

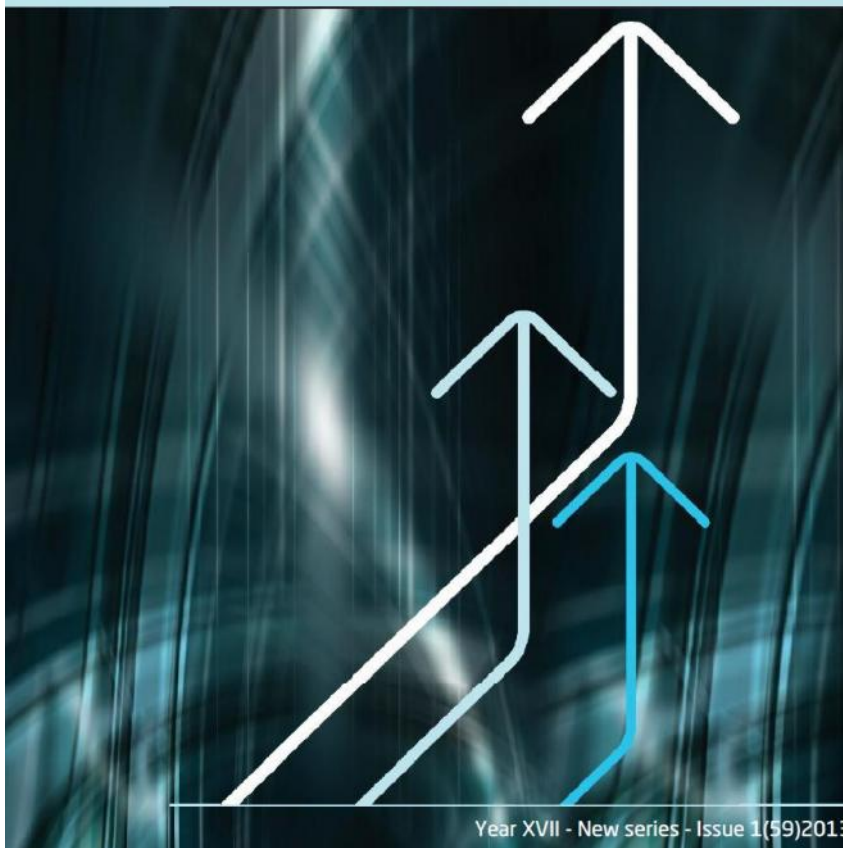


Romanian Academy

"Costin C. Kiriltescu" National Institute for Economic Research

"Victor Slăvescu" Centre for Financial and Monetary Research

# Financial Studies



Year XVII - New series - Issue 1(59)2013

“VICTOR ȘTEFĂNESCU”  
CENTRE FOR FINANCIAL AND MONETARY RESEARCH

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**FINANCIAL STUDIES**



**ROMANIAN ACADEMY  
NATIONAL INSTITUTE OF ECONOMIC  
RESEARCH  
“VICTOR ȘI VESCU”  
CENTRE FOR FINANCIAL AND MONETARY  
RESEARCH**



# **FINANCIAL STUDIES**

**Year XVII – New series – Issue 1 (59)/2013**

**ANNIVERSARY ISSUE**



ROMANIAN ACADEMY  
"COSTIN C. KIRI ESCU" NATIONAL INSTITUTE FOR ECONOMIC RESEARCH  
"VICTOR SI VESCU" CENTRE FOR FINANCIAL AND MONETARY RESEARCH

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## CONTENTS

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<b>THE COMING OF AGE OF FINANCIAL STUDIES JOURNAL</b> .....8 PhD Tudor CIUMARA	8
<b>FOREWORD</b> .....11 PhD Gheorghe MANOLESCU	11
<b>THE INTRODUCTION OF GLOBAL INCOME TAX SHOULD BRING ADDITIONAL REVENUE TO THE STATE</b> .....13 Interview with PhD Valentin LAZEA	13
<b>HAYEK – „THE ROAD TO SERFDOM” ROMANIA, RETURN FROM THE „THE ROAD TO SERFDOM”</b> .....18 PhD Floarea IORDACHE	18
<b>DOCUMENTARY: HYPOSTASES OF THE SUSTAINABLE DEVELOPMENT</b> .....34 Florin R. Zvan B. L. ESCU	34
<b>BANKING RISKS IN A GLOBAL ECONOMY</b> .....47 PhD Gabriela-Cornelia PICIU	47
<b>IMPACT OF THE FISCAL POLICIES ON THE STANDARD OF LIVING OF THE EMPLOYEES</b> .....58 PhD Elena P. DUREAN PhD Ionel LEONIDA	58
<b>INERTIAL BEHAVIOUR AND THE SUSTAINABLE DEVELOPMENT OF THE FIRM</b> .....68 PhD Mihail DIMITRIU	68

## THE COMING OF AGE OF FINANCIAL STUDIES JOURNAL

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PhD Tudor CIUMARA\*

### Abstract

Short presentation of the evolution of Financial Studies journal, starting from its first issue in 1995.

**Keywords:** financial bulletin, financial studies

### JEL Classification: B 26

Financial Studies is 18 years old this year<sup>1</sup>. Our journal first appeared under the name “Buletin financiar” in 1995, as a publication of the “Victor Sl vescu” Institute for Finance, Prices and Foreign Exchange Affairs<sup>2</sup> of the Romanian Academy. At the time, the goal was to publish financial news, studies, documentations and specialized information that would reflect the activity and interests of the Institute’s researchers. It was intended to have only the Institute’s personnel as authors of the materials published in the bulletin. The expected audience of the journal was represented by specialists working in public and private financial institutions, researchers and other academics, to whom the publication was distributed free of charge. In time, the journal became more and more focused on research papers and among those that published here we had an increasing number of external authors. Today, the journal’s focus remains on financial research, actively seeking an authorship as diverse as possible, while maintaining academic rigor.

There were a couple of changes in the name of the journal. First, in 2001, it was renamed “Studii financiare”, with the parallel title

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\* Director „Financial Studies”, scientific researcher III “Victor Sl vescu” Centre for Financial and Monetary Research, Romanian Academy.

<sup>1</sup> It should be noted that according to the cover of the journal we are only in the 17th year. This is due to the fact that the journal has a gap year in its publication (2002).

<sup>2</sup> The name of the institution changed in 2001 in “Victor Sl vescu” Centre for Financial and Monetary Research. It is part of “Costin C. Kiri escu” National Institute for Economic Research of the Romanian Academy.

“Financial Studies”. Then, since the end of 2012, only the English version of the title remained in use. These changes also reflect the different stages of the journal in terms of the language of appearance. Initially the journal appeared in Romanian, then we had bilingual editions, Romanian and English and currently we only publish in English. In the meantime, we also had changes regarding the format of the journal. Until 2009 the journal appeared in print and since then we switched to an exclusively online format.

The first issue of the journal appeared at the end of March 1995. In the foreword of the first issue, dr. Gheorghe Manolescu, the director of the journal and also of the Centre, stated the strong emphasis placed on theory of the journal. He also expressed the hope that the journal will represent, due to its content diversity, an impulse to a deeper analysis and understanding of financial realities. Now, after 18 years, we find that the mission of the journal remains unchanged. Financial Studies is a forum for the dissemination of new and substantial financial research. Although, like the institution it represents, it still focuses on fundamental financial research, Financial Studies welcomes empirical, applied and policy-oriented contributions.

Due to the fact that the journal was never formally financed, its directors and board members always struggled, especially when it appeared in print, to obtain essential donations and sponsorships. The initial sponsors of the journal were Banca Română de Comer Exterior, Banca Agricol, Banca Comercială Română, Banca Română pentru Dezvoltare and Banc Post. However, even with the occasional assistance from sponsors, the journal’s development has always been hampered by the lack of (sufficient) financial resources. This obviously seems rather ironic, considering the journal’s name.

In the 58 issues of the journal that appeared so far we had the privilege of publishing influential papers, written by important authors from Romania and abroad. Trying to honour those that published their work in our journal, in this anniversary edition we publish English translations of some of the best papers that appeared in our journal in the years when Financial Studies only had a print edition. The selection is based on the quality of the papers and was made by a committee consisting of the journal’s director, its editor-in-chief and the director of “Victor Săvescu” Centre for Financial and Monetary Research.



At this anniversary moment we also start a new tradition: the Financial Studies Awards. These awards are meant to offer, on a yearly basis, recognition to the authors of the best papers published in the journal and to those that have outstanding contributions to the development of the journal.

Today, Financial Studies actively seeks to establish itself as an influential outlet for high-quality papers on financial topics and as an important voice of financial academic research. To this end, we need the spirited support of all of ours readers, authors, editorial team and board members. We start a new stage in our journal's life with great objectives!

## FOREWORD

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PhD Gheorghe MANOLESCU\*

### **Abstract**

This paper is a translation of the *Foreword* to the first issue of the journal, published in April 1995.

**Keywords:** financial bulletin, finance, economy

**JEL Classification:** E60, F65, G20

The establishment, expansion and development of market economy in Romania, the institutionalization and instrumentation of its specific behaviours in all economic subsystems, presumes a sustained effort of adaptation, transformation and innovation in the field of the economic praxis and, at the same time, a continuous endeavour towards knowledge, in order to explain, understand and interpret the phenomena and processes that appear, interlock and consolidate so that, gradually, the economic action acquires the theoretical structure able to fundament and orient it.

The financial issues, under their different aspects, are a major component of the economic praxis and knowledge of the transition to market economy; its particular significance derives from the nature and characteristics of the market economy, as well as from the specificity of the relations between macro and microeconomics, between the public authority and the diversity of economic agents under the conditions of this type of economy.

Being aware of the complexity of these issues during the period of transition and of the responsibility of the fundamental research in this field, the “Victor SI vescu” Institute for Finance, Prices and Foreign Exchange Affairs of the Romanian Academy, decided to publish a quarterly “Financial Bulletin”. This publication will bring out

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\* *Scientific researcher I, the Director of the “Victor SI vescu” Institute for Finance, Prices and Foreign Exchange Affairs, Romanian Academy at the time when the first issue of the journal was published.*

studies with a strong theoretical content, drawn up by the researchers of the institute, outside the research plan, as well as by external collaborators willing to contribute to a better understanding and explanation of the transition phenomenology. The bulletin will also publish documentaries and translations, notes and comments, financial information, will notify on new books or other publications, and will provide a set of relevant charts presenting financial problems from different angles.

The topics include public finance, currency, credit, hard currency and international financial relations, prices, company finances and accounting theory, financial policies and strategies etc. Their ontological unity and epistemological integrability brings them closer to the field of theoretical research.

Hoping that the Financial Bulletin will be, through the diversity of its content and multitude of approaches, an impulse towards reflection and deeper understanding of the financial realities, and expecting the collaboration of all those taken up by the inconstancy of questions, we are waiting for your observations, suggestions and contributions.

PhD Gheorghe Manolescu  
Director of the "Victor Slavescu" Institute for Finance, Prices and  
Foreign Exchange Affairs, Romanian Academy  
April 1995

## **THE INTRODUCTION OF GLOBAL INCOME TAX SHOULD BRING ADDITIONAL REVENUE TO THE STATE**

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### **Abstract**

This paper is an exclusive interview with Mr. Valentin Lazea, state secretary – Department for Economic Analysis and Financial System Informatisation. The paper is a translation of the interview that was published in issue nr. 9 (1997) of Financial Bulletin (previous name of Financial Studies).

**Keywords:** taxation system, real economy, economic growth, budget revenues

**JEL Classification:** H2, H21

**FINANCIAL BULLETIN:** At the beginning of the year, in just two days, the national currency devalued by almost 100% in relation with the US Dollar. The National Bank had to intervene in a strong manner in order to stop the decline of the leu. Economic theory shows, however, that the financial-monetary policy measures yield results only on the short-term, 9-12 months. Do you think that the measures taken within the real economy for privatization, reorganisation, revival of the export sufficiently support the financial-monetary policy of the government?

**VALENTIN LAZEA:** I must begin by saying that the my answers to your questions represent my personal opinions, as specialist and that they must not be interpreted as official positions of the Ministry of Finance, or of the party that I represent, PSDR. Regarding the actions taken within the real economy to support the monetary and financial policies, we may say that, despite some hesitations, more has been accomplished in the last 10 months than in the 7 previous years. The most spectacular result was scored in agriculture where, at least in 1995-1996, was a hindrance to the reform. The fact that the idea of not crediting the agriculture with fresh money injected by National

Bank into the system was accepted, represents, in itself, a true revolution. Also, the shutdown of 20 bankrupt animal production units, despite the populist wave of protests, proved to be a success, largely closing up this "black hole" which was draining the state funds.

Although they are less clear, the measures for reorganising the industry are also noteworthy. The shutdown of the fifteen unprofitable units has to be finalised despite some diversionist actions that claim either the existence of court orders that contest General Assembly decisions, or the uniqueness of the heat sources of some localities which would be left out cold as those units are closed down. The Government cannot afford to go back on the issue of these 15 enterprises because its image would be seriously affected. We must also note the success of shutting down a large number of mines and the sacking of more than 60 thousands miners, representatives of a sector that produced much negative added value (it was decreasing the gross domestic product instead of increasing it). Even though undecided and hesitant, the measure of letting seven refineries of the existing nine at the will of the market also is a brave measure that has to be taken to its very end. Some of them will probably not hold and will close down. The Government will have to have the strength not to jump to their aid, otherwise it will do exactly as the V c roiu government did: each time the reform turned painful, it backed off. It is not without importance that the lack of credibility manifested within the international financial media regarding our country originates in this ambivalent attitude which our leaders had until 1996; the following months will test this government too.

**FINANCIAL BULLETIN:** Is the current taxation system a stimulant for work, saving and investments, therefore for long-term economic growth?

**VALENTIN LAZEA:** My position regarding taxation is very clear, even though it is not very often met within the public debates: Romania has the most liberal taxation policy in Eastern and Central Europe (actually in all Europe) and the possibilities to stimulate the economy further in this direction are exhausted. With consolidated budget revenues amounting to less than 27% of the GDP we cannot ensure the efficient functioning of a modern state. Those who are condemning the current taxation system in Romania probably don't know what they are saying. Let's exemplify:

The VAT rate is 18% in Romania (with many reductions to 9% and with many exemptions), while the standard rate is 22% in Poland and the Czech Republic and 25% in Hungary and the Slovak Republic.

