MEASURES TO RECALIBRATE THE MACROECONOMIC POLICIES IN THE NEW EU MEMBER STATES THAT ARE TO ADOPT THE SINGLE CURRENCY*

PhD. Napoleon POP – scientific researcher I, Director CCFM „Victor Slăvescu”, coordinator
PhD. Camelia Milea - scientific researcher III, CCFM „Victor Slăvescu”, executive coordinator
PhD. Iulia Lupu – scientific researcher III, CCFM „Victor Slăvescu”,
PhD. Candidate Adina CRISTE – scientific researcher III, CCFM „Victor Slăvescu”
PhD. Candidate Alina Georgeta AILINCĂ – scientific researcher, CCFM „Victor Slăvescu”
PhD. Floarea IORDACHE - scientific researcher III, CCFM „Victor Slăvescu”
Assistant univ. Alina ROTARU –„Spiru Haret” University, Bucharest, Faculty of Finances and Banks

As of September 2008, the vulnerabilities accumulated during the previous periods overlapped the devastating effects of the crisis in the new member states (NMS) of the European Union, deteriorating the main macro-indicators and increasing the economic instability, which generated a profound process of adjustment.

Under the conditions of the economic crisis, the accomplishment of the criteria of nominal convergence, necessary in order to adopt the euro, is a real challenge for all the new member states; this materialized primarily in the increase of the exchange rate volatility and of the fiscal-budgetary deficits.

---

* This paper represents the research project synthesis “Measures for recalibration the macroeconomic policies in the euro candidate countries”, elaborated in 2010, within the Victor Slăvescu Centre of Financial and Monetary Research, a component of the Costin C. Kirițescu National Institute of Economic Research, Bucharest. The research project belongs to the Romanian Academy priority programme: **Romanian Economy and the Euro System**.

Synthesis

During this period of great incertitude and national, regional and international disturbances which spread throughout the world states touched by the economic globalization process, the NMS need a balanced mix of macroeconomic policies adapted to the new conditions that will allow them to preserve their stability. Thus, the monetary policy should have a supportive role for the domestic economies of the NMS, while the fiscal policy should be a key macroeconomic instrument which to compensate the limited capacity of the monetary policy under the conditions of the economic recession, being an important short-term support for the economy.

Keywords: global economic and financial crisis, nominal convergence, public debt, monetary policy, foreign deficit

JEL classification: E 24, E 31, E 43, E 52, E 62, F 31, F 32, G01, H 63

As of September 2008, the new member states (NMS) of the European Union were confronted with serious challenges due to the misbalances and vulnerabilities which had built up during the previous periods, which has generated a profound process of adjustment. Under the impact of the international economic-financial crisis, the real GDP crashed or compressed significantly in most of the surveyed countries contributing, next to the external influences, to the tempering of the inflation and to the substantial deterioration of the fiscal positions. This situation led to the substantial increase of the premiums for the sovereign risk, as shown by the long-term interest rates.

There are three factors which acted before the crisis started and which aggravated the effects of the shock: the fast expansion of the credits to the private sector, the economic activity which exceeded the potential (overheating) and the foreign misbalance (large foreign deficits).

Generally, the economic activity in the NMS is moderate and “heterogeneous” because of the differences regarding the pattern of growth they followed and due to the vulnerabilities specific to each country. Thus, the countries with an intense activity oriented towards the export were affected by the substantial decrease of the foreign demand (Czech Republic). In some countries the effect of the foreign shock has been amplified by the domestic vulnerabilities; for instance, the “real estate balloon” and the overheating of the economy (Latvia) or the excessive governmental loans (Hungary).

In view of adopting the single European currency, the NMS will have to meet several rather rigid criteria which are meant to provide protection to the European monetary system against the possible macroeconomic shocks. The argument of maintaining the necessity to accomplish the nominal criteria of convergence comes from the possibility of weakening or even destabilizing the European monetary system by the integration of economies with serious misbalances, while protecting the economies of the countries adopting the euro from the possible shocks due to the direct confrontation with this area. This is why, within the current context of the global economic and financial crisis, the analysis of the level of accomplishment of the criteria for nominal convergence in the new member states shows their readiness to adopt the single European currency. Although it was paradoxically thought that the new member states might create a possible adverse shock for the euro zone, some of the euro zone member states which did rather well under the conditions of the global economic and financial crisis, such as Greece, Ireland, Portugal, Spain, induce an increasing pressure on this monetary zone. It is therefore possible that the new evolutions form the argument for an even higher “rigidity”, more precisely the accession to the euro zone is done only on sustainable bases (particularly as concerns the fiscal criteria!).

