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Implications of the Budget Deficit on the Labour Market in Romania

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Abstract

The budget deficit has now become a common phenomenon in many countries, amid a surge in public spending. In Romania, as well as in other developing or developed countries, this topic is one of the most difficult issues facing economic policy.

Under the current circumstances of economic activity, where financial needs are more advanced than available funds, budgeting at all levels is one of the primary issues, in particular by maintaining the principle of budgetary balance.

Structure and Content of the Article – the article is structured as it follows : introduction, main chapters and the last part which presents the final conclusions concerning the suggested topic (the consequences of budget deficit over the labour market in Romania). The means used to finance the budget deficit, e.g. the increase in fiscality, the decrease in public spending, or the increase of public debt, leave their mark on the evolution of the labour market on both short and long term, as mentioned in the article.

Key words: budget deficit, consolidated budget, labour market, public sector debt.
J.E.L. classification: E60, E62, H60, H61, H62, H68.

1. Introduction

During the making of the article we aimed to accomplish a number of objectives. The first and most important of them all consists in the analysis and understanding of the effects of budget deficit over the labour market in Romania. We tried to answer the questions concerning the real efficiency of a supra-state fiscal policy, the highlight of the limits of this type of policy and the quantification of the instruments and mechanisms through which the fiscal policy creates certain effects in the real economy.

As far as reaching the intended aim is concerned, we have used a methodology which mostly entails descriptive research, critical comparative analysis, synthesis, deduction and foreseeing.

2. Theoretical background

The concept of deficit is used in Romania (Bistriceanu, 2006, p.189) to define the conventional deficit, the primary and the operational deficit, plus the structural and quasi-fiscal deficits following the modern methods of sizing the public financial imbalance.

The conventional deficit is determined (Hoanţă, N., 2000, p.62) by decreasing the actual payments and is the need to finance the public sector. In this method, earnings do not include domestic or foreign borrowing. Expenditure does not take into account public debt repayments for the year, but reflects the interest on government debt.

The primary deficit of the consolidated general budget removes the government debt interest expense from the conventional deficit. In other words, lowering the level of public expenditure, the public revenue reported at the level of one year gives us the size of the primary deficit of the state.

The operating deficit includes the primary deficit and the actual interest paid on the domestic public debt account.

The structural deficit eliminates from the conventional deficit the amounts obtained from privatization, which are valued as sources of financing rather than revenues.

The quasi-fiscal deficit reveals the conventional deficit and quasi-fiscal operations in the form of:

• Interest subsidies on loans granted by the NBR and commercial banks to state-owned companies in the agriculture and energy sectors;
• Subsidies for the exchange rate benefiting the energy sector;
• Loans taken by the state under special laws;
• State-guaranteed loans;
• Budget arrears of economic agents.

Quasi-fiscal deficits can push the consolidated general government budget by oversolding the deficit, so the government is forced to borrow more from the foreign market. In principle, there is a positive relationship between the quasi-fiscal deficit, the government debt and the operating deficit changing in the same direction if direct investment decreases and exports are reduced in parallel with imports.

Starting from the literature (Bistriceanu, 2006, p.191, Călin, M., 2006, p.129), it is noticed that in our country, in the extremely complex climate in which the economic activity takes place, in the effort of shaping the place that the budget deficit possesses, a special role is given to the identification of the weight of the budget deficit in the expenditure and revenues structure of CGB - Consolidated General Budget.

Considering that the consolidated budget is an instrument of the fiscal-budgetary policy, this one, in addition to the correlation between the revenues and expenditures of the state budget, also captures the connections between them, such as the budget deficit, the current account of the balance of payments the balance is deficient and the gap between investment and saving.

