THE MINIMUM WAGE AND ECONOMIC GROWTH. ANALYSIS IN THE CASE OF ROMANIA

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Abstract

There are theoretical and empirical studies that highlight a variety of determinants of economic growth, including investments, physical capital accumulation, human capital, innovation, political and legal institutions, macroeconomic conditions etc. The purpose of our paper is to determine the extent to which the evolution of the minimum wage has influenced the economic growth in Romania in the period 2007-2021, the objectives pursued being the definition of economic growth and the method of measuring it, the evolution of the minimum wage in the period mentioned above, as well as determining the effects the minimum wage on some economic indicators (consumption, GDP/capita). In this sense, we use an empirical and descriptive methodology, by referring to statistical data and bibliographic references from national and international literature.

Keywords: GDP/capita, consumption, Romanian economy, global financial crisis

JEL Classification: E60; O47

1. Economic growth - concept and methods of determination/ measurement

The process of economic growth is a complex one of increasing the results of the national economy, based on the combination and use of direct production factors: labour force, fixed capital and the consumption of material circulating means. Economic growth is desired in any country because it enables the population to consume more goods and services and at the same time contributes to the provision of a greater amount of goods and social services, such as health, education, thus leading to the real improvement of living standards.

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Economic growth represents a real increase, in a certain period and in a certain space, of an economic indicator, GDP. A wide range of theoretical and empirical studies highlight a wide variety of determinants of economic growth. Thus, it is considered that investments, the accumulation of physical capital, human capital, innovation, geography, political and legal institutions, macroeconomic conditions, have a role in improving economic performance (Pânzaru, Ștefan, 2008).

In the economic literature, there are numerous approaches regarding the classification and ordering of economic growth factors. These were elaborated both according to the possibilities of quantifying the direct and indirect contribution, according to the order of action priorities through economic policy, but also based on their appearance in the issue of economic dynamics (Popa, 2012).

Therefore, Kuznets (2001) considers the economic growth of a country as an increase in the capacity to provide increasingly different economic goods, this capacity being based on advanced technology, as well as on the institutional and ideological adaptations that it requires them. Arndt (1978) considers economic growth as an increase in average per capita income (usually measured by GDP per population/ capita). Perroux (1981) appreciates growth as the increase in the size of the national economy expressed in the total of goods and services obtained during a period, including depreciation. In his opinion, however, only long-term quantitative growth constitutes economic growth, short-term growth means expansion.

Since Kuznets, there have been many attempts to create a GDP 2.0, which would more accurately reflect the level of economic growth. Nordhaus and Tobin in the 1970s add previously invisible goods to GDP: leisure and unpaid household activities.

There have been a number of variations on this theme for building an Index of Authentic Progress: by subtracting (toxic elements such as ecological footprint) or adding (volunteering) some elements (Voica, 2009). The adjustments also come along the lines of income inequality, spending on crime prevention and health insurance, etc. For example, the Human Development Index (HDI), published in the United Nations Development Programme's Human Development Report, is a comparative measure of life expectancy, literacy, education and living standards (UNDP, 2022).

David Pilling, in the book "Economic growth, a delusion. The wealth, poverty, and well-being of nations" summarizes the issue of

measuring the well-being of a nation and all the steps taken to achieve this goal.

Economic growth is defined as the process of increasing the dimensions of economic results, determined by the combination and use of production factors and highlighted by macroeconomic indicators - gross domestic product, gross national product and national income in real terms, both in total and per inhabitant.

In this paper, we express economic growth through the gross domestic product (GDP). According to the INS, it represents the synthetic expression of the results of the economic activity produced within the economic territory in a period of time, regardless of the contribution made by internal or foreign subjects.

It can be determined through several modalities/methods, and in the case of the expenditure method (the final production method) we consider to be a source of significant information on the main correlations that influence the evolution of the main macroeconomic aggregate (Anghelache, 2011).

Thus, according to the previously mentioned calculation method, GDP can be determined by adding up the components that express the use of goods and services that form the final production, respectively:

$$GDP = CP + CPL + IB + EXN \quad \text{or} \quad GDP = CF + FBCF + VS + (E - I)$$

where:

CP - private (personal) consumption
CPL - public consumption
IB - gross investments
EXN - net exports

CF - final consumption
FBCF - gross fixed capital formation
VS - inventory variation
E - value of exports
I - value of imports

For Romania, the GDP is mainly influenced by the evolution of private and public consumption.

