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POLICY-MAKING IN ROMANIA

THEODOR STOLOJAN
Former Prime Minister and Minister of Finance, Government of Romania

CONTENT

Introduction

The following developments highlighted Romania's process of transition in 1999:

- Romania experienced its third consecutive year of economic contraction;

- "...the current business climate is discouraging. Long the country of perpetual promise for investors, the country today is more a nation of perpetual problems, almost all of which are self-imposed and almost avoidable." (quotation from the monthly news of a foreign company , operating in Romania , August 1999);

- Citizens believe strongly that actors outside the country determine economic policy (e.g., international financial organizations);

- The Senate rejected a "customized" Government Ordinance that proposed granting tariff facilities for imports to only one company (September 1999);

- Ministers engage each other in disputes over governmental resolutions through mass media;

- Sixty-six percent of the population believes that the country is moving in the wrong direction (May 1999, survey of public opinion).

As always in Romania, hope remains. In 1999 the Government continued efforts to stabilize the economy, with support from an IMF program. At the same time the Government tried to accelerate privatization and the restructuring of large state-owned enterprises with support from the World Bank.

But hope alone does not suffice as a method for achieving progress. The situation described above persists in part due to the government's lack of efficiency and overall low level of effectiveness. In order to accomplish its goals, therefore, the government will need to improve substantially both its policy-making and its policy-implementation capabilities. Romania can only achieve good economic results through the consistent application of effective long-term policies.

1. Results of the Economic Policy in Transition

Romania's economic performance is hardly exemplary, if we accept that the sustainable recovery of growth output is the most useful criterion for assessing success in the transition[1]. The tenth year of transition in Romania brought the third consecutive year of economic contraction: -6.6 percent in 1997, -7.3 percent in 1998 and –3.5 percent forecasted for 1999. By all standards[2], Romania is experiencing a growth crisis.

Incentives for the sustainable recovery of growth are weak because Romania has not accomplished the main objectives of transition.

- <u>Economic freedom</u>. Romania liberalized economic activities, most prices, markets and trade, and it also built the legal and institutional framework to prevent anti-competitive practices. However, barriers still exist to efficient reallocation of resources in the decentralized system, including bureaucratic incompetence, red tape, regulations that lack clarity and give discretionary power to public servants, and the limitless proliferation of newly enacted taxes and duties.

- <u>Economic stability.</u> In 1999 Romania continued its struggle to achieve disinflation. At the end of July 1999, inflation was 33 percent (down from 41 percent in 1998). The exchange rate jumped from 8,744 Lei/US$ in July 1998 to 16,037 Lei/US$ in July 1999. More than 50 percent of the external debt in 1999-2000 is due in only two years, and exports have been stagnant for the past four years.

- <u>Development of the private sector.</u> The Government has privatized 67 percent of the joint stock companies, but by June 1999 it had sold off only 28 percent of the total capital the state holds in them. The economic environment for small and medium businesses is difficult. This has prevented Romania's vibrant small and medium business sector from absorbing the unemployment created by the restructuring of large enterprises. [Or "This has prevented Romania from developing a vibrant small and medium business sector that might absorb the unemployment created by the restructuring of large enterprises", depending on the authors' intent.] By the end of July 1999, foreign direct investment in Romania was US$ 4.1 billion, compared to US$ 26 billion in Poland (end of 1998). This places the private sector's share of GDP at 58.3 percent at the end of 1998, up from 58.1 percent in 1997 and 54.9 percent in 1996[3].

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[1] Thomas Wolf and Oleh Havrylyshyn , "Determinants of Growth in Transition Countries", Finance & Development, IMF, June 1999., p. 12

[2] Michael Bruno, "Deep Crises and Reform; What Have We Learned ?", The World Bank, 1996, p.1.

[3] The National Commission of Statistics, "Evolution of the Private Sector in the Romanian Economy 1990-1997", p.1; Jurnalul National, September 9, 1999.

- Security of property rights and the rule of law. In September 1999 Parliament was still debating the issue of restitution of property rights confiscated by the communist regime. Investors question the security of their investments because the state frequently changes its commercial law and alters the rules of investment after the game has begun. The security of property rights is also damaged in transactions on capital markets. [The meaning of this sentence is unclear. I would need to know the authors' intent to determine the appropriate wording.] Romania lacks adequate institutional capacity to enforce business transaction regulations.

