

# **ROMANIAN ECONOMIC AND BUSINESS REVIEW**

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The *Romanian Economic and Business Review* is the first peer-reviewed Romanian journal in the field of economics and business. This journal intends to provide a forum for academic analysis of the economic phenomena and institutions affecting the world economy in general, and Romania, in particular. *REBE* examines a wide variety of phenomena related to economic growth and business development and attempts to publish high quality research focusing on the role of institutions and public policy, within both a national and international context. *REBE* encourages cross-disciplinary research work of Romanian and foreign scholars.

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# ROMANIAN ECONOMIC AND BUSINESS REVIEW

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## THE ROAD TO 2057: ISSUES AHEAD EUROPEAN UNION

*Florin Bonciu\**

In March 2007 experts, politicians and general public had a good opportunity to reflect not only upon the achievements of the past 50 years, but also upon the prospects of the next 50 years.

If one looks how the idea of “an ever closer union” of 1957 that had among the few clear objectives the establishment of a customs union materialized 50 years later into a 27 member union, with 13 of them enjoying a common currency, common policies and a common market the conclusion is that a 50 years forecast is a risky enterprise. Not only because the entity under study is so large and complex, but also because its environment, the circumstances in the global economy are changing in ways difficult to imagine.

On this 50<sup>th</sup> celebration the European Commission tried anyway to identify if not the looks of European Union in 2057 then at least the issues laying ahead. And the somehow worrisome fact is that out of 4 issues (Facing globalization, Global warming, Europe in the world, Encouraging democracy and participation), 3 refer to aspects more or less outside EU control and only the 4<sup>th</sup> one is within.

As for the first issue (Facing globalization) it is ironical that some decades ago some feared that EU would become “Fortress Europe” and would raise walls around its boundaries that would affect world trade, among other flows. On the contrary, today it is EU that fears the rest of the world and is really affected by the world coming upon its “Single European Market” from all directions. In the past decades, by deepening integration EU got rid of internal barriers. Now, under the pressure of globalization, EU has to think about finding the right way in designing acceptable barriers towards outer world. Can this be done? Maybe as non-tariff barriers, maybe by championing environment protection rules, maybe by human rights related regulations. From the standpoint of 2007 EU is in defensive vis-à-vis globalization and it is still thinking about how the Lisbon Agenda dream may come true. Due to its long history and huge expertise in so many fields it is very likely that European Union will find a modus vivendi with globalization. But one may expect that this solution will imply a lot of changes in directions required by the global environment and to a less extent function of its own desires.

The global warming is even a more complicated thing. In fact, for the moment in EU there is a lot of drive towards action, towards offering an example for the rest of the world even at the price of badly affecting the European industry. Unfortunately, the current attitudes are no more than wishful thinking. The risk is that the world of today is really inter-connected and the industrial activities of one country or region cannot be limited to that area. Under these circumstances, it is very difficult to see how any EU decision on fighting global warming will be immediately and fully replicated by China or India, to name only two significant global players of the coming decades. And who can guarantee that if EU really applies the strict environment regulations the European companies will not relocate to countries where those same rules are not applied? The

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risks of global warming are real and terrible but from a theoretical point of view the only solution is to find new, more environmental friendly technologies that will be made available to all countries. Sounds a bit like utopia? Yes, but the risk is so high that only such an utopia can be a real solution. Again, from the point of view of this issue, EU will depend a lot on what others will be doing and will have to allocate a lot more on research and development in order to offer the rest of the world solutions and not only its good will. Till then, the commuting of EU officials between Brussels and Strasbourg is polluting more than a number of small countries.

The problems related to the 3<sup>rd</sup> issue (Europe in the world) is also a sort of irony of fate. Because this puts EU in the position of being a victim of its own success. As of 2007 EU counts 27 member countries, with more than 480 million inhabitants and by adding the GDP of its members is the first economic power of the world. The irony is that this position also implies a much more prominent role in the world affairs. If it is that big EU has to act in the global arena. It needs a single voice in significant situations, a consistent position and even a military force. All these have long been debated but results are still to be found. The recent individual responses to energy issues shows how far EU of today is from such a single voice. Thinking about the EU role on global arena another aspects appears. EU has always manifested as a champion of humanitarian assistance and development aid. Can this be done efficiently in a world of increasing competition? Is there a risk for EU of becoming a sort of UN in its foreign affairs dimension? For the moment it is difficult to answer these questions, but EU has to dedicate time for finding the right answers. The other actors in the world economy will put a lot of pressure on EU in the coming decades and maybe this 3<sup>rd</sup> issue will be the real resilience test.

The 4<sup>th</sup> issue is the only one internal to EU (Encouraging democracy and participation). That does not mean it is any way easier. EU is trying to form a 'de facto' empire based on democracy and soft power. Its citizens are not entirely convinced for supporting this idea and the goals of both transferring more powers to EU institutions and involving more the citizens at the same time are sometimes contradictory. The EU of the coming years has to change in order to compete globally but how to do so in a democratic way? The European Parliament has more power but the citizens are coming in small numbers to European Parliamentary elections. Is this good for democracy? Can this be changed? And what about the Internet revolution? Will European citizens remain European or they will migrate to Second Life and become virtual global citizens?

These thoughts are not meant to be pessimistic. In fact they are anxious with expectations. Because the road from now to 2057 is a road to be discovered, a road of great expectations, great adventures and unthinkable challenges. United in diversity but still Europeans we can succeed. Let the journey begin!



## CAN THE EU BECOME A GLOBAL PLAYER?

Gheorghii Prisacaru\*

### Abstract

*The birth of the European Economic Community and the EURATOM represented the materialization of a new and brave idea about the role which the economical integration could play in insuring the peace, stability and prosperity of the people in member states. Nobody can make today abstraction of the presence and the role of the EU: an area of great economic, geographic, demographic and political power. Europe should also act as an important player in finding solutions to major problems such as: terrorism, climacteric changes due to global warming, ensuring energy supplies, diminishing social and economical disparities between and inside states.*

I would also like to greet the organization of this symposium, on the occasion of the 50<sup>th</sup> anniversary of the Treaty of Rome. The birth of the European Economic Community and the EURATOM represented the materialization of a new and brave idea about the role which the economical integration could play in insuring the peace, stability and prosperity of the people in member states.

The treaties were signed only by six western european states. The historical conditions put Romania on the eastern side of the “iron curtain” and made it unable to participate at the west european projects. We are, now, amongst the righteous members of the EU and it is appropriate to celebrate the event that gave birth to the most complex economical an political structure on the European continent. And this symposium is most adequate as it is organized by the Faculty of European Studies.

I would like to briefly debate a subject of major interest, can the EU become a global player? This question is most welcome after the sever crisis caused by the failure of the referendums in France and Holland about the European Constitution, which made some analysts, like Werner Weidenfeld from The Institute of Security Studies of the EU, ask themselves if it is still possible to talk about the role of a “global player” of the EU. Personally, I am not amongst the euro-scepticals who doubt about the capacity of the EU to play an important role in the world.

There are positive premises that the Union could play such a part, and also a number of conditions that should be fulfilled by the EU for reaching this objective.

Next, I will try to enumerate a few factors which contradict with a simple, pessimistic approach.

First of all, the EU has gained in time an important role in the international relations.

We are not anymore in the early `70s when during the Cyprus crisis, being asked by a journalist “why doesn’t US associates Europe in solving this problem?”, the US Secretary of State, Henry Kissinger also responded with a question: “who do I call in Europe?”. This answer ment that as long as he didn’t have a credible interlocutor, the voice of the EU couldn’t matter in the world.

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Since then, the evolution in the components, nature and politics promoted by the EU, and also the political changes in the Central and Eastern Europe brought changes in the role of the Union in the world.

Nobody can make today abstraction of the presence and the role of the EU: an area of great economic, geographic, demographic and political power. The Union is the greatest internal market in the world, and the Euro – as common currency – gained a global importance. The gross income of the EU is similar to that of the US and its part in the world economy is over 20%. The most important economic partners are the US, Japan, China and Russia. Next to the economical reasons must be mentioned the cooperation between other countries promoted by the Union, like the human rights and the independent state. Finally, the Union is also a demographic power. If countries like Croatia, Macedonia and Turkey will join the existing 27 countries in the Union, the total population will be over 550 million, double the population of the US. If we add to this the fact that the Union changed from an economic structure to an economical and political structure, and also the fact that the Union is willing to negotiate, it's obvious that the EU has a major potential that qualifies it to play an important role in the world.

Secondly, the EU must face some great challenges, from the inside and also from the outside, and as a world player.

The constitutional referendums in France and Holland showed that the power of convincing is missing to the political elite of some european countries. Supporting the integration process will not be obtain automatically, through non critical positions, since the ambitious objectives must be explained widely to the public. Although, the population will not support the european projects, no matter how generous these would be. In the same time, we must remember that other projects failed: the creation of an European Defence Comission, the Fouchet Plan, the European Constitution elaborated by the European Parliament in the 80's. Although, in the end, these failures were overpassed through cooperation, tenacity and political compromises. That's why, the problem of the Constitutional Treaty should not be so dramatized. There can be found solutions for relaunching the Constitution, especially that nobody denies the necessity of growing the cohesion and efficiency of the Union. From this point of view, the Declaration from Berlin says that the time limit for reforming the european institutions in June 2009, the date of European Parliament elections.

In the world, Europe must face a new shaping of the relations with the US. After 50 years of relatively stable relations, they entered in a phase of incertitude. And if, in a specific period, at the beginning, and in the conditions of the Cold War the process of european integration enjoyed the support of the US, the events after September 11 showed that today, the US need the support of the EU which is one of the few suppliers of stability and security in the world. In these conditions, the EU doesn't comply anymore with the statute of "junior partner" of the US, trying to find answers of its own at the challenges put up by the world and to be considered an equal partner, whose opinion should be listen to. I don't see an Europe opposed to the US, but an equal and respected partner. The last position the US administration had on the nuclear politics of Iran and North Korea, the UN reforms or the climate changes seems to point to a change of attitude towards Europe, pointing to a rethinking and consolidation of transatlantic relations.

In these conditions, a new question appears: Is, today, the EU a global power? I

think the answer is, for now, negative. But, someday it can be.

It is necessary, first of all, a coherent external and security policy. The Iraqi crisis clearly showed that, without such policy, the US promotes “post-factum” consultations of an action in force, following its own interests in the light of unilateralism, or it uses its relations with some EU countries. If the EU had a common, coherent position in the Iraqi problem, before the hostilities begun, we can presume that the importance of its opinion would have been different.

That’s why, the famous phrase told by French president Jacques Chirac, “La Roumanie a perdu un bon moment pour se taire” for accusing its pro-american position was lacking the fundament. I think if the EU had a common position in this matter, elaborated in time and publicly exposed, Romania would have – in that period – supported the EU point of view.

From this point of view, the creation, by the Constitutional Treaty, of the position of Minister of Foreign Affairs, assisted by a professional diplomatic service, could be the solution to the problem.

It is also needed to consider the responsibility of the EU as a security factor, purpose in which a good balanced strategy for improving the performance of the EU is much needed. This means that for becoming an important player in the world, the EU must elaborate a strategy to respond to the internal and international challenges. Only if the EU will reform and will show more political initiative, it will be able to act, in the actual global conditions, as a global player.

Following its enlargement towards east, the EU is heading to regions with great conflict risk, like the Balkans, Caucasus and the Northern Africa. Another strategic region for the EU is Asia, where it intends to establish strategic partnerships with China, India and Japan. Because the number of global players, in the future multi-polar world, is constantly growing, and the sources of conflict also grow in numbers, the EU needs its own strategy for strengthening its influence in the world.

Finally, “the leadership” is an essential component which needs to be taken into account in an extended EU. The european power should also be efficiently organized to be able to play an important role in the world politics. We need to add the fact that, an Union of 27 countries will be able to act together as an world player in the Foreign Affairs, security and defense matters if this concept will be associated with a continuous improvement of its civilian and military capabilities, and aslo its capacity of reaction in crisis situation. To be a good security provider, in the region and worldwide, the EU needs to develop its strategic profile. According to some analysts, the lack of a strategic thinking could be the “Achilles heel” in the foreign affairs and security politics and in becoming a global player.

In these conditions another question is rising correspondingly: *Is UE today a global power?* For now, I think the answer is negative. But she might become one.

Heretofore, a EU coherent security and foreign policy is needed. The Iraqi crisis has shown clearly, that in the absence of this policy the United States either promotes negotiations after taking action pursuing their interests in an unilateral way, either selectively using its privileged relations with certain EU member states. If EU had shared a common and coherent position in the Iraqi problem, before launching the hot war, predictably the weight of its word would have been different.

Therefore, Jacques Chirac’s famous sentence saying that “La Roumanie a perdu un

bon moment pour se taire” when condemning its pro-American position was made without foundation. I think that if the EU had a common position in this matter, elaborated in time and expressed in public, Romania would have upheld the Union’s point of view.

From this point of view, setting up through the Constitutional Treaty the EU Foreign Ministry supported by a professional diplomatic service, might represent a solution.

Concomitantly, we need to take into consideration the EU responsibility, as a security provider means by which a well articulated strategy for improving the Union’s performances in this area is absolutely necessary and up-to-date.

This means that being an important worldwide actor, the EU must draw up and put into practice a strategy that should answer to all internal and international challenges. Only if the EU reforms itself and prove more political initiative, it will succeed in playing its part as a global actor.

As a result of its enlargement to the East, the EU is heading for regions with a high crisis potential such as: the West Balkans, Caucasian and North African countries. Asia is another EU strategic region, where it wishes to set up strategic partnerships with China, India and Japan. Taking into consideration the facts that the actors’ level on the international stage in a future multiple pole world is continuously rising and that the sources of conflict are ceaselessly dividing, the EU needs it’s own strategy in order to multiply its world influence.

Lastly, the leadership represents an essential component, which must be considered in an enlarged EU. The European power must also be well and efficiently organized in order to play an important role in the world politics. It should be mentioned that a Union with 27 member states will be capable to act as a global actor in the foreign policy and security and defense area only if this concept is accompanied by a continuously improvement of its civil and military capacities and also its capabilities of response in a crisis situation. To become a good regional and worldwide security provider, the EU must develop its strategic profile. To some analysts, the lack of a strategic thinking might represent the Achilles’ heel of the EU’s security and foreign policy and implicitly in its development as a worldwide player.

Europe should also act as an important player in finding solutions to major problems such as: terrorism, climacteric changes due to global warming, ensuring energy supplies, diminishing social and economical disparities between and inside states etc.

## EUROPEAN UNION AFTER 50 YEARS OF EXISTENCE

Mihai Berinde\*

### Abstract

*The unification process has been the central point of the european political and economic history in the second half of the last century. The advances made seem today impressing and impossible to imagine only a few years ago: peace and stability have been consolidated; economic growth has continued; european citizens' standard of living has been substantially improved*

A series of events have celebrated the end of 50 years of existence of European Union in March.

Leaders of european countries have met and signed the Berlin declaration, which draws the main steps for continuing the european construction necessary in order to achieve the so much needed prosperity, peace and solidarity.

European commissioners have used this opportunity to point out both the evolution of European Union and the challenges they will face in their field of responsibility.

European youth have joined in Rome to celebrate the event.

Experts in economy, politicians, artists, scientists and professors have participated to activities organized for this celebration, to emphasize the european trends, Europe's participation to global and regional economic and political processes.

Booklets of tens and hundreds of pages have been printed and distributed to those interested, describing the main steps in European Union's history.

Eurosceptics, who are not so optimistic about european evolutions, made their voice loud and clear these days. Each of them tried to draw in his/her own way another possible path, failing to succeed in circumscribing it in the complex processes of globalization and regionalization of economic and political phenomena.

What can be said, based on the achievements of european construction, is the fact that European Union represents a unique experience of peaceful integration and cooperation among former rival and competing states.

The unification process has been the central point of the european political and economic history in the second half of the last century. The advances made seem today impressing and impossible to imagine only a few years ago: peace and stability have been consolidated; economic growth has continued; european citizens' standard of living has been substantially improved.

The common currency is a historical success and common policies defend the principles and interests of Europe.

European Union is today the world most important economic actor, as well as the biggest donor for development and the most important supplier of international aid.

Also, European Union plays a crucial role in spreading stability in its neighborhood, especially through the enlargement process toward the central european and mediteranean countries.

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As far as external relations are concerned, Europe makes significant steps toward a European foreign policy.

These days many words have been said and written about what is Europe today, but the topic is far from being exhausted. Therefore, I do not intend either to make an exhaustive analysis of the 50 years of history in Europe, but I will remind only certain moments that I consider relevant.

Thus, after signing the Treaty at March 25, 1957, member countries play the most important role in accelerating the process of economic integration across Europe.

In 1968 a custom union is achieved among member countries. This stage represents the liberalization of intra-union trade, by eliminating custom duties and non-tariff barriers. Thus, a common custom tariff has been adopted and the germs of a single trade policy vis-à-vis third countries arise.

Indeed, in 1973 trade policy is transferred from the national competence of member states to the level of European Commission. This stage had a huge importance in the future economic evolution of Europe, because it led to the adoption of approaches specific to trade negotiations, both with the rest of European countries and in the field of multilateral trade relations.

In this period European Union has been constrained to solve certain structural economic problems. Thus EU has regulated its trade relations with third countries in the trade with textile products, supporting the Multifiber Agreement within GATT and bilateral Agreements with exporting countries.

True to the market mechanisms, the European Union did not hesitate for a moment to adopt and to put into use the Davignon Plan of restructuring of the ferrous metallurgy industry, so that even in this field, the quotient between the offer and the demand of goods would assure a solid development of this economic sector. This process implied, starting with 1978, the financial sustaining for the limitation of common production capacities and the reduction of imports in order to assure the necessary conditions for a real competition.

The creation of the common agricultural policy, which spun from the principle of assuring minimum guaranteed yields for the European farmers, has been a difficult process, requiring complex negotiations at community level and especially at international level, as a follow-up of the massive subventions introduced for the European producers as well as for sustaining exports.

The implementation of the common policies in the fields of trade and agriculture were followed by the implementation of a set of rules and common policies concerning competition and transports.

The passage of the European Community to a new level of integration, named the "common market", was marked through the process of transposing at community level the rules from the different economic sectors.

The nomination of Jacques Delors as the President of the European Commission stimulated the deepening of the intra-European integration process, embodied by the creation of the Economic Union and then by that of the Economic and Monetary Union.

Thus, in 1986, the European Single Act is signed, with the objective of implementing the European single market, in the perspective of the year of 1993, which was aiming to put into use the four fundamental liberties of movement, notably the free movement of goods, of persons, of capitals and that of services. At the same time, the single currency

also became a reality, which brought Europe today in a position in which it can assume new economic, social and political challenges.

The Lisbon Agenda is the document that clearly defines the necessary actions that must be carried out in order to help transform the European economy into the most competitive economy at international level.

The registered progress concerning the European economic integration process has triggered important legislative modifications, including the basic treaty.

All the mentioned aspects underline the efforts imposed by the European construction process and the political will of the member states in order to achieve the new European architecture, which implied profound changes at the intra-European level as well as that of relations with third parties. All this transformed the European Union into a credible entity with great possibilities of consolidation and development.

The fact that history has temporarily divided Romania from the other part of Europe made us really forget our traditional economic relations with Europe?

The answer is categorically NO.

In order to demonstrate this affirmation, I will present the evolution of the juridical relations between Romania and the European Union. Even if it is a type of presentation very rarely used, I have chosen it in this paper for I think that it is highly relevant in order to underline the important fact that, economically, at least, we have never detached ourselves from Europe even if we could have done so.

In 1969 appear the first contacts with the recently created European Economic Community, for the sector regulation of reciprocal trade with a series of agriculture products. Not very long afterwards, the European Union recognizes Romania's status as a developing country, a fact that enables Romanian products to enter the European market beneficiating from a series of custom facilities.

Starting with 1976, Romania regulates its textile products trade in relationship with the European Union through the periodical signing of a series of bilateral agreements of voluntary restraint. The reorganization of the common ferrous metallurgy industry and the Romanian export potential in this economic sector set the need for a definition of the bilateral juridical basis and the signing, starting with 1978, of the bilateral arrangements of voluntary restraint of the Romanian exports.

In 1981, Romania chooses a global approach of its relations with the European Union. Thus, besides the Agreement on industrial goods, the Agreement concerning the creation of a mixed intergovernmental commission is signed. In this way, the dialogue between the European Union and Romania is institutionalized. In other words, Romania de facto recognizes the existence of the European Union as an economic entity.

Through these efforts, Romania became the first and only COMECON member to reach this point in its relationship with the European Union.

On these basis negotiations regarding the signing of and Agreement on trade, economic and commercial cooperation between Romania and the European Union were started. Immediately afterwards, in 1987, Romania got the historical chance to become the first COMECON member who could establish diplomatic relations with the European Union. Only the limitations imposed by the Romanian political regime of that time, a regime that did not foresee Europe's evolution, caused us the loss of the respective opportunity. The issue was nevertheless brought up again in 1990 and concretized, which enabled us to move onto the negotiations for the European Association Agreement and

from there on, onto the long road of accession to the European Union.

It is thus easy to see that the European Union has always represented for Romania a significant partner while our country has permanently had the sentiment of belonging to the European values.