It should be mentioned that in the GDP measurement it is necessary to specify some considerations/differentiations, respectively the factors that must be taken into account in the GDP evaluation, as well as the difference between nominal and real GDP (Căpraru, 2021).

Thus:

- nominal GDP vs real GDP. Nominal GDP is calculated at current prices, including inflation. Real GDP is calculated at the price level of a reference year, thus using constant prices, extracting the

inflationary effect. In the case of high and/or rising inflation nominal GDP will be higher, but not necessarily as a result of the increase in the level of goods and services produced in that economy.

- GDP calculated at purchasing power parity - This indicator is used to compare the level of GDP between two or more countries taking into account purchasing power parity (expresses the equivalence between the level of prices expressed in the same currency in different countries). Thus, prices are brought to the same denominator (through a common currency), and the GDP comparison takes into account the volumes of goods and services of two or more countries.

- Potential GDP reflects the production capacity of an economy at a given time, in the context of the normal use of the factors of production, namely capital, labour and the total factor of productivity. In other words, it represents the maximum level of GDP that can be produced, using the available factors of production at full capacity.

If we compare it with real GDP, some conclusions can be drawn about the state of the economy. The GDP deviation (the difference between the actual and potential GDP) quantifies the demand deficit/surplus. A positive GDP deviation (actual current GDP is higher than potential - excess demand) indicates inflationary pressures, while a negative GDP deviation (deficit demand) indicates disinflationary pressures. The GDP deviation also shows us the cyclical position of the economy. If the difference is positive, then we are talking about an expansionary gap (and if the difference is very large, we can expect an overheating of the economy), and a negative difference, reveals a recessionary gap. In the long run, the GDP deviation tends to zero, bringing GDP to its potential level.

- GDP/capita - demographic developments must be taken into account. The increase in the phenomenon of labour migration abroad, the increase in mortality and/or the decrease in the birth rate are phenomena that distort the value of such an indicator (for example, its increase in the context of a relatively constant GDP may show a decrease in the well-being of the population).

When determining the GDP size, we must take into account the moment of comparison, the component that led to the increase in the level of the indicator, as well as which branches of the economy contributed to this increase.

To calculate the level of economic growth, we refer to the size of GDP in the past, at a given time (a quarter or more ago, a year, etc.).

If at the reference time we have witnessed an economic decline, in the following period, if there is an increase, it will appear relatively higher, as a result of the (lower) reporting base.

From the point of view of the GDP component that brought the increase (the largest), it starts from the GDP determination method (expenditure method), according to which GDP is composed of: C (private consumption) + G (government expenses) + I (investments of companies in capital goods) + (X (export)- M (import)). Currently, according to official statistical data, Consumption prevailed. Economists argue that healthy growth is achieved on the back of investment and positive net export. Also, increased government spending can lead to higher GDP (Căpraru, 2021).

The branches of the economy that contributed to growth over time were agriculture, industry, construction, services. An economy can specialize over time on the growth of a certain field of activity. It is important that, as a whole, there should be harmonious growth in all branches of the economy. Reliance on one or two branches is not beneficial in the long run, especially in crisis situations (Concordia, 2020).

In Romania, the increase in the minimum wage led to an increase in consumption, thus an increase in GDP due to government spending and consumption. Agriculture, industry, construction, services also contributed to the increase (where there are most minimum wage contracts) (FES, 2021).

2. The minimum wage in Romania - concept and evolution after 2007

The minimum wage in the economy is the lowest value of the hourly, daily or monthly wage that the law of the respective country allows employers to give to an employee. The first countries to legislate a minimum wage were Australia and New Zealand at the end of the 19th century. Currently, the minimum wage per economy is established in more than 90% of the world's countries (CES, 2014).

In 2010, worldwide, Luxembourg had the highest minimum wage at $1.687 per month, and Burundi had the lowest minimum wage at $6 per month, while the minimum wage in Uganda was $7. Out of the 120 countries analysed at that time, Romania was among the top 50 countries, with a minimum wage value of 320 dollars (PPP) in 2009.

