Black March" in Marosvásárhely (Tirgu Mures, Neumarkt am Mieresch).

This loss is unaccounted for Bucharest because of their work culture or the potential FDI, what could have come from the area of German languages (Cziráki, 2006, p. 194-197.).

From view of the economy we can find much imbalance situation. First, Romania was joined from three parts after the First and Second World War. The richest one, Transylvania and Banat have got more or less western cultural, social and economic milieu. The second, Wallachia is poorer, but it has got important commercial and raw material processing industry capacities and possibilities. The capital, Bucharest is situated here as well. And the last one, Moldavia is the poorest region between the Eastern Carpathians and the eastern state border (Réti, 2004, p.19.). The different developed territories have become more uniformed since 1945 to the detriment of the richer lands and in favour of poorer region<sup>2</sup>, but this “triad” is observable till today. The unification has changed since 1990, because the areas are relative developed or have potential developing capability (especially the capital, more cities in Transylvania and less in Regat) developed as an enclave, but the other in generally rural lands could not grow.

The social changes tax the patience and problem tolerance ability of Romania and the Romanian society materially. On the one hand the exodus of the young generation began to West to look for work before the accession to the EU. They got to know the Western-European work style and level of the wages. Their children are born abroad<sup>3</sup>, and they go home just as visiting or for a holiday.

But this new blood will miss for Romania in the long term<sup>4</sup> (Bogdán, 2010, p.4). In parallel the elder generation stays at home<sup>5</sup>, and young people, whose parents are abroad, have trusted to their grandparents (or to nobody)<sup>6</sup>. This is a serious problem to Romania, even the home-sent-money is a really huge amount for the families and for the current account, too. But it isn't possible, that they come back from the West, and this statement is really true for the second Romanian generation, who has been already born abroad (Bogdán, 2010. p.4).

But there is another problem, what is serious for the Hungarian and Romanian simultaneously. Ethnic compound of the society changes in parallel of aging. The decrease of Romanian population isn't so drastic, because the birth rate of gypsies is in excess of the other's. But this process excites strain home. We can see some examples in September in France that they have been sent from home. The French government could do it by rights, because these gypsies had stayed around Paris without administration. They couldn't certify to be able to work, and the law of Schengen let for instance Paris to send them back (Hollinger, 2010.).

### Upswing in the mid-2000s

Surprising or not, the mid-2000 years were the “Golden Age” for Romania after the Ceausescu-era (Sinhuber, 2007, p. 4-5.). The general possibilities of the Romanian membership are the free movement of people, goods, services and capital could help Bucharest to generate a perceptible growth (the free movement of these factors of production could stimulate it much better than the amounts from Structural Funds or the Regional Fund). The most important indicators improved, and the changes were perceived by the society, so the index of plausibility and eligibility of EU was high.

The Eurobarometer made a research in April-May 2007 and published it in June about the rata. After the accession Romania was the new membership, who answered that EU is a modern (81

<sup>2</sup> Same development plans were applied to all counties in 1976. The plans and ideas were written in the documents of National State Unified Plan. It led to huge and terrible distortions.

<sup>3</sup> It is very true, that on 1 January 2009 the very first child was Romanian in Italy but in Spain as well.

<sup>4</sup> In 2009 more than ten thousand Romanian babies were born just in Italy.

<sup>5</sup> As the report of Caritas Romania, an Italian civil endowment, 62 percent of Romanian, who work abroad, wouldn't like to go home. They just imagine their and children's life abroad.

<sup>6</sup> Új Magyar Szó, an Hungarian weekly newspaper in Romania, has got an interesting article about Romanian employees abroad. Sociologists made the “phantom picture” of an average employee, who works not home country. He is between 26-35 years old in general, and skilled or graduated.

percent) and democratic (82%) institution. And Romanians refused that statement principally that EU isn't efficient (just 16 percent of the asked people said it). For another question, what EU means to you, Romania answered in the largest percentage: democracy and economic prosperity. And next one, a good decide was to access to EU, Romania gave positive answer in the largest percentage with Polish people, too.

We examined similar questions in spring 2010, can say: Romania replied the strongest yes for the accession again (but it is true, the membership wasn't supported by so many people in 2010 than in 2007). But it is really interesting, that Romanians prefer EU as democracy and economic prosperity to free movement, what is a real benefit for Romania. In eleven countries EU is synonym with the freedom of traveling, studying and application for a job. We can explain a bit, that EU could infiltrate to the everyday life in the case of the old members, but eight countries from these elevens accessed to EU in 2004 or in 2007. It's also important, that the initial enthusiasm and expectancy for EU abated, now 50 percent of the people are thinking about EU as a good thing. With this result Bucharest is the eighth in rankings, but it is the third, if we regard just the group of the new member states. Now, let me see in the next, why did the Romanian society think about the accession in 2007 was a good, beneficial step.

