

# Romania

<b>Status Index</b> (Democracy: 8.20 / Market economy: 7.57) <b>7.89</b>		<b>Management Index</b> <b>6.33</b>	
<b>HDI</b>	0.792	<b>Population</b>	21.9 mn
<b>GDP per capita (\$, PPP)</b>	7.277	<b>Population growth<sup>1</sup></b>	0.1 %
<b>Unemployment rate</b>	N/A	<b>Women in Parliament</b>	10.9%
<b>UN Education Index</b>	0.89	<b>Poverty</b>	N/A
		<b>Gini Index</b>	30.3 (2002)
Source: UNDP: Human Development Report 2005. Figures for 2003 unless otherwise indicated. <sup>1</sup> Annual growth between 1975 and 2003.			

## A. Executive summary

Since 2003, Romania has made substantial progress toward completing economic and political transformation. However, as the likelihood of the postponement of EU accession to 2008 indicates, some deficits persist. Politically, the Iliescu presidency and the Nastase governments have been characterized by stability and enhanced efficiency. The political decision-making process, however, has been marred by state capture and corruption, particularly evident in connection with the elections of late 2004. Caught between the urgency of EU acquis implementation and the cumbersome procedures of the legislative, the executive (both the Nastase and the new Popescu-Tariceanu governments) has developed an overly strong tendency to govern by ordinances. As the government crisis of July 2005 on the EU-driven reform of the judiciary indicated, this problem persists. EU integration, however, has become an agenda shared by all major parties.

While Romania is considered to have a market economy, its functioning is hampered by a substantial informal economy, and by the state's strong role in the national economy. Over the past few years, Romania has achieved substantial and continuous economic growth. However, growth has been unevenly distributed. Rural poverty linked to subsistence agriculture has been a negative factor in socioeconomic cohesion. One of the largest in Europe, Romania's agricultural sector employs one-third of the labor force for 13% of GDP. Positive trends include the declining trade deficit, the reduction of bad loans and the consolidation of the financial sector as well as the introduction of a 16% flat tax by the new government. Thus, the state's obstructive role is decreasing and the state is being redefined as a facilitator rather than controller of market processes. Xenophobic nationalism constitutes the primary form of extremism in Romania today. The Greater Romania Party (PRM) is the main advocate of rightist populism. Despite the popular support for extremist parties and movements rooted in socioeconomic frustration or the mobilizing appeal of xenophobic nationalism,

Romania has shown signs of change by introducing an anti-discrimination policy and awareness campaigns regarding the long-taboo topic of the Holocaust.

## **B. History and characteristics of transformation**

Historically, Romania is characterized by the modernization deficits in the southern and northeastern regions, under Ottoman domination until 1878, and the more modern, urbanized economy of the western and northwestern regions, until 1918 under Habsburg rule. The modernization of the unified Romanian state in the interwar period was a political and economic modernization in dependency, a process that continued the trend initiated in the mid-nineteenth century. Western models of statehood, democracy, and market-economy were grafted on a Romanian society rooted in qualitatively different traditions. The result was a quasi-democracy dominated by a small political and economic elite neither representing wider societal interests nor having internalized the concept of people's sovereignty. National mobilization became a substitute for modernization and an integrative strategy.

Despite a breakthrough strategy after communist takeover in 1945-1947, in retrospect the regime only perpetuated some of the deficits of the pre-war period, especially during the last decade of Ceausescu's rule. Again, an external model of modernization was grafted upon a Romanian reality. Political elites continued to perceive the state and the bureaucratic apparatus as property rather than a policy instrument, resulting in rampant nepotism, etatism, and simulated reforms – even in the more liberal decade after 1965. By the early 1980s, the combination of an autonomous foreign policy and Stalinist approaches to modernization and domestic control had run its course and ended in nationalist mobilization and economic decay.

Lacking an outspoken and influential opposition – partly because the Ceausescu clan monopolized national(ist) mobilization and repressed any organized dissent or independent voice within the party – the revolution of 1989 was essentially a power struggle among different segments of the nomenclature rather than the promising beginning of political transformation. Thus, although Romania was the only country in Eastern Europe to witness a violent end of communism, the net outcome was generally rated as more of a “palace revolution” within the nomenclature than a clear break with the past. Being highly distrustful of market economics and pluralist democracy, Romania – facing some distinct disadvantages in comparison to most of the other East European EU accession states, increasingly fell behind in the reform process.

When the democratic opposition finally won the presidential and parliamentary elections in 1996, the expectations were correspondingly high. The new regime of

President Constantinescu and the Democratic Convention of Romania, however, failed to make inroads in economic transformation and their strategic management was generally rated as poor. In 2000, they lost the presidency and the parliamentary majority to Ion Iliescu and a minority government of the Social Democratic Party led by Adrian Nastase with the support of the opposition Democratic Union of Hungarians in Romania. Thus, those who had taken over power after Ceausescu's ouster in the December 1989 revolution are back in office. The amateurish politics of the 1996-2000 tenure of President Constantinescu and the center-right Democratic Convention created a sense of reform fatigue and political disillusionment among the electorate, as well as a broad impression of policy failure, only partially justified.

