

# THE FUTURE OF EUROPE

Security and Economic Development

Bucharest

22-24 November 2007

Organized by:



**The Academy of Economic Studies**

**The Faculty of International Business and Economics**

**EURISC Foundation**

**Scientific Committee**

Prof. Mihai Korca Ph.D., Prof. Gabriela Drăgan Ph.D., Prof. Silviu Neguț Ph.D.,  
Prof. Dumitru Miron Ph.D., Prof. Ioan Popa Ph.D., Prof. Ovidiu Rujan Ph.D., Reader Valentin  
Cojanu Ph.D., Reader Mariana Nicolae Ph.D.

**Organizing Committee:**

Teaching Assistant Roxana Voicu Dorobanțu, Teaching Assistant Alina Chiciudean,  
Teaching Assistant Alina Drăghici, Teaching Assistant Dan Dumitrescu, Teaching Assistant  
Mihaela Cristina Drăgoi, Teaching Assistant Alina Popescu

*The Conference is organised under the auspices of the CEEX-III Project, Security Culture  
and Regional Cooperation in the Balkans (2006-2008)*

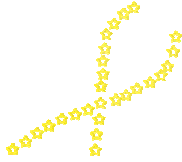
## **Argument**

Human rights, freedom and prosperity all play a salient role in defining the economic standing of societies in our days. A healthy economic development in terms of competitiveness, able to ensure an effective EU integration, assuming the exigencies of globalization, having normal access to resources and to international markets could be the very economic and sustainable basis not only for achieving the ideals of an unified, peaceful, and flourishing Europe, but also for increasing the capacity of European people to enrich and share their experience through international dialogue.

Developing initiatives in the field of economic competitive development and regional security matters seems to find an extremely favorable research and policy environment. The need for joint regional security studies and research in crisis management has become stringent considering the fact that the region of the South East Europe (SEE) has become the focus of the security efforts of the international community, as well as of varied regional programs.

Against these major foci of scientific interest, the Conference works were organized in the following topics of interest:

- European Development in Historical Perspective
- Security, Culture and Prosperity
- Conflicts in Europe: Origins, Resolution, Containment
- Resources, Growth, and International Cooperation



# AGENDA

**Thursday, 22 November 2007**

**17.00—18.00 — Registration** — Room 2013, Calea Dorobanților Building, ASE Bucharest

**18.00—18.30 — Plenary Session: Welcome Addresses** — Room 2013

**18.30—19.30 — Plenary Session: Keynote Speeches** — Room 2013

- The Lord Watson of Richmond, CBE
  - Member of the House of Lords Select Committee on the European Union
- Alain Servantie,
  - Advisor DG Enlargement, European Commission
- His Excellency, Lazăr Comănescu
  - Romanian Ambassador to the European Union
- Nicolae Idu, Ph.D.
  - General Director, European Institute of Romania, Romania

**20.30 — Reception**

— Casa Universitarilor Restaurant, Str. Dionisie Lupu, no.46, Bucharest

**Friday, 23 November 2007**

**09.00 — 11.00 — Conference Panels**

**11.00 — 11.30 — Coffee Break**, Room 1204, Mihai Eminescu Building, ASE Bucharest

**11.00 — 13.30 — Conference Panels**

**13.30 — 14.00 — Panel Conclusion**

**14.00 — 15.30 — Lunch**, Room 1204, Mihai Eminescu Building, ASE Bucharest

*During the Conference, a HELP DESK will be available in Room 1204, Mihai Eminescu Building, ASE Bucharest.*

## **CONFERENCE PANELS**

**Panel 1: Security, Culture and Prosperity**

Room 1012, Mihai Eminescu Building, ASE Bucharest

**Panel 2: Resources, Growth and International Cooperation—Section 1**

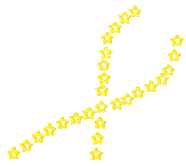
Room 1516, Mihai Eminescu Building, ASE Bucharest

**Panel 3: Conflicts in Europe: Origins, Resolution, Containment**

Room 1415 bis, Mihai Eminescu Building, ASE Bucharest

**Panel 4: Resources, Growth and International Cooperation—Section 2**

Room 1203, Mihai Eminescu Building, ASE Bucharest



## CONFERENCE PANELS

### Panel 1: Security, Culture and Prosperity

Moderator: Prof. univ. dr. Cristina Cristureanu, conf. univ. dr. Liliana Grigore

Room 1012

1. Laura Cismas, Alexandru Jivan, Claudia Cristescu, *West University Timișoara*  
**Remarks concerning Romania's Security and National Defence issue in the Globalization Framework**
2. Monica Parpalea, *Academy of Economic Studies, Bucharest*  
**"United in Diversity" – Quantification of Europe's Diversity and Ways to use it as a Growth Engine**
3. Dana Blideanu, Liliana Grigore, *Academy of Economic Studies, Bucharest*  
**Ways to intensifying the Romanian participation to the European Research Programs**
4. Bartosz Surawski, *Business and Administration School, Gdynia, Poland*  
**Knowledge-driven economy and knowledge workers: Polish experience in the integrating Europe.**
5. M. Kh. Tuseeva, P. B. Isahova, *University of International Business, Kazakhstan*  
**Social protection system of the population of Republic of Kazakhstan: Conditions and Prospects**
6. Alina Drăghici, *Academy of Economic Studies, Bucharest*  
**Economic Security in the Black Sea Region**
7. Ana Bobircă, Paul Miclăuș, Ștefan Ungureanu, *Academy of Economic Studies, Bucharest*  
**Energy Security: A Critical Issue in the European Energy Policy**
8. Cristiana Cristureanu, Ana Bobircă, *Academy of Economic Studies, Bucharest*  
**Airports driving economic and tourism development**
9. Cosmin Joldeș, *Academy of Economic Studies, Bucharest*  
**Romanian Pensions System Reform – Implementation of the II-nd Pillar**
10. Izabela Pruchnicka-Grabias, *Warsaw School of Economics, Poland*  
**Private Equity in Poland and other countries of Central and Eastern Europe – the Present State and Perspectives for the Future**
11. Mariana Nicolae, *Academy of Economic Studies, Bucharest*  
**Romanian higher education – a view from the inside**
12. Andrej Udovč, *University of Ljubljana, Slovenia*  
**Rural Space planning as a tool for natural resource management in Slovenia**



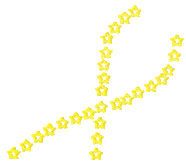
## CONFERENCE PANELS

### Panel 2: Resources, Growth and International Cooperation 1

Moderator : Prof. univ. dr. Rodica Zaharia, conf. univ. dr. Alexandra Horobeț

Room 1516

1. Marek Grzybowski, Ryszard Miler, Business and Administration School of Warsaw  
**MSA as the Aspect of European Maritime Security**
2. Livia Ilie, *University Lucian Blaga of Sibiu*, Alexandra Horobeț, *Academy of Economic Studies, Bucharest*  
**Challenges for the European Energy Market**
3. Delia Ionică, *Academy of Economic Studies, Bucharest*  
**The territorial dimension of the cohesion policy**
4. Andreea Gangone, *University Constantin Brâncoveanu of Pitești*  
**The social responsibility of the company – factor of supporting the European economic development**
5. Samazhan Umirzakov, *University of International Business, Kazakhstan*  
**Increase of national competitiveness on basis of innovation**
6. Gulnara Nurmukhanova, *University of International Business, Kazakhstan*  
**Foreign Experience of Competitiveness increase in the Economy Increase of Kazakhstan**
7. Camelia Oprean, Cristina Tănăsescu, *University Lucian Blaga of Sibiu*  
**The Convergence degree of innovation potential of Romanian Economy, by comparison with the Developed Economies of the EU Member States**
8. Ana Bal, *Academy of Economic Studies, Bucharest*  
**Determinants of Competitiveness in some EU Member Countries. Critical Aspects**
9. Alexandra Horobeț, *Academy of Economic Studies, Bucharest*, Livia Ilie, Lucian Belascu, *University Lucian Blaga of Sibiu*  
**Real exchange rates and competitiveness: a comparative analysis of CEE countries**
10. Florența Cîrceag, *University Constantin Brâncoveanu of Pitești*  
**The improvement of economic business management – competitiveness growth factor**
11. Radu Lupu, Dan Dumitrescu, *Academy of Economic Studies, Bucharest*  
**Distribution Event Studies on Eastern European Capital Market. Does Accession to EU influence the Event's Distribution for the new member states**
12. Rodica Milena Zaharia, Carmen Raluca Stoian, *Academy of Economic Studies, Bucharest*  
**Corporate social responsibility controversies**



## CONFERENCE PANELS

### Panel 3: Conflicts in Europe: Origins, Resolution, Containment

Moderator : Prof. univ. dr. Gabriela Prelipcean, asis. Univ. drd. Vlad Topan

Room 1415 bis

1. Gheorghe Săvoiu, Constantin Manea, Camelia Manea, *University Constantin Brâncoveanu of Pitești*

#### **The Romanian Rural Economy - a Resource of Growth and Regional Cooperation or a Source of Conflicts and Insecurity ?**

2. Sorina Aioanei, *Academy for Economic Studies in Bucharest*

#### **European Challenges for Islamic Banks**

3. Ramona Dumitriu, Răzvan Ștefănescu, *University "Dunarea de Jos" Galati*

#### **Decisions about the Future of the European Union: an Approach from a Romanian Perspective**

4. Emilia Iordache, Alina Vasilica Voiculeț, *"Constantin Brâncoveanu" University of Pitești, The Faculty of Management Marketing in Economic Affairs, Râmnicu Vâlcea*

#### **Customs Risk Management in the European Union**

5. Luiza Radu, Mădălina Istrate, *Ministry of Development, Public Works and Housing Territorial Networks - A Solution for Regional Problems?*

6. Florin Daniel Sălăjan, *Columbia University*

#### **The European Union in a Changing World: Globalizer or Globalized?**

7. Cristina Păsătoiu, *Faculty of Economy and Business Administration, Craiova*

#### **The role of the EU Common Agricultural Policy on the free trade agreement – the case of MERCOSUR**

8. Vlad Topan, *Academy of Economic Studies, Bucharest*

#### **The Origins of EU and the Flight from Liberalism**

9. Gabriela Prelipcean, Mircea Boscoianu, *University Ștefan cel Mare, Suceava*

#### **The Analysis of the Risk Management in case of Terrorism**

10. Valentin Cojanu, Alina Irina Popescu, *Academy of Economic Studies, Bucharest*

#### **Analysis of failed states: some problems of definition and measurement**

11. Ovidiu Horia Maican, *Academy of Economic Studies, Bucharest*

#### **The Future of European Constitution**

12. Jean Claude Berthelemy, Monica Beuran, Mathilde Maurel, *Centre d'Economie de la Sorbonne, France*

#### **Aid and Migration: Substitutes or Complements? Global Patterns and European Perspective**



CONFERENCE PANELS

Panel 4: Resources, Growth and International Cooperation 2

Moderator: Lect. univ. dr. Radu Musetescu, lect. univ. dr. Cristian Paun

Room 1203

1. Răzvan Buzatu, Expert of Parliament  
**The Beneficiaries of the "Reformed Treaty"**
2. Radu Mușetescu, Cristian Păun, *Academy of Economic Studies, Bucharest*  
**Oil, Security and Development: A Market-Based Approach**
3. Carmen Bălan, *Academy of Economic Studies, Bucharest*  
**The Alliances of European Retailers and Their Effects in the Field of Marketing and Supply Chain**
4. Cătălin Briceag, Phd. Candidate  
**Development Management for the companies that act in the Romanian Processing Industry**
5. Irina Eugenia Iamandi, Andreea Raluca Cărăgin, *Academy of Economic Studies, Bucharest*  
**The Role of National Organizations in Supporting Trade Missions Abroad. The Case of Romania**
6. Cristiana Tudor, *Academy of Economic Studies, Bucharest*  
**Profit Estimation on BSE: A Regression Model**
7. Gabriela Drăgan, Roxana Voicu-Dorobanțu, *Academy of Economic Studies, Bucharest*  
**EU-Russia relationship: Smooth as Oil? An analysis of the linkages between the European Union and Russia in the global oil market.**
8. Dan Anghel, *D.A. PRO Consulting*  
**Contribution to the creation of a target model for the privatisation process and for the implementation of a viable capital market in emerging economies**
9. Ana Maria Marinoiu, *Academy of Economic Studies, Bucharest*  
**The Romanian Contribution to the European Budget and the European Financial Allocation for 2007-2013**
10. Roxana Voicu-Dorobanțu, *Academy of Economic Studies, Bucharest*  
**The Paradigm and Paradox of Electronic Networks: profit facilitators, communication enhancers, isolators.**
11. Gheorghe Vlăsceanu, Liviu Bogdan Vlad, Alexandru Gavriș, *Academy of Economic Studies, Bucharest*  
**Energetic cooperation, the strength of economic development in the EU's countries**
12. Mihaela Cristina Drăgoi, *Academy of Economic Studies, Bucharest*  
**The socio-economic implications of the health care systems' reforms**
13. Silviu Neguț, Marius Cristian Neacșu, Viorel Mionel, *Academy of Economic Studies, Bucharest*  
**The European Union 's dependency on Russian energy**

*International Conference on*  
**“The Future of Europe”**  
**Security and Economic Development**

*Bucharest, 22-24 Nov.2007*

Contribution by  
Ambassador **Lazăr Comănescu**  
Permanent Representative of  
Romania to the European Union

**THE SECURITY – DEVELOPMENT RELATIONSHIP  
AND THE REFORM TREATY**

**1. The relation between security and economic development**

If my memory helps me well, which I hope is still the case; I remember that when delivering a speech 8 years ago when I was Ambassador to NATO, I referred to an author who was of the opinion that “it has long been a staple in international relations that economics and security conflict with each other”<sup>1</sup>. That is fully satisfying security necessarily means sacrificing at least some aspects of the economy or vice-versa.

I disagreed and continue to disagree with that author. I said at that moment that more and more security and stability – political and social alike – are multidimensional concepts with economics being in both cases one of the most important dimensions<sup>2</sup>. Developments since then confirmed that I was right. What I would like to stress, is that security and (economic) development go hand in hand, in a mutually dependant relationship.

Indeed, the economic, technological and political developments and transformations in the past few decades call for a much broader definition of security than the conventional one. It became absolutely clear that when speaking about security, while the military dimension is still there, nobody can deny dimensions such as the economic, social, or environmental ones, to mention but a few.

Take the EU’s case: military aggression by a Member State against another Member State is now highly improbable, or better said, unthinkable. Instead, Europe faces new threats which are more diverse, less visible, less predictable but which, if not dealt with appropriately, may have deep (negative) consequences. I think, *inter alia* about terrorism, proliferation of WMD, illegal migration, organized crime, energy security, or climate change.

---

1 Richard H.Schultz Jr, Roy Gordon, George Quester, Security studies for the 21<sup>st</sup> century, Brassey’s, Washington, London, 1997

2 NATO Colloquium: “Economic Developments and Reform in Cooperation Partner countries: The link between economics, security and stability” Brussels, 7-5 Nov. 1999



At the global level, the concept of 'human security' has been developed to encompass not just the achievement of minimal levels of material needs, but also the absence of severe threats to them be they of economic or political nature. I have in mind job security, income security, health security, environmental security, security from crime. In other words, human security in its broadest sense embraces far more than the absence of violent conflict. It also encompasses human rights, good governance, access to education and health care, and ensuring that each individual has opportunities and choices to fulfil his or her own potential. Freedom from want, freedom from fear and the freedom of the future generations to inherit a healthy natural environment – these are the interrelated building blocks of human and, therefore, national and international security

As globalization gradually takes hold of more and more areas of everyday life, security in the wider sense, is becoming an increasingly indivisible commodity. Conflicts in Africa can lead to a surge in migratory pressures on Europe, failed states can act as breeding ground for international terrorism, or a virus epidemic in Asia can have immediate effects at the opposite side of the globe.

Military force alone is no longer capable of preserving a state's capacity to protect its own values and way of life. **Tackling the root causes of conflict, in an anticipatory manner, is the most effective and cost-efficient way of ensuring security**, no matter how relative its definition might be.

Hence, a better understanding of the undisputed linkages between security and economic development has become urgent in a world where terrorism, weak state capacity, public health crises, and economic or financial crises can cross borders with ease.

Several connections between individual security and the level of development are now widely accepted. Human security forms an important part of people's wellbeing and is therefore an objective of development; lack of human security has adverse consequences on economic growth and poverty and thereby on development. Finally lack of development, or imbalanced development that involves sharp horizontal inequalities, is an important cause of conflict.

## **2. EU - internal / external security**

The European project, as such, is an example of the benefits of security, looked at in the wider sense, for development and growth. It is also a successful example of the benefits of appropriate policies of economic development for a climate of ever increasing security. The creation of the European Coal and Steel community and, afterwards, of the European Economic Community had as primary goals reducing insecurity and building trust between the participating members, in the aftermath of the Second World War. Sharing a common market, designing common policies, abiding by the same rules and developing financial solidarity have all contributed to a climate of political solidarity conducive to the stability and prosperity enjoyed today by the 27 EU member states.

The evolution of the EU candidates from Central and Eastern Europe, in the period from the moment of their application for EU membership, is clear evidence of the benefits for economic development brought about by a more secure and predictable environment. The high growth rates registered, closely linked to the degree of attractiveness for foreign direct investments, can be attributed, to a significant extent, to the opportunities and benefits generated by the prospects of EU membership. Though in a different way, NATO accession had similar effects. It boosted investor confidence and the business environment.

Besides the rules of the internal market, oriented towards economic efficiency through undistorted competition, EU's success is also due, to a large extent, to its unique approach, combining the unification of the continent with cultural and ethnic diversity. The prospects and requirements for EU membership have, in the '90s, defused potential conflict situations of ethnic nature. The attractiveness and transformative capacity of the EU is still relied upon as part of the solution to the existing trouble spots in the Balkans.

The EU model of openness, tolerance and diversity, operating within clear values and principles, is ever more relevant, as ethnicity or religion are, or are perceived to be, at the forefront of many of today's conflicts.

The EU has traditionally been at the forefront of **environment** protection policies, on the international scene (promoter of Kyoto, etc) as well as within the EU. At present, the growing concerns about the long term effects of climate change are determining environmental issues to gradually shift, from a values driven policy, to a security driven one. Given its economic weight and influence, the EU has a vital interest in playing a leading role in the struggle to strike a sustainable balance between economic growth in the developing, as well as the developed world, and long term environment concerns.

Turning to the external dimension, and looking at what the EU can and must do to increase security in the world, as the only way to ensure its own security, one cannot help noticing that the notion of security is a very relative and subjective concept. Obviously, the security needs perceived by an EU citizen are quite different from those of, for example, a Darfur refugee.

Intra-state wars or conflicts are the main sources of instability in the developing world and the main economic causes identified are group motivation associated with group inequalities, private motivation and incentives (individual gains from a situation of conflict), and a failure of the social contract, stemming from economic failure and poor government.

