ASSESSING THE IMPLEMENTATION OF REAL CONVERGENCE IN ROMANIA

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The convergence is an essential objective of the integration process of Romania in the European Union. Minimizing gaps in the level of development that arise between Romania and the average European Union can not be achieved solely through the use of market forces-they rather polarize and create divergences. So, are required, specific tools and mechanisms (economic models for assessing growth, the approximation of the real convergence of sigma and beta type). Economic transformations which are occurring globally, and increased aversion to risk have contributed to the significant decrease of capital flows to Romania; have increased also pressures on exchange rate - was recorded a cumulated depreciation of more than 30% of the national currency since August 2007. In early March, Romania called on the European Union and International Monetary Fund in order to support the balance of payments' stability, taking into consideration the massive decreases in flows of external capital-matter what cause polemics among economists and that impact a generalized scale of the economy.
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I. Introduction

Although it was introduced in analysis with a spatial scale that has undergone a process of transition in Europe, the concept of convergence began to enjoy more attention in the last 4-5 years, being induced by the last two enlargement waves of the European Union. This has replaced the phrase approach founded on the principle of restructuring, assessing also the integration of new EU Member States in the context of achieving a long-term economic growth.

The convergence is an economic category, which has won popularity among economists not only because of the catching up of gaps that it involves, but also because of it's usefulness in the validation of several models of economic growth. The concept can be examined from several perspectives: *real convergence* describes the convergence of income levels, reflecting the convergence of nominal price level convergence, while *institutional convergence* implies institutional harmonizing legislation. We can also talk about the convergence of business cycles, convergence behavior, and convergence of social stratification.

II. Assessing the implementation of real convergence in Romania

For such an assessment we need to compute the place that Romania has in the European Union rankings in terms of GDP per capita. It should also be defined and evaluated the rate of advancement of Romania to the convergence with the developed countries, taking into account the pace of their growth. From an economic point of view, Romania stands still in a marginal position in comparison with developed countries. For example, compared with 252,004 the EU average, Romania GDP per capita, calculated at the exchange rate, was 8,1 times lower, and calculated according to purchasing power parity (PPP) was 3,1 times smaller. Compared with the average of the ten countries that joined the European Union in 2004, the GDP per capita of Romania in 2004 were 2.35, i.e. 1.75 times lower, according to data provided by Euro stat. Among the 28 states and candidate countries in 2004 (EU 27 + Turkey), Romania is in the 26-ed position (before Bulgaria and Turkey), rating made according to GDP per capita expressed in euro according to the PPP. If it goes beyond the European area when analyzing the position of Romania based on per capita average income we observe that Romania recorded better positions. However, the spread between the extremes is more significant than at the European level. Among the 208 independent countries and territories, Romania is ranked according to GDP per capita by far the most extreme cases, but the worldwide media, presents the following values of key macroeconomic indicators:

Tabel no.1: Statistical data for Romania[312]

INDICATORS	***2007***
Population (mil.)	*21.55*
Δ% population $_{n/n-1}$	*0*
The average life $_{women}$ (years)	*76*
The average life man (years)	*69*
GDP $_{USD}$ (mil)	*166*
Δ% GDP $_{n/n-1}$	*6*
Δ% IGP $_{n/n-1}$	*5*
Net Direct Foreign Investments (%GDP)	*6*
Internet users (to 100 peoples)	*24*
Unemployment (% from the total labor market)	*6*

To answer the question if Romania manages to complete the process of convergence to the European Union and at the top of most developed countries worldwide in terms of GDP per capita, Romania's progress should be compared with developments in other countries or groups of countries. If progress is defined by the annual average growth of GDP per capita and we analyze the rhythm of Romania in relation to other countries or groups of countries we can easily see that the convergence of Romania is not only very difficult to achieve, but becomes almost an illusion, considering that the disparities are becoming larger, and the annual growth of Romania slower between 1990-2004 or even negative in the 1980-2003 period.

