

## THE CURRENT CRISIS IS NOT CRISIS OF THE EURO

*Interview with Ágnes Nagy*

*Member of the Board of Directors of the National Bank of Romania*

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### Abstract

Romania shows several positive results for all the economic crisis. We aim to answer the question: How could Romania reach these results? In order to explore the underlying facts, we have made an interview with Ágnes Nagy, Member of the Board of Directors of the National Bank of Romania. In the course of the conversation, we examined the measures and possibilities of the National Bank of Romania. We discussed what kind of reforms were introduced in Romania that attempt to reinforce the position of the domestic economy, what is the thinking about the current situation of the euro zone, and what is the attitude related to joining to the euro zone. Furthermore, the reader can gain insight into their approach to the problem of those who have foreign currency loan, and how they want to build investor trust.

*Keywords:* Romania, National Bank of Romania, International Monetary Fund framework agreement, Eurozone, currency loan, volatility, monetary policy, stabilization.

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*What are the main tasks and competences of the National Bank of Romania? (And how independent is the the bank from the Romanian Government?)*

According to the Law on the Operations of the National Bank of Romania, the main task of the bank is to safeguard price stability. It is in charge of the tasks related to monetary policy. In addition, it is the supervisory and regulatory authority of the money market and banking sector, it issues coins and banknotes and ensures financial stability. Its structure differs from that of the National Bank of Hungary, the members of the Board of Directors are appointed by the Parliament for a 5-year mandate and the task of the Board of Directors includes monetary decision-making, there is no separate monetary board to this end. The members of the Board of Directors are economists and lawyers, who are university professors and researchers as well.

Theoretically, its independence from the government is absolute because its fundamental law follows the fundamental law of the European Central Bank. However, independence depends on who and what ways can give effect to the letter of the law. The Chairman of the National Bank of Romania has been Mugur Isarescu since 1990. He and the directors surrounding him could manage to conduct a credible monetary policy. With this they achieved the practical independence of the National Bank of Romania.

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*What is the relationship between the National Bank of Romania and central banks of other countries, or the European Central Bank like?*

The National Bank of Romania is a member of the European System of Central Banks (ESCB), which the central banks of the European member states belong to, in this way it is connected to central banks of other countries as well as to the European Central Bank. Furthermore we have bilateral framework agreements which were entered into primarily in the area of supervisory functions. We conclude agreements with central banks of those countries whose commercial banks have a determining role in Romania.

*We can consider the lei a stable currency, by what measures could you achieve its stability?*

It was impossible to make balance adjustments only with monetary instruments on the macroeconomic mix. Therefore in July 2010, the Romanian government implemented drastic fiscal and income-side changes in order to offset the existing macroeconomic disequilibrium. First of all, it meant increasing the revenues of the government which they intended to achieve by increasing the VAT rate by 5 percent. Secondly, they decreased the salaries of civil employees by 25 percent. These measure were drastic interventions but stabilized the Romanian economy. In any event, if a country has stable economic bases, the confidence of private investors increase towards the country. At the same time we can say that the exchange rate volatility is extremely high. One of its components belongs to a certain country, while another component belongs to another country (in case of the euro - to the European Central Bank). The countries know their currencies much better so they know what they should do in order to make the encounter with external currencies successful and to maintain the confidence of the actors of the money market. The needed measures were taken in Romania that resulted in the current stability.

*The rate of inflation has recently decreased in Romania, consequently the National Bank of Romania decreased the inflation forecast for this year (to 3.3 %) that has a positive impact on the economy. What were the reasons for these actions?*

Twenty-one years ago, Romania had the highest inflation rate among the former socialist countries. However, during the past 21 years, inflation rate abated to an average level. Regarding the reduction to the rate of inflation, it is not a negligible fact that the countries started from different levels. The rate of decrease was significantly larger in Romania comparing to other countries, which even started from a high inflation rate, from a lower one than that in Romania. Following a huge reduction by 2010, when we reached a spectacular result (4.5% inflation rate), the government opted to raise the VAT. This slightly increased inflation, but the fiscal inflation faded off as a result of the influence of base effect. At that time, the inflation decreased from 4,5 % to 3,4% as expected. The primary reason behind was the drop of prices of the volatility commodities. The drop in prices of basic food products, especially the drop in price of egg, fruit and vegetable categories was typical. In 2011, the prices in the above categories have decreased by over 12%, and these abating prices had a great influence on the inflation because the food products are 33% of the Romanian consumer basket. However, for this, the reduction in inflation doesn't necessarily mean a change in competitiveness, more was it caused by a good yield in agriculture that year.