The 2003 European Security Strategy<sup>3</sup>, as well as the 2005 European Consensus on Development<sup>4</sup> acknowledge that **there cannot be sustainable development without peace and security**, and that **without economic development and poverty eradication there will be no sustainable peace**. At EU level, there is growing awareness of the fact that the inter-linkage between security, (economic)

---

3 A secure Europe in a better world: European Security Strategy, European Council, December 2003

4 "The European consensus", OJC 46/01 of 24.02.2006

development and human rights should increasingly shape the political vision of the EU.

The EU, as an important global actor, can avail itself of a wide array of instruments to promote long-term development and poverty eradication, to prevent and manage violent conflicts and to build peace in developing countries.

EU's global position in what concerns **trade and development assistance means it is uniquely placed for a forefront role in the economic development-security relationship**. EU trade policy aims to contribute to a more equitable integration of developing countries into the international trading system through coherent action on three levels: the **multilateral** (which remains the key area of EU trade policy), the **bilateral** and through **autonomous measures**<sup>5</sup>. As the world's largest provider of development assistance<sup>6</sup> and at the same time the world's largest trade entity (the EU can rely on important leverages to back up a political stance on the world scene.

**Increasing coherence** between these various instruments at the EU's disposal in the area of **security and development**, both at a **policy and an operational level**, is at the forefront of the EU's preoccupations<sup>7</sup>.

As a step in this process the Council has identified pragmatic guidelines for increased coherence in some of the areas spanning the security-development nexus: strategic planning, Security Sector Reform, partnerships with regional and sub regional organisations, and humanitarian assistance and security.

Since the adoption of the European Security Strategy in 2003, the Union has equipped itself with an operational crisis management capability and has conducted no less than 15 civilian and military operations on 3 continents. The EU has also developed a number of instruments in the second and third pillars, such as police and judicial cooperation, sanctions, fight against terrorism, non-proliferation of WMD and of small and light weapons (SALW).

The entry into force of the Reform Treaty will have a number of implications in what concerns the EU's external action in general and the security and development dimensions in particular.

### **3. The Reform Treaty/The Lisbon Treaty (RT)**

Reaching agreement on the RT<sup>8</sup> represented a significant step forward for the Union's capacity to concentrate on its internal and external priorities. This crucial issue having been set aside in a satisfactory manner, energies can now be dedicated

---

5 for more on EU trade policy see "EU and global trade", [www.europa.eu](http://www.europa.eu)

6 nearly 12 bill. euro committed in aid for developing countries in 2006, representing about 10% of the European Community's budget (source: Annual report 2007 on the European Community's development policy and the implementation of external assistance in 2006 – European Commission)

7 see, for example, the Commission's communication "Europe in the world – some practical proposals for greater coherence, effectiveness and visibility" COM(2006)278 final

8 The text of the Reform Treaty can be found in doc. CIG 1/1/07 rev1, <http://consilium.europa.eu/uedocs/cmsUpload/cg00001re01en.pdf>

to making the best of the existing instruments, as well as prepare for the new framework (the RT), in order to adapt and better tackle the current challenges.

One should not, however, overestimate the effects of the entry into force (hopefully by the beginning of 2009) of the RT. I would see the new treaty, as others have put it, rather as the “hardware” for the EU’s future evolution. The “software” has still to be written, and it is dependant on the common political will to implement and build upon the foundations and opportunities presented by the new treaty.

The RT will offer new possibilities and will act as a catalyst for action, but it will certainly not lead to automatic results. The desire to take advantage of the new tools on offer and the conviction that they serve the common interest will be essential.

What will the new Treaty bring in terms of security and development, the subject of our debate?

### **Internal**

On the EU internal side, the new treaty will introduce a series of innovations in the direction of increasing security and solidarity among the member states.

One of them is the **solidarity clause** in case of terrorist attacks or natural or man made disasters<sup>9</sup>. Thus, the Union shall mobilise all the instruments at its disposal, including military resources made available by the member states to: prevent terrorist threats in the Member States, protect democratic institutions and the civilian population or assist a Member State in case of a natural or man-made disaster.

Although it is unconceivable that, in case of need, solidarity and mutual assistance would not be available under the current arrangements also, the introduction of the respective provisions in the new treaty generates a higher degree of certainty and a more secure environment.

The mutual **assistance clause in case of armed aggression** also represents a significant step towards the Union as a political entity concerned with the security of its members. According to the new provisions, if a member state is the victim of armed aggression on its territory, the other member states shall have towards it an obligation of aid and assistance by all means in their power.

A new legal base regarding **civil protection**<sup>10</sup> is meant to improve the effectiveness of systems for preventing and protecting against natural or man-made disasters. Thus, Union action shall aim to support and complement Member States' action at national, regional and local level in risk prevention, in preparing their civil-protection personnel and in responding to natural or man-made disasters within the Union. It shall also promote swift, effective operational cooperation within the Union between national civil-protection services and promote consistency in international civil-protection work.

---

9 Art.2, par.176, pg 110 of CIG 1/1/07 Rev1

10 Art.2, par 149, pg. 98 of CIG 1/1/07 Rev1

The Reform treaty will also introduce a new legal base for joint action on **energy**<sup>11</sup>, topic at the forefront of international high politics today and an increasingly relevant component of national security. The Union's policy on energy shall aim to ensure the functioning of the energy market, ensure the security of supply and promote energy efficiency and energy saving and the developing of new and renewable forms of energy. The concept of **solidarity** between Member States in situations of difficulty of supply of certain products, **notably energy**, is also being introduced as a way of increasing the Union's capacity to act in unity when deciding on aspects affecting the security of its citizens.

The amendments introduced by the RT in the area of **justice and home affairs**<sup>12</sup> (ex. extending decisions by QMV, the possibility to establish the European public prosecutor's office, measures to promote and support member states action in crime prevention) are targeting the current challenges in ensuring **a secure common area of freedom and justice**, challenges which are due to the elimination of the internal borders, as well as to the external pressures.

## **External**

On the external front, EU's interests, including its security objectives, are pursued by, on one hand, the consolidation of existing instruments and, at the same time, by ensuring greater coherence and synergy between them. The large spectrum of means for external action at the disposal of the EU include commercial policy, development cooperation, economic, financial and technical cooperation, humanitarian aid, restrictive measures, as well as instruments in the CFSP field, such as the civilian and military crisis management operations or non-proliferation assistance.

The main innovation introduced by the RT is the position of **High Representative for foreign affairs and security policy**<sup>13</sup> (who will, at the same time, be vice-president of the Commission), which will bring together, under the same hat, the coordination of all EU's external action instruments, irrespective of the different pillars they belong to. By building a formal bridge between the areas of external action primarily under the responsibility of the Commission and those of the Council (CFSP area), the new arrangement is meant to ensure the conditions for improving coherence, efficiency and effectiveness of all EU's external initiatives.

Other elements of progress brought about by the RT in terms of strengthening the EU's ability to project stability refer to the possibility of **structured cooperation in defence matters**<sup>14</sup>, aimed at building up EU's capabilities in the field, in line with the present day needs and requirements. Also on the defence capabilities side, a Treaty basis for the European Defence Agency (established since 2005) will confer to it more weight and visibility and, hopefully, more resources.

Rapid reaction is becoming more and more crucial for preventing or containing conflict situations. The objective of improving EU capacity to react and make a useful

---

11 Art.2, par 147, pg. 96 of CIG 1/1/07 Rev1

12 Art.2, par. 63-68, CIG 1/1/07 Rev1

13 Art.1, par. 30.1, pg.22, CIG 1/1/07 Rev1

14 Art.1, par. 47(c)6, pg.31, CIG 1/1/07 Rev1

contribution to solving crisis situations around the world is addressed in the provisions of the new Treaty referring to the establishment of specific procedures guaranteeing rapid access to financing of initiatives in the CFSP field, in particular preparatory activities.

The new provisions on climate change<sup>15</sup> will strengthen the Union's capacity to act in unity and coherence and thus consolidate its ability to influence events at global level.

**A single international legal personality for the EU<sup>16</sup>** will strengthen its capacity to act as a global actor, including within the relevant international organizations. It should also contribute to a more unitary EU voice in the international fora, a prerequisite for taking full advantage of the EU's influence potential.

#### **4. Some conclusions**

It is an uncontested assumption that in developing countries, as well as in the world as a whole, there are strong connections between security and (economic) development. In all cases, societal progress requires reduced insecurity.

The European Union is uniquely placed to play a role in enhancing world-wide security through the varied instruments and the resources it has at its disposal, as well as through the power of its own example. The current challenges to security and development require the kind of **“soft power” and propensity towards multilateralism that are the “trademarks” of the Union.**

The new institutional and policy framework of the Union after the entry into force of the RT represents a step forward for consolidating the basis for action within the virtuous circle of more inclusive development, better security and more development.

The main challenge will remain the mobilisation of a joint political will and common vision of the Union's interests in relation to the outside world. The strengthening of CFSP, including its sub-component ESDP, will have to be accompanied by the acceptance that it represents only one of the dimensions of the wider external action of the Union, with which it has to be fully articulated.

There are reasons for optimism: the present general atmosphere within the Union is positive after the agreement concluded on the RT, while the ever increasing external challenges, multiplication of trouble spots and the high expectations of the affected parties act as catalysts towards an even more prominent role of the EU in the security-development equation.

---

15 Art.2, par.143(a), pg. 95, CIG 1/1/07 Rev1

16 Art.1, par. 54, pg.35, CIG 1/1/07 Rev1

Bucharest 22 November 2007

## "Ending age-old conflicts in Europe: History, Culture and Actors"

Alain Servantie, Advisor DG Enlargement, European Commission<sup>1</sup>

### 1. Introduction: Ending age old conflicts

Right after the disaster of the Second World War, on 19<sup>th</sup> September 1946, in Zurich, the former British Prime Minister, Winston Churchill, delivered a speech to the academic Youth calling for reconciliation, end of conflicts and unification of Europe “*And why should there not be a European group which could give a sense of enlarged patriotism and common citizenship to the distracted peoples of this turbulent and mighty continent? And why should it not take its rightful place with other great groupings and help to shape the onward destinies of men? In order that this should be accomplished there must be an act of faith in which millions of families speaking many languages must consciously take part... If Europe is to be saved from infinite misery, and indeed from final doom, there must be this act of faith in the European Family and this act of oblivion against all the crimes and follies of the past.... The first step in the re-creation of the European Family must be a partnership between France and Germany. In this way only can France recover the moral and cultural leadership of Europe. There can be no revival of Europe without a spiritually great France and a spiritually great Germany. The structure of the United States of Europe, if well and truly built, will be such as to make the material strength of a single state less important. Small nations will count as much as large ones and gain their honour by their contribution to the common cause. The ancient states and principalities of Germany, freely joined together for mutual convenience in a federal system, might take their individual places among the United States of Europe....*”

The second important statement was made by the French Minister Robert Schumann, on 9<sup>th</sup> May 1950: “*L’Europe ne se fera pas d’un coup, ni dans une construction d’ensemble: elle se fera par des réalisations concrètes créant d’abord une solidarité de fait. Le rassemblement des nations européennes exige que l’opposition séculaire de la France et de l’Allemagne soit éliminée : l’action entreprise doit toucher au premier chef la France et l’Allemagne. Dans ce but, le gouvernement français propose de porter immédiatement l’action sur un point limité mais décisif : Le gouvernement français propose de placer l’ensemble de la production franco-allemande de*

---

<sup>1</sup> The views expressed by the author do not necessarily represent the views of the institution he belongs to.

*charbon et d'acier sous une Haute Autorité commune, dans une organisation ouverte à la participation des autres pays d'Europe. »*

Both speeches led to the most important initiatives of an institutional nature, which aimed to the prevention of further conflicts. However, if the unification process in Western Europe indeed gave the continent its longest peace period in history, South-Eastern Europe suffered still conflicts, in the ex-Yugoslavia, in Cyprus, which deserve a special treatment to heal wounds.

## **2. Culture and rule of law: institutional actors in conflict prevention**

The first important text was the Brussels Treaty signed on 17 March 1948 creating the **Western European Union**. Its article X provides that "to settle disputes only by peaceful means", the High Contracting Parties will [...] refer them to the International Court of Justice or to conciliation".

The **Council of Europe**, created in 1949 under the inspiration of Churchill's speech, adopted in 1957 a **Convention for the Peaceful Settlement of Disputes** which provides that the parties "*shall submit to the judgment of the International Court of Justice all international legal disputes which may arise between them*" (article 1), and to conciliation or arbitration all other disputes which may arise (articles 4 and 19). However, so far only 14 countries have ratified it, among them 8 excluding arbitration (among them France, Italy, Netherlands, UK), 5 signed but did not ratify (among them Greece, Turkey and Ireland).

The **EU Treaty** (today Article 292) provides that "*Member States undertake not to submit a dispute concerning the interpretation or application of this Treaty to any method of settlement other than those provided for therein.*" Furthermore, the Copenhagen criteria (1993), drafted to precise conditions for future memberships imply good neighbourly relations for candidate countries.

The **Final Act adopted at the CSCE Conference in Helsinki** on 1<sup>st</sup> August 1975<sup>2</sup> includes a section on *Peaceful settlement of disputes*: "*The participating States will settle disputes among them by peaceful means in such a manner as not to endanger international peace and security, and justice. ... For this purpose they will use such means as negotiation, enquiry, mediation, conciliation, arbitration, judicial settlement or other peaceful means of their own choice including any settlement procedure agreed to in advance of disputes to which they are parties....*" The present OSCE, which stemmed from CSCE, includes a Conflict Prevention Centre (CPC) supports the Chairman-

---

<sup>2</sup> [http://www.osce.org/documents/mcs/1975/08/4044\\_en.pdf](http://www.osce.org/documents/mcs/1975/08/4044_en.pdf)



in-Office and other OSCE bodies in the fields of early warning, conflict prevention, crisis management and post-conflict rehabilitation.

Furthermore, the **Charter on Good Neighbourly Relations, Stability, Security and Cooperation in Southeastern Europe** signed at Bucharest on 12<sup>th</sup> February 2000, at the end of the Kosovo crisis, includes a reference to OSCE provisions on conflict settlement.

It appears indeed that these legal commitments helped to settle disputes between European countries since 1945 (with the exception so far of the Cyprus issue, and the disputes arising from Yugoslavia implosion, more similar to civil war than to international conflict).

The experience gained from the preparation of the last two enlargements of the EU show that a culture of the rule of law is necessary if one wants to favour peaceful settlement of conflicts. This means that training of lawyers and police officers is necessary and should be continuously anchored through the involvement of the executive power and the judicial sector in long term strategy<sup>3</sup>. Respect of the rule of law has implied cooperation between Croatia, Bosnia-Herzegovina, Serbia and ICTY to punish those involved in war crimes. Hence cultural actions are necessary to ensure that the notion of rule of law is clearly understood<sup>4</sup>.

### 3. Intercultural dialogue and conflict prevention

Conflicts in South Eastern Europe, like the Cyprus conflict (1963-1974) and the Yugoslav wars, which look like disputes between nations result from old internal rivalries between religious communities, turned through the ages into ethnic rivalries. The Ottoman Empire, a multi-cultural and multi-religious empire, had ensured for nearly 4 centuries what was called a *pax ottomanica*<sup>5</sup> in South Eastern

---

3 See recommendations of the seminar on lessons learned of the fifth enlargement in the field of justice and home affairs held on 23 May 2007, [http://ec.europa.eu/enlargement/5th\\_enlargement/key\\_recommendations\\_en.htm](http://ec.europa.eu/enlargement/5th_enlargement/key_recommendations_en.htm).

4 **The Communication from the Commission on Conflict Prevention** (COM(2001) 211 final, 11.04.2001) includes a section on the support to rule of law outside of Europe.

5 In 1545, the French traveler Belon is amazed by the *pax ottomanica*: "In all the islands of Greece, in the Mediterranean Sea, where Greek is spoken, the inhabitants acknowledge they are in safety under the Turkish power. They don't intend to live otherwise, and don't care keeping fortresses, because the Turks get rid them of this sorrow. Hence they prefer remaining in the fields than in the cities.... They did not change their language or religion

Europe; it imploded with the rise of nationalities, in the 19<sup>th</sup> century, as religious communities were confused with nations; exchange of populations to an extent unknown in Europe, massacres, disappearances and displacements are often still very present in memories, embellished by official history text books. Thus, roots of those conflicts are more deeply rooted in the subconscious prejudices of people of the area and the need was felt to go deeper into cultural actions to prevent further spreading of the conflicts and lead to reconciliation<sup>6</sup>.

The Stability Pact for South Eastern Europe, signed in 2000, examined a whole range of projects, a great number of them of a cultural nature aimed at promoting reconciliation and preventing ethnic conflicts<sup>7</sup>. They deal with Human Rights and National Minorities, governance in multiethnic communities (Awareness-Raising Campaign, International Center for Preventive Activities and Conflict Resolution in FYROM, civil society dialogue, exchange of youth and students; Promoting partnerships between towns and regions, including through transfrontier Cooperation; joint training of Media and Public Administration; Democratic Control of Armed Forces, etc). Some of these projects have been implemented by European organizations like OSCE, Council of Europe, EU; some through NGOs; we will survey some of the most significant projects below.

In the context of the Council of Europe, the Declaration on Intercultural Dialogue and Conflict Prevention, adopted by the European Ministers responsible for Cultural Affairs in Opatija (Croatia) on 22<sup>nd</sup> October 2003, defined the concept for a policy on intercultural dialogue with due regard for cultural diversity, affirming the safeguarding and protection of both tangible and intangible heritage in a spirit of cultural democracy<sup>8</sup>.

---

because the Turks came. A native old man of the island said that never the country had never been so well cultivated, and so rich, and that there had never been so many people living. And this should be attributed to the long-term peace they have had without being harassed. Pierre Belon, *Les observations sur plusieurs singularitez et choses memorables trouvées en Grèce, Asie, Judée, Egypte, Arabie et autres pays estranges*, Paris, 1553, chp. I, 23. See also Imperial Legacy. The Ottoman Imprint on the Balkans and the Middle East, Carl Brown ed., New York: Columbia University Press, 1996.

<sup>6</sup> See. Georges Corm, *Orient-Occident. La fracture imaginaire*, La Découverte, Paris, 2005 ; Georges Corm, *L'Europe et l'Orient, de la balkanisation à la libanisation, histoire d'une modernité inaccomplie* » ; Eric Hosbawm, *Nations and Nationalisms since 1780. Programme, Myth, Reality*, Cambridge University Press, Cambridge, 1990 shows that national ideas and feelings are a cultural and political production of Europe which emerged relatively late, around the French Revolution.

<sup>7</sup> See a list of all projects tabled on SEE: <http://www.stabilitypact.org/req-conf/000329-annex1.doc>.

<sup>8</sup> [www.coe.int/t/c/cultural\\_co-operation/culture/action/dialogue/pub\\_DGIV\\_CULT\\_PREV\(2004\)1](http://www.coe.int/t/c/cultural_co-operation/culture/action/dialogue/pub_DGIV_CULT_PREV(2004)1).

Main sources of financing have been the CARDS programme of the European Union, partly managed by the European Agency for Reconstruction based in Salonica, replaced since 2007 by the Instrument for Pre-Accession Assistance (IPA), managed by the European Commission.

