Globalization – Chances or Risks

MĂDĂLINA ANTOANETA RĂDOI
Finance – Accountancy Department
„Nicolae Titulescu" University
185 Calea Văcăreşti, 4th District, Bucharest
ROMANIA
madaradoi@gmail.com

ALEXANDRU OLTEANU
Finance – Accountancy Department
„Nicolae Titulescu" University
185 Calea Văcăreşti, 4th District, Bucharest
ROMANIA
aolteanu@univnt.ro

Abstract: - There are for and against arguments as regards the process of globalization. But what is globalization: a concept, a reality or a state as such? We can consider that globalization reflects the natural continuity of a process that appeared a long time ago and that has evolved ever since or a new phenomenon that was generated by the speed with which new technology and information flow. Milton Friedman, a fervent supporter of globalization, gives an answer to the question "what is globalization"; according to him, "globalization is not a simple tendency or phantasy but rather an international system. It is the new system that has replaced the Cold War system and that, like the former one, has its own laws and logic, being able to directly or indirectly influence today's politics, the environment, geopolitics and the economy of every country in the world." (Friedman, 2000). Globalization represents: the unlimited ascend of technology, the free flow of information, the annihilation of territorial limits, the uniformity of economy, the free flow of capital, the mobility of the person, as well as a political form of organization that aims at a future global government.

Key-Words: monetary policy, financial policy, sudden-stop, sovereign debts crisis, sudden formation of fixed capital, aggregated offer, aggregated demand.

1. Introduction

According to Lester Thurrow (2003), globalization - which is a phenomenon specific for the last two decades of the 20^{th} century - comprises two stages. The former one covers the '50s, '60s, '70s of the last century. It was mainly characterized by the fact that it was run by governments and directed by political decisions. Commercial agreements were at the basis of the globalization process and they were meant to cut taxes and, in consequence, the costs of traded products. The General Agreement on Tariffs and Trade (GATT), launched in the '60s, aimed at ensuring a free and global commercial regime for capitalist states. Important measures were taken at the time for liberalizing commerce; they were steps in accomplishing a form of "integrated capitalism". The second wave of globalization, specific for the '90s, is different because it relies on various technologies (microelectronics, computers, robots, telecommunication, new materials and biotechnology) that have generated a new form of economy, i.e. "knowledge-based economy". Corporations, which perform their activity at global level, have understood the force of new technology and have promoted them as new vectors of progress. Detractors of contemporary financial globalization insist on the inconvenient aspects which globalization poses, especially on the most visible ones: variable exchange taxes and financial instability. Thus, at the end of the 19^{th} century, the intensification of international financial relations was accompanied by a progressive generalization of fixed exchanges: gold started to be used as a hallmark between 1880-1913 in most of the countries; contemporary financial globalization started to develop in 1971, i.e. once the fixed rate exchanges, which were set up in 1944, ceased to exist subsequent to the agreements concluded at Bretton Woods. To Milton Friedman and Harry Johnson, who praised the qualities of stability, monetary flotation did not have the beneficial effects which they wished it could have. First of all, if - within an international context of strong capital mobility - the flexibility of exchange taxes is compatible with the perpetuation of important external unbalance, the very nature of this unbalance represents a problem. Secondly, the differences existing between the exchange rates of different currencies are obviously excessive. After the second half of the '80s, "excessive" volatility was explained either by maintaining the ordinary hypotheses of rational forecasting and homogeneity or by explicitly taking into consideration informational imperfections of financial markets and, particularly, of exchange markets. Modern economic analysis allows us to draw conclusions on the beneficial nature of financial globalization. Thus, apart from the frequent hypotheses of informational efficiency that characterizes financial markets international free capital movement favours an optimum distribution of financial resources at global level. Countries which have high national revenue do not invest this profit in national economy. In consequence, capital will flow from countries which have high capital towards countries whose capital is low; the law of diminishing returns will ensure a polarization of international financial flows from developed towards less developed countries. Apart from these "static" theoretical advantages posed by international financial liberalization (understood as resources allotment), several recent analyses have revealed the existence of "dynamic" advantages for contemporary international capital transfers. Even if these transfers are accomplished through direct foreign investments, they may also be accompanied by technological transfers that favour the spread of technological progress (Steinherr, 1992).