It is why, once adhered to the European Union, we must feel Romanian at home in all regards in Europe, and try to make the best of the advantages brought by the European construction. The need to operate with the European economic mechanism is great and we must guarantee the correct functioning of these mechanisms, which are not only European, but have an international vocation as well.

We must be at ease with the rules of the game, to set specific priorities and assure a professional representation in the dialogue with the European partners, enabling thus not only the turning account of the opportunities that come from the accession to the European Union but also the concrete contribution to the continuation of this process of European construction.

We cannot and we must not remain stuck in sterile and obsolete discussions about the costs of integration, when in fact the costs of non-integration in the European Union would have been, without a doubt, much greater.

Also, I consider it normal for the euro skeptics to look upon the European Union in its dynamic and see that in its 50 years of history, the number of member states has continued to grow, presently reaching 27.

They can thus see that the process of the European construction had the European Union as its major pillar and that it has been achieved in only one direction.

The fact that not one of the member states that make up the European Union has solicited to leave this family and the reality that all countries that have adhered have known important economic growth with benefic effects on the standards of life of their citizens, can represent the most eloquent answer concerning the benefic role in belonging to this entity.

At this anniversary moment, we must be conscious of the fact that we belong to the European Union and that we live in a region of peace, of democracy and of cooperation, with great hopes for sustainable economic growth and the positive evolution, therein, of our life standards.



## EURO MORTGAGE

Lorena Poenaru

### Abstract

*The unitary economical politics from monetary field had a considerable influence on the banking system. Economical harmonization and integration have actually the same purpose at the end: to create a compromise for the approach of national systems and to ease banking operations. Initially, the control politics of the capital international waves have been very important in the national plan of member states. Subsequently, there has been the phenomenon of the capital markets and payment means liberalization<sup>1</sup> and the Maastricht Treaty has brought important modifications in this aspect.*

The unitary economical politics from monetary field had a considerable influence on the banking system. Economical harmonization and integration have actually the same purpose at the end: to create a compromise for the approach of national systems and to ease banking operations. Initially, the control politics of the capital international waves have been very important in the national plan of member states. Subsequently, there has been the phenomenon of the capital markets and payment means liberalization<sup>2</sup> and the Maastricht Treaty has brought important modifications in this aspect.

European Central Bank setting up and introduction of euro currency had as purpose to destroy the intern barriers for the four fundamental liberties and to assure the prices stability, converting thus the euro area into an important actor of the world economy. Within community, the monetary politics and the economical one complete each other. Although the last one is a competence filed of the member states, the community control system contains common requirements. When the Council finds mistakes, issues between a national economical politics and the economical principles of the UE Treaty, it elaborates economical politics recommendations - the well known "multilateral surveillance system"<sup>3</sup>.

The complexity of the commercial field, has determined trade companies to promote its products also on other markets than the national ones. The cooperation and commercial representation relationships are often the ideal solution within an economy built on free competition, and the intensification of transfrontal commercial exchanges imposes an harmonization of the legislative settlement.

The Romania and Bulgaria joining on January, 1, 2007 has determined the pre-existent community construction of this event to add the European East civilization inside of a high level political and economical organization system. Europe takes its shape, where it will be done a re-analysis of the community priorities and of the institutional reforms modalities, in order that the geographical progression can be proportional with the achievement of the European Union aims. Within the actual international background, the economical field has an essential role for two important processes: integration and globalization.

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<sup>1</sup> by CEE Treaty and Directive 361/88/CEE

<sup>2</sup> by CEE Treaty and Directive 361/88/CEE

<sup>3</sup> Romanian Magazine of Community Law no. 4/2006, publishing Rosetti, Bucharest, p. 62

The evolution tendencies stress competition, implying the access to resources, the economical agents being forced to find out optimal solutions in order to face the continuous changes.

The harmonization of the judicial Romanian system with community disposition, complete the commercial connections among states, offering to its participants the needed legal protection. In Italy, the banking system reform, effected by Law 218/1990, has transformed the public law credit institutions into stock societies. Subsequently, the fiscal regime of banking reshaping operations has delegated the Italian government to realize a new reform in this field, introducing thus, fiscal advantages.

According to Romanian Law no. 58/1998, implying the banking activity, modified by the Law no. 485/2003, the banking activity is done by authorized credit institutions. Credit institution represents: a) the entity which carries on , with professional title, activity of drawing warehouse or other reimbursable funds from the public and of granting credits on own account ; b) the emitter entity of electronic currency, other than the one foreseen at “a” letter.

In Romania, the credit institutions can be set up and can operate as banks, cooperative credit organizations, emitter entity of electronic currency and savings bank for the locative domain. By special law, we can settle the foundation and the development of the activity by credit institutions, others than the ones presented, by respecting the Law principles concerning the banking activity from Romania. Banks can unfold, respecting the granted limit, also other activities permitted by legislation in force, as: drawing the investment societies and funds assets, distribution of participation titles at investment funds and action of investment societies, operating as Operator of Real estate Guarantee Electronic Archive, operations with metal and precious stones and objects manufactures with these ones, operations with delegation , processing data services, data bases management or other similar services for third parties, participation at the social capital of other entities. From the point of view of the banking management, it is very important to take in consideration the criteria influencing the organization method, the information system, the decisional process, as well as the appointment method of the lading staff.

Among the multinational banks there are the International Financial and Monetary Institutions, which have as common features the following: the capital consists of the Central Banks subscription from the states member; the management is assured by the member states governors; confers assistance and credits to the member states; supervises the functioning of the international banking – financial markets. The mixed banks are formed by the capital of two or several partners from different countries and they submit to the legislation from their residential country. The off- shore banks operate in certain free areas, which make only operations with non- residential individuals, assuring their anonymity.

The off-shore areas offers to the economical subjects the following priorities: fiscal facilities, a wide freedom, with no currency control, practically; the possibility to unfold operations with residents in any foreign currency; passing immediately the expenses to losses; anonymity, financial operations confidentiality.

The fields the banks are trained in are: retail banking, corporate banking, private banking, universal banking, investment banking. In the latest years, the financial performances have known an important economical development, internationally speaking. In most of the countries, the positive results appeared as a result of the

economical companies, especially of the banks. The economical advantages of the credit market development are, among others: a better variation of opportunities, the importance of completing the market, raising the clearances, risks diminution.

Services freedom in the banking or assurances field needs the liberalization of short time movements and respectively of assurance contract transfers.<sup>1</sup> The capitals movement liberalization has been made progressively, The Maastricht Treaty has not allowed the restrictions concerning the payments among the member states. The liberalization principle “*erga omnes*” refers to freedom among the member states but also the third parties countries. It needs a well determined fiscal control, in order to avoid the embezzlement, but without being a discrimination method or a restriction disguised against the free movement of capitals.

The supremacy of community law means that the european law is characterized by a superiority situation according to the entire intern juridical order. The supremacy attribute implies the fact that the community law removes from the application any contrary national stipulations. A free market economy supposes, among others, the trade freedom and the protection of the national economy, and creation of the necessary features for developing the quality of life.

In Switzerland, the State watches on the creation of a unit economical space and proclaims to fight against the damaging social and economical consequences of cartels and of other forms of limiting the competition. The State also takes into consideration the economical development specific to every random regime and cooperates with cantons and economical environments; it can derogate from the economical freedom principle in the credit and currency field, in the extern trade and public finances field, and establishes together with the communes and cantons the budget politics, according to the random situation. On the other side, it can force the enterprises to create crisis reserves, granting fiscal facilities and can also force the cantons to grant them, (when the reserves are free, the enterprises freely decide concerning their use, respecting the distributions foreseen by the law).

As the commercial liberalization progresses, it doesn't effect only trans-frontal issues, but also the ones from inside the frontiers. These might vary from the products settlement to the social and environment norms. By analyzing the EU decisional process in the extern trade field, it is important the connection between the operating capacity and the necessity of controlling, in the extern politics of the EU being included also the cooperation for development (financial assistance and credits). Among its objectives, the European Union must have in mind to continue to liberalize the trade, in order to establish the trust for the business environment within the world economy, as well as refreshing the disciplinary nature of the multilateral trade system. The economical motivation of the agents and promoting some advantageous payment techniques and methods in the banking system make that the European Union be often a predominant market for many countries, fact that determines that the intern evolutions of the EU are an important factor for their development and material conserving. Not lastly, the demand of an extern trade politics of the EU is determined by its importance within the international trade system.

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<sup>1</sup> Banking Directive from 15.12.1989, respectively the Directive concerning the assurances from 08.11.1990

The European Justice Court has given a general definition<sup>1</sup> concerning the nationalization of electricity distribution and production in Italy. It considered that these kind of monopolies “ must have, on one side, as object transactions over a commercial good which could form the object of the competition and of the exchanges among the member States and, on the other side, they could play an effective role in these exchanges.” The competition reflects the free initiative of the economical agents and an appropriation of the market economy. The politics in the competition field is conceived and practiced in order to prevent or to destroy an unfaithful behavior from the part of the participants at the market mechanisms. The main reason of politics in the competition field is the desire to promote competition. Sometimes, the rules of monitor the competition environment do not offer many options to the participants and aimed objectives are incompatibles.<sup>2</sup>

The community competition politics has a direct meaning for the candidate- states, even before their joining, and independently from this event, the obligations assumed in this domain having a double innovation character: it refers to instruments unknown to the economies with centralized planning and represents the first international contractual obligations of the associated countries.

At the World Trade Organization level, the trade- competition report is one of the most sensitive components found on the agenda of the new generation of multilateral trade negotiations. In redefining the economical structures from various States, every authority and business environment have an important role by their vision. The integration of the financial capital market has been influenced by introducing the euro and the technology for distance access of the trade with financial titles. The location competition, especially among regions, for tangible mobile assets, has raised once with the integration of the market factors, together with the integration of the market services and goods.<sup>3</sup>

Community law and international law meet their efforts and complete their objectives in order to aim the international relations from politics sphere in law sphere. The existence of some parallel competence brings a “complementary form of interests” as well as a normative one, which approach the European Community of the international community. For the European Union, an East spread may be justified also by certain political- economical reasons (which , at their turn, will have, in application, connections with community judicial system ): by integration, the East- European countries will be supported in maintaining the economical liberalism; the unity of the continent will be straighten , by vanishing the artificial boundaries created by some historical periods; The Eastern Europe , being a complex political space, will become a palliating conflict pressure region; by participation of the new members (who will enjoy a more balanced economy). By creating a commune European space, the European integration level is raising very quickly. The globalization phenomenon has also its effects on the national legislative backgrounds. By appearing the commune standards and regulations, there is a tendency of insisted harmonization of legislation. From the juridical point of view, The

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<sup>1</sup> Decision from July 15, 1964 , cause Costa ENEL

<sup>2</sup> Dumitru Miron “ The European Union Economy, pub. Luceafarul , Bucharest, 2002, p. 256

<sup>3</sup> Jacques Pelkmans “European integration . Methods and economical analysis” , European Institute from Romania, Bucharest, 2003, p. 199

contemporary Europe represents a potential field of important transformations, which have as a result the blur action of national boundaries, which tend to become a simple geographical delimitation. The economical reality and the European integration determine a progressive passing from national dimension to the community one, as well as new action with extraneousness character, which are more and more frequent. In the actual context of the exchanges liberalization, the transactions rapidity is a major concerning, which implies free movement of juridical acts and of the contracts in every member states from European Union. Within European Council held at Tampere (October, 15 and 16, 1999) the Union members established as main objective of the European construction, the creation of a freedom, security and justice space, expressing thus the will to create a Europe of the law.

In 1987, a commission of the International Union of the Latin Public Notary proposed (after the Switzerland pledge title – Schuldbrief), that besides the guarantee rights on the existent real estate property in the European States legislations, there should be instituted a pan – European mortgage. The guarantee right offered this way to the beneficiaries from EU would be better commercialized and free from the juridical and economical disadvantages of the accessory conventional mortgage.

Although the mortgage credits in the EU member states have a great importance, there is no international market of mortgage credits, one of the reasons being the different national judicial and legislative systems. There appeared the idea of “euro- mortgage”, a common additional of granting credits instrument in the European states<sup>1</sup>. The markets of mortgage instruments of the new member states had totalized less than 2% from the European general mortgage business. In order to reach the level of the most developed community states, it needs an efficient legislative reform in the mortgage and real estate field, if we want to earn foreign investments and guarantee the real estate property (Poland has considerable progress in this way).

In 1998, The Allemandes Mortgage Banks Association proposed the establishment of a guarantee right non – accessory flexible, to be a reform in the field, in the central and east – European countries. This kind of right has been introduced in Estonia, Hungary and Slovenia, and law projects in Bosnia and Poland. In 2004, The “Forum” Group established by the European Commission, concerning the mortgage credit, defined euro-mortgage as an alternative instrument of the mortgage transfer facilitation, which would not seriously modify the law national systems. The idea has been studies also by the European University Institute from Florence, by the German Public Notary Institute and by many specialist university professors. Land Information European Service, established in 2002 contents 8 countries: Austria, England, and Wales, Finland, Lithuania, Holland, Norway, Scotland and Sweden. The project aim is the creation of a common internet portal in order to approach all land books from Europe. Euro – mortgage would be thus a national instrument, but with some commune norms, which economical value would depend upon the judicial system from very European country<sup>2</sup>. The trans–frontal mortgage credit has still some issues with two contrary characteristics of the states

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<sup>1</sup> Workshop held at Berlin, November 2004- April 2005, participating experts and specialists groups from all around Europe

<sup>2</sup> “Main principles for an euro- mortgage”, Credit mortgage foundation Varsovia”, 2005, pub. Notarom, Bucharest, 2005

systems - rigidity and flexibility. A flexible but certain mortgage would destroy these disadvantages if it was adapted to the modern requirements concerning real estate financing. The euro- mortgage could exist before concluding the credit contract or the credit payment. Thus, the bank cannot undertake the risk of a payment, with no guarantee right and we can reduce the time concerning the loan. After the obligation is reimbursed totally or partially, a new obligation may be guaranteed between the same parts, without creating a new mortgage, which may also lead to the costs reduction. The proceeding is also possible when the old obligation is replaced with a new one (the novation), the loan being able to be prolonged or replaced with another one, after the expiration of the fixed interest period. Several obligations of the same creditor may be also provided for, and it can be transferred to a new creditor for a new loan, since it is accessory.

In the economic field, the euro-mortgage encourages the development of new financing techniques and the simplification of the transfer means by means of the banks, thus diminishing the costs, the risk and the time. The applicable law of the euro-mortgage is "lex rei sitae"- the law of the member State where the property is located. The national law may request an agreement between the owner and the future euro-mortgage 's holder, as a request separately of its drawing up. With regards to the interest, this does not exist in the case of the euro-mortgage, though any of the members propose that the national law should establish the production of an interest diversely to the interest rate set up through the credit contract. The euro-mortgage cannot be sunk only by paying the guaranteed debts, but its radiation will be necessary , through the agreement of the parties, from the national register where it has been recorded. The fiscal costs collected by the state are the same as those for the local and foreign creditors , according to the European legislation, and in order to avoid double taxation the states will levy a tax only on the guaranteed and registered amount.

Taken into account the fact that more and more companies and physical persons (commercial and private beneficiaries) own real estates in several European states, a single mortgage could offer a lesser risk for the entire credit.

In the frame of the economic and financing environment, the liberalization of the capital movement has been performed in three steps: the liberalization of the capital operations (commercial credits or direct investments), the liberalization of the financing title operations (bonds, shares) and the liberalization of the financing loan operations and those of money market instruments. The conversions of the single market<sup>1</sup> have been pointed out by the intensification of the competition between the firms, the speed-up of the rhythm of the improvement in the competitiveness, the rapidity of the operations, the deprive the national monopolies of courage.

The European banking reform had as an institutional support the European System of the Central Banks (ESCB), including the European Central Bank and the central banks of the member states of the European Union. ECB pursues to prevent from the currency speculations, the coordination of the money and fiscal policy, the administration of the financing assets, the reduction to and the prevention from the risk of payment non execution, the avoidance of a disordered fluctuation in the interest rate, the setting up of a coherent fiscal policy. In such a system, the central liquidity creating banks, have a certain position of monopole. The enlargement of the European Union has represented a

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<sup>1</sup> The program has been established by the White Chart of the European Commission in 1985.

major challenge and needed a careful strategic action, especially an institutional re-definition. The impact on the new members involves the elimination of the barriers in the commercial exchanges, the application of the competition policy, the access to the structural funding.

In the Quebec-Canadian law, there is a principle strictly respected, that is the patrimony of a physical person constitutes a common pledge of its chirographer creditors. As an exception, certain assets are deemed to be imperceptible (the assets necessary to the said person's profession and life, without he or she cannot live in their absence). In 1994, the civil law of Quebec, has simplified the regime of the guarantees recognized by the law. Thus, besides the pledge provided by the banking law and the mortgagee of the mercantile marine law, the main real guarantees are: the privileges, the credit sale, the redeem agreement sale (rarely met in practice) and the legal mortgage (arising out directly pursuant to the law, without being necessary to conclude an agreement). The conventional mortgage is a real right which saddles with a real estate or an asset, affected to the execution of an obligation. The parts who conclude the voluntary agreement are the mortgage constituent (the debtor) and the mortgage's holder (the beneficiary or the creditor). The mortgage has to comply with certain legal regulations essentially to the validity of the contract, and which belong to the nature of the private asset. The writ may be effected under the form of a private subscription instrument, when the object are only the assets, and when real estate is involved the authentic form is imperious.

In the case of the conventional mortgage a debtor's present assets are affected at one and the future ones – from the moment of their acquisition. The civil law of Quebec allows to any able person to alienate his assets, and to consent to a constitution of a guarantee. However, there are restrictive conditions for physical persons who want to conclude pledges. The merchants may pledge the company's assets that they run, -the notion having a general definition from the economic considering, in order to allow a larger exercise of the said activity. The mortgage agreement may be constituted on the present and future assets (in Romania, the mortgage credit law also allows such credits for the execution of buildings performed subsequently to the credit award). A special derogation from the Canadian civil Act (code) (Quebec) refers to the fact that the income produced by a building –rents and coverage insurance indemnities and which, according to the legal norm are assets- represent the object of a real estate mortgage. Since the mortgage is redeemed through the disappearance of the asset- object (art.2795 civil act-Quebec), the debtor is obligated to insure the asset and the mortgage's holder-creditor becomes the beneficiary of the insurance indemnity.<sup>1</sup>

In the Romanian legislation, simultaneously with the agreement of the parties, by means of a writ in authentic form, the mortgage will be transferred to another building, and the one on the initial building ceases its effects by law, at the date of the transcription of the new mortgage.

The rank of a mortgage on a future building will be determined by the moment of its transcription into the land register. The mortgage object will also include the existing servitude on the mortgaged asset. The papers concluded through the non observance of

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<sup>1</sup> “Quebec, law notions and notary writ models”/ Quebec Notary Chamber, The National Union of the Romanian Public Notaries, Canadian Agency for International Development, ed. Notarom, Bucharest, 2005 p. 259.

the norms in force are affected by absolute nullity.<sup>1</sup> The cession of a mortgage debt becomes opposable against thirds who did not know – in other way, except the ceded debtor, through the transcription of the cession at the Electronic Archives of Real Estate Guarantees<sup>2</sup> .

In general, the firm is a complex social and economic system, permanently influenced by the environment dynamics and the market features where the activity is performed. That's why, the crediting institutions have to modernize the demand facing strategies, the technology and the competition of the economic activity and by the quality of the methods have to cover in a great extent, the clients' needs. Some of them are aversive to risk, which determines hesitations to credit appealing.

The external environment uncertainty cannot be foreseen exactly, and thus the banks try to analyze the possible unpredictable influences and elements of the said environment. The fixation of some higher performance standards, by a qualified personnel, allows to certain banking institutions to enlarge them into the international business environment as well.

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<sup>1</sup> Law N0. 34/1.03.2006 for the modification and completion of Law N0. 190/1999, as to the mortgage credit for asset investments , Oficial Monitory, N0. 200/03.03.2006

<sup>2</sup> Legislative Compendium in notary matter, volume I/Public Notaries Bulletin ,ed. Notarom, Bucharest, 2006



## EMU ENLARGEMENT: WILL GREAT BRITAIN JOIN?

Mihai Sebea\*

### Abstract

*At this moment in time, from all the 27 European Union member states only 13 are involved in the 3rd stage of EMU: the 11 „founding members” which begun to use the euro from 1999, Greece which has joined the euro zone from 2001, and Slovenia starting 2007. From the group of the 14 countries which are outside the euro zone, only Great Britain and Denmark have a permanent derogation (the opt-out clause) which means that they will join the euro zone only when they decide to (and of course if the nominal convergence criteria will be met). In the exposed context, the present paper makes a synthetic analysis of Great Britain’s perspectives of joining the euro zone, relying on the stages and conditions established in Maastricht and also by analyzing the specific British tests and governmental plans.*

### 1. The euro launch – stages and conditions

Signed on the 7th of February 1992, the Maastricht Treaty establishes the implementation of EMU, based on two aspects. Firstly, there have been decided the stages that the member countries should follow in order to accede to the Economic and Monetary Union, and secondly, a series of criteria for the participants. Following the Delors Report proposal, the Treaty reiterates the three stages to fundament the EMU, but it also indicates a compelling calendar for achieving the Union and establishes two dates for introducing the single currency : the earliest on the 1st of January 1997 and the latest, on the 1st of January 1999.