Within the current context of the global economic and financial crisis, the new member states of the European Union which are not yet part of the Economic and Monetary Union, felt at full scale the devastating effects of the crisis as shown by the deteriorating main macro-indicators and by the increasing economic instability. Under the conditions of the economic crisis, the accomplishment of the criteria for the nominal convergence, required for the adoption of the euro, is a real challenge for all the new member states materialized primarily in the increase of the exchange rate volatility and of the fiscal-budgetary deficits.

After the start of the financial and economic crisis in the emergent countries (after September 2008), the **inflation** was tempered in the NMS because of the sudden drop in the economic activity and subsequently, due the correction of the misbalances; the propagation of the shocks from the international markets of the raw materials also affected NMS economies. Thus, the foreign pressure of the price for the agricultural products, oil and other goods decreased significantly, the direct effect being lower prices for energy and food, while the indirect effect being the decrease of the price of imported raw materials. The economic recession meant lower pay raises, constraints to the crediting activity and a lower consumption, affecting the domestic prices in these countries. In the inflation targeting countries, the evolution of this indicator was more sinuous, but with less dramatic decreases, however, compared to the countries targeting the exchange rate. Although the evolution of the inflation is on a descendent trend, this indicator exceeds the reference value in most NMS, except in Czech Republic and Lithuania. On the long term, we consider that the relation of the wages to the work productivity will be the determining factor for the evolution of inflation. The economic crisis reduced the positive gap between the wages and work productivity in the NMS, but the further reduction of the difference depends on the implementation of the structural reforms and on a prudent behaviour of the fiscal policy.

The convergence reports of the European Commission and ECB (2010) also considered negative figures for the reference value of the inflation indicator. Under the current conditions characterized by the incidence of significant commune adverse shocks (global financial and economic crisis, strong pressures to decrease the prices etc.), the authorities consider that the negative inflation is a significant marker for price stability in the European countries. Our analysis has shown that the negative inflation rates reflect the dramatic corrections undertaken in the countries which had unsustainable development in the past or which have adapted to the new macroeconomic environment by the austerity measures that they have adopted, on the background of a serious economic recession. However, in our opinion, this doesn’t justify taking negative values in calculation.

The global economic and financial crisis which prompted a revaluation of the general macroeconomic situation, the market of the long-term bonds also suffered. Thus, almost all the new member states displayed an increase of the differentials of the **long-term interest rates** in relation with the average value of the Euro zone during the analysed period (August 2008 – August 2010). As the national and international vulnerabilities increased and as the budgetary performance deteriorated, both in the Euro zone and outside it, a stronger differentiation occurred between the NMS in terms of meeting the criterion of long-term interest rates convergence. According to the Maastricht Treaty, of the new member states, only Czech Republic accomplished this criterion of convergence. Poland and Bulgaria reported values somehow in the proximity of the reference value, while Latvia, Lithuania, Hungary and Romania reported values of the long-term interest rates much above the reference value. At the end of 2008 and in the first half of 2009 (particularly in April-August 2009), on the background of increasing tensions on the international financial markets, of the fast deterioration of the public finances, of the decreasing ratings for loans, of the lower volume of liquidity and of the general deterioration of the internal economic conditions, the long-term interest rates soared and peaked in all NMS. During the second half of 2009, and in early 2010, the situation of the long-term interest rates improved significantly (with the exception of Latvia), when the risk aversion decreased worldwide and the perception of the participants on the financial-monetary market regarding the fiscal evolution improved, within the context of the conditions set by the international programs of financial assistance (IMF agreements) and of the anti-crisis measures. However, the current adverse fiscal evolutions, particularly in the euro zone (see the case of Ireland), will produce more tension on the international markets, particularly during the subsequent period, and will certainly be noticed in the higher risk premiums, implicitly, in the higher long-term interest rates, both in the euro zone, and in the NMS.