Even if the calculations for analysis and prediction require a long series of data, using the interval 1980-2000 for Romania becomes slightly unrealistic, given that the two decades are not typical in terms of continuity and economic stability. In that period, the Romanian economy has faced a profound and acute crisis, the centralized economy (in the 80's) has revealed it inefficiency and lack of capacity to innovate and to adapt, and on the other hand the transition to a new system (in the 90's), consisting in a general and profound restructuring of the whole economy (the technological and organizational concept of property management, economic and social, institutional system, etc..) developments that led to a profound negative trend of the national economy. Changes began to report positive results since 2000, when economic stability and functionality have been achieved on the basis of new principles. So that idea should be supported to achieve convergence scenarios, in the case of Romania to be considered growth rate since 2000 just because they are considered reliable for an assessment of the future evolution of the Romanian economy - 2000 was categorized as representing the start of a normal development.

312http://www.worldbank.org.ro/

Between nominal and real convergence between must be a right balance, as a forced nominal convergence is not sustainable and can explode in time, like inflation, which can be artificially taken down.
Achieving nominal convergence implies the fulfillment of criteria established by the Maastricht Treaty[313], namely price stability, long-term interest rate, exchange rate stability, fiscal sustainability position.
The process of catching-up of the countries in Central and Eastern Europe is influenced by the quality management of the two types of processes - the convergence of real and nominal convergence, the last inducing constraints for economies that wish to join the euro area. The process of nominal convergence has been privileged in relation to the real convergence, since its implementation requires a lower horizon of time. Joining the euro area will not be realized until after reaching the full criteria for nominal convergence, set in Maastricht on the inflation rate, interest rate long-term deficit and debt, and the stability of nominal exchange rate.
According to the European Central Bank, during April 2007 - March 2008, Romania has registered an average annual Harmonized Index of Consumer Prices (HICP) of 5.9%, clearly superior to the reference value of 3.2%[314]. Retrospective analysis over a longer period shows that, in Romania, inflation measured by consumer prices was placed on an evident descending trend, although initially recorded a very high level. The process of disinflation has been in the context of strong growth of real GDP, which exceeded the level of 5.0% almost every year since 2001. Reducing inflation was based on the accelerated growth of labor income, which exceeded 20% over several years. In the period between 2005 and mid 2007, the evolution of import prices has helped the process of disinflation due to the considerable appreciation of the national currency against the euro. Analysis of recent developments indicates that the annual HICP rate has accelerated from about 4% in January-July 2007 up to 8.7% in March 2008. Significantly increasing of food, import prices increase as a result of the depreciation rate since mid-2007 and increasing raw material prices on international markets, and substantial advancement of real GDP supported by increased domestic demand, continued to increase inflationary recently pressures. The increase in labor income reached 20.2% in 2007 compared to the previous year, being high net to productivity growth and thus leading to a significant increase in unit cost of labor.
Until 2008, Romania has not been the object of a decision of the European Union Council on the existence of excessive deficit. Given the budget deficit of 5% in 2008 and the possible evolutions of macroeconomic balances in 2009, chances are very high for things to change in this respect. In 2007 Romania registered a budget deficit of 2.5% of GDP, below the reference value of 3%. The share of public debt in GDP was 13.0% in 2007, being lower than the net reference value of 60%. Further fiscal consolidation is necessary for Romania to maintain a share of the deficit lower than the reference value and to fulfill the medium-term objective specified in the Stability and Growth Pact. We think that taking into consideration the terms of current economic and financial conditions and in view of the fact that 2009 is an election year, this goal will be almost impossible to achieve. In the convergence program is defined as the deficit adjusted for cyclical effects, which are not temporary measures approximately 0.9% of GDP. Regarding other fiscal indicators in years 2006 and 2007, the magnitude of the deficit has not exceeded the share in GDP of public investment.
In the period between 1 January 2007 (date of accession to the EU) and 18 April 2008, the national currency did not participate in ERM II, but was traded under a flexible exchange rate. In the reference period 19 April 2006-18 April 2008, the leu has been subject to depreciation

313 The Maastricht Treaty does not mention explicit criteria on real convergence, which involves the reduction of disparities between countries regarding the level of prices and productivity, involving increase revenue of the developing countries to the level existing in developed countries
314 computed according to the Maastricht Treaty

pressures until mid July 2006, then, it has appreciated significantly against the euro. Since August 2007, noted currency depreciated against the backdrop accentuated aversion to risk from international financial markets, as a result of financial turmoil and intense concerns on deepening current account deficit and inflation inflammation. In general, in most of the reference period, the Romanian leu was quoted at levels above the average net rate of exchange against the euro recorded in April 2006, under a relative high degree of volatility.