From a theoretical point of view, globalization offers the key for progress since it implies transparency, high quality standards and environmental protection. Briefly speaking, globalization refers to all that contributes to the improvement of living conditions at global level. However, globalization does not bring benefits to all states in a similar way. In the 20th century, the global average of personal income grew for some countries and it decreased for others. Although incomes grew, inequalities were more prominent than they had used to be at the beginning of the century.

The World Development Report 1999-2000: Entering the 21st century had as a main topic the impact of globalization over the poor people. The report shows that, on the basis of the present analyses, the number of poor people is going to increase. In 2015 it is estimated that the global number of poor people could amount at 1.9 billion. Moreover, considering the recent tendencies, inequality existing between industrialized countries and developing countries is going to become more acute. Consequently, reality contradicts the concept of globalization.

However, globalization offers a chance to poor and developing countries to grow economically. Due to globalization, developed countries export not only capital and workplaces but also new technologies and higher working standards.

2. Globalization and economic governance in Europe[1]

The process of globalization and the economic and financial crisis have required the urgent adopting of new economic decision-making procedures and new instruments for the application of these procedures. Governance has acquired an economic dimension once the financial crisis emerged; the EU was obliged to react in order to protect its unique market and the Economic and Monetary Union. Lately the EU and its member states have taken important decisions that will lead to a better economic and budgetary coordination of the EU as a whole and of the Euro zone in particular. As a result, EU interdependent economies will find themselves in a better position so that they would be able to find a path towards economic growth and the creation of workplaces.

In 2010 a new approach to economic surveillance and a new policy making calendar were agreed upon. The goal of this agreement is to ensure that policies are analysed and evaluated at the same time and that those policy areas which were not previously and systematically covered by economic surveillance – i.e. macroeconomic unbalance and financial sector issues – will also be considered.

The new approach was firstly put into practice in 2011 through the first "European Semester". The European Semester, one of the two main components of the new governance economic and financial European mechanism, creates a means of exchanging information and coordination between member states as regards fiscal policy, macroeconomic unbalance, financial sector issues and structural reforms that are meant to

[1] Dochia Aurelian, "Reflectii privind noul mecanism de guvernanta economica europeana", *Revista Economistul*, 22 (10-16 June 2013), p. 122.

enhance economic growth at EU level. All these issues will be dealt with before governments start to devise their budgetary projects and to present them for being debated upon by national parliaments during the second half of the year ("the national semester").

This preliminary coordination of policies should bring more efficiency to the implementation of political orientation and help EU dimension be incorporated within the elaboration of national policies. The annual cycle starts with the annual growth enquiry elaborated by the Commission, which comes with a general approach to priority actions that are to be adopted at EU and national level. Member states present stability and converging programs for the fiscal and national reform programs as regards structural reforms and growth and employment stimulation measures. The Commission evaluates these reports on the basis of an integrated analysis that covers fiscal, macroeconomic and structural policies and makes recommendations for the policies that are to be developed by each country.

The second component of the above mentioned governance, i.e. the procedure devised for excessive unbalance, is meant to institutionalize a monitoring mechanism, which brings early alarm signals and which requires the intervention for preventing the repetition of those situations in which EU member states accrued unsustainable deficits or lost competitiveness due to economic policies that are inadequate for the process of globalization. This procedure devised for excessive unbalance is meant to impose 11 economic indicators that are included in the so-called "scoreboard". These indicators are: deficit/surplus of the current account (the average for 3 years) expressed as percentage of the GDP; net international investment position expressed as a percentage of the GDP; the decrease recorded for the last 5 years of the export market share and expressed as a percentage; the increase recorded for the last 3 years of the unitary cost of the workforce and expressed as a percentage; the variation recorded for the last 3 years for the effective exchange rate in relation to a number of 35 countries and expressed as a percentage; the debt recorded by the private sector and expressed as a percentage of the GDP; annual increase of the volume of credits granted to the private sector; annual variation of the real estate goods in relation to the deflation factor for the consumption as calculated by the EUROSTAT; governmental sector debt expressed as a percentage of the GDP; the average for the last three years of unemployment; annual variation of liabilities within the financial sector. For each of these indicators thresholds are established; if these thresholds are surpassed, this is a signal alarm. One should mention that countries which accrue surpasses of these thresholds are subjected to a thorough analysis of the economic situation; the conclusions that are drawn comprise either recommendations for deficits correction or the initiation of procedures to be applied for the excessive deficits which require for a corrective plan to be thought out, assumed, monitored and evaluated. Non-observance of the plan of action leads to the application of financial sanctions for the country that finds itself in this situation.

