# THE GROWTH RATE OF PUBLIC DEBT IN ROMANIA - DETERMINANT OF A REAL STRATEGY MANAGEMENT

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**Abstract**
Contracting public debt is an omnipresent process in Member emerging. Low development of production capacities compared to consumption and investment, the existence of a reduced volume of savings internally, major imbalances in external plan or fluctuations in major capital are just some elements that determine the the orientation towards borrowings, and in particular to external funding. The growth rate in recent years emphasized, representing an issue of major importance for authorities, especially considering the sustainability of government debt. This may be evidenced at least by analysis of the level registered, of cost of financing and repayment period. In the paper is performed a descriptive statistical analysis on the evolution of growth in public debt and its structure by types of currencies, being presented and the factors affecting the maintenance of public debt to a sustainable level. The conclusion of the analysis carried out highlights a rapidly growing of the public debt in Romania after 2008, which requires the application of a clear strategy for its management so as to avoid the generated risks by high levels and inadequate structure.

**Key words** public debt, financing cost, repayment period, management strategy

**Clasificare JEL:** H 60, H 63

## 1. Introduction

Regardless of the organizational form of economy or the level of development of a country it is absolutely necessary a process of correlation between public spending and resources mobilized by the State in order to ensure welfare of the population. But, limited resources available the state to fund different economic or social goals requires dialing at borrowings. Thus, the realization of strategic investment, budget deficit, current account deficit, public debt refinancing and establishment of foreign exchange reserves are just some of determinants of borrowing process.

Establish optimal strategies for managing public debt is a goal of any governance in ensuring macroeconomic balance. In this respect, is necessary an optimum level of financing cost, corresponding of public debt structure, so, in the context of a real process of risks management, to ensure a control of the evolution of indebtedness. Cost funding is influenced by borrowings structure contracted (on external or internal market) and by the evolution of their specific yield (obviously, in the case of the variable interest). This may be increased if the currency risk is manifested by exchange rate volatility for the currency of denomination of external debt. At these risks are added and the refinancing risk (unable to be refinanced public debt) and market risk (difficulties in refinancing of public debt). As a result, the variety of risks that accompany the process of contracting public debt and the negative influences of rising public debt and the cost of financing, requires the substantiation of a public debt management strategy. In the context of previous specifications, it should be an analysis of the evolution of public debt in Romania, compared to the situation recorded in european plan. Thus, a comparison between the growth of public debt and the interest rate and the identification of the factors that significantly influence the development of state borrowing may represent important elements in establishing a point of view regarding the degree of the sustainability of public debt. To achieve these objectives, the paper is structured as follows: literature review; the analyze of the rate of growth of public debt and its structure; conclusions and references.

## 2. Literature review

The issue of public debt and its sustainability level is the subject of many debates in the context of registering a significant increase of borrowing by various countries. Important discussions were recorded in european plane, finalized by the Maastricht Treaty, with clear information on the budget deficit and the share of public debt in GDP.
Disregarding these by many countries has demonstrated the vulnerability of fiscal and budgetary policies in front of the economic challenges and generated the convergence of views regarding the need to apply a rules by sustainability on

medium and long term. Research carried out on the sustainable level of public debt have highlighted that it can not be represented by a exact numeric value but by that level of debt that allows payment of liabilities generated. Thus, it is considered that ,,a share of debt in of 150% is as sustainable as a share of 50% ” (Roubini, 2001) or that the debt level is determined of ,,the capacity of the national economy of generating primary surpluses, interest rate on markets that borrows the state, depending on the risk premium attached, and its economic growth rate (Socol, 2013). Also sustainable level of public debt must be analyzed in the light of the influence exerted on economic growth, according to the characteristics of each country. A study in the EU member states showed a balance of debt to GDP of between 80 and 94% for Member States of the EU from the period 1980-1995 and 53-54% for Member States from the period 1995-2010 (Mencinger et al, 2014). Another point of view expressed in literature specialzyed relate to maintaining a high level of public debt for a longer period of 5 consecutive years, which can generate the phenomenon,, overhang "- all income from national investments are assigned to creditors (Reinhard et all, 2012). At the same time, it is considered that, over some limits, a increasingly debt of level causes a low rate of long-term growth (Kumar and Jaejoon, 2010). Regardless of the opinions expressed, one thing is certain: public loans are a reality common, being extremely important to allocate their on productive destinations in order to ensure the capabilities of future defaults (IMF, 2003). Related to the level of public debt and its evolution in Romania, many economists considered that it is necessary to ensure his sustainability on long term, in a contrary case being possible to face with a situation similar to GreeceFor exemple, in the presentation of the Financial Stability Report 2015, the Governor of National Bank of Romania, said that should not get into such a situation, described at a television by the assertion ,,we were rich and one morning we woke up poor” (Isărescu, 2015). Also, a major importance has the budgetary deficit, because any increase of this (on amid to fiscal relaxation measures, increasing of salaries and others) can determine a growth of public debt (Dochia, 2016; Lazea, 2016). Moreover, the way in which it is managed public debt has to represent a strategic element both at national and European level (Grabara, Brezeanu and Paun, 2016).