During the past two years, the financial markets of the countries participating in ERM II crosses period of high exchange rate volatility, which has generated strong tensions within this mechanism. The exchange rates of the currencies not participating in ERM II also experienced strong fluctuations in most surveyed countries, starting with the end of 2008.

Within ERM II, none of the central parities of the Baltic States has been devalued in the period April 2008 – August 2010. The national currencies of Estonia and Lithuania have been constantly rated at the established central parities. On the other hand, the exchange rate of the Latvian latus in relation with the euro fluctuated within the fluctuation band of ±1% assumed unilaterally.

Latvia doesn't meet the nominal criterion of the exchange rate. Only Estonia and Lithuania accomplished the nominal criterion of the exchange rate.

The Bulgarian leva didn't participate in ERM II, but it was anchored to the euro within the system of the monetary board. Although the leva was stable in relation with the euro, during the surveyed period, Bulgaria doesn't accomplish the nominal criterion of the exchange rate.

The Romanian leu, the Polish zloty and the Mahyar forint were subjected to pressures between mid-2008 and August 2010. This depreciation was stronger until April 2009 (compared to August 2008) within the context of a climate of high incertitude on the international financial markets, which reflected the bankruptcy of Lehman Brothers, the adverse economic prospects in the surveyed countries and the concern of the investors regarding the external vulnerabilities, under the conditions of a stronger risk aversion. The depreciation of the Romanian leu, has been also determined by the major internal macroeconomic misbalances. The subsequent and gradual normalization of the conditions on the international financial markets caused this depreciation to reverse partially.

The Czech koruna has depreciated during the second part of 2008 (because of the stronger risk aversion and of the deteriorating feelings for the emerging markets), but it appreciated for the entire year 2008. The depreciation of the Czech koruna from the second half of 2008 also continued in 2009.

Although the annual figures show that, generally, Romania, Poland and Hungary accomplished the nominal criterion of the exchange rate convergence, because of the daily strong fluctuations, these countries don't accomplish the nominal criterion of the exchange rate convergence.

The financial crisis had a strong impact on the **public finances** from the European countries. Although they have stated from rather strong positions in 2007, both the budget deficit and the public debt deteriorated considerably reaching values not recorded recently for the European Union. In 2009, the budgetary position of the euro zone has deteriorated for a second, consecutive year, reaching significant values compared to the previous year.

If in 2007, the **budget deficit** was lower than one per cent of the GDP in EU 27, for 2010, the economic forecasts show a value in excess of 7%, and a decrease in 2011. The deficit for 2009 exceeded the reference value of 3% of the GDP in most EU 27 countries. Of the new member states, Estonia was the only exception, with a deficit of just 1.7% of the GDP in 2009. A very strong negative impact was felt outside the euro zone with a very high deterioration of the GDP deficit in Latvia (10.2%), Lithuania (9.2%), Romania (8.6%) and Poland (7.2%). A lesser worsening was noticed in Hungary, Bulgaria and Czech Republic, with deficits of 4.4%, 4.7% and 5.8%, respectively.

The **public debt** in EU 27 was about 59% of the GDP in 2007, and the forecast for 2010 is close to 80%. In 2009, the public debt increased by 9% in the euro zone compared to the previous year, reaching 78.7% of the GDP. The aggregate figures tend to mask the different evolution of the EU member states. Of the NMS candidate for the euro zone, Hungary is the only one exceeding the reference value of 60% of the GDP, from 2005 throughout 2009, when it reached 78.4%. The forecast shows the same level for 2010 and a slight reduction in 2011. Of the new member states which have joined the euro zone, Malta is the only one exceeding the reference value in 2009, with 68.8% of the GDP.

The strong deterioration of the fiscal indicators is due both to the automatic effect of the economic productivity, and to the measures taken by the governments of the EU member states. The measures introduced in order to support the aggregate demand, particularly the financial sector, generated additional pressures on the public finances. While the monetary policy has reached the lower limit using very low interest rates, the interventions of the fiscal policy helped the economies to get stabilized.

