

## ASPECTS REGARDING THE ECONOMIC TRANSITION OF ROMANIA

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*The purpose of this article is to briefly present the actions taken in Romania's economic transition from a centralized to a market economy and to explain why and where it went wrong. Wrong decisions taken in the transition process will be highlighted, while noting that measures to implement conditions conducive to the functioning of the free market, from macroeconomic stabilization, private sector development, restructuring of the national production system or the formulation and implementation of appropriate social reforms, found a marginal place in the execution of the governing program.*

*Despite the fact that this process has already begun more than 30 years ago, there are voices claiming that this process has not yet been completed. This is because, although a transition to last a short time was expected, domestic and international social, economic and political events extended the period of uncertainty, with institutional reform being difficult to achieve. All these aspects determined us to look for the answer to the question: Where was wrong that this transition is not yet complete and when will the transition of Romania to a truly functional and wealth-generating market economy be completed?*

**Key words:** *capitalism, economic reconstruction, market economy, Romania, transition..*

**JEL Classification:** *D40, H00, O10, P20, P51.*

**I. INTRODUCTION**

Romania marked in 1990 the beginning of the transition to a market economy. After 1989, Romania entered a process of institutional, legislative, economic, social, political reconstruction, etc., a process meant to ensure its transition to a functioning market economy and a democratic political system based on the rule of law. On the road to a market economy, Romania also joined a process of accession to the structure of the European Union that would ensure its access to the Community market. The period that followed December 1989 is a stage marked by profound transformations and which should have represented a new beginning for Romania, a relaunch from an economic and social point of view by applying and respecting the principles of the free market. However, it was found that December 1989 did not bring the necessary changes, so that, after the revolution, the Romanian economy experienced a rapid decline, deepened by the cumbersome reforms imposed by the newly installed political power, which made the implementation of the democracy and the market economy to last longer than expected. As a brief reminder, since the communist period the biggest problems of the Romanian economy have been the lack of competitiveness of local products, oversized enterprises, outdated technology, as well as the inefficient judicial system. In other words, Romania began the transitional process with a series of problems in all spheres: economic, political, social, institutional, etc.

Romania's transition was made on three alignments that proved to be compatible with the project of accession to the European Union, while ensuring the inclusion in the general trend of globalization: "political and economic liberalization, general restructuring, with a strong pivot in privatization and macroeconomic stabilization, against the background of the micro dynamics of the real economy" (Angelescu, 2006, p. 90). Therefore, Romania's transitional route had in view the observance of global rules but also aimed at completing the process of convergence to the European project. Among the first stages of the reforms related to the process of transition of the Romanian economy to the market economy system was the liberalization of foreign trade. As early as February 1990, the monopoly on foreign trade was abolished, multiple exchange rates were unified and devalued, by the end of 1990 most restrictions on trade were lifted, non-tariff barriers were considerably reduced, and tariff barriers were greatly reduced. (Ciupagea, 1999) said that we can talk about three different periods in the evolution of the Romanian economy after 1989: "(a) the 1990-1993 period, characterized by the pronounced decline of the entire Romanian economy, is the stage of system changes in the conditions of the massive presence of imbalances on domestic markets; (b) the years 1994-1996 coincide with the emergence of macroeconomic stabilization and a certain economic recovery, but in the context of preserving the old structures. The year 1995 stands out through the sustained efforts of Romania to demonstrate internationally its capacity to join the European Union, (c) the period after the 1996 elections began with the intention of more radical reform measures, unfinished due to the incoherent functioning of the institutional system".

In general, we shall note that the measures to implement conditions favorable to the functioning of the free market, from macroeconomic stabilization, private sector development, productive system restructuring to the reorganization of the social reforms, have found a marginal place in the implementation of the government program, the negative effects of these actions being felt in the long run.

**II. THE PROCESS OF PRIVATIZATION AND ITS INFLUENCE ON THE ECONOMY**

Capitalism, despite not being a perfect system, is the best-known system to date, which has generated prosperity in Western countries, but this transition from communism to capitalism has been a real challenge for former communist countries. As we already know, capitalism is based on private property, on private initiative in the process of production and investment, on price formation as a result of the relationship resulting from the confrontation of supply and demand, but also on the free functioning of markets. The success of capitalism depends on the existence of institutions, rules, a well-regulated competitive framework, but also on the proper functioning of the mechanism for allocating existing resources. Unlike capitalism, the characteristic of communist countries was the use of planning as a tool for allocating resources and implicitly for managing the economy. This system of centralized planning showed its limits in generating the welfare of the population but also in continuous economic development, so that in 1989 the collapse of communist political regimes in Central and Eastern Europe imposed the final transition to a free market economy.