#### **EMU stages**

As we know the first stage consisted of capital flows liberalization, which has been finalized at the end of 1993.

The second stage started in November 1993 and ended in December 1998. It established the European Monetary Institute, which had the task of monitoring the efforts of the EU Member States to meet the convergence criteria and was responsible for preparation for the creation of European Central Bank. During this stage, the Member States made significant progress towards policy coordination and towards meeting the criteria for EMU accession. At the end of the second stage, in 1998, the ECB was created, EMU was officially launched and the participating Member States selected for the final stage.

The third Stage (Stage three), which means the birth of euro and completion of EMU, started at 1 January 1999, following Madrid scenario. This stage was based on Council decision in May 1998 which settled the participating countries, following the convergence procedure that used the reports of the Commission and EMI. As the Commission recommended, the Council decided that 11 EU countries will participate in the final stage. From the fifteen members of EU, Greece didn’t meet the criteria, UK and Denmark used their „opt-out” clauses, and Sweden used some criteria to remain outside EMU.

Following the calendar, the Euro has circulated as a scriptural currency until the 1st of January 2002, the enterprises and the people beginning to use it according to the „no

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*obligation, no interdiction*” rule. From this date on, euro banknotes and coins have been launched into circulation, which have coexisted alongside the national currencies for maximum period of two months. From the last day of this period (28th of February 2002) the national currencies have no longer been accepted as a mean of payment.<sup>1</sup>

The settlement of the euro irrevocable exchange rates by the EU Council has been made in accordance with the Commission’s proposals and only after consulting the European Central Bank, on the 31st of December 1998; these have been used and applied from the 1st of January 1999<sup>2</sup>. It must also be mentioned that all the ministers, the central bank’s governors, the European Commission and the European Monetary Institute have released two press statements regarding the implementation of the irrevocable euro exchange rates beginning with the 3rd of May and 26th of September. After establishing the final and official rates, the Euro has become the single currency of the 11 countries, the national currencies being considered as its subdivisions.

### ***The convergence criteria***

EU member states are evaluated using the following criteria, as Maastricht Treaty asks:

1. **Price stability:** “the achievement of a high degree of price stability; this will be apparent from a rate of inflation which is close to that of, at most, the three best performing Member States in terms of price stability”; this mean that inflation rate will not exceed by more than 1,5 pp the average of inflation rates of the three best performing states. (the index is the annual average of HICP)

2. **Interest rate convergence:** “the durability of convergence achieved by the Member State and of its participation in the exchange-rate mechanism of the European Monetary System is being reflected in the long-term interest-rate levels;” the long term interest rate (ten years maturity) will not exceed by more than 2 pp the average of long term interest rates of the three countries from the previous criterion;

3. **Exchange rate stability:** “the observance of the normal fluctuation margins provided for by the exchange-rate mechanism of the European Monetary System, for at least two years, without devaluing against the currency of any other Member State”;

4. **Sound fiscal position:** “the sustainability of the government financial position”; this will be apparent from having achieved a government budgetary position without a deficit that is excessive as determined in accordance with Article 104(6); The excessive deficit situation is evaluated using two reference values: budget deficit/GDP ratio less maximum 3%, and public debt/GDP ratio max. 60%;

Another condition for stage three of EMU is the legislative criterion meaning that the national legislation concerning central bank has to comply with the Treaty provisions (Articles 108 and 109) and ESCB status.

As a result, since 1st January 1999, eleven countries from the EU have adopted the euro as their currency, on the base of irrevocable rates settled by Council decision, and since 1st January 2001, after meeting convergence criteria, Greece joined the euro zone as well.

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<sup>1</sup> The dual circulation period has been shortened from 6 to 2 months.

<sup>2</sup> Practically speaking, the first day of euro was 4th January.

## BOX 1 LAUNCHING THE SINGLE CURRENCY

### 1st of January 1999

- Euro becomes the national currency of the 11 EMU member states ( Germany, France, Belgium, Italy, Luxemburg, Holland, Ireland, Spain, Austria, Portugal and Finland)
- The national currencies become nondecimal euro subdivisions; the exchange rates between the two are pronounced irrevocable.
- Euro still remains just in a scriptural form (there are no euro coins and banknotes).
- The common monetary policy is applied.
- The legislative aspects concerning the single currency come into force.
- The financial markets begin to use the euro (valutary markets, bonds and shares markets)

### 01.01.1999- 31.12.2001

- The tranzit period and the „no obligation, no interdiction”principle.
- **19.06.2000**
- The Council’s decision (427/2000) for Greece to adopt the single currency. The Council’s reglementation no.1478/2000 establishes the exchange rates for the two currencies as 340,750 drahmas for 1 euro.

### 1st of January 2001

- Greece adopts the single currency (The Council’s Decision from 19.06.2000).

### During 2001

- Informative campaign regarding the security elements of the euro banknotes).
- **At the end of 2001, the banks and the** most important retailers receive euro banknotes and coins.

### 1st of January 2002

- Begins the circulation of the euro banknotes and coins.
- The national banknotes and coins begin to be withdrawn from circulation: the period of double monetary circulation).
- All the scriptural transactions must contain the sum in euro.

### • **28th of February 2002**

The national banknotes and coins are completely withdrawn of circulation, so the double circulation period comes to an end. After this date, for a short period of time the remaining coins and banknotes could be exchanged by the commercial banks and onwards the exchange was made only by the central banks (the deadlines were decided by each country).

## 2. Stages and conditions for EMU enlargement

If previously I have mentioned the EMU's stages and criteria, I will continue by naming the specific features of the monetary union enlargement process, in the case of the 14 member states that are outside the euro zone. Consequently we can classify those states in two: the three EU- 15 states which are outside the euro zone and the new members of the Union, on the other hand.

The first stage of the EMU was achieved by the EU – 15 countries once with the capital flows liberalization, and by the new members, at the moment when they acceded to the Union.

At present, all the EU countries outside the euro zone participate to the EMU's second phase, are implementing *convergence programmes*, and are coordinating their economic politics in accordance to the Commission's recommendations. Depending on their strategy, the countries will join the ERM 2, an intermediary phase of the monetary integration which implies connecting the national currency to the euro and the obligation to maintain the exchange rate evolution in certain limits. After the accession, the resolution regarding the MRS 2 must be applied and also for the national central banks it is necessary to sign an agreement with ECB. Even if the Treaty provides the participation to the MRS 2 with two years before the accession to the EMU, the situation remains debatable. The Council's Decision to allow Italy and Finland to take part to the EMU final stage without them participating two full years to the EMS consists an example in this case

At the moment, only 7 EU member states are taking part to this mechanism: Denmark (from the 1st of January 1999, the only country which has chosen a +/-2,25% fluctuation scale), Estonia and Lithuania (from the 28th of June 2004), Cyprus, Latvia and Malta (from the 2nd of May 2005) and Slovakia (beginning with the 28th of November 2005). The Czech Republic, Poland and Hungary, countries with sustainable economy policies are currently outside the MRS 2.<sup>1</sup> It is important to mention that the main reason for a country to participate in MRS 2 is due in order to meet the convergence criteria. Still in the second integration stage the states are constantly bending every effort to obtain the nominal convergence and implicitly the "entry ticket" for the euro zone.

All in all, the participation to the second phase of the EMU implies meeting and maintaining the convergence criteria, and, at the moment of joining the stage three, giving up to the monetary policy independence and also to the exchange rates used for adjusting the economic unbalance. Once part of the EMU, the member states will establish stability programmes.

It is important to emphasize that the unilateral euro adoption („*euroisation*”) by the member or candidate countries is considered to be inconsistent with the EMU framework and not acceptable by the EU. All the countries are bound to follow all the three stages stipulated in the Treaty.

Here we have to mention a very important event, the first euro zone extension towards East, the accession of Slovenia, on the 1st of January 2007.

Once with achieving important progress concerning the nominal convergence,

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<sup>1</sup> [http://ec.europa.eu/economy\\_finance/euro/world/euro\\_world\\_6\\_en.htm](http://ec.europa.eu/economy_finance/euro/world/euro_world_6_en.htm)

Slovenia has requested for convergence reports. In May 2006, the European Commission and the ECB have released the results of the reports and has recommended the country's accession to the euro zone, based on the compliance with the convergence criteria. On the 16 of May, the Commission released a statement saying that Slovenia has reached high levels of sustainable convergence and that it is prepared to use the single currency. Based on the convergence report, the Commission has proposed the Council for Slovenia to join the euro zone starting the beginning of 2007.

After Parliament consulting and discussions held inside the European Council, on the 11th of July 2006, ECOFIN has agreed for Slovenia to take part in the final EMU stage from the 1st of January and has also established the irrevocable exchange rate between Slovenia's tolar and the euro: 239,64 tolar for 1 euro.

Lithuania also requested the Commission's evaluation concerning its compliance with the convergence criteria, but the European institutions have ruled against and have released a negative result. Consequently, Slovenia's experience definitely represents an example for all the other EU members which are preparing for the single currency.

Concerning the entry conditions I will have one comment for now, referring at "price stability" criterion. The Commission is using a reference based on the inflation in three best performing EU member states. At the moment of the first evaluation this procedure was the right one. But we have to remember that EU member states had their own currency and independent monetary policy at that time. I believe that in the present, the criterion should be used from a different point of view, because there is a monetary union and an unique monetary policy for twelve countries. One could say that using the inflation values from three countries means a great importance for regional indicators, instead of euro zone indicators. Moreover, the criterion is based on three countries from EU, which could not be members of euro zone. Considering the EU enlargement, the reference value could be influenced by inflation rate from small and unrepresentative countries. We can imagine that UK will join EMU, on the base of inflation from countries that are not in EMU (maybe Lithuania and Malta)! To conclude, the economy of the country that wants to enter euro zone has to be convergent with the euro area, not with three countries from EU but outside euro area. Using the euro inflation, it eliminates even the possibility to use one country deflation rate for reference value.

### **3. Great Britain on the road to euro**

Great Britain represents a particular case concerning the changeover to euro. The country's officials have stated that Great Britain will join the EMU only when this step will be in accordance with the national interest.

It is well known the special status of the British people, and the European accession process emphasizes this situation at both politic and population level. It is known that Great Britain has ratified the Maastricht Treaty only after obtaining derogation (the opt-out clause) regarding the participation to the third and final stage of the Economic and Monetary Union. It is appropriate to mention a similar situation back in 1971, when the monetary changes had a different aspect (replacement of the metallic coins), Britain was reluctant to the change. Then, Great Britain changed to the decimals subdivisions, because the existing system was growing difficult the transactions (see box no.2)

### **Box 2 The British monetary systems-until 1971-named „LSD”**

Changing to the decimal monetary system took place on the 15th of February 1971, and stated that 1 pound could be divided in 100 units.

Until that moment, the divisions were the following :

1 Pound = 20 Shillings

1 shilling = 12 pennies

*So, the sums were written after the template: £4 15s. 6d. (= 4 pounds, 15 shillings and 6 pence).*

The British people were not very satisfied with the introducing the „new money” process, one of the most frequent question being: „how much this is expressed in old money?”. Even back then, the British conservatism was obvious. An example in this sense is represented by the launch on the 1 pound coin in 1983, which was not welcomed by the population. The reason for such a behavior was that a coin couldn't possibly have the same worth as a banknote.

*This could represent the justification for the British population's reluctance to the euro introducing, and possible positive effects that this could have.*

Even since 1997, the British government has announced that they are not against the euro introduction, but this will happen only when certain advantages for the nation will be clearly known.

After 6 years, there still exist uncertainties concerning the governmental plans for the future monetary policy. On the 9th of June, the British government, through de Chancellor of the Exchequer, Gordon Brown announced that UK „is not prepared” for the single currency and that Britain will take this step only when the nation will acquire positive results.

In the case of Great Britain the decision will definitely be based on the specific tests carried out by the Treasury.

#### ***The British tests and the government's plans***

A costs-benefits type analysis for determining a country's possibility to join the euro zone is a very complex process. In order to establish whether for Great Britain this will represent a successful step, there is carried out a series of five economic tests. These tests were applied in 1997 and 2003. In 2003, once with the public release of the tests' results, there have also been edited a set of 18 support studies which sum up a total of 1900 pages!

The five tests measure the economic implications, taking into consideration: (1) *the economic convergence*, (2) *flexibility* (3) *the impact on foreign direct investments*, (4) *the impact on financial services and on London-as a financial center*, (5) *the impact on economic stability, growth and employment*. A decision regarding the EMU accession will be made in accordance with the tests' results and also with the referendum results. The tests were launched back in 1997 at the Finance Minister's – Gordon Brown

initiative.<sup>1</sup>

Concerning the economic cycles' convergence, during the last years, Great Britain has been very close to the euro zone level, fact which emphasizes the intensification of the accession process. At present, Britain has obtained even a better convergence rate of the economic cycles than some of the euro zone country members in the period before starting to use the single currency. Britain has also proved that it meets all the convergence criteria stated by the Maastricht Treaty. Still, there have been determined certain structure differences comparing to the euro zone which are estimated as potential risks. So, even if the convergence rate is close to its level in the euro zone, it was considered that the test is not yet passed.

Referring to the next test, the results show that that the labor market flexibility has increased in comparison the middle 90's; the reduction of unemployment has transformed Great Britain into one of the countries with the higher employment rate, with better results even than USA. The test's results indicate that even if the flexibility level has risen, it is not prepared to face any asymmetrical shocks caused by possible structural divergences. In conclusion, neither this test has been passed.

Concerning the investments test, to reinforce the advantages of becoming a member of the euro zone, we can mention the reduction of capital costs for the English companies in the case when the long term interest rates of the euro zone will continue to reduce and as a consequence the participation in a large financial market will reduce the financing costs. These costs could diminish especially for the small and medium enterprises, as long as the EMU membership provides the elimination of the hurdles that these companies encounter on the financial market of the euro zone. The Treasury Report shows that an effect of participating to the euro zone could be increasing the direct investments level. Statistics indicate that Great Britain's share of EU investments has decreased after launching the EMU; and this could be a sign that the longer the monetary integration is postponed, the higher the opportunity costs shall be. The conclusion is that only under certain circumstances (eg: ensuring the sustainable convergence), the level of FDI will increase, and the test could be passed.

Regarding the financial service problem and the supremacy of the City, the euro zone accession will not have negative effects. On the contrary, the participation to the EMU will strengthen Britain's competitiveness by offering the financial services important advantages. Therefore, EMU's membership could offer Great Britain the possibility to from the high level of integration and efforts to create the single market. This test was considered as passed.

The last test refers to Britain's possibility to increase its productiveness and

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<sup>1</sup> The questions for each test are the following:

1. Are business cycles and economic structures compatible so that we and others could live comfortably with euro interest rates on a permanent basis?
2. If problems emerge is there sufficient flexibility to deal with them?
3. Would joining EMU create better conditions for firms making long-term decisions to invest in Britain?
4. What impact would entry into EMU have on the competitive position of the UK's financial services industry, particularly the City's wholesale markets?
5. In summary, will joining EMU promote higher growth, stability and a lasting increase in jobs?

employment level as a direct consequence of EMU member status. The trade could double in the next 30 years, whereas the national revenues could increase by 5-9%. The main concerns about the accession to the EMU are related to the use of fiscal policies as adjustment instruments within the Growth and Stability Pact, and also joining a zone where the inflation rate is limited to 2%, factors which could lead to a decrease of the stability level, and productivity and employment rates. Moreover, the convergence with the euro zone could not be sustainable and the flexibility level of British economy couldn't face any possible shocks which would affect the euro zone. This test could be considered passed only when the convergence with the euro zone would be sustainable.

Hence, the final decision whether or not to join is complicated for the government, especially taking into account the pessimistic public opinion. This issue is difficult to tackle as long as the citizens' opinion seems to be divided in a perfect balance between participation and staying outside the euro zone.

### ***The stages of adopting the euro for Great Britain***

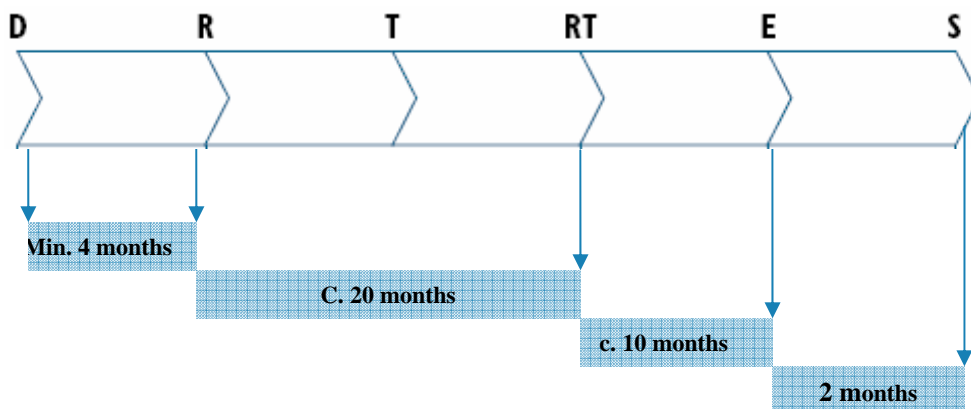
Leaving aside the debates concerning the effects of adopting the euro, we have to praise the British authorities' efforts for preparing the transition to the single currency. It was stated that the country will begin the EMU joining process the moment the Government, the Parliament and the population (via referendum) decide it is convenient. Starting 1997, the Government designs plans in order to switch to the single currency.

There have been prepared three national plans for the accession, strategies and situation reports. Moreover, for each semester, The Bank of England is editing informative publications and leaflets containing the implications of euro using in order for the financial sector to be prepared. All these measures are considered necessary legal (Britain has to comply with the *acquis communautaire*) and also procedure (the technical switch must be successful) steps.

At present, Great Britain continues to participate in the second phase of EMU, and is preparing for the third and final stage. Now, we will present the calendar of the euro adopting process established by Britain.

The third *National Changeover Plan* announced by the Government, contains the phases of this complex process. Taking into account the positive experience of the 12 countries and also the negotiations carried out for the management process, in July 2006 the Government announced the reduction of the time period for the two currencies to circulate simultaneously from 6 to 2 months. Therefore, the EMU joining process has the following stages:





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Graphic no. 1 – Changeover to euro plan – Great Britain

In the first graphic, the information have the following signification:

- **D:** *Decision* – The Government's decision to join the EMU;
- **R:** *Referendum* – the British electorate officially expresses its interest in the monetary union;
- **T:** *Time of entry and start of transition*. Great Britain joins the EMU. The euro – pound exchange rate is irrevocably settled;
- **RT:** *Retail Transition*. Beginning of the retail transition phase. There will be available retail financial services denominated in euro;
- **E:** *Euro* – the cash begins to circulate and the transition period is over. All non-cash transactions will be denominated in euro. The planned date for achieving this stage is considered the 6th of April ( while for the other 12 candidate states it is the 1st of January)
- **S:** *Sterling* – The pound is no longer a legal mean of payment. The end of the double circulation period.

We can see now that the main problem is considered to be the government's decision. It is obvious that a positive decision will be taken once having the guarantee of the advantages that Great Britain will obtain. The correct timing is a key factor for the process success.

Under these circumstances, the only issue remaining is obtaining the "entry ticket" from the European institutions after examining the convergence criteria. It is well known that even from 1998, Great Britain had complied with the Treaty criteria. Nowadays, Great Britain has to elaborate the Convergence Programmes, and for example the December 2005 Programme shows that the member state has important potential to fulfill all the convergence requirements: price and interest rate stability as well as the fiscal criteria. It shall be decided the moment when the pound will undertake ERM 2 (*Exchange Rate Mechanism 2*).

## Conclusion

I consider that Great Britain will not be able to remain much longer outside the euro

zone, especially that the single currency has proven its viability. The problem is not whether Britain will join or not EMU, but when it will happen. The referendum date and the promotion campaigns results will be decisive. For the people, business environment and for the British financial institutions it is crucial to be strongly prepared in order to face the transformation and to reduce the negative effects to a minimum.

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Information on the UK government strategy for euro adoption

<http://www.euro.gov.uk> – *information about the single currency*

[www.eurocoins.co.uk](http://www.eurocoins.co.uk)

## TURKEY LIKE A CANDIDATE OF EUROPEAN UNION

Raluca Bughea\*

### Abstract

*Turkey applied for associate membership in European Community in 1959, and signed the “Ankara Agreement” on September 12<sup>th</sup> 1963. Since 1964, Turkey has been a European Union Associate Member. Turkish accession will change the EU’s borders but it will also change Turkish relations with its neighbors. Overall, Turkish accession will extend and deepen EU foreign policy interests in its surrounding regions. Turkey will have considerable impact on the European Union, but it is an impact that can be managed as previous enlargements have been.*

Turkey applied for associate membership in European Community in 1959, and signed the “Ankara Agreement” on September 12<sup>th</sup> 1963. Since 1964, Turkey has been a European Union Associate Member.

On April 14<sup>th</sup> 1987, Turkey made formal application to join European Community, but European Commission, in 1989, refused to begin accession negotiation. The same attitude was taken in 1997, when European Council in Luxembourg decided to start accession discussions with Central and Eastern European States and Cyprus, but not Turkey. Turkey was officially recognized as a candidate for membership at the European Union on December 12<sup>th</sup> 1999 at the Helsinki summit of the European Council, and the negotiations started on 3<sup>rd</sup> October 2005.