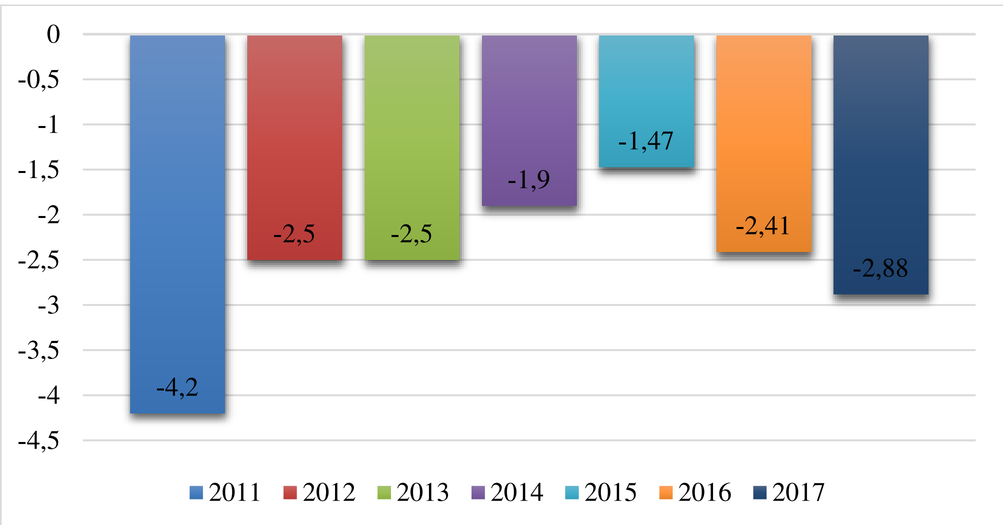
Nowadays, the understanding of the budget deficit and the interest for its continuing diminution are of great importance for Romania, especially in the context of our country facing big problems in the evolution of the economy.

Analysis of statistical data related to the Romanian budget deficit

In the following, some statistical data regarding the evolution of the budget deficit, its weight in the Gross Domestic Product as well as the structure of the general consolidated budget during the period 2011-2017 are captured.

The graphs below show the level and evolution of the general consolidated budget as a share of gross domestic product.

Graph no.1 Evolution of the budget deficit in the period 2011-2017

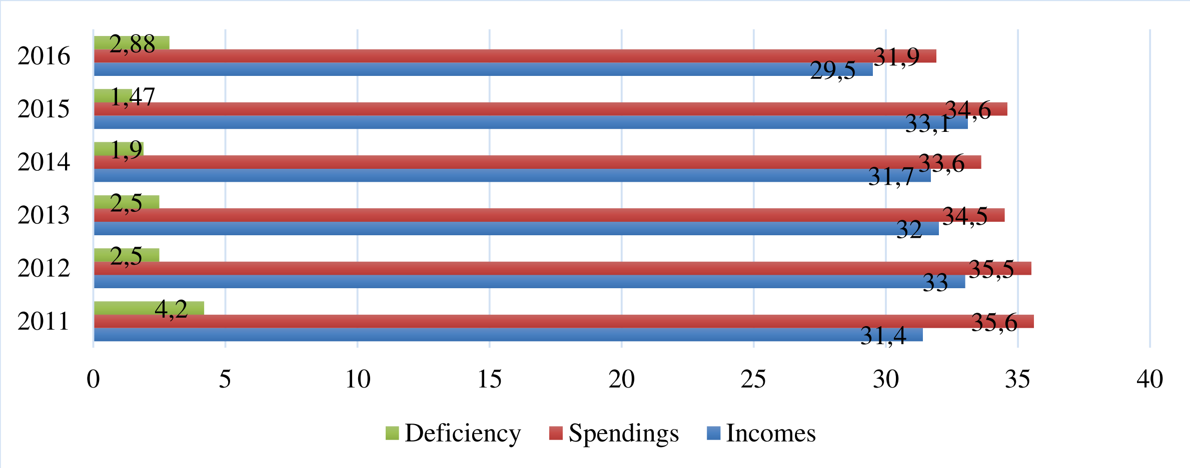


Source: Ministry of Public Finance , http://www.mfinante.gov.ro

According to the graph above, it can be noticed that the largest deficit is recorded in 2011 of -4.1% of GDP. This was due to the economic crisis that has developed globally. The budget deficit further shows a downward trend reaching -1.47% of GDP in 2015. In recent years, this negative development is caused by the fiscal reforms adopted by the government in 2015 (wage growth, non-taxation of pensions below 2000 lei).

