



## ANALYSIS OF BUDGET DEFICIT IN ROMANIA DURING 2006 - 2012

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**Abstract:**

*The current economic crisis teaches us a very important lesson. In periods of economic boom, it is indicated that the economic policies to be more cautious to prevent the accumulation of imbalances and to ensure the safety margins that would allow an appropriate response in cases of large unfavorable shocks. The significant role of fiscal policy in macroeconomic policies is already known. It must be brought into account the fact that fiscal policy has a limited space for maneuver, in the sense of working as a stabilizer, being limited by budget deficit threshold.*

**Keywords:**

Budget balance, fiscal policy, automatic stabilizers, economic growth, sustainability

**JEL Classification:**

E32, E62

### 1. Introduction

In recent decades, the budget deficit has become a feature of national economies, finding increasing size of this indicator. The presence of budget deficit occurs due to the decrease of goods and services production in economy, increased spending in order to achieve certain social programs, increasing marginal costs of social production, increased activity of invisible sector of the economy, excess monetary emission and which is not accompanied by increased economic. The existence of budget deficit is also due to the fact that levels of income and expenditures are affected by the state of the business cycle.

In developing countries, but also in developed countries, governments cannot cover expenses based on revenues, leading to the formation of the budget deficit. There are raised questions about the permissible size of the budget deficit, the impact of this indicator on the economy on long and short term, the options to cover this deficit.

### 2. Literature review

Since the beginning it has to be made a first differentiation in the origin of budget deficit. To some extent, the budget deficit occurs as a result of discretionary economic policy. In addition, levels of receipts and budget expenditures cannot be accurately determined by economic policy makers. Moreover, the income and expenditure are influenced by the stage of the business cycle. More specifically, when the economy shrinks, the volume of collected revenue decreases, so the budget deficit is heading towards deficit, while during an expansion period occurs a

growth of budget revenues, which means that the budget goes towards surplus.

A low level of deficit or surplus public can hide the existence of large imbalances. This is the case when the budget balance is the result of favorable circumstances, for example, large public revenues accumulated during economic expansion.

Therefore, the budget deficit taken at face value, it is not a fair indicator for assessing the sustainability of fiscal policy. Therefore, structural budget deficit it is determined.

There is some controversial opinion regarding the acceptance of the notion that the budget deficit has a "detrimental" effect on economic life. For example, the presence of substantial deficits is not necessarily a cause for concern. Boskin (1987) exposed this issue by presenting the case of Japan, which in the mid 80s recorded high deficits, but in reality the net investment situation was a favorable one.

According to Blejer and Cheasty (1991) consolidated budget balance is the difference between expenditure (including interest charges, excluding borrowings) and fiscal and non-fiscal revenue (including grants, excluding loans).

Tanzi, Blejer and Teijero (1988) believe that the conventional budget balance shows information about the net effects of fiscal policy on aggregate demand. They consider that the methodology of determination is constructed to provide a way to quantify the contribution of the public sector to form aggregate demand and the effects on the current account.

Consolidated budget balance is the foundation from which starts in predicting other indicators reflecting the size of budgetary imbalances. One such indicator is the

primary budget balance, whose importance stems from the fact that this indicator measures the degree of fiscal sustainability. Blejer and Cheasty (1991), showed in a study that by determining the primary budget balance:

- are eliminated the effects of previous deficits captured by interest expenditures. In other words, public interest expenses on loans contracted are seen as expenses related to previous financial years, the expenses wearing the stamp of economic policy promoted in those years;
- it is completely removed the "non-discretionary" component through fiscal and budgetary policies adopted and promoted by the government. It is about the impact of inflation on interest costs, and hence the size of the budget deficit;
- allows evaluation of the effectiveness of public finance policies on achieving a sustainable economic system that is based on real growth.

### 3. Methodology of research

The literature and practice appeal to several indicators underlying the determination of the size of budgetary imbalances. Authorized institutions in Romania, such as the Ministry of Finance and the National Bank of Romania, bring to public attention the following balances: conventional balance (general government balance), the primary balance general consolidated budget and structural balance of general consolidated budget.

Aforementioned indicators help monitor fiscal policies promoted by the government of the country and respect the nominal convergence criteria which our country must fulfill.

### 4. Analysis of public budget imbalance in Romania based on budget balances. results

Following are presented the evolutions of budget balances in Romania for period 2006-2012, but also comparisons with European Union member states.

#### 4.1. Analysis of the consolidated budget balance in Romania 2006-2012

Consolidated budget balance is the indicator most commonly used to estimate the size of budgetary imbalances. Based on this indicator is assessed the fiscal and budgetary policy adopted and promoted by public authorities.

Knowledge of budget deficit and the continuous care regarding diminishing this indicator are of great significance for our country, especially that Romania faces major challenges in the development of the economy. In addition, as a member state of the European Union, Romania is required to comply with the condition imposed by the European Community Treaty on the limitation of the budget deficit to 3% of GDP and public debt at 60% of GDP. The table below shows the dynamic of the budget balance as a percentage of GDP in the period 2006-2012.