The profit tax rate is 38% in Romania compared to 40% in Poland and Slovak Republic, 29% in the Czech Republic and 18% in Hungary.

The tax rates for social insurances are between 30-40% in Romania for the employers and 4% for the employees, while in Hungary the corresponding figures are 47% and 11%, in the Czech Republic they are 35.25% and 13.15%, in Poland 40% and 0% and in the Slovak Republic they are 38% and 12%, respectively.

It is true, however, that Romania has a very high marginal rate of wage taxation (60% of the income exceeding a certain level), but this affects a very small number of employees (under 5% of the total workforce); this marginal level will most certainly be removed in the future, maintaining the highest taxation rate at 40%.

Under these conditions, no well-intended person may say that fiscality is excessive in Romania.

**FINANCIAL BULLETIN:** The intention to introduce a system of global taxation of the incomes as of January 1<sup>st</sup>, 1998, besides the huge costs it will involve, will it not increase tax evasion, since the state doesn't have enough means to check the correctness of the fiscal statements?

**VALENTIN LAZEA:** In my opinion, the introduction of the global income tax should bring additional revenue to the state budget, not decrease the existing revenues. Otherwise it would be foolish to spend a lot of money with training the staff, advertising and purchase of computers (long-term debt of the state) if the revenue to the budget would decrease.

Two preconditions are required for this increase of the budget revenues:

- The bulk of incomes (from wages, dividends and interests) should be taxed at the source, which would make the attempt to falsify the incomes less effective.
- The taxation rate for the global incomes should not be too different from the current rate used for the tax on wages. In other word, besides discarding the 60% marginal rate, the other changes should be purely "cosmetic".

If these two preconditions are observed, there is no reason for the revenue to the state budget to decrease. True, there will be many undeclared sources of income (those are not taxed presently either, as a matter of fact), so that ultimately the measure should be beneficial for the budget.

The more sophisticated sources of income (capital gain, use of in kind goods, etc.) are more difficult to evaluate and control at this moment. They require specific procedures that can only be integrated in time.

**FINANCIAL BULLETIN:** The Government planned rather small rates of economic growth for the next three years, 1-2% each year, lower than the average rate of growth stated by the programs of the other governments from Central and Eastern Europe (4.5% per year). How will the budget be able to support important sectors such as health care, education or national defence, whose funds are scarce currently?

**VALENTIN LAZEA:** Your question has two different aspects. On the one hand, the rate of growth will depend, in our country, on the rapidity and depth of the reorganisation. If privatization will be largely concluded by 1999 and the large state monopolies and autonomous units will be broken down, way may witness, starting that year, annual growth rates in excess of 5%.

However, until these measures from the real economy are finalised, the monetary-financial restart could be hasty, repeating the error made in 1995-1996, when money was pumped into an economy that was insufficiently reorganised.

The second aspect of your question concerned the support from the budget of the sectors which, by definition, represent "public goods": health care, education, national defence.

I absolutely agree that these sectors should consume most of the budget funds. In this respect, I don't agree with the exaggerated allocation, in 1997, of the funds with social destination (the human capital would have been much better stimulated if part of that money would have been directed to schools and hospitals than to the families with many children), as I also cannot agree with the stronger accent, in the 1998 budget, on economic expenditure.

Two things are needed to ensure proper funds for the health system, education and national defence: ending the process of tax

reduction (see the answer to the second question) and making a hierarchy of the budget priorities within the Government.

**FINANCIAL BULLETIN:** For the first time after 1989, the small and medium enterprises started to massively “produce” unemployment. What does the Ministry of Finance intend to do to improve the economic and social environment in which the small and medium entrepreneurs conduct their activities?

**VALENTIN LAZEA:** The subject of the small and medium enterprises is a common subject lately. The Ministry of Finance should provide an equal treatment with the other tax payers. By this, I understand a correct, nonpartisan attitude of the fiscal inspectors, who should objectively control those enterprises.

It would be completely unrealistic to demand fiscal facilities for enterprises that represent over 75% of the total number of companies. Anyhow, wherefrom this idea that the small and medium enterprises should be unconditionally supported? Firstly, most of them operate in the field of services (not of direct production) and have a very low export activity; and the export is the drive for relaunching the Romanian economy. Secondly, it is not even true that most of them would have gone bankrupt if restrictive financial-monetary policies are implemented. As far as I know, in the first half of 1997, the average number of newly established companies balanced the average number of discontinued companies.

Of course, considering the many similarities of mentality, tradition etc. it is possible that in Romania “hold” the Italian pattern of the multitude of small, family companies as fabric of the national economy. However, stimulating them excessively, while endangering the budget equilibria, seems a luxury that Romania cannot afford.



# HAYEK – „THE ROAD TO SERFDOM” ROMANIA, RETURN FROM THE „THE ROAD TO SERFDOM”

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PhD Floarea IORDACHE\*

## Abstract

This paper is a version with minor changes of the article published in issue no. 15-16 (1999) of Financial Bulletin (previous name of Financial Studies).

**Keywords:** market economy, liberal system, socialist doctrine, political systems

**JEL Classification:** B14, P1, P2

## 1. Introduction

By its vast work written between 1931-1979, with over 200 titles of books and articles, covering very diverse areas of the social sciences, Hayek remains a visionary of the 20<sup>th</sup> century, a thorough researcher of the society, one of the most fertile spirits.

In 1974 he received, along with G. Myrdal, the Prize for Economic Sciences in memory of Alfred Nobel. Having a purely scientific connotation, the prize is rather special, because the two of them are prominent researchers whose area of interest goes beyond what the term of “pure economy” suggests. After all, G. Myrdal remained a consequent supporter of the statist policies, while Hayek, particularly representative for neo-marginalism, a current which started in 1920 and developed the theory of the economic calculation while making the apology of the liberal system, devoted his career to fighting the statist policies.

The best known work of Hayek, which put him into the focus of the world, was “The road to serfdom”, which may be seen as a two-

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\* *Scientific researcher III, “Victor Slăvescu” Centre for Financial and Monetary Research, Romanian Academy*

way street “if the stimulants to change the direction of travel are rather strong and the arguments in favour of liberty are rather convincing” (Hayek, 1997, p.310).

One way of the road is crossed by the questions and responses of Hayek, by his observations and analyses on British ground of the curious anomalies of the Western Europe contemporary with him. This is the 1940-1943 period, when Hayek was writing his book, when England, although didn't resemble to Hitler's Germany, or with the fascist Italy and the communist Russia, was not far from the same danger. The danger came from the manifestation of the same despise towards 19<sup>th</sup> century liberalism, from the acceptance of the progressist British of the conclusions which Germany took after World War First and which finally led to the establishment of the Nazi regime.

It is known that in 1933 Hitler's regime took power in Germany, which changed the balance of forces in Europe, and started, together with other countries, the race for economic and military preparation of the Second World War.

The title of the book, “The road to serfdom”, thus towards dependency, is significant; the book is a true demonstration of three important problems: why has the liberal tradition been abandoned; how was it abandoned and why the abandonment of this doctrine led to totalitarianism after the First World War, among other countries in the Nazi Germany, fascist Italy and Bolshevik Russia.

As it is well-known, the consequences of the Second World War were very damaging for Romania, both in terms of human losses (over one million victims account for the blood tribute of Romania), material losses (total losses of about 3.7 million \$) and political losses (due to the agreement between the great powers, Romania was thrown into the Soviet influence area which affected the subsequent political and economic-social life). Thus, the totalitarianism, the dictatorial system of centralised governance, ruled in Romania for more than 4 decades.

The 1989 revolution brought freedom from these structures, hopes for the Romanians and also many questions which come over and over again, obsessively: where are we heading? Towards what kind of economy? When and how will the reform yield results? Will everybody benefit from it? These questions are just a fragment of

those than can cover the other way of the road of Hayek's book. Because, just like Romania, other East European countries are experiencing a period of transition towards market economy; this is a very general and vague formulation which doesn't completely satisfy the people, irrespective of one's training. Hayek's book, far from being obsolete, was an instrument which undermined the Soviet system and it is very relevant and actual for these days.

My intention, in writing these lines, was to take a round trip of Hayek's "road". In one direction, I would like to highlight some of Hayek's main ideas that come forth from his book, which remind of some features of the neoclassic liberalism from the interbellum period and from the early post-war period.

In the other direction, it seemed important to show the reversed way that Romania crosses since 1989 to this moment, from totalitarianism towards market economy, for whose understanding I felt the need to give a brief account of the movement of ideas from the economic thinking in the interbellum Romania, of the forced placement of our country in the European penumbra, thus in totalitarianism.

In his book, Hayek warns, without going into details, about the attraction of the "middle way". The economic life must not be run according to an extreme decentralization of the free competition, while the idea of the absolute centralization was stressing many people due to the huge difficulties to enforce it and due to the horror of having everything run from a single centre. Because of this, the combination of the two methods, Hayek's warning about the "middle way", which seemed the most balanced way to his contemporaries. For the past 50 years, this idea has been very important and current; it draws an increasing number of supporters because it seems balanced and reasonable. The question is, however, if it leads to a "road towards serfdom" given the important trends towards the mixt economy and the increasing role of the government in the economic life.

## **2. Hayek and the „Road towards serfdom”**

For Hayek, writing the book was a duty which he could not neglect. Given the period and atmosphere in which it was written, trying to clarify the most burning and most important problems, which were far beyond those of the economic theory, his courage was

enormous. A political book by excellence, it doesn't express, however, beliefs originating from personal interests; rather, it starts from the discontent towards the erroneous interpretation given to the Nazi movement by the British progressive circles. Hayek was supported in his endeavour by his extraordinary experience gathered during the successive periods when he lived in different countries (native Austria, USA, contact with the German intellectuals) harmoniously mixed with his interest for the evolution of the political thinking, area which he analysed for more than 30 years.

Thus, it was not difficult for him to notice how the British ideals and political strategy were influenced by the German thought and practice, how England, after more than 2 centuries (it reached the supreme liberty in 1870, when it was the intellectual leader in the social and political areas) comes to import German ideas. Hayek noticed and draws attention to this change of the direction of spreading of ideas, from Germany towards England and the rest of the countries. At the same time there also was a change in the direction of ideas: the classical liberalism, defender of the market economy and of the private property and profit, was discarded and the orientation shifted towards socialist ideas. The latter, although were improved in Germany during the last quarter of the past century and the first quarter of the 20<sup>th</sup> century, due to its impressive material progress and due to the extraordinary reputation of the German thinkers and scientists (Hegel, Marx, List etc.), don't originate from here. The French thinkers were the ones who set the bases of the modern socialism, but they never thought that their ideas were to be put into practice only by a dictatorial government. "Socialism was for them just an attempt to end the French revolution" (Hayek, op. cit., p. 37). They considered that the freedom of thinking was the root of evil in the 19<sup>th</sup> century society. Most of those who embraced socialism, despite the warning, thought in the promise of a higher freedom, of a "new liberty" that could be the obvious inheritor of a liberal tradition. The "new liberty" promised by the socialist doctrine was the freeing from the empire of necessity and the leap towards the empire of liberty, of the economic liberty, without which the gained political liberty was meaningless.

During the 18<sup>th</sup> and 19<sup>th</sup> centuries, the classical economic liberalism had been attacked, from multiple directions and for the

most variable reasons, both by the adversaries of the market economy and private property on the production means, and by some defenders of the market economy on grounds pertaining to the economic policy or to methodology. At the end of the 19<sup>th</sup> century, some thinkers tried to revive liberalism in response to the intensifying attacks against the liberal economic thinking and to the improper performance of the classical economic liberalism. These thinkers have been labelled as neoclassical and their thought as neoclassicism. This created a bridge between the classical liberals who assumed and supported several features of the paradigm of the classic liberalism (individualism, hedonism, deductive method in explaining the economic phenomena, defence of the market economy and of the private property etc.) and also a revolution made by the neoclassic (they reject strongly, for instance, the objective theory of the value and price). The neoclassics were against all currents that were criticising liberalism (such as socialism, Marxism, radicalism etc.) but, at the same time, they minimised several economic and social problems of their time (economic crises, unemployment, etc.) or even intently eluded other (social inequities, etc.). The amplified criticism from the opponents (mostly Marxists, Keynesians and radicals) determined the liberal neoclassic to adapt to the new situation from the interbellum period and from the beginning of the post-war period.

Several movements appear towards the adaptation to the requirements of reality, among which: a) concern of some neo-marginalist thinkers for the improvement of the rational economic calculation, which resulted in the development of econometrics (we may include here R. Frisch, I. Fisher and Fr. Divisia); b) effort of the German neoliberals, the “ordoliberals” who proposed the establishment of the social market economy; c) strong argumentation against the collective property and of the excessive intervention of the state in economy, against the directing and centralised planning, from the ultraliberal publicists led by F. Hayek.

Hayek is one of the most important representatives of the neoclassical and neoliberal thinking from the mid-20<sup>th</sup> century, a visionary and a profound researcher of society. In his “Road to serfdom” he noticed bitterly how in the middle of an European civilisation appeared this clash of ideas that leads to conflict, while the

values in the name of which the war is fought are threatened in England too, while they are already destroyed elsewhere. This transformation of the European thinking is lived at different intensities in different countries. England lagged in this process of transformation and he calls it somehow “lucky”; nevertheless, the slow evolution of things produced the change and the direction of action is reversed, as the author noticed, while most of the British ignored it.