- Delivery of public goods. Public services such as basic health, education and defense do not receive adequate funding, and reform in these sectors has been delayed. This has resulted in deterioration of the quality of these fundamental public goods. The persistence of old-style budgeting practices has weakened the state's effectiveness, as it cuts expenditures across the board instead of redesigning objectives consistent with new priorities and available resources. The state further compromises its efficiency through wasteful spending on rampant bureaucracy.

The economic policy outcomes described above result from diverse factors, including unfavorable conditions at the beginning of the transition. But everyone in Romania recognizes that the country has also suffered from poor leadership and policy-making, and weak institutional capabilities of the State.

2. How to Improve Policy-Making

In 1990, Romania chose a gradual path of reform from the centrally-planned economy to a market economy. But gradualism is not an excuse for delaying reform. Actually, the economic policy of transition in Romania may be best characterized as a "stop and go" policy and partial reforms. This kind of policy failed in all transition countries, and had failed badly. Romania is no exception. To understand this way of policy-making in Romania, and what should be done to improve it, we should focus on five issues: (i) electoral cycles and consistent policies; (ii) stakeholders' participation in policy-making; (iii) capability for policy-making, building consensus and implementation; (iv) civil service corps; and (v) communication with mass media.

2.1. Bridge Electoral Cycles Through Consistent Policies

The literature of political economy has argued that severe crises promote reform. Romanian policy-makers missed the linkage between crisis and reform. Romania met two important windows of opportunity for a bold and consistent reform, and missed both: December 1989, and; November 1996.

<u>December 1989</u>

Any attempt to understand policy-making in Romania in the first years of transition has to start with an analysis of the four main characteristics of Romania's environment on day one of transition:

a) **Inexperience**. When Romania's transition clock started ticking, its emerging leaders, the media and the population lacked knowledge about the principles of democracy and the market economy;

b) **Centralized Decision Making**. Romania had one of the most centralized decision-making systems among the former socialist countries. Hungary had started its economic decentralization in 1968. In Romania, "The New Economic Mechanism" introduced in 1978 was supposed to give more decision-making power to enterprises. This mechanism failed, and during the 1980s it became a huge bureaucracy with institutionalized forms that gave a false image of enterprise and public participation in decision making. In reality, the Romanian enterprises remained strictly within the framework of the centralized plan for their basic decisions;

c) **The Exhausting 1980s**. The 1980-1989 decade of sacrifices to prepay the foreign debt and to invest in what can be described only as megalomaniac projects exhausted the economy and the population;

d) **The Violent Revolution**. Unlike other former socialist countries, Romania began its transition violently, with an overnight dismissal of the old political system. The first post-communist government filled a temporary political vacuum and it did not enjoy widespread popularity. Even after the first election, in May 1999, the results were contested and the fight for political power was immediately reopened. Therefore, the first two years of transition were dominated by political demonstrations, aggressive strikes and finally by coal miner riots in September 1991, ending with the collapse of the Government.

These characteristics had two important consequences:

- First, on day one, transition started within enterprises, social units and local and central administrations as a chaotic process without any preparation or underlying principles. Under the pressure of workers and trade unions, the new administrative management teams from most enterprises (elected by popular vote) rejected the old norms for output, labor input and other costs but did not replace them with a new economic system based on profitability. These actions and the state's failure to assert itself as an owner chaotically ended the old equilibrium criteria and mechanisms and opened the gates for the massive de-capitalization of state-owned enterprises;
- Second, the new authorities in power after the revolution relaxed their economic constraints. For example, they put the people's needs first in their allocation of scarce energy resources, increased energy import and generally increased all social expenses on the account of reducing investment. While the population expected this, it was entirely inconsistent with the targets of economic stabilization for our transition to a market system because the increased consumption could not be financed by an economy with negative growth and ineffective structure. The output decline that had begun in 1988 accelerated drastically after 1989 and the energy intensity of the economy technological structure could not be further supported. After exhausting the international reserves of the country, Romania faced inflation and external disequilibrium.

