

Executive Summary¹

Lucian Boia, one of the foremost Romanian historians of recent years, defined Romania, in one of his recent books, as the “**transition country of Europe**”. Romania is indeed situated at a geographic crossroads of Europe. It is almost impossible to categorize Romania as being in either Central Europe, Eastern Europe or the Balkans. That is why most prefer to say that Romania is located in South Eastern Europe, a more vaguely-defined region, in itself a region of transition.

Geographical ambiguity has brought with it historical uncertainty. The whole history of the modern Romanian state is crammed in less than 150 years, effectively the demographic time-span of just five generations, including the present one. In this short but intense period, Romania and its people have grown accustomed to transition. The country made its first transition from just two small principalities still vassal to the Sublime Port of Constantinople in the middle of the nineteenth century, to a modern, capitalist, European democracy in the time-span of just one generation. Unfortunately, this transition was barely complete when the flames of the Second World War engulfed Europe. At the end of this conflagration, Romania found itself trapped behind the Iron Curtain, only this time without any transition. Although some might say that there was a transition to the communist dictatorship which kept the country hostage for almost five decades, this cannot be true. The transition to dictatorship did not occur. Romanian society has been frozen in the grip of autocracy for five decades, which have witnessed not only material deprivation and oppression, but which above all severely damaged the very fabric of society and made human development afterwards a daunting challenge.

But this challenge was bound to come, and it did so in December 1989. After the bloodiest anti-communist revolution in Central Europe, Romania embarked on what was to be Central Europe’s longest and most tortuous transition. This came to epitomize concepts like “chaotic transition”, “Stop - Go Transition” and other terms now in common usage by academics, analysts and decision makers alike.

However, one cannot say that the quest was unsuccessful. In 1990, Romania barely qualified as a medium human development country, with severe economic and social problems; where even supplying electricity during the winter months was problematic. Seventeen years later, it is a country which ranks among the nations boasting high human development levels, is a full member of NATO and of the European Union.

From an economy that barely reached, as measured by its GDP at market exchange rates, around \$bn.30 in 1989, Romania’s economy boasts now a GDP of \$bn.127. This represents a share of 0.9% of the total European GDP (including Russia) in market exchange rates terms, and almost 1.7% in PPP terms. So in 17 years, Romania’s economy multiplied by a staggering 4.3 times, and this has translated as increasingly visible improvements in living standards for the majority of Romanians. Admittedly, this translation came only after long travail, which might explain the relative lag in perceptions. Therefore, human development as broadly measured by the Human Development Index has risen steadily from 0.772 at the beginning of the nineties to 0.805 in 2004. The Human Development Report of 2005 still ranked Romania 64th in the world in terms of Human development; the 2006 edition ranked it 60th. A leap of four places took seventeen years of harsh reforms, and is mostly due to the economic achievements which eventually brought a belated and still-limited measure of prosperity for the majority of Romanians. There is much to celebrate for an economy that along with the full EU Accession on January 1st 2007 entered its seventh consecutive year of growth, at rates that far outstrip those of developed economies, and which rank it stellar even among its sibling Central European nations and economies. But much remains to be done. Life expectancy at birth still remains among the lowest in Europe, barely creeping over the threshold of 70, and still below that for the country’s male population. Infant mortality, which although falling sharply, remains the highest in the 27 member states Union. The education

¹ Executive Summary has been elaborated by Dr. Catalin Ghinamaru, coordinator of the NHDR Romania-2007 team of authors

system plagued by high drop-out rates endangers the country's ability to take the opportunities offered by an economy increasingly dominated by knowledge and information. A string of disparities that keeps rural areas mired in a past might look nice for fans of folklore and unspoiled traditions, but bodes badly for sustainable development. And finally, but probably most worryingly, the population may age and shrink before witnessing even a glimpse of the relative wealth already enjoyed for decades by those in the "old" EU member states.

If this year (2007) proves as bountiful for Romania's economy as the last six have been, then at the end of it, Romania's economy should be larger than that of Denmark (as expressed by its GDP at PPP), a member of the EU since 1973. However, despite this premise, Romanians will still (by the broad measure of the GDP per capita at PPP) be 3.65 times poorer than the Danes. They will thus remain the EU's poorest nation, apart from their Bulgarian neighbors.