Whereas many politicians from the first and second Iliescu presidency (1990-1996) returned to power in 2000, "sadder and wiser" after four years in opposition, most political parties now feature a younger management for the first time since the revolution of December 1989. The stability of the political system, however, is deceptive and based on shrewd control and clientelism rather than a culture of constructive policy-making. Simulated reforms, etatism, nationalist rhetoric, and blurred distinctions between the state, parties, and private still run high in Romania. Overall, the new leftist government did better than most analysts expected, probably because popular expectations were at a all-time low and because the process of EU integration nevertheless provided much-needed assistance as well as the basic framework and incentive for reforms.

The Romanian economic transformation process of the past 15 years has suffered from some disadvantageous initial conditions, erratic management, and wavering popular support for economic and political transformation. The size of the national economy with the predominance of poorly mechanized agriculture, on the one hand, and run-down obsolete industrial complexes, on the other hand, have made transformation particularly challenging. Specifically, Ceausescu did his country a very bad service by striving for autarky by paying off foreign debt at the expense of domestic consumption and investment in capital goods.

Governments' reluctance to implement reforms that would make them unpopular because of transition hardships, price liberalization and labor reduction has produced legacies of bad credits, backlogs in large privatization and pseudo-employed workforces. The changes of government and the absence of a coherent concept with enough public and political backing have resulted in erratic transformation policies, especially in privatization with ever-changing laws and institutional set-ups, that made both the Romanian population and international investors extremely wary. Overall, the hesitation in thorough transformation has been self-defeating by losing the initial momentum domestically, not being competitive for most Western investment decisions for the former Eastern Block and thus depleting the critical resources for constructive policies.

The EU eventually decided to open accession negotiations with Romania in 1999 because of its stabilizing role in the Balkans and as it reportedly fulfilled the basic criteria of political democratization, while failing to meet the criteria of transition to a market economy. Romania remains the slowest of the accession states and from today's perspective, accession in 2007 seems a *fait accompli* not the least because of Brussels' unwillingness to decouple the accessions of Romania and Bulgaria. Bulgaria's reform results are rated higher and in the case of Romania, serious doubts remain, but fear of a (nationalist) backlash and weighing of the bureaucratic complications of separate accession dates for Bulgaria, Romania and Croatia seem to have fixed Romanian membership for January 1, 2007.

### **C. Assessment**

The period January 2003-January 2005 concerns the Iliescu presidency and the Nastase government. Current President Traian Basescu was sworn in on December 20, 2004 and the new Popescu-Tariceanu government was installed on December 29. Their outlook has been included in the trends section, but not in the assessment of the state of affairs in democracy and market economy.

Assessment

#### **1. Democracy**

##### **1.1. Stateness**

The last major challenges to the state monopoly on the use of force occurred with the marches of the miners from the Jiu Valley to the capital in 1990-1991. As smaller outbreaks of violence in 1997 and 1999 indicated, the Jiu miners still constitute a potential veto power of some kind. Indirectly, the successor organizations to the notorious Securitate seem to be reticent regarding political control and public accountability. Conversely, the army is no longer a potential veto power, despite deficits in civil-military control. By historical tradition, the Romanian concept of the nation is defined strongly in ethnic terms. A civic concept including the strong Hungarian and Roma minorities has thus far failed to find acceptance beyond formal legal texts. The initiation of a Roma Inclusion Plan is a positive action to counter widespread stereotypes and practices of discrimination.

The Romanian Constitution provides the normal guarantees of liberal constitutionalism and defines the nation in ethnic terms ("national sovereignty resides with the Romanian people"). Support for nationalist-extremist, openly anti-Semitic and xenophobic parties and movements indicates that public

perceptions of citizenship may be disharmonious with the constitutional stipulations. However, the state's constitution and the official citizenship are not directly challenged. Rather, political rhetoric and day-to-day practice deviate substantially from legal concepts of the nation and civil rights.

Romania has no law on religions, but, apart from the "national" Orthodox Church, fifteen churches have been recognized as "official" religious associations. Since the end of communism, the Orthodox Church is again independent from politics and conversely religious dogma has no impact on state policy-making. The introduction, during the Constantinescu administration, of mandatory religious education in primary and secondary schools has not been subject to much debate, and nor has it made much practical difference since compliance is mostly formal. However, recent conflicts indicate that the separation of state and religion is not absolute. Nevertheless, the Romanian Orthodox Church's insistence to be recognized as the privileged denomination blocked a new law on religions for more than five years since 1999. Up until then, the 1948 law on religious domination remained valid and allowed for substantial state control.

Partly because of the existing communist administrative structures, Romania has reformed state institutions since 1989 and increasingly with EU assistance and guidance: The administrative structures and resource allocation cover the entire country.

## **1.2. Political participation**

Romania elections in the 2003-2005 period were generally rated free and fair and include the June 2004 local and the November 2004 parliamentary and presidential elections. No relevant restrictions of suffrage exist and no groups are barred from executing their passive or active electoral rights. Nevertheless, the principle and practice of democratic elections are not fully installed and internalized as the 2004 elections indicate. Controversies over candidate lists before the elections, and accusations of electoral fraud, still tend to overshadow the democratic process ; this is irrespective of the validity of the fraud claims and the justification of disputes over candidates.