Among the member countries of the European Union, only Bulgaria had a lower minimum wage than Romania ($292).

In May 2014, citizens of Switzerland rejected the introduction of an economy-wide minimum wage of around 3,300 euros, the highest minimum wage in the world, given the country's high cost of living.

In Romania, until 2011, there was an obligation to grant a minimum salary for people who finished a university, which was equivalent to two national minimum salaries.

Ever since the introduction of the first minimum wages, at the end of the 19th century, they have been very controversial. As the name suggests, the minimum wage represents the lowest amount that the employer is obliged to pay the employee. Many countries in the world have clear provisions in this sense, although there are often many exceptions to the rules.

At the European level, the introduction of the "European minimum wage" can have both positive and negative effects.

Among the positive effects are the following:

- Stopping labour migration;
- Improving the standard of living;
- Creating the necessary premises for the development of the future workforce;
- Promotion of collective negotiations for establishing salaries;
- A corresponding degree of adequacy of the legal minimum wages;
- Effective access to minimum wage protection.

Among the possible negative effects of the implementation of the future directive, without taking into account the differences between the strength of the economies of the member states, the different structure of the labour market and the different levels of income in the member states, we mention:

- Closing companies that cannot support the wage increase;
- The migration of multinational companies to other non-EU states where labour is cheaper;
- The increase in inflation.

The increase of the gross minimum wage, in the context of the application of complementary public policies aimed at reducing the level of poverty and the integration of vulnerable groups on the labour market, can lead to the reduction of income inequalities (Socol, 2018). Sometimes, the increase in the minimum wage causes a moderate

increase in the amount of wages between the minimum and the average level, thus widening the target group of beneficiaries of the measure. Employers' costs may also increase significantly in this context.

The minimum wage in Romania was first introduced in 1949. The level of minimum wage in Romania is determined at national level by the government after consulting the trade unions and employers' organizations. There is only one minimum wage determined by law. The minimum wage has only one fixed component and is calculated on monthly gross basis. It has typically adjusted twice a year in January and July, except for 2016 in which the minimum wage will be adjusted only once in May. In recent years, the Romanian government has extensively utilized the minimum wage as a tool to achieve the objective set out for Europe strategy 2020 in order to reduce the number of persons at risk of poverty and social exclusion by 580,000 persons (IMF, 2016).

Figure 1
Arguments "For" and "Against" the Minimum Wage Increase
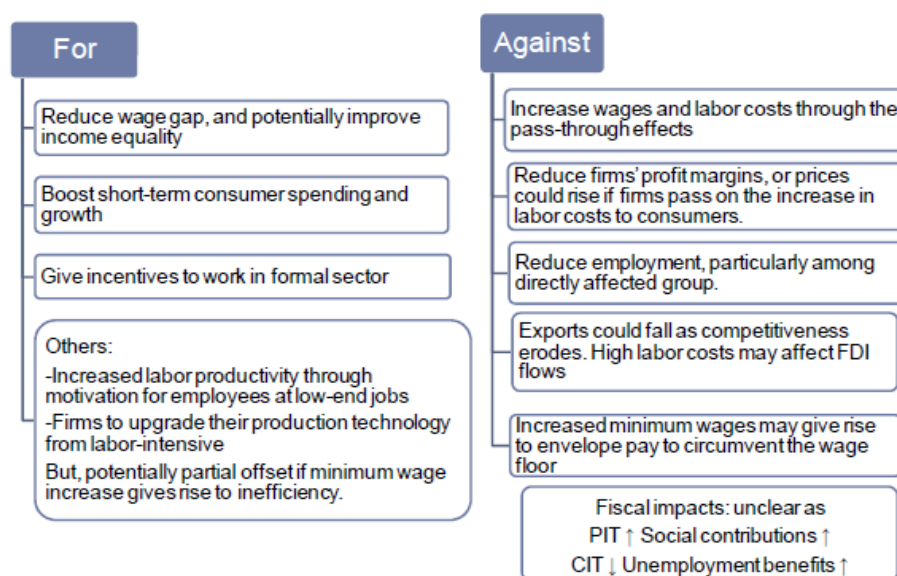

Source: IMF (2016)

We believe that there is a need to introduce/increase the minimum wage in Romania. The high share of workers (employed

persons) at risk of poverty (full-time/part-time), the accentuated income inequality, the inequity of the distribution of the net national income between labour and capital, the asymmetric dissemination of the benefits of economic growth and the slowness of the social lift, as well as the asymmetry of negotiation between unions and employers (especially after the flexibility of the 2011 Labour Code in Romania) there are just as many arguments for raising the minimum wage to a decent level that would ensure the potentiation of the economic and social multiplier effects of using this tool.