The language of figures may be "cold", but nevertheless, it provides the most objective picture of the foundation on which one must build. These and other figures provided, give an accurate image of Romania's state of human development at the point of its EU entry. They therefore form the substance of the [1st Chapter](#) of this report.

To reach the point where it could claim a place among those countries which have achieved a high level of Human Development, Romania had first to rebuild a democracy practically from scratch, or worse. Five rounds of free general and presidential elections have now been held; of these, three have seen an alternation in power between the left and the right of the political spectrum. A new democratic Constitution was approved by referendum in 1991, and was similarly amended in 2003. This was not only to prepare the country for its imminent accession into NATO and the EU, but also marked the country's progress on the path towards a fully-fledged democracy. Although much still remains to be done to hold accountable a "political class" many judge as corrupt and aloof, to uproot corruption in general and build a truly independent judiciary, much has been achieved. For without the re-establishment of democracy, the restitution of properties abusively confiscated under communism, the opening of the archives of former communist-era secret police, and especially without a vibrant press, human development would not have been possible. Developing institutions accountable to the public, creating mechanisms through which every citizen and every community can express their opinions, and through which they can act in accordance with those opinions and legitimate interests, remain at the heart of human development. Without democracy, human development is a practical impossibility: the harsh experience of Central and Eastern European nations (especially the Romanian one) remains painful testimony to that. But the democratic construction risks remaining shallow and incapable of delivering human development if institutions do not link with the people, and if real power is not given to the people where they need it most - in communities. It is this community involvement which must be restored and strengthened in the years to come in order to render the Romanian *democracy truly inhabited by democrats*. In other words, not that individuals and communities should simply go through an assimilation process with regard to the rules of democracy, but have adopted them as their most cherished values. For this to happen and chief among them, the application of law has to turn irrevocably into the Rule of Law. This is the broad message conveyed by the first part of the [2nd Chapter](#), dedicated to deepening democracy in Romania as the very foundation that will allow the nation to lock in the gains of seventeen years of Plan to Market Transition.

But democracy in poverty cannot last. So alongside the restoration of democracy, Romania had to follow the thorny road of Plan to Market Transition: to re-equip its economy with market institutions, to free the forces of the market and effectively to force the state out of the market. Romania's transition lasted fifteen years according to the Liberalization Index cumulative scale. It took almost eight years to reach the so-called "critical mass of progress in Plan to Market Transition threshold". This is the point from which changes were irrevocable and, on the other hand, the reform was starting to show its benefits. Eight years is almost double the time-span needed by Poland or Hungary to reach the same threshold. However,

after reaching this point, it took Poland and Hungary almost ten years to achieve what is conventionally called “the end of transition”; whereas it took Romania only half of that period to make the “end of transition” finishing line. The years between the critical mass and the “finishing line”, which coincides with the country’s entry into the European Union, have been characterized by growth rates averaging more than 5%. This is a full percentage point more than the average growth rate recorded by Poland, the country which registered the longest continuous period of growth in the region following the attainment of the critical mass threshold. This time has been well-spent. Inflation, the arch-enemy for more than a decade, has been tamed; the economy is now overwhelmingly in private hands; and perhaps as a result of a very long transition, the residue of central planning has been thoroughly purged. So apart from any exogenous random shocks, the economy can continue to enjoy strong growth for the decade to come, thus not only entrenching stability but also preparing the country for its next step - the entry in to the Euro Area.

These and many more considerations, as well as a recommended agenda to entrench stability and predictability as a solid basis from which to pursue high-value added human development form the contents of the second part of the Report’s [2nd Chapter](#).