**Funds managed by the EAR on Civil society & media**

<i>C million</i>	1998	1999	2000	2001	2002	2003	2004	2005	Total
Serbia	5.0	3.0	1.0	2.0	3.0	7.0	7.2	4.5	32.7
Kosovo		1.0		4.0	3.0	1.0	1.0	1.0	11.0
Montenegro		1.0				1.0			2.0
former Yugoslav Republic of Macedonia					5.5	3.0	5.2	2.0	15.7
<b>Total</b>	<b>5.0</b>	<b>5.0</b>	<b>1.0</b>	<b>6.0</b>	<b>11.5</b>	<b>12.0</b>	<b>13.4</b>	<b>7.5</b>	<b>61.4</b>

**IPA – instrument for pre-accession assistance<sup>9</sup>**

Resources will be given to allow regional programmes in education and research and regional projects in favour of civil society dialogue for about 40 millions € for years 2007-2009. By having a regional strategy with common benchmarks, results of national government progress can be shared and allow political dialogue on the issue in the region.

The overall objective of this area of intervention is to assist the Civil Society Organisations of the Beneficiaries (in areas such as minority rights, women's rights, environmental protection, etc) to develop a pluralistic democracy, respecting the human and social values of the EU, actions to guarantee a supportive legal environment for civil society activities, to strengthen administrative capacity and also to facilitate networking and partnership building.

Proposed Activities:

- i. Promote regional cooperation projects involving civil society organisations from both the beneficiaries as well as the EU Member States;
- ii. Provide technical assistance projects to assist Civil Society Organisations in delivering improved services, support and communications;

<sup>9</sup> [http://ec.europa.eu/enlargement/pdf/mipd\\_multibeneficiary\\_2007\\_2009\\_en.pdf](http://ec.europa.eu/enlargement/pdf/mipd_multibeneficiary_2007_2009_en.pdf). CARDS: "Regional cooperation in the Western Balkans: A policy priority for the European Union", Luxembourg: Office for Official Publications of the European Communities, published in December 2005. (PH:2006/2112)

iii. Promote European media content and local productions; public service broadcasting and professionalism in the media

iv. Facilitate the return of refugees and internally displaced persons, and (re)integration of those who wish to remain in their hosting country.

The final beneficiaries of assistance in this area of intervention will be non-profit organisations, in particular non-governmental organisations, foundations and charities, as well as local or regional authorities, inter-governmental organisations, education and research institutes, think-tanks and other non-profit institutions or associations of a social, economic or cultural character in the EU-27 and beneficiary countries. A limited number of profit-making organisations (notably those in the Media) and public media operators may also benefit from support.

In the field of Education, support is given to the participation of the Western Balkan countries in the Erasmus Mundus and Youth Programmes. The Youth Programme - established in 2000 – supports projects leading to an enhanced intercultural dialogue and tolerance among young people, social inclusion of disadvantaged youngsters, as well as the strengthening of youth NGOs and the development of civil society.

#### **4. Major Projects of Cultural Interest**

##### **Refugee return**

One of the main policy frameworks identified to address the issue of refugee return is the Sarajevo Declaration (or "3x4 Initiative") signed in January 2005 in which the governments of Bosnia and Herzegovina, Croatia and Serbia Montenegro agreed to bring a genuine and successful close to the refugee chapter in South-Eastern Europe by the end of 2006. The European Union has financed the 3x4 Initiative components i.e. refugee return and local integration. National Programmes relating to refugees and internally displaced persons in Bosnia and Herzegovina, Croatia, Montenegro and Serbia aim at assisting municipalities, facilitating capacity building of local civil society organisations, as well as returns and repatriation. Since the Sarajevo Declaration, certain progress has been made, but the international community has expressed its concern that the process is far behind schedule and that greater cooperation between the governments of the region is still necessary.

##### **Cultural Heritage**

**The Regional Programme for Cultural and Natural Heritage in South East Europe 2003-2007**, launched by the Council of Europe in cooperation with the

European Commission, shows a trans-national purpose paying special attention to issues connected to multiple cultures and religions throughout the area. The challenge is the long-term reconciliation between individuals and communities necessary to ensure that conditions are created whereby potential conflicts can be managed and resolved through non-violent means. It offers a global exchange of expertise and experiences between neighbouring countries facing similar situations in the fields of protection, conservation, rehabilitation and enhancement of cultural and natural heritage, as a means of building a local identity also favours the construction of a European identity achieved by piecing together a European heritage through which a number of values can be shared. The Regional Programme includes three main complementary components:

Component A: Institutional Capacity Building Plan (ICBP)

Component B: Integrated Rehabilitation Project Plan/Survey on the Architectural and Archaeological Heritage (IRPP/SAAH)

Component C: Local Development Pilot Project (LDPP)

Particular attention has been paid in the first instance to rehabilitating the architectural heritage (particularly orthodox churches) in Kosovo.

### **Education**

Between 1993 and 2000, the Western Balkan countries were included in the Tempus Programme<sup>10</sup>. Over the period 2001-2006, the European Community has allocated over €101m to the Tempus Programme for the Western Balkan countries; this will continue with the inclusion of the WB countries in the Erasmus Mundus programme. Turkey is already participating fully in the Socrates programme, and will participate in the Lifelong Learning programme as from 2007. IPA regional programme in the field of Youth and Education aims at supporting projects *inter alia*:

- Contributing to strengthening democracy and civil society by facilitating the integration and active participation of young people, and by developing youth structures and the voluntary sector.
- Enhancing intercultural understanding.

---

<sup>10</sup> Exchange of youth as a means to overcome misunderstandings were at the basis of the decision taken by President de Gaulle and German Chancellor Adenauer, when they created the Office Franco-Allemand de la Jeunesse in 1963; "L'Office a pour objet de resserrer les liens qui unissent les jeunes des deux pays, de renforcer leur compréhension mutuelle et, à cet effet, de provoquer, d'encourager et, le cas échéant, de réaliser des rencontres et des échanges de jeunes » (<http://www.ofaj.org/>). In 40 years, 233.516 programmes were financed, with 6.177.000 participants (5% of the population of both countries).

- Increasing the number of intercultural exchanges, cooperation and solidarity activities among youth of the Western Balkans region.
- Encouraging youth to take part individually or in groups in non-profit, voluntary activities abroad including, helping in local projects in a wide range of fields: social, ecological and environmental, arts and culture, new technologies, leisure and sports;

The Task Force Education and Youth is a network of regional and international key actors in the field of education and youth. Within the Education Reform Initiative of South Eastern Europe (ERI SEE) its partners are international institutions, donors and the Ministries of Education of the South Eastern European countries represented by a network of Senior Officials. In its work the Task Force Education and Youth strongly builds on existing institutional frameworks and expertise, as well as on regional ownership. Through an inclusive approach it supports the inclusion of the countries of South Eastern Europe into a wider European Area of Education.

In the former Yugoslav Republic of Macedonia, the 'Triangle' project, so-called because it is based on a partnership between three universities, two from the former Yugoslav Republic of Macedonia and one from the Netherlands, managed by the EAR, involves 30 young people from diverse ethnic in a concerted effort to improve inter-ethnic relations, to understand and establish democratic stability in the country, and to initiate co-operation and respect among the students. This will be done by carrying out research into the existing judicial system and into ethnic relations, according to the European Convention for the Protection of Human Rights and the European Framework Convention on the Protection of National Minorities. (200.000 €)

### **History Teaching**

The critical role played by history text books in shaping prejudices vis-à-vis neighbouring countries and minorities, and inflating nationalistic feelings has been addressed in several projects<sup>11</sup>. The Turkish History Foundation, in 2002,

---

<sup>11</sup> On Turkey see Türker Alkan, *Political integration of Europe, Content analysis of the Turkish, French, German and Italian History Textbooks*, roneo, 1980: Turkish History textbooks mainly present neighbouring countries as enemies- Greece is negatively dealt in 98 % of cases. On Greece, see (AFP ATHENS, Aug 2, 2007) - A new Greek history schoolbook attacked by the Orthodox Church and nationalists for allegedly obscuring Turkish atrocities has been revised... a petition accused the authors of "embellishing" the Ottoman Empire and obscuring centuries of "rape, genocidal slaughter, impalings, pillage and Islamisation." The head of the Orthodox Church of Greece, Archbishop Christodoulos, also blasted the book for teaching children "adulterated history" and accused the authors of "sacrificing truth" for the benefit of Greek-Turkish relations. [...] Contrary to past editions, the book did not qualify the Ottoman Empire's four-century rule of Greece as "slavery" and did not

with the support of UNESCO, the Heinrich Böll Foundation and the Consulate General of the Netherlands in Turkey, with the participation of teams from Bulgaria, Croatia, Greece, Romania and Turkey. The project aimed to bring together academics and history teachers from the Balkan countries; to review primary and -particularly- secondary level history textbooks currently in use; and to propose alternative ways of reflecting the political, social and cultural history of these countries. The main objective of the project was to prepare a final report on the history textbooks and the teaching of history in the five Balkan countries<sup>12</sup>.

The Joint Historic Project, launched by the Center for Democracy and Reconciliation in Southeast Europe (CRDSEE), with the support of USAID and the German Foreign Ministry, brings together historians, teachers, pedagogues, CSOs and students to work together towards the emergence of democratic and peaceful societies in the region, through multi-perspective history education. The aim is to revise ethnocentric school history teaching by avoiding the production of stereotypes, by identifying attitudes that encourage conflict, by suggesting alternative teaching methods, and by promoting the idea of multiple interpretations of one event. History that instils values of academic rigor and critical analysis would serve as a solid basis for democracy, reconciliation and tolerance in Southeast Europe<sup>13</sup>.

#### **Media<sup>14</sup>**

The development of free, independent and professional media is a key element to sustaining stable and functioning democracies in the Western Balkans. Increasing awareness of European media standards in the region and accelerating necessary reforms in the media sector are important priorities." The Commission which, in cooperation with the Council of Europe, launched a regional initiative on media reform in 2004, bringing together representatives of governments, broadcasting regulatory authorities, public broadcasters and other

---

claim that the Greeks "suffered much hardship" under the Turks, one of its authors told AFP. It also broke with the "national myth" that Greek Orthodox Church leaders made a substantial contribution to the Greek Revolution of 1821-29, historian Maria Repoussi said."

<sup>12</sup> ***IMPROVEMENT OF BALKAN HISTORY TEXTBOOKS PROJECT REPORTS*, Turkish History Foundation, Istanbul, 2001**

<sup>13</sup> <http://www.cdsee.org/jhp/index.html>

<sup>14</sup> <http://www.stabilitypact.org/media/overview%20MTF%20projects2004-2.pdf>

stakeholders. , these projects have facilitated the networking of media-operators at a regional and EU level

The Charter for Media Freedom adopted in Thessaloniki in June 2000. provides a common, shared set of practices and points of reference for media reform and development in the countries of the region to ensure the highest international standards of freedom.

The EAR is helping some larger organisations, both public and private, improve their management and journalism. It is also assisting smaller independent media organisations with grants. However, one of the main problems in the western Balkan media today is not so much the freedom of expression itself, but rather the question on how this freedom should be properly used. Significant efforts are therefore underway to develop an effective legal framework for media, in cooperation with the Council of Europe. More must be done in adopting, amending, and effectively implementing the legislation, and in raising professional and ethical standards necessary to cement a culture of independence and sustainability, minimize sensationalism and bolster understanding and dialogue between communities. Expert advice and training are regular components in most of the Agency's programmes, not least in the media sector, to ensure that improvements and change can be sustained. Separate training courses have however been organised for journalists. In FYR Macedonia, more than 60 Albanian and Macedonian journalists and editors received training from the Danish School of Journalism to improve the quality and standard of reporting in the country. A further 100 journalists participated in a series of debates on a national code of ethics. A third element of the project involved monitoring the media, for instance in examples of inflammatory language designed to agitate inter-ethnic relations<sup>15</sup>.

**Achieving Media Responsibility in Multicultural Societies<sup>16</sup>:** The equal participation of ethnic minorities is a major challenge for the sustainability of democratic transition in South Eastern Europe. Respecting and practicing minority rights is also a key factor for the European integration of the countries of this region. In recent years their governments have made a major effort to adapt their legislation to international standards. However, despite the emerging legal provisions and mechanisms, poor cross-community communication, discrimination and poverty still affect the situation of ethnic minorities throughout the whole region, and more especially the Roma. With the "Minority

---

<sup>15</sup> <http://www.ear.europa.eu/sectors/sectors.htm>

<sup>16</sup> [http://www.kbs-frb.be/code/page.cfm?id\\_page=153&ID=394](http://www.kbs-frb.be/code/page.cfm?id_page=153&ID=394)



Rights in Practice in SEE” project, the Fondation roi Baudouin aims to support action plans and initiatives aiming at fostering policy change at local, national and international levels in order to overcome discrimination and advocate for the effective participation of ethnic minorities. The project is co-financed by the Charles Stewart Mott Foundation and the Soros Foundations. It operates in Albania, Bosnia and Herzegovina, Bulgaria, Croatia, Macedonia, Romania, Serbia, Kosovo and Montenegro as well at the regional level through thematic workshops and at the European level with policy events, bilateral consultations with decision makers and the dissemination of briefing papers and reports. Finally, since January 2006, the project includes a new capacity building component called DIANET (Dialogue for Interaction. Advocacy and Networking Capacity Building). This programme aims at enhancing the networking and advocacy capacities of NGO’s in Albania, Macedonia and Serbia with the support of the European Commission (CARDS Network to Network Programme).

A group was engaged in the former Yugoslav Republic of Macedonia promotes inter-ethnic reconciliation through children and adult theatre, and the media (financed by EAR).

The importance of broadcasting and movie coproduction, supported by the Eurimages programme of the Council of Europe<sup>17</sup> and by the Media programme of EU should also be mentioned in this context.

### **Public Administration, including twinning and transfrontier cooperation**

EU assistance in this sector is focused on helping societies in the region build and strengthen their own democratic institutions. Support is given to enhance the framework for democracy with training offered to officials to help administrations function correctly. Also important are efforts to build democracy from grass-roots level to eradicate discrimination, reconcile ethnic tensions and improve human and civil rights. The creation and implementation of anti-discrimination laws has a double value in an area as ethnically complex as the Western Balkans. They help protect a minority community in one of the countries in the region and also provide reassurance to majority groups in other countries that their ethnic cousins are adequately protected in a neighbouring country. In this way, democratic stabilisation can promote acceptance of the European values of co-existence and reconciliation. Legislation is one of the first steps, so CARDS helps ministries improve the legislative process. Institutions are being assisted to administer new laws on elections, media and support to civil

---

<sup>17</sup> [http://www.coe.int/T/DG4/Eurimages/Default\\_en.asp//](http://www.coe.int/T/DG4/Eurimages/Default_en.asp//)

society, and officials are being given new skills and organisational methods. On-the-spot experts from EU member states are funded through "twinning" programmes to share their experiences with their counterparts in the region.

**A Regional School of Public Administration** has been launched for Western Balkans, under a contract with OECD financed by CARDS 2006, aiming at giving a common administrative culture to officials of the Western Balkans geared to European values and governance.

At the local level, culture may be taken into account both in the prevention of conflict situations and in post-conflict social reconciliation. For example, projects launched by the Council of Europe like:

- "Sarajevo, Intercultural City of the Council of Europe" Pilot Project, December 2003
- Project "Shared Cities on building inter-community dialogue and promoting a common civic identity and consciousness, focusing on five case studies: Belfast , · Mitroviça , · Nicosia , Narva/Ivangorod (Estonia/Russian Federation), Uzhgorod (Ukraine)
- All twinning between cities, equally supported by the Committee of Regions of the Council of Europe and the recent call for proposals for civil society dialogue with Turkey.

Furthermore IPA and the transborder activities of the Regional Fund promote transfrontier projects particularly in the fields of environment, prevention of disasters, transport, etc.

In conclusion, the ultimate aim of all projects is to help bringing reconciliation where wars and conflicts brought hatred<sup>18</sup> it appears that there is a broad range of instruments linking prevention of culture and conflicts; the most important is the political will of leaders to use them appropriately and help overcoming old hatred.

---

<sup>18</sup> See "Reconciliation" - The Process of Overcoming Conflict Related Emotions: Dealing with Humiliation, Victimization, Guilt and Distrust, Arie Nadler, Professor of Social Psychology, Argentina Chair for Research on the Social Psychology of Conflict and Cooperation, Tel Aviv University, Ramat-Aviv, 69978, Israel, Abstract of Introduction to be made in Brussels, Feb 14, 2003: "In my work I have distinguished between two types of emotional deterrents to the end of conflict: Socio-emotional barriers, and the barrier of distrust. Removing the first type of barriers is labeled socio-emotional reconciliation, and rebuilding trust between the adversaries is labeled trust-building reconciliation."

# REMARKS CONCERNING ROMANIA' SECURITY AND NATIONAL DEFENCE ISSUE IN THE GLOBALIZATION FRAMEWORK

LAURA CISMAS<sup>1</sup>,  
ALEXANDRU JIVAN<sup>2</sup>  
CLAUDIA CRISTESCU<sup>3</sup>

## **Abstract:**

The end of the XXth century and the beginning of the XXIst have been marked both by the growth of globalization's amplitude and by the changes of the international security environment. The main threats are terrorism, mass destruction weapons, the growing world polarisation between rich and poor, the faulty governance, the emphasize of the rivalries between the biggest economic powers of the world.

Crises and conflicts management as well as the effective control of a war suppose a collective defence, namely alliances and coalitions, as no country is able to defend by itself, so far. Of course, collective defence does not exclude the national one, but the latest depends on the first.

The present paper attempts to explain Romania's role as a security beneficiary and provider in South-Eastern European security environment, as a member of both EU and NATO,

**Key words:** acquis, border secure making, combat of illegal traffic, migration, reform;

---

<sup>1</sup> Professor PhD Laura Cismas is teaching at the Faculty of Economics, West University of Timisoara, [laura13cismas@yahoo.com](mailto:laura13cismas@yahoo.com).

<sup>2</sup> Professor PhD Alexandru Jivan is teaching also at the Faculty of Economics, West University of Timisoara, [alexandru\\_jivan@fse.uvt.ro](mailto:alexandru_jivan@fse.uvt.ro).

<sup>3</sup> MA Candidate.

## 1. The European Security and Defence Politics (ESDP)

ESDP has been developed after 1990 inside of Western European Union (WEU), NATO and EU, in times when WEU adopted the „Petersberg” missions meant to manage casual destabilisations, especially in Eastern Europe. These kinds of missions include those of peacekeeping and those of fighting forces in crises management, including peace imposing.<sup>4</sup>

In 1996, on the NATO summit in Berlin it has been decided for a European Security and Defence Identity to be created, a European „pillar” inside of NATO expected to allow European countries a military intervention there where NATO one would not be possible or would be limited. For this sake, EU would have the possibility to use NATO’s military capabilities<sup>5</sup>.

The grounds of Foreign and Common Security Policy (FCSP) are set trough the Treaty of Maastricht (1992)<sup>6</sup> and driven deeply in 1999, after the Treaty of Amsterdam.<sup>7</sup>

According to the Berlin Declaration (1992, June, Petersberg Hotel), WEU fulfills humanitarian and rescue missions, peacekeeping ones as well as missions of the fighting forces during the performance of some crises management operations (known as “Petersberg missions”). Among the most famous WEU missions, we mention: the mission of monitoring the embargo against Yugoslavia (1993, The Adriatic Sea and the Danube); support for the EU administrative mission in Mostar (1995); the contribution to the mission of instructing Albanians policemen (MAPE, 1999-2001); the assistance mission of de-mining (Croatia, 1999 – 2001).

