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Romanian External Debt Evolution -Pre and Post Accession to Eu

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The present paper is studying the evolution of Romania's foreign debt before and post accession in the European Union, namely the period 2000 – 2013, in the large context of the specific macroeconomic policy objectives of the times. According to our research results, the economic effect of external debt may be considered positive and for long-term, as a greater proportion of funds were used to finance investment projects, especially by private sector, and only a small part of this debt was oriented to cover public budget deficits.

Keywords: *external debt, external loans, debt structure.*

JEL Classification: *H60, H62, H63*

Introduction

Economic growth represents one of the most important goals for a country. One of the instruments that may help to reach this objective and to offer this way better life conditions to population is debt, namely foreign debt. Foreign debt allows economies to invest and to consume over their capacity. They may lead to fast economic development by financing investments and engaging national financial resources but also they may have negative effects by financing nonproductive activities. The foreign debt growth usually represents a signal of a reduced production capacity of national economy which cannot face the need of public or private investments and consumption. This additional financial resource may be taken in consideration only when there is a balance between the added value foreign debt generated and foreign debt service, meaning interest and reimbursement. That means foreign debt has to be orientated more to investments, production and exports, which are important levers of a durable economic growth, and less to final consumption and imports. Otherwise, the debtor economy has to identify alternative resources, as new debts or rescheduling. The first possibility, new credits are the most dangerous, because overdebts may overburden production and exports and the country risks lack of liquidity and foreign investors'exodus.

Romania's external debt dynamics in pre and post accession to the European Union is a complex topic in the broad context of macroeconomic policy objectives of this period of time. Its study requires an interlinked and comprehensive analysis of various macroeconomic indicators which debt influence and is influenced by.

Foreign debt in pre-accession period

Pre-accession period is characterized by a strong economic growth, which is based on services and industry, the annual advance of GDP having an average of 4%. Imports grew from 14 to more than 40 million euro and exports doubled, reaching 24 million euro in 2006. The trade balance rising value from 2 to 6 million euro gives us information that, before 2007, Romania was more consuming than producing country. Although accession period has a striking consumerist trend (consumption reaching 80% of GDP) gross capital formation registered a real revival in the late pre-accession period, when it represented 31% of gross domestic product, compared to 22 % measured in 2001. That represents a sign of interest in economic development, helped by the stabilization of the national currency, as inflation dropped up to 6.5%. In addition, fiscal measure to reduce income tax from 25% to 16% represents a real incentive for investments, which grew over 6 times. Mostly private ones, investments were still funded by national resources, external credit covering less than 10% of needs. That happened although the national reserves increased to over 22 million euro, representing a very good signal for foreign investors.

So, in a growing economy, with macroeconomic indexes signaling stabilization, but still indicating the reluctance of foreign investors, foreign debt increased in nominal terms, especially since 2004, as Chart 1 shows. That year, thanks to advances on macroeconomic stabilization line, Romania obtained from the European Commission the market economy statute. In addition, in the same year were completed the negotiations on our country accession to the European Union, paving the way of signing the Accession Treaty (April 2005). As an effect, foreign debt grew, because of the confidence vote won from Europe.

Foreign debt in post-accession period

Post accession period is marked by year 2007, when Romania submitted to European Commission its first convergence program, in conditions of respecting the Maastricht criteria on the general government deficit and public debt. In 2008 started US high-risk mortgage crisis, which changed the perception of foreign investors in the economies of Central and South-Eastern Europe, leading to a massive withdrawal of funds. Romania economic environment was deeply affected. Thus, exports have fallen sharply because of liquidity problems, foreign banks limited activity, increased costs and tighten credit conditions, which limited credit access. In addition, liquidity crisis developed a real aversion of foreign investors to emergent countries.