The discarding of liberalism, of its basic principles according to which “there are not severe rules set or ever”, little use of constraints and “beneficial role of the competition”, was due, according to Hayek, among other, to the slow emergence of the benefits of the gradual improvement of the institutional framework of a free society. The author admits that there were still a lot of things to learn, but the progress could be achieved only by the addition of new ideas to the old and rudimentary rules of the 19<sup>th</sup> century economic policies. However, contrary to Hayek’s observations, the idea that the only way to do was to remodel society from scrap, removing completely the old templates, gained increased acceptance, and this meant leaving the road they just embarked on, the road of socialism, so as to keep going on progressing. Unlike the classical liberalism which believed in the existence of a “natural order”, and unlike his contemporaries who wanted to use natural sciences method to study the social phenomena, Hayek displayed a new conception about society and its economy. In his vision, the market economy is a self-regulating mechanism. It relies on the private property and on the economic action of the free individuals within the process of competition. This is why he was fighting fiercely the supporters of the social planning who wanted to “rationalise” the economic life. The centralised economic planning, which replaces competition – this is the basic problem with which he doesn’t agree and about whose dangers he warns. The rejection of planning doesn’t necessarily mean the dogmatic acceptance of the „laissez-faire” principle or of the invisible hand principle, which reject the private monopoly and the governmental interference in any kind of economy because it manipulates the price, thus affecting its functions of regulation.

According to the liberals, the efficient competition was the best way to guide the individual efforts and a properly designed legal

framework can be only beneficial for the competition. According to Hayek, competition is “the only method by which human activities can adapt to each other without the coercive or arbitrary intervention of the authorities”. Regarding the role of the state of right, Hayek supports an active state, within limits, areas and forms strictly determined by law, a state that may ensure public services that cannot be provided using the normal market processes. His conception is thus different from that of the old liberals who were stressing on the passive role of the state and from the planners that were assigning a decisive role to the state. Hence, the question which became creed of many reasonable people, contemporary to Hayek, if it is possible to find a “middle way”, to mix the “atomizing” competition with the centralized direction.

To this question, and to the second one, whether the “middle way” is a toad towards serfdom, Hayek doesn’t provide a detailed answer because he was rather concerned with the dangers of the collectivist economy.

Convinced advocate of individualism, Hayek considers that the researchers of society must focus on the active individual, hence, in his book, he brings arguments to the incompatibility between individualism and collectivism, as well as the incompatibility between socialist planning and democracy. Freedom of the individual is the supreme value for Hayek, more important than the economic prosperity. But freedom of the individual to follow his/her purposes, including to make economic transactions with other people, must not be understood as an abuse of power, as doing anything while bothering the other people around. People can enjoy this liberty only if liberalism is not discarded. Democracy is understood in its essence as a means, a utilitarian mechanism to save the domestic peace and the freedom of the individual. Planning, the guidance of the economic activity presumes just supressing this liberty.

Hayek’s message regarding economic planning is a double one. A first aspect of the message regards the fact that the planning of an economic system in all its details is impossible to be done by a single individual or group. Any individual can only comprehend with his vision a limited area of the people’s needs, and the fact that he/she can be egotist or altruist is of minor importance. People’s needs, in their wide variety, must have a ranking, a full order so that the planner

can select and chose. Thus, all human values must have their proper place, using a complete code, and this code doesn't exist. Therefore, according to Hayek, the attempts to satisfy individuals' requests with the aid of the state lead to failure from the beginning.

The second side of the message refers to the consequences of engaging democracy on the road to planning. Mainly, this means that for the adoption of a system of directed economy, the people must agree on the mechanisms to be used and on the purpose of planning. Only that people agreed with the adoption of a system of directed economy, but they were convinced that this will lead to prosperity. Actually, this agreement is marked by the fact that the object of planning is described vaguely by formulas such as "common welfare" or "general welfare". But the welfare of all the people in a country, or the happiness of just one person depend on a lot of things or, as the author says, "they cannot be weighed on a single scale". Therefore, the effect of democracy engaging on the path of planning in the absence of an agreement on the purposes is a failure from the beginning.

The author goes even further in arguing the incompatibility between planning and democracy showing that even if there is a clear mandate from the people, a unanimous will, this doesn't mean that the people or its representatives (included in democratic meetings) are able to reach a comprehensive agreement on a specific plan. Thus, concludes Hayek, they will end by saying that the parliaments are inefficient or that the democratic gatherings are unable to materialise the clear mandate of the people. All these failures are seen only in the "contradictions inherent to the assigned mission", in the fact that the system of the majority decision is not adequate to solve such task, that one cannot gather majority opinion on any issue. An economic plan must have a unitary conception, it must be coherent and so there not be separate votes for each problem of that plan. Even if a democracy would succeed to develop separate plans for each sector of the economic life, it would still have to integrate these plans because, as Hayek put it, more separate plans might do more harm than no plan at all. On the basis of a consensus regarding planning and the impotence of democratic gatherings to produce a plan, one reaches a special stage, the typical stage of establishment of an economic dictator who will be able to act supported even by



those who detested him in the beginning. The example of Hitler is significant; he took advantage of the decay of democracy and he made it to the top.

In order to be successful, a consensus on planning requires narrowing the individual options, which is not at all compatible with the type of personal liberty characteristic to the modern Western liberalism. But the civil liberties are closely connected to the economic ones. According to Hayek, the supremacy of the right, predominance of the known law to the detriment of the influence of the abusive power, thus to the detriment of an expanded discretionary authority of the state structures, is the only way of protecting the political liberties of the people. It must be acknowledged and observed by all people, legal or natural persons, public or private. In the case of the implementation of a comprehensive economic plan, where the state should get involved in the minutest aspects of everyday life, demanding power to this purpose, the supremacy of the right is the only hindrance to the state planning. The erosion of the supremacy of right in the economic life goes hand in hand with the erosion of the individual freedom. Hayek saw clearly this in 1944 England, namely the same phenomenon that had occurred in Russia and Germany some 30-40 year before happening in England at that time. Because of this, Hayek was warning the world to take measures in full awareness to preserve the liberal tradition, which observed the individual rights. He rejects the thesis that socialist planning would be "unavoidable" in the complex world of England of those years, and he continues with arguments why planning is closely linked to totalitarianism. The fact that a directed economy must be led according to dictatorial criteria is unanimously recognised by most supporters of planning, European or not (such as Stuart Chase, well-known American supporter of planning). All these supporters were trying to convince the people that this authoritarian leadership will only apply to the economic problems, an area considered of secondary importance. Hayek shows, however, that economic planning will not affect just the marginal needs, but will allow the individuals to decide what is marginal. The planner will direct the allocation of the limited available resources to accomplish the desires of all people; therefore he will have to decide what purposes will be accomplished and what purposes will have to be discarded. In a

word, the economic planning means directing most of people's life, both as producers and consumers. Hayek also shows that the promise of the supporters of planning that each person can select an occupation is a utopia. Then, the economic liberty cannot be separated for too long from the political one.

By promising to meet collectively the needs of the people, the socialists only paved the way to totalitarianism because, could we speak of liberty when people have to enjoy some things in a prescribed form and at a pre-set moment? The answer is just one. No.

The problem of the economic life planning, in its whole, makes the ranking of different individuals and groups a political problem, and a very important one. Borrowing from Lenin the well-known expression "Who, Whom" ("Complete works"), Hayek shows, in the chapter with the same title, that in directing the economic activity the state will have to use its power in order to accomplish someone's ideal of justice and distribution, because socialism promised just a fair and equitable distribution of the incomes, and no more.

Hayek shows the same knowledge and clarity when he proved how liberty is sacrificed on the altar of security. He starts his demonstration by clarifying the term of economic security, term as vague as any other economic term (such as socialism, economic planning etc.). A limited security can be achieved for all people, representing the security against any serious material lack or, in other words, the certitude of a minimal level of subsistence. Besides the limited security, there also is the absolute security which, in a free society cannot be accomplished for everybody. It represents the relative position which a person or group of persons enjoy compared to the others. This distinction is not accidental; it coincides with the distinction between the security that can be provided for all people, additionally outside the action of the market economy and the security that can be provided just for a fraction (group of people) and only by dismantling the market. Of the numerous details presented by the author it is worth mentioning the unemployment, crucial problem of that time and not only. Hayek admits that solving this problem calls for planning, but not that planning that would replace the market and undermine the individual liberty. This unwanted planning leads to a

particular security which is meant to protect particular individuals, undeserving, when their income decrease.

While not presenting here all the important ideas of the “Road to serfdom”, we still have to mention one more. This is the even greater danger that may arise from planning “at the international level”, as some of Hayek’s contemporaries were envisaging.

The “Road to serfdom” remains one of the most significant works of political thought of the 20<sup>th</sup> century; it served to waken and warn many intellectuals on the hard consequences of well-intended collectivist measures.

### **3. Romania and its return from the „Road towards serfdom”**

There is no mistake in saying that the movement of ideas from the interbellum Romanian economic thinking was characterised by maturation and diversification. There were three main currents: the liberal current renewed under the name of neoliberalism, the peasantry current and the socialist elements of the economic thinking.

The liberal economic thinking from the interbellum period assumed elements both from the previous Romanian liberalism and from the universal liberalism. Thus, the Romanian interbellum liberalism expressed, as defining elements, among other, the idea of the modern private property on the basis of the free initiative of the economic agents and of their full liberty of movement, the idea of industrializing Romania and its protection from the ruining foreign competition, the idea of priority given to the interests of the Romanian entrepreneurs versus the interests of the foreign entrepreneurs (in other words it expressed the interests of the great industrial and financial autochthonous bourgeoisie). Like in the case of the universal liberalism, in Romania too, the liberal economic doctrine had to respond to the great events, to submit to the criticism of the younger generations of liberals and to enrich, ultimately, with innovations, the most important of which being the stronger role of the state in supporting the process of industrialization of the country. The new economic doctrine was the neoliberalism, which brought some innovations in the social problems (unemployment, pauperization and income imbalance were very strong at that time because of the adverse effects of the contemporary market economy).

During the same period, the peasantry current was also active in the Romanian economic thinking, plus three other currents of ideas

which included the communist, socialist and social-democratic thinking, whose common feature was the Marxist idea of class struggle.

These current principles of economic thinking from interbellum Romania, besides the common elements of the thinkers, have also been engaged in solving some complex problems of economic history and economic policy and often, the opinions of the different thinkers were controversial. Thus, the doctrinaire controversies referred to the way of governing and administrating the country, the genesis and evolution of the modern market economy in Romania, the role of bourgeoisie in the modern Romanian history, the nature and particularities of the Romanian economy from the interbellum period, the perspectives of Romania, etc. This shows that different currents of ideas existed, diversified and matured in interbellum Romania, like in other countries. There was a continuation of the ideas, a continuation of the modern development which started in Romania in the 19<sup>th</sup> century, to which new elements add, elements which came from two main directions: change of the relations of power between the social groups engaged in the real life (political parties, social classes etc.) and the international events. Regarding the latter, we may remind the world economic crisis of 1929-1933, the expansion of totalitarianism, the preparation and start of the Second World War, the immixture of external factors in the policy of the small and medium countries.

This very brief draft of the economic thinking in interbellum Romania aims to show the situation in Romania up to World War Two, which was about to change for a long period the destiny of our country.

As the history shows, the events from Bucharest on August 23<sup>rd</sup> 1944, and the declaration of the Romanian Government from the same day stated that Romania left the war led by the Tripartite Pact, cessing of hostilities against the Soviet Union and joining of forces with the Allied Powers. This materialised in signing of the Armistice Convention between the Government of Romania and the governments of the United Nations. Signed in Moscow in September 1944, this Convention ascribes to Romania the statute of defeated country, which politically meant that it entered under the influence of the Soviet communist occupation. Thus, strictly exogenous

motivations were the reason of socialism installation in Romania, the Romanian people being compelled to accept this ideology of occupation.

The disturbances which caused the fall of communism and implosion of the former USSR, radically changed the economic map of the Central and Eastern Europe. For our country, the events from late 1989 were the starting point for great changes at all levels of the society. This year is seen as the starting moment of the reverse direction of "Hayek's road", the return from serfdom. Next to the other countries which detached from the former communist block, Romania may bring the clearest evidence that the failure of the excessively centralised economic planning is a very good argument in favour of economic and political freedom. In over four decades of totalitarianism, with no political freedom, there could be no economic freedom. It is what Hayek said in his "Road towards serfdom" that the two liberties are inseparable. Of course, other arguments in favour of liberty added to the arguments which Hayek brought in 1940-1943, so that finally, the pledge for comprehensive economic planning has been demolished. Presently, due to the contribution of famous professors and economists, we may understand better the functioning of the markets or of the state (The members of the "Virginia School" headed by J. Buchanan had a major contribution in this understanding).

Before embarking on the "reversed road of Hayek", I would like to show, facts revealed by reputed professors and economists, that according to the official statistics, the year 1989 found the Romanian economy with serious problems, but not at "zero level". This is an economy that could have lead successfully on a new path towards the efficient integration within the world economy. Furthermore, the inexistence of foreign debt and the existence of own availabilities of almost \$2 billion, provided the possibility that under conditions of ability and responsibility, the economic re-technologization could have started, followed by the real improvement of the standard of life of the population. We needed a coherent program o reform which to accomplished in order and with efficiency the necessary changes in the system. Only that the changes after 1989 were mostly political in Romania, so that the place of the communist dictatorship was swiftly taken by the pluralist democracy. The fight for power starts and the

national production fails to receive the proper attention. The warning launched by reputed scientists, professors and economists regarding the danger of economic disorganisation and crash was not received. Hence, rightfully, the road of return from totalitarianism, from centralised, dictatorial power, is scattered with a multitude of questions, one of which turned obsessive: towards what kind of society are we heading? The response that we are heading for market economy passing through a process of transition is not satisfying. This is a vague, very general formulation, given the historical diversity of market economies worldwide.

The priority of the democratic political transformations, the emergence of the pluralist democracy, which absorbed most of the energy, determined a diversity of opinions on what would suit better the Romanian economic realities during transition.

Thus, arguments were in favour of a market economy with social orientation, because it would not yield contradictions regarding the relations of property, while ensuring a high level of social protection. Social protection, however, requires huge financial resources and the social economy can function only within the limits of the capitalist society, being a superior form of capitalism. It presumes a high level of economic efficiency and a proper legal framework. Such an economy developed up to now only in those countries which reached a high level of productivity and high GDP per capita. Given these features of the social economy and knowing that since 1989 to the present moment Romania didn't turn yet a country with capitalist economy, with no proper fiscal instruments and proper legal framework for social economy, with no other necessary conditions, it is hard to believe that such an economy would be suitable now. Our country first needs to have a capitalist economy in order to hope, later on, for a social economy, needs a structural adjustment.