As a consequence of adopting the Treaty of Amsterdam, the FCSP acknowledged new developments. It has been created the position of the High Representative for Foreign Policy and Common Security, while the European Council got new competences in defining the strategic orientations concerning security and defense. Much more, EU became the beneficiary of WEU capabilities, taking over the Petersberg missions, too.

Trough signing the Maastricht Treaty (1992) a new common army has been created, as a consequence of the signal given by Germany and France who were setting EUROCORPS<sup>8</sup>. These have been considered to be a first step towards the construction of an autonomous European defense.

In September, 2001, the European Parliament has elaborated a resolution to foreseen the establishment of a common security and defense European politics, including Petersberg missions. However, there has been a tendency to stump the distinction between security and defense, trough emphasizing the concept of defense with reference to territorial one, putting thus aside any interpretation that would have suggested an eventual rivalry with NATO.

Some states have token measures to restructure their armies and endow with adequate equipments, even with common ones, in view of a European Quick Reaction Force setting. It is considered that a European Common Politics in matters of security and defense is not a goal in itself, but an instrument of EU foreign policy.

---

<sup>4</sup>Conf. Article 17 of the Treaty of European Union, <http://www.europa.eu.int/eurlex/en/treaties/selected/livre106.html>.

<sup>5</sup> Berlin Agreement, plus, [www.nato.int/shape/news/2003/shape\\_eu/se030822a.html](http://www.nato.int/shape/news/2003/shape_eu/se030822a.html)

<sup>6</sup> Tratatul de la Maastricht (sau Tratatul U.E.), [http://www.europa.eu.int/eurlex/en/treaties/dat/EU\\_treaty.html](http://www.europa.eu.int/eurlex/en/treaties/dat/EU_treaty.html)

<sup>7</sup> Tratatul de la Amsterdam, <http://www.europa.eu.int/eurlex/en/treaties/dat/11997D/htm/11997D.html>

<sup>8</sup> Considere „A Force for The European Union and The Atlantic Alliance”, [www.eurocorps.org](http://www.eurocorps.org).

The development of the European Security and Defense Policy (ESDP) contributes to the strengthening of the transatlantic link and will lead to a strategic partnership between EU and NATO. We have to add that, as concerning the crisis management, the decisions adopted by the two organizations are independent one to the other. The eventual crises can be solved either through civil or military means, since the diplomatic ones prove to be insufficient. The armed force can be used only in accordance with the foundational principles of EU and with the member states Constitutions, as well as with the principles of UN Charter or of ESCO. According to the international public law, using an armed force supposes an ad-hoc mandate given by the Security Council of UN, in the absence of which the EU can not militarily intervene, with the exception of emergency cases and under the express call of the UN General Secretary.

In this respect, it was Mrs. Chancellor Angela Merkel to make the following remark with the occasion of the 50<sup>th</sup> anniversary of EU setting: We will struggle together against terrorism, organized crime and illegal immigration. We defend citizens' liberties and their civil rights also through the fight against those infringing on it."<sup>9</sup>.

## **2. Communitarian Acquis in the field of police co-operation and the combat of organised criminality. EUROPOL. CEPOL.**

The Acquis includes norms concerning the fight against the organised crime and witnesses' protection, EUROPOL setting up, the punishment for belonging to a criminal organization, the OCDE Convention concerning the combat of corruption in international commercial transactions, the Common Action from December, 1998 related to money washing, the identifying, following, blocking, sequestration and confiscating the crime's instruments and results, the Council's Directive related to prevention of using the financial system for money washing a.s.o.

In the framework of co-operation in the view of organised criminality combat, the member states can, under the requirement of another member state, identify, follow, freeze or confiscate the instruments of a given crime or its results. As for the prevention of money washing, the member states have to assure themselves that this activity is legally prohibited and that the financial institutions ask for client's identification on the ground of a strict evidence. The request for clients' identification is to be applied for any transaction that is over 15.000 Euro.

EUROPOL is an organism created at the level of member states, having its headquarters in Hague, Netherlands. Its mission is to make the competent authorities from the member states more efficient and to strengthen the co-operation in the following fields: prevention and combat of terrorism, of illegal traffic with drugs, with human beings, with clandestine immigrants, with radioactive materials and nuclear substances, with vehicles, the combat of Euro falsification prevention of money washing associated with international criminal activities.

---

<sup>9</sup> Declarația de la Berlin, din 29.03.2007 făcută cu ocazia aniversării a cincizeci de ani de la semnarea Tratatului de la Roma

## **The traffic with human beings**

The Combat of sexual women exploitation – multidisciplinary politics:

- immigration – the victims of such traffic who decide to witness can benefit a protection form in the destination state;
- judicial co-operation – introduction of drastic penalties, of the same dimension in all member states and the extinction of these penalties to third countries;
- co-operation in the matter of employment and social assistance, meant to help victims' reintegration and a strict supervision of labour conditions in order to prevent any kind of migrants' exploitation;
- co-operation with third states through different programmes and common action plans. These means of co-operation have to be developed with different regions in the world, that are providers of traffic victims.

## **Europol – The European Police Office**

Europol's mission is to improve the efficiency and the co-operation of competent authorities from the member states in order to prevent and combat terrorism, narco-traffic and other means of trans-national organized criminality.

The setting up of Europol has been provided in Maastricht Treaty, February 1992, but it started working only in 1994 under the label of "Ant drug Unit". Starting from 2002, January, the 1<sup>st</sup>, its mandate has been extended to other kinds of transnational criminality, such as: money washing operations, traffic with human beings (including juvenile pornography), clandestine immigration, terrorism, cyber-criminality or financial crimes. Europol facilitates the information changes between the link officers of Europol in member states; it provides the necessary operational analyses for specific operations; elaborates strategic reports of criminality combat through identifying the main threatening on the ground of the information provided by member states, assures expertise and technical support for the inquests and operations to take place in EU space.

Europol is working on the basis of an computerized system - *The Europol Computer System* – (TECS) – containing a certain amount of information related to persons that are followed up, because of their criminal activities or crime commitment.

The Europol leadership is appointed by the Council of European Union, on the level of Ministries for Justice and Internal Affairs, who have the right to control and question on the Europol activity.

## **The Police European College (CEPOL)**

CEPOL has been created in 2000, December, in the bases of EU Council's Decision. It is an organism that binds together the national institutes that train the police officers in the member states. Its aim is to assure stages of training and specialization for European police officers, according to the latest terrorist threatening to the European security.

### **3. Romania' security and defense dimension in the context of globalization**

Once with Romania's admission as a full member of NATO, its defense politics has a pro-active character, meaning that there is no longer meant only a defense of national territory and a preventive diplomacy, but also politics that offensively promote the country's interest and sustain global stability in any region where NATO has missions. As it is put down in official documents for the first decade of the XXIst century, Romania's defense objectives list:

1. the consolidation of Romania' statute as NATO member state, the integration in the EU (attained objective) and the development of a strategic, adequate profile inside of these organizations;
2. the continuation of the reform of military organism, in order to develop a credible, modern and efficient defense capacity;
3. the strengthening of civil and democratic control on the army and the improvement of the mechanisms meant to do it, according to the principles and the values of a constitutional democracy;
4. the consolidation of Romania's statute as a provider of regional and global security;

According to Romania's geo-strategic position in the South –Eastern European space – as a NATO and EU frontier country – the national defense policy will have as main objective, the defense and the promotion of Romania's vital interests, as well as the active participation of our country to the security assurance for the interest zones of NATO and EU.

In this respect, the official documents mention that Romania has to take into consideration the following actions: the development of the institutional and combative capacity of its military structures, the army's equipment with specific logistics for the collective missions, the participation to European security and defense policy, the active participation to the gaining of the objectives aimed by the Pact for Stability in the South-Eastern Europe and the maintenance of stability in the Caucasian-Caspic zone, in that of the Black Sea and of the Balkans, the fight against terrorism; the continuation of the programs of professional re-conversion and human resources management improvement; the revise of the force structure of the army, the development of the civil-military relations.

Taking into consideration of these requirements, the yearly military expenditures will have a 2.38% weight in the BIP (Brut Inner Product), level that is to be preserved in the 2005-2008

interval<sup>10</sup>. Starting with 2004, as Romania is a NATO member state, there have been provided in the defense' yearly budget, the national contributions representing the participation obligation of our country to the common budgets of the Alliance (the civil, the military and the infrastructure budget). In this context, the participation to the common budgets represents a part of multi-annual arrangements of resources management and of allied requirements, established by the NATO's Military Authorities. The percentage contribution that costs Romania for the military Budget and for the NATO Security Investment Program – (NISP), in the interval of 2004-2007, is 1.3233% every year. In addition, for the period 2006-2014 there are also annexed the Costs for the Objectives of the 2006 Force, already assumed by Romania. (see, table no. 1)

**Table no. 1.**

**The Costs for the 2006 Force Objectives, assumed by Romania for the period 2006 – 2014 (mld RON)**

Allocated Funds until 2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	After 2014	TOTAL
2,510	1,411	2,945	3,168	2,997	3,168	3,349	3,467	2,568	2,390	7,456	34,757

From the point of view of stability, the states from the West Balkans can be divided into three categories:

1. The first group of states, and the most stabile consists of Romania and Bulgaria, that are already NATO and EU members;
2. The second group is made up of states like Croatia, Macedonia and Albania, where an acceptable stability is to be found, Croatia being also on the list of countries asking for EU and NATO adherence and having real perspectives in this respect;
3. The third group and the most sensible one includes Serbia and Bosnia-Herzegovina. It has to be emphasized that Bosnia lays under international leadership on the national territory, for ten years, and also the fact that both states have a great instability potential.

We must also take into consideration the fact that the whole Ponto- Caspical zone of the ex-soviet space is extremely instable, the local risks and threatening affecting both Romania and the EU. In this respect did two major politico-military Romanian analysts put down: “In this period, the main features of the Central and South-Eastern European security environment can be described like: the maintenance and extension of some high risky grade zones; the existence of some inefficient managed crises as a fact that improves the danger of their restart or of some others coming into scene; the persistence or the development of some inner disputes that can degenerate into conflicts with obvious tendency to internationalise; the perpetuation and encouragement of some territorial claims and of autonomy trends of some ethnic, religious or cultural communities, the extension of the existence and influence of Islamic fundamentalism

<sup>10</sup> According to the Governance Program 2005-2008, chapter 27, Official Journal no. 1265, from 2004, December, the 29th;



area, with its radical wing, that amplifies the instability of the Balkanic area; tendencies to rebuild the old influence spheres or to become regional leader coming from some states in this space or from the adjacent one; the nearby existence of some instability zones like Middle East, ex-Yugoslavia, Caucasus or Trans-nistria; the appearance of non-military risks and threatens, with negative effects on the national security, like organised crime, the traffic with drugs, armament or strategic materials, illegal persons' migration, the emphasizing and diversifying some states in the region efforts to integrate into European and Euro- Atlantic security and economic structures.”<sup>11</sup>.

The process of globalisation brings also the perspective of some combined threatens like: the development of terrorism, since there is possible for mass destroying weapons to be purchased, possible co-operations between fundamentalist elements, collaborationist ones and international criminal organizations.

NATO remains the cornerstone of Euro- Atlantic stability, since the common defence represents the core on which the special security depends on. As for the EU, its extension towards Ukraine, Republic of Moldavia, the ex-Yugoslavian countries, the Caucasus region, that of Caspic Sea and an important segment of Middle East, all these impose the necessity to assure European security and stability. Here is where the necessity of establishing of a common agenda of the two organisations came out, each of them having its strengths and offering specific advantages. The fact that these instable regions are placed in the immediate neighbouring of the European and Euro-Atlantic space, turns for the co-operation of the two organisations be absolute necessary in order to attain the common politico- strategic aims.

The operational dimension of ESDP is nowadays, a reality. We can mention, therefore, the European Union' steps to manage the security issue both in the Balkans and in the Caucasus, and in Africa, Middle East and Asia, being expressed in the launch of a number of 15 operations in this geographical perimeters, so far. Romania took part to such operations, both trough contributions with forces and capacities, and trough effective engagements.

#### **4. Romania's Contribution to the Consolidation of an Area of Freedom, Security and Justice**

Romania, as a European Union member state, is among the countries that take part to this area's consolidation. The achieved progresses as well as the provided measures point, mainly, to the harmonization of legislation, institutions and practices in our country with the European ones, in the matter of Justice and Internal Affairs. The assurance of an efficient management of the boundary, close to the reform of the legal system represent a priority, especially since the Northern and the Eastern Romania's frontier became the external EU' one, once the joining took place. Romania is also interested in promotion of the principles and practices used by the European Union in this region, through own initiatives meant to assure consistency to the combat of illegal immigration, of the traffic with human beings, of the transnational criminality, in general. Romanian presence in Kosovo, as well as in Bosnia- Herzegovina is an example of how our country implies in the management of the regional problems, together with the EU and third

---

<sup>11</sup> Dr. Sorin Frunzăverde and Dr. Constantin Onișor, *Sourth-Eastern Europe. Main Security Dimensions*, 1992, edition, 2004;

countries implied in this process. The network of linkage officers in the member states and also in the on-going joining process, the activity in the framework of some European and international organizations reflect Romania's preoccupation for a constant and permanent dialogue with EU partners in the view of developing of some optimum reaction capacities towards the political developments and the operative necessities in the field. Still, here there are some difficulties encountered by and some achieved progresses of Romania in the implementation of the Communitarian acquis in the field of Justice, liberty and security:

### ➤ **The Schengen Action Plan**

It had been elaborated in the direction of the transposition and the implementation of Communitarian provisions. It is completed by the National Strategy for Integrated Management of the Frontier, 2004-2006 and by the Strategy of Securitizing Romania's Frontier in the interval 2004-2007.

The most serious problems to be solved for the frontier' securitizing lay on the administrative capacity. Trough this, we mean the endowment with modern equipment, the profesionalisation of the personal from the Frontier Police (by giving up the calling for recruits) , and filling the vacant jobs.

Among the safeguarding clauses connected to the chapter of Justice and Internal Affairs, there was also the speeding of the efforts to modernise the equipment and the infrastructure to the coming external EU frontier. Another requirement was the recruiting of 4438 frontier police agents and officers in order to fully occupation of all the vacant jobs, especially at the border to Ukraine, Moldavia, the Black Sea Beach. In the same respect, Romania has to implement all the necessary measures to effective combat of illegal immigration, including the strengthen of the co-operation with third states.

In 2004, July, there has been realised a fezability study in the direction of a further implementation of the Integrated System of Frontier' Security. The Govern has borrowed 650 millions of Euros in order to apply the strategy of secure making border and has already contacted a company expected to realise it. In order to improve the border police efficiency, Romania has bought mobile supervision vehicles, gifted with thermo detecting machines. Romania's Northern and Eastern frontiers are European Union' external borders and, since Romania is situated at the confluence of some great migration flows from the ex-soviet republics, from the Middle East, from Asia and Africa, Romania has huge responsibilities to border' securiting.

### ➤ **The Visas Policy**

Romania goes on in aligning to the positive EU' list. The on-line visa system has been established and is already operational. This system links the Authority for Foreigners to Romania's diplomatic missions in Russia, Ukraine, Turkey, Serbia, Montenegro and Egypt. Many persons have been employed in these diplomatic missions in order to manage the visa's liberating. The Consulates have been gifted with special apparatus to detect the false or falsified documents and it started the distribution of the new visa self-stick. The growth of the efficiency of border control has been reflected in the increase number of Romanians who have not been

allowed to go out of country, from a number of 417969 persons, in 2002 to 1.216.625 persons, in 2003.

### ➤ **Data Protection**

**The Institution of Ombudsman** is the national authority charged to supervise and control the activities of dealing with personal data. The Communitarian acquis is applied through some specific laws (682/2001, 677/2001) in order to protect individuals against the automatic processing of personal data and against their free movement, as well as for the protection of private life in the telecommunications field.

### ➤ **Migration**

The legislation concerning the foreigners' regime in Romania is nowadays meeting the European standards. It provides the conditions of entrance, of sitting and of leaving Romania. This is how a legislative framework is given in order to combat the illegal migration. There have also been regulated:

- the distinction between visa (up to 90 days) and residence permission (more than 90 days);
- the regime of the season workers statute;
- the mandatory request of an affaires plan for the foreigners asking for the establishment of LTD-s;
- the introduction of the notions of short-time resident, long-time resident and permanent one;
- the assurance of minor's protection since they are not accompanied and come from other states than the ones with high migration potential;
- the principle of volunteer return.

It has also been adopted The National Strategy regarding Migration and the Action Plan. It has been set up a "frame agreement" concerning the re-admission of Romanian and foreigner citizens, meeting the provisions of the Convention on the Statute of Refugee Persons and of the Protocol on the Refugee Statute.

In the negotiation process of the re-admission agreements, the state risk of migration potential has been taken into consideration. In order to combat immigration and clandestine emigration, Romania will go on appointing linkage officers and attached persons charged with internal affaires. It has also been created The National Authority for Foreigners as well as a National Centre for Visas.

### ➤ **The Asylum**

The National Office for Refugees – as the central charged authority – has made great efforts to train and educate its personal, but also in the field of international and inter-institutional co-operation. A greater accent will be on the persons who have already been given some sort of

protection. The second appeal has been rejected inside of accelerated procedures to examine the asylum requests and of border procedures. It has also been regulated the temporary protection offer in the case of a massive influx of dispelled persons. Concepts like “refugee person”, “obvious ungrounded requests”, “country with a general non-existing a serious persecution risk”, “accelerated procedures”, “third safe country” have been defined.

The non-accompanied minors encounter a special attention during the whole asylum procedure. Those who have already achieved the refugee statute do benefit the same rights like the Romanian minors in difficulty. The National Office for Refugees co-operate eith non-governmental organisations and with UNHCR to assure some decent accommodation conditions to the asylum solicitors as well as for the integration of the persons who have already obtained some protection form.

There are four centres that host the asylum solicitors and the refugees: two are situated in Bucharest, one in Timisoara and one in Galati. The number of places in these centres is 1400, that is more than necessary in regard to the number of asylum solicitors across one year. Great efforts are made to train the personal working in those centres.

#### ➤ **The Police Co-operation and the Combat of Organised Criminality**

Romanian legislation now meets the Communitarian standards with regard to money washing, the identification, following, blocking, sequestration and confiscation of the crimes’ instruments and results, the criminal punishment of the moral persons for coins’ falsification or of other values, the protection of witnesses, the prevention and the combat of organised crime, especially of the computer one.

Romanian police had been de-militarized and organised according to the Law 360/2002 regarding the policeman statute and the Law concerning the police organisation. In order to turn police’ activity more efficient and to orient police forces towards the citizens’ needs of security, it has been established the proximity police, some regional centres of rural police and it has been re-organized the public order police for the urban zones.

As for the international co-operation, attached personal for internal affairs and linkage officers have been appointed to Romania’s diplomatic missions from other states or from international organizations.