Next, we present the evolution of the minimum wage in Romania, in the period 2007-2021 (according to Table 1, in the Appendix).

Figure 2
The minimum gross salary during the period 2007- 2021
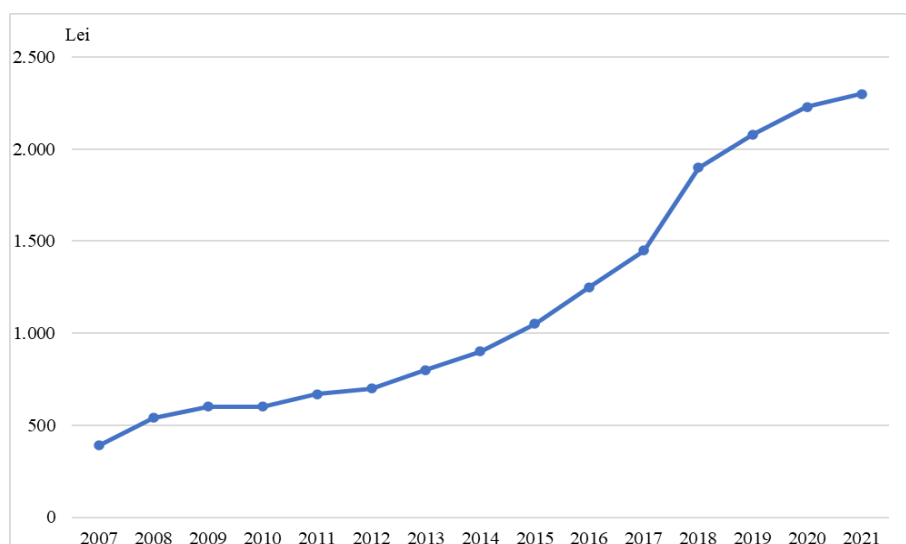
Source: data based on Table 1 (Appendix)

We observe an upward trajectory of it, especially starting with 2016, when it increased by 16% compared to 2015, and in 2018 there was a 37% increase compared to 2017. If we consider the year 2021 compared to the year 2007, the minimum wage is currently approximately 6 times higher. As a matter of fact, the most employees with minimum salary were in retail trade, wholesale trade, land and pipeline transport.

3. The relationship between minimum wage and economic growth

In our work, we express economic growth through the GDP/capita indicator. Therefore, in the following we show that there is a directly proportional correlation between the minimum wage and GDP/capita, as well as between the minimum wage and the effective individual consumption of households (abbreviated AIC).

In the case of determining the relationship between the minimum wage and GDP/inhabitant compared to the AIC, the difference between these two concepts must be made.

Effective individual consumption more faithfully reflects the well-being of a citizen of a certain country than the Gross Domestic Product per capita. The latter is based on goods and services purchased and paid for by a household. Instead, the AIC is calculated based on the goods and services actually consumed by individuals, without taking into account the fact that they were contracted and paid for by households, government or non-profit organizations. That is why it is preferable for international comparisons and better reflects the standard of living.