Democratically elected rulers do have the effective power to govern. As such, no political enclaves exist, although some interest groups and stakeholders have demonstrated disproportionate political influence and may be considered to have limited veto powers. Both managers from state and private corporations ,and trade unions, have the power to block reform processes. Thus, Romania ranks high in indices reporting on state capture.

The Romanian 1991 Constitution provides the usual political and civil liberties, including freedom of expression, association and assembly. The government has

demonstrated some inclination, by a variety of direct and indirect instruments, to curtail these freedoms beyond the formal rules. Since early 2002, various government measures, decrees and draft laws originating in parliament have produced a consistent pattern of action aimed at curtailing freedom of speech and association, individual rights and personal privacy, blocking NGO and public influence on government, and waylaying transparency. At the same time, some checks and balances in the system, for example, the ombudsman or the judiciary, have been strengthened. The previous excessive use of emergency ordinances has been curbed somewhat through the reform of the legislative process in the revision of the constitution in October 2003.

Romania's Freedom House rating for independent media indicates structural deficits. The plethora of media outlets, especially newspapers, of early post-communist years has been drastically reduced by competition for funding, advertising, etc. Due to increasing prices, the cumulative circulation of major newspapers has decreased significantly after the boom in the early 1990. Nevertheless, in newspaper and even in radio and TV broadcasting, a competitive landscape has emerged. However, the government keeps strict control over audiovisual media, e.g. directly via state-owned TVR or media-regulation bodies, but also indirectly via hidden subsidies or private media's tax debts. Consequently, political partisanship is a common phenomenon and criticism of state policies is muted or confined to niche-market channels.

Beyond the constitutionally defined freedom of expression and press freedom, the government has been inclined to curb media freedom: by threatening a press law, or via generous and arbitrary application of the laws on libel (of public officials), and by the distribution of false information (provisions in the Penal Code). Local media in particular has been subjected to pressure in recent years by local party bosses who formally, or informally, control much of the local administration, control law enforcement agencies, and also influence courts. Recent scandals, involving the wire-tapping of news agencies involving the then-ruling PSD party, and also ongoing investigations concerning radio and TV censorship, are more than party politics after elections. The Romanian Media Monitoring Agency particularly criticized radio and TV coverage of the last elections.

In sum, neither party nor corporate actors have demonstrated fundamental qualms about the freedom of the press in those cases where the results contravened their interests. Despite persistent international pressure and criticism, there remain legal stipulations that can be abused easily in order to curtail the practical freedom of the press. However, at the same time in June 2004, slander, an oft-used instrument against unwelcome media criticism, was removed from the Criminal Code.

### **1.3. Rule of law**

State powers in Romania are independent and checks and balances in political power are stipulated in the constitution. The government, however, has demonstrated a tendency to consider the protracted and partly redundant legislative procedures of the two chambers of parliament “obsolete.” Thus, there is a substantial tendency to rule by emergency ordinances that only require retrospective, legislative approval.

Although an independent judiciary exists in Romania, the annual EU Progress Reports have repeatedly pointed to structural weaknesses. In Romania, the public identifies customs officers, the police and members of parliament as the occupational groups most likely to be involved in corruption. The public reputation of the judiciary as politicized and corruptible is partly substantiated by the number of penal cases brought against judges, and by the selection procedure by the minister. Politicians have been tempted on several occasions to violate the judiciary’s separation from political interference and paternalism; e.g. by making public statements on legal cases prior to the court’s verdict. Political interference in the judiciary is facilitated institutionally by the broad powers of the Ministry of Justice in appointing top magistrates, the bodies that supervise the functioning of judiciary, the daily management of courts and the total control over the office of prosecutor. Thus, the institutional separation of the judiciary is still incomplete and, where it exists, it only partly reflects political reality. The separation of powers was recently improved by reducing the minister’s say in the nomination of judges, thereby increasing the independence of the judiciary.

Efforts have been made to improve the anti-corruption institutional framework by the creation in 2002 of a special Anti-Corruption Prosecutor Office, with territorial branches. Legislation passed in 2003 that encompasses conflict of interest, declaration of personal assets and civil service issues may be regarded as a step forward. However, it contains a few “strategic loopholes” that allow dignitaries and civil servants to avoid real transparency in personal finance. Moreover, proper and consistent enforcement of such laws is always a problem in Romania. Scandals uncovered by the media are indicative of conflicts of interest involving politicians and private businesses, e.g. in connection with public procurement. Transparency International’s Corruption Perception Index for 2004 ranks Romania 87th of 145 with a 2.9 score.

A civil society campaign in the run-up to the 2004 elections is indicative of increased societal activism on the issue, but most of all of the widespread corruption and insensitivity on the part of politicians. The change of government has unveiled some potentially serious cases of corruption, e.g. multi-million state contracts with Western firms without tender. The abolishment of a law granting immunity from prosecution for former ministers is a positive development and a

step toward a culture of transparency and accountability. Overall, however, the EU Progress Report repeatedly identifies corruption as a major flaw in Romania's transition process that might even threaten EU accession. The latest reform in April 2004 of anti-corruption mechanisms failed to resolve the problem that false, or incomplete, declarations concerning conflicts of interest are neither monitored nor sanctioned. This was demonstrated by the NGO campaign before the November 2004 elections.