The benefits of economic development are reflected by the evolution of populations. It is in the state of their demographic developments, in their birth rates and death rates, in their infant mortality, school enrolment and literacy rates that we can see how economic development translates into human development. The very fact that populations in Central and Eastern European countries, particularly Romania, have begun to fall dramatically after the collapse of communism clearly shows the failure of a regime which rejected democracy and markets altogether. The demographic shocks suffered by Romania’s population during the last half of the twentieth century, laid the unfortunate foundation for a sharp decline which threatens the future of the nation. Although the country currently enjoys a peak in working age population, the mere fact that these large generations have failed to procreate sufficiently makes the sustainability of the country’s long term development questionable. Moreover, it means that in a little over a quarter of century from now, its social security systems (crucial for a society that aims for a higher degree of inclusion as part of its ideal of human development) will be under an immense strain. Migration, which has become a defining phenomenon for the whole region (but especially Romania) may soon make matters even worse. The question that is asked in the [3rd Chapter](#) of the Report (and around which the entire discourse evolves) is whether these unfortunate trends can be reversed, or at least arrested. This is because a depopulated country will no longer attract investors, and an ageing population cannot generate the necessary levels of economic development the country needs to bridge the development gap (human development included) that separates it from the wealthy members of the 27-member club it just joined. Of course, immigration might be a solution, and the country will have to prepare itself, together with its siblings in the region, for multiculturalism. But the Irish example, where economic development and investment in human resources coupled with intelligent management of EU aid have brought back population growth must also be considered. Unfortunately here there are no simple answers and no simple solutions. But something must be done, for otherwise discussion of human development will be in vain.

The economy is back on the growth trend and long-awaited prosperity has finally started to be felt by a population long been accustomed with privations than with abundance. However, one still cannot say that the type of economic development witnessed in the years since the attainment of critical mass of progress in transition has been particularly conducive for human development. Employment rates, and most worryingly activity rates, have been falling for more than a decade now and Romania has slipped back instead of getting closer to the Lisbon targets agreed by the member states of the Union. Large swathes of the population still live in underemployment, practicing subsistence agriculture and feeding into undeclared work and migration for employment abroad, thereby further depleting and wasting the country’s human capital. The fact is that labor, as a factor of production, has contributed little to the country’s undoubted economic and social progress in the seventeen years since

the country started to return to democracy and a market economy. Causes for that are many, and some of them are not necessarily connected with the dynamics of transition, but with the underlying developments of the current age of globalization that favor capital over labor. Nonetheless, it is true that the current state can be attributed largely to the fact that Romania's human resource is poorly prepared for the challenges and opportunities of today's economy. The proportion of higher education graduates is low, both as share of total population as well when weighted against the total working age population, and also when calculated as share of total employment. The education system is still far from responsive to the needs of the market, and what is most worrying is that companies are still reluctant to invest in human resources development.

Some changes for the better have occurred during the last couple of years. But investment in Research and Development remains inadequate, which remains the great challenge for the decade to come. Without this, economic development capable of generating high returns, high quality jobs and in the end propel human development on a wider scale is impossible. If investment in human resources at enterprise level is fostered by the arrival of EU funds, investment in research and development of a higher level (the next vital step in securing the country and its people a worthy place in a global economy based on innovation and information) is more problematic.

A simple exercise looking at few relevant numbers tells the whole of the story. Assuming that Romania continues its growth into the decade to come, and GDP growth rates stay at the same levels as during the last two or three years, i.e. above 6%, then by the middle of the next decade, its GDP expressed at market exchange rates in USD will practically double, exceeding \$bn.210. Betting on a weak dollar for the next ten years, this may equate to around EURbn.150. The total of funds allocated for Romania by the EU Commission amounts to roughly EURbn.30, which means effectively 20% of the country's prospective GDP in ten years, at growth rates that far exceed those normally recorded by developed economies. Most of this money, provided it is used, which is still uncertain, will go on far more basic needs than research and development. If the Romanian Government adheres to the EU objective of allocating the equivalent of 3% of its GDP for research, then using the same estimated GDP figure, by 2017 this will mean around EURbn.4.5, or no more than 15% of what the Commission will allocate for more basic needs. Still, it is worth a try, as [Chapter 4](#) of the Report argues. Otherwise, not only will the country be ill-prepared to enter the EURO Area (an objective to be achieved around 2013-2015) but it will also become a "transit" economy, a mere re-exporter of goods and services, vulnerable to the volatility of global markets and which will thus be unable to foster human development at more than a basic level. This is not enough.