In conclusion, the economic-financial crisis has adverse implications for the accomplishment of all the convergence criteria in the new member states. Thus, **the exchange rate stability is endangered by a high volatility of the exchange rates, the fiscal-budgetary deficit is affected mainly by the recession**, which acts to increase it**, the long-term interest rates are affected by a cumulated effect both in terms of the monetary indicators, and in terms of the fiscal-budgetary indicators, while inflation tempering** (currently in the stage of de-inflation) **can rapidly turn into deflation.**

Sustainability is highly important for the accomplishment of the convergence criteria. The adoption of the euro is an irrevocable process, therefore the process of convergence must be accomplished in a sustainable manner, not just in a particular moment. The achievement of a high level of sustainable convergence in the NMS requires a significant intensification of the efforts of these countries. These efforts refer mainly to the need of achieving and maintaining a sustainable price and exchange rate stability, to the reduction of the large budget deficits and to the accomplishment and maintenance of an optimal level of the public finances.

In 2009, the **foreign deficits** of the EU member states not included in the euro zone decreased (both in nominal terms and as proportion of the GDP). In many countries the contraction was strong and the current an capital accounts passed from deficit to surplus. This was due to a strong reduction of the domestic demand and of the lower inflows of capital in the region, due to the enhancing global financial crisis. Consequently, the adjustment was strong in the countries which had reported the highest deficits before the crisis broke out – the Baltic States, Bulgaria and Romania.

These strong adjustments of the foreign deficits have been accompanied by a worsening of the financing conditions and by several major changes in the structure of financing. The net flows to "other investments" reversed in Czech Republic, Bulgaria, Latvia, Lithuania and Sweden and decreased in Estonia, Hungary, Poland and Romania. In some countries, such as Hungary, Latvia and Romania, the decrease of the flows of private credits has been compensated partially by the international and European programs of financial support. Compared to 2008, in 2009, the inflows of foreign direct investments continued to be lower in the NMS which had joined the EU in 2004 or subsequently, although Bulgaria continued to have net inflows of about 10% of the GDP. The evolution of the net flows of portfolio investments was rather heterogeneous: Denmark, Sweden and the United Kingdom reported substantial inflows, while Bulgaria, Estonia and Hungary reported outflows.

The difficulties of foreign financing which became chronic, as well as the associated restrictive macroeconomic policies continue to affect the domestic demand in Hungary, Latvia and Romania. On the other hand, in Estonia and Slovakia, the production starts to refresh because of the measures adopted before the crisis started, which provided these countries with more room for manoeuvres.

The period which elapsed since the start of the financial and economic crisis reflects the vulnerability of a development based almost exclusively on the massive inflows of foreign capital, under the conditions in which the risk aversion of the investors increased and the financing conditions became more severe. The cycle of the effects induced by the crisis didn't end.

The vulnerabilities due to the harsher conditions of foreign financing and to the high dependence on foreign funds for financing caused difficulties for the balance of foreign payments in some of the NMS (Hungary, Romania, Latvia) in the autumn of 2008, when the inflows of foreign capital contracted due to the international financial crisis.

On the medium term, the improvement of the foreign misbalance in the NMS must be supported by continued efforts for fiscal consolidation by policies which to stimulate job creation and a higher productivity, as well as by policies to improve the national capacity for export and to ensure a sustainable development of the domestic demand. The unfolding economic adjustment supports the relocation of the resources towards the tradable sectors, but it has to be accompanied by other policies too. The future growth must come from the tradable sector (the Latvian capitals are anchored in the non-tradable sector). The regulation of a flexible labour market and the provision of an attractive business environment are necessary in order to draw inflows of foreign investments. The matching of the wages and work productivity is essential for a sustainable domestic demand and for the foreign balance.

In the case of Romania, on the medium term, the foreign balance will depend much on the structural policies aimed to a favourable investment climate and to remove the hindrances to foreign investments[1], to improve the infrastructure (agricultural, roads, energetic, institutional, financial etc.) and the EU structural funds. A proper, consistent and coherent legislation of the investments may support properly and concretely a national program of investments which Romania needs.

---

[1] *The acting regulations are deficient and inadequate to the process of economic revival. The constraints to credits, the market incertitude and the low rates of using the capitals are the causes for the low rate of investments in Romania.*

Particular attention must be paid to the bank credits sector in Romania within the financing by viable projects. NBR should play an important role in the decrease of the banking interest rates and to stimulate the commercial banks to get actively involved in the Romanian economy.