Due to the quasi-revolution of 1989 and neo-communist continuities, violations of human rights under the Gheorgiu-Dej and Ceausescu regimes were not tackled comprehensively and purposively during the first decade of post-communism. Concerns about Romania's international reputation, particularly in response to European pressure, have induced the Iliescu/Nastase regime to address specific issues more seriously. These issues include a collective and historical rethinking of the country's communist history. Initiatives by NGOs and internationally-supported academic organizations played a crucial role in this process. Concerning the long-taboo issue of the Holocaust in Romania, the previous government has installed a commission, received a highly critical report and begun teacher trainings on the topic. A Holocaust commemoration day was introduced in the national calendar.

#### **1.4. Stability of democratic institutions**

In spite of the EU-style Civil Service Law passed in 1999 (a condition for having Romania included in the enlargement process at Helsinki), the hiring of obedient staffers and clients has continued to politicize the state administration, to the detriment of political neutrality and administrative functionality. In civil service, the rule of the game is still personal loyalty, not performance. The very size of the state administration, the high fragmentation and volatility of public institutions in Romania have produced counterproductive friction. These, and a lack of functional cooperation between central ministries and agencies continue, and are directly related to, the hegemonic attitude of the executive. Deficits in administrative institutional capacity are still a spearhead of EU criticism in the 2004 Progress Report.

The nationalist-extremist wing of the political spectrum is not fundamentally committed to the democratic institutions. External and domestic constraints exclude a fundamental reversal of democratic order, but political attitudes and public opinion point to a certain preference for an authoritarian governing style. Recent surveys, however, indicate that these preferences are waning and democratic awareness is increasing.



### **1.5. Political and social integration**

As the last elections in 2004 indicate, between elections there is still substantial fluctuation of parties, leaders and electoral choices. The number of parties participating in parliamentary elections remains high, but the profile of the main contestants seems to be consolidating with a more pronounced political program and basis in society. The PSD dominates the left wing; whereas the center-right might be consolidating into a new party emerging from the victorious electoral coalition PNL-PD of 2004. Right-wing votes are increasingly concentrated on the PRM. Polarization within the political spectrum is high as (unlike in Central Europe) the dichotomy between “former communists” and “democratic opposition” largely perpetuates itself, despite the rise of a nationalistic right. Whereas the SDP is particularly strong in the rural and poor regions of the northeast and south, the constituency of the democratic opposition is concentrated in the cities and more affluent provinces. Despite regular splits and mergers, the main parties are stable, voter volatility notwithstanding. A typical problem of instability concerns the mobility of elected functionaries between elections for opportunistic reasons; e.g. elected majors gravitating towards the (nationally) ruling party.

Civil society is equally fragmented and feebly rooted in society, as it is often perceived as elitist. Nevertheless, the impact of NGOs is growing: A number of well-placed (i.e. in relation to the international community) NGOs have been able to exert substantial and beneficial influence on government policy-making in recent years. A few of them have established themselves as functional think tanks or human rights organizations. A 2001 law regulates the status of NGOs “of public utility” as well as their tax exemptions and reductions. However, in an attempt at over-regulation, the law prescribes government approval for their registration. A subsequent law passed in 2003 extended this restrictive procedure of registration to all civil associations, public utility or not.

The government has been compliant to the desires of particular interest groups representing their clientele, e.g. especially trade unions, state industry, or a few well-connected business groups. A number of nationalistic, xenophobic, and extremist organizations have found mass appeal and thus undermine civil integrity and democracy. Conversely, the Hungarian minority has demonstrated a high degree of ethnic organization and their civil organizations have largely been constructive actors.

Recent surveys have shown a marked decrease of the part of the electorate that would sacrifice democracy to a “government with the right policy.” The increasing reputation and trust in NGO and other civil society organizations also indicates the consolidation of democracy as a principle rather than a mere procedure.

Lacking a strong civic tradition, both NGOs and voluntary non-profit organizations are still largely an urban phenomenon. In 2001, a special law was adopted to promote voluntarism and social self-organization. Network density and participation remain weak, however.

## **2. Market economy**

### **2.1. Level of socioeconomic development**

Social exclusions in Romania are a dominant rather than a marginal phenomenon. As education encompasses most of the population (adult illiteracy 2.7% and UNDP Education Index 0.88 for 2002), the key factors of exclusion are poverty and gender. In the UNDP's gender-related development index (GDI) Romania ranks 56th (0.775 for 2002), the ratio of estimated female to male earned income is 0.58 for 2002 and the Gini coefficient for earnings inequality is 30.3 (2000). Rural poverty linked to subsistence agriculture is a negative factor in socioeconomic cohesion. The mismatch in the sectoral distribution of GDP and labor force, however, is telling: Agriculture accounts for almost 13% of GDP and employs some 34% of the labor force; industry 31% and 26%; construction 6% and 5%, services 49% and 35% (2003). The proportion of the population earning less than \$4 a day (1990 PPP USD) for 1996-1999 reached 23% and according to the EBRD, 20.5% of the population lives in poverty (EBRD 2000).