Considering the structure of the BGC over the period 2011-2017, there is an increase in expenditures due to the reduction of revenues.

Graph no. 2 The structure of the General Consolidated Budget



Source: Ministry of Public Finance, http://www.mfinante.gov.ro

From the above graph, it is highlighted that 2011 was the largest gap between revenues and expenditures with a direct impact on the budget deficit of 4.2% of GDP.

It can also be highlighted that in 2012 the revenues increase without a substantial change in spending, this resulted in a deficit reduction of 2.5% of GDP.

In 2013 and 2014, these prospects remain, expenditure is lower than revenue. In 2015, the smallest cash deficit is recorded in the entire analysed period.

In recent years this trend changes, revenues begin to decline at a rate advanced over expenditure at the end of 2017 reaching a budgetary imbalance of -2.88% of GDP. This evolution was driven by the fiscal loosening that began in 2015.

3. The impact of the budget deficit on the labour market

Over time, the literature has circulated more currents of opinion according to which we can study the impact of the budget deficit on the economy. First, are taken into account the short-term effects on short-term consumption and long-term effects on the national economy, investment and job creation.

Secondly, the long-term deficit neutrality hypothesis is hypothetical by financing it on the basis of public debt contracting.

Table no.1 Evolution of the number of employees and unemployed in the period 2011-2017

Indicator / Year	2011	2012	2013	2014	2015	2016	2017
Average number of employees (thousands of persons)	6153	6230	6271	5850	6062	6201	6390
Unemployed at the end of the year (thousands of people)	461	494,7	512,3	478,3	436,2	418,2	351,1
Unemployment rate (%)	5.1	5,59	5,65	5,29	4,9	4,77	4,02

Source: National Institute of Statistics, http://www.insse.ro/cms/

So it appears that the budget deficit is a result of lower volume of economic activity on the one hand, with the impact of reducing the income of individuals and legal entities, which means a reduction in the tax base, so a reduction in revenues. On the other hand, the existence of a large budget deficit implies a decline in government investment, with consequences for jobs as well as budgetary spending on employment.

The methods used to finance the deficit, for example: increasing taxation, reducing public spending, increasing public debt, are impacted on the short and long term labour market.

Thus, considering the implications of short-term budget deficit causes a decline in the national economy, leading to a reduction of supply on the market, implying an increase in interest rates. In this situation, the volume of investment diminishes, consumption decreases, with effects on the capacity of economic activities and jobs.

According to the table it is pointed out that the number of unemployed oscillated during the analysis period from 461 thousand in 2011 to 351 thousand in 2017. In 2017, the highest percentage of employees and the lowest number of unemployed were reached. In 2014, there is an increase in the number of unemployed and a decrease in the number of employees, which shows a decrease in the volume of economic activity, with consequences on budget revenues and budget expenditures.

4. Ways to reduce the budget deficit

The budget deficit leads to an accumulation of public sector debt. If deficits are unsustainable, this can lead to higher bond yields (higher interest payments), and at worst, lead to a loss of confidence in the government. Although this is rare for countries with their own currency (ie not in euro).

The obvious way (Jackson, J., 1997, p.217) to reduce the budget deficit is to increase tax rates and reduce government spending. However, the difficulty is that this fiscal tightening may generate lower economic growth - which in turn can cause a higher cyclical deficit (the government gets less tax revenue in the recession). The best way to reduce tax deficits depends on the situation of a country.

Different policies (Moşteanu, T., 2004, p.78, Ştefură., G., 2007, p.115) to reduce budget deficit:

1. Reducing government spending

The government can reduce its public spending to reduce the fiscal deficit. For example, in the 1990s, Canada significantly reduced its public spending. They have evaluated many departments and have cut spending by up to 20% over four years. This proved to be a successful policy in reducing the budget deficit. During this period of spending cuts, the Canadian economy continued to grow, which also contributed to a reduction in the budget deficit.