The differences result from the fact that the share of payments made directly by households for important services, such as health and education, differs substantially from one country to another. Thus, the apparent order of the countries according to the standard of living, which would result from the comparison of the classic GDP/capita, may undergo important changes.
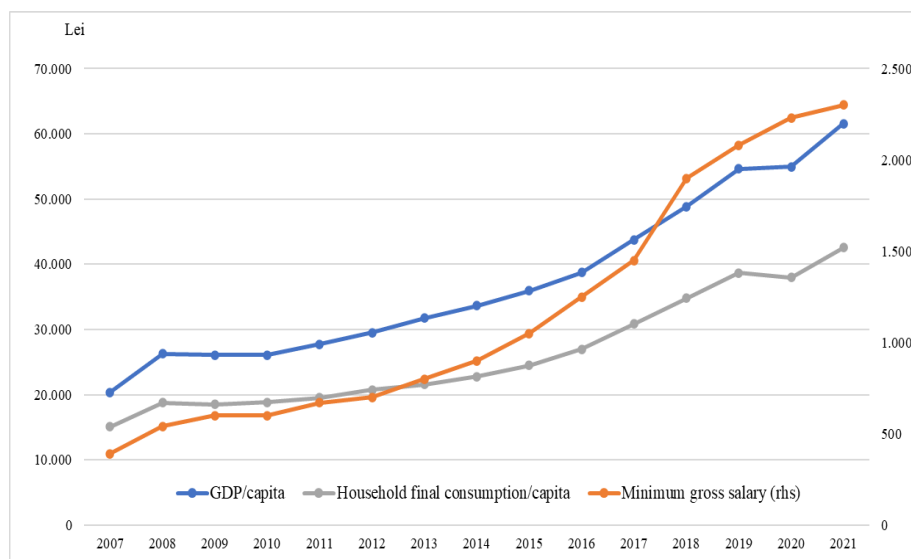
The actual individual final consumption of households includes: the expenses of households for the purchase of goods and services in order to satisfy the needs of their members, the expenditure for individual consumption of public administrations (education, health, social security and social actions, culture, sports, recreational activities, household waste collection) and the expenditure for individual consumption of non-profit institutions serving households (religious organizations, trade unions, political parties, unions, foundations, cultural and sports associations) (INS, Methodological specifications).

During 2007-2021, both the minimum wage and GDP/inhabitant increased, the minimum wage at a faster rate (approx. five times), and GDP/inhabitant three times (see Table 2, in the Appendix). The peak was reached, for the two indicators, in 2021.

However, the year 2009 is an exception, when the GDP/capita indicator registered a lower level of 219 lei compared to 2008. Household consumption/inhabitant increased approximately 3 times in 2021, compared with 2007. The minimum wage influences consumption, its increase implicitly leading to an increase in the population's expenses.

In the analysed period, final consumption experienced a sharp evolution, with significant increases from one period to another. The exception is the year 2009, when it recorded a decrease of 234 lei, compared to 2008. It is noted that the evolution of the two macroeconomic indicators (GDP/capita and household consumption) is very similar, with sharp increases for the period 2010-2021.

Figure 2

Evolution of gross minimum wage, GDP/capita, household final consumption/capita in the period 2007-2021

Source: processing according to Table 2 (in the Appendix)

In order to verify the influence of the minimum gross salary per inhabitant, measured in lei, and of the effective individual consumption of households per inhabitant (Ron) on the GDP per inhabitant (Ron) at the level of Romania, the VAR econometric analysis method was used.

VAR-type models are frequently used for forecasting interconnected time series systems and for analysing the dynamic

impact of innovations on the system of variables. The VAR approach circumvents the need for structural modelling by treating each endogenous variable in the system as a function of lags, of past values, of all endogenous variables in the system. The VAR model has the following advantages:

- does not require a clear separation of endogenous and exogenous variables;
- they can be used to deduce how economic variables respond to shocks;
- are widely used in macroeconomic modelling, being included in most econometric programs.

A VAR model was also chosen for an additional reason, namely the impossibility of stationarity in the level, the first difference or the second difference of the GDP per capita indicator. The result of the VAR model is shown in Table 3.

Table 3

VAR type analysis

Vector Autoregression Estimates
Date: 10/16/22 Time: 20:50
Sample (adjusted): 2009 2021
Included observations: 13 after adjustments
Standard errors in ( ) & t-statistics in [ ]