### **2.2. Organization of the market and competition**

A substantial informal economy and the state's powerful role in the economy hamper a viable market economy in Romania. However, the institutions of a market economy are in place and include the freedom of trade, currency convertibility, etc. In 2004, the share of administered prices increased to 22.5% and in 2003 budgetary transfers and subsidies still amounted to a stable 14% of GDP.

While formal regulations prohibiting monopolies exist, implementation has failed to prevent quasi-monopolies (partly by state-owned companies) from developing in key sectors of the economy, e.g. in energy and banking. Moreover, some early entrants on the market at the beginning of the 1990s have secured preferential treatment and tend to oppose today the complete liberalization and transparency of markets and state allocations. The December 2003 amendments to the competition law and the strengthening of the role of the Competition Council vis-à-vis political influence have improved the framework for combating monopolies. The

degree of state capture, however, continues to waylay effective anti-monopoly policies, as some of the recent scandals indicate. The EBRD index of competition policy remained unchanged at a low 2.3 since 1998.

The EBRD index of foreign exchange and trade liberalization has risen from 3.0 in the early 1990s to 4.3 in 1998 without any progress since. The EU-15 has long become Romania's primary trading partner. In 2003, the EU-15 accounted for 62% of total Romanian trade – an increase of almost 10% in turnover within one year. Due to the improved competitiveness of Romanian agricultural products, the trade deficit declined. Overall, non-transition countries account for 83.9% of foreign trade (2003) and the share of tariff revenue in imports is down to 1.7% (2003), whereas the share of trade in GDP has recently risen to over 70%.

As a positive trend, bad loans have been radically reduced over the past few years and the financial sector has consolidated while stock-market capitalization and domestic credit are beginning to grow. Thus, the EBRD indices for banking sector reform have moved up a notch for the first time in five years in 2004, from 2.7 to 3.0 (whereas the index and other financial institutions have failed to improve on the 2.0 achieved in 1998). Domestic credit to the private sector is on the rise and the National bank has accordingly tightened controls and regulations to avoid soft loans. The percentage of non-performing loans has gone down from almost 60% in 1998 to 3.8% in 2000 and 1.6% in 2003. The introduction of a credit bureau to monitor the credit risk of consumer loans in August 2004 constituted another improvement. Only two major state-owned banks remain: 21 out of 30 banks are foreign-owned, but in 2003, 40% of assets were still held by state-owned banks.

### **2.3. Currency and price stability**

Controlling inflation, an independent central bank and foreign exchange policy have improved over the last two years. With new business legislation and increased financial discipline, inflation reached 15% in 2003 and 2004, one third of the level in 2000.

The government's budget balance (-2.4% of GDP in 2003, -1.6 in 2004) underscored the Nastase government's sincere and partly successful efforts to curb the deficit and increase Romania's credibility with international financial institutions. Government expenditure has been reduced via small steps from 35% of GDP in 2000 to 32% in 2003.

## **2.4. Private property**

2003-2004 marked a significant upsurge in the political will of the leadership and concerted effort to stimulate the business environment by improving tax legislation (bankruptcy law), enhancing the judiciary's independence and reducing bureaucratic red tape. The new government's decision to immediately introduce a 16% flat tax also illustrates an attempt to reduce the state's obstructive role and redefine it as a facilitator, rather than a controller of market processes.

The private sector meanwhile accounts for 70% of GDP (2004), up from 55% in 1996, and 75% of employment (2001). Accordingly, the EBRD ratings for small- and large-scale privatization are not impressive; 3.7 and 3.7 respectively. The management of privatization has been highly erratic. Small-scale privatization was initiated in 1991/1992 with a voucher system, followed by a new law and a second voucher round in 1995, large-scale privatization in 1997, and yet another privatization law in 1999. In 2001, the Nastase government upgraded the State Ownership Fund to ministry status (Authority for Privatization and Administration of State Assets, APAPS) with a corresponding new privatization law (April 2002). In agriculture, the protracted process of land restitution, structural regional differences and a multitude of decentralized privatization regimes have further complicated the consolidation of private-sector production. Yet, the privatization of a number of major state-owned enterprises in the energy sector in 2004 improved the overall balance.

## **2.5. Welfare regime**

Organized by the state, social security covers all relevant risks in principle. As the high poverty rate indicates, social security functions on a subsistence level throughout the country. Similarly, health care is available for all citizens throughout the state territory, but is insufficient, especially in rural settlements. More importantly, social disparities and inequality in access to health care and basic services are increasing rather than decreasing.

Romanian society retains elements of heterogeneity and discriminatory access. Education, basic social security and health care offer limited compensation for social differences. Egalitarian attitudes are widespread in the state-provided services, but a lack of resources is paramount. In the long run, the main threat to state welfare services is represented by a gradual depletion of assets due to poor policies, the government's lack of analytic and feedback capacity, indecision in applying necessary but painful remedies and periodic outbursts of populist commitments. The UNDP Gender Empowerment Measure (0.465) and other relevant indicators are lower than in comparable East Central European Countries,

e. g. with a 0.46 to 1 gender ration of average earned income. The adoption of a National Action Plan for Equal Opportunities might mark the beginning of new thinking in this field.