Therefore, the December 1989 crisis did not lead to a bold and consistent reform. Its failure resulted from the revolutionary context, and because Romania held enough resources to face the disequilibrium in the first years of transition: a) almost no external debt and a comfortable level of international reserves; b) a high level of saving backed by a physical structure of the Romanian economy designed for decades to support big investments and strictly controlled consumption; c) a soft source of lending such as emergency loans received from the international financial organizations.

The privatization policy before 1997 best demonstrates the country's stop-and-go policymaking. Romania approved the first concept of mass privatization in August 1991 but implemented it only in 1995.

<u>November 1996</u>

In 1996, people were already fed up with the inconsistency of economic policy and lack of a rise in their living standard. They therefore voted for change, and the opposition took power. The momentum for a bold and consistent reform was great, and people were ready to accept this reform. Unfortunately, the new Government missed this opportunity. The new Government came to power with an economic program which proved to be unsustainable when faced with economic reality. That program was replaced by the agreements with the IMF, World Bank and European Union. Soon, fights among the political forces in government led to another government comprised of the same political coalition. In 1999, this new government started again the effort for reform based on programs agreed upon with international organizations.

In a democracy, political parties compete for citizens' votes through the electoral programs based on different political ideologies: liberal, social democratic etc. However, in transition from the centralized planned economy to a market economy, despite ideological backgrounds, political parties were supposed to arrive at a more consistent and comprehensive view of the objectives and strategies of economic transition for at least two reasons.

First, there are certain objectives (milestones) of transition which cannot be ignored by any political party which has to lead a transition from a centrally planned economy to a market economy. These milestones refer to:

- Economic freedom through liberalization of economic activities, prices, trade and markets, and promotion of competition;
- Economic stability through a prudent monetary and fiscal policy and hard budget constraints at the enterprise level ;
- Private sector development through privatization and setting an environment which encourages small and medium businesses and foreign direct investment;
- Changing the role of the state from the main provider of goods and services into a catalytic and facilitating role, encouraging and complementing the activities of private businesses and individuals.

Second, transition has proved to be a long-term process running beyond electoral cycles. Therefore, different governments supported by different political parties or coalitions had to pursue the same objectives for periods of time longer than an electoral cycle.

In Romania, as everybody may notice, the transition objectives lack consistency and comprehensiveness between governments. Most governments claimed that the only real economic reform is the one that started with its own administration. To make this concept effective, each government wasted time and resources to change laws and regulations. This produced an uncertainty within the business environment which, together with the weak capability of governments for policy-making and implementation, finally transformed Romania into a country of perpetual problems and promises.

Actually, we may say that the linkage between economic policies of different governments in Romania has been built by the international financial organizations.

Thus, one of the main jobs of policy-makers in Romania is to build a consistent and comprehensive view among the political parties on the objectives and strategies of transition. Different governments should build on achievements of previous governments, rather than spend months lamenting the legacy of previous governments, and then years justifying the bad outcomes their own actions left for subsequent administrations.

2.2. Improve Participation of Stakeholders in Policy Making

The reform supported by the International Monetary Fund, the World Bank and the European Union has been the core of all governmental economic programs in the last years. The good news is twofold:

a) The programs agreed upon with the IMF, WB and EU included the appropriate measures for transition such as liberalization of prices, trade and markets, stabilization of prices, privatization and institutional reform; and,
b) These programs kept governments on the right path, even though the policy was stop-and-go for years and the cost of delay was high.

The bad news is also twofold:

c) The government lost credibility . People have the perception that economic policy is developed outside the country. This perception has become stronger in 1997-1999. Indeed, the Government focused its policy too much on agreements with IMF, WB and EU ; and,
d) The agreements with the international organizations did not approach issues which were not on the agenda of these organizations. Two examples of such issues with negative impact on people follow.