Another option emerged too, after 1989, that the only chance of the Romanian economy to be efficient is the Romanian neoliberalism, which should start from the theory of the liberalism and neoliberalism while taking into consideration the particularities of the Romanian economic environment and while not leaving aside the role of the state in the economy, the monopolist character of the national economy and the accomplishment of equilibrium while the production factors are underused. The Romanian neoliberalism was necessary

from the very beginning of the transition because it put the efficiency criterion to the forefront, the only means to stop state interventionism (the state must reduce its economic role and accentuate its central and local administrative role), it could hasten the pace and depth of efficient privatization, it could create market mechanisms etc. It was also possible because it was not incompatible with the institutional system and the legal framework. Adding to these was the international environment, the association of Romania to the European communities, which forced the adaptation of a particular democratic standard.

Other “voices” showed that Romania must not be directed towards that form of capitalism which existed before World War Two, because it generated contradictions, irreconcilable social tensions and it may ensure the economic-social future of the country. We must not ignore the fact that the great Romanian economists of the interbellum period, peasantry, liberals or whatever, focused on the national interest. This idea should be continued in our time by the higher economic school.

The return to centralised management was not desired by the population and would have no perspective. Given the historical experience of the Romanian people and the contemporary movement of the world economy, it results that the only way Romania may go is towards the mixed, social-humanist, market economy. Only this way, and only in such kind of society, where the private property coexists with the public property, we may speak of full democracy. In a democratic world the individual liberty, which was Hayek’s main concern, demands a free society. Likewise, the freedom of a society presumes a free individual.

Since we are now witnessing the increase of international economic interdependencies, the expansion of globalization of many problems, we must not forget Hayek’s warning that the “problems raised by a conscious direction of the economic life at the national scale will unavoidably amplify when the same thing is tried at the international level” (*op cit.*, p. 244).

We must not also forget what N. Titulescu said when Hitler’s Germany, invoking the interdependencies, was denying the independence of many states: “the interdependency presumes the

independency of the parts. Where the independence disappears, only the dependence remains”

In his paper „Un projet ouvert”, academician Professor Tudorel Postolache showed that Romania must take into consideration three types of simultaneous transitions. “First, our transition from the order economy to market economy and dictatorship of the state of right is simultaneous with another transition, broader, of the western countries towards another type of economy based on a high economic, cultural and information level and towards another type of society, the information society. Second, the current world economic dynamics present two types of stages: one given by conjuncture and the other structural, long-term, maybe for the next two decades. Finally, the third simultaneity concerns the fact that our preparation, as well as the preparation other candidate countries to join the European Union, is simultaneous with the preparation of the EU countries and by the EU to define the new profile of tomorrow’s Europe”.

Presently, under the conditions of globalization, of the global economic and financial crisis and of other crises, the questions raised after the 1989 revolution remain, and I would like to remember just one of them: on what road is Romania heading now?

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## DOCUMENTARY: HYPOSTASES OF THE SUSTAINABLE DEVELOPMENT

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### Abstract

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### 1. General framework

Lately, the notion of sustainable development is frequently used revealing complexity and multiple hypostases of manifestation. Therefore, before actually presenting this subject we need to describe the concept itself both in its strictly limited, acceptable meaning, and in a broader meaning. Following are some defining particularities of the concept from the positive competition and pluralist democracy points of view.

History shows us that sustainable development is not something new. Problems related to this concept have their roots embedded in the Christian origin dimension of the human being – *creatio ex nihilo*. At the same time, it is noteworthy that the archaeological discoveries prove the existence of concerns for sustainable development as far back as in antiquity. They are traceable in all ancient people such as the Sumerians, Maya or the Mediterranean people. The ancient world transmitted us the first ideas regarding the relations between the growth of the population and the economic growth on the one hand, and the biunivocal interdependencies between the use of resources and the sustainable functioning of the ecosystems, on the other hand.

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From this angle, it is very possible that the sustainable development is closely related to the continuous inheritance of the experience regarding the relations between the natural and the artificial, socio-economic environment, in which people manifest through action and aspirations (Oliphant, 1999). For instance, the famous words of Stefan the Great in the theatre show "Sunset" by Barbu tef nescu Delavrancea are emblematic for us, Romanians: „Moldova is not mine, nor yours; it belongs to the heirs of your heirs to the end of time”.

The historic legacy was a bridge over time, a source of inspiration for the researchers of our days. For instance, the well-known US researcher Alvin Toffler, in his book "The Third Wave" considers that mankind experienced transformations marked by so-called "waves" (Toffler, 1980). The first wave was the agrarian revolution – the period of transition towards an organised manner of using the agricultural land, when the first peasants and the first traders appeared alongside with the first market-towns. The second wave – the industrial revolution symbolized by Watt's machine – appeared after prolonged efforts and "anthropocentric-Renaissance" sought, and after geographical discoveries, entailing a higher flow of resources from the colony-countries towards the western countries, the appearance of the first industrial funnels, of the first town workers, when the villagers migrated towards towns.

At that time, as mentioned by Bela Csikos-Nagy and Peter Elek, pollution was a *sine qua non* condition of development; the people considered that the nature which God created has own means for self-regulation and renewal. All these aspects are joined symbolically in the so-called *Situatione Dei* stipulation from the Roman Right Code, subsequently reviewed in the Napoleonic Code (Csikos-Nagy i Elek, 1995).

Presently, the reality shows the impact of the third wave figured by Toffler: the IT revolution of knowledge. The explosion of IT networks, of the "ecologically friendly" standardized technologies and biotechnologies remind us of the enthusiasm and effervescence of the second wave.

However, as Ruth Hillary and Johan Thorensen show, next to the technological aspects we must not overlook the managerial and social aspects (Hillary, 1997; Thorensen, 1998). Within the context of transition towards the society needing to save resources and to

valorise the human capital, the integrated management of the natural resources and of the development of the productive, managerial qualities becomes necessary, being achievable by the cooperation between the managers, shareholders and employees.

## **2. Possibilities to approach sustainable development – concept, patterns, indicators**

The best known definition of the sustainable development is that given by the Brundtland Report in the 1980 years under UN aegis within the debates on environmental and human development issues: sustainable development is meeting the necessities of the current generations while not compromising the capacity of the future generations to meet own needs.

However, the concept of sustainable development cannot be framed within a precise context because of its many dimensions and significances that are equivalent – one might say that there is no single, universal definition. Thus, the concept of sustainable development displays several apparently contradictory elements referring to the:

- Economic growth compared vs. the limits of the economic growth;
- Individual interests vs. collective interests;
- Intergeneration equity vs. intrageneration equity;
- Adaptability and elasticity vs. routine.

Nevertheless, these contradictions are part of a complex process that hosts the sustainability – development binomial: on the one hand sustainability which refers to the necessity to set a rational optimum for the use of scarce resources paying attention to the issues of social justice and equity and, on the other hand, development which presumes continuous and sustained economic growth ignoring the limited character of the natural resources.

When these concepts are joined they form a totally new antinomic, concept which means much more than the mere merging of the two concepts, showing its economic, social and ecological aspects.

Ecologically, the sustainable development is easier to understand because it refers both to the procedures to measure the physical and biological processes and to finding the possibilities to measure the continuous functioning of the ecosystems.

The economic definitions, too, refer to the conceptions that highlight the limits of the economic growth and the rare or limited character of the natural resources, as well as to the opinions that consider that these limits do not exist essentially within the so-called stock versus flow syntagm, free goods or non-free goods.

At the same time, sustainable development also reveals a social dimension: although the limits of the biosphere and geosphere resources are not accurately known, the suggestion is that the limits of Earth's sustainability are inherently related to the approach of the social gaps confronting the people not just in terms of the strictly material meaning of wealth and poverty, but also in terms of egotism and possibilities of opening towards a true human solidarity. Thus, for the people, social sustainability appears much more urgent than the ecologic sustainability.

Within this context we must mention the human aspect of the sustainable development, which refers to the political and institutional framework of the society, remembering of the importance of the social interdependencies between the private goods and the public goods afferent to the triad **objectives – restrictions – options**, circumscribed to the political institutional strategic theory and practice.

In other words, given the complexity of the interdependencies within the natural environment, the option for sustainable development doesn't mean simply finding the means for somatic biological survival; it also involves exo-somatic qualitative aspects by the continuous aspiration towards solidarity and Christian kindness – the true element which gives a true meaning to the sustainability of the biosphere components, even to those that apparently have no benefit for the mankind.

Therefore, the continuous development of the planet, sustainable or not, will anyhow involve the transformation and interaction of the resources and people within an economic, social, politic, cultural and educational framework, which displays difficulties of approaching. The "ecologic" goods play an essential role within the process of knowledge and evaluation of the particularities and significance of the public and private economic goods.

Relations of interdependency between economy and ecology, between the economic and "ecologic" goods can be set by taking into consideration the particularities of the economic goods integrated into

the particularities of the economic variables of the consumption and production and of the ecologic variables known so far (of the material flows – energy and factors of energy reconversion).

One may notice, within this context, an interesting theoretical statement based on the principle of energy conservation – nothing is lost, everything is transformed. In other words, the human society doesn't produce and actually consume the goods: it keeps bestowing them different significances from the perspective of a true utility.

The economic, ecologic and social aspects of the sustainable development reveal the possibility of a practical representation of the sustainable development both in one dimension, economic, circumscribed to the indicator of the sustainable economic welfare (ISEW), as well as in multiple dimensions, socio-cultural, using myths (patterns) imagined by so-called ecologists and cultural anthropologists who tried in their way to express the relations of interdependencies existing between man and the environment.

***a. Sustainable development in terms of the Indicator of the Sustainable Economic Welfare (ISEW)***

Starting from the studies of A.C. Pigou (Pigou, 1932) one may integrate organically the economic, social and ecologic information within the national accounts system and within the GDP indicator of the sustainable economic welfare. Researchers such as Herman Daly and John Cobb (Daly and Cobb, 1989) developed the basic methodological model of such indicator - the Index of Sustainable Economic Welfare.

Essentially, they suggest that besides the well-known material welfare, identifiable using the system of the national accounts, we may also take into considerations other aspects such as:

- That production which is not relevant for the market;
- That production that is not intended for consumption, but which is necessary in order to compensate for the damages generated by the economic system itself (the so-called "defensive costs");
- The potentially identifiable welfare in the nature of the present production and consumption;
- The efforts of the public sector and of the households to achieve the potential welfare (in relation with the duration and intensity of work).

The methodology for the calculation of the indicator of the sustainable economic welfare runs along three stages:

- First, one calculates the basic consumption, which refers to all that was consumed under the given conditions of production, determined by the “market forces”, as shown in the system of the national accounts. However, we may also take into consideration other aspects too, derived from the change of the private consumption structure and of the investments. The changes in these two items are deemed necessary in order to determine the information regarding the state of the economic welfare under the conditions of the autonomous character of the household activity.

- Second, the so-called deductible items must be calculated. They refer either to the economic activities which do not actually generate economic welfare but which are necessary for the maintenance of the welfare standard (defensive costs), or to the evaluation of statistical prognoses of the present production and consumption. The first group of activities includes the defensive ecological costs as well as the “social” costs, which show accounting difficulties; for the second group the calculation takes into consideration only those potential costs pertaining to the greenhouse gas effects or to the progressive depletion of the resources. The difference between the basic consumption and the deductible items generates a partial result called the gross indicator of the sustainable economic welfare (gross ISEW).

- Last, but not least, this result is weighted with an index of income inequality, either as the Gini coefficient, or as the Atkinson index, which produces the potential ISEW.

The critiques appear automatically.

At first sight, it may seem that ISEW would measure the sustainable economic and social welfare given the present socio-professional structure of the society and the state of the economic progress. Actually, it tries to measure both the production determined by the market, and the non-relevant production of the market, failing to take into consideration the premises mentioned in the beginning of ISEW analysis. Therefore, we may not speak of the sustainable economic welfare, but of an approximative estimation since there is no single way of measuring the economic welfare, this being one of the many possible variants. From this perspective, the incorporation of the “green” accountancy within the system of the national accounts might change the classical GDP into an ecologically-adjusted GDP.

Thus, the measurement of the sustainable development using ISEW method may be regarded as being prospective

***b. Sustainable development from the socio-cultural anthropological perspective***

The myth or the imagined model looks like a perception of a system formed of the elements of the surrounding economic and physical reality, on the one hand, and of the imagined ideal, on the other hand.

C.S. Holling, Peter Timmerman, Michael Thompson, and Steve Rayner are among the specialists concerned by the aspects circumscribed to the matter-concern binomial. They revealed the necessity of considering the cultural factors too, next to the economic and ecological factors (see Clark and Munn, 1986).

When analysing such ecological patterns of cultural inspiration, one must take into account that they actually and potentially generate a specific relativism in knowledge by the fact that the ideas about the sustainable development may be placed within different hypostases and configurations, limited, nonetheless. Thus, there are at least four possible situations, each pattern relying on specific hypotheses and imperatives regarding the approach of the ecological problems confronting the human society. Because each pattern deals with just one side of the surrounding world, a drop into the ocean, they should be accepted as being perfectible; they cannot be considered as the single point of view.

***1. The individualist pattern***

The first pattern claims that the nature is robust and that the economic system is merciful regarding the impact of anthropic action because nature is presumed to have enough resources.

Graphically, this pattern is represented by a sphere that is moving within a pool with two sides which actually reflect the fact that irrespective of the changes affecting the environment, it will always return to the bottom of the pool.

In this very accessible form the pattern approaches the subject of the global ecological changes supposing that the green technology is the only one that will prevent, correct and restore the social and ecological balances.

This is the individualist-autonomous point of view about the world; the invisible hand is the only regulating drive for this system.

This point of view is supported largely by companies and industrial branched adept of the ecologic-industrial transformation, being considered by experts such as James W. Dudley, as “leading branches of the values”, suggesting the idea of a plan of disseminating the “green” technologies via the market drive mechanisms. Thus, the institutions designed to manage the global ecological transformation promote market efficiency and environmental protection through the economic policy of *laissez-faire*.