## **2.6. Economic performance**

GDP growth rates have been substantial (5-6%) for the past four years. Due to budget deficits, unemployment, external debt and the current account deficit, as well as persistent backlogs in structural reforms, the sustainability of growth is far from assured. Control of macroeconomic trends has definitely increased, but the foundation of the market economy remains weak due to structural reforms ahead and flaws in other macroeconomic factors.

## **2.7. Sustainability**

To some extent, environmental hazards have been reduced by de-industrialization, but air pollution due to industry is still significant in some cities and in the Northwest. The Danube delta wetlands are threatened by water contamination. Although Romania has managed to close negotiations on the relevant *acquis communautaire* chapter, the implementation of EU environmental protection standards remains minimal in practice, as indicated by the 2004 Progress Report.

In order to counter the effects of a brain drain, some efforts have been made recently to improve R&D and higher education in the IT sector. Overall, state funding for higher education and research investment is far below the European or ECE average. The unchecked proliferation of private institutes for higher

education, without the necessary regulatory framework, has worsened the situation. Thus, R&D accounts for merely 0.4% of GDP (1996-2002) and education for 3.5% (1999-2001) of GDP.

## **3. Management**

### **3.1. Level of difficulty**

Several factors in various fields combined to constrain policy options for transition management in Romania during the 2000-2005 period. The prominence of subsistence farming in Romania acts as a key socioeconomic constraint, as does the sheer size of the country with its relatively low degree of urbanization and strong links between smaller cities and rural areas. Forced industrialization in the

1950s and 1960s and the austerity policies of the 1980s have produced non-viable and run-down heavy industry. Weak infrastructure adds to the structural obstacles to socioeconomic transition in rural areas. The absence of a clear political break from and disavowal of the communist nomenclature in the management of agricultural and industrial enterprises have left an unfortunate legacy. The apparent lack of a viable alternative was perpetuated by the utter failure of the democratic opposition's interregnum 1996-2000.

The continuity of a strong xenophobic nationalist tradition from communism to post-communism has increased conservatism and popular resistance to reforms. Unlike, for instance in Bulgaria, the strength of the nationalist-extremist political wing has distorted the "normal" dynamics of a neo-communist versus democratic-reformist bipolarity. On the one hand, the prospect of EU membership and the process (including guidance and assistance) of accession since 1999 has stimulated the reform process. However on the other hand, the deeply ingrained tradition of simulated reforms and state capture on the part of the state, and the structural skepticism and subversion of the population vis-à-vis state policies, have at times brought the reform process to a virtual standstill.

Civil society traditions are weak, with a small number of active and sustainable NGOs and a much-reduced participation in public life and voluntary associations. Despite reforms driven by EU accession, institutional stability and the rule of law still suffer from significant deficits. In contrast to Bulgaria or Serbia, the anti-intellectualism of Romanian communism regarding active, competent NGOs and think tanks was pronounced.

Ethnic Hungarians constitute the main ethnic minority and despite their involvement in each government since 1996, the potential for ethnic conflict remains high. However, it is currently subdued despite the electoral strength of extremist-nationalistic parties. Nationalist parties' virulent racist and aggressive propaganda finds however resonance among significant sections of the population. Nevertheless, ethnic divisions do not predetermine politics.

Whereas religious antagonism is insignificant, the potential for social conflict is much higher because of the high poverty rate. Further income disparities are bound to aggravate these social tensions. The Roma population's social rather than ethnic problems, including widespread discrimination, exacerbate these tensions. The National Council for Combating Discrimination (February 2004) was a nominal improvement and communicated an important signal via its public awareness campaigns. The same is true of the 2001 Roma Strategy to counter the de facto discrimination of this 2-2.5 million minority population.

### Profile of the Political System

Regime type:	<i>Democracy</i>
System of government:	<i>Semi-presidential</i>
1. Head of State:	<i>Ion Iliescu</i>
Head of Government:	<i>Adrian Nastase</i>
Type of government:	<i>single party minority</i>
2. Head of State:	<i>Traian Basescu</i>
Head of Government:	<i>Calin Popescu Tariceanu</i>
Type of government:	<i>coalition minority</i>
<p>Source: BTI team, based upon information by country analysts, situation in July 2005. Constraints to executive authority (1-6 max.) measures the institutional votes gained by party <math>i</math>; <math>p_i</math> is the share of parliamentary mandates controlled by party <math>i</math>. For presidential/ semi-presidential systems, the geometric mean of <math>p_i</math> ministries/ ministers denotes the situation on 1 January 2005.</p>	

### 3.2. Steering capability

The outgoing government demonstrated reasonable reliability and capability regarding reform, but regularly backtracked on strategic priorities for reasons of political expediency and because of interest-group pressure. The one-party government performed better than previous center-right cabinets by projecting an improved image abroad as one competent team, although genuine change lagged behind. Nevertheless, the years 2003 and 2004 have seen a substantial increase in legislative action (less so in effective implementation) in a number of crucial policy fields: business environment, banking, tax regulation, devolution, etc.