## 3. The analyze of the rate of growth of public debt and its structure

According to previous explanations, the use borrowings for productive or unproductive goals represent an option for the various governance. As a result, effective management of volume and structure of public debt can exert a positive influence on economic development. Instead, the application of inadequate measures on categories of borrowings, contracting period, the cost of financing and currency of denomination can have negative effects both the stability and the future economic development. So, any debt management strategy should be linked to several essential aspects: its size and trend registered in the previous period; the cost of financing and the risk of increasing it; structure and terms of repayment to investors. As a result, these issues reflect the contents of the study conducted in Romania, but also in other EU countries. Regarding public debt, the relevant indicator is the share in GDP, taken into account under the Maastricht methodology, since it enables comparisons at European level (Table 1).

**Table 1 The share of public debt in GDP in the period 2004 - 2015**

| Country/group | 2004 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 |
|---|---|---|---|---|---|---|---|---|---|---|
| EU 28 | 60,9 | 57,5 | 60,7 | 72,8 | 78,4 | 81,1 | 83,8 | 85,7 | 86,7 | 85 |
| Romania | 18,6 | 15,7 | 12,3 | 23,2 | 29,9 | 34,2 | 37,3 | 37,8 | 39,4 | 37,9 |
| Bulgaria | 36 | 16,3 | 13,0 | 13,7 | 15,3 | 15,2 | 16,7 | 17 | 27 | 26 |
| Czech Republic | 28,5 | 27,8 | 28,7 | 34,1 | 38,2 | 39,8 | 44,5 | 44,9 | 42,2 | 40,3 |
| Poland | 45 | 46,4 | 46,3 | 49,4 | 53,1 | 54,1 | 53,7 | 55,7 | 50,2 | 51,1 |
| Greece | 102,9 | 103,1 | 109,4 | 126,7 | 146,2 | 172,1 | 159,6 | 177,4 | 179,7 | 177,4 |

Source: ec.europa.eu

From the data summarized in Table 1 it is clear that, from the group of countries analyzed, Romania (obviously except Greece) recorded the highest growth rate after the crisis of 2008, practically, the public debt being double in 2015 compared to 2004. This situation can be the result of pro-cyclical fiscal policies adopted in Romania, with consequences in the accumulation of deficits and, thus, increasing of public debt (Kumar, M.S., Jaejoon, W., 2010).

It should be noted that after 2013, there has registered a slight reversal of the two components (corresponding to the resident of creditor), at external government public debt in favor of internal debt. In addition, bond market development resulted in the reduction of debts to international financial institutions from 48.9% in 2011 to approximately 26.8% in 2015. Against this background, the cost of funding (regarded as average interest rates) was reduced both as a result of lower domestic interest rates and as the benefit of favorable interest rates for borrowing from international financial institutions.

Interest rate applied borrowing arrangements is an important indicator in determining a country's ability to secure the payment obligations generated by debt. Thus, studies to identify the correlation between interest rates and debt have shown that an increase of 100 basis points in the real interest rate, can cause an increase of 1.1% of GDP on public debt (Lungu, 2012) and that the relationship between the interest rate and the service of public debt is directly proportional (Moinescu, 2013). In addition, a comparison between the growth of public debt and interest rates provide information necessary to establish a country's ability to meet its payment obligations. In Romania the pace of annual growth recorded high levels of public debt between 2007-2010, surpassing the level of interest rates in that period (Table 2).

If it is into account the composition on currency (Table 2), it can be identified a growing trend in the range of 2002-2008 of the share of borrowings in local currency (from 21.08% to 59.7%) and significant decrease those expressed in dollars (from 39.22% to 9.17%). It is noted that euro borrowings exceed that into national currency, which requires special attention to the volatility of the exchange rate (a depreciation of the national currency could generate an increase in public debt as a percentage of GDP).