Every country, that wants to join the European Union, has to fulfill some conditions. In June 1993 the European Council of Copenhagen, Denmark (from which they took the name) laid down the conditions (the so-called *Criteria of Copenhagen*) for the accession process of Central and Eastern European Countries to the EU. The *Copenhagen criteria* are the rules that define whether a country is eligible to join the European Union. The criteria require that a state have the institutions to preserve democratic governance and human rights, a functioning market economy.

The Copenhagen criteria are:

1. The political criteria: "Membership requires that the candidate country has achieved stability of institutions guaranteeing democracy, the rule of law, human rights and respect for and protection of minorities."

2. The economic criteria: "The existence of a functioning market economy as well as the capacity to cope with competitive pressure and market forces within the Union."

3. The adoption of the *acquis communautaire*: "Membership presupposes the candidate's ability to take on the obligations of membership including adherence to the aims of political, economic and monetary union."

4. The fourth criterion laid down in Copenhagen is "The capacity of the Union to absorb new Member States while maintaining the momentum of the European integration process."

In connection with the enlargement process the European Council of Helsinki of 10

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and 11 December 1999 confirmed that all States willing to accede to the European Union have to share the values and goals of the European Union as stipulated in its Treaties.

In connection with Turkey's candidacy for EU Membership, the European Council of Helsinki decided, in December 1999, that the criteria for accession, especially fulfillment of the political criteria are also to be applied to Turkey before the start of accession negotiations.

In addition, the Council formulated other political conditions for Turkey's accession, such as the resolution of the existing conflict between the EU Member Greece and Turkey, and the Cyprus problem.

The European Union opened accession negotiations with Turkey pressing the country to allow ships and aircrafts of EU's member Cyprus into its ports and airports and recognize the Greek government of Cyprus. Turkey has been refusing to recognize Cyprus' Greek government and has been supporting the unacknowledged Turkish state of Cyprus in the northern part of the island. Turkey said on 12 July 2006 it had opened one of its ports and an airport to Cyprus' Greek ships and planes.

The other conflict between Turkey and Greece over sovereignty and related rights in the area of the Aegean Sea is called the Aegean dispute. Since 1998, the two countries have been coming closer to overcome the tensions through a series of diplomatic measures, particularly with a view to facilitates Turkey's accession to the European Union. However, as of 2006, differences over suitable diplomatic paths to a substantial solution are still unresolved.

Talking about the other *political criteria's*, Turkey continues sufficiently fulfill them and has continued political reforms. However the pace has slowed during the past year. Significant further efforts are needed in particular on freedom of expression. Further improvements are also needed on the rights of non-Muslim religious communities, women's rights, trade unions rights and on civilian control of the military.

Regarding free expression of opinion, many problems still remain and in this respect the new penal code only constitutes limited progress. In the field of protection of minorities and the exercise of cultural rights, the prohibition on the use of the Kurdish and other languages was lifted, but these minority groups are still discriminated. Cultural rights in the field of broadcasting and training in minority languages are still considerably restricted.

There has been little change in the situation as regards children rights. Implementation of legal provisions concerning education and employment under the age of fifteen needs to be improved.

Women's rights receive growing public attention in Turkey, and civil society is increasingly able to play a positive role in this area. However in practice women's rights are not always protected, in particular in the poorest areas of the country. 'Honour crimes' need to be investigated more systematically and where appropriate followed-up with the prosecution and convictions.

And also there is limited progress on legislative reforms in the fight against corruption. Corruption remains widespread and still remains a serious problem in all sectors of the economy and public life.

Turkey is a large country in population terms – there are some estimation that in 2015 Turkey will have a population of 82.1 million, and in 2025 85 million people and will be the largest EU member state.

As regards *economic criteria*, Turkey can be seen as a functioning market economy, as long as it firmly maintains its recent stabilization and reform achievements. Stability-oriented macroeconomic policies have contributed to strong economic growth and growing resilience to shocks, after 2001 crisis. Budget deficits and government debt levels have been significantly reduced and some key measures have been taken to enhance the social security system. Turkey's economy is characterized by major regional inequality.

On one hand Turkey had to fulfill these formal criteria's and join the European Union, but the other hand there are the other European countries, who already are members of EU, and they must think about Turkey as a different country, with different traditions and different religion.

Firstly, we have to raise a question if the Turkey is a European country? According to the Maastricht Treaty of the European Union and to the Treaty Establishing a Constitution for Europe "*Any European State may apply to become a member of the Union*". Therefore it is essential to define whether the applicant is an European country or not. Geographically only 3% of Turkey's territory, called the Thrace lies in Europe. The rest of Turkey's territory is called Asia Minor. So, from a geographical point of view, Turkey is an Asian country. Turkey is a large but poor country, with strategically important but complex and sensitive geographical location.

Although, traditions and habits of Turks are totally different from European customs. Based on their religious-traditional background, up to 50% of women (according to Amnesty International) suffer from domestic violence, and there are still up to 300 "honor killings" per year in Turkey. ("Honour killing" is the murder of a female family member because of her improper behavior, such as not wearing a hajib, having sex before marriage, adultery suspicions and others). These deeply rooted customs can in no way be considered to be acceptable in Europe.

Even though among Islamic countries, Turkey is undoubtedly closest to the Western conception of democracy, it is impossible to ignore the threat of gradual but steady Islamisation.

Despite, a number of legislative changes have been adopted, Turkey still ranks among countries with substantial violation of human rights. Gender equality, fundamental freedoms including freedom of workship and zero discrimination of minorities seem far away. There are still a high number of incidences of prisoner torture and degrading treatment of women.

Also Turkey still hasn't recognized the massacre of 1,5 million Armenians in years 1915-1923 as genocide. Before World War One, the Armenians were the largest non-Turkish minority. The 1915/16 genocide of the Armenians, in the course of which at least 1 million Armenians were killed, led to an "ethnic cleansing" of Anatolia. Moreover, 500,000 Assyrian Christians fell victim to the genocide. Turkish official quarters still deny the Armenian genocide and the "ethnic cleansing". Far from it, it is commonly taught in schools that no genocide has ever occurred.

It was always going to be difficult to get Turkey into the EU. On top of complications arising from its poverty, its mostly Muslim culture and its mistreatment of the Kurds, it would be the largest member, with the most votes in the Council of Ministers and the most seats in the European Parliament. Even so, the accession talks have been unnecessarily fraught.

So these reasons shows that accession of Turkey to European Union is a long process and must be very well considered.

Otherwise, for the EU, a rejection of Turkish membership would represent a huge lost opportunity. Europe's foreign policy, and its hopes of global significance, would suffer a catastrophic loss of credibility if it were seen to be blackballing a moderate Muslim country that has NATO's second-largest army. The EU's reputation in the Muslim world, which is watching the membership talks with Turkey closely, would sink, perhaps even below America's. The election in 2002 of the Justice and Development (AK) party as Turkey's first single-party government in 15 years changed the political landscape. Under Recep Tayyip Erdogan, who became prime minister in 2003, the mildly Islamist AK party has undertaken ambitious reforms with the long-term aim of bringing Turkey into the European Union. These weakened the country's meddlesome generals and began reversing decades of corruption, economic mess and authoritarian abuse of power.

But formal talks on EU membership have stumbled badly since 2005. Meanwhile, an upsurge in ultra-nationalism, the long-term future of Cyprus and a festering Kurdish problem remain unresolved and damaging to relations with America and the EU. Discouraged, Mr Erdogan seems to be having second thoughts on further integration. At home, disturbing resistance from secularist generals in April 2007 caused him to call an early election, which his party is likely to win<sup>1</sup>.

Turkish accession will change the EU's borders but it will also change Turkish relations with its neighbors. Overall, Turkish accession will extend and deepen EU foreign policy interests in its surrounding regions. Turkey will have considerable impact on the European Union, but it is an impact that can be managed as previous enlargements have been.

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## CELEBRATING 50 YEARS WITH TWO NEW PROVOCATIVE MEMBERS

*Sorina Costache, Ovidiu Folcut and Ramona Ichim<sup>1</sup>*

### Abstract

*Romania and Bulgaria were admitted into the European Union. Their perspectives in the European Union depend mostly on their previous economic evolution and on their efforts to become European competitive economies. Given the political chaos that has taken hold in other eastern European countries, most of them much richer and stronger than the two newcomers, it is clear that the Balkan pair's road to EU prosperity and stability will be hard.*

On 1st January 2007, Romania and Bulgaria were admitted into the European Union, after they have been made further progress with macroeconomic stabilization, economic reform and completed membership preparation. Their perspectives in the European Union depend mostly on their previous economic evolution and on their efforts to become European competitive economies.

Although united by weak institutions and their poverty, Bulgaria and Romania differ in size, history, politics and economic structure. Romania, with some 22 million people, is the second-biggest eastern European country after Poland. Bulgaria is just over a third as big. This could be a plus, as small countries' elites often work better. But Romania's political class has recently outscored Bulgaria's. Big countries also matter more to foreign investors.

Joining the EU has meant intense pressure to meet Brussels standards, which neither country yet does. The biggest worry is lawlessness. In Romania this takes the form of corruption; in Bulgaria, of organized crime. Criminal-justice systems are weak and high-level sleaze widespread. Romania has made more progress. Bulgaria has moved more slowly. Some politicians still seem untouchable, as do some organized-crime groups. A recent OECD study rates Bulgaria higher for investment promotion, but Romania higher on anti-corruption and business integrity.

### **Pre-accession period for Bulgaria**

Bulgaria experienced a decade-long delay in its transition to a market economy. Its delay in proceeding with reforms left the country far behind other transition economies. In early 1997, the country experienced a severe economic and financial crisis. In July 1997, after several months of chaos involving a sharp decline in GDP and per capita incomes, the collapse of the banking sector, and a major foreign exchange crisis, Bulgaria

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adopted a Currency Board Arrangement. The devastating effects of the economic crisis on the social conditions of the country placed considerable strain on many vulnerable groups, and poverty became a serious and widespread problem. In 1997, the year of the crisis, the government adopted a comprehensive economic reform program supported by international financial institutions and other development partners. Wide-ranging reforms included major trade and price liberalization, social-sector reform, and restructuring of the financial, enterprise, agriculture, and energy sectors, including the divestiture of state-owned enterprises. The implementation of the program lowered inflation, improved investor confidence and helped transform Bulgaria into a market economy.

Since 1997, the country has recorded sustained economic growth of more than five percent per year.



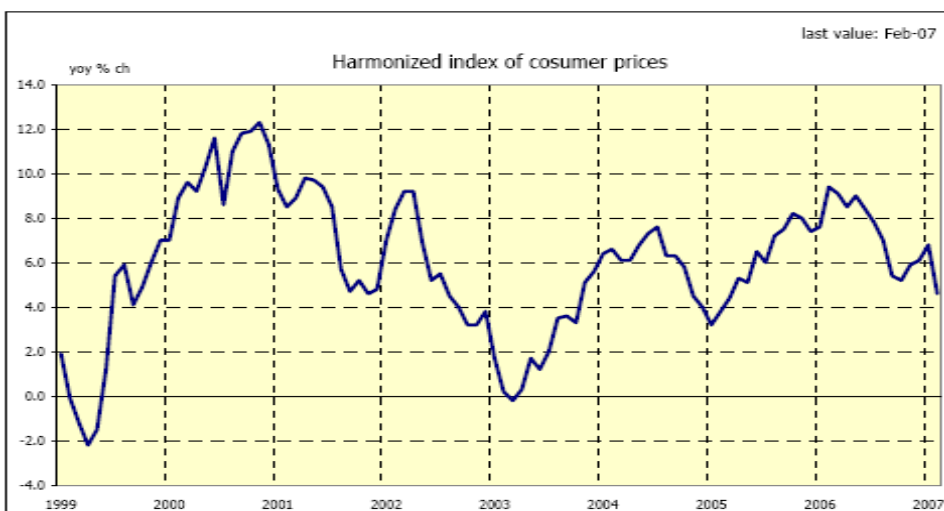
Note: yoy % ch - growth rate compared to the same period of previous year

Phase one of Bulgaria's structural reforms resulted in the private-sector share of gross value added to the economy reaching 79 percent in 2005. The financial system is now fully privatized.

Current government reforms build on the gains of the past six years and focus on promoting growth and reducing poverty. Accordingly, the government has embarked on a strategy of creating an investment climate that encourages private investment, increased productivity, and sustained growth.

Consumer price inflation, one of the most important indicators for Bulgaria's accession at the Euro zone, remained at above 8% in the first and the second quarters of 2006, mainly due to the hike in excise duties on alcohol and cigarettes and also of a price overhang from oil and food price increases in the second half of 2005. As the impact of this higher oil and food price is starting to wane, inflation has started to fall since July 2006 at above 7% at the end of the year.





New social sector reforms are emphasizing the development of human capital to complement investments in physical capital. They include social-protection programs that target high levels of long-term unemployment and entrenched poverty.

### **Bulgaria's perspectives**

Growth in domestic demand will ease slightly over the forecast period. This, together with the strength of the euro, will cause real GDP growth to slow from 6% in 2006 to an annual average of closer to 5% in 2007-08. Real GDP growth will slow further to an average of around 4% per year for the rest of the forecast period, as Bulgaria's poor demographic situation increasingly weighs on the economy's ability to expand quickly.

Increases in excise duty pushed up prices in 2006, but inflation is forecast to fall sharply in 2007 as a result of strong base effects, and more gradually in 2008-10. It's expected that Bulgaria to adopt the euro in 2010 or 2011. The current-account deficit is estimated to have risen close to 16% of GDP in 2006. It is forecast to decline gradually over the forecast period, as more moderate growth in domestic demand and lower oil prices lead to a slowdown in import growth. However, the deficit will still be around 10% of GDP in 2011.

As there is little scope for discretionary monetary policy under the currency board, excessive growth in domestic demand is the main economic risk. The BSP's desire to avoid a repeat of the 1996-97 economic crisis should ensure that fiscal policy remains cautious, although the size of the budget surplus is set to fall from the high level in 200

(3.8% of GDP). However, if domestic demand were to grow more strongly than expected, an even more restrictive fiscal policy might be required. If this should prove politically impossible and the current-account deficit increases further, doubts could arise about the sustainability of the currency board.

Key indicators	2006	2007	2008	2009	2010	2011
Real GDP growth (%)	6.0	5.4	4.9	4.4	3.7	3.8
Consumer price inflation (av; %)	7.3	5.6	3.3	3.0	2.8	2.9
Budget balance (% of GDP)	3.5	2.0	1.4	1.2	1.0	1.0
Current-account balance (% of GDP)	-15.7	-13.4	-12.7	-11.7	-11.0	-9.8
Short-term central interest rate (av; %)	2.9	3.8	4.0	4.0	4.0	4.0
Exchange rate Lv:US\$ (av)	1.56	1.46	1.44	1.51	1.54	1.55
Exchange rate Lv:€(av)	1.96	1.96	1.96	1.96	1.96	1.96

### **Pre-accession period for Romania**

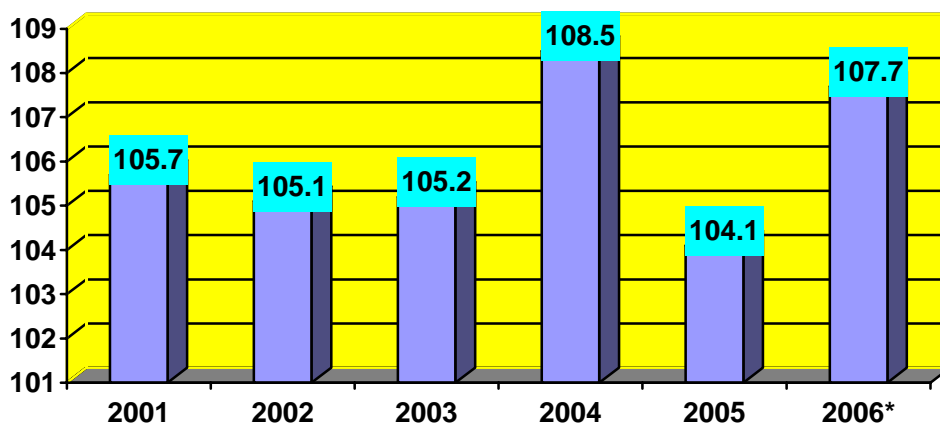
Romania's transition, which started in 1990, was more difficult than that of the other CEE countries in many respects. By the late 1980s, Romania's economy was on the verge of collapse after 40 years of rigid central planning that emphasized self-reliance, an excessive focus on heavy industry, and large, inefficient infrastructure projects.

In an attempt to minimize the social costs of transition and often to placate vested interests, the Romanian government initially hesitated to impose tight fiscal constraints and to privatize large loss-making enterprises. In the late 1990s, attempts to impose macroeconomic stability without full structural support led to negative economic growth and to doubling of the poverty rate from 20 percent in 1996 to 41 percent in 1999.

Since 2000, the government has implemented macroeconomic policies which are supportive of growth. A disciplined fiscal policy, which complemented a tight monetary policy and was augmented by strong advances in structural reforms, led to improved financial discipline in the enterprise sector and has placed public finances and the financial system on much firmer footing.

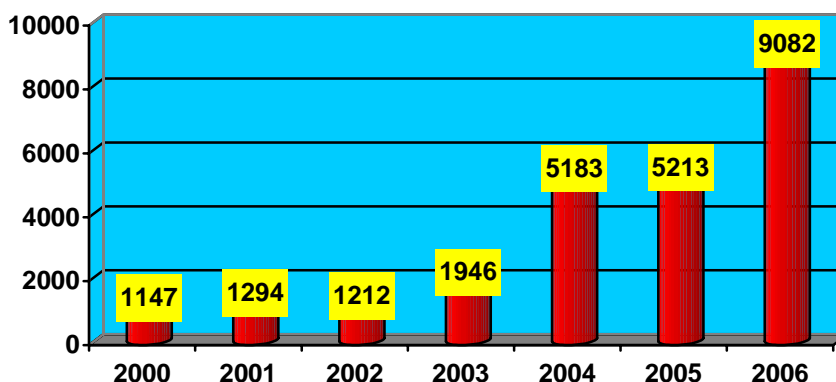
These improvements resulted in robust GDP growth for five consecutive years. In addition, inflation and interest rates declined steadily, the fiscal deficit was brought under control, foreign exchange reserves increased to historic highs, and external debt was held to comfortable levels. Export growth remained vigorous, fuelled by private investment and the initial competitive depreciation of the lei currency. The competitiveness of the enterprise sector was boosted by productivity gains.

### GDP evolution for Romania



Romania is now a visible and attractive destination for international investors as a result of better sovereign ratings and improved access to international capital markets. As a result, after two years of stagnation (2004, 2005) the FDI value increased from above 5.000 million Euro to 9.000 million Euro. In Bulgaria, Foreign direct investment reached a record high of € 2400.4 million in 2005, corresponding to 11.2% of GDP.

### FDI in Romania mil. Euro



Source: Romanian National Bank

Romanian economic policy will focus in the short term on the remaining large privatizations, restructuring the energy sector and investing in health, education and infrastructure. Fiscal consolidation will become more important after 2008, once the parliamentary election is out of the way, as the authorities seek to contain external deficits.

Strong domestic demand will result in real GDP growth of 6.4% in 2007, following estimated growth of 7.7% in 2006. Growth is expected to average more than 4% per year in 2008-11. There will be a slowdown in 2010-11, owing to efforts to bring down inflation, as Romania strives to meet the criteria for euro adoption, although Romania is not likely to enter the euro zone until around 2013-14.

### **The perspectives for Romania**

It is expected a further rise in the current-account deficit in 2007-08, and a modest decline thereafter to just over 10% of GDP by the end of the forecast period. Coverage of these deficits by foreign direct investment (FDI) will decline markedly after 2007, increasing Romania's dependence on the international capital markets.

Key indicators	2006	2007	2008	2009	2010	2011
Real GDP growth (%)	7.7	6.4	5.6	4.4	3.8	3.7
Consumer price inflation (av; %)	6.6	4.4	4.6	4.0	3.2	3.0
General government budget balance (% of GDP)	-1.7	-3.0	-3.0	-2.2	-2.1	-1.6
Current-account balance (% of GDP)	-10.9	-12.3	-12.9	-11.7	-11.3	-10.5
Commercial bank lending rate (end-period; %)	13.5	15.0	12.6	11.0	9.0	8.0
Exchange rate Lei:US\$ (av)	2.81	2.61	2.62	2.65	2.68	2.66
Exchange rate Lei:€(av)	3.52	3.47	3.54	3.43	3.40	3.35

### **Human development in these two countries**

As a result of this solid economic growth, the unemployment decreased in the last five years at above 5% in Romania and 10% in Bulgaria, but it is necessary to take into consideration the relative high level of emigration encouraged by low pay, poor working conditions and bad public services which may create serious problem. As many as 2,000,000 Romanians and 800,000 Bulgarians live abroad. Entry into the EU may stimulate emigration, though most existing members have slapped on temporary labor-market restrictions. That is partly because immigrants from Poland and other countries were more numerous than expected. EU member states such as the UK and Ireland, which had previously pursued an open-door policy with respect to immigration from new member countries, have imposed restrictions on migrant workers from Romania. This may turn out to be a blessing in disguise for Romania, which already faces labor shortages in some sectors. In order to minimize the macroeconomic, demographic and social negative effects of the emigration, both countries should implement coherent policies.