Overall, a substantial part of the strategic reform drive, in terms of consistency and prioritization, is externally induced by international financial institutions and the EU. Typically, the government has shunned the short-term costs of restructuring, privatization and increases in utility prices. Thus, some reforms have been implemented only partially and other measures necessary for a coherent policy have been omitted. A substantial part of enhanced policy-making activity is produced hastily, without coordination and coherence between ministries and sometimes without realistic feasibility checks. The introduction of preparatory meetings before cabinet decisions improved this situation in 2004. The same applies to an improvement in the higher transparency of draft laws and the political decision-making process.

Responsiveness to mistakes has certainly increased, responsiveness to input and pressures from society and NGOs less so. The degree of state capture constrains government flexibility in modifying or redefining harmful policies. Learning

processes did occur, but the number of truly innovative directions or the coherence of the overall policy framework remained minimal, compared to other more advanced transition countries.

### **3.3. Resource efficiency**

Government funding for strategic priorities, such as developing human resources in higher education, has been below average. The health care system does not function properly due to misallocations in funding basic health care for all citizens, which is related to the existence of powerful rent-seeking groups. Deficits in the state budget and tight international financial institution conditionality have prevented massive investment in transformation relevant services. An overly controlling state has provided disincentives to foreign direct investment by creating bureaucratic hurdles. Recent measures to improve the training, quality, remuneration and overall professionalism of public administration certainly constitute a step forward in this area.

Effective use of state resources for political and economic modernization is hampered by the non-transparent influence of interest groups and the politicization of state positions. Both lead to the misuse of human and financial resources as well as reduced strategic consistency and reliability. Two telling indicators are Romania's 2.9 rating and its rank of 87th of 145 in the 2004 TI Global Corruption Index, and the frequent habit of staff replacement by party-political motives in neutral state institutions. This has included the reinvention of entire institutions, with the corresponding loss of institutional memory and efficiency. The government carries out some of its announced reform projects, but backtracks on some of its other electoral promises, strategic priorities, or the implementation of passed legislation.

The Transparency International ranking cited above, with a score of 2.9 on a scale from 0 to 10 is corroborated by other studies, including successive EU Progress Reports and national surveys. Until recently, the legal framework for the fight against corruption and against conflicts of interest, has been insufficient. Implementation also remains deficient. State capture is a key negative factor in Romania's transition to a market economy. As noted in the introduction, some of the combined traditions of the interwar and communist periods have been exacerbated by post-communist transition: etatism, nationalist mobilization as a substitute for reform strategies, economic autarchy as an alternative to global integration, etc. The government has instrumentalized some of these negative traditions for political gain, while making only partial inroads on other stubborn legacies. European identities, and positive traditions or lessons learned in economic and democratic reform from the interwar period, are used for legitimization purposes rather rhetorically and uncritically.



### **3.4. Consensus-building**

Although the political establishment has accepted in principle the goal of a market-economy, a strong sub-current of etatism remains.

Coalitions with stakeholders holding leading roles in the state, economy, or authoritarian-style governance, have all reduced the purposeful and dynamic drive for reform. Reformers have thus far demonstrated limited control over actors with veto powers (e.g. state capture), who can delay or mislead the reform process.

The party landscape is to a limited extent representative of societal groups and cleavages. The government has not been able to reverse the trend of growing social and urban-rural disparities. The main Hungarian party's participation in government has helped diminish the ethnic divide; recent programs are intended to improve the integration and acceptance of the Roma population.

The political leadership has failed to make a priority of promoting social trust and solidarity. Clientelist networks rather than civic engagement play a dominant role in politics on all levels.

By upholding the key role of the state, albeit at a basic level, in most policy fields, the government promotes continued reliance on the state rather than societal engagement. Involvement of think tanks and NGOs resulted due to Western pressure, the increasing reputation/popularity of the organizations concerned, or the lack of in-house competence on the part of the state administration.

Due to the incomplete break with the Ceausescu past and the continued relevance of nationalist mobilization, reconciliation remains controversial more than a decade after the 1989 revolution. The political elite have not completed the process of reconciliation, as initiatives in this direction were hijacked by party politics.

### **3.5. International cooperation**

Political actors have used resources and advice offered by international financial institutions and international organizations—primarily those from the European Union—to invigorate the transformation process and overcome certain blockages. Conversely, unwelcome policies suggested by external parties have not been implemented, such as privatization, the fight against organized crime or state policies on reforming the public administration. The Nastase administration has demonstrated increased readiness to cooperate with the European Union and use

the prospect of EU membership to erode domestic resistance and focus on reforms, albeit less so than many other accession states. This is in part due to the strength of nationalist, anti-European sentiments.

Despite the fact that the general framework of the EU accession process has reduced the scope for alternative policies, Romania remains a relatively difficult partner for international donors and NGOs in an ECE comparison. There have been repeated examples of the government's reluctance to implement certain reforms and inclination to sidetrack the implementation of unwelcome policies. State capture and the high level of corruption have added to these risks.