Table 2 **The dynamics and structure of public debt in the period 2002-2015**

| Years | Dp (mill. Lei) | $Rg_{PD}$ | Dp/PIB | The structure of government debt by currency | | | |
|---|---|---|---|---|---|---|---|
| | | | | Lei | Euro | USD | Others |
| 2002 | 43867,4 | 29,72 | 28,8 | 21,08 | 33,49 | 39,22 | 6,21 |
| 2003 | 51363,2 | 17,08 | 25,9 | 18,08 | 41,89 | 31,83 | 8,2 |
| 2004 | 55819,7 | 8,67 | 22,3 | 20,27 | 41,44 | 31,08 | 7,21 |
| 2005 | 59010,9 | 5,71 | 19,5 | 22,89 | 38,97 | 30,73 | 7,41 |
| 2006 | 63340,8 | 7,33 | 17,4 | 40,85 | 35,63 | 17,93 | 5,59 |
| 2007 | 82324,3 | 29,97 | 18,3 | 53,18 | 30,67 | 12,22 | 3,93 |
| 2008 | 109795,1 | 33,36 | 19,2 | 59,7 | 28 | 9,17 | 3,13 |
| 2009 | 147329 | 34,18 | 26,7 | 47,1 | 41,5 | 6,32 | 5,08 |
| 2010 | 194459,2 | 31,98 | 34,2 | 45,3 | 42,8 | 4,7 | 7,2 |
| 2011 | 223255,2 | 14,81 | 37,2 | 48,1 | 42,5 | 2,9 | 6,5 |
| 2012 | 240842,6 | 7,87 | 38 | 44,0 | 44,8 | 5,6 | 5,6 |
| 2013 | 267150,9 | 10,92 | 39,6 | 44,3 | 46,2 | 6,4 | 3,1 |
| 2014 | 295655,5 | 10,66 | 42,1 | 39,6 | 49,4 | 9,7 | 1,3 |
| 2015 | 315691,6 | 6,77 | 42,1 | 42,7 | 46,2 | 10,1 | 1 |

Source: www.mfinante.ro; own computation based on data from www.mfinante.ro

In the public debt management strategy for the period 2016 -2018, prepared by the Public Finances Ministry, the main objectives aimed the procurement of resources necessary to cover financing needs, in the context of minimizing costs on medium and long term; limiting financial risks that may affect the costs of government debt and expanding of the internal market bonds. [15]

The currency risk remains an important element in this strategy because Romania has not adopted the European single currency and the share of debt denominated in foreign currency is high (approximately 57.3% at the end of 2015). Next to it, the refinancing risk remains a very important element, that can generate the concentration of the repayments on short intervals.

## 5. Conclusions

At the level of many emerging countries recorded real problems in terms of the possibility of supporting important areas such as health, education, private sector development or ensuring important goals of economic growth and improved living standards.Data recorded on level of public debt shows that, public loans, contracted on foreign or domestic markets, have become increasingly a permanence of our days, at the level of many countries. Procurement of necessary resources of state can be achieved on domestic or foreign markets, differentiated process at Member state, especially in relation with the degree of development.

Thus, less developed countries have a high process of indebtedness in foreign markets, amid to the absence of resources to their markets, while developed countries are oriented mainly towards the resources on the domestic markets. As a consequence, internal and external level of public debt is the result of the combined action of internal and external factors, economical, financial or social and of the political and startegic decision adopted by various governments over time.

The problem of public debt sustainability is the most controversial aspect of discussions on the maximum threshold that can be achieved of it. The diversity of opinions expressed the literature converge nevertheless towards a common point: it can not establish with certainty a threshold level, and, moreover, can not generalize such a level for all countries (differences are generated by borrowing capacity, volume of resources collected, possibility of issuing its reserve currency).

In the Romania, level of public debt has doubled in the interval of just a few years, but, the reduction of interest rate and increased residual maturity compensates for this negative aspect. To ensure a reasonable degree of indebtness, it is necessary actuation to attract foreign investment, develop infrastructure and create jobs so as to ensure economic growth with positive impact on revenue collected and borrowed resources. It is also necessary to apply a founded strategy of Public Debt Management, both in terms of funding costs and risk that accompany it (currency risk, refinancing risk or the liquidity risk) and maintaining the primary deficit within reasonable limits. In a contrary case, the share of cost with public debt, (in present is by 1,6% of GDP) can record a significant level, with negative influences on the allocated resources for different domains (education, infrastructure, health, defense, culture, environmental protection and others).

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