### **2. The egalitarian pattern**

The second pattern is totally opposed to the first pattern: nature is very frail, vulnerable to an irreversible collapse because of the ecological degradation or exploitation of the natural resources.

Graphically, this pattern is represented by a sphere in an unstable balance over the convex pool.

At this state, the pattern illustrates the ecological transformation as manifestation of the multiple environmental effects of the human activity.

The continuous development within a materialist conception is presumed to lead, ultimately, to the irreversible destruction of the planet. This point of view is essentially egalitarian and is supported by the ecologist movement, which claims the need for a radical change of the society. Such conception mitigates either for the return to nature, abandoning the industrial development, or for the development of a universal ecological code of strict moral principles.

The most convinced ecologists suggest a radical transformation based on the revaluation of the economic, political and social interdependencies and building harmony between man and the environment. As Eduard Goldsmith, founder of „The Ecologist”, says, ecology is the only support preventing a failure that would doom the world.

### **3. The hierarchical pattern**

Within this acceptance, nature is considered robust, but within particular limits.

Graphically, this pattern is represented by a sphere which is rather stable in its central point, but the sides of the depression do not exclude that the sphere runs towards either side.

This point of view has a hierarchic-administrative significance, meaning that the ecological degradation and the use of natural



resources must be surveyed, administered by an institutional body. An ecological disaster may be avoided by an adequate scientific understanding of the ecological limits and using standard operational procedures. This view is widely spread in many countries and it aims at a particular bureaucracy that is to administer the process of ecological transformation.

The strategy proposed by the Brundtland Report is such an example, by the ecological transformation that may be managed „top-down” within an institutionalized framework, such as the UN, for instance.

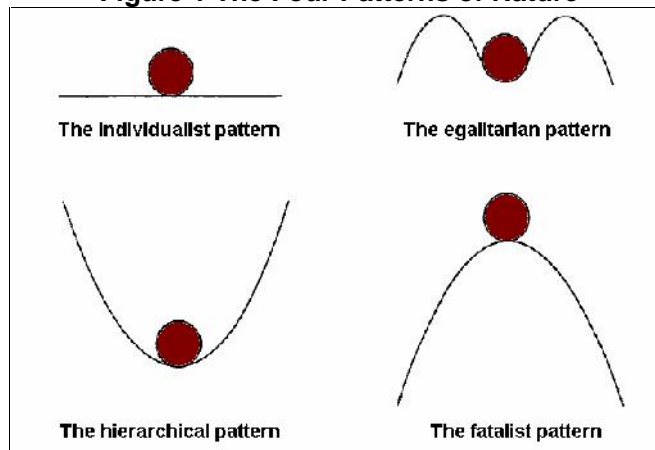
#### 4. *The fatalist pattern*

This pattern considers nature as chaotic, unpredictable, doing as it pleases.

Graphically, this pattern is represented by a sphere which moves in any direction horizontally, with no vertical disturbances, advancing infinitely on the horizontal.

This pattern is essentially fatalist expressing the impossibility of a significant transformation or content transformation, life being led by odds not by work or skill. From obvious reasons, the followers of such opinion do not quite support their opinion because the management strategies are reduced to the survival of the strongest.

**Figure 1 The Four Patterns of Nature**



Source: C.S. Holling, in Clark and Munn (eds.), 1986

If one of the four hypostases would really be complete we might presume that all its opponents would trust that perspective either by testing it experimentally, or by accidental surprise.

However, these points of view show that the analysis of the relation between the society and the environment is particularly complex and invites to meditation and reflexion.

Depending on the conceptions on the perspectives of the environment, the different groups will fundament their own strategy on the sustainable development.

These views may receive both appreciation and criticism. It is important, however, that each of these patterns attempted in its own way to show the importance of being aware of the incertitude regarding the natural resources, the need to implement strategies for resources management and the important impact of the technical progress. Therefore, the topic of the sustainable development is rather difficult and it invites at contemplation, to the good and balanced understanding of the phenomena and processes.

### **3. Romanian contributions to the topic of sustainable development**

The Romanian scientists too were concerned by the sustainable socio-economic development, with influences pertaining to the spirit of the time and to the specific field of activity.

Overall, the most reputed Romanian author is undoubtedly Nicholas Georgescu Roegen with his book "The law of entropy and the economic process" published in Romania too in 1971. Essentially, the author highlights the importance of integrating the economic science with other disciplines (mathematics, physics, biology and philosophy), within the context of approaching the economic and social development as complex process with an irreversible entropic-dynamic character, of considering the impact of the wastes and their incomplete recycling.

From another perspective, and under the influence of different circumstances, the opinion formulated by the economist Mihail Manoilescu (in Dinu, 1993) concerning the delicate issue of the economic development from the angle of making the budget. He highlights the essential aspects of the budget construction starting from two "extreme" acceptations – **budget balance at any cost** and the so-called **golden budget**. The first one shows that the

appreciation of the national currency and the conception of the budget balance at any cost with the purpose to “enhance the leu” were done by a formal balancing of the budget. Irrespective of the budget structure, the monetary construction selected its “victims of sacrifice” among the large mass of the producers, and the budget cut was “selecting” the political clientele of the state servants. A strange understanding of things can be noticed, where the misery of the producers is associated to the misery of the employers in order to achieve the objective of currency appreciation: “misery plus misery equals prosperity!” Such conception proved tragic at that time just because it underestimated the role of the state; the author considered it anti-organic, thus anti-political. The second “extreme” acceptance supports meeting the needs of the state at any cost and recommends paying the employees in gold, at least equally with the pay before World War One, by acknowledging the depreciation of the national currency in relation with the gold. In the opinion of Mihail Manoilescu, the conception of the budget in gold “overestimates the possibilities of the state, whose role is hypertrophic because it legitimates its exigencies independently of the level of energy and force of the national life at a particular moment”. In other words, the first conception of the budget balance at any cost illustrates the image of the begging-state, while the budget-gold formula illustrates the image of the wasting-state. Given their hardly measurable impact on the Romanian society of that time, Manoilescu proposed the so-called **“budget of the maximal effort of the real power of the nation”**.

Unlike the two points of view mentioned above, the new philosophy started from the necessity to appreciate the honest work of the people and to assume the responsibility of the state institutions as depository of a wealth of goods in the form of the cultural heritage of the nation and of the patrimony of the public, social institutions. The state is accountable for the material, patrimonial management within the limit allowed by the pace of the economic life as factor that determines the level of tempering state expenditure.

The essence of this conception highlights the idea that in principle it is only allowed to cover the budget deficit in relation with cashed revenues, while borrowing is not allowed for supporting the governmental administrative body. This imperative doesn't exclude borrowing itself; it only means that the money must be used for productive purposes, public investments, with education and culture

having priority; the public employees must be paid fairly for fair work. From this perspective, the duty to work together with becoming aware of the government's responsibility as manager of the national patrimony of traditions, monuments of human and national resources, may be essential characteristics which actually provide content to the sustainable development. **However, presently, it seems that the real economic substance has been sent to the back worldwide, while the speculation lacking any real economic content appears in the forefront, which leads rather to catastrophe than to development.**

The socio-economic development is not a mere technological process of administration and utilization of the natural physical resources; it is also relevant in the social plan, from the ontic and axiological perspective of the organic integration between the natural and artificial economic, social, cultural and educational environment. As Professor Gheorghe Manolescu highlighted, the natural, physical and human resources "continuously change their form and content within the context of a borderless asymptotic positive economic finality" (Manolescu, 2000).

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## **BANKING RISKS IN A GLOBAL ECONOMY**

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### **Abstract**

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**JEL Classification:**G21, G33, G34

The end of the second Millennium brought a new problem to mankind, that of globalization. In its evolution, the world economy determined a higher interdependence of the economies, the local development of an economy being possible only in direct and diverse contact with international material, informational and financial economic flows.

During recent years, the global economic integration has been accelerated on a multitude of fronts, speed being a characteristic of these times. While trade liberalisation, which started long time ago, still continues, the changes were extreme in the sphere of finances, not seen before. The great banks and financial groups, already gigantic, are caught in a frenzy of mergers. We call it today “mergermania”, the great ones becoming even more powerful.

The fall of communism created an attraction for the emerging markets, with opportunities for large investments, which attracted the private financial capital in the accelerated financing of external imbalances of the developing countries.

The reform from these countries, characterised mainly by price liberalization, monetary stabilization, control of inflation, reduction of the budget deficit and transfer of part of state property into private property

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(privatization) didn't manage to stimulate the "market creation" effect due to the misunderstanding of the concept of intermediation. The effects were divergent and manifested in a hyperbola of prices and with chronicized (2 figures until recently) inflation in some countries, Romania among them. Inflation eroded the savings of the population and slowed the rate of investments in the economies where the value is volatile, which caused higher dependence of the East on the Western financial flows.

Essentially, worldwide, we may say that there is an increase of the global trend to de-save by the "fall of the national saving" both in the developed states and in the developing states.

Within this context, the chances for Romania to learn from this phenomenon depend largely on the establishment of the proper framework allowing the utilization of the benefits brought by globalization and the decrease of its adverse effects.

The influences of globalization are felt by the Romanian banking system too.

The banking activity in Romania is not up to the exigencies and standards of the European banking industry, the Romanian banking market having a small number of operators (Table 1).

**Table 1. Structure of the Romanian credit institutions**

	December 2004	September 2005
Banks with full or majority state capital	2	2
Banks with majority private capital (including the branches of foreign banks), of which:	37	37
- Banks with majority foreign capital, of which:	30	30
- branches of foreign banks	7	6
TOTAL banking system	39	39
CREDITCOOP	1	1

Source: www.bnr.ro

In order to analyse the banking structure specific to the Romanian banking system we need to consider the type of property. Essentially, the structure of property of the banking system is an indicator of quality which reflects the intensity of banking reform and reorganisation, being in direct proportionality with the structure of property in economy.

Thus, at the end of September 2005, the Romanian banking system

consisted of 39 commercial banks, of which 31 with full or mostly private capital, 2 with state capital and 6 branches of foreign banks. The banks (Romanian legal persons) with mostly private capital that operate in Romania hold 73.2% of the social capital and 64.3% of the assets of the Romanian banking system. If we add the branches of the foreign banks, the above figures become 47.6% and 71.7%, respectively. The highest proportion is held by investors from Austria (26.6% of the aggregate capital), Greece (11.4%) and Italy (8.2%) at the end of the first quarter 2005.

The process of privatizing the banks with majority state capital experienced an important moment in December 2005, when the Romanian Commercial Bank (BCR) was privatized, the largest bank with state capital. The first two attempts of privatization had failed mainly due to the unfavourable international environment. The winner was Erste Bank, which will pay 3.75 billion Eur for 61.88% of BCR shares.

Thus, with the privatization of BCR, the evolution of the Romanian banking system will be determined by foreign capital, by its interests and by the way in which the foreign banks will direct their crediting policy, shifting the weight from crediting the Romanian state (safe debtor) towards the real economy.

The privatization of the Romanian Commercial Bank (BCR) and the House of Savings and Bonds (CEC) set for 2006 will increase the proportion of banking assets held by foreign investors to 90%, one of the highest in Europe, as shown by Fitch analyses. The perspectives of the Romanian banks are positive because of the improved situation of the market boosted by the economic growth and by the experience of the foreign shareholders. For the time being, the foreign investors control 64.3% of the banking sector assets. Thus, the effects of the banking internationalization on the Romanian banking system are visible particularly as participation in the social capital of the commercial banks, Romanian legal persons, or by the initial capital, in the case of the branches of foreign banks.

Comparing the structure of property in economy with that from banking, we may notice that the banking system is private to a larger degree than the Romanian economy in general.

The banking internationalization overlapped in Romania the process of financial reorganisation of the banks and was reflected particularly in quantitative terms by the number of foreign banking operators and by the



volume of their assets. The qualitative side of the phenomenon will be emphasized during the coming years, by the emergence and development of new banking products and services both for the retail and for the corporate segments and by the specialisation of particular banks or by the establishment of specialised banks (saving facilities for housing).

In terms of the level of capitalization of the banking system we may notice the consolidation of the position held by banks with foreign capital.

Although the number of the banking institutions increased seven times since 1991 to the present time, the Romanian banking system is still rather concentrated (Table 2).

**Table 2. Level of concentration of the banking system in Romania (top 5 banks)**

<b>March 2005</b>			
<b>Assets</b>	<b>577160.3</b>	<b>15673.1</b>	<b>59.1</b>
<b>Credits</b>	254985.6	6924.3	59.4
<b>State bonds</b>	3991.0	108.4	43.1
<b>Deposits</b>	396662.4	10771.6	56.8
<b>Own capital</b>	74189.3	2014.6	61.4

Source: www.bnr.ro

In March 2005, the Romanian banking market was dominated by five banks: Romanian Commercial Bank, Romanian Development Bank, Raiffeisen, HVB and CEC, *which hold together 59.1% of the total assets of the banking sector.*

According to the data presented by the Financial Market, the market share of BCR increased much mainly due to the mortgage credits; BRD and CEC displayed a descending trend of their market share, while Raiffeisen Bank, Eximbank, Unicredit Romania and Finansbank Romania increased their market share. The reduction of banking concentration is another effect of the internalization of the banking capital in Romania.

Business internalization, as specific form of the global economy, and of the banking intermediation, engages considerable financial, human and material resources; the banks will have activity on the foreign markets only if they estimate sufficiently significant profits to cover the risks they take.

Under the conditions of internationalized business and banking credits, the banks seen from the perspective of business are submitted to the international risk, and when they are not involved in purchases or mergers with other entities, the financial risks tend to aggregate, particularly during the first stage of the processes.

In its extreme form, the credit risk, which amplifies in the case of international credits, causes losses to the financing bank due to the debtor bankruptcy and the loss is permanent in this case. The external disturbing factors specific to the credit agreement, which make the people break their promise, is the policy of that organisation which we call State, which tends to intervene into the free relation of the sides, acting in reverse direction of the "invisible hand" principle. A characteristic example of the Romanian transition is the anti-inflationist monetary policy adopted by the central bank, state entity which sets the increase of the minimal compulsory reserve, globally motivated by the necessity to inhibit credits by blocking a part of the financial resources of the banking society at the central bank. Thus, that particular bank can only use (a lower) part of its total resources that it has drawn in deposits, which decreases the number and volume of transactions (credit contracts) concluded by the financier and which determines it to grant just short-term credits. At the same time it pays a passive interest calculated at the total level of the financial resources drawn from its clients which, compared to the interest given by the central bank for the established reserve, can only make the loans more expensive. Thus the cost of the anti-inflationist operation of the state is thrown on the debtor, not by will of the lender, but by will of the state to stabilise inflation and do a social good.