	GDP/capita	AIC/ capita	Gross minimum wage
GDP/ capita(-1)	0.520212	-0.118039	-0.022106
	(1.10735)	(0.91674)	(0.05146)
	[0.46978]	[-0.12876]	[-0.42957]
GBP/capita(-2)	1.209755	0.999835	0.101127
	(0.93244)	(0.77194)	(0.04333)
	[1.29741]	[1.29523]	[2.33370]
AIC/ capita(-1)	-0.734229	0.188454	0.125775
	(1.48244)	(1.22727)	(0.06889)
	[-0.49528]	[0.15356]	[1.82564]
AIC/capita(-2)	-1.886946	-1.436518	-0.117212
	(1.70545)	(1.41189)	(0.07926)
	[-1.10642]	[-1.01744]	[-1.47888]
Gross_min_wage(-1)	23.42894	17.57011	0.022296
	(13.3822)	(11.0787)	(0.62191)
	[1.75076]	[1.58593]	[0.03585]
Gross_min_wage(-2)	-2.186011	-4.504922	-0.475202
	(13.5902)	(11.2509)	(0.63158)
	[-0.16085]	[-0.40040]	[-0.75240]

C	18927.55	11994.88	-1352.414
	(20853.2)	(17263.7)	(969.113)
	[0.90766]	[0.69480]	[-1.39552]
R-squared	0.990940	0.987176	0.993277
Adj. R-squared	0.981880	0.974351	0.986554
Sum sq. resids	16003988	10968643	34564.68
S.E. equation	1633.197	1352.075	75.89980
F-statistic	109.3773	76.97640	147.7379
Log likelihood	-109.5983	-107.1426	-69.70285
Akaike AIC	17.93820	17.56040	11.80044
Schwarz SC	18.24240	17.86461	12.10464
Mean dependent	39481.79	27556.77	1266.923
S.D. dependent	12132.87	8442.429	654.5404
Determinant resid covariance (dof adj.)	7.05E+14		
Determinant resid covariance	6.93E+13		
Log likelihood	-262.4887		
Akaike information criterion	43.61364		
Schwarz criterion	44.52625		

Source: own calculations according to data taken from the INS, 2022 (Table 2)

According to the data in the table, it can be seen that in the case of all three equations, especially the one of interest (with GDP per capita as the dependent variable and the other two indicators analyzed as independent), the influence of the endogenous variables on the exogenous is around 99%. The extracted equation is analyzed in the following:

GDP/ capita = 0.520211997803*GDP/capita(-1) + 1.20975543902* GDP/capita(-2) - 0.734228554406*AIC/capita(-1) - 1.88694613022*AIC/capita(-2) + 23.4289385052*gross min wage(-1) - 2.18601133198*gross min wage(-2) + 18927.5495522cap

It can be noticed the minimal influence and the oscillating trend of the effective individual consumption of households per inhabitant on both lags, varying between -0.734228554406 on lag 1 and +1.20975543902 on lag 2, proving that the gross minimum wage, for the analysed period, has the greatest influence, especially on lag one (+23.4289385052), on lag two being, as in the case of the first independent indicator, negative (-2.18601133198).

In conclusion, in the short term the gross minimum wage has a significant impact on GDP per capita, but in the long term this influence decreases. On the other hand, the influence of the actual individual consumption of households in both the short and long term is much smaller.

4. Conclusions

In our paper, we made an analysis of the gross minimum wage in Romania, in the period 2007-2021, as well as its evolution in correspondence with the GDP/ capita and the individual consumption of households' indicators, being a proportional relationship. I expressed the economic growth by means of GDP/inhabitant, and about consumption it is well known that it has an important weight in determining the GDP.

The increase in the minimum wage led to an increase in consumption, so the increase in GDP was achieved due to government spending and consumption. Also, agriculture, industry, construction, services contributed to the growth (where there are most minimum wage contracts).

Also, in this interval, both the minimum wage and GDP/inhabitant increased, the minimum wage at a faster rate (approx. 5 times), and GDP/inhabitant three times. The peak was reached for both indicators in 2021. However, the year 2009 is an exception, when the indicator registered a lower level of 219 lei compared to 2008. Household consumption/inhabitant increased by approx. 3 times in 2021, compared to 2007. The minimum wage influences consumption, its increase implicitly leading to an increase in the population's expenses.

In the analysed period, final consumption experienced a sharp evolution, with significant increases from one period to another. The exception is the year 2009 (the year of economic and financial crisis), when it recorded a decrease of 234 lei, compared to 2008.

It is noted that the evolution of the two macroeconomic indicators (GDP/capita and household consumption) is very similar, with sharp increases for the period 2010-2021.