- ♦ First, these programs do not address the issue of a system to manage state participation in joint stock companies and other state assets. The reason was clear: privatization was a priority and the government should focus on privatization and not on building a management system for the state's assets. The principle was right. But privatization takes years and the state remained without a concept how to manage its assets in a market economy. The result was also clear-cut: a huge decapitalization of the state-owned enterprises which lowered the confidence of people in a market economy.
- ♦ Second, The second example of an issue overlooked by the international financial institutions is that of restructuring. All international financial organizations supported the idea that restructuring should be done by the new private owners and not by the state. This concept was also right. However, for one reason or another, the state found itself involved in restructuring in two cases: when privatization of a state-owned enterprise failed and liquidation was not desirable; when private enterprises lacked a critical mass of ownership concentration and, in a weak institutional environment, do not have incentives to restructure. Liquidation may not be a solution for all these private enterprises. Before a case-by-case approach, the state needs a systemic solution which sets a framework for out-of-court resolution which should be neutral to ownership and industry sector. Otherwise, the state will act on an ad-hoc and discriminatory basis or will not act at all, with an unnecessarily high cost for society.

On September 21, 1999 the whole country awaited the result of negotiations between the government and the IMF, to learn how much Romania could spend from its budget. Once again, the country learned how the government wanted to spend more for education, health, police, defense, infrastructure etc. but the IMF did not allow it. Foreigners and Romanians have the perception that "not for the first time, Romania is being forced towards reform because it has simply run out of money."

This kind of policy-making in Romania should stop, and the government should regain its own capacity to manage public expenditure. Today, the government and the public do not recognize the limits on how much the state can provide: they fail to set expenditure limits to reflect financing limits.

"Policies that are imposed from outside may be grudgingly accepted on a superficial basis, but will rarely be implemented as intended. Development cannot be just a matter of negotiations between a donor and the government. Excessive conditionality of foreign donors reinforces traditional hierarchical relationships, rather than involving large segments of society in a discussion of change and thereby catalyzing change in ways of thinking."

To match the "IMF targets," perhaps, the government will choose the easiest path: increase taxes and cut all expenditures across the board in real terms, avoiding the reordering of priorities based on progress of the public sector and institutional reforms. As usual, the result of this policy is the waste of the already scarce budget resources because no public good is fully funded and a further shrinking of the small and medium private sector.

But the budget issue is only part of the government's policy-making problem. The Romanian government should bring stakeholders into the policy-making process. That means bringing government closer to the people. The government should enable broad-based policy discussions on key policy decisions and priorities and direct participation of users and other beneficiaries in the design, implementation and monitoring of public programs. Bringing government closer to the people means also decentralizing political, fiscal and administrative responsibilities to lower-level authorities and to the private sector.

Romania has an opportunity to improve its policy-making process through participation in the first pilot project for countries in transition: the new approach to development launched with the support of the World Bank -- the comprehensive development framework. By the end of June 1999, more than 550 people from all segments of Romanian society participated in country consultations: business leaders, labor representatives, academics, activists of civil society and government officials. This is a good beginning which, if continued, will deliver a 15- to 20-year long-term development strategy which should provide much more than what in Romania is known as a "shared vision." This strategy elaborated by Romanians should be the first pillar of a new policy-making process in Romania.

2.3. Create a Strong Coordination Unit for Policy Making in Government

Everywhere, policy-makers should translate vision into strategic priorities, identify problems, provide alternative policy responses to them -- including evaluation of costs and benefits, of winners and losers -- build consensus for decisions, and monitor implementation.

Everybody who follows the policy-making activity of the Government may draw the conclusion that this is not the best part of the Government. Several facts indicate weakness in the government for policy-making: (a) long-delayed reform and lack of consensus building; (b) the abuse of “Emergency Ordinances”; (c) regulations approved and blocked because of their inconsistency with other governmental commitments.

Long-delayed Reform and Lack of Consensus Building. The Restitution Law is a “must” to enforce ownership rights and to build a solid base for private sector development in Romania. A solution for this issue has been expected since August 1991, when the Privatization Law was approved, including an article which required a special law for restitution.

