

THE EFFECTS OF ECONOMIC CRISIS IN ROMANIA

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Abstract: *After a 7.1 percent economic increase in 2008, Romania was concerned with the trust in 2009 and less expected that the current financial crisis that began in the U.S. and Europe already spread to produce severe consequences on the Romanian economy. The result was a return of 180 degrees in the economic situation, which demonstrated that the development model that followed until then, one based on consumption was unsustainable. Considerable drop in the volume of goods exports and tightening credit conditions have led more companies to restrict their activity leading to an accelerated increase of unemployment of around 60, among the highest in the European Union.*

Keywords: *financial meltdown, world crisis, economic decline, recession, real estate market, credit crisis, unemployment, inflation.*

1. International context of crisis

Current economic crisis is a no resemblance the Great Depression of 1930 here, is considered the largest in the last 70 years. Then the main cause that triggered the Great Depression, collapse of the banking system was just and that lasted a decade. Ironically now that it was all triggered by U.S. financial system crisis. Officially it was launched in 2007 with the bankruptcy of a powerful American companies home loans, American Home Mortgage and which has spread quickly to investment funds and to financial giants. U.S. housing market collapse was caused mainly by lower interest rates by FED, from 6.5 percent to 1 percent, in a period of only 3 months was practically an invitation to consumer credit and for people with high credit risks that normally would have been rejected by tougher rules on credit past. So the real value of homes was artificially inflated due to speculative resale made by a fund, tricked the banks that took over mortgage securities risk, also called subprime. If commercial banks were protected by tougher regulations in favor of debtors and creditors, investment banks have entered the free and irresponsible game of speculation and poor risk management. Housing crisis has spread rapidly and on credit cards, auto loans debts and then in industry. Falling financial giants like Lehman Brothers or are in danger of collapse. Bankruptcy of a bank entails destabilization and even bankruptcy of another. A bank shall borrow from one another for cash and bank finance institution itself. U.S. central bank intervened to provide liquidity banking system daily injecting billion in an attempt to avoid bottlenecks markets. The largest investment companies in the U.S., Goldman Sachs and Morgan Stanley have abandoned their status to survive the financial crisis for the U.S. government created a rescue plan worth 700 billion dollars. Federal Reserve approved the transformation of the two companies to invest in bank deposits under the jurisdiction of the Central Bank and passing the two banks under strict supervision. Major financial institutions around the world were on the verge of becoming insolvent. The actions of governments in the United States, Europe, Japan and China, which have injected huge amounts of liquidity to support these institutions, the collapse was attenuated.

The failure of the financial system, as seen by Joseph E. Stiglitz "gives birth to a vicious circle: banks reduced their financing activities, and causing firms to reduce production, which leads to lower overall production and revenues. As the decline of the latter, profits are shrinking, and some companies are forced to go bankrupt. When companies declare bankruptcy banking situation is worse, they further reduce financing activities, accelerating economic decline".[1]

The effects of U.S. financial collapse had global repercussions and. Financial problems have affected large sectors of the economy resulting in decreased growth rate. International trade have witnessed unprecedented steep decline by the end of 2008 and early 2009. Economic decline occurred simultaneously in the countries of the world, and a drastic reduction in international trade has helped to amplify the adverse impact of the turmoil in financial markets and endanger the integrity of global economic systems. The European economy is also badly affected by the slowdown of world economy, the reduction of confidence in the financial system and tighter financing conditions. Wave economic crisis has reached Europe after four to five months after its birth in the U.S.. It strikes one by one European economies and the first that entered into

recession and economic declined since the third quarter 2008 were a time: Spain with 0.2 percente, followed by Italy with 0.5 percente, Germany and Great Britain with 0.5 percente, France 0.1, Portugal 0.1 percente. The state of recession is defined as decreased economic activity, reflected in GDP for at least two consecutive quarters. Thus in quarters II, III and IV in 2008 in Europe or registered negative growth rates with significant mechanical impact to -4 percente on the annual growth rate of GDP for 2009. The decline in euro area GDP reflects a significant reduction of international trade, especially exports. Significant decrease in exports, coupled with the low level of trust and funding constraints, has led to significant cooling of the dynamics of corporate investment and stock clearance hampered economic growth. According to recent analysis by Boston Consulting Group, the world wealth has declined in 2009 to 11.7 percente due to the recession, reaching a level of 92.4 trillion dollars while European assets fell by only 5.8 percente. To get back to the level in 2007 when it reached 108.5 trillion dollars it would take six years of growth.