In the 1920s, the UK drastically cut spending (known as Geddes Ax), but, combined with the gold standard (fixed exchange rate), it contributed to deflation and lower growth. Therefore, during this period, attempts were relatively unlikely to reduce debt to GDP.

In the Eurozone crisis, many European countries have cut government spending to try to reduce budget deficits. For example, Greece, Ireland and Spain have cut spending. However, these spending cuts have contributed to a decline in economic growth, which has led to lower tax revenues and debt growth. These spending cuts were much less effective in reducing the budget deficit, because these countries can not devalue the euro, is a fixed exchange rate, and cannot pursue a relaxation of monetary policy. As a result, spending cuts were less effective in reducing the deficit, but also caused other economic problems.

Other estimates of government spending cuts (Moşteanu, T., 2008, p.47):

It depends on the type of government expenditures that are intended to be cut off. If pension expenditure is reduced (eg increasing retirement age) then there may be a real increase in production capacity. If public sector investment is reduced, it will have a greater negative impact on aggregate demand and economic supply. Therefore, the temptation is for the government to reduce benefits and pensions, as this can reduce spending with a lower impact on economic growth - but it will be at the expense of increased inequality in society.

2. Increase in taxes

Higher taxes increase the revenue and help reduce the budget deficit. As with spending cuts, they could lead to lower spending and could lead to a decline in economic growth. Again, it depends on when taxes are raised. In a recession, tax increases could lead to a significant decrease in spending. During high growth, tax increases will not affect spending as much. It also depends on the type of tax to be increased.

3. Economic growth

One of the best ways to reduce the budget deficit as a percentage of GDP is to promote economic growth. If the economy grows, then the government will increase tax revenues without raising taxes. With economic growth, people pay more VAT, companies pay more corporation tax, and workers pay more income tax.

High economic growth is the least painful way to reduce the budget deficit, as there is no need to increase tax rates or reduce spending. However, many countries with a fiscal deficit crisis are often stuck in recession.

4. Rescue Plan

Under certain circumstances, countries may be eligible for rescue from an international organization such as the IMF. This means that they can benefit from temporary funds to finance a temporary lack of liquidity. The bailout can reassure investors and give the country more time to deal with the deficit. For example, in the 1970s, Britain sought rescue funds from the IMF. A rescue plan usually comes with strict guidelines on deficit reduction - this can be politically easier when imposed from outside. However, in the case of heavily indebted countries, a rescue plan may be insufficient to deal with the underlying indebtedness level. Also, the rescue conditions can be extremely controversial.

5. Default mode

Sometimes countries are at a stage where they cannot manage their budget deficit. It can be said that Greece is very close. The government has attempted cuts in spending and tax increases, but the budget deficit continues to be high. Also, fiscal consolidation has caused an economic depression.

5. Conclusions

Deduction played a crucial role at the end of the article, especially in order to formulate conclusions concerning the future evolution of the Romanian economy and the influence of budget deficit over the market, based on the previously built framework and on the former recorded experiences of other states.

The budget deficit is the result of diminishing public (Chirleşan, D., 2008, p.137) revenues and/ or increasing public spending. A reduction in public revenue may be caused by a decline in the market economy or even the inability of tax authorities to collect income from individuals and businesses.

As regards the Romanian economy, the major expenditure growth was highlighted.

Social assistance spending has recently accelerated as a social effect from the aging of the population.

As far as the implications for the labour market are concerned, a budget deficit causes a decline in government investment that affects employment and therefore involves higher government spending to support employment.

In Romania, in the context of the financial crisis, the number of unemployed has risen, with the post-crisis situation decreasing this number by predicting for the years 2019-2020 a continuation of the diminishing of this negative effect caused by the budget deficit and not only.

Methods of diminishing the budget deficit vary from tax to economic growth and loans. However, regardless of the method used, account must be taken of the context in which the economy is located so that the effects are the ones expected.

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