The global credit risk is the risk that expresses the probability of deterioration of the banking assets engaged for credits. The global risk of insolvency is an increasing unctio of the mass of credits, of the interest rate and of the national economic medium. Furthermore, as the volume of credits increases, the cases of insolvency multiply fast, expression of the fact that the increased volume o credits brings an increasing number of potentially insolvable persons. The increase of the interest rate due to economy overheating is another factor which amplifies the global insolvency.

During the past decade, under the incidence of large scale economic, political, social and financial phenomena, the problem of credit risk displays new trends, as follows:

1. Unprecedented expansion of the credit, revealing, on the one hand, business internationalization and, on the other hand, the increasing deficit of resources and on the necessities of crediting for the large transnational companies.

2. Enormous development of the varieties of banking intermediation, materialized in the diversity and novelty of the banking products and services offered to the customers, which increased the risk of crediting, thing that may catch the economy of any country in unprecedented situations with long-term adverse consequences.

Within this context, the merger of banking companies came as a modern method to manage the global risk of crediting, both within each individual country, and worldwide. The new banking entity resulting from the merger has a consolidated capital that covers better the losses caused by the risk of credits. The merging process is a general characteristic of the modern economies and it can be observed in all economic branches, but mostly in the financial area.

Globalization and internationalization of the banking credit meant on the credit market:

- Diversification of the “credit” products both for the corporate segment, or the households and for the state;
- Development of transactions by means of IT technologies and networks;
- Lower price of the credits (in parallel with lower margins), process visible in the EU member countries, influenced both by the rate of domestic saving, specific for each country, and by inflation, fiscal policy and monetary policy of the particular countries;
- Development of the consumption credit and of the mortgage credits;
- Higher elasticity of the demand for “credit” products.

Of course, Romania might benefit mainly from the positive effects of globalization, but for a functionally open economy and with frail structures, the emergence of risks is very high.

Given the fact that in Romania the credits for the private sector are rather low (35.4% of the non-governmental credit), much less than in other EU member countries (where these credits may exceed 100% of the GDP) and then in Central Europe countries, we may witness a new episode of fast expansion of the credit, similar to that from 2002-2003. The fast expansion of the credit might trigger the spectacular increase of

assets price (“asset bubble”) and economic overheating.

The fast increase of credit may be due to multiple causes, such as:

- **Increased financial intermediation** – the faster increase of the credit compared to the GDP, as the economy grows, such as it is the case of Romania;
- **Normal cyclic movements** – that accompany the period of economic revival, when the credit grows faster than the GDP, (because the requirements of the companies or investments and circulating capital fluctuate depending on the economic cycles);
- **Excessive cyclic movements (*credit boom*)** – the excessive expansion of the credit is unsustainable and will end by collapsing. The credit-booms are often associated with banking and currency crises.

These risks might amplify with the adoption of the Euro, which will stimulate the demand, with higher volumes of credits in the Romanian economy. The decrease of the risk premiums will decrease the costs of external financing of the banks, allowing them to finance the fast increase of the credit with external funds. Also, the interest rate evolution, significantly determined by the Euro Zone conditions, might increase the risk for a new credit-boom, while the cyclic and structural influences will keep inflation at a higher rate than the rest of the Euro Zone leading to lower or even negative interest rates.

The reorganization of the banking system in Romania, together with the high risk aversion of the banks after the 1999 crisis, and the stronger surveillance and banking regulation, improved bank performance. Presently, the banks display very good indicators of liquidity and solvency and they seem to be resistant to a large array of shocks and risks (Table 3).

**Table 3. Main indicators of banking prudence**

	<b>September 2005</b>
<b>A. Capital risk</b>	19.3
Solvency rate ( > 12%)	8.4
Rate of own capital (own capital/total assets)	0.3
<b>B. Credit risk</b>	0.2
Overdue and doubtful credits (net value/total credit)	2.1
Rate of credit risk	3.4
General risk rate	47.5
<b>C. Liquidity risk</b>	
Liquidity indicator (actual liquidity/required liquidity)	2.5
<b>D. Profitability</b>	

*Financial Studies - 1/2013*

ROA (net profit/total assets)	2.0
ROE (net profit/own capital)	16.9

Source: www.bnr.ro

Analysing the evolution of the main indicators of prudence, we may notice that the expansion of crediting didn't affect the quality of the credit portfolio, which remained constant. The rate of the credit risk and the general rate of risk increased slightly to 3.4 and 47.5%, respectively. The rate of capital profitability (ROE) and the rate of economic profitability (ROA) were 15.6% (December 2004) and 16.9% (March 2005) for ROE and 2.0% (December 2004) and 2.0% or ROA.

The aggregate solvency indicator at the end of the first quarter 2005 was 19.2%, higher than the set limit of 12%. Significant progress has been achieved in the evolution of the indicators defining the quality of the assets portfolio, the proportion of overdue and doubtful credits within the total volume of credits being of just 0.4% at the end of the first quarter 2005.

However, the evolution of crediting is still hampered by the structural deficiencies of the credit market in Romania, which is common to the economies in transition and because of this the credit still is risky and expensive for the banks (Table 4).

**Table 4. Factor hampering the increase of the volume of credits for the private sector in the transition economies**

Factor	Countries where this factor is relevant (%)
Poor protection of the creditors	87.8
Lack of trust in debtors	50
Finalization of the process of reorganization after periods of crisis or change of the owner	5
Inadequate accounting standards	37.5
Direct external financing	25
Other	37.5

Source: www.bnr.ro

After all these deficiencies are removed, the Romanian banks will probably direct their attention on credits for the private sector. This is very likely, given the high proportion of EU banks capital in Romania, the adoption of the community acquis in terms of banking regulations, the

increasingly tight connections with the interbanking market and with the Euro Zone, as well as the increasing cooperation between the surveillance organisms from Romania and the EU.

Because Romania has a very low level of banking intermediation, it will be important to identify the moment beyond which the increasing banking intermediation may turn into a “credit boom”, with adverse economic effects.

The literature shows that the mere increase of credit proportion within the GDP should not be interpreted as warning for economic overheating. However, two channels of increasing the volume of credits may signal potential expansionist effects in the economy: higher propensity of the banks to give loans because of improved microeconomic factors (privatization, profitability and credit risk) and higher inflow of capital through the banks, which is similar to monetary expansion, which requires the intervention of the central banks on the hard currency market.

In Romania, the emergence of these effects can be favoured by several evolutions: first, the privatization of the state-owned banks which redirected the credits from the state sector towards the private sector; second, the banks will be increasingly tempted to enhance their profitability by giving loans, while they are now investing in safe placement funds whose profitability is limited (state bonds, deposits in the central bank); third, the decrease of the credit risk will prompt the banks to grant new credits while the liberalization of the capital movement will favour the inflow of capitals through banks.

In the hypothesis of a “credit-boom” the authorities must step in using monetary, fiscal and prudential instruments. “Credit ceilings” might be set, compelling the banks that report high increases of the volume of credits to invest part of their resources in instruments remunerated below the market interest rates (case of Greece and Croatia). There also is the possibility of introducing prudential requirements such as the “pro-cyclic” capital requirements, of restrictive rules regarding the collaterals or the imposition of higher provisions or the banks reporting high increases of the volume of credits. Unlike the “credit ceilings”, the prudential instruments do not affect the financial health of the banks.

Within the commitments assumed towards the European Union, Romania pledged to enforce a program for the liberalization of the capital movement, which was largely introduced in 2001-2005. So far, the implementation of the measures to liberalize the capitals was not

confronted by major incidents because Romania didn't attract "destabilizing" foreign capitals in terms of volume or structure.

Although the inflow of foreign capitals is generally a desired factor for Romania, if they display potential to become volatile they may affect the proper functioning of the economy. Romania seems to be particularly vulnerable due to some characteristics. The low level of monetization of the economy and of banking intermediation compared to other countries from Central and Eastern Europe tend to amplify the marginal impact of any additional inflows of capital.

There are serious fears as to the behaviour of the local banks after the liberalization of capitals. Much of the bank assets are invested in state bonds. Capitals liberalization provides the non-residents the possibility of access to the local market of the state bonds. This phenomenon may decrease bank profitability because it will decrease the volume of the available state bonds and will decrease the interest rate for these investments. In this situation it is possible that the banks are tempted to take short-term foreign loans using state bonds as collaterals. The risk of such operation is a mismatch of the maturities.

In the Romanian banking system there is a high probability that other risks appear due to the (increasingly pregnant) presence of the foreign financial institutions on the market. Although the banking sector would benefit from the competition generated by the foreign financial institutions, which will ultimately increase the efficiency and reduce the costs of the financial intermediation, this may entail some risks. The local financial institutions might get entangled in increasingly risky operations willing to preserve their market status. This would deteriorate the financial and prudential situation of these financial intermediaries.

The Romanian survey authorities should have proper access to information from the mother financial institution, supplied under conditions of reciprocity by the survey authorities from the country of origin. Although the presence of information flows between the surveying authorities tend to disadvantage the survey authorities from the host country, this balance will have to equilibrate in the future.

The banks remain the most important financial intermediaries in Romania. The banking system is the most important segment of the Romanian financial system, holding 37.7% of the GDP net assets. The dominance of the banking sector is also proved by the secondary role of the Romanian market of capitals. The summed capitalization of the two

stock exchange units from Romania (the Bucharest Stock Exchange and Rasdaq) amount to just 11% of the GDP, half the rate in the countries recently admitted in the EU. The market concentrates in the sphere of action of 77 intermediaries whose proportion within the total assets of the financial system is of 0.1%. Except for the banking system, the other financial intermediaries have a low proportion of the total financial assets, which shows the underdevelopment of the markets for capital, of the investment or insurance funds.

The Romanian banking system reached financial stability by a large value of the banking concentration. This is mostly a private-owned system dominated by the foreign capitals. Banking concentration is high and the profitability is good, determined by the maintenance of a large general margin, which is characteristic to the type of unstructured economy.

The influences of globalization on the Romanian banking system opened a new stage in the organization and management of the credit and money in the national economy. It transformed the conditions in which the immediate and long-term prosperity of all states is decided.

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## IMPACT OF THE FISCAL POLICIES ON THE STANDARD OF LIVING OF THE EMPLOYEES

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### Abstract

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The concept of “quality of life” includes its most important component, the “standard of living”. Ensuring a decent standard of living depends on the level of society development quantified in the GDP and in the manner of its allocation. The impact of fiscal policy on the standard of living can be best perceived on the occupied population, which is taxed, the employees representing the most relevant category. This is supported by the figures on the proportion of employees within the total occupied population (over 50%) in 2003 amounting to 56.04%. The analysis of the income from wages in 1990 – 2005 yielded the following conclusions:

- In 1992-1994, the real gross average income decreased, while in 1994-1996 it increased. This had no influence on the proportion of wages tax collection, which increased continuously, which increased the fiscal pressure on the work;
- In 1996-2000, the real gross average income decreased dramatically due to the peak inflation of that period, which eroded all earnings;
  - In 2000-2004, the increase resumed, both of the real gross average income, and of the fiscal pressure on it;

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- The lowest fiscal pressure felt by the employees was in 1998 and 1999.

This evolution shows that a fiscal relaxation was attempted in 1998 and 1999, but it was not supported by the available resources, which caused a boom of the fiscal pressure during the subsequent period.

**Keywords:** fiscal policy, net income, gross income, quality of life.

**JEL Classification:** H2

In this analysis we will show what was the impact of the different fiscal policies on the standard of living, the quantitative expression of the quality of life. The analysis will be done according to political cycles since they have a significant impact on the standard of living. Thus:

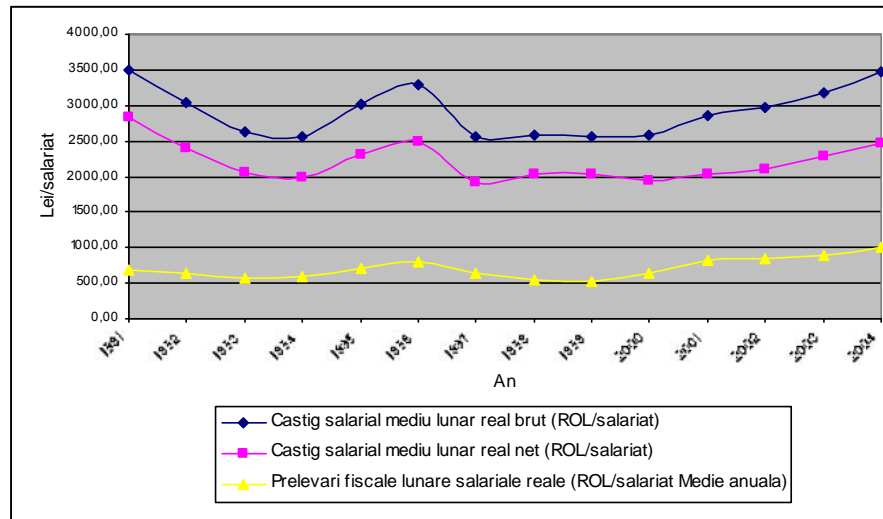
- In 1992-1996 and 2000-2004 Romania had social-democrat governments, with left orientation, whose doctrine was promoting more the social policies, with the state supporting a decent standard of living;

- In 1996-2000 and as of 2005 to the present moment, Romania had governments oriented towards the right, whose doctrine emphasizes the stimulation and promotion of the market economy, with the „laissez-faire”, not the state policies, in charge of the standard of life of the population.

The standard of living of the employees can be inferred from the average monthly earnings. In order to make a comparative analysis, we transformed the values of the average monthly earnings into real values using the index of the consumer prices compared to 1990.