The GDP rata what show us the economic achievement, didn't decrease under five percent between 2001-2003, but between 2004-2008 the average was 6,85 percent<sup>7</sup> and just 2005 year was weaker because of the general election of person of the president. Romania could catch the 42 percent of the average of EU with this economic growth and qualitative development, but the reason hides rather differences according to regions.

The other very important index for Romania is the inflation. The long term lack of goods brought on a high inflation rata, and it could be pushed off till mid-2000s to one digit (first the Romanian inflation rata was 9,1 percent just in 2005). Since middle of this decade it stabilized about six percent, but this may be a phenomenon what appears together with the economic increase.

We can approach this question from another side. According to Romania – European Community Partnership Agreement and the Central European Free Trade Agreement since 1997 the goods have been moved free and without obstacle, that affected inflation. So an average citizen can feel the positive affect because of free movement of a production factor. The prices of goods and services decrease when the market was become free. It is a beneficial affect of the common European market.

The next question, what concerns many Romanian citizens, the problem of unemployment. One of the most important promise on general or self-government election is reduction of unemployment and expansion of employment. Those huge heavy-industries, was dreamed by Ceausescu, must have been axed and demobilized, and the employers must have been discharged. If we compare its volume with the other transformation countries, we can say, this process created a huge unemployment. With numbers: about 10.500 thousand people worked in 1991 and 54.000 persons were unemployed.

The most difficult year after 1990 was 1999 after cessation of the heavy-industry, the manufacturing industry with their week quality products and the inefficient agricultural co-ops, when the employment stabilized around 8.300 thousand people, while the unemployment caught his record; at least 2.500 thousand people didn't have any work (Sánduly-Szabó, 2004, p.181).

The unemployed could find work neither on public sphere (even its redundant numbers should be rather decreased) nor by the new multinational companies. Accordingly mass of the Romanian employees tried to find new job and new life abroad before accession to EU, and this process has just strengthened since 1. January 2007.

This process has got many factors, but if we analyze the macroeconomic data, it is clear, that the employment increased, the unemployment decreased a bit, but one of the most important index for Romanian workers is the gross average wages and earnings doubled to 4828€. So we can tell

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<sup>7</sup> The Romanian GDP changes was compared with the year before: 2004: 8,5%, 2005: 4,2%, 2006: 7,9%, 2007: 6,3%, 2008: 7,3%

about the earlier years of Romanian labor market that in parallel with outflow of Romanian employees the indicators of labor market improved while it has become base of demand. Thus the doubled earnings are equalizing the gap of number of the workers, and it strengthens the statements of the neoclassical and monetary economics. But the economics will not be able to explain in the future either, that the unemployment rate is favorable around six-seven percent, but in long term Romania lost its best citizens and employees. So this loss will affect growing of the country adversely. It is enough just to think of one data: the Romanian people in Italy as employees produce 1,2 percent of the Italian gross domestic products.

### Negative effects in the economy

The positive and negative processes were noticeable in Romania till 2008 as to macroeconomics.

Volume of the FDI to Romania was favor. It had two reasons. One of them is more general, so it wasn't typical of the Romanian economy. The global economical prosperity attracted the investments, even it was heightened by that fact, that Bucharest liberalized its whole capital market because of the membership. That is to say, all obstacles were demolished, what had been against of capital.

The other one pertains to just Bucharest specially. Romania had relative low labor cost level, it could still strengthen the inflow of FDI. Add to that billion euros, what were spent home by employees from abroad, increased the purchasing power of Romania. The chance of the inflow FDI was grown by it, because it means a higher demand for the produced and distributed goods, so it is worth to produce to Romanian market.

These favorable processes were weakened by that fact, that considerable citizens left Romania. It has had serious consequences, because the wages jumped up just in few years. From 2004 to 2007 the average income doubled, and in parallel of course it obstructed the competitiveness of the country. Even it is true, if we consider, which part of the Romanian society stayed at home. The reports show us, that the unskilled, unqualified workers stayed in Romania without any degrees. It could have been disadvantage for them, if the number of companies with their supplying new jobs had fallen back. But it happened just due to affects of the crisis.