In order to have a complete view about the quality of life in these two countries it's interesting to compare their Human Development Index, a comparative measure of life expectancy, education and standard of living for countries worldwide. Taking into consideration these criteria, Bulgaria is on the 54<sup>th</sup> place with HDI of 0.816 and Romania on the 60<sup>th</sup> place with an index of 0.805, both countries falling into the first category of countries with a high human development which includes 62 countries.

A low evaluation of the quality of society in Bulgaria and Romania has its roots in the economic, social and political context of these two countries. The countries' transition has led to profound changes in economic and social structures, which are often associated

with negative processes such as a weakening of social control, increased crime, widespread corruption, and greater income inequalities and polarization. All of these factors, in turn, seem to have affected the feelings of people in Bulgaria and Romania in relation to the quality of the society in which they live

The accession of Bulgaria and Romania opens new opportunities for Europe, but also significant challenges. The EU of 27 Member States will become even more heterogeneous in terms of cultures, political traditions, level of economic development and living conditions. The research has revealed large discrepancies in quality of life between the two candidate countries and the EU25, especially with regard to material living conditions, quality of employment and working conditions, health and subjective well-being.

## Challenges

Bulgaria faces a number of challenges, such as the following:

- *Increasing employment opportunities.* Reducing unemployment based on private sector-led growth requires a better business climate for job creation, improved skills among the population through education and training, increased labor-market flexibility, and the implementation of well-targeted employment services.
- *Improving governance.* Weak governance is limiting investment and constraining the business climate. Governance needs to be improved through aggressive implementation of anti-corruption measures, public administration and judiciary reform, and the strengthening of local government.
- *Modernizing education and health services.* Like many transition countries with aging populations, inadequate delivery systems, and excess infrastructure, the modernization of education and health services poses a major challenge. Substantial reforms and investment in the education and health sectors will be required to reverse the deterioration in social indicators and to improve Bulgaria's competitiveness.
- *Investing in physical infrastructure.* Strengthening transport infrastructure would enhance Bulgaria's competitiveness. Management and delivery of water, management of waste water and waste services should be improved at the municipal level.
- *Tackling poverty.* Despite overall poverty reduction, pockets of poverty persist among certain groups, particularly the unemployed, the ethnic minorities (mainly the Roma), and large households. While the growth agenda is expected to have a positive impact on poverty, accompanying initiatives to address regional disparities, increase employment, and improve the living standards of vulnerable groups through targeted poverty interventions will be needed to mitigate the impact of reforms.
- *Improving external balances.* Large current account deficits over the past five years are likely to continue. A continued inflow of foreign investment is needed to finance the current account deficit and sustain an adequate level of reserves.

As Romania strives to alleviate poverty and to meet its EU integration commitments, it faces a number of challenges, such as the following:

- *Accelerating structural reforms.* Key challenges include completing the privatization agenda, improving the business climate by eliminating administrative barriers, and implementing a transparent, predictable and efficient tax system. These

reforms are aimed at enhancing revenue collection in order to co-finance the absorption of the EU Structural and Cohesion Funds that Romania would receive after accession.

- *Reforming public institutions and improving governance.* Public services need to be delivered in a manner which benefits the population. This can be achieved through the development of a merit-based civil service that is adequately remunerated. A supportive legal and regulatory framework is also necessary.

- *Reforming the legislative process and the judiciary.* In the past, reforms were impeded by frequent changes in legislation and the lack of capacity to implement new laws. It is therefore essential to streamline existing legislation and develop an effective system to pass new laws. In addition, the professionalism and integrity of judges must be enhanced and the independence of the judiciary strengthened. The judicial process also needs to be improved through greater speed and efficiency in the courts.

- *Reforming the pension system.* Despite recent parametric reforms, the public pension system faces significant challenges deriving from the aging of the population, the demographic structure, and poor revenue collection performance. Further reforms are needed to ensure medium and long term financial sustainability and higher pensions.

- *Developing rural areas and reducing poverty.* With the majority of Romania's poor living in rural areas, agricultural sector reforms are essential to reduce the country's high levels of poverty. Although Romania has fertile agricultural land, vast tracts of forest and a rich network of rivers, its rural areas suffer from inadequate infrastructure and inefficient agricultural production. In addition, access to education and social services in these areas must be improved.

- *Reforming the energy sector.* Although energy sector reforms have been impressive, the restructuring should continue mainly in the generation sector. The privatization of electricity generation companies has been delayed, affecting the sector efficiency and the competitiveness of the power sector within the European market.

The European Union is increasingly being characterized by a variety of economic, social and cultural differences among its Member States. Thus, an important focus of EU social and economic policy is to foster economic and social cohesion in order to reduce the inequalities that are currently visible across Europe, lowering the gap between older and new Member States with respect to living and working conditions.

Romania has the advantage of size, demography and newly confident elite that wants to put the country on the map of Europe. Bulgaria has a stronger industrial base. But given the political chaos that has taken hold in other eastern European countries, most of them much richer and stronger than the two newcomers, it is clear that the Balkan pair's road to EU prosperity and stability will be harder. The only question is how much.

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## ROMANIA IN THE EUROPEAN UNION: POLITICAL INTEGRATION VS. ECONOMIC INTEGRATION

FLAVIA ANGHEL AND BOGDAN GLĂVAN\*

### Abstract

*Although highly beneficial from a pragmatic point of view, Romania's accession in the European Union is problematic, especially in the long run and from a theoretical perspective. In the short run, adoption of european model emphasizes the advantages of economic integration. In the long run however, political considerations can dominate economic liberties.*

### Motto:

“Frankfurt, Bremen, Hamburg, Luebeck are large and brilliant, and their impact on the prosperity of Germany is incalculable. Yet, would they remain what they are if they were to lose their independence and be incorporated?” (Johann Wolfgang von Goethe, *Maximen und Reflexionen*, 1828).

Romania's accession in E.U. is, undoubtedly, a moment worth celebrating. It has a huge signification as romanians join with full rights a family of peaceful and prosperous people.

Still, there is a price for Romania's accession in E.U. This price is not related, as some are tempted to think, to the fact that Romania can become a “market” for western commodities or to the fact that romanian government would lose its capacity to grant privileges to crony businesses. The real price of european integration is the danger of conflating the “aquis communautaire” with the optimal institutional recipe for Romania's development.

Essentially, there are only two ways to allocate resources in society: the economic way and the political way. The former reflects the process of voluntary interaction among individuals searching for a better satisfaction of their needs. For this we can use alternatively the better known expression “market process” or “capitalism”. The political way implies the employment of coercive methods by the state authorities, which are also stimulated to fulfill their own interests. For this we can use as synonymous the words “socialization”, “centralization” or “central planing”.

For a long time, Romania's economy has been characterized by forced allocation of resources through political directives issued by the government. This situation persisted many years after the official fall of the communist political regime, due to an aggressive form of interventionism.

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Romania's accession to E.U. is beneficial because it weakens the mechanism used by the political authorities to exploit the wealth of the productive members of society to the benefit of interest groups specialized in rent-seeking. But it is insufficient because it does not acknowledge and consequently does not solve the inherent problem plaguing the political allocation of resources. In last instance, few people realize the reason for which European institutions and legislation are better than domestic ones. Often, most analysts emphasize the superiority of E.U. institutions in terms of "simplicity", "transparency" and "efficiency". These features are not essential for the advancement of the final goal – general wellbeing. Simplicity and transparency in legislation are not inherently good. For example, minimal law legislation, and, for that matter, all legislation about fixing prices, is very simple and clear. Moreover, if penalty for those who do not obey the law is high enough, then the law is also very "efficient", that is it will be observed probably in all situations. However, economists generally admit that such a piece of legislation has strong negative effects on economic development.

In fact, these criteria are not decisive. The crucial reason is the compatibility with the economic order based on private property and individuals' freedom of action within the framework provided by their property. Incidentally, the most basic principle of European Union, namely the freedom of circulation for labor, goods and capital, is consistent with this criterion. Consequently, the adoption of the main tenets of European legislation will have a significant positive impact on Romanian economy. For example, elimination of trade barriers will increase trade relations and deepen the social division of labor. Also, integration requires complete liberalization of energy and communication sectors, with equally positive effects on prices and consumer's satisfaction.

Instead of understanding this, the public at large falls prey to the illusion that "l'aquis communautaire" is the genuine recipe for economic development. E.U. has a specific institutional framework. Since West-Europeans enjoy a higher standard of living, and prosperity is, in turn, dependent on the quality of institutions, it results that European institutional structure won the historical battle against its ideological opponents. According to this perspective then, everything Romania has to do is to achieve a simple "institutional transplant", i.e. copy the European legislation and wait for results.

There is nothing farther from the truth. Economic theory and experience have shown repeatedly that nations grow rich to the extent that their members are free to accumulate wealth, without injuring the property of their fellows. It is true that in general, E.U. institutional framework is more permissive from this point of view. The expropriation of private property through heavy taxation, bureaucracy and discretionary monetary manipulation has been considerably slight in the western part of the continent than in our country. And this is not only an abstract theoretical observation. Having the freedom to choose the state in which they wish to be taxpayers, millions of East-Europeans have voted "with their feet", leaving their native country and going west. Institutional competition (or, from the state's perspective, fiscal competition) is the element which has forced Eastern political authorities to adopt, sooner or later, the West-European model.

However, despite its supremacy, E.U. is only a political organization, and presents the inherent weaknesses of all political organizations. Marinescu and Popescu (2006) illustrate this fact by pointing only to a single aspect of integration: "The Brussels bureaucracy, also called Eurocracy, has developed specific forms of hierarchical coordination and administrative harmonization (read *standardization*) in almost every



domain of public policy. The transposition of the 97.000 pages of European legislation means importing institutions, administrative structures, legal practices and economic policies. The *acquis* illustrates probably the best way the legislation can be turned into a governing (political) instrument, thus creating a radical discrepancy between Legislation (governing regulation) and Law (applying the rule of law through the distinction between good and evil). Moreover, the project of the European Constitution, the longest and most politicized constitution of all times - 270 pages and 70.000 words, in comparison with the only 17 pages and 4.500 words that the USA Constitution counts) is a clear example of European centralism at economic, institutional and political level”.

In the context created by E.U.’s enlargement, the conclusion european institutional model is the proper “recipe” for Romania’s future development is especially problematic. The integration of east-european states into the E.U. reduces the scope of institutional competition, with potential negative repercussions in the future.

Consider, for example, the monetary situation. Monetary competition among states is advantageous for individuals, because it forces governments not to use abusively their privilege as money producer. When a government makes inflation and devalues its currency, the existence of monetary alternatives provides honest citizens with a way to protect their wealth.

Until now, euro has proved to be a safer currency than leu. The perspective of euroization represents one of the factors that determined romanian government to reduce inflation. Yet the european currency is not intrinsically better than leu. It has proved to be more stable in order to resist the competition of other international currencies.

The same with taxation. Competition among states limits the fiscal burden governments can place on their taxpayers’ shoulders. Therefore, diversity and not “harmonization” is the guiding principle of optimal institutional framework. It is worth to mention here the example of Switzerland, a model of fiscal federalism that manage to resist in time. Switzerland is formed by 26 + 1 fiscal jurisdictions, and the marginal income tax varies from 23% to 48% in different cantons. The fiscality reflects, perhaps more than anywhere else in the world, the will of the population, which has access to important political decisions due to the wide-practiced referendum.

In the absence of competition, states are much less stimulated to refrain from committing abusive actions and adopting policies to expropriate productive individuals to the benefit of some interest groups. Yet this is precisely the context created by E.U.’s enlargement.

Until now, romanian state has proved to be more powerful and dangerous than the political establishment called E.U. Romanians are for the moment the winners of dismantling national political authority and adopting “l’aquis communautaire”. However, as its competitors tend to disappear, E.U. will assume naturally the position of Leviathan.

What is the solution, then? In order to find the solution we have to understand that Romania’s integration in the E.U. does not change fundamentally the road to prosperity. Integration represents, first of all, a process of remodeling of the political authority. Society will benefit from this process only to the extent to which political processes of wealth accumulation are weakened and voluntary (free market) methods are enhanced. An opposite situation is equally likely to occur, especially in the long run. And, in some cases, even very fast. See the famous case of european regulations on agriculture which will impact romanian peasants’ life right after our entrance in E.U.

Our chance to avoid repeating past experience lies in understanding the past. The road to prosperity consists in the acceptance of those institutions that generate adequate incentives for economic growth. The foremost institution is the private property right. Free interaction among individuals in society, without legislative and bureaucratic restrictions, is the optimal recipe for development and a better standard of living. The enforcement of mutual voluntary contracts which bring no injury to other people's property is the sufficient condition for promoting general wellbeing. Compared to this, integration in E.U. is only a necessary step, in the current historical context. Outside E.U. it is more difficult to preserve the functioning of a free market economy. This, though, should not make us less vigilant when it comes about defending free market principles inside E.U.

If we analyze the political positions taken by various E.U. officials during the last decades, the danger of extending political power to the detriment of market power is overlooked. Moreover, political unification (centralization) is considered an important complement (if not the crucial determinant) of economic integration. The confusion seems to be fueled by the general use of expression "integration" in all fields of social life. Thus, an essential aspect is overlooked. Economic integration, that is market enlargement, is founded on the framework of private property rights and free competition among individuals to obtain resources for a better fulfillment of their needs. Political integration implies an altogether opposite thing: more ample employment of coercive means and their harmonization at the level of an European super-state; put it shortly, political centralization

What is the projection in the political area of the economic principle of competition among property owners? Since private property rights are the ferment of economic prosperity, then freedom of association represents their necessary political complement. If we are not free to associate with (or separate from) other people, our property right is to that extent affected. In fact, the lack of freedom of voluntary association, in order to achieve any goals people deem important, without bringing any harm to other individuals' property, situates people in a state of slavery.

Therefore, between political integration and economic integration there is a real tension, and not an essential compatibility – as many would think. The former, i.e. political centralization, endangers the latter. If we wish to defend economic integration, then we have to advocate the dismantlement of statist barriers which prevent the free circulation of labor and capital; we have to support the enlargement of free competition among economic agents from different countries within a single European market. Overemphasizing the importance of political integration – centralization of collective decision-making in a super-state, with uniform legislation (regarding taxation and overall regulation of businesses) arising from the democratic principle of "majority rule", endangers the market economy. One should not forget, the complement of economic freedom is political freedom, these two are coextensive.

Therefore, the real solution for increasing Romanians' wellbeing (as well as the prosperity of all Europeans) consists in increasing the scope of competition, both in economic and political field. Political competition arises when individuals exercise their property rights and decide to associate with other people or refuse to do so. It results in a variety of regulations, legislations and customs that individuals adopt voluntarily, and in the possibility of changing them according to individuals' preferences. This process can

have two main outcomes. On the one hand, it can lead to a decrease in the number of different legislation until the most fitted legislation prevails if people adhere spontaneously to it. On the other hand, it can determine a larger institutional variety, if people choose to secede from the previous political organization. Thus, political unification and secession are two aspects of the same phenomenon, equally possible effects of freedom of association.

Based on these considerations, we reject the bureaucratic project of european political unification. Political monopolization realized through the use of coercive means – the lack of the possibility to separate (secede) from actual political organization – affects the fundamental right of free association and paves the way for a more ample attack on private property rights in the future. For those who still believe that coerced “harmonization” among E.U. members do not affect the functioning of the market economy, the recent debate on the issue the working time is an useful example. The existence of a common regulation in this field has a direct impact on the competitiveness of industries located in different regions and, in fact, on the ability of individuals to decide how to employ their labor. The position of Great Britain in this respect reflects a closer sympathy of the fundamentals principles of the market economy than many of other E.U. member states have.

The alternative model of building political communities by consent – jurisdictional and administrative decentralization – serves better the aspirations for prosperity of everybody and is the fortunate complement of “economic liberalization” achieved through european integration.

It is worth quoting the famous french philosopher and political scientist De Jasay: “The road to Brussels is paved with good intentions and the framers of these new constitutional arrangements are motivated by the best political correctness one could desire. They are preparing something that will be neither Soviet Russia nor Nazi Germany. In fact, whether knowingly or not, they are creating a new European constitutional arrangement largely as a reaction to these very same horrors. It is such a pity that they do not see the unintended but very probable effects upon the next generation of what they are now creating. In politics and economics, and perhaps elsewhere too, you often avoid doing harm by refraining from doing anything very much or, in the words of the 18th century French liberal Physiocrats, laissez faire laissez passer. But how will the sons who strive to correct the sins of their fathers learn this important lesson?”

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## RURAL DEVELOPMENT IN EUROPEAN UNION

Iuliana Mircea\*

### Abstract

*The rural development is a very important and complex issue, involving different sectors and policies of European Union. With over half on the population in the 25 Member States of the E.U. living in rural areas, which cover 90% of the territory, rural development is a vitally important policy area. Farming and forestry remain crucial for land use and the management of natural resources in the rural areas, and as a platform for economic diversification in rural communities.*

Rural areas account aprox. 90% of the territory of the European Union and are home to some 50% of the population. While urban people often believe rural areas would be just farms and forests, the reality is quite different. Rural areas in Europe are characterized by extremely diverse physical environments, a broad range of economic activities, unique social networks and century-old cultural traditions. In rural areas we can find industrial production sites and high-tech service centers, but also facilities for the energy and water supply of cities. In some parts of Europe we have unspoiled natural landscapes, in others monotonous cultivation areas, commercial forests, and large recreation facilities, such as theme-parks or ski-slopes

The European Union has had a dedicated rural development policy since 1999. Known as the "second pillar" of the Common Agricultural Policy (CAP), the rural development policy is managed through a legal instrument (the Rural Development Regulation), and absorbs approximately 15% of the total CAP budget.

The rural development is a very complex issue, involving different sectors and policies, such as agriculture, structural policies, social policies, community development and all sorts of local initiatives.

“Rural development” means all the instruments of agricultural policy, which are different from the traditional “market support type” instruments of the Common Agriculture Policy. These policies are aimed still at the structural transformation of agricultural production, including considerations of environmental sustainability. Their actions are targeted primarily at farmers, and their operations mostly remain within the agricultural sector. This type of policy will be referred to as agricultural structural policies.<sup>1</sup>

### **Agri-environmental measures in European Union**

Agri-environment measures are designed to encourage farmers to protect and enhance the environment on their farmland. It provides for paymentsto farmers in return

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<sup>1</sup> Gusztav Nemes, (2005, p.20-21).

for a service – that of carrying out agri-environmental commitments that involve more than the application of usual good farming practice.

Agri-environment measures may be designed at national, regional or local level so that they can be adapted to the particular farming system and environmental conditions, which vary greatly throughout the E.U. This makes agri-environment a potentially precise tool for achieving environmental goals.

Agri-environmental measures are diverse, but broadly speaking, one could say that each measure has at least one of two broad objectives: reducing environmental risks associated with modern farming on the one hand, and preserving nature and cultivated landscapes on the other hand.

Agri-environment commitments have to go beyond usual Good Farming Practice which is defined as encompassing mandatory legal requirements and a level of environmental care that a reasonable farmer is expected to apply anyway. They are compiled in Codes which Regions draw up and submit to the Commission with their Rural Development Plans – this means that a farmer can only be paid, for instance, for environmental commitments that go beyond statutory requirements defined in his regional Code of Good Farming Practice.

These measures designed to rural development began in a few Member States in the 1980s on their own initiative, and was taken up by the European Community in 1985 in Article 19 of the Agricultural Structures Regulation<sup>1</sup>, but remained optional for the other Member States. In 1992 it was introduced for all Member States as an “accompanying measures” to the Common Agricultural Policy reform. It became the subject of a dedicated Regulation<sup>2</sup> and Member States were required to introduce agri-environment measures throughout their territory. In 1999, the provisions of the Agri-environment Regulation were incorporated into the Rural Development Regulation<sup>3</sup> as part of the “Agenda 2000” CAP reform. The aim of their incorporation was to help achieve coherence within Rural Development Plans.

In the last few years it has been a important increase in the area of land covered by agri-environmental contracts in most Member States. For instance, the figure below shows the planned allocation of Rural Development Regulation spending by Member States from 2000-2006.