Figure 1 shows this evolution.

**Figure 1 Evolution of the average monthly wage (lei-ROL, constant 1990 prices)**

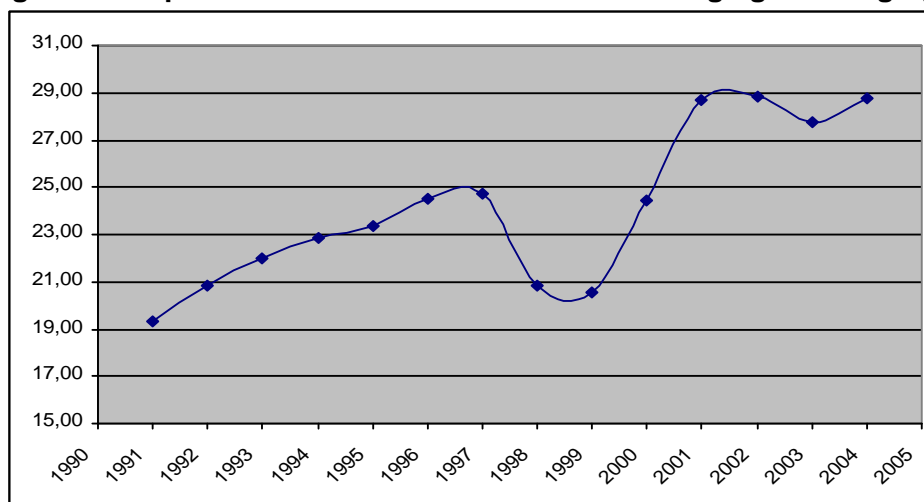


Source: Calculated by the authors using data from the National Institute of Statistics, [www.insse.ro](http://www.insse.ro)

Making an analysis by political cycles, as mentioned earlier, from Figures 1 and 2 we may notice the following:

- In the first election cycle, in 1992-1996, the wages followed the evolution of the economic cycle: decrease in 1992-1994 and increase in 1994-1996. The proportion of taxes collected from the gross wages, however, increased constantly throughout the period, which shows a higher fiscal pressure on labor, even when the real gross wage increased;

**Figure 2. Proportion of tax collection from the average gross wage (%)**



Source: Calculated by the authors using data from the National Institute of Statistics, [www.insse.ro](http://www.insse.ro)

- In 1996-2000, a strong decrease of the average real gross wage earnings was noticed (1997) followed by a flat period at about 2550 ROL, in 1990 prices. This is explainable if we consider that 1997 was the year when inflation peaked (for 1995-2004 interval), which eroded strongly all earnings, including wages. A strong decrease of the fiscal pressure was noticed in 1998 and 1999, to the historical minimum of 20.8% in 1998 and 20.5% in 1999. All along the surveyed period, such a low fiscal pressure on the worker has been noticed only in 1991. This evolution confirms the fact that 1998 and 1999 were the years in which a strong fiscal relaxation was attempted, which was not supported, however, by the existing resources, which only made the fiscal pressure burst during the subsequent period;

- 2000-2004 showed a resumed growth of the average gross wage earnings and of the fiscal pressure on them.

**Table 1. Average wage earnings 1991-2004**

Year	Average nominal gross monthly wage (RON/employee)	Average nominal net monthly wage (RON/employee)	Average nominal monthly tax collection from the wage (ROL/employee)	Consumer price index (compared to previous year, %)	Consumer price index (compared to 1990, %)	Average real gross monthly wage (ROL/employee)	Average real net monthly wage (ROL/employee, in 1990 prices)	Real monthly tax collection from the wage (ROL/employee, annual average in 1990 prices)	Proportion of the tax collection from the average gross monthly wage (%)
1991	9.475,92	7.647,75	1.828,17	270,20	270,20	3507,00	2830,40	676,60	19,29
1992	25.471,67	20.172,33	5.299,33	310,40	838,70	3037,04	2405,19	631,85	20,80
1993	78.347,17	61.102,17	17.245,00	356,10	2.986,61	2623,28	2045,87	577,41	22,01
1994	181.694,33	140.112,67	41.581,67	236,70	7.069,31	2570,18	1981,98	588,20	22,89
1995	281.286,50	215.624,83	65.661,67	132,20	9.345,63	3009,82	2307,23	702,59	23,34
1996	426.610,25	321.986,83	104.623,42	138,80	12.971,74	3288,77	2482,22	806,55	24,52
1997	846.449,67	636.821,42	209.628,25	254,80	33.051,99	2560,96	1926,73	634,24	24,77
1998	1.357.132,17	1.073.898,08	283.234,08	159,10	52.585,72	2580,80	2042,19	538,61	20,87
1999	1.957.731,25	1.554.736,50	402.994,75	145,80	76.669,98	2553,45	2027,83	525,62	20,58
2000	2.876.644,75	2.173.478,08	703.166,67	145,70	111.708,16	2575,14	1945,68	629,47	24,44
2001	4.282.622,00	3.053.597,75	1.229.024,25	134,50	150.247,47	2850,38	2032,38	818,00	28,70
2002	5.452.097,00	3.881.178,33	1.570.918,67	122,50	184.053,15	2962,24	2108,73	853,51	28,81
2003	6.741.152,00	4.868.103,50	1.873.048,50	115,30	212.213,29	3176,59	2293,97	882,63	27,79
2004	8.261.491,08	5.882.575,27	2.378.915,81	111,90	237.466,67	3479,01	2477,22	1001,79	28,80

Source: Processed by the authors using data from the National Institute of Statistics, [www.insse.ro](http://www.insse.ro)

A deeper analysis must be done by comparing the earned wage with the minimal consumption basket (Tables 1 and 2). It was approved for the first time by OUG nr. 217/2000, published in M.O. 606 of 2000, its structure, at October 2000 prices, being as follows:

**Table 2. Minimal monthly consumption basket**

No.	Product type	Amount		Value (October 2000 prices)
		MU	Monthly/average household	Lei (ROL) monthly / average household
<i>Food products</i>				
1.	Flour	Kg.	3,084	21.458
2.	Corn flour	Kg.	5,888	33.150
3.	Bread	Kg.	31,966	277.512
4.	Bakery	Kg.	0,505	12.934
5.	Pasta	Kg.	0,701	11.536
6.	Rice	Kg.	1,402	14.343
7.	Beans	Kg.	2,103	40.621
8.	Potatoes	Kg.	13,179	44.012
9.	Carrots, parsnip, celery	Kg.	1,682	18.786
10.	Dry onions	Kg.	2,524	12.237
11.	Sour cabbage and pickles	Kg.	3,084	35.328
12.	Tomato sauce	Kg.	0,841	16.406
13.	Canned vegetables	Kg.	0,561	11.872
14.	Apples	Kg.	3,084	25.317
15.	Citrus, meridional fruits	Kg.	0,561	12.455
16.	Canned fruits	Kg.	0,701	22.599
17.	Cattle meat	Kg.	0,701	28.919
18.	Pork	Kg.	2,524	120.683
19.	Poultry meat	Kg.	2,804	117.945
20.	Sheep meat, etc.	Kg.	0,421	15.027
21.	Meat preparations	Kg.	2,524	111.601
22.	Fresh and frozen fish	Kg.	0,841	20.347
23.	Fresh milk	l.	14,861	87.558
24.	Sour milk, yoghurt	l.	0,701	10.395
25.	Cow fresh cheese	Kg.	1,122	37.122
26.	Sheep fresh cheese	Kg.	0,701	27.537
27.	Sweet cow cheese and cream	Kg.	0,981	28.114
28.	Eggs	Pcs.	42,000	52.596
29.	Lard	Kg.	0,701	11.794
30.	Edible oil	l.	2,804	51.610
31.	Margarine	Kg.	0,561	11.484
32.	Sugar	Kg.	2,804	31.784
33.	Chocolate, candy	Kg.	0,140	8.453
34.	Soft drinks	l.	2,383	16.222
Total (1-34)				1.399.757
Other foods				209.964
<b>TOTAL foods</b>				<b>1.609.721</b>

**Table 2. Minimal monthly consumption basket (continuation)**

No.	Product type	Amount		Value (October 2000 prices)
		MU	Monthly/average household	Lei (ROL) monthly/average household
<i>Non-food products</i>				
35.	Garments			35.113
36.	Knitwear			22.415
37.	Footwear			57.909
38.	Books and school supplies			122.462
39.	Medicines			110.296
40.	Hygiene articles			35.844
	Total (35-40)			384.039
	Other non-food items			193.556
	<b>TOTAL non-food items</b>			<b>577.595</b>
<i>Services</i>				
41.	Water, sewage, salubrity			58.137
42.	Electric power	kWh	84,10	118.848
43.	Thermal or other sources of energy	Gcal	0,86	234.075
44.	Cooking gas	m3	29,16	44.119
45.	TV subscription			50.551
46.	Phone	Impulses	50	37.285
47.	Public transportation	travels	42	114.890
48.	Health care			124.969
49.	Taxes and dues			44.023
	Total (41-49)			826.897
	Other services			122.381
	<b>TOTAL services</b>			<b>949.278</b>
	<b>Grand total</b>			<b>3.136.594</b>

Source: OUG nr. 217/2000

This consumption basket was calculated for a household of 2.804 persons.

The level of the minimal consumption basket was updated quarterly by the National Institute of Statistics until 2<sup>nd</sup>Q 2003, when this assignment passed to the Ministry of Social Solidarity and Family, which ceased publishing it.

**Table 3. Coverage of the basic monthly consumption basket by the gross and net average wage**

Year	Average real gross monthly wage (ROL/employee, in 1990 prices)	Average real net monthly wage (ROL/employee, in 1990 prices)	Real minimal monthly consumption basket (ROL/person in 1990 prices)	Coverage of the basal consumption basket from the gross wage	Coverage of the basal consumption basket from the net wage	Difference of coverage, gross – net
2000	2575,14	1945,68	1036,15	2,49	1,88	0,61
2001	2850,38	2032,38	946,73	3,01	2,15	0,86
2002	2962,24	2108,73	946,26	3,13	2,23	0,90
2003	3176,59	2293,97	918,96	3,46	2,50	0,96

*Note: the analysis was limited to 2003, since there were no available data for the minimal consumption basket for 2004 – 2006*

*Source: Calculated by the authors using INSSE data*

Table 3 shows that fiscality had a strong impact on the standard of living of the employees in 2000-2003, materialized in a decreasing rate of coverage of the minimal consumption basket using the net wage compared to the gross wage. Thus, in 2000, the gross wage covered 2.49 times the minimal consumption basket, while the net wage covered it just 1.88 times, which means that the power of the net wage to cover the minimal consumption basket was 0.61 times lower than that of the gross wage. Thus, the taxes paid by the employee from the gross wage would have covered an additional 0.61 of the value of the minimal monthly consumption basket.

The loss of consumption generated by the taxes increased year by year, reaching in 2003, 0.96 of the value of the minimal monthly consumption basket. In 2003, the gross wage covered 3.46 times the minimal consumption basket, while the net wage covered it just 2.50 times.

The continuous deterioration of the net wage capacity to cover the minimal monthly consumption basket demanded action from the authorities. The most important measure was the introduction of the single taxation rate of 16% as of 1<sup>st</sup> January 2005. This aimed both the relaxation of the fiscal burden on all employees and a fiscal equity of work taxation, so that the



people on higher wages do not have additional fiscal burdens compared to the people with lower wages.

### **Conclusions**

The concept of “quality of life” includes its most important component, the “standard of living”.

The provision of a decent standard of living depends on the level of society development quantified by the GDP and on its distribution.

The employees represent the most important category of occupied people whose earnings are taxed. This is supported by the 56.04% proportion of employees within the total occupied people (in 2003).

The analysis of the wage earnings in 1990-2005 showed that:

- In 1992-1994 the average real gross wage decreased while in 1994-1996 it increased. This didn't influence the proportion of tax collection from the wage which increased continuously and this increased the fiscal burden over the work;

- A significant decrease of the average real gross wage was noted in 1996-2000, due to the peak inflation, which eroded all earnings strongly;

- The lowest fiscal pressure felt by the employees was noticed in 1998 and 1999.

From this evolution we may conclude that fiscal relaxation was attempted in 1998 and 1999, but it was not supported by the available resources, and the fiscal pressure soared subsequently.

The coverage of the minimal monthly consumption basket by the wage showed that:

- Fiscality had a strong impact on the standard of living of the employees in 2000-2003, as showed by the decreasing coverage of the minimal monthly consumption basket by the net wage compared to the gross wage;

- The continuous deterioration of the net wage capacity to cover the minimal monthly consumption basket demanded action from the authorities. The most important such measure was the introduction of the 16% single taxation rate. This aims a fiscal relaxation for all employees, creating the premises for a fiscal equity of work taxation.

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## INERTIAL BEHAVIOUR AND THE SUSTAINABLE DEVELOPMENT OF THE FIRM<sup>B</sup>

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PhD Mihail DIMITRIU\*

### **Abstract**

As increasingly obvious signs tell us that the natural environment is changing abruptly and, unfortunately, noticeably, the natural resources, while being increasingly depleted, have to support a growing population. In this context, strategies for the sustainable development of the society have to be implemented. This situation will entail a rethinking of the place and role of the firm within the society. During the transition towards another type of human society, the problem of behaviour, including the behaviour of the economic agent, will appear more and more frequently and in terms that we can not even imagine now. Within this context, the paper attempts to capture several aspects concerning the inertial behaviour of the firms in the financial domain.

**Keywords:** behavior; inertia; management; development; growth; sustainability; durability.

**JEL Classification:** D01, D92, F43, G34, H32, L25, L51, M14, O12, O15, O23, Q01, Q20, Q28, Q56

The goal of sustainable development, assumed directly or indirectly by the European Union member states, is a process of transformation by which the economic system will have to develop own self-regulating mechanisms, adequate disponibilities and capacities to receive information through specific instruments and procedures. This will lead, in the end, to another type of

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economic, sustainable growth for the sustainable development of the human society.