Since end of the third quarter of 2008 the second mentioned factor, the growing tendency of the FDI ended because of the higher income. The investment susceptibility fell back drastically, though it is true for the global economy as well, but especially for the European economy. In addition to the recent Romanian exodus is streaming abroad now too, there isn't any chance that the wages can reduce. The labor market has stayed a supply market in Romania.

In addition to the spending money is dramatically lower than earlier because of the crisis and more and more families live abroad. We can attest this assertion, if we examine the next process. In 2009 just 3,5 billion euro was spent home by the Romanian employees, who works abroad. This amount is less by 35 percent compared to last year<sup>8</sup>. Or on the other hand, the purchasing power decreased in the country.

Since 2009 this process what is strength of Romania turned to opposite direction. Last years the favorable wage level was coupled with skills labor force. Both of them are going to worse situation because of the crisis in from of the Romanian competitiveness.

The possibility of state role fell off because of the bad macroeconomic situation from view of the state. Bucharest could keep the deficit of the budget under three percent of GDP as written on the Maastricht criteria, between 2002 and 2007 it didn't grow over 3 percent. But the crisis showed the problems, and the deficit increased more than eight percent<sup>9</sup>. In the meantime the public debt

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<sup>8</sup> But it is fact as well that Romania is in the first ten countries according to account of this home-spent-money.

<sup>9</sup> The main problem is the large loss of revenue. The recent Boc-administration has to set the side of expenditure of budget. This effort has gone opposite of the civil servants.

jumped up, and it doubled. It is important to mention, that one part of the debt is because of the recession. The Romanian politics is responsible on the other part., because they wanted to perceive the trouble too late, and just later one year after collapse of Lehman Brothers started to put the budget in order. This president election was caused of this one year slip. During the campaign and election the economic, financial and structural problems could not be attended.

Now, let us support these statements with data. We need the valid of gross average income that can mean competitiveness advantage or disadvantage for the economy. In addition to the change of the FDI inflow is also necessary, it is another measuring instrument. And we have to examine the change of the current account, because how the change of home-spent money can influence the current account<sup>10</sup>. Of course this text uses GDP as the growing index.

The Romanian economy could develop by six percent between 2000 and 2008. This is an even considerable solution, if we know that Romania is an emerging country.

In parallel the wages grew, the employees were given surplus from the produced. This is true not just for the earlier showed average income, but for the minimum wages as well. It's really important, because it also determined the wages of civil servants. The minimal wage increased by 5,6 times from 2000 (when was just 24,53 €) to 2008 (it was already 138,6 €). Here it's very important to tell, that Bucharest enhanced the account of minimal wage in 2009 in spite of the crisis. Romania isn't alone with his step, Greece, Spain or France did it too. But only Athens and Bucharest did this enhancing without any funds and in addition to they had to ask help from International Monetary Fund and/or European Union. They could avoid the insolvency only with this help.

In Romania like in other Central-European countries the inflowing FDI contributed to the quality growing and development. Till 2002 just about 1-1,1 billion dollar capital came to Romania, after the simplified tax-system and the coming EU membership could double or treble it year by year. But in 2009 the crisis hindered its intensity, and it fell back by 55 percent. This large decrease of the inflowing FDI was unprecedented compared with former years.

And here lower intensity of FDI meets the increasing of wages that means disadvantage from view of competitiveness<sup>11</sup>. In longer term Bucharest will have to calculate on this eventuality apart from the form of crisis, as I prejudice.

### Solutions, possibilities

There can be many solutions for the problems, what I mentioned in the first part of this essay. Now I would like to show some variations that they can help to resolve this just now shaping competition handicap of Romania.

Of course the Romanian economy is neither static, it can also change, especially if the problems are realized in time and the possibilities are caught by this middle-size European country. They have got chance to fight these disadvantages off, but the new competitiveness advantage will rests on structural reforms, not on fluctuation of exchange rate.

#### *Sectors with higher added value has got the future*

<sup>10</sup> We have to examine the income row of the current account. It contained the accounts of home-spent-money. If we compare it with this Hungarian data too, can say, during years between 2007-2010 Romania had better solution than Hungary. The Romanian valid in 2007 was just 51 percent of the income part of Hungarian current account. In 2008 the scissors open drastically and the different was 87 percent point in favor of Romanian. The different was still significant in 2009, it was still 74 percent and it didn't change until the second quarter of 2010. The Romanian valid is such favor because of these accounts of home-spent-money.

<sup>11</sup> We can not repeat it enough times; it is just true, if the FDI purposes the industries with low wages and also low-added-value (European Communities, 2009, p. 67).