An additional effect, in conjunction with all other specified effects was depreciation of Romanian national coin. The inflation rate reached in 2008 the 7.85% level. In this context, the budget deficit problems were imminent, so in 2008 the country's budget deficit rose to 8% of GDP. Imports decreased due to the decrease in consumption and production, generated by the bracking of economic activity, the growth of prices, the absence of liquid money and job cuts. At the same time, exports also felt down, but trade balance exceeded 20 million euro, as a sign that national economy was blocked.

The solution to the economic recovery was to sign a loan agreement with the European Union, International Monetary Fund and other international financial institutions for 19.95 billion euro, in order to avoid sudden and disorderly adjustment of economic imbalances and to moderate and timely spread the costs of correcting these imbalances. This huge entry of major foreign loans did not affect Romania's public debt in terms of Maastricht Treaty, because, in new conditions, it has not exceeded 60% of GDP (56.5%).

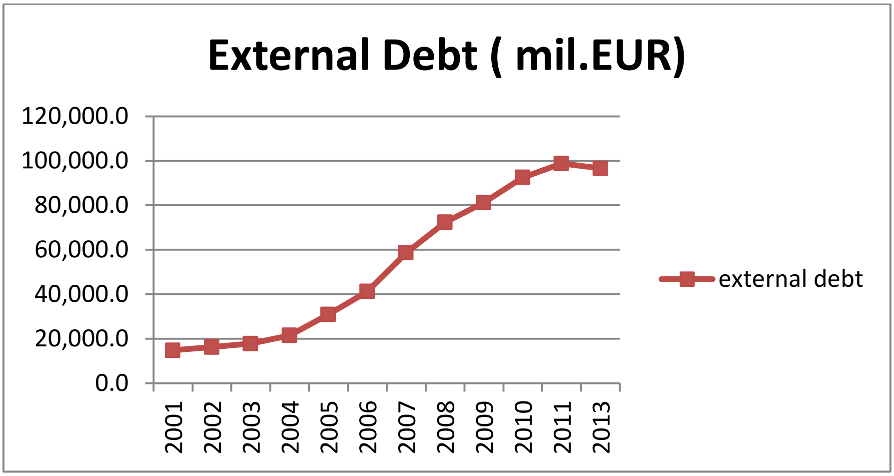

Figure 1: Romanian external debt evolution between 2001 and 2013 (billion EUR, nominal terms)
Source: the web site of the National Bank of Romania,www.bnr.ro

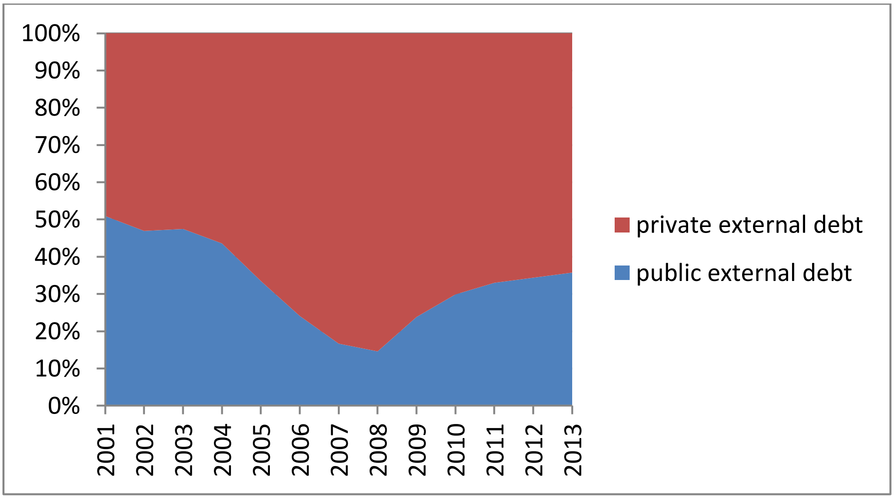

Figure 2: Romanian external debt structure, taking into consideration the debtor category (public or private), between 2001 and 2013