This process of change targets first the economic agent and then the relations within which it evolves. The change by transformation is achieved at different paces and extents by the different components of the economic environment, the goals of the sustainable development requiring the disposal of some components (specific to the “optimal” economy), the change of others (assumed distorted from the “market economy”) and the emergence of new components (rejected by the “market economy”). The structural and functional diversity and disparity of the economic environment, as well as the different behaviour of the economic agents may *alter, turn away or break off* the processes required for the changes, through transformation within the economic system. Generically, these three phenomena, unspecific to change, circumscribe the concept of inertia, particularly the economic inertia. In economic terms, inertia signifies the preservation of the identity or behaviour, or continuing the evolution within the same qualitative and quantitative limits at the level of the economic entities. The inclination towards inertia manifested by any economic entity shows not so much the rejection of change, but the existence of selectivity and adaptability, built within the structures of the economic entity, which might give them the freedom of option, of choice.

To this end, the negative aspects related to change can be attributed to the economic entity to the extent to which the economic environment becomes permissive to change, which is beneficial to the sustainable development of society, and the entity selects an inertial behaviour. The opposite situation, namely in the conditions of an economic environment rejecting the change which is beneficial to the economic entity, its inertia, even though is a positive factor for the economic environment where it functions, can not contribute to the change towards the sustainable development of the society.

### **1. Nature and change of the financial inertia related to the sustainable development**

The nature of the inertia of the financial component of the economic agent is defined by the fact that, in its essence, the finances, at the microeconomic level, are generated entirely within the relation of the economic agent with its environment. They are not a “product” of the economic agent, rather a “resultant” of its confrontation with the environment, being thus of relational essence.

The economic agent behaves inertially within an inertial financial environment; within a changing financial environment, the economic agent, through selectivity and adaptability, no longer behaves inertially. Thus, the process of environmental change, of the financial environment in our situation, will have to provide the economic agent with a different “relational field” within which the economic agent may perceive, accept and assimilate properly the change of its own financial component. Oppositely, financial inertiality may develop materialized, among other, as low quality financial services and financial blockage. To have a proper understanding of the content of financial inertia, we must consider the fact that the finances are an “expression” of diversity using a homogenous standard. Being an expression, it is obviously determined by these diversities, by that something. Thus, financial inertia is a relational “mirror” of the assembly of inertias inherent to the changing economic agent.

### **2. Forms of the financial inertia**

The forms displayed by the financial inertia are very diverse, requiring several typologizing criteria. If some forms are determined directly by the financial environment, other are generated by the perception which the economic agent has on the change of the environment; if some forms of financial inertia display a low temporality, others last longer; if some are specific to the financial structure, others circumscribe the financial flows.

This diversity of forms of the financial inertia is, nevertheless, a hypostasis of the same form of manifestation of the economic agent, by selectivity and adaptability, to a changing economic environment. In fact,

these forms are ways in which the economic agent participates both at its own change, and at the change of the environment.

It is obvious that all forms of financial inertia can also be regarded in relation to the managing system and, from this approach, they are directly linked to the behaviour and attitude of the decision maker.

The most significant forms of inertia of financial management are those linked to the following types of financial management:

a. passive financial management and inertia in budget financing.

The economic agent, focused on production, cut off from the economic environment, is in a continuous financial "expectation"; irrespective of its financial status. The state has to provide, under different forms, financial supplements required to meet the financial needs of the economic agent. Obviously, within an economic environment without institutional and instrumentary opening, the economic agent, which is far from the state of equilibrium based on economic calculations, has one final opportunity for equilibrium in the public finances, and the financial management acts in this direction (inertially).

This form of financial inertia is directly related to the financial inertia of the environment within which this vicious circle of subsidies is created, unproductive, inefficient and financially redundant.

The incertitude or deforming of the processes of change through transformation during the transition period, the lack of synchronisation in the activity of the decision making body between the macro level and the mezzo- and microeconomic levels, a conservative behaviour, maintained this circuit of subsidies which has mainly affected the private economic agents, ending by compromising the spirit of the change.

This type of financial management can also occur in developed countries, as measures which are "atypical" for the sustainable economic growth are proposed. The market mechanisms are expected not to be sufficient in the future so as to change an economic mechanism oriented towards "optimality" and "efficiency", intervention measures being required, requiring to be "supported" by the state (subsidies, state aids etc.). The transit to a sustainable economic growth for a sustainable development of the society will involve a change of behaviour at the microeconomic level. The rush for profit,

market segment, competition, will have to be replaced by the concern for the natural environment, for the level and quality of the resources that are used (only renewable resources should be used!); this change of behaviour will not happen concomitantly in all the firms worldwide. A good deal of time there will be firms working inertially, within the spirit of the current economic system, but they will be gradually “compelled” (through levers, instruments, means) to change.

b. the passive management and the “consumptionist” behaviour. The economic agent, confronted with an uncertain, unpermissive economic and financial environment, have not yet acquired the exercise of the risk and self development, turning to the “consumptionist” behaviour, focused on production which affects all categories of investments (replacement, modernization, development and strategy). This is being maintained by the process of decapitalization of the economic agents, by the break between the real circuits and the financial circuits of the economy (financial blockage), and not last, by the inertia and lack of adequate instruments and levers of the monetary circuit within the economy.

The disequilibrium between the sources which finance the investment, in conditions of a dramatic reduction of all financial resources, pushes the economic agent towards an inertial behaviour to disinvest, behaviour which is degenerative and multiplicative.

The relation between the attitude towards financial risk and disinvesting is obvious, particularly under the conditions in which the state will take “drastic” measures for the “forced” reorientation of the way the resources are allocated within the economy.

c. passive management in relation to decapitalization.

The inertia of decapitalization is a synthesis of the effects of the other forms of financial inertia within a changing environment. Decapitalization, as a process of relative reduction of the permanent, active financial resources on the background of the shrinking of overall financial sources for the patrimony and particularly, the absolute decapitalization, generates a deterioration of the structure of permanent capitals, with effects on undersizing the circulating funds of the economic agent.

The denaturation of the permanent financial resources, particularly of the payments, financial debts etc, generates a passive managerial behaviour (of impotency, seemingly), with direct effects on solvability and financial liquidity. Obsessed by the financing of the exploitation cycle, cycle which will not be acknowledged by the economic environment, financial management maintains the attained level of inertia towards decapitalization by a negative treasury, chronicized under the conditions of commercial cycles without equivalent.

### **3. Dimensions of financial management inertia**

The causes, effects and influence of the forms of inertia that are characteristic to financial management circumscribe dimensional coordinates by which each form of inertia can be defined and measured so as to highlight its adverse or positive potential for change.

a. The structural dimension shows the financial state of the economic agent confronted with one or several forms of financial management inertia, state identified at certain moments of the economic cycle (sustainable, for a sustainable development of the society!).

The discerning, delimitation and description of some financial structures generated by different forms of inertia is one way to analyse their causes, effects and influences on the quality of the services performed by the “financial department” at the microeconomic level. The balance structures, corrected and adapted to financial analyses can yield relevant information for the analysis of the financial inertia. The correlated analysis of the different structural modules and the determination, on this basis, of different rates of financial inertia may provide an insight on the inertial “mechanisms”, allowing the development of possible “programs” to alleviate or resorb the impact of managerial inertia during the process of change.

An inertial interpretation of the structure of assets (particularly of the financial ones) and of liabilities (particularly of the permanent ones), an approach in inertial terms of the balance structures and of the final aggregate components of the account of results are ways for the pragmatic utilization of the structural dimension inherent to the financial management inertia.



b. The functional dimension highlights the financial movements, flows and circuits which were affected or not by the inertia. The economic environment, its normative, institutional and instrumental components, shape in a determined way the financial flows and circuits of the economic agent, burdening them, under the circumstances of a non-permissive environment, with new inertia. The functional dimension allows highlighting the ebb of some financial flows and expansion of others, the rigidization of some financial circuits under the conditions of deteriorating banking circuits, of the financial flows required for the economy to function, or it may display the denaturation of its functionality.

However, in our opinion, the functional dimension shows, from the inertial perspective, the preservation for a long time to come, of the lag between the primary and secondary financial circuits, the inertia of the primary circuits being displayed on the background of the lack of circled monetary values and of openings without productive finality (production within the frame of sustainable development!).

c. Behavioural dimension, noticeable directly at the management level, which requires the existence of a way to perceive the change. The first two dimensions provide the coordination plan for the definition and measurement of financial management inertia as an oriented relation of the economic agent with the environment, predetermining the forms of financial inertia, while the behavioural dimension reveals the process of inertia sedimentation within the behaviour of the economic agent, which may become bearer and generator of some forms of financial inertia. The "learning" lag of the inertia by the manager proves, eventually, a lag of perception of the change at the microeconomic level, with consequences on the overall inertia of the economic system.

d. The temporal dimension allows measuring the duration of inertia, of the lags between the different forms of the financial management inertia, of their temporal desynchronisation, which might allow evaluating the possible speeds, paces of changes at the microeconomic level.

From the temporal perspective, hierarchies of the forms of inertia can be elaborated, function of which the strategies for their reduction, synchronisation or reorientation may be developed, even for the valorisation

of their correlated evolution, for the fast assimilation of the change at the level of the economic agent.

#### **4. Inertia and the financial policy – framework for defining**

From a financial perspective, we may consider that a commercial society holds at any moment a “collection” of “productive” financial resources represented by inputs supplying determined services to achieve a certain goal. In other words, a given assembly of financial resources opens the way for an assembly of activities. The environmental pressures, the short-, medium- and long-term objectives (more or less formalized currently at the level of the commercial companies), as well as the specificity of the intervention of the financial management require a certain evolution in volume, structure as well as specific interactions between the financial resources and the achieved actions, major goal of the economic and financial calculations.

The nature, volume and quality of the financial resources held by the commercial company define the pertinent conditions of the future evolution of the activities (their nature and volume). The policy of “financial resources management” is therefore a major element in judging the level of inertia.

On reasons of simplification, we can perform the analysis on two successive plans:

- within the context of the “operative” inertia, which requires to analyse, within an invariant framework of activities, the responses to the variation of the achievement of planned levels. The major problem is therefore, to choose the stock of capital depending on the flow of “services” achieved by the company;

- within the context of the “strategic” inertia, the emergence of threats or opportunities for the commercial company involves a modification in the nature of its activities. The more or less invariant response to the variations in the field of activity raises the issue of preserving the fundamental financial potential of the economic agent.

This formal distinction that we have adopted masks the unity of the two levels of inertia: operative and strategic, both of them depending directly on

the investment decisions (in the broad meaning) and on the technological, financial and human constraints, which are tightly linked.

The operative inertial behaviour is directly linked to the decisions assumed due to the change in volume of the flow of services provided by the company. The operative inertia consists in the way of responding to the variations of the volume, with adequate costs of adjusting, and it will manifest as an ever increasing period of response to an approximately equal increase of the volume of activity, and the corresponding financial costs increase much faster than the increase of the volume of activity.

In many cases, the existence of some factors requires the technical or economic limits at the output level. In other cases, the risk linked to the irreversible character of some financial resources should force the commercial company to make a long-term prediction of the required financial flows. Each time, the inertia is linked directly with the over- or underevaluation of the demand for outputs. The trend currently displayed is to respond post factum to all the changes in the economic environment (change in the legislative framework, the level of interests, input price level, exchange rate, etc.).

The solutions to avoid the inertia of the financial policy of the commercial companies are currently limited: one is growth-related and consists in selecting an excedentary financial capacity required to respond to the increased volume of outputs; the other, on a more general level, attempts to discard the risk and to avoid more or less the investments.

### ***Conclusions***

The inertial behaviour is displayed by the specific way of action both during the design and during the implementation and application of the financial policies and strategies, by the duration and type of response of the financial management at the different changes of the economic environment. Major influences are thus manifested on the level and quality of the economic and financial activity, including in the area of the products and services it supplies.

The operative inertial behaviour can be reduced by selecting a surplus or by avoiding it within the financial capacity of the firm. These ways of

intervention are just two particular aspects within a wider picture: the investment policy which, after all, also involves the financial policy.

It is obvious that no company can survive in the long run without innovation and development. Because it involves a decision-making process to mobilise resources, the financial decision, linked to the investment decision, in its three components – nature, dimension and moment of application – is conditioned by the operational inertia of the financial management.

It is obvious that in the future too, the problem will display very varied degrees of intensity related to the specificity of each economic agent's activity.

The future use of practices resulting in an excedentary financial capacity will represent a means of securing a lower inertia, within rather small limits. If the existence of factors improperly used allows a response to the random variations of the demand, with small financial costs and within an, as short as possible, period, this response affects at the same the profitability and increases the average costs.

Corrections can be used to modify the volume of assets, but they also involve a change of the level of short-term inertia, within a perspective of long-term increase of the volume of the commercial company's output.

On the other hand, avoiding the supplementation or the "pressures" on the financial capacity allows having a lower level of operative inertia and a certain level of strategic inertia through the savings foreseen in the funds for investments.

This means will also be used in the future in the domains where the degree of technicity is quite poor and where there is a monopoly which allows a "separation" of the financial costs and of the risk by drawing different economic agents in cooperation.

The analysis of the strategic inertial behaviour within the financial policy can be related to the improvement of assets liquidity and to the incomplete utilization of the indebteding capacity.

Under these terms, seeking to reduce the inertia and the maintenance of the financial independence are synonyms and they are reduced to the fact that the enterprise has to avoid being in a state of financial vulnerability. This

remark shows that, actually, the hierarchy of the development and security goals varies within the economic context: in the periods of economic recession. The existence of a margin of financial “manoeuvre” is a guarantee of survival; during the periods of economic growth, the firm must increase the volume of investments because the risk appears to be limited and the prospects of future profitability seem interesting.

Financial management inertia seems imminent and, voluntarily, it is accepted, because the firm hardly resists the “temptation” to employ “inertially” all its financial resources in the struggle for development. The most delicate issue is therefore, the one raised by the conjectural relaunch. If the growth perspectives at the macro- and mezzo economic levels do not come true, unfavourable effects may appear for the firm.

Irrespective, however, of the trends displayed at the macroeconomic level, we may say that, at the level of the economic agents, the experience of the past ten years shows a quite high level of inertia of the financial management, which is likely to continue in the future too, which is a problem for the desired and achieved speed of the process of transformation.

## **Financial Studies**

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