It has also been set up the Anti-Drug National Agency. Co-operation agreements have been signed up with other countries in the view of combating the organized crime, the illegal traffic with stupefying, terrorism and other serious crimes. An EUROPOL department has been created inside of the General Police Department.

#### ➤ **Customary Cooperation**

Romania has adopted a set of legal and organizational measures that have to be implemented with regard to the adherence to the Napoli II Convent. In this respect, it is regulated the usage of the Customs Integrated Computer System.

The co-operation with European customary administrations is taking place according to a specific reciprocal assistance protocol. Mobile controlling teams have been established in order to

prevent, to detect and punish the customary fraud and to strengthen the customary controlling operations.

➤ **The fight against fraud and corruption**

The legal framework for the protection of the financial interests of the European Communities has been modified according to the standards. It has also been adopted the regulations for fraud combating and for the falsification of the means of paying, Euro's protection against falsification, corruption combating. In this respect, there have been established:

- in 2002, The National Anticorruption Prosecutor's Office;
- in 2004, The Office for Combating the Communitarian Frauds;
- in 2004, The Service for Combating the Organised Crimes and Corruption.

As a linkage point with the OLAF, it has been designated the Control department of the Prime Minister, while this latter competences have been taken by the Inspection Direction of the Prime Minister.

It has been adopted the national Anticorruption Strategy, consisting of: The National Program of Corruption Prevention and The National Program of Actions against Corruption. And all these because corruption still remains Romania's most important problem. Therefore, it has been raised the question: what still is to be done?

Two safeguarding clauses have been formulated with regard to the fight against corruption:

- The acceleration of the fight against corruption by orienting it towards the high level corruption. It is essential for these anti-corruption regulations to be rigorously applied. Another very important issue is the assurance of a real independence of the Anti-Corruption National Prosecutor's Office. In order to meet its duties, it has to obtain more financial and human resources, training and logistics.
- The assurance of an independent audit on the impact of present day anti-corruption strategies. The results of this audit have to be accompanied by proposals for an action plan as well as by budgeting provisions in order to fulfill these duties. The strategy's implementation must be supervised by a unique and independent organism, with clearly definite obligations. It has to be avoided the superposition of the responsibilities regarding the corruption prevention and investigation. The accordingly procedures must be simple and transparent, in order to grant correct sanctions and discouraging effects.

So as the European observers' remark, there is enough legislation in Romania with regard to corruption prevention and combating, but there are serious problems in their application. Even some institutions from the judiciary system meant to instrument and judge the corruption cases, are affected by corruption. The sanctions that have been applied in such cases resumed to internal disciplinary means or to integrity tests. But the criminal pursuit in the corruption cases is essential for discouraging future practices and also for growing people's trust in these institutions.

The national Anti-corruption Prosecutor's Office has had – from its very beginning - obvious successes while instrumenting corruption cases on a low and medium level. But the high level cases

have not been attacked with too much decision, proving the political sensitivity of such cases as well as the lack of a total independence of this Office.

The combating of drugs traffic and consume is still based on weak institutions and on a critical inter- institutional communication. The drugs transits in Romania as well as the internal production of synthetic drugs remain serious problems, while the statistics of the border control show that the discovery rate is low.

Some other existing problems are related to the institutional capacity of the agencies expected to deal with the prevention and control of money washing.

➤ **Judicial cooperation in civil and criminal matter**

Three important conventions have been adopted in this respect:

- a Convent regarding the profs obtaining from other countries;
- a Convent on the notification in other countries of the judiciary and extra-judiciary documents notification;
- A third Convent to facilitate the access to justice;

From an institutional point of view there has been created a net of national correspondents for international legal and judiciary co-operation, with regard to Romania's participation to EUROJUST.

Romania's legislation meets the acquis related to racism and xenophobia's combating. And the system of children protection has also been reformatted.

➤ **General evaluation of Romania's progresses in the domain of justice and internal affairs.**

A first such evaluation realized in 2000 proved that Romania was not institutionally prepared for the adherence. The adaptation of the communitarian acquis in the domain of justice and foreign affairs was in an incipient stage. Remarkable progresses have been made after 200 in many chapters referred by chapter 24. There have been realized fundamental reforms on the institutional level, agencies have been created and laws and regulations largely compatible to the Communitarian acquis have been adopted. Although this chapter has been closed at the end of 2004, there are still lots to be done in implementing the adopted regulations. Three main directions have to be followed:

- the legislation completion where there is still necessary or its revision;
- the implementation of the final legal framework;
- the strengthening of the administrative capacity.

Romania has to give priority to the following problems:

- the immediately alignment to Schengen plan of actions;
- the modernization of the equipment and of the infrastructure; the recruitment of trained personnel for the border police, especially for the Northern and Eastern Border;

- the implementation of an integrated action plan and of a reform strategy in Justice;
- the rigorous application of the present day anti-corruption strategy as well as the realization of the effective independence of the national Anti-Corruption Prosecutor's Office;
- the realization of an independent audit on the result and the impact of present day anti-corruption strategy;
- a clear duties separation between police and gendarmerie, as well as the recruitment of necessary personal for the free jobs in both institutions;
- the development and the implementation of a multi- yearly coherent strategy on criminality prevention, including concrete actions to prevention and combating the human beings traffic.

## **5. Conclusions**

The concept of European Union as an area of freedom, security and justice has been introduced by the Treaty of Amsterdam, that entered into force in 1999, May, the 1st. It provides that EU must be preserved and developed as an area of liberty, security and justice, where the free movement of persons and their right to residence on the whole EU territory are assured. However, these represent essential elements of the European citizenship. These objectives are sustained by legal and institutional mechanisms meant to determine the function of this area without prejudicing the rights and the interests of the member states citizens.

The area of freedom, security and justice includes a number of policies meant to assure that for the Unions' citizens, the liberty is granted, since each one enjoys access to justice and derive security benefit. Starting from the applied policies it turns out that the European Union promotes all over the world the application of the rights and liberties that its own citizens enjoy. These policies do not deny the access in the European Union of those whose freedom and security is not granted in their origin states. In this respect, common policies in matter of asylum and migration are promoted, as well as a constant preoccupation for external borders' management and efforts to combating the illegal migration and the connected trans-border criminality.

One of the objectives on which these policies ground is to assure an open and safe Europe, which to respect in whole the provisions of the Geneva's Convention on the refugee' status and of other relevant instruments on human rights, a Europe capable to answer humanitarian needs in the solidarity spirit. All these are important for Romania, as well as for the European Union and for NATO, because the risk factors addressing the security and national defense still exist in a world that encounters a continuous globalization process.

## References:

- Sorin Frunzăverde, Constantin Onișor – *The South-Eastern Europe. Main Security Dimensions*, edition A'92, 2004;  
*Micro-monographs – European Policies*, chapter: ”Justice and Internal Affairs”, *European Institute Romania*, 2005;  
The Series: *Communitarian Acquis no.15* “A Space of freedom, Security and Justice”, (basic documents) The European Institute, Romania, 2004;
- The Series: *Europe on the move* “Freedom, security and justice for all. Justice and home affairs in the European Union” European Commission, Directorate-General for Press and Communication, 2003;
- Justice and Internal Affairs, The Centre for Legal Resources, Romania, 2004, <http://www.crj.ro/publicatii.php>
- The Ministry for Foreign Affairs - *UE Integration: The Aria of Freedom, Security and Justice*, [www.mae.gov.ro](http://www.mae.gov.ro);
- The Ministry of Administration and Internal Affairs, *The Integrated System for the State Border Security*, [www.mai.gov.ro](http://www.mai.gov.ro) ;
- Ferreol, Gilles (co-ordinator), *The Dictionary of European Union*, Polirom, 2001;  
<http://www.europa.eu.int/eurlex/en/treaties>  
<http://www.eurocorps.org>.
- Official Journal, No. 1265, from 2004, December, the 29<sup>th</sup>, The Governance Program 2005-2008, chapter 27;



**“UNITED IN DIVERSITY” – QUANTIFICATION OF  
EUROPE’S DIVERSITY AND WAYS TO USE IT AS A  
GROWTH ENGINE**

**MONICA CRISTINA PARPALEA <sup>1</sup>**

**Key words:** Diversity, Demography, Growth, Immigration, Statistics

**JEL code:** J15 Economics of Minorities and Races; Non-labor Discrimination

---

<sup>1</sup> Geopolitics and International Relations Master 1<sup>st</sup> year Student (Academy of Economic Studies Bucharest); mail: [moniparp@yahoo.com](mailto:moniparp@yahoo.com).

“United in diversity” is the motto of the European Union that came into use around year 2000. Taking into account the accelerated increase of immigration and the rise of more and more radical movements in Europe, this motto is still valid as concerning the increase of ethnical and religious diversity. How can we use the increase of minorities to help Europe’s Growth?

Using the statistical research (Eurostat database) and theory of scholars I’ll show the current situation of UE population structure, the positive aspects as well as the possible threats and social risks within the European Union.

This paper will focus mainly on 3 directions: demography, migration and religion.

The two World Wars were devastating for Europe. Those were the roots of some of the problems that we are currently facing. For example, the last boom of Europe’s population immediately after the Second World War has created a record number of pensioners nowadays and in the same time the low birth rate (that has become a European characteristic), represents a challenging problem on medium and long term for the governments.

## 1. EU Countries Demographical Characteristics

The demographical characteristic of the 27 countries currently forming the EU are at first glance quite uniform. The result of low birth rates cumulated with the net immigration is seen in the evolution of the number of inhabitants between 2001 and 2005 negative for some countries and constant for others (Table 1). The ageing population represents the biggest threat to the EU development. We can see that all the ex-communist countries have a negative growth partially because they are the main source of emigration but also because of the less developed economy. The highest growing rates are in the catholic countries of Ireland and Spain.

I’ll use the Gini – Stuck coefficient to ponder the differences between countries revealing the uniformity of the augmentation of population in the period 1995 – 2005.

$$G = \sqrt{\frac{n \sum g_i^2 - 1}{n - 1}} \quad n = 27 \text{ EU Countries}$$

g = each country’s percentage of population augmentation out of the total EU population increase

The total population increase between 1995 and 2005 was only 12 million inhabitants.

The result of the Gini–Stuck coefficient is 0,44 indicating a medium level of diversity concerning the population increase trend, mainly because of the negative values the former communist countries have.

Table 1. Annual growth of population between 1995 and 2005

Country	Population (millions)		Population growth (average annual growth per annum in %)	
	1995	2005	1995-2000	2001-2005
EU-27	477,03	488,96	0,2	0,32
EU-25	445,9	459,5	0,2	0,40
Euro area	298,7	310,9	0,3	0,60

1	Belgium	10,1	10,4	0,2	0,4
2	Czech Republic	10,3	10,2	-0,1	-0,1
3	Denmark	5,22	5,41	0,4	0,3
4	Germany	81,5	82,5	0,2	0,1
5	Estonia	1,45	1,35	-1,1	-0,4
6	Greece	10,6	11,1	0,6	0,3
7	Spain	39,3	43	0,4	1,5
8	France	57,8	60,6	0,4	0,6
9	Ireland	3,6	4,11	1	1,8
10	Italy	56,8	58,5	0	0,6
11	Cyprus	0,65	0,75	1,4	1,8
12	Latvia	2,5	2,31	-1	-0,6
13	Lithuania	3,64	3,43	-0,7	-0,4
14	Luxembourg	0,41	0,46	1,3	0,9
15	Hungary	10,3	10,1	-0,2	-0,3
16	Malta	0,37	0,4	0,6	0,7
17	Netherlands	15,4	16,3	0,6	0,5
18	Austria	7,94	8,21	0,1	0,6
19	Poland	38,6	38,2	0	-0,1
20	Portugal	10	10,5	0,4	0,7
21	Slovenia	1,99	2	0	0,1
22	Slovakia	5,36	5,38	0,2	0
23	Finland	5,1	5,24	0,3	0,3
24	Sweden	8,82	9,01	0,1	0,4
25	United Kingdom	57,9	60	0,3	0,4
26	Bulgaria	8,43	7,76	-0,6	-0,5
27	Romania	22,7	21,7	-0,2	-0,9

Source Key figures on Europe Statistical Pocketbook 2006

The table number 2 shows the life expectancy for the citizens of each EU country. We can easily see that once again the ex-communist countries have the smallest life expectancy, in part because of a deficient health system and also because of the low income, diet or certain damaging habits (such as smoking cigars or alcohol consumption).

The inequality of the life expectancy indicator throughout Europe, along with the individual income status is greater than any other social indicator. For example, the life expectancy of a man from Latvia is shorter with almost 13 years (12,9) than that of a man from Sweden. The situation is better as it concerns the women thus the biggest difference between the smallest life expectancy (Romania) and the highest (Spain, France) is 8,7 years.

We notice that Romania is in a very bad position being last at women life expectancy and second to last overall. I guess this has to be connected with the low life standards and with the large rural percentage of population which receive inadequate health care.

Table 2. Life expectancy age

Country	Medium life expectancy age (years)	Male	Female
EU-27	76,8	73,5	80,2
EU-25	77,2	75,1	81,2

	Euro area	78,9	76	81,9
1	Latvia	71,35	65,5	77,2
2	Romania	71,4	67,7	75,1
3	Estonia	71,45	66	76,9
4	Lithuania	72,1	66,4	77,8
5	Bulgaria	72,45	68,9	76
6	Hungary	72,75	68,6	76,9
7	Slovakia	74,05	70,3	77,8
8	Poland	74,6	70	79,2
9	Czech Republic	75,8	72,6	79
10	Slovenia	76,5	72,6	80,4
11	Portugal	77,35	74,2	80,5
12	Denmark	77,55	75,2	79,9
13	Luxembourg	78	75	81
14	Ireland	78,25	75,8	80,7
15	United Kingdom	78,45	76,2	80,7
16	Germany	78,55	75,7	81,4
17	Malta	78,7	76,7	80,7
18	Netherlands	78,75	76,4	81,1
19	Finland	78,8	75,3	82,3
20	Belgium	78,8	75,9	81,7
21	Greece	79	76,6	81,4
22	Cyprus	79,2	77	81,4
23	Austria	79,25	76,4	82,1
24	Italy	79,65	76,8	82,5
25	France	80,25	76,7	83,8
26	Spain	80,5	77,2	83,8
27	Sweden	80,55	78,4	82,7

Source Key figures on Europe Statistical Pocketbook 2006

The table number 3 shows data about Marriages in Europe. This institution was most important especially for the birth rate, but as Religion's influence over people decreased dramatically and as the woman status improved, the significance dropped and we can see that from the indicator of percentage of births outside the marriage that reached almost a third of all live births raising with more than 10% since 1996 (23%).

Divorce is not possible in Malta. The lowest divorce rates are in the country that last legalized it such as Ireland (1995), Spain (1981), Scotland (1976) and in the most religious driven countries such as Greece, Romania and Poland.

The result of the Gini–Stuck coefficient for marriages is 0,24 and for divorces is 0,29 indicating a low level of diversity concerning the population drive toward marriage and some difference regarding the attitude toward divorce, mainly because of some peaks. The most unstable citizens as it concerns marriages are by far the Belgians, Estonians and the Czech.

Table 3. Marriage and divorce indicators

Country	Marriages (per 1.000)	Divorces (per 1.000)	Divorce rate per 100 marriages	Mean duration of Marriage at divorce (years)
Year	2004	2004	2003	2003

	EU-27	5	2,1	40,2	12,1
	EU-25	4,8	2,1	40,5	12,3
	Euro area	4,6	1,9	37,7	12,8
1	Belgium	4,1	3	75	12,9
2	Czech Republic	5	3,2	67,1	11,3
3	Denmark	7	2,9	45	11
4	Germany	4,8	2,6	52,1	:
5	Estonia	4,5	3,1	69,6	10,1
6	Greece	4,2	1,1	19,6	:
7	Spain	5	2,1	20,1	:
8	France	4,3	2,1	45,7	13,2
9	Ireland	5	0,7	0,7	12,9
10	Italy	4,3	0,8	15,4	15,8
11	Cyprus	7,2	2,2	12,8	13,4
12	Latvia	4,5	2,3	48,3	10,2
13	Lithuania	5,6	3,2	62,4	:
14	Luxembourg	4,4	2,3	51,3	12,6
15	Hungary	4,3	2,4	55,2	10,9
16	Malta	6	:	:	:
17	Netherlands	4,7	1,9	39,7	12,8
18	Austria	4,7	2,3	50,5	11,1
19	Poland	5	1,5	24,9	12,3
20	Portugal	4,7	2,2	41,3	12,7
21	Slovenia	3,3	1,2	33,6	12,8
22	Slovakia	5,2	2	41,2	12
23	Finland	5,6	2,5	52,2	12,5
24	Sweden	4,8	2,2	54,1	11,8
25	United Kingdom	5,1	2,6	2,8	:
26	Bulgaria	4	1,9	39,2	10,5
27	Romania	6,6	1,6	24,7	10,4

Source Key figures on Europe Statistical Pocketbook 2006

Most important indicator for the future of Europe is the birth and fertility indicators as we already saw that the EU population is ageing continuously.

We can see in the Table no. 4 the severity of the EU demographic problem. None of the countries reaches the minimum fertility rate of 2,1 which can assure at least a constant level of the population.

The result of the Gini–Stuck coefficient for the births rate is 0,03 indicating a constant level of births throughout Europe, probably the thing that most unites us.

New policies should be implemented to convince Europeans to have more children.

Some help regarding this problem we received from migrants, as so in 2000 Europe was hosting the largest migrant population with over 56 millions migrants, followed by Asia (50 millions) and North America (40 millions)<sup>2</sup>.

<sup>2</sup> Source Alexandra Delcea – “Remittances and International Migration: Romanian in the Context of the European Union ” Bucharest, Paralela 45, 2007, page 42

Table 4. Birth and fertility indicators

	Country	Number of live births (thousands)		Crude birth rate (‰)		Total fertility rate (number of children)		
		Year	1995	2004	1995	2004	1995	2004
	EU-27		5131	5082	10,7	10,4	1,4	1,4
	EU-25		4822	4796	10,8	10,5	1,4	1,5
	Euro area		3103	3217	10,4	10,4	1,4	1,5
1	Belgium		115,5	116,0	11,4	11,1	1,6	1,6
2	Czech Republic		96,1	97,7	9,3	9,6	1,3	1,2
3	Denmark		69,8	64,6	13,3	12,0	1,8	1,8
4	Germany		765,2	705,6	9,4	8,6	1,3	1,4
5	Estonia		13,5	14,0	9,4	10,4	1,3	1,4
6	Greece		101,5	104,0	9,5	9,4	1,3	1,3
7	Spain		363,5	453,3	9,2	10,6	1,2	1,3
8	France		729,6	767,8	12,6	12,7	1,7	1,9
9	Ireland		48,8	61,7	13,5	15,2	1,8	2,0
10	Italy		525,6	562,6	9,2	9,7	1,2	1,3
11	Cyprus		9,9	8,3	15,2	11,2	2,1	1,5
12	Latvia		21,6	20,3	8,7	8,8	1,3	1,2
13	Lithuania		41,2	30,4	11,4	8,9	1,6	1,3
14	Luxembourg		5,4	5,5	13,2	12,0	1,7	1,7
15	Hungary		112,1	95,1	10,9	9,4	1,6	1,3
16	Malta		4,6	3,9	12,4	9,7	1,8	1,4
17	Netherlands		190,5	194,0	12,3	11,9	1,5	1,7
18	Austria		88,7	79,0	11,2	9,7	1,4	1,4
19	Poland		433,1	356,1	11,2	9,3	1,6	1,2
20	Portugal		107,2	109,3	10,7	10,4	1,4	1,4
21	Slovenia		19,0	18,0	9,5	9,0	1,3	1,2
22	Slovakia		61,4	53,7	11,5	10,0	1,5	1,3
23	Finland		63,1	57,8	12,4	11,0	1,8	1,8
24	Sweden		103,4	100,9	11,7	11,2	1,7	1,8
25	United Kingdom		732,0	716,0	12,6	12,0	1,7	1,7
26	Bulgaria		72,0	69,9	8,6	9,0	1,2	1,3
27	Romania		236,6	216,3	10,4	10,0	1,3	1,3

Source Key figures on Europe Statistical Pocketbook 2006

## 2. Migration quantifications

In every member state, a proportion of the population is made up of people from other countries — usually with close historical ties to the host country. The EU regards ethnic and cultural diversity as a great asset, and it promotes tolerance, respect and mutual understanding — values that Europe's long history has taught us.<sup>3</sup>

In table 4 you can see that most of the immigrants settled in countries that have a deficit on the labour market (Spain and Italy) and that are in the same time boundaries of the EU with one very prolific region – Africa.