The differences between short-term interest rate from the three months EURIBOR were tempered, easily exceeding 2 percentage points at the end of 2007, before increasing to 5.1 pp in the three months that ended in March 2008.

In March 2008, the rate of real effective exchange rate in relation to the euro stood at a level above the average historical net recorded in the last ten years, and the real bilateral compared to the same currency easily exceeded these values. However, real economic convergence makes difficult any assessment of the historical evolution of real exchange rate. Regarding other external developments, since 2002, Romania registered a progressive increase in the deficit of current account and capital balance of payments, which stood at 13.5% of GDP in 2007. Although significant external deficits may be partly generated by the alignment of an economy such as Romania, deficits of such magnitude raise sustainability, especially if they persist for long periods. It seems that very large deficit recorded recently has caused also an overheat of the economy. From the perspective of financing, net inflows of direct investment covered almost entirely by external deficit in 2006. However, lately, a significant deficit was financed by net inflows of other investment in the form of foreign loans contracted by the banking and non banking sector. In this context, the net international investment position of Romania has deteriorated from -19.3% of GDP in 1998 to -46.6% of GDP in 2007. In the reference period April 2007 - March 2008, long-term interest rates were on average at 7.1%, higher than the reference interest rate criterion.

III.Conclusions

The harmonization of the two types of processes - the real and nominal convergence – is the solution to stimulate the process of catching-up of our economy. Romania recorded a slow convergence of the monetary variables (inflation rate and interest rate) in accordance with the criteria set in Maastricht. The public finance situation is favorable in the spirit of these criteria, but shows a low degree of economic modernization. The real convergence process could be stimulated by promoting a mix of expansionist policies, but the process of disinflation would be affected in the absence of a flexible offer. This is the consequence of structural reforms over the economy, to improve economic incentives, as well as attracting foreign capital. Such advocacy for policies to boost supply is justified by the prospect of joining the euro area (and prior to ERM2) authorities would have only fiscal policy tools, whose use will be constrained by the Stability and Growth Pact. Another reason has its explanation in the increasing integration of markets, increase competitiveness, which requires domestic companies to ensure the sustainability of economic growth.

From the Romanian perspective, the coordination of economic policies including the interactions between policy decision at national level and at the supranational level (especially the European Commission and European Central Bank), as representatives of the interests of Member States (especially in the areas of fiscal and monetary).

Motivation of coordination on the economic level is found in growth of interdependences of the Romanian economy and that of other European Union countries (70% of Romania's trade is done with the European Union), the proper functioning of the single internal market and achieving economic and monetary union (adopting the euro and fulfilling the Maastricht criteria on inflation rate, the nominal interest rate on long-term budget deficit, public debt and low fluctuation of exchange).

Adopting the euro should not be viewed as an end in itself, so that the training should be reviewed in the light of cost-benefit analysis. In other words, the timing of joining the euro area is a matter of temporal optimization. In fact, it should include two phases: the first refers to the fulfillment of a sustainable nominal convergence criteria and the second stage involves carrying on a basic criteria for real convergence criteria which are not stipulated in any explicit strategy in the post or in the Convergence Program of Romania. Convergence is about revenue, price convergence, the convergence of productivity, education standards, infrastructure development, economic and social cohesion, structural convergence with EU economies etc.

The Convergence Program of Romania should achieve simultaneous convergence of real and nominal convergence in the relationship with the European Union. Prerequisite for achieving this objective is to implement a combination of appropriate macroeconomic policies that ensure the continuation of disinflation and maintaining external sustainability. Without continuing the process of disinflation, limiting deepening current account deficit, increase predictability and performance of fiscal policy over the medium term, high absorption of European funds and strengthen structural reforms, the objectives of the Convergence Program should remain just good intentions. It's looking to a founded concept of a mix of macroeconomic policies by matching monetary policy and exchange rate policy with fiscal policy, income and structural reform. Macroeconomic projections are based on macroeconomic analysis sensitivities, on the impact of wage growth, agricultural production and the depreciation of exchange rates on the macroeconomic framework. Analog, in terms of long-term sustainability of public finances there sensitivities analysis on the budget and public debt. An advantage is the correlation of macroeconomic indicators of the monetary tax, resulting in an increased effectiveness of macro policies in solving failures faced Romanian real economy.

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