The pace and quality of the transition to a market economy were dictated by the internal characteristics of each country. However, inevitably, a general theory of transition was outlined, which in many cases omitted many relevant aspects of national specificity, which led to distortions and, ultimately, failures. Thus, (Gelb, 1991, pp. 12-13) recalls that a plan of reform measures was developed within the World Bank, scheduled to be implemented during 10 years, which included 4 stages:

1. economic macro stabilization that was to be completed in 4 years;
2. price reform and market formation, which had to be completed within 3 years for goods and services and 5 years for labor;
3. restructuring, privatization and formation of the private sector, a measure that had to be completed within 5 years;
4. redefining the role of the state and its institutional reform by including social protection programs, being by far the most difficult and long-lasting measure that had to be fulfilled within 5-10 years.

Thus, among the first stages which Romania began the transition with was the restitution of agricultural land, a measure that highlighted the lack of vision of specialists in the privatization process but also the fact that the specialists at that time neglected industry, betting on agriculture as a field with potential. What was intended to be an advantage in the transition process, namely the procedure for returning agricultural land to rightful owners, proved to be a total failure. This measure which, in theory, should have been a very good one, did not take into account the real potential of the landowners to work the land, nor did it take into account the fact that this measure shattered the farms, making it difficult for them to be worked and exploited. Thus, due to the lack of experience of the new owners, to their advanced age, to the reduced mechanization of agricultural works and to the cumbersome process of obtaining of property titles, the agricultural productivity and the agricultural production decreased, becoming unpredictable and oscillating, as can be seen in fig. 1:

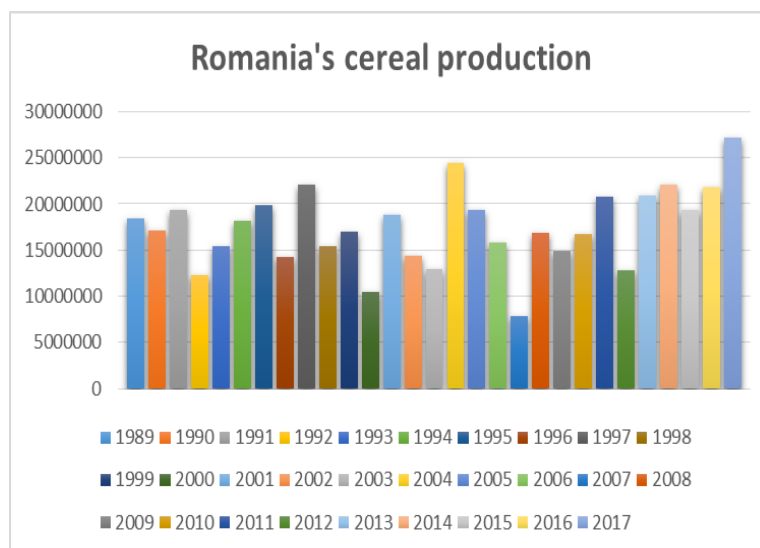


Figure 1- Romania's cereal production during 1989-2017

As can be seen from the figure above, agricultural production had an oscillating trend which means that agriculture was affected by too many factors to be a basic element in the Romanian economy. During the communist regime, agriculture ensured large productions, indeed far below potential, but this situation was due to the fact that little was invested in its mechanization. The fact that the mechanization of agriculture was not a priority in the communist system (it directed its investments to industry) was a behavior also taken over in the capitalist system. At the same time, the fact that this sector did not benefit from investments and it was returned to the rightful owners, led to the fragmentation of agricultural holdings and led to the creation of an economic sector dependent on subsidies and state interventions. The increase in cereal production after 2007 took place in the context in which, following the accession to the European Union, Romania had to submit to the policies and programs developed by this organization, including the development of agriculture.