<sup>3</sup> Source <http://europa.eu>

These figures are showing just the top of the iceberg as the International Centre for Migration Policy Development estimates that 400.000 people are smuggled into the EU annually.

Table 5. Net Migration indicators

	Country	Year	Net migration (thousands)		
			1995	2000	2004
	EU-27		670	445	1838
	EU-25		691	677	1847
	Euro area		619	917	1576
1	Belgium		2	13	35
2	Czech Republic		10	7	19
3	Denmark		29	10	5
4	Germany		398	168	82
5	Estonia		-16	0	0
6	Greece		77	29	35
7	Spain		71	390	610
8	France		-15	103	100
9	Ireland		6	32	48
10	Italy		32	55	558
11	Cyprus		7	4	16
12	Latvia		-14	-5	-1
13	Lithuania		-24	-20	-10
14	Luxembourg		4	4	2
15	Hungary		18	17	18
16	Malta		0	10	2
17	Netherlands		15	57	-10
18	Austria		2	17	62
19	Poland		-18	-410	-9
20	Portugal		22	47	47
21	Slovenia		1	3	2
22	Slovakia		3	-22	3
23	Finland		4	2	7
24	Sweden		12	25	25
25	United Kingdom		65	144	202
26	Bulgaria		0	-221	0
27	Romania		-21	-4	-10

Source Key figures on Europe Statistical Pocketbook 2006

In practice, old immigrants are attracting the new ones and in time they become an ethnic group. They see themselves as culturally distinct from other groups in a society, and are seen by those other groups to be so in return. Different characteristics may serve to distinguish ethnic groups from one another, but most usual are language, history or ancestry (real or imagined), religion and styles of dress or adornment.<sup>4</sup>

To avoid the potentially social problems, can ethnic diversity be accommodated and the outbreak of ethnic conflicts averted? There are 3 primary models of ethnic integration: assimilation (the

<sup>4</sup> Anthony Giddens – *Sociology – 5<sup>th</sup> edition*, Cambridge UK, 2006, pages 487-488

immigrants change their language, dress, lifestyle and cultural outlooks as part of integrating into a new social order ), the ‘melting pot’ (the traditions of the immigrants are blended with the ones of the pre-existing population to form new, evolving cultural patterns expressed through hybrid forms of cuisine, fashion, music and architecture) and cultural pluralism (the ethnic cultures are given full validity to exist separately, yet participate in the larger society’s economic and political life) or multiculturalism (ethnic groups exist separately and equality)<sup>5</sup>.

### 3. Religion into EU citizens life

The EU citizens are not too attracted by spiritual guidance the Church would offer. While Muslims are striving to attract more and more followers the dominant religion in EU – Christianity fails to adapt to recent times and less and less persons attend to Sunday service, for example. More and more people declare themselves as atheist (don’t believe in the existence of God), agnostic (non spiritual person) or deist (not attracted to any religious aspect)<sup>6</sup>.

Table 5 presents the estimated situation of the non-believers in the EU countries<sup>7</sup> and the official statistics dividing citizens after their religion.

The only think that is common to all EU countries is Christianity, As seen below many citizen don’t care about spirituality and this gives Turkey a little leverage against those who oppose invitation into EU, based on this criteria.

We notice that highly traditional cultures have fewer non-believers and surprisingly many of the formal communist countries have incredible high rate of non-believers, probably as a result of denigration of the religion in the past.

Table 6. The EU citizens’ religious affiliation

	Country	Non-believers (% )	Predominant religions
1	Romania	4	Romanian Orthodox 87%, Protestant 8%, Roman Catholic 5%, Islam and other (2002)
2	Greece	6	Greek Orthodox 98%, Muslim 1.3%, other 0.7%
3	Cyprus	10	Greek Orthodox 78%, Muslim 18%, Maronite, Armenian Apostolic, and other 4%
4	Portugal	10	Roman Catholic 94%, Protestant (1995)
5	Malta	12	Roman Catholic 91%
6	Poland	12	Roman Catholic 95% (about 75% practicing), Eastern Orthodox, Protestant, and other 5%
7	Ireland	14	Roman Catholic 91.6%, Church of Ireland 2.5%, other 5.9% (1998)
8	Italy	19	Roman Catholic approx. 90%, Protestant, Jewish, Islamic
9	Spain	24	Roman Catholic 99%, other 1%
10	Austria	24	Roman Catholic 74%, Protestant 5%, Islam 4%, none 12%
11	Lithuania	27	Roman Catholic 79%, Russian Orthodox 4%, Protestant (including Lutheran, evangelical Christian Baptist) 2%, none 10% (2001)

<sup>5</sup> Anthony Giddens – *Sociology – 5<sup>th</sup> edition*, Cambridge UK, 2006, pages 497-498

<sup>6</sup> Real International Statistics on Religion by Carles Vilar <http://www.religionstatistics.net/statofrel1.htm>

<sup>7</sup> Real International Statistics on Religion by Carles Vilar <http://www.religionstatistics.net/statofrel1.htm>



12	Finland	27	Evangelical Lutheran 89%, Greek Orthodox 1%, none 9%, other 1%
13	Latvia	29	Lutheran, Roman Catholic, Russian Orthodox
14	Belgium	30	Roman Catholic 75%, Protestant or other 25%
15	Slovenia	30	Roman Catholic 68.8%, Uniate Catholic 2%, Lutheran 1%, Muslim 1%, atheist 4.3%, other 22.9%
16	Slovakia	31	Roman Catholic 60.3%, atheist 9.7%, Protestant 8.4%, Orthodox 4.1%, other 17.5%
17	Bulgaria	37	Bulgarian Orthodox 83%, Islam 12%, other Christian 1% (2001)
18	Luxembourg	38	Roman Catholic 87%; Protestant, Jewish, Islamic 13%
19	Netherlands	38	Roman Catholic 31%, Dutch Reformed 13%, Calvinist 7%, Islam 6%, none 41% (2002)
20	Hungary	40	Roman Catholic 67.5%, Calvinist 20%, Lutheran 5%, atheist and other 7.5%
21	Sweden	40	Lutheran 87%, Roman Catholic, Orthodox, Baptist, Muslim, Jewish, Buddhist
22	United Kingdom	40	Christian (Anglican, Roman Catholic, Presbyterian, Methodist) 71.6%, Muslim 2.7%, Hindu 1%, other 1.6%, unspecified or none 23.1% (2001)
23	Denmark	42	Evangelical Lutheran 95%, other Protestant and Roman Catholic 3%, Muslims 2%
24	Czech Republic	45	atheist 39.8%, Roman Catholic 39.2%, Protestant 4.6%, Orthodox 3%, other 13.4%
25	France	50	Roman Catholic 90%, Protestant 2%, Jewish 1%, Muslim (North African workers) 3%, unaffiliated 4%
26	Estonia	52	Estonian 67.9%, Russian 25.6%, Ukrainian 2.1%, Belorussian 1.3%, Finn 0.9%, other 2.2% (2000)
27	Germany	54	Protestant 38%, Roman Catholic 34%, Muslim 1.7%, unaffiliated or other 26.3%

Source: [www.infoplease.com](http://www.infoplease.com) and Real International Statistics on Religion by Carles Vilar  
<http://www.religionstatistics.net/statofrel1.htm>

#### 4. Conclusions

As we can see Europe is not as diverse as one might think as the social indicators show.

EU is trying to implement a multiculturalism model based on equality that will hopefully moderate radicalism's manifestations on one side and meet the immigrants' expectations too. In the same time it is critical for the growth of our community to better manage our existing labor force and create clever policies to attract specialists in top fields of the industries. The wise way to increase immigration would be to attract people from similar cultures.

Even though the ageing of the population is already acknowledged since several decades more policies helping rejuvenate the community are needed.

As a concrete proposal I would like to suggest the implementation of a European program that would allow people from the countries who are rendering movies or shows to listen the original version (subtitled, off course) for let's say 5% of all the imported spectacles.

## References

Anthony Giddens – “*Sociology – 5<sup>th</sup> edition*”, Cambridge, UK, 2006

Alexandra Delcea – “*Remittances and International Migration: Romania in the Context of the European Union* ”  
Bucharest, Paralela 45, 2007

Eurostat 2005 - <http://epp.eurostat.ec.europa.eu>

<http://www.worldfactsandfigures.com/religion.php>

<http://www.religionstatistics.net/statofrel1.htm>

<http://www.infoplease.com/>

Gateway to the European Union <http://europa.eu>

# WAYS TO INTENSIFY THE ROMANIAN PARTICIPATION TO THE EUROPEAN RESEARCH PROGRAMS

DANA BLIDEANU<sup>1</sup>,  
LILIANA GRIGORE<sup>2</sup>

## Abstract

The essential role of the RDI activities in sustaining economic performance and convergence represents a key statement of the revised Lisbon Strategy.

These activities are financed and promoted at European level through large Community Programs and Initiatives.

Romania's active participation to these programs represents at the same time a challenge and an opportunity.

The challenge is generated by the need to reduce the gap with the developed countries of the EU.

Some of the opportunities are: better turning to account of the Romanian scientific and technical potential, better integration into the European Research Area, and not least, more efficient absorption of EU's research funds.

The present paper is aimed to highlight ways to intensify Romania's participation to the European Research Programs.

**Key words:** Knowledge-based economy, European Research Area, Lisbon Strategy, European Framework Programs, national policies of RDI, innovation capacity.

---

<sup>1</sup> Professor Ph.D., Department of International Business and Economics, Academy of Economic Studies, Bucharest, Romania.

<sup>2</sup> Assistant Professor Ph.D., Department of International Business and Economics, Academy of Economic Studies, Bucharest, Romania.

## **The ERA concept and reality**

The topics of the present paper suggest that a short review of the European Research Area concept might be necessary.

In March 2000, the Lisbon European Council defined the goal for the EU to become the “most competitive and dynamic knowledge-based economy in the world by 2010, capable of sustainable economic growth , with more and better jobs and greater social cohesion”.(8)

In order to achieve this goal, the vision of the European Commission to create a European Research Area (ERA) was made the key element of the Lisbon Strategy.

The creation of the ERA is about setting up a genuine European “internal market” for research, to increase pan European co-operation and coordination of national research activities.

The EU has a long tradition of excellence in research and innovation but this excellence is often scattered across the EU, with 80% of public sector research in Europe being conducted at national level, mainly under national and regional research programs. Therefore the scientific and technical potential of the UE are not fully exploited.

To tackle this problem, the Commission proposed in January 2000, the creation of an European Research Area, aimed to contribute to a better integration and organization of Europe’s scientific and technological area and to the creation of better overall framework conditions for research in Europe.(2)

The Commission initiative (2000) for ERA combines 3 concepts;

a) The creation of an “internal market” in research- an area of free movement of knowledge, researchers and technology, with the aim of increasing cooperation , stimulating competition and achieving a better allocation of resources;

b) A restructuring of the European research, in particular by improved coordination of national research activities and policies;

c) The development of a an European research policy that not only addresses the funding of research activities but also takes account of all the relevant aspects of the EU and national policies.

The main developments expected to occur once ERA is established are:

- material resources and facilities optimized at European level;
- more coherent use of public instruments;
- more dynamic private investment;
- a common system of scientific and technical reference for policy implementation;
- more abundant and mobile human resources;
- an attractive environment to researchers and investments;
- a area of shared values.

Seven years after the ERA launch, the Commission ‘s Green Paper “The European Research Area: New perspectives”(April 2007) stated that some progress has been made, but there is still

much further to do to built ERA, particularly to overcome the fragmentation of research activities, programs and policies across Europe.

As detailed in the supporting Commission Working Document for the Green Paper, many actions have been taken to make ERA a reality: (3)

a) The funding of the 7 Research Framework Program has been substantially increased and new initiatives have been launched (The European Research Council, The European Institute of Technology etc);

b) Initiatives have been launched to improve the coordination of research activities and programs. They include the European Technology Platforms, through which industry and other stakeholders develop strategies research agendas in areas of business interest and the ERA-NET scheme which supports the coordination of national and regional R&D programs;

c) Policy coordination through the “open method of coordination” and the use of voluntary guidelines and recommendations.

This process resulted in all Member States setting national R&D investment targets in the context of the overall EU 3% of GDP R&D investment objective and taking measures to improve their research and innovation systems;

d) The adoption of a “broad –based innovation strategy”, which will improve the framework conditions for research and innovation. In this context, a new Community framework for State aid for research and innovation and guidance for a more effective use of tax incentives for R&D were adopted in November 2006; also a European patent strategy is being proposed.

Since the launch of the ERA concept in 2000, major changes have occurred in and outside Europe, three of them being of outstanding importance:

1) The increasing globalization of the knowledge production which raises the question of better access to foreign knowledge and investment.

In 2000 Europe compared itself only to USA and Japan. Countries like China and India or South Asia countries were not mentioned.

Today the main drivers of the internationalization of R&D are the growing S&T capacities of China and India and the expanding global production chains inside MNE’s .

China is one of the world’s largest spenders on R&D ; it produces 3 times more graduates in engineering than the US and has close the same number of full time researchers in all Europe Member States together.(3).

India accounts for almost the same number of engineers as the US and has the largest pool of young university graduates of the world.

2) Since 2000, a sizeable degree of global political consensus has been reached on the approach to take to major global challenges, due to the leadership role played by the EU. Part of this consensus is that S&T has an important role to play;

3) EU enlargement since 2000 has further increased the EU overall R&D capacity but it has also increased the diversity in terms of S&T development gaps, scientific culture and specialization patterns.

The discrepancies between member States in terms of R&D intensities have also grown larger, ranging from 0.4 in Cyprus to 3.86 in Sweden (2005).

It is obvious that, within this changing context, the ERA concept must be subject to gradual changes.

The Green Paper “The European Research Area: New Perspectives” above mentioned raises a number of questions on how to deepen and widen the ERA so that it fully contributes to the revised Lisbon strategy.

### **The Research Framework Programs**

The main financial and legal instruments to implement the ERA are the Research Framework Programs (the first Program was launched in 1984).

They are drawn up and proposed by the Commission and have to be adopted by the Parliament and the Council.

The Framework Programs are instruments based on a competitive approach and they have as main criterion the scientific excellence.

There are no national or regional quotas (in contrast with the Structural Funds).

The FP’s organizes calls for proposals for transnational collaborative research projects linked directly to the research “performers”, without any interference by national or regional governments.

There are frequently situations of countries with low R&D expenditures doing surprisingly good in FP proposals.(12).

The Frame Programs significant impacts on economy and science & technology can be summarized as follows (6):

- Economic benefits (increased turnover and profitability, enhanced productivity and market share);
- Innovative performance(enterprises participating in FP tend to be more innovative, are more likely to patent and engage in innovative cooperation with other firms and universities);
- Scientific performance( more excellence through EU wide competition);
- Human resource development (thousands of researchers have participated in top transnational teams, benefiting from training and knowledge sharing);
- Integration of ERA (better coordination of national efforts, more cooperation links, concentration of research efforts through larger projects with critical mass, ERA becomes more attractive to researchers worldwide).

On April 2005, the Commission adopted the 7th Framework Program (FP 7) following FP 6 (2002-2006).

So far the programs have been designed to last for a period of 4 years.

FP 7 will be synchronized with the duration of the EU’s financial perspective and thus cover the 7 year period 2007-2013.

FP 7 is organized into 4 specific programs, corresponding to 4 major objectives of the European research policy:

1) Cooperation (32,30 bn Euro) refers to gaining leadership in key scientific and technology areas by supporting cooperation between universities, industry, research centers and political authorities across EU and with the rest of the world.

The program consists of 10 thematic research areas;

2) Ideas( 7,46 bn Euro) refers to the establishment of an autonomous European Research Council which will support and stimulate basic research carried out by individual teams competing at the European level;

3) People (4,72 bn Euro) aims at strengthen training, career prospects and mobility of European researchers;

4) Capacities (4,29 bn Euro) means developing and fully exploiting the EU's research capacities through large scale research infrastructure, regional cooperation and innovating SME's.

As compared to FP6 the FP7 Program has some new features:

- Duration extended from 4 to 7 years;
- Budget increased to 54,5 bn Euro compared with 17,6 bn Euro for FP6;
- New structure;
- Flexible funding schemes;
- Joint Technology Initiative;
- Simpler procedures.

### **Romania's participation to the European Research Programs**

The first period of the post-accession to EU is marked by the imperative need for Romania to reduce the existing gap with other member states of the EU.

In this respect, the alignment to the recent policies of the EU in the field of the RDI is of outstanding importance.

These policies are generated by the new frame given by the Lisbon Strategy, according to which science and technology are regarded as key instruments to achieve growing economic performance and ensure long term development

Within this context, the government program for 2005-2008 sets some strategic objectives for the RDI field (7):

- strengthening the role of RDI system in assuring the competitive dimension of the Romanian economy;
- a better correlation between the RDI system and the industrial policy and a more tighten link between the RDI system and the economic environment;
- an increased financial support to the RDI field;
- improving the R&D capacity of specific entities, public authorities and researchers.

As regards the unfolding of international R&D activities, there are several options to follow, namely (14)

- Bilateral cooperation;
- Cooperation through European Programs like EUREKA, ESF., COST.
- Cooperation through the 7 th Frame Program;
- Cooperation through other European Programs and Initiatives (the Program for Competition and Innovation, LIFE etc )
- Cooperation in the frame of some international organizations.

EUREKA is a pan-European network for market-oriented industrial R&D.

Created as an inter-governmental initiative in 1985, EUREKA aims to enhance European competitiveness through its support to business, research centers and universities who carry out pan-European projects.(13)

There are 19 projects in course of execution with Romanian participation.

COST (European Cooperation in the field of Scientific and Technical Research) is the oldest European networking system in research, established in 1971.It consists of 34 members and is trying to bring together research teams from different countries working on specific topics. One of the main characteristics of COST is its flexibility: there are not set-areas for cooperation , but scientists themselves put forward proposals for COST.