Have been reached the climax of a huge economic avant that lasted over 25 years, some economic analysts wonder. As George Soros said *"the crisis has brought the entire financial system on the brink of disaster and is kept under control with great difficulty. This will have long term consequences; not only is business as usual, but by the end of an era"*. [2]

2. Internal situation

Romania hasn't missed any of recession. She was affected by the crisis in a few weeks after the collapse of Lehman Brothers September 15, 2008. The effects were felt immediately on the capital market in October 2008 when it registered trading at the Bucharest Stock Exchange BET spectacular falls above the critical 15 percente. But even so, hit by financial crisis, Romania did not believe that will be affected, as the guvernatii at the time, considering the growth record of 8 percente, estimated for 2008. The same opinion was shared by the President of Romania. He also denied that Romania is in crisis, until June 15, 2009. Almost three quarters of the outbreak of the crisis Traian Basescu told the Romans: "Romania enter recession"

Officially, Romania entered into technical recession in 2009, after the economy has declined for two quarters in a row. Romanian GDP in the first quarter of this year, the steepest decline, after 10 years of sustained growth and continuous, going down by 6.4 percente from the same period last year and 2.6 percente over the last quarter of 2008, according to the National Institute of Statistics. The economic crisis that starts to cross Romania is primarily an internal crisis caused by unsustainable economic growth. The Romanian economic development before the crisis was not a sustainable. Exports without much value added, consumption debt, unsustainable external deficits in the lack of local market products. The international financial crisis was only trigger domestic economic crisis that has affected funding sources. Sooner or later we would have collapsed even if it broke any world crisis. Romania, strongly anchored in trade with EU member states affected by the downturn felt a marked weakening of export volume. Almost 70 percente of its exports are directed to it. Result of decreased trade, lower the orders and reduce financing conditions, industrial production was inscribed on a decendend trend, registering a peak in December 2008 to decrease by 18 percente months and reaching in August 2009 to a decline of 15.8 percente compared with same month of previous year. More and more companies have reduced production, have restricted or temporarily suspended their activities and most, especially small firms, have entered into bankruptcy. Most affected by world crisis were manufacturing, construction and real estate market.

The buildings, one of the industries with the greatest momentum in recent years has been completely paralyzed by the financial crisis. Developers are left with open sites because people no longer have access to loans for housing. Thus those who invested in new buildings with the money remained stuck. If, in the first phase, most hit were small investors who started projects with a loan from the bank and built with the client money, the crisis now affects and the important players that were planning to raise thousands of homes. Basically only small and medium projects at an advanced stage will be completed in 2009. Large projects have been frozen, the expansion of large firms budgets were cut and most residential construction sector has entered the so-called stage into conservation. Property market in the third quarter 2009 showed the drastic decrease in the volume of real estate transactions of 93.5 percente over the same period in 2008. More and more real estate firms that have appeared during the housing boom when prices have exploded, now have gone bankrupt because of the diminishing market transactions and their inability to survive in too small fees collected in rent. Soaring prices of real estate sector which in 2007 had an average of 2,000 per square foot for older homes was driven by easy access to credit, the large number of speculative investors and offer relatively low housing segment in new. The year 2009 was for a reduction in average house prices of 65 percente old, land 30 percente and rents 20 percente.

Investment property market fell amid the credit crunch and a decrease in investor confidence in the market, entered into an alignment of strategies that developers of new financial conditions will dominate the world economy during 2009. The tendency to invest in this period are cash-generating properties such as industrial and logistics space, commercial space for street or shopping centers considered the safest investments.

Almost no one could anticipate that will be real consequences of this economic crisis. Forecasts officials announced changes rapidly from month to month highlighting the expected evolution of a Romanian economic situation. If in the first quarter contraction was 6.2 percente at the end of second quarter 2009 was 8.7 percente. Throughout this period over 600,000 people were left without a job and more than 100,000 companies have suspended their operations, which generated a growth of unemployment. Considering the negative performance of the first two quarters are likely to go down performance due to rising unemployment and shrinking levels of production forecasts for the third quarter of 9.2. percente. But expect a moderation of economic decline in the fourth quarter to 7.3 percente.

3.Unemployment and Labor Market

Following the massive redundancies, natural consequence of declining economic period, unemployment, the most dramatic effect of the crisis, posted one of the most accelerated growth rates in the EU, approximately 60 percente, similar growth in Spain in April 2009 when it registered the top of the crisis in terms of those who are unemployed: 3.65 million people were without a job in Spain, the highest number in Europe. Although compared to other European countries, where the effects of the crisis were felt more deeply, the unemployment rate remains among the lowest in Europe. This accelerated growth is new to Romania, especially in conditions which in recent years the number of unemployed has fallen steadily. Basically the number of unemployed has doubled in the last 12 months. The latest official statistics, unemployment in Romania was in August of 6.6 percente, almost three percentage points less than the EU average which is 8.9 percente.

Taking into account that in Romania did not reach the maximum level of crisis is believed that unemployment will continue to grow in the next four to six months. Unemployment will grow more slowly in conditions in which the government will keep promises made - reducing the number of budget tax relief on reinvested profits, payment of debts to state controls more than 60 days or pay salaries on time. By the end of the year is expected to increase in the rate meet monthly rate of 0.3 percente, but should not exceed 8 percente. Number of unemployed in Romania will reach 685,000 at the end of this year, up 70 compared to December 2008, estimates the National Forecasting Commission.