Referring to industry, at the institutional level, the privatization of state-owned enterprises was legislated by transforming them either into joint-stock companies or into autonomous administrations (already obsolete in Western states), moving from state administration to private administration. The real and most pressing problem of Romania in the post-communist period was related to the way in which the privatization process took place. Moreover, as well characterized (Poenaru, 2017, p. 7) “the transition period, deregulation and minimization of the role of the state in economic and social terms made possible the unjustified and onerous privatizations during the transition period, which affected the Romanian economy more than World War II.” In this context, we can talk about a process similar to looting, a process carried out continuously and even consciously by the state which, through its actions, has lost its purpose: the welfare of the population. Thus, just like a private agent, the state used its assets to enrich the political class, transformed overnight into an entrepreneurial class too (functions, generally incompatible), to the detriment of the well-being of the population. The aim was to create optimal conditions for attracting external capital, but not to improve living conditions for the population.

More specifically, after 1989, approximately eight thousand “productive units” were privatized in two stages, many of them famous brands on the domestic or even international market (Copilaş, 2017), and most of them went bankrupt. In the first stage, the privatizations were doubled by certain measures meant to win the sympathy of the population so that the population was “put in possession” of shares issued by certain privatized companies but which, in the context of rampant inflation that Romania faced after 1990, quickly lost value. In the second stage, which took place in the early 2000s, the Authority for the Administration of State Assets sold approximately 600 large units for which the amount of approximately 10 billion euros was collected (Copilaş, 2017). The damages brought to the Romanian economy were and are invaluable. The result of these actions, along with the lack of competitiveness of the Romanian products, led to the bankruptcy of the enterprises, which led to the destruction of enterprises and the sale of fixed assets at ridiculous prices. The effects of these actions were felt in the industry’s ability to create added value, an evolution that can be seen in the fig. 2 below:

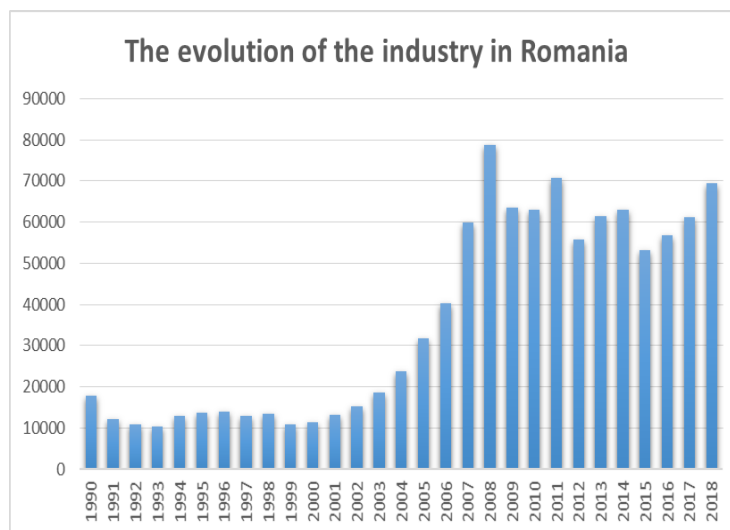


Figure 2- The evolution of Romania's industry in the 1988-1996 period

From the figure above you can see the trajectory of the industry which, since 1990, generates an added value in progressive decline until 1993. Starting with 1994, a short and slight recovery can be observed, followed by a decrease for the next year from when a positive and constant evolution begins until 2008. Against the background of the outbreak of the economic crisis in 2008, in 2009 and 2010 there was a sharp decline in the added value generated by the industry which lasted until 2010. What followed the year 2010 can be assimilated

to a recovery period after the economic collapse of 2008, a fluctuating trend being registered, so that only from 2016 we can talk about a stabilization of the Romanian industry.