A number of 87 cooperation actions are on course with Romanian participation.

ESF (European Science Foundation) aims at promoting European Research Excellence.

Romania is participating through the National Council of Scientific Research in the High Education, which is one of the 75 th member of ESF.

As regards the Framework Programs, the results of Romania's participation to the last Program (FP6) reflect the limited capacity of the Romanian CDI system to face the challenges of the European Research Area. In terms of costs, the contribution of Romania to FP 6 was 65.mil.Euro, out of which 50% were public financing and 50% from Phare sources for Romania.(13).

Within this Program, the Romanian researchers concluded contracts for only 52.mil.Euro.

Romania's participation to the European Research Programs is deeply marked by the vulnerability of the RDI system, which went a difficult period after 1989.

The underinvestment and delayed restructuring permitted only a weak connection to the global trends in science and technology and the still fragile enterprise sector in Romania could not exert a real innovation demand.

Due to chronic underinvestment the number of researchers decreased drastically from 1990 to 2004, while the average age of scientists increased.

The low attractiveness of the research career determined qualitative losses of the human resources and made it extremely difficult to attract top young people into research.

The brain drain phenomena has accentuated due to a set of factors, mainly: low wages in the RDI system, the delayed institutional reform, the poor quality of the research and development



infrastructure, the absence of an evaluation system stimulating and compensating real performance.

With only 2,5 researchers /1000 workforce in 2004, Romania is on the bottom of the European Union hierarchy, outrunning only Malta(1,7) and Cyprus (1,4) but remaining far from other transition countries , for example Poland and Hungary (3,7) (5)

Official European statistics show that the highest level of this indicator is realized by Finland(16,2), Sweden (10,7) and Luxemburg (10,5).

The low funding level had a negative impact on the international cooperation and the participation of Romania to European Research Projects and Networks, disconnecting Romania from the main European research goals and reducing the access to performing products and technologies.

The consequences also refer to the low number of articles in the mainstream scientific publications, low number of citations of the scientific results published by Romanian authors and in the low number of patent applications with Romanian authors.

As regards the last aspect we are witnessing the following paradox: despite the high performance of Romanian participants in the international “fairs” of innovations, the number of patent applications decreased dramatically since 1990.

The Romanian Patents Office statistics show the following evolution of the patent applications from 2001 to 2006:

	2001	2002	2003	2004	2005	2006
Total nr. of applications	1409	1682	1046	1160	1100	1027
Romanians	1128	1477	881	937	916	814
Foreigners	281	205	165	164	68	62

OSIM Annual Report, 2006

The structure of patent applications with respect to the type of applicants is different from the one existing in other developed European countries.(10)

In the European countries, about 70% of the applications originate from companies.

In Romania about 60% of the applications are from individuals, 17% from companies and the rest from universities and research institutes (in the European countries applications from individuals amount to only 20% of the total number of applications). (10)

The universities and research institutes from Romania have a weak activity as regards patent applications, compared with similar entities in the European Union.

The Romanian Patent Office data show that, out of 165 research institutes, 47 have applied in the 1992-2004 period for only one patent, 24 applied for 2 patents. and only 6 institutes ( 4 from the chemical sector and 2 from electric sector) have applied for over 100 patents.

In the higher education area the situation is similar: out of 100 entities, only 27 had patent applications over the same period.

As it is known, universities are key actors both in the European Higher Education Area and in the European Research Area.

Their importance to ERA is illustrated by their share in total research expenditure which is around 22% in Europe- 25 (10% in Romania), compared to 13.5 % in the US and 13.8 % in Japan (2005).

Research active universities are the main producers of scientific knowledge in Europe today, acting as "knowledge creators" and represent an important training ground for researchers.

In Europe, universities employ 36.6% of researchers (2004) compared to around 14.7% in the US and 25.5% in Japan (2003). (3)

Romania is again below the European average, with a share of only 26.6% researchers employed in the higher education but it is worth mentioning that it doubled the share in a short period of time (from 12,4% in 2000).

The insufficient performance of the high education system in Romania is reflected by the absence or the very low positions of the Romanian universities in the different European or international classifications.

Despite the general statement that the European High Education sector is priority focusing on national goals, the commitment of universities to transnational research is growing. This can be seen from the fact that 33% of the FP6 participants (contracts signed in 2005) were higher education institutions. (In Romania the share of higher education institutions participation in FP6 was 24%).

The level of innovative performance of the companies is another aspect with strong impact on international cooperation.

The 4th edition of the European Innovation Scoreboard (nov.2004) classifies firms in 5 categories accounting their innovation activities (4):

A) **Strategic innovators**: for these firms, innovation is a core component of their competitive strategy. They perform R&D on a continuous basis to develop new products or process innovations;

B) **Intermittent innovators**: the firms perform R&D and develop innovations in-house when necessary or favorable, but innovation is not a core strategic activity;

C) **Technology modifiers** : the firms modify their existing products or processes through non-R&D based activities. Many firms in this group are essentially process innovators;

D) **Technology adapters** : the firms primary innovate by adapting technologies developed by other firms or organizations;

E) **Non-innovators**

Romania's situation versus this classification reflects a weak level of innovation, having in view that more than 70% of firms are non-innovative and the share of strategic innovators in the total number of firms is only 3%.

## Ways to intensify the Romanian participation to the European Research Programs

The above subject will be treated based on a SWOT analysis regarding the Romanian RDI system in the context of extending its participation into European Research Programs:

<p><b>Strengths:</b> the existence of a R&amp;D strategy for a medium term (2007-2013), an important creative potential in the category of high studies population, a high degree of adaptation of the young people to new technologies, the existence of poles of excellence in the principal fields of science and technology, the experience gained in the pre- accession period in participating into European consortia projects.</p>	<p><b>Weaknesses:</b> the chronic sub-financing of the National RDI system until the last years, the gap versus other European countries as regards research infrastructure, weak abilities of researchers to start and manage research projects, lack of professional practices in the cooperation direction, low degree of integration between academic and company research, lack of experience in identifying partners in order to promote projects with Romanian coordination.</p>
<p><b>Opportunities:</b> the Lisbon ambitious targets (mainly the total R&amp;D expenditures objective), increased funding for FP7, simplified procedures for FP7, the existence of European networks of excellence facilitating the interaction with partners from other states of EU, significant collaboration opportunities with Romanian researchers working in other countries.</p>	<p><b>Threats :</b> potential new knowledge and technological gaps distancing Romania from other European countries in case of insufficient integration to the European Programs, insufficient absorption of the Community funds compared to the Romanian financial contribution, the brain drain phenomena may accentuate, the predominance of Romanian entities as subcontractors or partners in the European projects and not as project coordination managers.</p>

The SWOT analysis suggests that the ways to enhance Romanian participation to the European Research programs fall into 2 categories: general and specific actions.

The **general actions** derive from the national policies in the R&D domain, aimed to increase the quality and performances of the RDI system, as a mean to respond to the European targets of the Lisbon Strategy.

A large majority of the EU member states, including Romania have a multi annual and strategic approach to R&D offering a stable and predictable environment to an endeavor which is inherently long term in nature.

These members have put in place specific strategies for stimulating both the quantity and quality of the R&D activity.

Common elements of these strategies are : the long term character and the analytical view based on identifying bottlenecks, formulating challenges and matching the portfolio of policy instruments to address these challenges.

In Romania such a strategy was adopted in February 2007, covering the 2007-2013 period.

The strategy is the result of large dialog exercise between the main actors interested in the RDI system, carried out in the 2005-2006 period, to the initiative of the Romanian Authority for Research and Development (13).

The strategy sets down the objectives of the CDI system, offers the ground for the organization of the RDI system and establishes the principal domains for the public investment in R&D and for stimulating the innovation in the next years.

An important instrument to increase performance in research and to change the attitude regarding the access to resources was the **project-based funding by competition**, which was launched in 1995 and was extended in 1999. The evaluation criteria have been more and more directed towards scientific performance proven by the researchers , towards the novelty and credibility of the proposed research topic and towards the institutional ability to provide the appropriate environment and infrastructure needed for establishing and developing strong research groups with international visibility.

As it is known, the volume of financial resources allocated to R&D is an important element determining a country's scientific and innovative performance.

The **public funding** of the Romanian R&D showed a radical change starting with 2005 together with the first substantial increase in GDP share assigned to this field.

The GDP share of public expenditures allocated to R&D was doubled in 2005-2006, with a subsequent increased target of 1% in 2010, but is still low compared with the EU average.

It is worth mentioning that since 2000 not much progress has been made in the EU towards the 3% objective ( GERD/GDP) and the absolute R&D expenditure gap with the US and Japan has not been reduced ( the share GERD/GDP is only 1,85% in EU and 2,70 % in US or 3,20% in Japan), while a similar gap is emerging with a small group of Asian economies (China, Taiwan, Singapore, South Korea). (3)

In terms of R&D intensity , one can distinguish between 3 groups of countries inside the EU: a first group with a R&D intensity above 2,4 GDP (Sweden, Finland, Denmark, Germany an Austria), a second group having an intensity close to the EU average, with values between 1,5 and 2,1% (France, Belgium, Netherlands, UK, Luxemburg) and final, a large group of countries with R&D intensity below 1,5% GDP(with significant differences within the group).(5).

The EU is also making little progress towards the 2/3 objective for business financing of R&D and still lag behind Japan and US ( the share of GERD financed by business is 53% in EU and 63% in US or 75% in Japan).

Although domestic R&D efforts are largely financed by the business enterprise sector in Europe, US and Japan, the role of government in the financing of R&D should not be underestimate.

The level of government – funded R&D intensity is substantial in many high R&D intensive countries ( Nordic countries, Germany, France, Austria, and US) , showing that high private involvement in the funding of R&D does not preclude government funding.

Moreover, in low R&D intensive countries, government - funded R&D is higher than business funded R&D. Government –funding of R&D is critical for creating and developing S&T

capabilities, a prerequisite for catching up with countries at the technological frontier or for supporting projects with high social benefits.

A strong impact on preparing the Romanian R&D Community for the FP7 is expected from the **CEEX Research of Excellence Program** launched in 2005 by the National Authority for Scientific Research (12)

In the CEEEX Program, the priorities of the public R&D funding were those from FP7, and the projects focused on the creation of powerful consortia, the promotion of interdisciplinary research, the development of human resources, the international promotion of the Romanian R&D system. The program provides convergence with the European practices.

**Specific measures** to enhance Romania’s participation in the European Research Programs include:

- 1) Better information systems referring to the European Programs and the extension of external contact points;

It is expected that the Romanian Office for Science and Technology, recently inaugurated in Brussels resolve some of the above problems.

The Office is aimed to promote the participation of Romanian researchers to European Research programs by facilitating the contacts with European institutions and by offering them better knowledge about the Romanian research policy and potential;

- 2) Assuring the synergy of the national programs of research with the thematic areas specific to ERA; the National Program for Research is very close in its thematic structure with FP7;
- 3) Increasing the international visibility of the Romanian R&D system by stimulating the exchange of researchers, experiences and results in the reference scientific and technical domains;
- 4) Organizing scientific manifestations with foreign participations including high personalities in different areas of science;
- 5) The formation of consortia/networks of institutions and organizations with visibility at national level, able to cooperate with similar partners in the European Union;
- 6) The development of scientific equipments at European levels.
- 7) More efforts to improve the researchers ability to initiate and manage the research projects.

As regards point 7) there are several critical ways to change the management practices in R&D activities, according to specific problems (11)

The problem	Old practices	Specific practices for the new economy
Training the project promoters	Focus on the current management of the projects	Focus on developing the abilities to initiate new projects

Promoting new projects	Priority accorded to obtain new projects and to attract funds	Priority accorded to the feasibility of the projects, to carry them in the agreed terms and to obtain the expected results
Responsibility in the project management	Individual responsibility	Collective responsibility
Carrying out the project	Execution along with other activities, current modifications of priorities	Concentrated efforts on the project
Dominant type of management approach	Coordination of individual efforts of the project partners	Facilitating cooperation between the project partners
Capitalization of experience	Accumulation of knowledge on an individual basis	Collective accumulation of knowledge

## Conclusions

After a long period of decline in the Romanian capacity to sustain efficient R&D activities, the accession to the EU brings new opportunities and perspectives.

Romania has fully aligned its R&D national policies in the new frame given by the Lisbon Strategy and the consequences are not only a radical change of public R&D funding but also the restructuring of the R&D system.

This new context is expected to have a strong impact on Romania's participation into the large European Research Programs, with great opportunities for the R&D system and its integration into the European Research Area.

However, specific actions are also required to improve the present management practices and to bring them to the European level.

## References

- Prof. dr. Anton Anton- Starea cercetarii si directii de actiune- o abordare pragmatica; [www.ad-astra.ro/library/papers/anton .pdf](http://www.ad-astra.ro/library/papers/anton.pdf);
- Commission of the European Communities: Green Paper: “The European Research Area-New Perspectives”, Brussels, 4.04.2007;
- Commission Staff Working Document accompanying the Green Paper “The European Research Area”, Brussels.4.04.2007;
- Commission Staff Working Paper, “European Comparative Analysis of Innovation Performance” Brussels, 19.11.2004 ;
- Commission of the European Communities, “Annual Report on Research and Technological Development Activities of the EU in 2006”Brussels, 13.09.2007,[www.eu.int/ueDocs](http://www.eu.int/ueDocs);
- Commission of the European Communities, “Towards the 7 th Framework Program”, Brussels, 2005.[www.eu.int/ueDocs](http://www.eu.int/ueDocs);
- Document de politici publice sectoriale pentru fundamentarea propunerilor de buget pe anul 2007 Ministerul Educatiei si Cercetarii, Autoritatea Nationala pentru Cercetare Stiintifica, martie 2006;
- European Council, Lisbon, 22-24 March 2000, Presidency Conclusions- [www.eu.int/ueDocs/cms](http://www.eu.int/ueDocs/cms);
- Filip, F.G, H.Dragomirescu : “Problema cunoasterii in Romania. Reflectii in context european” in I.Gh.Rosca (coord) ”Societatea cunoasterii”, Editura Economica, Buc.2006, p17-30
- Oficiu de Stat pentru Inventii si marci – Raport anual 2006, [www.osim.ro](http://www.osim.ro)
- I.Gh. Rosca, H.Dragomirescu, “ Societatea cunoasterii- orizontul european si vocatia romaneasca”, in C.Angelescu (coord)- “Aderarea Romaniei la Uniunea Europeana. Batalia cu timpul” Editura Economica, 2004, p356-363
- Report from the Danish Institute for Studies in Research, 2003, [www.atsk.an.dk](http://www.atsk.an.dk)
- Strategia Nationala in domeniul Cercetarii Dezvoltarii si Inovarii pentru perioada 2007-2013, Guvernul Romaniei, martie 2006, Ministerul Educatiei si Cercetarii
- [www.ancs.ro/programe internationale](http://www.ancs.ro/programe_internationale)

# **KNOWLEDGE-DRIVEN ECONOMY AND KNOWLEDGE WORKERS: POLISH EXPERIENCE IN THE INTEGRATING EUROPE.**

**BARTOSZ SURAWSKI<sup>1</sup>**

## **Abstract**

The article presents Poland's position along the way to the knowledge-driven economy. Starting with criteria for a knowledge economy, it analyses Poland's position in comparison to the rest of the EU, and to world leaders. It explains the features and requirements of knowledge workers as a vital group of employees, and proceeds to show their proportion and composition within economies of world leaders and the Polish economy. Further, it presents factors in the labor market, which threaten the development of knowledge workers in Poland. Analysis shows, that Poland has made impressive progress since 1989, but is now at most a developed industrial country, with good prospects, but only at the doorstep of transition to a true knowledge economy.

---

<sup>1</sup> Business and Administration School in Gdynia, Poland



## 1. Introduction

To be named a 'knowledge economy' is surely a compliment. It automatically places an economy among the world leaders and hopefuls. It implies high level of development, fast progress, high standard of living. In OECD's report "A new economy? The changing role of innovation and information technology in growth" (2000) we read, that knowledge is the most important endogenic factor of production and the most important input into the engine of capitalism. Intangible assets and non-material factors of development (among them notably knowledge) grow in importance: research shows, that the material factors can only explain a half of the differences in the level of economic development (L.Ziemkowski (ed.), 2003). To be counted among knowledge-based economies makes attracting foreign investment and international trade easier. On the other hand, not joining the knowledge-based economies is a threat of building an unbridgeable gap and becoming a permanent periphery of the developed world. Is it possible to bridge such a gap in just 20 years? Can a country, which just 20 years ago shed the burden of half a century of communist utopia, and since then has been going through permanent transformation, to catch up with the world leaders?

Poland is a middle-size country, the 6<sup>th</sup> largest in the E.U., with 38,2 mln inhabitants. In the last four years, the economic growth averaged 4,65%, reached 6,2 in 2006, and is expected to exceed that result in 2007. Dynamic development is attributable to the accession to the E.U. in 2004, and the results of a fundamental re-structuring of the economy in the 90s and the new, modern branches of economy reaching international level of competitiveness. GDP is 605,4 bln USD (1698,3 bln zł), which gives 15 890 USD (44 490 zł) per capita. In Purchasing Power Parity, GDP is 631,8 bln. USD (1771,7 bln. zł), and 16 600 USD (46 550 zł) per capita. The level of development is middle-high (HDI index = 0,862 (37°), 2006). Agriculture contributes 2,8% to GDP, manufacturing – 31,7%, and services – 65,5%. The country is expected to develop fast, aided partly by E.U. structural funds, which will bring additional € 61 bln to its economy in the years 2007-2013. When one recalls the state of the country in 1989, the success of the transformation seems dazzling. But is it sustainable? Jumping to the world's first league requires structural changes from an industrial economy to a service and knowledge-based economy. Can Poland join one of the centres of the world economy, or will it remain just a decent suburb? Is Polish economy knowledge-based, or at least moving in that direction?

## 2. What makes a knowledge-based economy?

To characterise Poland's evolution, it is necessary first to comment on the meaning of, and the criteria defining the 'knowledge economy'.

First of all, we should remember about two ways of understanding knowledge: broadly defined, knowledge is a set of information, opinions and beliefs, to which we attribute cognitive or practical value. In the narrower sense, knowledge is interpreted as scientific knowledge. Talking about the connection between knowledge and the economy, we tend to think about the narrow definition – which may exclude the all-important cultural foundation (beliefs, values, mentality) for economic success.

The term 'knowledge economy', as the most concise, is in common use. To convey its meaning better, though, we can use the term 'knowledge-driven economy'. In such an economy, knowledge (expenditure for, and capital of knowledge), as a factor determining the rate of economic growth and the level of economic development, becomes more important,

than the expenditure for and the accumulated level of, physical capital (L.Ziemkowski (ed.), 2003).