As it is observable in the most countries, the high wages are negative factor in the global competition only in that case, if the country specializes for labor intensive products. As earlier cited Commission Report 2009 emphasized too, labor intensive industries began their production in Romania according to European labor share.

At the same time if Bucharest wants to bring the Romanian employees back in longer term, while the government would like to keep the new employees, who just start their own life, doesn't avoid the increasing of salaries. If they choose this way, they will be handicapped in the labor intensive production against Far-Eastern countries, which have got comparative advantages in this industry (this theory has been strengthened by the well-known Romanian economist and member of the European Parliament, Daniel Dăianu too (Dăianu, 2009, p. 326-327). So one of alternatives is the next: those industries, which produce small added value in GDP must be reshaped, and at least share of so-called Medium-technology industries must be grown. Of course higher qualification is necessary, but the employees can earn more money with better skills as well. Unfortunately against this favor process, the ratio of qualified and well-paid jobs diminished between 2004-2006 in the technology industries.

### *Federation state*

The other advice can be creation of a federation state, because till today the centre government is still strong. The three plus one new regions can be empowered to wider legislator and executive power. This decision could disengage new energy, which produces extra development and of course extra public revenue for the budget.

We can mention more arguments to support our statement. First of all, it is the GDP and even important also the potential developmental ability. We examine data from 1996, then we can say, how much developed region is Romania compared to average level of GDP of EU 27 (EU27 average is the 100 percent). We can assess that in 1996 the first three regions contained two Transylvanians and one eastern region from the eight Romanian regions (of course except for Bucharest, the capital isn't in our analyses). These were the Centre Region (in official name is Centru), the Banat (Vest) and South-East Region with Romanian coast (Sud-Est). If we compare them in 2007 the first "provincial" region is the West Region (Vest) belongs to Temes – Arad – Krassó-Szörény (in Romanian: Timiș – Arad – Caraș-Severin), the second is the historical Transylvania so-called Centre Region, and the third one is North-West (Nord-Vest) with Bihar - Szatmár – Máramaros counties (Bihar – Satu Mare – Maramureș).

This isn't enough reason by itself for restructuring the state as a federation of course. But there is a stronger argument, that these three regions could have by ten percent better result compared with 1996, and the other rural regions produced just by 3,5 percent better development. So we can say, the western regions could improve three times faster, and they paid also more money to the centre budget. At the same time there is a question, how much money could they receive back?

If significantly part of the consumption of budget money can be referred to federation competence, all federation government could use that money, which is produced there. It can divide the expansion of efficiency, because all groups of regions can be urged for a better achievement.

And which can the federation provinces be? It is worth to take acknowledge of Bucharest separately. The West (Vest), Centre (Centru) and the North-West (Nord-Vest) can belong to the first federation territory, because they stand on similar developmental level (a bit over 40 percent of EU27 average). The second developed region alliance can collect the southern lands near Danube: Oltenia (Sud-Vest Oltenia) and the strategic located Muntenia (Sud-Muntenia). And the third territory may cover eastern part of country with North-East (Nord-Est) and South-East Regions (Sud-Est). But the last one must be rethought at once, because the relative richer coast is together with the poorest regions.

As I wrote it, extra one region can be founded. It allows of a three-level public administration system kept the European norms. The new Szekler Development Region is in the Transylvanian Region as an extra stair of Romanian public administration system. It may be a really important

step, because Harghita (Harghita), Kovászna (Covasna) and the eastern part of Maros (Mureş) can attest not to hang from Bucharest as a matter of money of budget. While Bucharest can have less problem, because nobody complains by the government, that the centre budget underfinances the eastern part of Transylvania.

### Hungarian interests on the both parts of the border

Hungary needs to know the political, economic or social process in Romania and Budapest must be able to forecast the changes in the future. There are two main reasons of this pressure. One of them is that the Romanian economical process affects the all citizens; either Romanian or Hungarian ethnics too. The Szekler Land where Hungarians live mainly, feels the enhancing of the purchasing power, and of course growing of the inflation or decreasing of the inflowing FDI. And as not just cultural or emotional contacts but closer economic relations have been built up by Hungarian people between Hungary and Transylvania, accordingly the achievement and developmental ability of each other play important role in intensity of these Hungarian – Hungarian economic relations.

The other important reason is that Hungary has become the third greatest exporter to Romania (Budapest could overtake France and China as well) (ITD Hungary, 2010). This solution is due to the Hungarian products which flow to especially Transylvania. If the Romanian purchasing power decreases, the demand will decrease in the case of products from Hungary too. That's why Budapest has to know and forecast these processes.

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