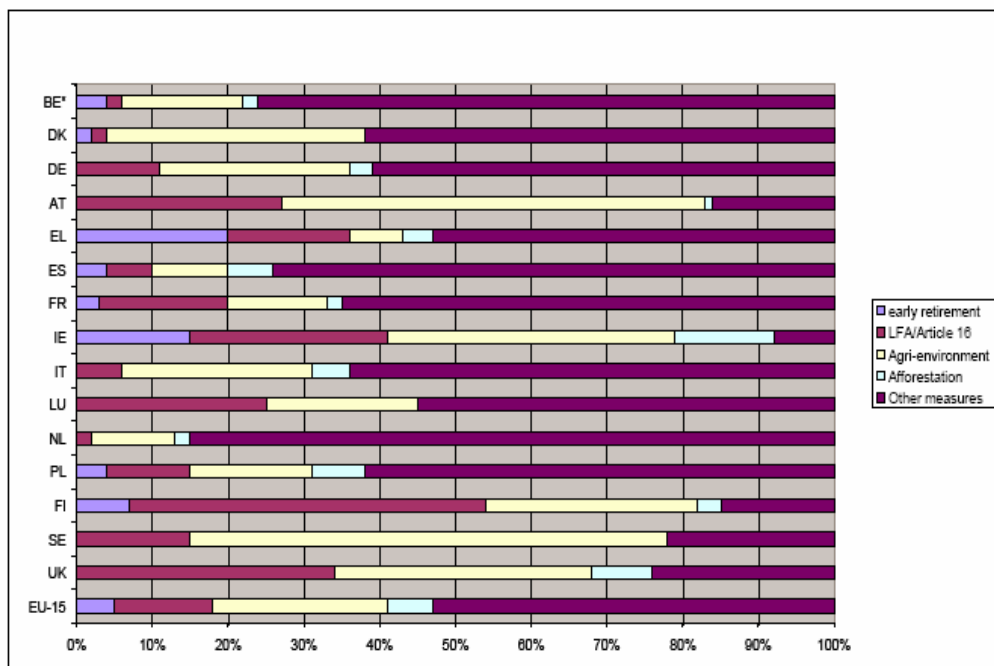
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<sup>1</sup> Council Regulation (EEC) No. 797/85 of 12 March 1985 on improving the efficiency of agricultural structures, OJ L 093, 30.3.1985, PP. 1-18;

<sup>2</sup> Council Regulation (EEC) No. 2078/92 of 30 June 1992 on agricultural production methods compatible with the requirements of the protection of the environment and maintenance of the countryside, OJ L 215/85, 30.6.1992;

<sup>3</sup> Council Regulation (EEC) No. 1257/99 of 17 May 1999 on support for rural development from the European Agricultural Guidance and Guarantee Fund (EAGGF), OJ L 160/99, 26.6.1999;

## Planned allocation of Rural Development Regulation spending in E.U. 2000-2006



### The principles of agri-environmental measures

Agri-environment measures follow a number of basic principles which are essential to the policy achieving its environmental objectives:

- agri-environment is optional for farmers, who may choose to sign a contract to carry out one or more measures designed to provide an environmental service. This optional nature tends to promote constructive cooperation and a positive attitude to the environment on the part of farmers;

- agri-environment is a specific policy: these measures can be tailored to different agronomic and environmental circumstances, which allows for a wide variation in both these parameters throughout the E.U. and within each Member State. These have chosen to implement the policy in very diverse ways. This policy enables agri-environment to be a highly refined tool for environmental integration, able to achieve certain environmental results which are not possible for other instruments;

- the diversity of measures and environmental situation and the long lead-in time for some of the environmental effects to be perceivable, requires a structured and long-term approach to monitoring and evaluation;

- agri-environmental contracts compete economically with the most profitable land use, so payment levels have to be set sufficiently high to attract farmers to join schemes while avoiding over-compensation. This requires a calculation of appropriate payment levels by Member States;

- agri-environment payments may only be made for action farmers undertake above the reference level of mandatory requirements as currently defined by codes of “good farming practice”. This ensures the respect of the Polluter Pays Principles which requires that private actors have to bear the costs of rectifying or avoiding damage to the environment;

- Member States have a wide degree of discretion in how to implement agri-environment measures. This means that wider contextual and institutional issues as well as attitudes have a great influence on agri-environment measures uptake and their environmental effectiveness.

Agri-environment measures are established by Member States or Regions and submitted to the Commission for approval as part of their Rural Development Plans. Sometimes new measures or amendments are submitted during the programming period. The proposed measures are examined in detail by the Commission services to check their conformity with the Regulation. Where necessary, discussions take place between the Commission services and the Member State/Region to see how the measures can be improved. The proposals are then put for an opinion to the Committee on Agricultural Structures and Rural Development (STAR), which is a Committee of Member State representative, chaired by the Commission approval, the measures can be implemented.

### **Measures and their objectives**

Impacts of agri-environment measures are complex to analyse. The classical approach to evaluation would be to relate each measure to its environmental impacts, and then to draw some more general conclusions about the impacts of the measures as a whole. This is often not possible as there is insufficient empirical material available to relate each measure to the environmental situation observed. It is particularly difficult to isolate the effect of agri-environmental measures from those of the many other drivers that influence environmental outcomes.

In order to facilitate understanding about the diversity of agri-environment measures included in the Rural Development Plans, a list of the main categories of measures is set out below. With each category is a brief description of the sort of environmental impact one might expect such measures to have. The real impact might vary from measure to measure, both because of differences in each measure’s focus and design, and because of differing local conditions where the measure is applied.<sup>1</sup>

#### 1. Measures related to productive land management:

- Input reduction – these measures includes reductions in fertilizers and plant protection products. This can be combine with crop rotation measures and also other measures such as organic farming. Expected impacts include: securing water quality, enhance biodiversity and soil quality.

- Organic farming – this is defined and controlled approach to farming which incorporates a wider range of measures: enhanced soil quality, preserving water quality and biodiversity enhancement.

- Extensification of livestock – this can be expected to have positive effects on

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<sup>1</sup> Agri-environment Measures, European Commission, Directorate General for Agriculture and Rural Development, March 2005;

water quality, soil quality, biodiversity and landscape preservation.

- Conversion of arable land to grassland and rotation measures – conversion of arable land to grassland can have positive effects on water quality, water quantity, soil quality, biodiversity and landscape.

- Actions in areas of special biodiversity/nature interest – measures to promote biodiversity in such areas are many and diverse and include postponing mowing dates to protect nests, the establishment of buffer strips and input reduction. There may be secondary positive effects on water quality and quantity.

- Genetic diversity – this measure type concerns the rearing of rare local breeds indigenous to the area and in danger of being lost to farming and the preservation of plant genetic resources naturally adapted to the local and regional conditions and under threat of genetic erosion.

- Farmed landscape – it refers to maintaining farming system which lead, as a side effect, to characteristic landscape. Such measures generally have positive impacts on biodiversity.

- Water use reduction measures – these are designed to preserve water resources by reducing irrigation and/or reducing water loss from the soil by growing ground cover.

## 2. Measures related to non-productive land management:

- Set aside – set- aside managed for environmental purposes could be expected to have positive impacts on biodiversity, water quality and soil erosion. Measures include both large areas of set-aside and small ones such as uncultivated field strips. It is worth noting that set-aside, in order to have positive environmental effects, must be implemented according to site-specific circumstances and often needs to be combined with appropriate management.

- Upkeep of abandoned farm land and woodland – this can be expected to be positive for biodiversity by continuing to provide habitats for farming-dependent species of plants and animals, and it will be positive for the landscapes. It may also help avoid fires and this in turn is positive for biodiversity and soil erosion.

- Maintenance of the countryside and landscape features – this category seeks to protect landscape features such as linear features (hedges, stone walls) and point features (isolated trees, ponds ). These measures will very often have positive impacts not only on landscape, but also on biodiversity.

- Public access – this category of measures seek to provide access for the public to agricultural land of environmental interest.

## **Rural Development policy 2007-2013**

On 20 February 2006 the Agriculture Council adopted EU strategic guidelines for rural development. This guidelines set out a strategic approach and a range of options which Member States could use in their national strategy plans and Rural Development programmes.<sup>1</sup>

The guidelines aim at the integration of major policy priorities as spelt out in the

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<sup>1</sup> Council Decision on 20 February 2006 on Community strategic guidelines for rural development (programming period 2007 to 2013), (2006/144/EC);



conclusions of the Lisbon and Goteborg European Councils. On the basis of these strategic guidelines, each Member State will prepare its national strategy plan as the reference framework for the preparation of rural development programmes. This strategic guidelines are:

- a) Improving the competitiveness of the agricultural and forestry sectors;
- b) Improving the environment and the countryside;
- c) Improving the quality of life in rural areas and encouraging diversification;
- d) Building Local Capacity for Employment and Diversification
- e) Translating priorities into programmes
- f) Complementarity between Community Instruments.

The future Rural Development policy 2007-2013<sup>1</sup> will focus on three areas in line with the three thematic axes laid down in the new rural development regulation: improving competitiveness for farming and forestry; environment and countryside; improving quality of life and diversification of the rural economy. A fourth axis called "Leader axis" based on experience with the Leader Community Initiatives introduces possibilities for locally based bottom-up approaches to rural development.

### **Leader+**

Leader+ is one of four initiatives financed by European Union structural funds and is designed to help rural actors consider the long-term potential of their local region. Encouraging the implementation of integrated, high-quality and original strategies for sustainable development, it has a strong focus on partnership and networks of exchange of experience. A total of EUR 5046.5 million for the period 2000-2006 has been spent, of which EUR 2.105,1 million was funded by the EAGGF Guidance section and the remainder by public and private contributions.

Leader will be in 2007-2013 in its fourth generation after the implementation of Leader I, Leader II and Leader+ initiatives. Currently, under Leader+. 893 LAGs (Local Action Groups) operate in the EU-15. In the EU-10, a similar measure has been implemented in six of the new Member States with more than 100 LAGs foreseen. In the EU-15, around 52 million people are covered by the territories where the local action groups are implementing their local development strategies.

Leader+ is structured around three actions, in addition to technical assistance:

- Action 1: support for integrated territorial development strategies of a pilot nature based on a bottom-up approach. Implementation of Action One is through Local Action Groups selected in an open procedure based on the criteria laid down in the programmes. These include the rural nature of the territories, their homogeneity in physical, economic and social terms, and integrated and innovative development plans. Economic and social partners and associations must make up at least 50 % of the local partnership, and the relevance and effectiveness of this partnership is also taken into account.
- Action 2: support for cooperation between rural territories. This action applies to

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<sup>1</sup> Council Regulation (EC) No. 1698/2005 of 20 September 2005 on support for rural development by the European Agricultural Fund for Rural Development, OJ L 277, 21.10.2005;

rural territories selected under action 1 (integrated rural development strategies) and is implemented under the responsibility of a coordinating LAG. It expressly provides for the encouragement and support for cooperation between rural territories, and foresees cooperation taking place between regions in the same Member State (interterritorial cooperation) and between at least two Member States (transnational cooperation).

- Action 3: networking. In each Member State a National Network Unit exists to: collect, analyse and disseminate information at the national level on good practice; organise the exchange of experience and know-how; and provide technical assistance for cooperation (as above). Active participation in the network is mandatory for Leader+ local action groups.

Taking into account the particular characteristics of the initiatives, the evaluation of Leader+ involves several levels of implementation and target definition:

a) At the European level, there are a series of overall and specific objectives that must be considered when implementing the programme. The way in which these objectives have been taken into account in the elaboration of the programme makes part of the ex ante evaluation;

b) At national/regional level for each of the programmes, there must be a definition of the specific objectives for the implementation of Leader+. These objectives which are specific to the programmes presented under the initiative and which aim at specific problems of the territory envisaged are different from, even though complementary to the objectives of the Community initiative. In order to avoid confusion, during the rest of the document they will be referred to as “programme-specific objectives”. The assessment of the coherence, relevance and expected impact of these programme-specific objectives is also an integral part of the ex ante evaluation;

c) Finally, the objective defined at the LAG level should comply with the objectives at the two former levels. Insofar as they are reflected in the selection criteria formulated in the programme, they make part of the ex ante evaluation.

The rural development policy in European Union evolved as part of the development of the CAP, from a policy dealing with the structural problems of the farm sector to a policy addressing the multiple roles of farming in society and, in particular, challenges faced in its wider rural context.

Rural development remains the key tool for the restructuring of the agriculture sector, and to encourage diversification and innovation in rural areas. On the one hand, rural development can help promote competitiveness in the agricultural and food processing sectors. On the other hand, local initiatives, such as Leader, can play an essential role in connecting people to European ideas and encouraging innovation and entrepreneurship.

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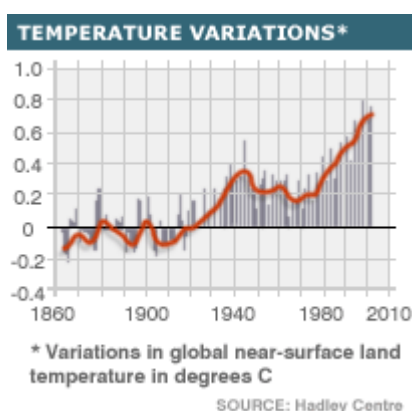
## CLIMATE CHANGE IN THE EUROPEAN UNION

Anda Veronica Dan\*

### Abstract

*It is now universally accepted that climate change is happening and that is caused by man's behaviour. Global warming is accelerating and the average temperature is likely to rise up to 4 degrees by the end of this century if nothing is done. The European Union has risen the occasion by putting in place the world's most famous ambitions global strategy for combating climate change.*

Climate change is one of the greatest environmental, social and economic threats facing the planet. The warming of the climate system is unequivocal, as is now evident from observations of increases in global average air and ocean temperatures, widespread melting of snow and ice, and rising global mean sea level. The ten warmest years on record all occurred after 1991. Since the beginning of the 90s, climate change has moved up high on the international and European political agenda. The Earth's average surface temperature has risen by 0.76° C since 1850. Most of the warming that has occurred over the last 50 years is very likely to have been caused by human activities. In its Fourth Assessment Report (AR4), published on 2 February 2007, the Intergovernmental Panel on Climate Change (IPCC) projects that, without further action to reduce greenhouse gas emissions, the global average surface temperature is likely to rise by a further 1.8-4.0°C this century. Even the lower end of this range would take the temperature increase since pre-industrial times above 2°C, the threshold beyond which irreversible and possibly catastrophic changes become far more likely.



Projected global warming this century is likely to trigger serious consequences for humanity and other life forms, including a rise in sea levels of between 18 and 59 cm which will endanger coastal areas and small islands, and a greater frequency and severity

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of extreme weather events. Human activities that contribute to climate change include in particular the burning of fossil fuels, agriculture and land-use changes like deforestation. These cause emissions of carbon dioxide (CO<sub>2</sub>), the main gas responsible for climate change, as well as of other 'greenhouse' gases. To bring climate change to a halt, global greenhouse gas emissions must be reduced significantly. The European Union is at the forefront of international efforts to combat climate change and has played a key role in the development of the two major treaties addressing the issue, the United Nations Framework Convention on Climate Change (1992) and its Kyoto Protocol, agreed in 1997<sup>1</sup>.

In a report, published in January 2007, EU: *Climate change will transform the face of the continent* by Michael McCarthy and Stephen Castle, marks a step change in Europe's own role in pushing for international action to combat climate change, as it will be used in a bid to commit the EU to ambitious new targets for cutting emissions of greenhouse gases. "Climate change will alter the supply of European ecosystem services over the next century," the report says. "While it will result in enhancement of some ecosystem services, a large portion will be adversely impacted because of drought, reduced soil fertility, fire, and other climate change-driven factors. Europe can expect a decline in arable land, a decline in Mediterranean forest areas, a decline in the terrestrial carbon sink and soil fertility, and an increase in the number of basins with water scarcity. It will increase the loss of biodiversity."

The report predicts there will be some European "winners" from climate change, at least initially. In the north of the continent, agricultural yields will increase with a lengthened growing season and a longer frost-free period. Tourism may become more popular on the beaches of the North Sea and the Baltic as the Mediterranean becomes too hot, and deaths and diseases related to winter cold will fall.

But the negative effects will far outweigh the advantages. Take tourism. The report says "the zone with excellent weather conditions, currently located around the Mediterranean (in particular for beach tourism) will shift towards the north". And it spells out the consequences.

"The annual migration of northern Europeans to the countries of the Mediterranean in search of the traditional summer 'sun, sand and sea' holiday is the single largest flow of tourists across the globe, accounting for one-sixth of all tourist trips in 2000. This large group of tourists, totalling about 100 million per annum, spends an estimated €100bn (£67bn) per year. Any climate-induced change in these flows of tourists and money would have very large implications for the destinations involved."

While they are losing their tourists, the countries of the Med may also be losing their agriculture. Crop yields may drop sharply as drought conditions, exacerbated by more frequent forest fires, make farming ever more difficult. And that is not the only threat to Europe's food supplies. Some stocks of coldwater fish in areas such as the North Sea will move northwards as the water warms.

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<sup>1</sup> Decision No 280/2004/EC of the European Parliament and of the Council of 11 February 2004 concerning a mechanism for monitoring Community greenhouse gas emissions and for implementing the Kyoto Protocol.

There are many more direct threats, the report says. The cost of taking action to cope with sea-level rise will run into billions of euros. Furthermore, "for the coming decades, it is predicted the magnitude and frequency of extreme weather events will increase, and floods will likely be more frequent and severe in many areas across Europe."

The number of people affected by severe flooding in the Upper Danube area is projected to increase by 242,000 in a more extreme 3C temperature rise scenario, and by 135,000 in the case of a 2.2C rise. The total cost of damage would rise from €47.5bn to €66bn in the event of a 3C increase.

Like it was said before, the European Commission wants to hold back the rise in global temperatures to 2C above the pre-industrial level (at present, the level is 0.6C). To do that, it wants member states to commit to cutting back emissions of carbon dioxide, the principal greenhouse gas, to 30 % below 1990 levels by 2020, as long as other developed countries agree to do the same.

The EU has been taking serious steps to address its own greenhouse gas emissions since the early 1990s. In March 2000 the Commission launched the European Climate Change Programme (ECCP). The ECCP has led to the adoption of a wide range of new policies and measures. Among these is the pioneering EU Emissions Trading Scheme<sup>1</sup>, launched on 1 January 2005, which has become the cornerstone of EU efforts to reduce emissions cost-effectively.

Monitoring data and projections indicate that the 15 European Union members at the time of the EU's ratification of the Kyoto Protocol in 2002 (EU-15) will reach their Kyoto Protocol target for cutting greenhouse gas emissions. This requires emissions in 2008-2012 to be 8% below 1990 levels. However, Kyoto is only a first step. Ambitious action to reduce global emissions is needed after 2012, when Kyoto's targets expire, in order to limit global warming to 2°C. In January 2007 the European Commission set out proposals and options for achieving this in its Communication "Limiting Global Climate Change to 2 degrees Celsius: The way ahead for 2020 and beyond".

### *EU Kyoto commitments<sup>2</sup>*

Since the end-90s, the EU has committed itself to play a global leadership role as regards the fight against global warming. After the American government decided to withdraw from Kyoto, the EU used all its diplomatic power to keep other countries (esp. Russia) to their word and succeeded in getting enough countries to sign. On the other hand, its own Lisbon priorities (competitiveness, jobs and economic growth) prevented the Union from making climate change policy really one of its main concerns. The fact that climate change is still seen as an environmental issue (and therefore dealt with by DG Environment) is significant.

### *The European Climate Change Programmes (ECCP)*

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<sup>1</sup> Directive 2003/87/EC of the European Parliament and of the Council- for the European Trading Scheme.

<sup>2</sup> The Kyoto Protocol enters into force in February 2005.

The first ECCP was launched in 2000. It is a stakeholder structure under which the Commission debates with industries and NGOs and prepares new cost-effective measures to fight climate change. ECCP identified and implemented around 30 measures: eg. the emission trading scheme, the "linking directive", the directive on the promotion of electricity from renewables or the voluntary agreement with car producers to reduce CO<sub>2</sub> emissions from cars.

ECCP II started in 2005. It will review what has been achieved with ECCP and focus furthermore on carbon capture and storage, inclusion of the transport sector into the ETS and adaptation policies.

#### *Costs and benefits*

There are large uncertainties and debates over the costs and potential benefits of mitigating climate change. It is therefore necessary to find the most cost-effective solutions to reducing greenhouse gas emissions. The most extensive study on the costs of climate change mitigation, the UK's 2006 Stern Report estimated that the cost of action can be limited to 1% of global GDP each year.

On 27 October 2006, the **European Environment Agency** warned that, with existing measures, only two EU-15 countries (Sweden and UK) would reach their reduction targets. With these existing policies only, the EU-15 is on track to reach only a 0.6% reduction by 2010. Additional policies and measures in the context of the Kyoto flexible mechanisms and actions related to carbon sinks, will be needed to reach the 8% reduction goal by 2012. Also, European industry has expressed worries that the EU's climate change policy might undermine its competitive position in the world economy. It has, on several occasions, criticised the EU's "going-it alone" strategy and has underlined the need for global solutions. On the other hand, Green NGOs, think that EU policies do not go far enough. NGOs pointed to a lack of urgency and to shortcomings in EU policy. In a joint position paper for the start of ECCP II, CAn Europe, Friends of the Earth, Greenpeace and WWF demanded a thorough review of the first ECCP and more ambitious targets and policies. Despite all of those opinions, the Commission has published a positive mid-term review of the 6th Environment Action Programme (EAP), concluding that implementation is "broadly on track". Looking ahead, the Commission is seeking to develop further actions, particularly with respect to climate change.

The Commission focusses in its mid-term review on European leadership in the battle against global climate change. In the coming years, the Commission intends to capitalise on this leadership by setting "the agenda for a new international agreement" to take effect after the expiration of the Kyoto Protocol in 2012. The Commission also promises to propose an improvement to the emissions-trading system later this year.