Reforms in infrastructure, competition and company policy are required in order to draw direct foreign investments. The last two types of reforms should try to reduce the abuse of the monopoly position and to improve the effective corporatist control enforced through the financial institutions and national markets, thus supporting the market-generated reorganisation. The progress in some areas of infrastructures such as the decentralization and commercialization of the electric power may create new opportunities to draw foreign investors.

In order to stop the adverse effects of the crisis, the macroeconomic policies have been calibrated on the short-term to preserve the trust and stability of the financial-banking sector. In some cases, the foreign financing has been endured by IMF programs, by swap arrangements or by other kinds of agreements with the central banks from the developed European banks.

In the coming period, the **monetary policy** should support the domestic economies of the NMS. In these countries, the perspectives regarding inflation are mixed, which reflects the utilization of different currency systems and of different levels of contraction of the economic activity. However, the fear of increasing inflation starts to alleviate, being replaced by the fear of a falling demand due to the financial problems. In the NMS, the objective of price stability is complicated by the need to support the foreign stability under the conditions in which the financing flows still are rather uncertain.

The countries which are particularly confronted with difficult foreign conditions (current account deficit financed largely by new loans, frail inter-banking flows, formation of reserves) have “hardened” the monetary policy conduit in order to maintain the foreign stability, despite the adverse consequences for the domestic economy. The access to official financing (regional lines of credit and conditioned financing imposed by IMF) might alleviate the seriousness of the effects, but they would act rather on the short-term. On the long-term, the conditions imposed, by IMF form instance, will affect the evolution of the economies which asked for such loans.

In the countries which joined the ERM II, given the limited space of action of the monetary policy, within the context of the current flat exchange rate systems assumed within the unilateral agreements, it is imperiously necessary that the other policies support the economy in order to cope with the specific national shocks and to avoid the re-emergence of the macroeconomic misbalances.

The **fiscal policy** should compensate the limited capacity of the monetary policy under the conditions of the economic recession, being an important short-term support for the economies. However, the space to supply such support will be limited if the efforts in this direction erode the credibility in the absence of a medium and long-term vision. Hence, the **fiscal policy must be calibrated in order to stimulate the economy under conditions of sustainability and it must be prudent**. Thus, under the conditions of the crisis, the governments are confronted with a difficult problem – to apply a short-term expansive policy to stimulate the economy or to apply a restrictive economy which the decrease large fiscal-budgetary deficits. This problem turns more difficult as the return from crisis seems ever farther away. The fiscal space is an important characteristic of the economy which can help it during the crisis. A larger fiscal space provides the possibility to apply incentives without affecting the sustainability of the public finances.

The immediate reaction of the fiscal policy in the NMS depended on the fiscal "barriers" from the pre-crisis period, on the currency exchange system and on the stage of the economic cycle in which the economy is. The countries which already had a vulnerable fiscal situation, such as Hungary, accelerated the measures of fiscal adjustment. For the Baltic States, the maintenance of their monetary systems (anchoring the exchange rate) required strong measures of consolidation, although their public debt was rather low. On the other hand, other countries could let the automatic fiscal stabilizers to work, or to allow the discretionary fiscal relaxation.

One of the consequences of the current crisis is the increase of the public debts to unseen values. Even the debts of the rich countries turned unsustainable.

A high level of the **public debt** has significant negative effects on the economic growth. The negative effects come from the impact on fiscality. The size of the impact depends, partly, on the way in which the risk premium is affected by the increase of the debts. Much greater effects appear in the cases in which the risk premiums spread within the entire economy, as it happens under the current conditions.

A practical problem, of utmost importance, is the knowledge of the level at which the public debt becomes unsustainable, so as to take in good time useful measures to protect the economy from a possible overstepping of the limit of the public debt.