*How is Romania going with the convergence criteria, how are the chances of accession under the present circumstances?*

Romania is steadily and consistently maintaining the predetermined date of 2015 since joining the European Union in 2007. Romania must pursue the reforms that are required to joining the euro zone in order to enhance the country's fiscal and economic competitiveness. This is a necessity regardless of the actual accession will happen or not.

*What do you think about the euro crisis, how serious is it and is there a chance that the euro will finally fail? Can financial measures for crisis management prevent recession or is that too late?*

I think the euro zone will not fail, but it will expand. It will do so for two reasons. First, Europe can thrive better amidst the world economic competition having a common currency than the countries having their own currencies. Secondly, the recent crisis is not the crisis of the euro. Allegedly, Greece's battered conditions resulted from the introduction of the euro. Though in 1933 they were in a similar situation, they couldn't finance the national debt and euro did not exist that time. Therefore the national debt can be associated with the economic culture of a given country and not with the currency.

*Continuing the previous train of thought: If China decides that it takes part in aiding the euro, how big economic and political influence could it gain in Europe? What could be the consequences of such in the surrounding countries?*

There is an enormous expansion in China. The numbers themselves, however, do not present the actual situation. We must analyze also background structure: the currency is not absolutely liberalized in China, and the pricing of goods is not driven by the market. The Chinese Communist Party decided that it supports all factories producing for export, for example with the reduction of the price of the electric energy, tax cuts, etc. As such, the prices are kept low by administrative measures. So if we say regarding China that it is good that they come, we have to look at closely what they come with. Their investments is only one side of the coin. The other side is what they will expect in return. Will they bring in more goods at very depressed prices? I think that the leaders of the European Union will be able to manage these problems in the near future under adequate guaranteed conditions.

*Without the new 8 billion EU-IMF aid package (the third, accepted in October, which has not been transferred yet, as the fulfillment obligations had not been accepted by Greece) Greece could default on its debt until the end of December. In your opinion if Greece decides or is reduced to quit the euro zone, what kind of effect will this have on the euro or the economies in the region?*

Certainly it is feasible that they secede but it needs to be investigated whether the secession will land the country into favorable position. If Greece switches to another currency, it will not change its dead-end position because its liabilities have to be redeemed in euro. Its resources will not grow either, as market investors will not invest, as they will not have more confidence to invest just because the currency of the country had changed. Moreover if they secede, they need to have the people understand that the secession has its costs. That is why I think that the secession is not the right track.

Currently they asked the previous president of the central bank for prime minister thereby signal the money markets that they are determined to implement those urgent reform measures in Greece that they cannot avoid.

*Has the economic crisis caused credit crisis in Romania as well? If yes, to what extent do the Romanian banks, the national bank itself contribute to help the currency credit debtors?*

The indebtedness in foreign currency exists in Romania as well. The indebtedness in euro is typical rather than in Swiss franc. Almost 60 percent of the debtors have claimed euro credit and the other 40 percentage have indebted mainly in domestic currency. Whilst the foreign currency debtors suffer from exchange risk, the burdens of lei debtors are higher because of the rate of interest of domestic currency loans. So, if we express the cost of both types of debtors in lei, there is no big difference between the two. Thus the main problem is the indebtedness, regardless of the currency. However, in my opinion it is not a solution if we single one debtor out and give to him or her administrative aid. We should handle the problem uniformly. The central bank is responsible for managing the monetary policy.

The rules, approved by the National Bank of Romania in 2011, regarding the consumer credit have precisely defined the conditions of borrowing. They determined, inter alia, the period of credits, and their percentile rate corresponding to total value of borrowing as well. Besides the consumer credits, the indebtedness in long term credits is also significant. But presumably in the medium term Romania will become a member of the eurozone, and hereby the exchange risk of long term credits, which was borrowed in foreign currency, will disappear then.

*Various analyses regarding investments find Hungary especially risky. How safe can investors feel about their interests in Romania? Could the National Bank of Romania improve their comfort level?*

The central bank and the government of the country should together achieve the economic stability of a country and thereby the positive outlook of investors of investing in the country. This task is not easy neither in Romania nor elsewhere. Romania's vulnerability comes from its need of external resources because the household saving rate is low. Still, as a whole, the country's money market can be evaluated favorably as a result of the standby agreements concluded with the IMF (International Monetary Fund) in 2009 and of the implementation thereof by Romania. In March 2011, Romania has subscribed a new loan contract that aimed to assure market investors. The 3.6 billion euro aid functions as a kind of reserve; the government does not aim to draw down this money. In the long run, internal stability cannot be achieved from external import, therefore the Romanian government and the National Bank of Romania have to use the remaining period to ensure credibility of the domestic market. In my opinion, both the Romanian government and the National Bank of Romania are committed to this extremely important task and they consider it as their number one mission.

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