In this regard Stavros Dimas stated that even before negotiations on a global agreement start<sup>1</sup>, the EU leaders have agreed that the EU should make a firm, independent commitment to reduce our emissions by at least 20%. There are compelling reasons for making this independent commitment. This will lead to a number of advantages. First, the economic cost of making this independent commitment is limited. It will cost between 0.02 and 0.09 per cent of the European Union's annual GDP. Compared to the consequences of inaction, this is a reasonable price to pay, especially if

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<sup>1</sup> Stavros Dimas-Member of European Commission, responsible for environment- Climate Change: European leadership and the role of the European Parliament, Brussels, 27 March 2007.

the important co-benefits of action in other areas are taken into account. These include increased energy security, efficient use of resources, improved competitiveness through innovation, and significant health benefits from reduced air pollution. This will give a clear signal to economic operators that we are serious about moving towards a low-carbon economy. Therefore it will be saved 20% of energy needs by 2020 by improving energy efficiency. The European Council has also committed itself to legally binding targets for raising the share of renewable energies to 20% and of biofuels to 10% by the same deadline of 2020. It has welcomed the Commission's intention to have up to 12 large scale carbon capture and storage demonstration projects in operation by 2015. Also Mr. Dimas said that, in order to avoid a policy gap after 2012 it is essential that negotiations on a global agreement are launched at the UN ministerial conference on climate change in Bali at the end of the year.

At the same time, in December 2006, it has been proposed a directive to tackle carbon dioxide emissions from aviation by bringing this sector into the EU emissions trading scheme from 2011. CO<sub>2</sub> emissions from aviation have grown almost 90% since 1990, much faster than any other transport sector. By 2020 our approach will save over 180 million tonnes of CO<sub>2</sub> every year – equivalent to twice Austria's annual emissions from all sources today. Also in January it has been proposed a revision of the fuel quality directive that, among other things, requires a 10% cut in greenhouse gas emissions from transport fuels by 2020. Cumulatively this will save around 500 million tonnes of CO<sub>2</sub>, or as much as Spain and Sweden together emit in a whole year. In February 2007, it has been revised the EU's strategy for reducing CO<sub>2</sub> emissions from new cars. The voluntary agreement with the car industry did not deliver and we have decided to propose legislation to reach the long-standing goal of cutting average emissions to 120 grammes per kilometre by 2012. This will be achieved by improvements in vehicle engine technology, down to 130 grammes per kilometre, couple with complementary measures that will deliver the remaining 10 grammes. All of these initiatives have been sent to the Parliament.

Relevant legislative revisions or policy measures are outlined in seven Thematic Strategies that deal with: soil, air pollution, the marine environment, natural resources, pesticides, the urban environment and waste. All seven strategies have been adopted. Also, progress has been made in a number of areas over the past five years. In January 2007, for example, the EU committed to reducing greenhouse-gas emissions to 30% below 1990 levels by 2020.

Another important activity which is planned to take place later this year, will be to propose revisions to improve and strengthen the scheme, in anticipation that it will play a central role in a post-2012 global climate agreement. This revision will broaden emission trading to new sectors and gases, streamline the allocation process and prepare the ground for linking the EU ETS with other trading schemes around the world.

Recently, the Commission president, José Manuel Barroso, gave US President George Bush a preview of the new policy during a visit to the White House. President Bush and European leaders claimed progress in the effort to reduce global warming, largely by agreeing that climate change requires global action without infringing on the rights of nations to choose their own strategies. "I think that each country needs to recognize that we must reduce our greenhouse gases and deal, obviously, with their own internal politics, to come up with an effective strategy," Bush said at a U.S.-European



Union summit at the White House. It was recognized that technology is going to lead to solutions, and that we're willing to share those technologies." The agreement the leaders signed promotes alternative fuels and energy efficiency, with a promise of cooperation on emerging technologies. It is intended to clear a path for a broader discussion about climate change at the G8 summit this June in Germany.

Among latest events that took place in this domain, deserve to be reminded the Commission's propose in January 2007, that EU to undertake a 'unilateral' 20% reduction in greenhouse gas emissions by 2020. Also, in February 2007, the Parliament has adopted a resolution in order to reduce to 30% by 2020 and 60-80% by 2050

If nothing is done, Europe, the richest and most fertile continent and the model for the modern world, will be devastated by climate change . The ecosystems that have underpinned all European societies from Ancient Greece and Rome to present-day Britain and France, and which helped European civilisation gain global pre-eminence, will be disabled by remorselessly rising temperatures, EU scientists forecast in a remarkable report which is as ominous as it is detailed. Much of the continent's age-old fertility, which gave the world the vine and the olive and now produces mountains of grain and dairy products, will not survive the climate change forecast for the coming century, the scientists say, and its wildlife will be devastated. The year 2008 will be a crucial to take forward the Energy and Climate Package. The Annual Policy Strategy for 2008 therefore rightly confirms climate change as a core priority for the Commission.

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## SUPPLY CHAIN FLEXIBILITY

Simona Daniela Grigore\*

### Abstract

*To be flexible means to have the ability to vary as you like, according to the needs. Flexibility is the ability to adapt, in a reversible manner, to an existing situation, as opposed to evolution, which is irreversible. Companies must realize the real competition is not firm-to-firm, but supply chain-to-supply chain.*

### Introduction

One strategy for gaining and keeping a competitive advantage in a dynamic environment is to create a flexible organization.

Flexibility is the organization's ability to meet an increasing variety of customer expectations without excessive costs, time, organizational disruptions, or performance losses.

To be useful in achieving company objectives, flexibility should be viewed from a value chain perspective (satisfying customer needs) rather than from an equipment or process perspective. From a customer's perspective, cross-functional and cross-company efforts are needed to eliminate bottlenecks, increase responsiveness, and create a level of performance that enables firms to build lasting competitive advantage. Therefore, value chain flexibility is broadly defined to include product development, manufacturing, logistics, and spanning flexibilities.

Flexibility may be defined as the ability to change or react with little penalty in time, effort, cost or performance. Flexibility can improve the company's competitiveness, particularly for the decision-making process of implementing technologies. But managers do not have a comprehensive view of flexibility because they focus more on machine flexibility than on total system flexibility.

Flexibility in supply chains may well represent a potential source to improve the company's efficiency and may be a significant measure of supply chain performance.

Supply chain flexibility is defined to encompass those flexibility dimensions that directly impact a firm's customers and are the shared responsibility of two or more functions along the supply chain, whether internal (marketing, manufacturing) or external (suppliers, channel members) to the firm.

### Flexibility: concept and types

Flexibility is a complex and multidimensional concept, difficult to summarise. Flexibility is defined as an attribute of a system technology for coping with the variety of its environmental needs.

Flexibility reflects the ability of a system to change or react with little penalty in time, effort, cost or performance.

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There has even been a proliferation of papers that review the flexibility literature. The published reviews consider different aspects of flexibility such as definitions, classification and measurement of flexibility, choices, interpretation and requests for flexibility:

- functional aspects (flexibility in operations, marketing, logistics),
- hierarchical aspects (flexibility at shop, plant or company level),
- measurement aspects (focused on global flexibility measures vs context specific ones),
- strategic aspects (centred on the strategic relevance of flexibility),
- time horizon aspects (long-term vs short-term flexibility),
- object of change (flexibility of product, mix, volume).

Flexibility types in the manufacturing literature can be reviewed through different frameworks. The classical approach to flexibility frameworks has a bottom-up structure related to a manufacturing hierarchy with three hierarchical flexibility levels:

1. basic- comprise flexibility of the system components: machines, the material handling units and the transporting network.
2. system: the basic flexibility types at the manufacturing system level; an important type of system flexibility with implications for the supply chain system is routing flexibility.
3. aggregate levels: the aggregated attributes of the manufacturing system technology enabling it to cope with the variety of changes and needs at the strategic level.

### **Supply chain flexibility components**

A complete definition of supply chain flexibility components will include the flexibility dimensions required by all the participants in the supply chain to successfully meet customer demand.

Flexibility in the supply chain adds the requirement of flexibility within and between all partners in the chain, including departments within an organization, and the external partners, including suppliers, carriers, third-party companies, and information systems providers. It includes the flexibility to gather information on market demands and exchange information between organizations.

Six components of supply chain flexibility have been identified from the literature on manufacturing flexibility, strategic flexibility and the limited writings on supply chain flexibility:

1. Operations system flexibility (both manufacturing and service) – ability to configure assets and operations to react to emerging customer trends (product changes, volume, mix) at each node of the supply chain.
2. Market flexibility – ability to mass customize and build close relationships with customers, including designing and modifying new and existing products. . A critical need in today's competitive environment is the ability to design and introduce new products as customers' needs, materials, and technologies change.
3. Logistics flexibility – ability to cost effectively receive and deliver product as

sources of supply and customers change (customer location changes, globalization, postponement).

4. Supply flexibility – ability to reconfigure the supply chain, altering the supply of product in line with customer demand. The flexibility of supply includes flexibility in establishing the relationships with partners. Companies may choose to solicit short-term bids, enter into long-term contracts and strategic supplier relationships, form joint ventures, form consortiums, create problem-solving councils or vertically integrate.

5. Organizational flexibility – the ability to align labor force skills to the needs of the supply chain to meet customer service/demand requirements.

6. Information systems flexibility – the ability to align information system architectures and systems with the changing information needs of the organization as it responds to changing customer demand.

### **Dimensions of supply chain flexibility**

Supply chain flexibility takes into account two main aspects:

a. process flexibility of each supply chain plant, concerning the number of product types that can be manufactured in each production site (supplier or assembler);

b. logistics flexibility, related to the different logistics strategies which can be adopted either to release a product to a market or to procure a component from a supplier.

The flexibility dimensions are:

a. Product flexibility, defined in a supply chain framework as the ability to handle difficult, non-standard orders, to meet special customer specifications, and to produce products characterised by numerous features, options, sizes, and colours.

b. Volume flexibility, defined as the ability to effectively increase or decrease aggregate production in response to customer demand). Volume flexibility directly impacts supply chain's performance by preventing out-of-stock conditions for products that are suddenly in high demand or by preventing high inventory levels.

c. Routing flexibility- is the capability of processing a part through varying routes by using alternative machines, flexible material handling, and flexible transporting network; this flexibility reduces the negative impact of environmental uncertainty and unforeseen inefficiencies in the production process.

d. Delivery flexibility is the company's capability to adapt lead times to the customer requirements; an example of high delivery flexibility is JIT, when suppliers deliver the products to the customer at the right quantity, place and time.

e. Trans-shipment flexibility involves movement of stock between locations at the same echelon level where physical distances between the demand locations and the supply locations are small .

f. Postponement flexibility implies the capability of keeping products in their generic form as long as possible, in order to incorporate the customer's product requirements in later stages.

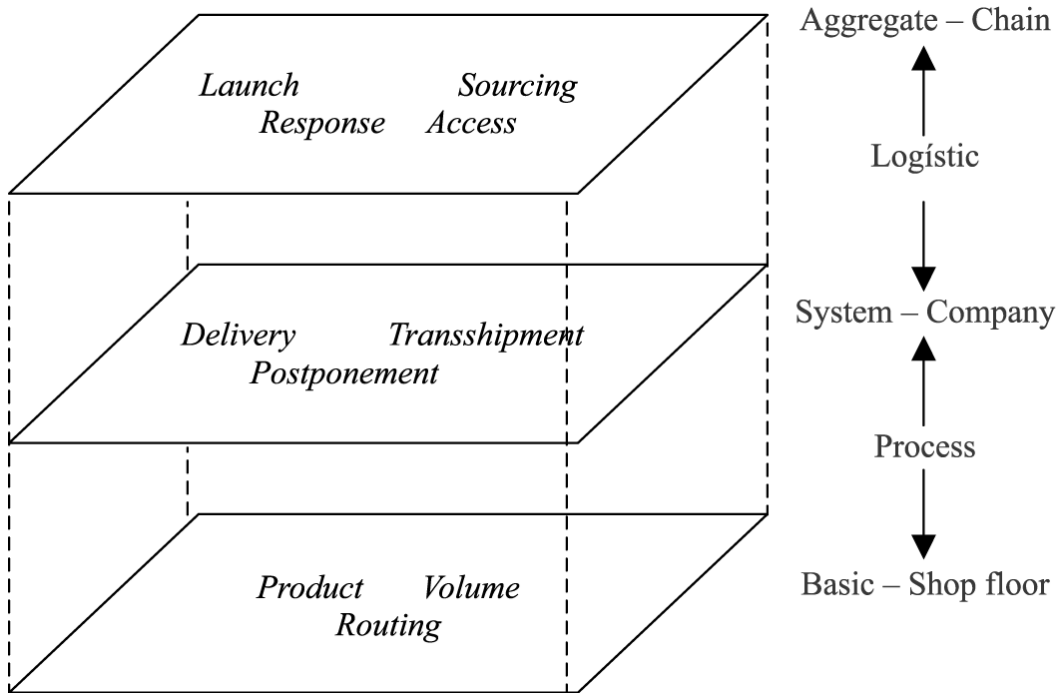
g. Sourcing flexibility is related to the company's ability to find another supplier for each specific component or raw material.

h. A flexibility dimension suitable to many industries is responsiveness to target markets (response to market flexibility). This flexibility captures the overall ability of the firm to respond to the needs of its target markets

i. Launch flexibility – the ability to rapidly introduce many new products and product varieties is a strategically important flexibility that requires the integration of numerous value activities across the entire supply chain.

j. Access flexibility – the ability to provide widespread or intensive distribution coverage. This flexibility is facilitated by the close coordination of downstream activities in the supply chain whether performed internally or externally to the firm.

**Figure 1.** Supply chain flexibility dimensions



Source: Angel Martínez Sánchez, Manuela Pérez Pérez

## Conclusions

To be flexible means to have the ability to vary as you like, according to the needs. Flexibility is the ability to adapt, in a reversible manner, to an existing situation, as opposed to evolution, which is irreversible. This notion reflects the ability to stay operational in changing conditions, whether they are predictable or not, completely different or not from conditions known in advance. This adaptability is required from firms that, for economic reasons, are currently turning to efficient techniques of organization and management of the zero stock, just-in-time and tight-flow type which can make them fragile. Competition amplifies the development of the market by creating new situations. This aspect, combined with the above mentioned techniques of organization, reduces the stability of the firm. The impact of an unexpected event

immediately spreads across the structure because of the increased tension in the coordination links.

Companies used to operate in the context of a market that was prepared – because of the scarcity of the available goods – to absorb all proposed products and services provided if they were consistent enough with demand .

In such a situation the existence of inventories is an essential factor that guarantees uninterrupted operation. Building up stock is justified by the certainty of being able to sell it.

The current economic context leaves the conflict of scarcity more and more behind us, thus removing the certainty of selling; on the contrary, protection by means of stock becomes a danger in itself. Calling production for stock into question has thus led to just-in-time production. This kind of operation makes the production system more vulnerable.

As the classic organization of production, even though it is effective, high costs of operation are generated under these circumstances. It became necessary to create a new, efficient organization, complex to install, but capable of adapting itself continuously while, at the same time, optimizing the time required and the cost of change. This is how the flexible organization was born.

Flexibility in supply chains may well represent a potential source to improve the company's efficiency and may be a significant measure of supply chain performance .

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## THE INSTITUTIONAL CHANGE AND IT'S IMPLICATIONS ON ECONOMIC DEVELOPMENT

Ramona Frunză and Marian Stanciu\*

### Abstract

*The guide in the elaboration of this article was the work of the famous attorney of the new institutionalism, D. North, named "Institutions, Institutional Change and Economic Performance".*

*His central idea was focused on the retaining wall of the necessity of an institutional change that to permit the economic performance. The author observes that the productive activity depends in an essential way by the institutionalization on property rights and by the observance of the contracts. If a system of property is institutionalized in a good manner and in same time he's stable, then we can talk about by a fosterage of the investments on a long term, in these way facilities the productive activity. On the contrary, when the property is affected by risks and raised costs, the peoples will be attracted to the direct gaining based on speculation and on the obtaining of one fairly substantial part by the property existing already.*

*Considering all these, our step try to astound, essentially, the reasons for that the structures of governance must refer at an institutional change in a state, change that must generate the economic performances.*

Nowadays, the study concerning *the institutions* and their impact on economic growth and development represent an important research theme for the contemporary economists.

Why and how do institutions change? How do institutions persist in a changing environment and how do processes that they unleash lead to their own demise? At all these questions we will try to find some answers.

Development of the game theoretic perspective on institutions thus requires extending it to studying institutions as a product of an historical process in which institutions endogenously change. Furthermore, doing so will enhance integration of this perspective with complementary perspectives, such as that of institutional *path-dependence in economics* [North, D., 1990, David, P., 1994, Greif, A., 1994] which says that the institutions from past and the institutional elements are a part of the medium who implies the processes that go to the creation of the new institutions.

After many decades of economic deprivation and political oppression, socialist regimes in the countries of Central and Eastern Europe withered away by the end of 1980 years. The end of socialism created an opportunity for people in these countries to develop better institutions. Indeed, new leaders in the region immediately announced plans for institutional restructuring. In the early 1990s,

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most citizens seemed willing to bear the cost of transition, and free-market ideas enjoyed significant political capital.

The transformation of the Central and Eastern Europe countries socialist economies into capitalist-or free-market, private-property- economies was the new leaders' major stated objective in the early 1990s<sup>1</sup>. Conceptually, genuine capitalism is institutionalized as prescribed by the doctrines of classical liberalism. Its main traits are the rule of law, constitutional democracy, and open markets<sup>2</sup>. The rule of law, which the constitution embodies, guarantees stability and credibility of private-property rights, contractual freedom, and an independent judiciary. Those institutions, often seen as guarantors of so-called *negative rights*, protect individual members of the community from being forced by a majority rule, decision makers in government, labor unions, and other rent-seeking groups to subordinate the pursuits of their private ends to a desired outcome.

James M. Buchanan observes: „ in a rule-of-law state there is an explicit prejudice in favor of previously existing rights, not because this structure possesses some intrinsic ethical attributes, and not because change itself is undesirable, but for the much more elementary reason that only such prejudice offers incentives for the emergence of voluntary negotiated settlements among [individual members of the community] [*Buchanan, J. 1975, p. 52*]. Open markets reflect a network of contractual rights and possibilities based on the rule of law and constitutional democracy. In a world of bounded rationality, open markets provide freely choosing individuals with strong incentives spontaneously to develop, try and accept institutional arrangements („rules of the game,„) that minimize the transaction costs of voluntarily (1) letting resources find their highest-valued uses and (2) accepting the risk associated with the development (innovation) of new opportunities for exchange.

In others words, the institutions that offer greater incentives for voluntary interactions are more efficient than institutions that provide fewer options for free exchange.

The neoclassical type of thinking explain so-called „trinity of the transition process“: the macroeconomic stability, the privatization and the liberalization of prices.

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<sup>1</sup> Although some leaders in Central and Eastern Europe countries believed in the transformation to capitalism, others misunderstood the implications (costs) of capitalism, and still others merely paid lip service to the transition to capitalism in order to please the West and local free-market parties.

<sup>2</sup> The *rule of law* means absence of arbitrary power on the part of the ruling group; subjection of all citizen to the same stable and credible laws, also, to the democratic elections. The absence of discretionary power means that no rule is to be enacted with the intent of helping or harming particular individuals.



Institutional reorganization supposes a destabilization of the rules of community. The politics that over impose the objective of the macroeconomic stability through institutional reorganization can be explained only by the neoclassical suppositions which affirm that it's creating new equilibrium momentary or that it's possible the good adjustment of the economic processes by the govern.

If in the '80 years the option by neoclassical type was for „the retired state,, and for the affirmation of the civil society, at the beginning of '90 years the attention was focused on the role of institutions which can accelerated or stop the development. Since of the beginning of XX century, the attorneys of the old institutionalism T. Veblen and J.R. Commons criticized the economic theories for the ignorance of the role of institutions in the development [Veblen, T., 1948, Commons, J.R., 1961]. This „old institutionalism'' it wasn't resume than later by the economists , through „the new institutionalism'' for analyze the emergence of the markets, the property rights or the state but, especially for explain the differences between the economic performance of the nations.

In other way, the fundamental question is formulated something like that: how can be explaining these differences between the economic performances of the developed states and the underdeveloped states?

Is obviously for everyone that the gap between the riches nations (developed) and those that are poor (underdeveloped) has the tendency to conserve themselves and especially to grow. Afterwards, some states hold for a long period in a stagnation form or economic decline while others states advanced them permanently on the way of the accumulation of wealth. Again, the question is: how can be explaining these divergent tendencies? The theoretical response at all these questions supposed, at the beginning of '90 years, a contest of the neoclassical economic theories and an invocation of the institutions<sup>1</sup> and organizations like explanatory factors of the economic performances. The assumption of this approach is that the models of development, economically or politically, are specific of one institutional context that is the property to vary in function by the historical time or by the geographical space. In consequence, it can't exist an universal model of the development but only institutional alternative models. The institutional constraints has the mission to establish the different type of organizations (firms, trade-unions, political parties), all of these acting in the directions that bringing them maximum of satisfaction [Vlăsceanu, Lazăr, 2001, p. 56].

Accordingly, to analyze the conditions and the frame of the development means to consider the formal and informal rules that regulate the rapports between

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<sup>1</sup> *The institutions* are sets of formal rules (laws, juridical norms, contracts) or informal (values and social norms) that settle the actions of peoples or of organizations and the interactions between the participants at a development process.

the social actors and the organizational frames within they unfolded the activity. These rules aren't only compelling but also incentive, namely not fix only the limits of the activities or exchanges but they are the rewards that can be obtain in a known frame.