The last studies published by the International Monetary Fund (September 1, 2010) argue that despite the very high public debts (expressed as percentage of the GDP), many countries still have room for fiscal manoeuvres. They argue this hypothesis by the fact that, generally, the countries tend to respond to the emergence of high levels of the debt by cutting the debts, but differ in their ability to do this. Each country will have a limit of the debt which is partially a function of its history of fiscal consolidation. According to the calculations of the economists from the International Monetary Fund, the theoretical limit is much higher than the current or forecast (short-term) debt even for countries with huge debts such as the United Kingdom and the USA.

Refreshing the public debts may turn difficult much before they reach the limit of unsustainability, as shown by the case of Greece.

For the countries with a low probability for the existence of the fiscal space, the message is that they need fiscal adjustments which to take them away from their fiscal history. Even the countries with a wide fiscal space should make medium-term adjustments in order to take into calculation the engagements and future debts.

The International Monetary Fund warns that many countries with developed economies have too large debts entailing serious risks, but it discouraged the hypothesis of a sovereign bankruptcy in Europe. The Fund claims that several countries are dangerously close to the upper limit of the debts, a threshold which might cause the financial markets to perceive a risk of bankruptcy and to react defensively, by increasing the interest rates for the new loans.

The options to reduce the risk of unsustainability include: increasing the fiscal effort for several years in order to reduce the public debt from the higher admitted level, or structural reforms of the institutions which have close connections with the fiscal space and which may have a permanent impact on the surplus-generating capacity.

The economic revival and the reduction of the interest rates are not enough to stabilize the public debt in the region. In most EU 10 countries, the negative primary balances will continue to increase the percentage of the debt within the BDP in 2010. According to EC prognosis, the level of the public debt will exceed 40% in 2011 in all EU 10 member states, except for Estonia, Bulgaria and Romania. The economic literature suggests that the levels of the public debt in excess of 40% of the GDP produce unrest in the financial markets from the emergent countries. Even in this situation, the level of the debt is below the euro area, except for Hungary, partly due to the reforms to improve the fiscal sustainability of the pensions system.

The measures of consolidation set by the Pact of Stability and Growth are no longer enough to stabilize the level of the debts. It is important that the countries continue their progresses to accomplish the medium-term budget objectives. The policies of fiscal consolidation should include strengthening the national budgetary context in order to put to use the credibility of the measures and strategies aimed to support the medium- and long-term fiscal sustainability. Additional structural reforms are required in order to improve productivity and to support the long-term investments.

The consolidation started under adverse economic conditions may be more efficient, even of the conditions are some of the most difficult. The consolidations based on expenditure were more successful in the past than those based on a higher taxation. It is not always a solution to increase the fiscality as a means for more revenue to the state budget. Thus, the increase of the flat rate might amplify the fiscal pressure and deter the investments. Also, an increase of the VAT without implementing criteria for lower VAT rates which the EU included in the directive in the VAT, may have adverse effects on the short-, medium- and long-term, slowing the economic growth. The increase of the direct and indirect taxes when tax evasion is high will only encourage the tax payers to avoid paying.

At the same time, the fiscal consolidations done gradually seem to be more successful than those applied all at once. The results depend largely on the undertaken structural changes too.

The past experience has shown that many times the fiscal consolidation is done to the detriment of the public investments, which affects the economic growth that is vital in order to reduce the debt. The level of economic growth, the level of the debt, of the deficit, of the taxes and expenditures influence the type of measures which need to be taken in each country. The context in which the measures have to be implemented is of similar importance.

Depending on their fiscal results the NMS can be divided in four groups (Staehr, 2010):

- Hungary, Latvia and Romania, which asked financial support from IMF and which directed their fiscal policies towards meeting the conditions imposed by IMF (constrained fiscal policies);
- Czech Republic and Poland followed a rather expansive policy meant to counter the effects of the financial crisis;
- Bulgaria and Estonia maintained a restrictive fiscal policy at the price of slowing the economic activity (negative growth and deflation);
- Lithuania managed to finance its large fiscal deficit without loans from IMF.

It is necessary to continue the efforts to reform the markets for goods and services and the labour market as well, making them more flexible and more favourable to economic expansion and higher employment. In the countries within the ERM II, given the limited room of action of the monetary policy, within the context of the flat exchange rate system, it is imperiously necessary for the other policies to support the economy thus coping with the national shocks and avoiding new macroeconomic misbalances.