In April 1999, the Presidency and the leaders of the main political parities acknowledged that they should cooperate to find a viable solution to the restitution issue. Nobody followed up, and in August 1999, the Parliament was asked to interrupt their summer vacation for the Restitution Law Draft. The Chamber of Deputies approved the Restitution Law in the absence of the main opposition political party which elected not to participate in debates because the political coalition in power ignored their views on this issue. The Senate Chamber did not debate this Law because of the very thin majority of the political coalition in power. However, as expected, a strong debate has started within Romanian society about this important Law with consequences for the future financial capability of the State to deliver fundamental public goods to its citizens. According to the Draft of Restitution Law, whenever the old properties cannot be returned to the former owner, the State has to pay compensation in cash, governmental bonds, shares etc.

Today, the amount of this compensation is not known, because the Government could not offer any estimate. The Government has announced that it may assume the responsibility for that Law in Parliament. This means that both Chambers of Parliament may give the Government a vote of confidence or not. The political coalition has enough votes to pass the Law through this procedure. The main opposition political party, which is leading in all polls for the next elections, has made a statement that it would cancel the Restitution Law (if returned to power) if the current coalition in power further ignores its views on restitution. At that point (September 1999), the Presidency called for an expert group to study the restitution issue and for dialogue between the political coalition in power and political parties in opposition. Certainly, the way the political parties in power and the Government have approached this issue is a case study on how not to act as policy makers.

The Abuse of “Emergency Ordinances”. According to the Romanian Constitution, the Government is empowered to issue “Ordinances” and “Emergency Ordinances” when the

Parliament is on vacation or it faces an emergency situation. After publication in the "Monitorul Official", the ordinances become effective immediately and have the power of Law (which normally should be approved by Parliament). Then, ordinances are to be sent to Parliament for debate and approval or rejection.

In the last years, what was supposed to be an exception has become an abuse of the Government: for example, between January and August 1999, the Government issued 293 Ordinances, out of which 123 were Urgent Ordinances. This abuse has created an unstable and unpredictable climate for business, and an ineffective check and balance system which has to protect firms and citizens against the arbitrary and "customized" regulations of the government. Bureaucratic incompetence has further exacerbated this situation.

Inconsistent Ordinances and other Regulations. The abuse of Ordinances and lack of capability for consensus building led to inconsistency in the policy-making process. At the end of August, 1999, the Government approved 15 emergency ordinances for supporting the reform of the agricultural sector. After approval, the Prime Minister was obliged to stop all these ordinances because they were supposed to be inconsistent with the reform program for agriculture supported by a World Bank loan. A debate among ministers has arisen in the mass media about this inconsistency between Government measures. Finally, the Ministry of Agriculture has started clearing these ordinances with the Bank.

All the above-mentioned facts prove that coordination of economic policy, prioritizing, consensus building, etc. has yet to be achieved at the level of policy makers.

The most striking fact about the Romanian government is the lack of a strong coordination unit of policy making with the following consequences:

- laws and regulations approved but not implemented because of lack of money; draft laws sent to Parliament without any evaluation of impact on the fiscal deficit;

- everything is a priority and the government hesitates to identify and eliminate programs of lower priority to meet its financing constraints. Actually, the government does not have a clear process for identifying priorities and eliminating lower priority commitments. The government attempts to cover everything and prioritize at the level of budget execution based on the "bargaining power" of local and central authorities;

- the cross-conditionality built into the agreements of Romania with the international financial organizations is the main instrument for coordinating economic policy and setting priorities.

The coordination unit of policy-making should support the government to meet the following tasks: (i) identify and analyze problems and elaborate proposals on priorities; (ii) define the policy alternatives for the identified priority problems ; (iii) monitor and evaluate the results of policy implementation.

2.4. Build a Civil Service Corps (CSC) that Is Highly Professional, Motivated and Accountable

The public institutions give force to laws and regulations. The central and local public administrations must translate visions and policy statements into priorities, options, strategies and action plans. The quality of CSC determines the effectiveness and efficiency of these institutions.