Thus, researching the history of the development of different economies, C.D. North affirms: „if the organizations [...] dedicate their efforts on the *unproductive activity* then the institutional constraints offer a structure of incentives for an activity like this one'' [North, D. 1990, p. 92].

The countries of the third world are poor because „the institutional constraints define a set of recompenses of the political/economical activity that not encouraged the productive activity [North, D. 1990, p. 110]. In this direction, C.D. North compares the American economy of the XIX century with the economy of the contemporary countries in development to set off the institutional differences and their divergent effects. The institutional frame that appeared in USA at the beginning of XIX century (*The Constitution*, *The Northwest Ordinance* and the norms by comporment that remunerate the supported labor) would have gone at the development of those political and economical organizations that was centered on the supported labor, productivity, saving, investment and valuing the education. In this context of formal and informal opportunities appeared those organizations that had followed to benefit by stimulants and recompenses available, concomitantly making more powerful the prevalent institutions and continuing their development [Vlăsceanu, Lazăr, 2001, p. 57].

The economic growth was constantly induced by the institutional frame that stimulated the organizations to engage in the productive activities. If we report us at the countries in development we can see that here the institutional frame is a mixture that generate two kinds of opportunities (productive and redistributive) for the political and economical contractors.

In opinion of North, the institutional frame works, in the underdeveloped countries, in a manner that „favored the activities that promote specially redistribution not production, that create monopolies not the conditions of competitiveness and that restrict not extend the opportunities [...]. The organisations that developed in this institutional frame will become more efficient – but they will be more efficient in to make the society more unproductive and the basic institutional structure more generator by unproductive activity. This direction can persist because the transaction costs of the political and economical markets of these economies together with the subjective models of the actors not conduct them to results more efficient “[North, D. 1990, p. 9].

The institutions are identified with „constraints on behaviour in the form of rules and regulations’’ [North, 1981, p.18]. Culture is important to the extend that „moral and ethical behavioural norms aimed to reduce enforcement costs [Levi, M.,1988, p.47].

The new institutionalism examined the variety of institutions but the micro-

economic theories it utilize – transaction cost economics, the theory of property rights and public choice theory – constrained most of its historical analyses to institutions defined and enforced by the state

[Alston, L., and Higgs, R., 1982, p. 28]. This historical analysis is guided by three deductive assertions [Davis, L. and North, D., 1971, p. 19]. *First*, institutions defined and enforced by the state – property rights, rules and regulations- determine economic performance through their impact on transactions costs. *Second*, the economic implications of a given institution change over time due to technological change, population growth, market integration, and other factors. Therefore, the economic outcomes depend on efficient institutional change. Furthermore, the specialization increases transaction cost (holding institutions constant) implying that institutional change is even more important in advanced economies [Wallis, J., and North, D., 1986, p. 126]. *Third*, the institutions are usually inefficient since they are determined through a political process and are influenced by the transaction cost of bargaining.

We consider that the acknowledgement of the importance of the institutions which determine economies to work properly: *private property, contract, free market*. The government structures, which decide in an economy, must make every effort to take the necessary measures to protect a fundamental right, the one to private property, and to try to shape a conception typical for a democracy and free economy.

In the last decades we are witnessing a series of phenomena and processes which characterize mankind evolution and indicates the fact that we are facing a period of profound transformations. Therefore, we argue the idea that economic and social transformation can be conceived only through the specific institutions of market and economic development. The question that raises is: which are the institutions that count in the transition process? How an communist economy can be transformed in an performant market economy? At a first analysis we can state that the most important institutions are those related to the right and protection of property, economic adjustment, macroeconomic stabilization, social protection and the conduct of enterprises in a competitive environment. Yet, the simple realization of them, but without respecting the principles of economic development and the European frame of development, means an effort what could cost Romania another 50 years of attempts and failures.

We emphasize that the differences between national economies of different states concerning growth and development of the economy are given by *the level of development and particularism of the institutions*.

The institutions model the behaviour oriented to accomplishing of some economic objectives. But this becomes possible only if there is compatibility between these objectives and the institutional-cultural values that enable the achieving of them [Thomas, C., Daniel, 2005, p.56].

The institutional measures, the acknowledgement of the property right, the transformation of the state enterprises in capital companies, the privatisation of the public-owned assets, the right of establishing companies, the law of bankruptcy, the adopting of an investment code became the foundation of the new market economy

[Lovell, W. David, 2002, p.32]. The modern institutions differ from all types of social order by their dynamism, by the extent that they undermine the traditional habits and by their global impact.

The reorganization that we assist now, suggests that the actual mutations are equivalent to a radical change of the paradigm. The institutions from a society demonstrate the strongest change resistance. The transformation of the institutions would favorably affect the reaction of individuals and organizations. The institutions and their adaptability are the most that matter for explaining the different growth rates and economical development [North, Douglas, 1990, p.42].

Taking into discussion the case of Romania, after 1989 the emphases fall over the privatizations of the activity of the economic agents, the liberalization of using of the economic levers, the adopting of a series of macroeconomic politics that favored the reorganization of the production according to the economic effectiveness principle.

The reorganization by privatization has arisen numerous controversies and is the subject of a permanent dispute in theory. Romania has known during the past decade an economic decline, being positioned after 1985 in the economic decreasing area that profoundly accentuated after 1989. The complex process of reorganization at the micro level as well as the macro level requires *immense social costs* hard to be supported by the population. The expected investments were quite reduced; no flux of competitive technique and technology has been produced by the new owners. *The investments* that have been made were especially focused on light industry, the food industry, trade and tourism, sectors in which the possibility of investment recovery is more probable. So the reduced investment attracted a high rate of unemployment fact with considerable implications in economic development of our country.

In the actual world economic context, Romania must not only to become a functional state in the competitive economic system of market economy but it must give priority to the economic sectors, its branches and subbranches in the direction of orienting of the national economy through those branches that are not consuming big amounts of natural resources and that offers the possibility of capital accumulation in a short time for this accumulation to be reinvested, so the national investment flux, capable to revitalize the economy to be assured and this to assure also the growth of the living standard of the population.

The institutional analyze demonstrated that the rhythm and the direction of the development are historical dependent, and the discrepancies in the history, through revolutions, not eliminate totally the path dependence<sup>1</sup>, namely by history and will survive and perform the most efficient institutions in the reduction of transaction costs (the capitalist firm for example).

Thus, in a functionalist vision, the institutions, like *incentive alignment* or *governance structures* are the result of the efforts that suppose to minimize the transaction costs. The institution of the modern firm capitalist is, in the opinion of Williamson, the guerdon of *economizing on transaction costs* but not to one historical process of path dependence or of the exploitation of the workers by the capitalists [Williamson, O., 2002, p.37]. The

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<sup>1</sup> *The path dependence* means that the institutions existing at a given moment are in a considerable manner determinate by the precedent institutions, resulting an incrementalist historical evolution

holders of capital had become the owners of the firms who economizing transaction costs but not because of history [Păunescu, Mihai, 2002, p.38]. In the support of these can come so-named „state of development”, namely that state in which „the politic concentrated many power, autonomy and capacity at the central level for model, apply and encourage the realization of one explicit objectives of development, or through the establishment or the promotion of the conditions and direction of economic growth, or through the direct organization of these, or through a mixture of both” [Leftwich, Adrian, 1995, p. 12].

We consider that the institutional change is a necessity in a state for generates de economic performances only if this realizing and imposing concordantly with the just, ethics and morals rules of the society.

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## THE DIMENSION OF THE UNDERGROUND ECONOMY, IN ROMANIA, IN THE PERIOD AFTER 1989

Stela Toader\*

### Abstract

*In the period after 1989, the underground economy in Romania had a constantly ascendent evolution. In this article we think about the distinguishness of the underground economy level and of the real possibilities of Romanian economy through the dimension of the real total gross domestic product, providing a reason seriously enough to amplify the struggle against the phenomenon of the underground economy, especially as a result of our country's integration in the European Union. Practically, starting with the 1st of January 2007, the internal struggle against the underground economy and the fiscal fraude (as assimilated phenomenon) becomes one of the interests of the community, because they will affect, from so on, no only the public budget but also the community's.*

The underground economy had drawn the attention of the specialists starting with the 60's, when this phenomenon took remarkable proportions. The first proceeding where the problem about the underground economy is grasped and made publicly, on a specialized level, belongs to the American P. Gutmann, who, in 1977, appreciated that the statistically unregistered economic activity can't be considered as a negligible entity anymore. In 1989, Pierre Pestieau defined the underground economy as „the whole of the economic activities realized out of the penal, social or fiscal laws, or which gets away of the inventory of the national accounts”<sup>1</sup>.

As concerns this motivation, V. Tanzi<sup>2</sup> sees the development of the underground economy as the product of two grand categories of parameters: those that imply the urge to avoid the taxes, and those that imply the urge to avoid governamental rules and restrictions. Therefore, everything that „gets rid of” the reglementations of the public power allows the possibility of including a variety of practicies under the mark of the „underground economy”: fiscal fraud, working on the black market, drug dealling, illegal trade with weapons, corruption, prostitution, robbery, but also gardening, domestic activities, etc.

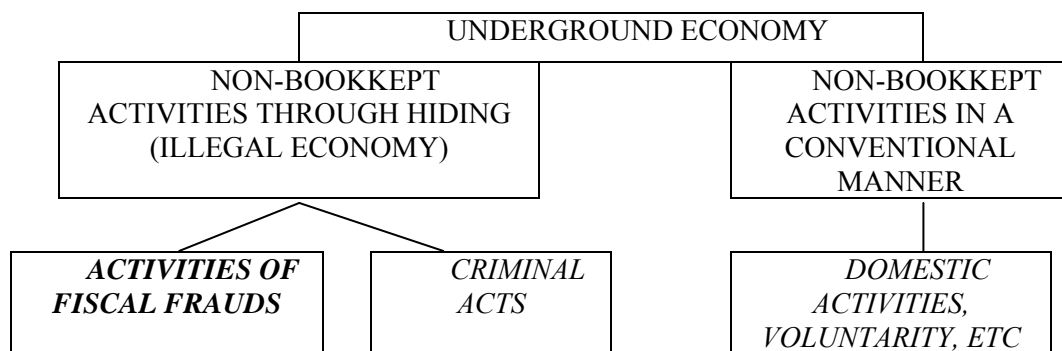
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*Activities asimilated to the concept of underground economy structured according to the relation with national bookkeeping*

The preponderance of a sector or another, the way of acting and the way in which it influences the official economy varies from one country to another, according to the economic and administrative system and also to the social and historical particularities.

Generally, it is noticed that, in those countries economically developed, the unstated legal activities, in order to elude itself from the payment of the fiscal bonds, form the most important part of the underground economy, meanwhile in non-developed countries, the unregistered production in a conventional manner (unofficial licit) is very important, frequently outrunning the official economy, because of the fact that the self-consumption is very strong, and the possibilities to register statistically all the activities are very low.

The area of all the activities that are included by this economy, but especially its extent, still is almost entirely unknown due to its fluidity, dynamics, flexibility up to economic reality.

It is doubtless that this area of activity develops in steps that are difficult to hit by the official sector, today attaining to represent a substantial part of the activity of the global economy, both in the East-European countries and the Western ones. That is why the importance of knowing its dimensions, causes and consequences over the official activities is unquestionable.

The dimension of the underground economy in Romania, like in all ex-communist European countries, is significant.

The Romanian underground economy was analysed and evaluated by numerous state institutions (National Institute of Statistics, The Ministry of Public Finances, Financial Guard, Romanian Intelligence Service, National Bank of Romania), non-governmental organizations (Romanian Centre for Economic Policies, The Centre for the Institutional Reform and the Informal Sector), independent researchers, the results being very different because of the diversity of the methods that were used.

According to the Romanian Intelligence Service, the illicit activities from Romania represent, in this period, 35-40% of the gross domestic product, which invokes the reality of a real parallel economy, just as vigorous as the official one.

Corresponding to a reasearch made by the Romanian Centre for Economic Policies from the National Institute of Statistics, in 2000, the underground economy represented 31% of the entire gross domestic product of Romania and approximately 45% of the gross domestic product of the official sector. For the same year, official dates presented by



the National Institute of Statistics showed that the underground economy succeeded in making 21% of the entire gross domestic product and 27% of the gross domestic product of the official sector. In the structure of the underground economy, evaluated by the National Institute of Statistics, for 2000, industry occupied the first place with 8,7% of the gross domestic product, followed by trade, public alimentation and tourism with 5,2%, transports with 3,2%, other services 2,3% and constructions 1,7%. The study of the Romanian Centre for Economic Policies shows that there is 72% of the entire underground economy in the formal sector, meaning in the economic structures organized as judicial persons, as enterprises, cvasi-enterprises and public institutions. From the amount of the underground economy, 51% is realised in the field of services, the same proportion as invoked in the data of the National Institute of Statistics.

The complete unpronouncement of the value added tax, with the evasion of the income taxes, represents the most important part of the underground economy, according to the evaluations of the National Institute of Statistics, which reported the following inadvertences: labour on the black market, evasion in the value added tax, the unofficial sector, formally unregistered by convention.

The conclusions of the study show that in Romania the underground economy is obviously a subsistence economy, the labour on the black market representing 46,5% of the entire underground economy.

According to some studies made by Friedrich. Schneider<sup>3</sup>, between 1990-2003, in Romania, the underground economy had an ascendance evolution.

-% in oficial gross domestic product-

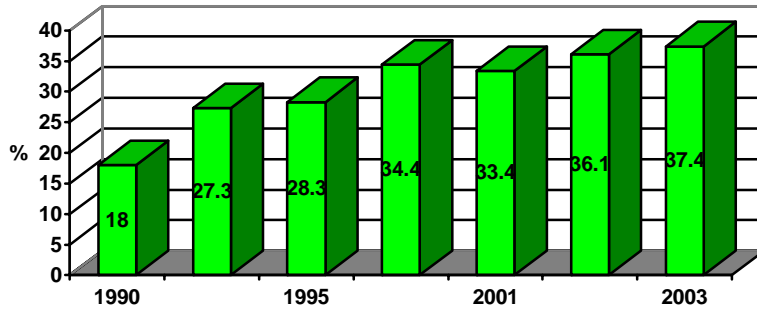
	1990	1990-1993 (average)	1995	2000	2001	2002	2003
Underground economy	18	27,3	28,3	34,4	33,4	36,1	37,4

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<sup>3</sup> F.Schneider, D.Ernste, „Increasing Shadow Economies all over the World – Fiction or Reality? A Survey of the Global Evidence of their Size and of their Impact from 1970 to 1995”, The Institute for the Study of Labor (IZA), Bonn, 1998.

F. Schneider, „The Size of Development of the Shadow Economies and Shadow Economy Labor Force of 22 Transition and 21 OECD Countries: What do we really know?”, Institute of Public Finance, Zagreb, 2002.

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■ The weight of the underground economy in the oficial gross internal product

We may see that in 2003, the estimated underground economy represented the double of the estimated one for 1990.

Supplied data of F. Schneider's study allow the estimation of the entire gross domestic product (created in the official and underground economy) and also its variation comparing to the variation of the gross internal product created only by the official sector.

Index	1990	1995	2000	2001	2002	2003
$E_c / \text{oficial Gross Domestic P}$	18%	28,3%	34,4%	33,4%	36,1%	37,4%
$GDP_{\text{oficial}}^n$ (millions RON)	85,7	7.213,6	80.377,3	116.768,7	151.475,1	190.335,4
$I_{PIB_{\text{deflator}}}$ (fixed base 1990)	100%	9.376,6%	111.524,1%	153.234,1%	189.090,9%	225.774,5%
$E_c^n$ (millions RON)	15,42	2.041,44	27.649,79	39.000,74	54.682,51	71.185,43
$E_c^r$ (millions RON)	15,42	21,77	24,79	25,45	28,91	31,52
$GDP_{\text{oficial}}^r$ (millions RON)	85,7	76,93	72,07	76,20	80,10	84,30
$\Delta GDP_{\text{oficial-year-report1990}}^r$	-	-10,23%	-15,9%	-11,08%	-6,53%	-1,63
$GDP_{\text{total}}^r$ (millions RON)	101,12	98,7	96,86	101,65	109,01	115,82
$\Delta GDP_{\text{total-year-report1990}}^r$	-	-2,39%	-4,21%	0,52%	7,8%	14,57%

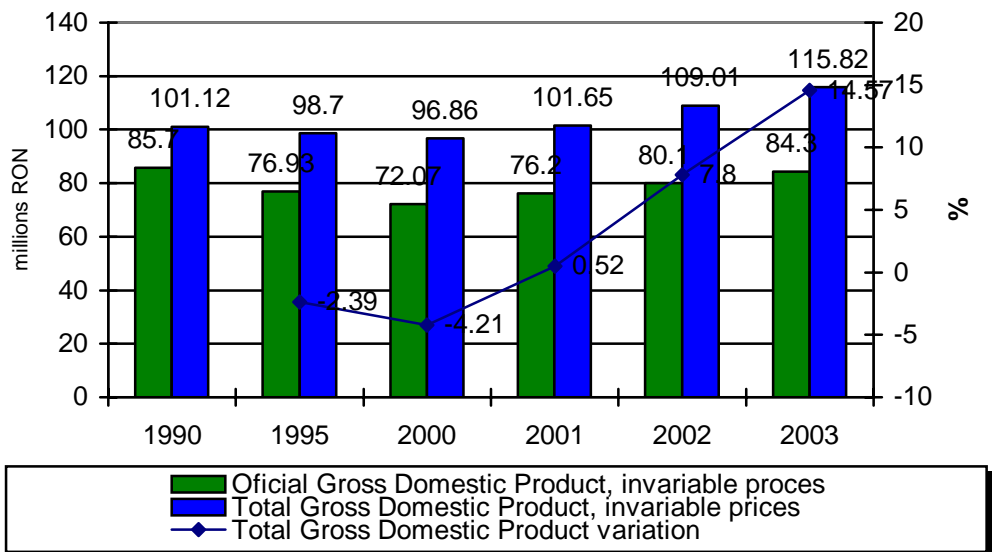
*Official and total Gross Domestic Product of Romania, between 1990-2003(selected years) and their variation comparatively with the basic year 1990*

From this analysis it is clear that the official gross domestic product, presented in

invariable prices, was situated, between 1991-2003, under its position in 1990. hence, its variation was negative in every year comparatively with the basic year, which means that Romania registered a real negative increase in the official sector, decreasing toward the end of the period.

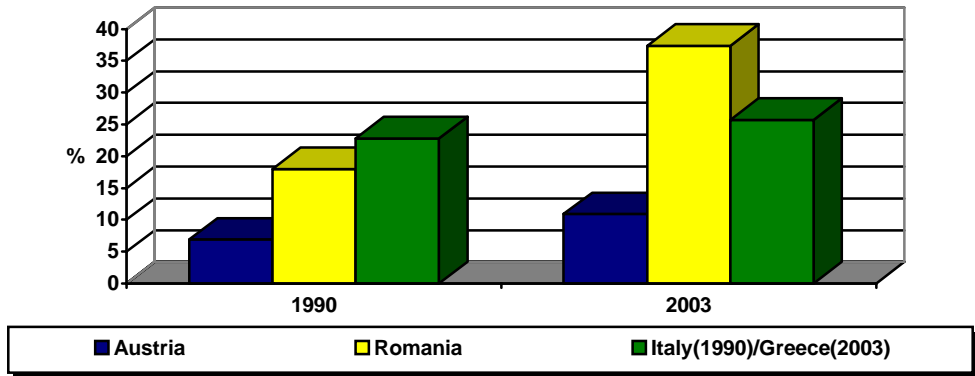
Total gross domestic product, expressed in current prices, was situated under the position from 1990, in 1995 and 2000 (and also probably in other years not comprised in the analysis because of the lack of data about the underground economy). Between 2001-2003, total gross domestic product registered real values over the position from 1990, due to the inclusion in its calculation of the value created in the informal sector. Therefore, starting with 2001, the total gross domestic product of Romania registered a real positive increase, that reached to 14,57%, comparatively with 1990.

These data give information about the real possibilities of Romanian economy, sustaining the assertion that the underground economy evolves erroneous signals to the factors of decision and hence induces inadequate macroeconomic strategies.



*Official and total Gross Domestic Product of Romania, between 1990-2003 (selected years) and their variation comparatively with the basic year 1990*

Comparatively with the state members of the European Union, according to the same data provided by F. Schneider, in 1990, the underground economy in Romania, was lower with 4,8 percentage than in Italy (22,8%), the country with the highest estimated level at that time, and with 11,1 percentage higher than in Austria (6,9%), where was estimated the lowest level. In 2003, the underground economy outrun with 26,5%, the lowest estimated level, for Austria (10,9%) and with 11,7 percentage, the highest estimated level, for Greece (25,7%).



*The underground economy in Romania, comparatively with the states of the European Union (marginal estimated levels)*

*The increase of the underground economy generally produced the increase of the governmental concern for the cessation of this phenomenon, perceived not only as a „fiscal gap”, but even as a threat for the national security.*

Even in Romania, the latter-year evolution of the underground economy must be a reason for a continuous concern and preoccupation for the decision parameters, because of the fierce involvements that this phenomenon has in the financial, economic, and social field.

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