The current global economic-financial crisis caught Romania with an economy insufficiently restructured after 10 years of fast, unhealthy economic growth based on the consumption of imported goods. Romania had a high deficit of the current account (about 13% of the GDP in 2007) when the crisis started, as well as a very high level of crediting (about 60%). The evolution of the current account deficit until 2007 yields the conclusion that the dynamics of the economic growth was hiding the core problem of Romania: it produced little but consumed a lot.

The intensification of the financial crisis made it increasingly difficult the economic recovery and the payment of the debts in the economically weaker countries (Portugal, Ireland, Greece and Spain). Therefore, the investors started to lose confidence in euro and be afraid that the European Monetary Union might collapse.

The worst scenario – break down of the euro zone – is, however, very little probable. However, the problems of the sovereign debt in Greece and in other “peripheral” countries have stressed the lack of political power in Europe. The European Central Bank sets the interest rate for the countries within the euro zone but it has no power on the fiscal policy. Hence, it is difficult for the European Union to overcome the current situation by taking direct control over the budget of the countries experiencing difficulties.

The threat to the euro is not on the short-term. Even if countries such as Italy and Spain will avoid bankruptcy for the time being, what will happen if the governments of these countries are too weak to impose the required reforms? Without the implementation of the necessary measures, the difference between the powerful states and the weak states from the euro zone might enlarge further.

In order to become sustainable, Romania needs to accomplish the nominal criteria and this calls for structural reforms: a budget deficit small or equal with 3% of the GDP requires the balancing and self-financing of the public system of pensions, while a stable exchange rate requires observing the correlation between the increase of productivity and the increase of the real wage.

The abundant liquidity created by the world banks and the desire of the oil and gas exporting countries to limit the appreciation of their currencies is one of the main causes of the financial crisis.

The challenges of the global financial crisis for the monetary policy can be approached under the following aspects: the monetary policy must look beyond the balance of payments and financing the immediate liquidity in order to support economic relaunch, growth and sustainable development; the liquidity and credit which are now pumped within the system risk to contribute to a future explosive cycle if this pumping is not regulated and monitored; the monetary policy from the developed countries needs to avoid developing policies, structures and norms which undermine or exclude the interests of the developing countries.

Within the context of the effects of the global financial crisis on the euro, the convergence of the monetary policies of the NMS outside the euro zone with the monetary policy of the euro zone will be affected by factors and causes specific (endogenous) to the monetary and financial space and by exogenous causes specific particularly to the real and nominal space of the economy (production, workforce, investments, prices etc.).

One may say that there will be a differentiated distancing of the monetary policies from the real policies; this differentiation will depend on countries, sectors of activity and time and will generate distortions, lags and deregulation of the processes and phenomena of the monetary policies, which can be called deficits of convergence; among these deficits are:

- Misbalances in the convergence of the saving potential and on the instruments used to collect the availabilities, as well as in the convergence of the monetary (liquidities), banking (saving) and financial (placements) flows;
- Misbalances in the convergence of the placement flows and circuits and in the use of the availabilities, in the supranational coordination of the financial funds and markets;
- Misbalances in the institutional and regulatory convergence of the national financial systems and in the convergence of the modalities to implement the decisions of financial-banking management;
- Misbalances in the convergence of the instruments and techniques used to cover the risks and manage the liquidity crises;
- Misbalances in the convergence of the configuration and dynamics of the financial and monetary markets towards the establishment of a single financial market based on confidence, equity and functional harmonisation;
- Misbalances in the convergence of the indicators evaluating the transparency of the efficacy and stability of the financial , monetary and banking systems and markets;
- Misbalances in the convergence of the prices, due dates and conditionality of the saving and investment financial-monetary flows, as well as in the convergence of company, state, population and banking institutions liquidities in the euro area.

The measurement of the level of monetary convergence, thus of the deficits of convergence can be done using a set of structural and operational indicators derived implicitly from the explorative content of the mentioned deficits.