In the process of NATO and EU integration, Romania has demonstrated increasing readiness to cooperate with Hungary and Bulgaria, and even Ukraine and Moldova. However, in many respects, especially in the case of Moldova, Ukraine and Bulgaria, regional cooperation is comprised of political declarations rather than the optimization of regional resources and synergies. Domestic resistance therefore easily halts cooperative initiatives on a multilateral and bilateral basis. Realism and restraint in managing sensitive issues in bilateral relations with Hungary (status law) or Moldova (e.g. basic treaty) has increased markedly, at least on the highest political level.

#### **4. Trend of development**

##### **4.1. Democratic development**

Romania's 2003-2005 development trends in electoral democracy are marked by electoral events (local elections June 2004 as well as parliamentary and presidential elections in November 2004). In the broader sense of liberal democracy, the changing relationships of trust and respect between politics and society are paramount. Whereas there were no significant changes in stateness and the electoral process—serious allegations of fraud and media bias accompanied each election—the amount of trust between political actors and society seems to have decreased. Romania's Transparency International Corruption perception Index ranking may be read as an indicator of distrust in politics (rather than actual corruption). The recent scandal over the ruling PDR's highest-level involvement in quelling media criticism, and manipulating policy-making for party political reasons, reveals not only a serious lack of self-restraint and respect for the rule of law, but also for citizens' rights. Whether the new government's promises will result in a change of paradigm in terms of political culture remains an open question.

The years 2003 and 2004 marked a rush of legislative initiatives in several

important policy fields to improve consistency and courage in terms of fiscal discipline, business environment, devolution, etc. The gap between legislative and policy practice, however, remains profound.

#### 4.2. Market economy development

Macroeconomic trends for Romania are mixed. Recent IMF data for 2004 shows: 8.4% GDP growth, but 7.8% of GDP current account deficit and 9.2% inflation. Thus, robust economic growth over the past 3-4 years has brought interest rates and inflation down considerably. The fiscal deficit was brought under control and foreign reserves increased markedly. International competitiveness linked with the advantages of low labor costs have fuelled exports and foreign direct investment—doubled from 2002 to 2004 (estimate).

There are several caveats to the sustainability of these economic trends. First, foreign direct investment remains low in absolute per capita terms compared to other EU accession states. GDP per capita (2003) was at 47% of the average of the eight new member states of 2004, but foreign direct investment per capita at no more than 13% (2002) – closer to the level of Albania (11%) than to Croatia (22%). Despite the solid GDP per capita PPP growth of the past three years, the gap between Romania and the EU average has diminished from 70 to 67% only.

**Table: Development of macroeconomic fundamentals (2000-2004)**

	2000	2001	2002	2003	2004
Growth of GDP in %	1.8	5.3	4.9	4.9	5.8
Export growth in %	23.9	10.6	16.9	11.1	na
Import growth in %	29.1	17.5	12.1	16.3	na
Inflation in % (CPI)	45.7	34.5	22.5	15.4	11.9
Investment in % of GDP	19.5	22.6	23.5	24.6	na
Tax Revenue in % of GDP	31.2	30.1	29.7	30.0	na
Unemployment in %	10.5	8.8	8.4	7.2	na
Budget deficit in % of GDP	-3.6	-5.8	-3.4	-5.8	-5.6
Current account balance in billion \$	-1.347	-2.349	-1.573	-3.318	-3.764

Source: EBRD Transition Report 2004

#### D. Strategic perspective

Completing the EU accession process, which now seems a foregone conclusion, and the loss of international leverage vis-à-vis reform policies, constitute the key

challenges to Romania's political and economic transition. Deficits in administrative capacity persist, as do state capture, ingrained corruption, and the weakness of the judiciary. The international community must be more alert and inventive in supporting the new government to help sustain the momentum of the reform process. Such reforms include improving the business climate, completing privatization and reforming the pension system.

Romania will be unable to reduce poverty without international and EU assistance. Countering the increasing disparities between rural and urban areas (Bucharest vs. the remaining 21 million throughout the country, a more modernized Transylvania vs. the structurally weaker Moldavian and Wallachian regions) will also require international support. The ethno-political dimension of regional policy must be recognized in the distribution of EU structural funds. In Romania, as in most other post-communist transition countries, regional disparities and ethnic concentrations tend to overlap and thus increase the conflict potential for regional development strategies in terms of ethnic discrimination or preferential treatment.

Reducing rural poverty and improving the competitiveness of the vast agricultural resources of Romania would significantly boost not only the sustainability of economic transition, but also contribute to the maturation of the party political landscape and the actual functioning of democracy beyond electoral procedures.

Two other crucial reform projects also rely on well-targeted international assistance and guidance. The relative health care and education advantage inherited from the communist legacy is eroding with the next generation. Conversely, human capital is a key factor in economic competitiveness. The social welfare system is in need of a radical reform. Overly broad coverage inherited from communism makes the system socially ineffective, a burden on the state budget and a disincentive to private entrepreneurship and economic initiative. An optimized system covering real social risks for the weakest in society is a core issue in the overall Romanian reform process.