Under the present conditions of an accelerated globalization process, the effectiveness of economic governance must be reflected in the forecast, prevention and correction of the macroeconomic situations which pose a high risk and which exist in certain states.

Elisa Parisi Capone (2012) has made a test for 11 countries which are members of the Monetary Union and calculated the indicators included in the "scoreboard" for every year starting with 2000 and up to 2011, including the level of the threshold surpasses; this test adequately signals situations that pose a high macroeconomic risk. By adding the situations in which threshold surpasses occurred and by expressing them as a percentage for every indicator, she obtained an aggregated value of the macroeconomic unbalance instances for a country and for a certain year. The result revealed that in the last decade critical thresholds have been surpassed; thus, none of the 11 countries - which were part of this analysis - managed to permanently maintain itself within the prescribed limits. For instance, at the beginning of 2000 the aggregated indicator for Germany pointed out a percentage of over 250% of the recommended level; in Austria the aggregated surpass amounted at 160%, while in Finland the aggregated surpass was higher than 450%. These initial surpasses generated no consequences; countries managed to correct unbalance instances to a good extent. For countries like Greece, Portugal, Ireland or Spain indicators were permanently surpassed throughout the decade.

We should mention a weak point of these indicators, namely the insufficiently developed critical thresholds, a fact which makes them easily challengeable; thus, in the next period, these thresholds should be adjusted but not as an attempt to adapt to the present needs because this would not make the system credible. Another weak point of the system is represented by the fact that, for some instances in which there was an excessive surpassing of the thresholds, no sanctions were inflicted on several countries (e.g.: Germany, France, Greece, Italy, etc.).

As regards Romania, in the last decade our country has constantly and significantly surpassed the critical threshold, especially for the following indicators: the deficit of the current account; the liabilities of the financial sector and the variation of the actual exchange rate. In consequence, after the crisis broke out it was necessary for us to adopt the adjustment strategy; in 2012 this made it possible for Romania to have the best indicators on the scoreboard within the economic governance mechanism.

3. Conclusions

The illustration of globalization phenomena in the great economic and financial crisis led in 2009-2011 to a deterioration of Romania's economic potential. The growth rhythm of the GDP dropped from 4.5% in 2008 to 2.3% in 2009 and to 2% 2010-2011. This evolution was determined by the effects generated by the Great Recession: the sudden stop phenomenon of international financial flows affected Romania (e.g. the sudden stop phenomenon of the international capital flows, determined by the bankruptcy of the Lehman Brothers, has triggered the re-orientation of capital towards developed countries, which pose a lower risk); the crisis of the sovereign debts in Europe; the lack of domestic capital.

The slump recorded in investments in 2009 (the gross formation of the fixed assets dropped 24% year after year) led to an unfavourable evolution of the total productivity of production factors (whose contribution to the dynamic of the potential GDP decreased with 0.3 percentage point in 2008 to zero percentage points in 2009 and to -0.6 percentage points in 2011).

On the other hand, starting with 2013 the Romanian economy increased with 3.5% per year; this has been the best growth rhythm since 2008; this evolution is also determined by the excellent amount of exported goods (with a positive impact on domestic industry), and also by the excellent level of the agricultural production.

Similarly, demand has become stable on the domestic market and has attained a good level, a fact which is reflected by the retailing activity. At the same time, the gross formation of fixed assets became stable in the fourth trimester of 2013, after the decline recorded in the previous trimesters; this fact is reflected by the dynamics of direct foreign investments (+155% every year).

All in all, in 2013 Romanian exports increased with 10% year after year, from 49.6 billion EUR (the highest level ever recorded): the EU component increased with 8.8% every year, amounting at 34.5 billion EUR, whereas non-EU component increased with 12.8% every year, amounting at 15.1 billion EUR. On the other hand, imports increased with 1% every year, amounting at 55.3 billion EUR, this evolution being mainly determined by the EU component (+4% every year, to 41.9 billion EUR). The non-EU component has decreased with 7.2% every year, amounting at 13.4 billion EUR.