Source: authors' own processing, based on data provided by the web site of the National Bank of Romania, www.bnr.ro and Romanian Ministry of public Finance, www.mfinante.ro;

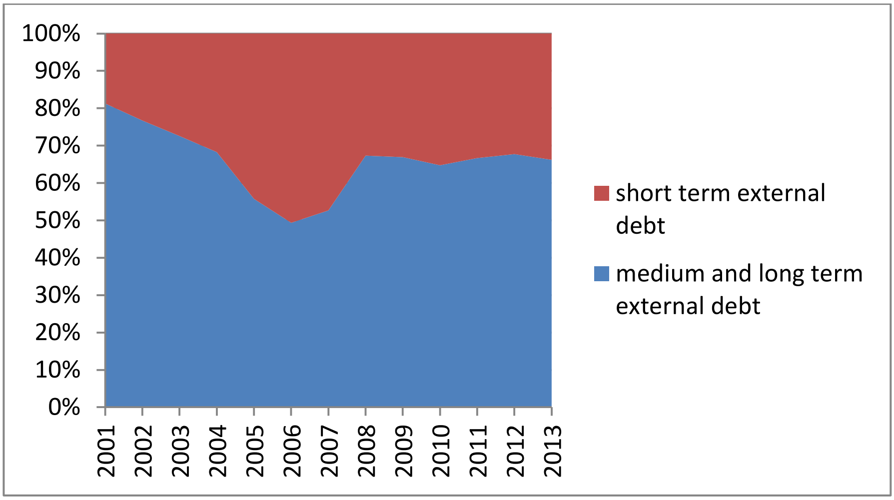

Figure 3: Romanian external debt structure, taking into consideration its term (long and medium term or short term), between 2001 and 2013

Source: authors' own processing, based on data provided by the web site of the National Bank of Romania, www.bnr.ro and Romanian Ministry of public Finance, www.mfinante.ro

Economic recovery efforts have long-term effects, such as public budget deficit reduction to 2.5% in 2013, the revival of exports and imports with the improving of trade balance. Final consumption reduced from 88% to 78% of GDP in behalf of gross fixed capital, which accounted for over 25% of GDP at the end of the period. In addition, inflation has fallen below 4%. Although national economic context was a revival one, the contribution of foreign loans to investments reached only 5% of financial needs. External public debt financed more the private sector, as seen in Chart 2, according big attention to production and export (over 40% of foreign private debt).

In the context that external debt increased to almost 100 billion euro in 2012, the public share (which is not directly productive), has been growing, to the detriment of the private one. As public investments reduced, the foreign public debt was surely used to correct some economic problems

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induced by the international crisis. That means that public foreign debt service has no added value support and it will aggravate the fiscal pressure for next generations.

As shown in the Chart 3, long-term external debt exceeded short-term debt, as a sign that interest for added value and sustainable development outweigh final consumption, financed by the short term debt. This situation precedes a very risky period (2008), when short-term debt reached 50% of Romania's external debt, a sign of maximum vulnerability, induced by the international economic crisis.

Conclusions

Romania's foreign public debt analysis reflects a process of adaptation and directing it for the needs of the economy, according to EU requirements. Situated on an upward trend until 2012 and signaling reduction since 2013, foreign debt stimulated private sector development and exports revival, and also the public sector restoration in an unfavorable international context, characterized by inflation, state's inability to face public spending, decreased economic activity, unemployment, political instability. Most of it private and for long-term, the external debt of Romania represents a necessity. As shown, it contributes to the economic recovery when added value is generated and there are respected conditions seeing sustainability and equity. So, we consider there is a real need to build a stable legislative framework and to offer incentives to foreign investors, as to encourage private foreign investments, because this represents a sure way of building a strong economy, by the added value induced, by jobs created, by tax collected. Also, we have to take care about the volume and type of foreign debt, as to limit national economy exposure and to ensure a healthy economic development.

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