Amid the international financial crisis, Romanians working abroad have started to return home. Most affected will be fellow working in Spain, one of the European Union countries most affected by the crisis. That's because the Spanish Government said it would give up a good part of foreign workers. This leads to the assumption of increasing the number of unemployed to over one million by the end of 2009.

Social effects of unemployment impact given the lack of a job are the most complex: deepening poverty, deteriorating earnings many years, discouraging actions seeking a new job and the period of unemployment lasting more than six Monday may cause irreversible damage to the individual. All these effects can escalate into broader social movements, if the government rushes to implement anti-crisis measures for this period. Among the measures taken by the Government in the first quarter 2009, was to extend the three months period during which unemployment benefit and the employer and employees to be exempt from social security contributions during temporary interruption of activity for a period of three months.

Labor market recorded a further deterioration in this period. There are many opinions on evolution. If one expects a marked normalization of extreme labor market in recent years and a forced maturity, others see a return to it in time to level a few years ago. Given the unpredictability of market companies have seen the difficulty to estimate the real impact of the crisis on the company. Those who have recruited heavily in previous years has suffered a similar adjustment during this period. The job has become not so sure, and operated companies measures to reduce costs by reducing employees' salaries, which was reduced to 20 or even 40, icing wages or forced offs.

4.Consumption, inflation and rising prices

Economic growth in Romania in recent years was mainly based on increased consumption financed by external loans, consumption for some countries is the main engine of growth. Creating a culture of over-sustainability without having it corroborated with a relaxation control mechanisms but has led to deepening

economic slippages. Easing of financial resources and the expectations of worsening financial situation, the final consumption of the population has decreased 3 times compared with last months of 2008. Decreasing consumption allowed Romania to go through a steady trend of disinflation in recent months. The current account deficit will decrease from 12.3 percente of GDP in 2008 to 5.5 percente in 2009, also due to decrease consumption.

The decrease was due to consumption and tighter lending conditions and increase costs available until that time to record low levels, and the fear of job loss leading to default and unable to pay its debts. In addition no longer can afford to access a loan to cover expenses in case of need as it did in past years when it could rely on a secure income. Banks, who two years ago gave credit conveyor, without analyzing the current profile candidate, now looks reluctant to open doors to new clients and prefer not to take risks and sell loans only with additional guarantees. Loans for personal needs such as "credit only bulletin released in 2006, are already the history. Stimulus-financing for recovery and support came from National Bank of Romania has decreased so far, amid lower inflation, four times the interest rate from 10.25 percente in early 2009 to 8 percente in October 2009 and has substantially reduced rates applied to liabilities in reserve requirements from 18 percente to 15 percent lei and foreign currency dela 40 percente to 30 percente for institutions. Price rises during this period was a temperate, average consumer price increase being 3 percente, is estimated by the end of growth of 4,3 percente. There were 10 percente peaks increase which shows that there is still rigid markets and increasing 8 percente amid gains in exchange rate depreciation of 4.5 percente. The trend of moderation of prices will continue this year, however, for inflation to fall until the end of 2009, within the target range of NBR, the 2,5-4,5 percente, it takes more favorable conditions, among which leu appreciation. Despite the decrease in consumption is expected for the period following a price increase.

The IMF estimates that inflation this year will be placed at 4.3 percente, the central point when 4.5 percente was in the stand-by agreement negotiated in March when contracted a loan of 19.95 billion euros over a period of 2 years.

Inflation could become the biggest obstacle of adopting the single European currency by Romania to the original term, since it is a process difficult to control by the state under the current economic crisis and the period it will succeed, because very many companies working on the Romanian market will be tempted to compensate for reduced sales volume by pressure on prices. The only industries that communicate price reductions are substantial, unfortunately, those who have experienced dramatic declines in sales volumes, so that their share in the index of inflation is insignificant: the auto industry and, respectively, the real estate. Obviously, increasing fuel and energy prices also have a major impact on product prices and, consequently, inflationary effects. Of the 27 European Union Member States, in June, Romania had the highest average annual rate of price increase, 5.9 percente respectively, compared with the same month last year, compared to an average of 0.6 percente in the EU bloc.

5. Is it the year 2010 out of the crisis?

Forecasts for 2010 aren't the most optimistic for Romania in the conditions in world economy show signs of recovery. Romanian economy will register declines in first half of next year following the end of 2010 only to assist the beginning out of the crisis, analysts believe. Since the increase in recent years has been based on consumption financed by external loans, once external financing and economic growth has gone missing. Since the increase in recent years has been based on consumption financed by external loans, once external financing disappeared without a viable strategy in terms of freeing resources for employment without an acceleration of reforms Financial economic recovery will be a very slow. In Europe the economic situation started to improve from the second quarter 2009, estimated GDP growth is the end of the 0.1 percente. One by one strong economies like Germany, France, Portugal and the Czech Republic leave the state of recession and returning to growth. Specialists believe that economic recovery will be the fund boost consumption and public investment. For Romania are expected to increase in 2010 of 0.5 percente and 2.4 percente in 2011 as forecast last autumn of the National Forecasting Commission.

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