Ten years of transition in Romania are also ten years of depreciation in the quality of the CSC. The following three facts are relevant:

- In 1999 the CSC does not have a status approved by Law. The main negative consequence is that the CSC has become the target for politicians' abuse. In the last years, the new "concept" of "algorithmic manager" has been applied at almost all levels of public administration management jobs. That means managers in public administration are appointed based on political allocation of management jobs in each public institution, according to the structure of the political coalition in power and negotiations among the political parties. Unfortunately, this "concept" has been extended to the most important state enterprises. Many of these "algorithmic managers" proved to be incompetent and/or corrupt;
- The CSC is poorly paid, unaccountable and unmotivated because of lack of incentives. As expected, the best specialists left the CSC. At the high levels of public administration, the CSC lacks experts in policy analysis, and it has a culture of institutional isolation (i.e., officials do not share information). People have the perception that, too often, a real debate on policy issues based on arguments is replaced by "deals" between different political forces;
- Incentives for corrupt behavior (use of public power and resources for private interests) are high because many public officials have wide discretion in implementing laws and regulations, and yet they have little accountability. Too often, politicians and CSC have accepted to be in positions of "conflict of interests". These laws and regulations change frequently and in an unpredictable way;
- The slow progress of reform in the public sector has increased the weaknesses of the CSC because of uncertainty and discretionary power of political leaders and ministers in the CSC.

Therefore, to strengthen the effectiveness of the CSC, Romania should achieve two main objectives. The first one is to protect the CSC against abuse by the politicians. This requires the approval as soon as possible of the CSC's status. The Status Law of CSC should be implemented before the local elections in spring 2000, in order to prevent a new round of "algorithmic managers". The status of CSC should solve at least three problems: (a) identify the public jobs which may be run by politicians and the public jobs which are professional; (b) introduce a merit-based recruitment and promotion system; and (c) define the concept of "conflict of interests" in the public sector and establish means to prevent it.

The second objective is to accelerate the reform of all public sectors -- education, health, defense, police, central and local administration, social insurance system etc. -- according to the new role of the state in a democracy and market economy. Most of these sectors cannot deliver the required public goods because they are not fully funded and the only way to remain within a sustainable fiscal deficit is through reordering of priorities, and not across-the-board cuts in expenditures.

2.5. Cooperate with the Mass Media to Build Consensus for Reform and Obtain Feedback

Implementation of any reform which concerns the population can be effective only if it is understood and supported by the people. Today, due to progress in communication, mass media offers the most powerful way to achieve this objective.

In Romania, the communication between policy makers and the population through mass media has lacked adequate transparency and consistency. Too often, politicians have tried to use mass media to build up their own public image instead of promoting the goals, strategies and responsibilities of their institutions. Policy makers from the same government have sent contradictory messages on the same issue to the media because of their different political interests. The abuse of Ordinances issued by the last governments did not allow any room for building the support of the population through mass media.

To improve communication with the mass-media, policy-makers should promote and debate major decisions prior to their implementation, and they should keep communication transparent and consistent.

Taking into account the fact that during transition the speed required and the challenges are greater than in a society with a stable social system, policy makers may use media information in the policy making process. In transition, a policy-maker’s only source of information should not be governmental bodies with their slow and biased process. Rather, policy-makers should have access to quick and varied information, and the mass media can provide this. In order to use mass-media information in policy making, policy-makers should keep in mind that quick information can be misunderstood or unimportant. The policy-maker needs to expose the bigger problem behind the soundbite.

3. Conclusions

In transition, there are objectives and strategies which have to be pursued by different governments with different ideologies during several electoral cycles in a consistent and comprehensive way. Stop-and-go policies and partial reforms will fail.

Policy-makers should strengthen their capability to formulate, coordinate and monitor the implementation of good policies over a longer period of time. Government actions cannot be limited to agreements with the international financial institutions because their agenda does not and cannot cover all important problems in a country.

Governments should increase participation of stakeholders in policy making, because reform is for the benefit of the people. Participation of Romania in the comprehensive development framework pilot program is a great opportunity to involve people in policy-making.

A strong coordination unit of policy making is a must for the Romanian Government. The main job of this unit is to help policy makers to formulate, coordinate, and monitor implementation of the policies.

Only a civil service corps which is highly professional, motivated and accountable can support the policy-makers to translate visions and political statements into priorities, strategies and actions.

Reform may be successful only if the people will understand it and support it. The mass-media is a powerful way to communicate with the people and policy-makers should improve their cooperation with the mass media.

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