At the same time, in order to verify the influence of the minimum gross salary per inhabitant, measured in lei, and of the effective individual consumption of households per inhabitant (lei) on the GDP per inhabitant (lei) at the level of Romania, the VAR econometric analysis method was used, according to which, especially in the case of the equation with GDP per capita as the dependent variable and the other two indicators analysed as independent, the influence of the endogenous variables on the exogenous is around 99%. In conclusion, in the short term the gross minimum wage has a significant impact on GDP per capita, but in the long term this influence decreases. On the

other hand, the influence of the actual individual consumption of households in both the short and long term is much smaller.

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- Ministry of Public Finance, IMPACT ANALYSIS regarding the minimum gross salary guaranteed in payment for the year 2020
- National Institute of Statistics, online TEMPO databases

Table 1

Evolution of minimum gross salary during the period 2007- 2021

Valid from	Gross	Net wage	Gross (higher education)	Net (higher education)	Change (increase) compared previous period	Government decision	Note
		Minimum salary					
			LEI		**%**		
1 January 2021	2 300				+ 3,1	HG 4/2021	
1 January 2020	2 230	1 346	2 350 (€ 491,74)	1 413 (€ 295,67)	+ 7,2	HG 935/2019	
1 January 2019	2 080	1 263	2 350 (€ 502,58)	1 413 (€ 302,19)	+ 9,5	HG 937/2018	
1 January 2018	1 900	1 163			+ 31,0	H.G.846/2017	*OUG 79/2017 - The gross salary also increased due to the transfer of contributions from the employer to the employee*
							25% of Romanian employees earn approximately the minimum in the economy
1 February 2017	1 450	1 065			+ 16,0	HG 1/2017	*1,3 million employees, representing 30% of the total, work on the minimum wage.*
1 May 2016	1 250	925			+ 19,0	HG 1017/2015	
1 July 2015	1 050	785			+ 7,1		
1 January 2015	975	732			+ 8,3	HG 1091/2014	*In 2015, Romania had the second lowest salary in the European Union, after Bulgaria. About 2,4 million workers earned the national minimum wage or less, which represented 40% of the total number of active workers. Of these, 1,6 million worked full-time and 0,7 million worked part-time.*
1 July 2014	900	678			+ 5,9		
1 January 2014	850	644			+ 6,3	HG 871/2013	*At the end of 2014 there were over one million employees (20% of the total wage earners in the economy) who had the minimum wage, almost 12 times more than in August 2011.*
1 July 2013	800	609			+ 6,7	HG 23/2013	*In December 2013, Romania had the second lowest salary in the European Union, after Bulgaria.*
1 February 2013	750				+ 7,1		
1 January 2012	700				+ 4,5	HG 1225/2011	*În April 2012, Romania was the only country where almost a quarter of employees had the minimum wage.*
1 January 2011	670				+ 11,7	HG 1193/2010	*In August 2011, fewer than 90,000 workers were paid the national minimum wage.*
1 January 2009	600		1 200 (€ 298)		+ 11,1	HG 1051/2008	
1 October 2008	540				+ 8,0	HG 1051/2008	
1 January 2008	500				+ 28,2	HG 1507/2007	
1 January 2007	390				+ 18,2	HG 1825/2006	

Source: The Ministry of Labor and Social Justice, the minimum gross salary in the period 2007-2021

Table 2
**Evolution of gross minimum wage, GDP/capita, household final
consumption/capita in the period 2007-2021**

Years	GDP/capita	Minimum gross salary	Household final consumption/capita
2007	20 385	390	15 092
2008	26 285	540	18 770
2009	26 066	600	18 536
2010	26 104	600	18 854
2011	27 740	670	19 516
2012	29 501	700	20 760
2013	31 766	800	21 568
2014	33 626	900	22 780
2015	35 916	1 050	24 494
2016	38 751	1 250	26 941
2017	43 786	1 450	30 861
2018	48 847	1 900	34 765
2019	54 654	2 080	38 660
2020	54 954	2 230	37 969
2021	61 553	2 300	42 534

*Source: INS, Main aggregates, per inhabitant - SEC 2010, current prices, Tempo
databases*