Thus, the deficit of the commercial balance was corrected with 40.8% every year, to 5.7 billion EUR: the EU component enhanced with 13.9% every year, amounting at 7.4 billion EUR; the non-EU component recorded an excessive level of 1.7 billion EUR, which is comparative with the 1.1 billion EUR in 2012.

The dynamic of exports in 2013 reflects an amelioration of international competitiveness for Romania and a phenomenon of economic inflection within the Euro Zone or reorientation of companies towards non-EU markets. On the other hand, the evolution of imports in 2013 illustrates the difficult atmosphere that characterizes real economy (for most of the year).

All in all, in 2013, the average unemployment rate amounted at 7.3%, from the level of 7%; this evolution was determined by the difficult investment environment.

Given the evolution of the macroeconomic and financial indicators at global, European and domestic level, the Romanian GDP is estimated to increase with 3.3% per annum in 2015; this evolution is reinforced by the re-launching of productive investments, a process which is signalled by the dynamic of several recent macroeconomic and financial indicators (this process is also illustrated by the curve of returns): decrease of financing costs in economy; gradual amelioration for the banking sector; macroeconomic and financial stability as illustrated by the low level of current account and budget deficits and by banking solvability; decrease of the financial deficit within the banking sector or of the inflection signals for non-performing credit rate; amelioration of the absorption rate for European funds.

Macro-econometric provisions illustrate that productive investments could increase with 9% per year in 2015.

Re-launching investments in real economy will determine the amelioration of the situation existing on the labour market (the annual average rate for unemployment could be reduced to 6.4% in 2015), generating a positive impact for private consumption. In this macroeconomic scenario, the main component of the GDP could speed up to 1.1% per annum for 2015.

As to the net level of the external demand exports are expected to develop, whereas imports are expected to be sped up. According to this macroeconomic scenario for 2015 exports will increase with 7.4% per annum, while imports are expected to increase with 5.8% per year.

At present, domestic economy seems to be ready to receive productive investment flows (both from the outer and the inner spheres).

It is important for the mix of domestic economic policies to preserve and ameliorate this macroeconomic scenario for Romania, contributing to the sustainable re-launching of economy.

The National Bank has implemented a set of measures that are meant to ensure a normalization of the monetary policy for the last months: reference interest has gradually dropped to the lowest level ever recorded: 2.25%; a process of gradual convergence has been initiated for the rates of the minimum obligatory reserves that are applicable to liabilities expressed in RON and in currency for credit institutions, which were directed towards the levels recorded in the Euro Zone; financial stability has been ensured for Romania.

As regards accession to the Euro Zone, the process of convergence (nominal and real convergence towards the Euro Zone) is dependent on an adequate mix of medium-term and long-term economic policies that will basically rely on: avoiding economic departures; reducing dependence on external financing by generating capital at domestic level; a sustainable level for fiscality; creation of public and/or public-private investment funds that should correspond to the present economic issues at stake: infrastructure, pensions, healthcare and education (World Macroeconomic Report, 2014).

In the absence of an adequate long-term mix of economic policies, Romania's economy risks to follow the same path that it has followed in the last decades, i.e. a short period of economic growth, followed by a longer period of adjustment.

References

[1] T. Friedman, "Lexus şi măslinul. Cum să înţelegem globalizarea" (Bucureşti: Ed. Economică, 2000);

[2] Thurow Lester, "Fortune Favors The Bold: What We Must Do To Build A New And Lasting Global Prosperity"(New York, USA: HarperCollins Publishers, 2003);

[3] Steinherr Alfred, "The new European financial marketplace" (London: Longman Press Publishing House, 1992);

[4] Dochia Aurelian, "Reflectii privind noul mecanism de guvernanta economica europeana", Revista Economistul, 22 (10-16 June 2013), p. 122;

[5] Capone Elisa Parisi, "Macroeconomic In balance Scoreboard – A visual ranking among 11 ex countries", Economitor (9th November 2012);

[6] World Macroeconomic Report, SSIF Broker, January 2014.