Another controversial aspect found in the post-communist evolution of Romania was the one related to foreign investments. It must be borne in mind from the very beginning that privatization and foreign investment must not be seen as a bad thing; on the contrary, when they are well regulated and the reforms are coherent and aim at the common good of the population, they have a positive impact, as demonstrated by many other economies (e.g. Scandinavian economies). It's just that in the case of Romania, things went differently: the new installed power came from the old communist structure, and the newly established capitalism was a political one, very different from the Western rational capitalism. The distinction between these two types of capitalism was made by the sociologist Max Weber who argued that while rational capitalism considers and relies on long-term investment and the accumulation of profit on the market by legal means, but neglects the origins of capitalism based on primitive accumulation (which does not fall into the rational sphere), political capitalism seeks to make a profit with the help of politics, on paths on the edge of legality, thinking and acting in the short term. The privatization actions in which Romania took part fell within the sphere of political capitalism. In this context, the state transformed its civil servants into private agents interested only in their own welfare by using the properties and resources of large state-owned enterprises, through what would be called ""parasite companies". The whole process was well surprised by Cătălin Augustin Stoica who wrote that "the strategy presupposed the existence of state companies, located in the center of the network, and of several private companies with the role of satellites, around them. The satellite companies were controlled (directly or indirectly) by the directors of the state companies or, as in our case, other relatives of the management, union leaders, etc. "Recombined ownership (...) came with ingenious accounting practices: the profits went to the private satellite companies, while the losses were transferred entirely to the state company" (Cătălin Augustin Stoica, "Elements for a sketch of post-communist political capitalism", in Copilaș, *The End of History Is Postponed*, 2017, p. 20). The fact that in Romania it was wanted to directly replace the state monopoly with the private monopoly over the economy in a society that did not have the necessary framework to achieve this and did not have the competitive experience necessary to operate this approach, inevitably led to systematic destruction and exploitation of public resources to meet private purposes. In other words, the heads of state-owned enterprises acted at the same time as owners of private companies, so they had every interest in the losses being reported by state-owned enterprises while the profit was collected by their own enterprise. Through such actions, they managed to accumulate illegitimate capital, but they also managed to discredit the state in order to be able to buy its assets at ridiculous prices.

Another mistake made in the transition process was the complete privatization of all state-owned enterprises, without taking into account the fact that in "Western economies, not only in communist ones, there were and continue to be many planned sectors (e.g. France)" (Copilaș E. , 2017). Thus, in addition to the fact that in Romania the newly installed capitalism was political, all the actions undertaken in the 1990s were only "to drain it of resources and not to find solutions to problems that were extremely serious and complex at the same time" (Ibidem). In this process were also involved multinational companies which, in order to eliminate competition, took over and even eliminated various state-owned enterprises in Romania. Of course, the state, through competent and efficient institutions, could lead certain key sectors much better. It was even recommended to maintain control and supremacy over sectors of national interest and which, through the existence of state monopolies, could have provided sufficient income to pay obligations to public workers.

But the essence is different; it was not privatization itself that represented the problem of post-communist Romania – a large part of which was inevitable - but the way in which this process was managed, systematically ignoring the general social interest. The effect of these measures has been a steady decline in GDP (see fig. 3) and therefore poverty has been on the rise:

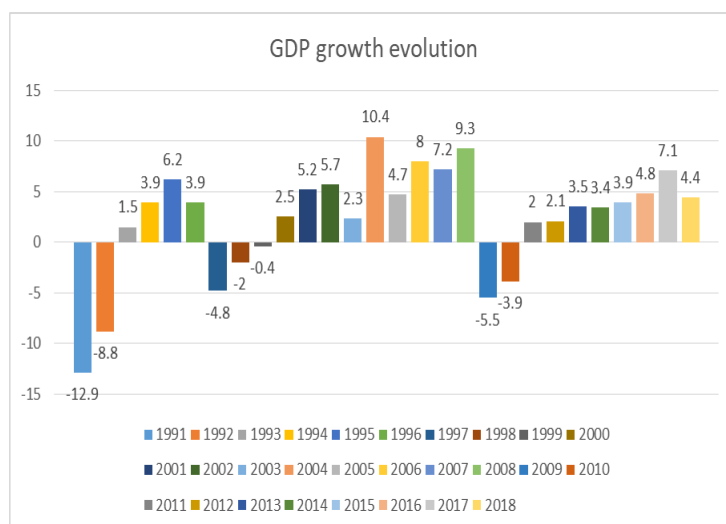


Figure 3- GDP evolution (%), in Romania, during the 1991-2018 period

As can be seen from the figure above, the period immediately following the fall of communism was marked by a decline in gross domestic product. An overview will show that the evolution of GDP is fluctuating and, if for the period 1991-1999, the influencing factors of the gross domestic product could be assimilated with the domestic ones, i.e. the actions taken with the stated purpose of passing the Romanian economy from the centralized to the free market, for the years 2009 and 2010, years in which also the evolution of the GDP was negative, the global factors can be invoked, those that triggered the economic crisis from the year 2008. What needs to be mentioned about this figure is that the first decade of the transition was marked by controversial policies, damaging privatizations but also failed attempts to reorient the economy so that, in this context, we can explain the fluctuation of GDP and, although a low level of GDP does not necessarily mean poverty, it is known that until the first period of transition, Romania's economic situation was not good. The economic recovery after 2000 is due to the negotiations carried out by Romania with the European Union in order to join its structures, a context in which our country receives a series of directives that must be respected.