Such indicators can be approached in a dual manner, as shown below:

f) Functional indicators which show the functional convergence of the monetary policies and operational indicators which show the instrumental convergences of the monetary policies;

g) Economic indicators, divided in indicators of the real convergence of the real sector of the economy and of nominal convergence, of the financial-monetary sector of the economy;

h) Institutional indicators (which show the convergence of the institutions – attributes, responsibilities, competencies – involved in the accomplishment of the monetary policies) and regulatory indicators – rules, norms, procedures – aiming a harmonized application of the monetary policies;

i) Flow indicators (aiming the convergence of the nature and dimension of the financial functions) and structure indicators (aiming the convergence of the relations and interdependency between the entities, instruments and variables of the monetary policies);

j) Descriptive indicators (aiming the convergence of the different aspects, dimensions, variables of the monetary policies) and prospective indicators (aiming the convergence of the dynamics, evolution of these aspects, dimensions and variables of the monetary policies).

Although the crisis of the NMS has been determined by external factors, being by definition an external shock because the recession from the developed countries gas stopped the inflows of capital, the domestic vulnerabilities and imbalances played a crucial role in the progress of the events and effects induced within the national economies. The crisis has revealed the significant differences between these countries, explained by the diversity of development during the transition years. The Baltic States suffered dramatic decreases of the economic activity, reflected by the strong depression of the GDP growth, while the GDP decreased in Poland, but without recession. The countries which generally managed to avoid an explosive phenomenon of the domestic demand increase and stimulation of crediting on the basis of the capital inflows displayed less adverse effects and less dramatic recessions.

During this period of great national, regional and international incertitude and turbulence which spanned all over the world, the NMS need a balanced mix of macroeconomic policies adapted to the new conditions, which will bring stability.

Long-term adjustments are required in the economic policies of many of the surveyed NMS due to the cumulated impact of at least four factors:

- The continuous convergence of the level of incomes in most NMS, which might generate additional pressure by higher prices or higher nominal exchange rates (or both);
- Avoid the build-up of new macroeconomic imbalances over the next period. This risk exists particularly in the situation in which the process of income convergence is accompanied by a strong expansion of crediting and by higher prices of the assets due, for instance, to the low of negative real interest rates;
- The necessity, in many countries, to transfer the resources from the sector of non-tradable goods to the sector of tradable goods, which requires the substantial increase of the contribution of the exporting sector;
- The demographic structure, which is anticipated to suffer rapid and important changes over the next years.

References

1. European Central Bank (2010), *Convergence Report 2010*, Frankfurt am Maine
2. European Commission (2010a), *Convergence Report*, Economic and Financial Affairs Directorate, European Economy, Special Report nr.3/ 2010
3. European Commission (2010b), *European Economic Forecast - Spring 2010*, Directorate-General for Economic and Financial Affairs, European Economy 2/2010
4. European Commission (2010c), *Macro structural bottlenecks to growth in EU Member States*, Directorate-General for Economic and Financial Affairs, Occasional Papers 65/July 2010
5. European Commission (2010d), *Public Finances in EMU - 2010*, Directorate-General for Economic and Financial Affairs, European Economy 2/2010
6. International Monetary Fund (2009), *World Economic Outlook,* aprilie
7. International Monetary Fund (2010), *Regional Economic Outlook. Europe. Building Confidence,* October
8. Pop, Napoleon et al. (2008), *Evaluarea politicilor macroeconomice ale țărilor membre ale Uniunii Europene, din punct de vedere al proceselor de convergență necesare adoptării euro (Evaluation of the macroeconomic policies of the EU*

member states in terms of the processes of convergence required to adopt the euro), Research project CCFM „Victor Slăvescu", Bucharest.

9. Pop, Napoleon şi colectiv (2009), *Tendințe în conduita politicilor macroeconomice de adoptare euro în noile state membre ale Uniunii Europene. Performanțele politicilor macroeconomice ale României în adoptarea monedei unice europene (Trends in the conduit of the macroeconomic policies of adopting the euro in the new member states of the European Union. Performance of the macroeconomic policies in Romania with the view to adopt the single European currency)*, Research project CCFM „Victor Slăvescu", Bucharest.
10. Staehr, Karsten (2010) - *The Global Financial Crisis and Public Finances in the New EU Countries from Central and Eastern Europe*, Working Paper Series 2/2010, Bank of Estonia

*** Annual reports (2008, 2009), Monthly bulletins 2010 and Reports in the financial stability of the central banks