Table 1. Consolidated budget balance of Romania during 2006-2012

Year	2006	2007	2008	2009	2010	2011	2012
Budget deficit	-1,7	-2,9	-5,7	-8,6	-6,8	-5,5	-2,5

(Source: Eurostat)

During the period 2008-2009 budget revenues fell sharply, while costs have risen, so widening the budget deficit, which peaked in 2009 the maximum amount of 8.6% of GDP. This phenomenon can be explained by the fact that economic fluctuations affect both revenue (decreases due to the decrease in economic activity) and expenditure (increased funding for social security, unemployment funds from increasing the number of people assisted social).

The level of consolidated budget deficit increased significantly in 2008-2010. The causes underlying this increase are: reduced economic output, lower budget revenues amid the economic crisis, increased share of shadow economy, excessive spending for the fulfillment of social programs institutional factors and political instability.

Since in 2009, the budget deficit has peaked the maximum value, the government proceeded to implement austerity measures which contributed to the decrease from year to year of this indicator. Thus, this indicator, in 2011, was 5.5% of GDP (31.97 billion RON), down to the value achieved in the previous year, 6.8% of GDP.

The budget deficits problem is not only encountered in Romania. Entire Europe is worried about the risk of these deficits.

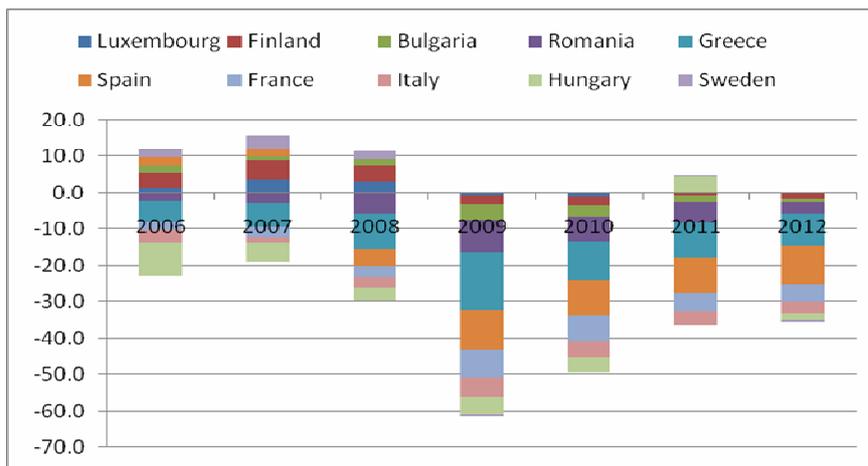
In the European Union, in 2009, the budget deficit increased 3 times compared to the value achieved the previous year, from 2.4% of GDP in 2008, to 6.9%. At the end of 2008, Romania was ranked on 8th place among European countries on the budget deficit.

For 2012, it should be noted that the average budget deficit UE28 was 3.9% of GDP. This year the lowest deficits were achieved in Estonia and Sweden (both 0.2% of GDP), Luxembourg (0.6% of GDP) and Bulgaria (0.8% of GDP) and Germany (0.1%) reported surplus. Of the 17 EU member states recorded budget deficit above 3% of GDP: Spain (10.6%), Greece (9%), Ireland (8.2%), Portugal and Cyprus (both 6.4%).

Romania has made that year a budget deficit below the EU average.

On the background crises manifested internationally and building the welfare state, a large part of European Union Member States faced with significant budget deficits and achieving large stocks of public debt. Thus, in the light of previously reported facts it can be explained the public finance imbalances obvious in some European countries.

Graph 1. Evolution budget deficit within member states of EU



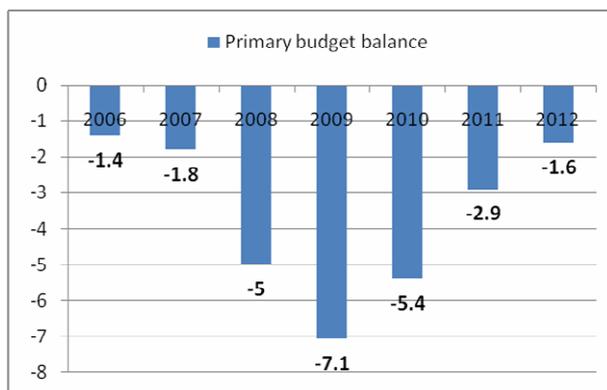
(Source: own processing based on Eurostat data)

Decreasing the budget deficit is not the goal itself, but a goal of stimulating economic activity, the state having less need for deficit financing, allowing banks to increase their lending to private sector firms.

#### 4.2. The analysis of the primary balance in Romania during 2006-2013

Primary budget balance is the difference between consolidated balance and public debt interest costs. The primary deficit/surplus and its evolution is presented in the chart below.