Although in the period before the transition to a market economy, Romania's economy could easily be manipulated in such a way as to consume only goods and services from domestic production, with the first steps towards the free market and "gaining" access to other markets, the consumption structure of the population has changed. In this context and against the background of the harmful privatizations that did not leave room for the possibility of reorienting the economic activity for the former state companies that, in the end, took the road of dissolution, Romania's foreign trade balance was long negative. These aspects have led to other negative effects on the Romanian economy. Thus, if in 1989, although we did not have access to the financing markets and the industry was equipped with technology, for the most part, obsolete, the performance had been managed to pay off most of the external debt. Starting with 1990, Romania's external debt began to grow slowly but surely. Thus, if in 1989 Romania's foreign debt amounted to just over one billion dollars, by 1991 it had doubled to \$ 2,159,379,246, steadily increasing until 1999 when it experienced a slight decrease from \$ 10,107,804,714 in 1998 to \$ 9,110,874,002. The problem arises when these loans are contracted to pay for consumption (as is the case in our country) and not for investments in infrastructure or industry that, over time, can generate income. In other words, the situation where a country pays its imports with borrowed loans without these imports being felt as investments in various economic sectors can be interpreted as that where a company consumes more than it produces, which is in total contradiction with the principles of the free market or the classical economy, this situation seems to be generated just as in Keynes's theory that an economy can be revived by increasing consumption and deficit. The fact that until 2013 Romania's debt has grown steadily, with few exceptions, is, in fact, a confirmation that the simple economic recovery through consumption does not work if it is not supported by production or investment in the infrastructure because, without production, i.e. income to cover consumption, external debt will always exist.

That in Romania the industry did not represent an economic sector of interest, can be concluded from the fact that since 1990 the services sector has grown at the same time as the share of agriculture has decreased. Also, as we said in the paper, during the first years of transition the industry was "kept" in order to secure jobs, a major change not being observed, as it was neglected and lacked investment. But the most worrying aspect is that during transition, the structure of economic sectors has changed, the share of industry being overtaken by the share of services, which means that the Romanian economy is focused on trade, services, etc., the productive sector having a worryingly small share.

Having all these premises, political capitalism has achieved its goal, namely the systematic weakening of the state, while criminalizing it as an incompetent administrator of the economy, all to increase colossal private profits (Copilaș, 2017, p. 99). Thus, after the big privatizations, those mismanaged too, the Romanian industry was destroyed and lacked investments. In addition to the decrease of the industry ratio, during the same period it can be seen that the primary sector (agriculture) also experienced a downward trend. This further highlights the lack of interest in productive structures, the poor coordination of privatizations and the misunderstanding of the reasoning of the free market, making the needs of the population largely covered by the production of other countries.

### III. CONCLUSION

From the analyzed data we could conclude that in the first decade after the Revolution, respectively in the period 1990-2000, the transition took place more slowly and after 2000, against the background of Romania's declared intention to join the European Union, this process knew a slight acceleration. However, misunderstood and misused economic policies, privatizations and actions to the detriment of the welfare of the population have caused public institutions to lose their universality, efficiency and quality of services, being populated by opportunists who have used national resources as their own. These aspects determined the creation of a dependent relationship between the Romanian economy and the production of other countries which, corroborated with the arbitrary decisions taken by the political decision makers of that time, brought developmental delays compared to other former communist countries.

Therefore, unlike the role adopted by Romania's public policy during the transition period, it should have guided the development trajectories of the economy as a whole, ensuring coherence between the behavior of enterprises and social, economic, health, etc. objectives. Regarding the fact that Romania does not yet have an institutional system sufficiently developed and able to issue coherent public policies, (World Bank, 2020) considers that, although according to Romania's Economic Memorandum (2020), per capita income, from the European Union average, increased from 26% to 63% in 2017, "this economic success is based on the vague foundations of unfavorable demography, weak human capital and inefficient institutions". In this sense, the option of institutional reform of Romania should be considered, taking into account the expansion of the role of the state in response to the need for public action in the economy and society. At the same time, Romania's major challenge is the same for the last 30 years: ensuring stable economic growth, improving living standards and continuing institutional reform, all aimed at generating welfare for the population, in accordance with the principles of the free economy.

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