To avoid this, the country needs to develop its substantial domestic market and take advantage of its peaking working-age population, which offers an unprecedented window of opportunity. But this also means that it has to find its own market niche in a world where nations and producers increasingly tend to specialize. Romania needs to identify that specific comparative advantage which can be turned (via investment in human resources and in R&D) into a competitive advantage which will give it the edge and help create a strong domestic market; an active and integral part of the single European market. This comparative advantage is Romania's bountiful natural factor with respect to agriculture. Not only does it offer the possibility of producing cheap, safe and healthy food for which all consumers of the continent yearn, but it also provides numerous possibilities for developing into the exclusive niche of agro-tourism. Moreover, it holds the potential of entering the high-tech domain of bio-fuels by using the fortunate combination of the country's expertise in processing fossil fuels and the richness of agricultural raw materials that it can provide. It can thus offer not only new hope and prospects for more than half its population currently living in rural areas, which might otherwise depopulate and thus render all investment in infrastructure useless. But it will open wide the window of development into a domain that holds a fantastic hope, both for the energy security of the continent as well for arresting climate change, which threatens the development of the whole of humanity. These arguments, together with others in favor of

rural development and building a strong agricultural pillar as vital for the economic and human development of Romania's rural areas are the put forward to the reader in the [5th Chapter](#) of our report.

Opening to the world meant also that the country's citizens were finally free to travel, and even to work abroad. They started to enjoy what is actually a fundamental human right; that of settling, living, working, retiring and ultimately dying wherever they freely choose to do so. That is the challenge of migration, and especially of migration for employment abroad, as well as that of multiculturalism. Of course no-one need fear it, as multiculturalism and cultural diversity are the very strength of Europe. They give it the edge in global human development, and migration has been the main way in which European culture and values have spread across the globe. So the very fact that Romanians, though belatedly, joined this trend only shows how much they share the common cultural heritage of Europe.

However, migration has costs and benefits. The country loses precious human resources, but it may be that the country cannot yet offer enough opportunities for development for those who choose instead to migrate, even temporarily. On the other hand, migration brings benefits. Migrants are sending back their earnings in the form of remittances. These have helped end the long period of depreciation of the national currency and thus close a channel that has long fuelled into CPI inflation. They boost the solvency of the domestic market and thus contribute to investment attractiveness, which ignites growth and ultimately creates the basis for human development on a mass scale. But this is the present, with benefits seeming to outweigh costs by far; what is in store for the future? Membership of the EU means that migrants can now choose to stay where they have migrated for work; but they can also choose to return to their homeland as its development and job-generating prospects improve. Which of these will happen first is still a matter of conjecture. As the economy continues growing, the unemployment rate will fall and reach a level from which it finally puts significant upward pressure on wages, thus starting to chip into the competitive advantage of cheap labor. Immigration appears to be the obvious solution to the labor shortages already emerging. This indicates that a policy must be developed for migration, bearing in mind both sides of the issue, as well as long-term and short-term implications. An analysis of the impact of remittances on economic development and of the so-called brain-drain phenomenon on human development make up [Chapter 6](#) of the Report.

But human development does not necessarily mean leaving the markets to decide, and thereby restrict the chance for development only to those who are capable of seizing the many opportunities markets provide. It also means including and keeping in the mainstream those that are less able to seize these opportunities, and those who have withdrawn from the mainstream into inactivity or underemployment. It also means ensuring that human development grows into a process which continues throughout life. Human development need not stop during periods of disability, spells of unemployment or sickness, and does not have to come to an abrupt end with retirement. This is where social security, with its ample network of both public and private systems, contributive and non-contributive schemes, comes in to play. Social security is at the core of what we call the "European Social Model"; it is what distinguishes the European approach to the functioning of the labor market from different approaches elsewhere in the world, especially in those large emerging economies that are now starting to re-shape the global economic and social landscape. [Chapter 7](#) of the report, while arguing for the diversification of social security schemes to suit the many needs of individuals in an open economy and society, also argues for their sustainability and robustness as a prerequisite for the provision of adequate benefits. They represent pillars of general economic and social predictability and stability; essential ingredients for long periods of economic growth.