Graph 2. Evolution of primary budget balance in Romania



(Source: [www.mfinante.ro](http://www.mfinante.ro))

Looking at the table above, we can easily see that in most years Romania has recorded a deficit. This indicator highlights the low level of budget revenues

insufficient to cover budget expenses less borrowing costs associated with contracting state loan.

Table 2. Evolution of structural budget deficit in Romania

Year	2006	2007	2008	2009	2010	2011	2012
<b>Structural budget deficit</b>	-3,5	-5,3	-7,9	-9,1	-6,2	-3,0	-2,7

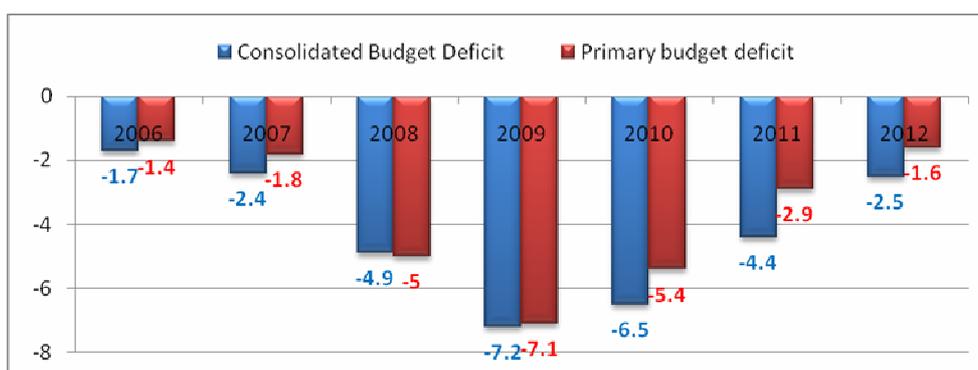
(Source: European Commission)

During periods when the primary balance recorded positive values, the surplus was not big enough for a possible finance of interest expense, which is reflected by the conventional balance, which recorded a deficit.

The chart number 3 presents the evolution of the consolidated budget balance and the primary budget balance.

If we compare the evolution of the two indicators, we find that during the analyzed period, when the primary balance has been negative, these values were reflected in the consolidated deficit amount, and when the primary balance has been positive, the size of government deficit decreased, but still this indicator achieved a significant level.

Graph 3. Evolution of consolidated budget deficit and primary deficit in Romania



(Source: own processing based on Eurostat data and [www.mfinante.ro](http://www.mfinante.ro))

#### 4.3. Analysis of the structural balance in Romania

Cyclically adjusted balance is an indicator which analyzes government budget imbalances at without influence induced by fluctuation cycles.

This indicator is commonly used in research on sustainability fiscal and budgetary policies, but also in research targeting episodes of fiscal adjustment taken in various countries. During the economic ascent, fiscal policy adopted was a procyclical, leading to exhaustion of necessary fiscal space to stimulate the economy during the recession that followed. During the crisis, reducing the structural budget deficit led inevitably to preserve procyclicality of fiscal policy. In this way, automatic action, favorable and stabilizing of cyclical budget deficit through automatic stabilizers has canceled the procyclical discretionary policy.

To ensure the sustainability of fiscal policy was necessary to implement decisive measures which led to the reduction of the structural budget deficit from 9.1% of GDP in 2009 to 3.0% of GDP in 2011. Supporting

regarded especially the spending side, reforms were adopted in wage budget staff and the public pension system.

The report of Fiscal Treaty recalls the Romanian success to reduce the structural budget deficits in recent years. Compared with EU countries, Romania had one of the best fiscal adjustment programs, managing to achieve a reduction of 1.8% per year in terms of structural deficit.

#### 4. Conclusions

In 1984, economist Robert Eisner said at the annual meeting of the American Economic Association that "The budget deficit is like a sin. Most often is perceived as something morally wrong, very difficult to avoid, not always easy to identify and quite difficult to measure accurately". His works (Eisner, 1984, 1989, 1994) is based on the idea that it is important to know the indicator underlying the size of budgetary imbalances before proceeding to the analysis of these

budgetary imbalances, to determine their impact and determinant factors.

Structural deficits reflect a chronic problem that must be addressed through changes in taxation and spending policy changes. Increase structural budget deficit warns of another problem, namely, the increasing part of the deficit caused by interest payments associated with debt. This increase can lead to the problem called "deficit exploded."

In the period 2006-2012 we estimate the evolution of Romania was an oscillatory one, given the events experienced by our country and similar situations internationally. Since 2010, following austerity measures implemented, the budget deficit declined continuously, which allows us to say that Romania had one of the most ambitious fiscal adjustment programs in the European Union. However, future challenges circumscribe to sustainability of fiscal and budgetary policies in order to maintain this indicator within the limits set by the Maastricht Treaty.

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