KENNESAW STATE UNIVERSITY
COLES COLLEGE OF BUSINESS
Bagwell Center for the Study of Markets and Economic Opportunity

Commentary

Title:

"Much to Celebrate: Romania's Transition to an Open Economy 1989-2019"

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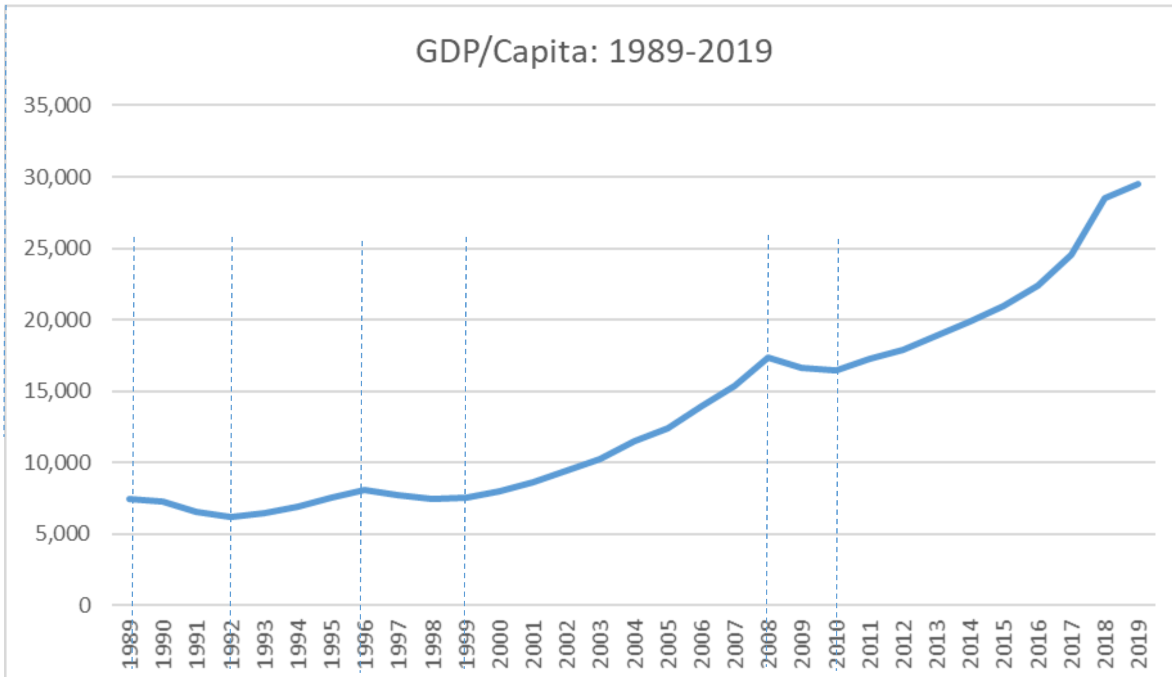
In 2019, Romanians had their 30-year anniversary of the fall of communism in 1989, and there was much to celebrate. However, there is also still much to be done. As we can see in Figure 1 below, Romania has accomplished a great deal economically, but not without some significant setbacks along the way. While at first, the economy declined sharply as per capita income and production fell from $7,486 in 1989 to a low of $6,177 in 1992, it later recovered to $8,075 in 1996. As we can see, the transition had a rough start with the economy only getting back to the level under communism in 1995.

Figure 1



Source: International Monetary Fund

All of the Eastern European countries that had been dominated by (or directly absorbed by) the Soviet Union suffered rocky starts when they moved from state owned and controlled economic systems to free or open ones. Some had rockier starts than others had due to both different initial conditions and to different policy paths chosen to get to an open economy. As to initial conditions, on the positive side Romania had virtually no external debt to repay due to the draconian policies of the communist Ceausescu Regime. On the negative side, Romania is farther east (and therefore farther from Western markets and investors) than other transition economies like the Czech Republic or Poland that had borders with European countries like Germany or Austria. Overall, a neutral start.

The real problem for Romania's early transition was the choice of economic policy. At the time, two major, and competing, theories of transition were in play. One plan, "Shock Therapy", postulated that to make a successful transition from a centrally planned government-owned system the new government would need to make a dramatic choice to immediately privatize all state-owned industry, remove all price controls, open the country to foreign competition, and remove all subsidies to both firms and consumers. The idea was that without a complete change to the system there would always be a strong temptation to go back to communism when the going got rough, and therefore no real reform would be forthcoming. Pitted against the bracing "Shock Therapy" plan was the idea of gradual transition, where most of the government owned firms would remain in state hands and the conversion to a market system would be phased-in over several years. The goal was to avoid disruption, thereby keeping the population in favor of reform.

Romania chose the gradualist approach. The main problem with this approach is that the loss-ridden and inefficient state-owned firms would continue to drag down the economy. The real danger here is that the economy would continue to do badly and investors would be leery of committing to new projects. Romania paid a high price in lost growth opportunities. As we see in Figure 1, "Much of the 1990's in Romania were marked by great economic hardship, including high unemployment, skyrocketing inflation, and shortages of consumer goods."[1]

Economic growth finally gets untracked starting in 2000, the year that negotiations for accession to the European Union began. In order to meet the EU's standards Romania began in earnest the hard work of reform. Romania had several excellent years of economic growth, averaging 10% annually from 2000 to 2008. This dramatic growth was interrupted by a serious setback caused by the "Great Recession" of the United States, which affected many economies around the world. After recovering from this downturn growth returned again, leading to major increases in living standards. In 30 years Romania moved from one of the lowest ranked economies in Europe to middle income, ranking just behind Greece in GDP per Capita.[2] Even though there were many hardships in the beginning, and there are still many economic reforms that are necessary for Romania to reach the higher ranked economies, the transition has clearly been a major success.

One of the factors, in addition to reforming the economy, that have been identified as crucial for a nation's economic success by the European Bank for Reconstruction and Development is education. No advanced economy can function without a large number of well-educated people. While Romania has had a long history of technically trained engineering talent during the communist years, the country was missing the crucial knowledge of how markets function. We here at Kennesaw State University are proud to have been partnered with the Romanian-American Business School (part of ASEBUSS), founded in 1993 near the beginning of the transition to a free economy, specifically to provide this kind of training. Contributing our expertise in executive education, KSU has been instrumental in helping Romanians prosper and thrive. More than 750 men and women have received KSU certification in business as part of the Executive MBA programs run jointly with ASEBUSS. Kennesaw State University congratulates the hard working people of Romania on the past 30 years of achievement, and look forward to 30 more.

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[1] Constantin, Goschin, Danciu, "The Romanian Economy from Transition to Crisis: Restrospects (sic) and Prospects." https://pdfs.semanticscholar.org/2a04/d22b8e793c584ca86bd03157b6cf4218e519.pdf

[2] According to Sir Suma Chakrabarti, President of the European Bank for Reconstruction and Development, Romania's GDP/Capita started at 33% the EU average in 2000 and shot all the way up to 60% by 2017. See: https://www.ebrd.com/news/speeches/romania-and-transition.html