The chapter also substantiates its approach on the fundamental right of individuals as consumers and contributors to benefit fully from their contributions to social insurance schemes. The principle of "money of the insured for the insured" further strengthens the principles of accountability and responsibility of both individuals and organizations. It finally features a bold but demanding agenda for the decade to come. This includes leveraging

towards the opportunities offered by markets and diversifying social security systems to give more choice to the individual and reduce the burden on the state. But this has to be matched by hedging, which the authorities must provide not only for those unfortunate enough not be able to contribute, but also for those who do contribute to public social security schemes. These must be linked into a support network that is able to withstand those shocks and corrections which are part and parcel of the way markets function. This particular mixture of leverage and hedging, which actually brings market philosophy at its highest extent into the functioning of social security schemes, also ensures that they remain a solid foundation on which society can base its long-term human development.

For all of these objectives, Romania could until now depend only on its own resources, ruined by fifty years of systematic economic and social pillage, waste and mismanagement. But as a member of the EU, and before that as a candidate country, Romania is able to count on the support and solidarity of the EU, which has shown that it has both the means and the will, TO INCLUDE ROMANIA into the MAINSTREAM of the continent's development, just as it did with Ireland and the young democracies of the Mediterranean Belt. Some EUR bn30 will be available to Romania only until 2013, to help the country invest in the development of human resources at enterprise level, to improve its education system and to render its agricultural sector more competitive. If complemented by national resources, which thanks to benign economic and demographic conditions are growing steadily as the economy develops, this will make a tremendous difference. Romanians of the current large generations making the bulk of the workforce may yet see the gulf between their living standards and those of their counterparts in the "old" member states starting to narrow. However, this requires above all firm, responsible and accountable political guidance and cautiousness in the design and implementation of macro-economic, fiscal, labor market and social security policies. All these underpin the improvement of the so-called administrative capacity. In addition to growth, the country needs stability and predictability, not only to entrench growth and relegate to the past the memory of discretionary and arbitrary changes, but also to generate that continuous stream of projects which will ensure that the EU money is put to good use. These and other considerations are the substance of [Chapter 8](#).

Romania stands today on [what is](#) a [watershed](#) of its history. It can look deeply into its past, but more importantly it can gaze far into the future. A future that will see important changes, one of the most significant of which being the shift from the LEU to the EURO, which will firmly anchor the economy into the European one. But Romania must also continue its transition. This time it will be from a Plan to Market Transition Economy to a Developed Medium-Sized Emergent Market Economy, able to provide ample development opportunities for all its citizens, now also citizens of Europe. It will have thus to consolidate the rule of law, to entrench macro-stability and strive to maintain high growth rates. It will have to encourage investment in human resources; find its specific market niche by capitalizing on its comparative advantages and turning them into competitive ones; it must commit resources and efforts to Research and Development. By doing so, it will open the gates wide for sustainable job creation in sectors of high added-value, sectors which will lure back many of the migrants who quit the country in search of better opportunities abroad. Romania must also attract immigrants, without fearing multiculturalism but welcoming it. It will thus generate the necessary resources to make social security systems sustainable and robust, and enable them to provide adequate benefits not only for the current generations but also for those to come. It may even be able to reverse the worrying demographic trends, and improve general prosperity before large swathes of its population turn grey. These and other proposals make up a broad and detailed [Agenda for the Decade to Come](#), which is the substance of the concluding [9th Chapter](#) of the report.

Finally, while looking into the future Romania should not forget that it is one of the great nations of Europe; in this part of the continent, many of the solutions it has adopted have become good practice. It should therefore look beyond its borders and project its experience towards the battered region of the Western Balkans and the Black Sea Basin, and aim to

become a powerhouse of human development for a still-troubled region straddling the transit routes between Europe and Asia.

By doing so it will show that, as an integral part of the European Construction, it puts European ideals not only at the very heart of its own Human Development Project but that it can put them at the heart of Human Development for the whole continent, thus re-branding itself into that “**country of the future**” which its first king, Carol 1st foresaw...well, *less than 150 years ago*.