Therefore an economy may be said to be a 'knowledge-driven economy', if the correlation between economic growth and investment in knowledge is stronger, than the correlation with capital investment. By knowledge capital we can understand knowledge accumulated within a society (and measure it for example through the level of education or the past expenditure necessary to educate citizens to the present level). The annual expenditure or investment in knowledge is easier to identify and can have more measures. There are many versions and opinions on the subject of what the indices of a knowledge economy should be: e.g. Whether to take into account the yearly expenditure for computer software? Or to measure expenditure for primary education? Or expenditure for adult learning and business training? Here are two proposed sets of features, which should single out knowledge economies (A.Kukliński (ed.), 2003):

1. The share of employees with higher education in the working population,
2. GDP per capita
3. R&D expenditure
4. The share of the service sektor in GDP
5. Falling physical weight of GDP
6. Frequency of profession change within working life
7. Innovative attitude (e.g. number of patents)
8. Openness to international trade (e.g. share of exports in GDP)
9. Access to information (level of IT saturation)
10. Cross-cultural cooperation

Another set of key criteria names six indices (L.Ziemkowski (ed.), 2003):

GERD	gross expenditure for research and development (% GDP),
ICT	expenditure for information and communication technology (% GDP),
EPO	number of patent applications to the European Patent Office (per 1 mln. inhabitants)
INT	internet access (percentage of inhabitants)
EDU	percentage of people with higher education in the working population
EXP	share of high-tech exports in total exports

### **3. Does Poland meet the criteria of a knowledge economy?**

The level of education of the workforce was placed first on the OECD's list. The minimum level for a knowledge economy is suggested as 20%, and is reached by countries such as USA, the Netherlands, Sweden, Finland or Japan. Poland seems to be doing surprisingly well in that respect, noting in 2004, 20,9% people with a Master's diploma or higher, and 6,1% with a Bachelor or Engineer – 27,0% in total (PCSO, 2006), However, the sample for this calculation did not include individual farmers and the self-employed. But even including them, the criteria is met.

A knowledge economy provides high incomes to citizens. The suggested threshold is 20 000 USD in PPP. Only about 25 countries reach that level. Poland, with 16 600 USD, has not reached it, but Over the past years has made a quick progress towards it. In 2005, income per capita reached 50% of the EU's average (11 700 EUR versus 23 400 EUR for EU), which still places Poland at the end of the new EU members.

Incomes may be rising, but Poland is far from being a research centre. If we consider knowledge the main engine of capitalism, expenditure for research and development should exceed 2% of GDP. All leading countries devote much more. At the end of the 90s the OECD average was 2,2%, and 1,8% for EU – but that level was achieved thanks to the richest: Japan (3,0%), USA (2,7%), Sweden (3,9%) or Finland (3,2%). Poland at the time spent just 0,7% of GDP. In the 00s the situation has hardly changed, with leaders moving up by 0,1, and Poland – falling by 0,1.

Economic development has lead to major changes in the structure of GDP. In the past, agriculture and mining were most important, then manufacturing took over, and now the service sector produces majority of GDP. The borderline is 65%, and most developed countries reach and pass it. The trend is followed by less affluent countries, as well. Poland moved from 60% in the 90s, to 65,5% in 2006. It must be remembered, though, that high share of services is not always an advantage, and may well indicate underdevelopment of the first two sectors. High share of services is justified, when GDP per capita is over 12-15 th. USD. Under that line it usually means, that an economy cannot produce enough material goods to accomodate for the basic needs of its citizens. Poland fell into that category in the 90s, but has successfully revived production since then.

Physical weight of GDP is an interesting indicator. With the rising share of services, the total physical weight of GDP should rise slower. In the past, the higher was the output, the more it weighed. It induced transportation, storage facilities, road-building. But with the technological progress, miniaturisation, conservation of natural resources and environmental protection, the relationship weakened. Since the World War II, the GDP of USA has risen 5 times, but the weight of it – just 3 times. The process is also associated with the freer movement of economic growth-poles and centres of business.

Development of knowledge, and its influence on economies, bring about two important consequences: product life-cycle shortens, and employees are forced to change professions more frequently. It enforces lifelong learning and intellectual flexibility. It is estimated, that over 17 years, 50% of workposts in Poland have either been transformed, or liquidated. It seems that the necessity of a radical economic transformation has succesfully enforced a major attitude change.

If knowledge is a genuinely leading growth factor , it should be reflected in the innovative activity – and in the number of patents. This indicator may be misleading, though. Firstly, within the EU, it is measured by the number of patent applications to the European Patent Office. This requires innovators in many countries to change from their national patent offices to EPO. Secondly, due to the pace of technological progress, patents may not be the best way of protecting intellectual property, since they devalue faster than it takes to patent an invention. Also, there are more and more innovative solutions, which are difficult to patent, such as organisational solutions or business models. Thirdly, multinationals, whose employees develop new products in countries such as Poland, patent them from their headquarters, thus obscuring the actual distribution of innovative activity. Poland's performance in patent applications is dismally small, even if we take into account the three mentioned factors. In 2002, the EU's average was 134,7 patents per one million inhabitants,

the leading countries reaching 300 (Finland – 306,6, Germany – 297,4, Sweden – 294), and Poland at the bottom with just 4,7.

Poland has become a truly open economy, though. It has integrated well into the economy of the European Union, and making progress in the world markets. Globalisation is one of the main mechanisms of knowledge transfer. But it also means, that a knowledge-based economy must be open to outside influence and international competition. Openness enforces constant development of competitive strengths and acceptance of international models and rules, often at the expense of domestic ones. The share of exports in GDP is 34%, but in that, 77,2% of exports are to the EU-countries. Other directions of exports, such as USA, Eastern Europe and Japan, are slowly developed.

Open societies and open economies experience a revolution in the supply of information, mainly thanks to the development of information technology and infrastructure. A knowledge economy must be characterised by broad access to information within the whole society – not just within the leading groups. A good indicator of that is the level of internet access of households. In this respect, discrepancies between countries are large, but the situation is very dynamic, with some countries ‘exploding’ their internet access over just a few years. The most advanced countries, such as Sweden, Finland or the Netherlands, passing 70%. EU’s average is ca. 50% in 2006, and Poland has reached 35%, or 70% of the average, and displaying high dynamics: in 2000, internet access was only 10%. Still, Poland is trailing behind smaller countries, like Estonia or Slovenia, which have already passed the EU’s average).

Knowledge-driven economy is a product of cooperation of business people and researchers, coming from different countries and cultures. It leads to cultural changes such as limiting particularism, and promotion of communication and collaboration. Cross-cultural cooperation is hard to measure with indicators. In the last years, Polish economy and society were subjected to internationalisation and the influence of other cultures. Some factors were: Poland’s integration into the EU, sharp rise in inward and outward tourism, increased access to information about the world, emigration of Poles to EU countries, major foreign investment in Poland and bringing multinational business culture and foreign employees to Poland. Poland has almost no significant ethnic and national minorities, and has not been recently exposed to inward migration, but on the other hand, sharing essentially the same culture base with western European societies, it experienced the ease of working with business partners in EU (again, as also shown by the example of Poles so easily settling in the UK).

Summarising, Poland meets about a half of the criteria for a knowledge economy, and part of other indices move in a desirable direction.

We can also analyse Poland’s position along the way to a knowledge economy according to the second set of criteria: GERD, ICT, EPO, INT, EDU and EXP.

The level of GERD was already mentioned above Poland spends just 31% of EU’s average on research and development. There is a positive correlation between economic growth and expenditure on R&D – and especially private (business) expenditure. EU’s average shows the dominance of business expenditure in GERD, with 1,22% of GDP (2004). Government contributes 0,24%, and education - 0,41%. This proportion hardly changed from 2000 to 2004. On average, business contributes 65% of annual R&D expenditure. In case of the leading countries: Sweden, Finland, Denmark and Germany, the corresponding share is 70%, and in Sweden – even 74%. Japan and USA note still higher shares – 75% and 78% respectively. In Poland, this share was 28% in 2004, and it is even lower than previously – 0,17% of GDP in 2004 compared with 0,24 in 2000. As we see, Poland’s economy is not driven by its own business-oriented research. There may be an interesting analogy with the

situation of Ireland in the 90s. There, the level of R&D expenditure compared to GDP was low, and the share of high-tech exports was high. The reason might have been, that Ireland based its high-tech exports not on its own research, but on technology brought from USA. A similar situation may now be seen in Poland, where multinationals place their manufacturing plants to sell production in EU, but bring with them technological solutions and high-tech half-products developed elsewhere.

Poland may not be able to produce a working R&D sector for many years. Brown and Duguit (2000) remind us, that to obtain knowledge, information has to be put into practice. This shows a threat to economies relying on imported technology: they not only do not possess R&D facilities, but are not efficient in producing researchers, because universities can transfer information, but graduates have little opportunity to change it into valuable knowledge through practice. A few multinationals have started to move their R&D centres to Poland, headed by Intel's research centre in Cracow, but the trend has yet to change.

But Ziemkowski claims, that the knowledge capital of a society is determined chiefly by good education – the ability to circulate now freely accessible knowledge within the society, and not necessarily to produce new knowledge. A country does not have to be a major R&D centre to possess a high knowledge potential. Indeed, in education Poland is doing much better.

In IT expenditure, Poland's situation is slightly better: in 2004 it spent 2,0% of GDP on IT, compared to the EU average of 3,0% (67% of it). The leading countries spend ca. twice as much relative to GDP: Sweden – 4,3%, UK – 4,2%, Finland – 3,8%. And EU's distance to USA is significant here – USA spends 4,7% of GDP on information technology.

By comparison, expenditure on telecommunications can be highly surprising. In 2004, EU's average was ca. 3,2% of GDP per annum, and the value for Poland was 5,1% - 160% of the average. More surprising still, are the leaders: Bulgaria with 7,0%, Estonia with 6,3%, and Latvia with 5,3%. The most advanced economies, Sweden and Finland, note 4,3% and 3,3% respectively. The reason behind that is the huge deficit in communication infrastructure in the new EU countries. Consequently, money is being poured into, most of all, mobile phone networks, but also into landlines, satellite and other modes of communication. The values of EPO and INT were described earlier.

Poland's expenditure on education is also above EU's average. In 2003, it was 6,3% of GDP, or 115% of EU average (5,5%). It is still behind EU's leaders: Denmark: 7,0%, and Sweden: 6,8%. The development of private higher education is shown by a sizable (0,7%) share of private education expenditure, compared to e.g. Sweden's 0,2%. Since 1994, Poland has been experiencing a boom in higher education. The number of students in 2004 was 2,04 mln., and increased by 30% compared to 2000, and virtually doubled, compared to 1990. Germany, a country of 90 mln., had only 300 th. more students. There are over 500 institutions of higher education – most of them small and medium private colleges established after 1991.

Poland displays high demand for education and new qualifications, and at least half of students are part time (extra-mural), who work, have their own families, and are often in their 30s, 40s or 50s. This boom is due to market's requirements – a diploma has suddenly become the norm. This has also forcibly transformed Poland into a country, where the need for constant, life-long learning is considered obvious. This is aided by wide promotion of skills' development by the wave of EU-subsidised training courses and post-graduate programmes of 2004-06. It can be suspected, that 'the seed fell on fertile ground': the value of education and competence is highly regarded in the Polish society (as opinion polls consistently show). The mass character of higher education, however, leads to lower quality. An example of that is the

rush for Management programmes and the consequent ‘overproduction’ of graduates, who cannot find proper employment.

An idea of the level of primary and secondary education is given by the results of the PISA study. In 2003, Polish pupils were ranked 24<sup>th</sup> in maths, 16<sup>th</sup> in reading comprehension, 19<sup>th</sup> in science and 25<sup>th</sup> in problem-solving. The results are within the OECD’s average – worse than Finland, the Netherlands or South Korea, but better than USA, Italy, Spain or Russia. The results improved significantly in comparison with the 2000 edition.

The level of exports and the degree of openness of the Polish economy, were mentioned earlier. It is worth noting, though, that Poland still has a deficit in the trade of goods (71,9 bln EUR of exports and 81,2 of imports), but has reached a small surplus in the trade of services (10,8 bln. EUR of exports to 10,0 of imports). Poland has been receiving major foreign direct investment, coming 7<sup>th</sup> in the world last year, with 8,5 bln. USD in 2005, and over 10,0 in 2006, resulting in 31 th. new workplaces. Foreign investment, largely by major multinationals, is bringing new and valuable knowledge to the Polish economy. But Poland is still perceived as a location for manufacturing and simple services. According to the ranking of investment attractiveness by Ernst&Young, Poland is ranked 7<sup>th</sup> most attractive country. It comes highest in locating manufacturing – second only to China. It is 5<sup>th</sup> in the service centre category, but falls out of the top ten, when it comes to where to locate an R&D plant or the company’s headquarters – company units with highest added value and requiring mostly knowledge workers.

Summarising the six criteria, Poland is not close to leadership in any of them. It reaches the EU average in ICT and EDU. Poland’s economy is not close to a knowledge economy. But when we compare indices with the level of GDP, it has improved significantly over the past few years. In 1999, it did not reach EU averages in any criteria, and the mean was around 40% of EU – the same as GDP. Now GDP is 50% of the EU average, but four indices are above that. When we take three main pillars of a knowledge economy: innovation system, education, and IT and communication system, Poland is doing well in education, catching up in ICT, but far behind in knowledge creation. There is still much to be done to stop world leaders (USA, Japan, Sweden or Finland) from running away, let alone to narrow the gap.

#### **4. Who are knowledge workers?**

If an economy is to be knowledge driven, knowledge workers are the group of employees to drive it. Peter Drucker is most frequently considered the author of this term, and its greatest promoter. He first described the ‘knowledge worker’ in “Landmarks of tomorrow” (Drucker, 1959). He wrote, that in the 20<sup>th</sup> century the great challenge to those managing the economy would be to increase the efficiency of knowledge-based work, as in the 19<sup>th</sup> century the challenge was increasing the efficiency of physical work.

Productivity of knowledge workers may not be the only factor of global competitiveness, but most probably the deciding one – at least in the majority of industries of developed economies. It is worthwhile to pursue a rise in the efficiency of the most costly and most growth-inducing part of the working population. In many countries this group decides the size of economic growth. As less skilled work may be moved elsewhere, efficiency of knowledge work is vital to the survival of developed economies. What are the features of knowledge workers? What are their expectations and requirements? How many are there?

Drucker noticed a new group of workers entering businesses in the 50s – professional university graduates, such as engineers, researchers, lawyers, psychologists, who did not fit or obey the ‘command and control’ scheme. Terms alternative to ‘knowledge workers’ were professionals or specialists. They were a narrow group at the beginning. Now it can be said, that knowledge is increasingly necessary in any type of work – also in physical or simple service jobs. In manufacturing, work either becomes robotised, or requires more technical knowledge. Drucker says: "Knowledge results when the intellect (the capacity to think) does purposeful work using data and information, It affects all levels and functions in organizations. Every individual is now a knowledge worker." But the fact, that more and more jobs require theoretical background, does not mean, that everyone is a knowledge worker. Where to draw the line, then?

As usual, definitions try to enclose a complex term in one sentence, and convey part of the meaning. Authors underline knowledge attained through education and experience, engagement in knowledge processes, cognitive role of learning and developing knowledge through different transformations, and the aspect of value creation. Examples are:

“Knowledge workers represent a high level of specialised knowledge, education or experience, and creation, transfer, distribution and practical use of knowledge are among the most important objectives of their work.” (Davenport, 2006)

“People who enrich given information and who learn from the information that is communicated.” (Hayman, Elliman, 2000)

“A person, who produces value, using his/her mind and not hands, through creativity, analysing, synthetising, making judgements etc.” (Horibe, 1999)

Knowledge workers have more interesting features, some of which should be mentioned to help distinguish them within the workforce:

- They own the means of production (brains with knowledge), which cannot be owned by employers. They create and own most of the intangible assets of companies (Propst, Raub, Romhardt, 2000), They resist capturing their unique knowledge by companies (Easterby-Smith, Lyles, 2006),
- They are among the highest earners, and through e.g. pension and investment funds – they may own their employers,
- They can mainly be found in the ‘middle-class’ – they form the backbone of that social group. Many, due to the wise commercial use of their intellect, form the higher class. Those in the public sector (teachers, doctors, civil servants) may economically belong to the lower class, but always mentally aspire to a higher status. Knowledge-related professions are among the most highly regarded, and are by themselves sources of status.
- Many of them are self-employed, work irregularly, on contracts with different companies, do not progress within one company, but build their own brand in the labour/B2B market (Easterby-Smith, Lyles, 2006),
- They can be more loyal to their profession, than to their company, and to themselves than to their profession (Easterby-Smith, Lyles, 2006),
- There are whole professions, the core of which is knowledge work,
- Their brain, not their physical abilities, is their main working tool. Their main effort is the intellectual. (Davenport, 2006),

- They must understand, command, maintain and develop a large body of knowledge (Pinchot, Pinchot, in: Myers (ed.), 1996),
- They know more about their specific field than their superiors (Knight, 2002),
- Knowledge work is rarely routinised – its content rarely stays the same for long. It is largely associated with problem-solving, and the problems solved change with time. K-workers are able to undertake major, complicated tasks and resolve complex problems,
- Knowledge work is irregular, does not fit in regular working hours, is invisible, less structured, than manufacturing or administrative work, cannot be made more efficient by standardisation, is hard to control. It is harder to measure – its results may become apparent with much delay,
- Knowledge workers resist close control and instruction, must have flexibility and freedom, are independent and demanding, Many are hesitant of climbing the management ladder, preferring positions of specialists/experts,
- They are highly mobile and, given appropriate technical support, can work remotely – working hours and workplace change meaning
- They cannot produce much value alone – they require teamwork and dialogue (Pinchot, Pinchot, in: Myers (ed.), 1996), They are humanists, with higher social awareness, they value belonging to a community, social climate and relationships based on trust, negotiations rather than conflicts (Von Krogh, Ichijo, Nonaka, 2000),
- They rely on communication and maintain networks of contacts. They are computer-literate and proficient at using ICT,
- They need to UNDERSTAND the information they pass, not just transfer it (Seely Brown, Duguid, 2002),

The last element brings us to an important question: who are NOT knowledge workers? It is easier with manual work – but what about service work? Is a man in a call-centre a knowledge worker? Is office work synonymous with knowledge work? As Seely Brown and Duguid (2002) point out, it is not sufficient to work with information to be a knowledge worker. Businesses increasingly need not more and more information, but more and more people to understand it – more intelligence. Therefore while trying to approximate the proportion of knowledge workers within an economy, it is important to distinguish between those, who just need to handle information in their work, and those who need to understand it to be able to use it! Knowledge must be understood, information can just be held. Thus the distinction between information workers and knowledge workers. And between information economy and knowledge economy: the first shows a marked indifference to people. In that, it is similar to the older industrial economy. It threatens to use people as interchangeable processors. Therefore, another, deeper feature of the knowledge economy is the renewed focus on people, both as employees and as customers and stakeholders. So, we should also remember, that even workers in seemingly non-knowledge positions solve problems, notice relationships, and may have insightful and innovative ideas (Ch.Evans, 2002).

What are the requirements of knowledge workers for efficient work?

- They prefer thinking-friendly environments, are demanding of their work environment, appreciate higher standard of living, often move to the countryside or to regions and countries with higher general living standards. But money motivation is secondary for them – there are more important motivators. Money motivators may even discourage.



- They require opportunities to broaden their knowledge and gather new experience, opportunities for horizontal promotion – career as experts, wider responsibility, more resources, more freedom to choose new tasks,
- They want to work with other talented professionals, guided by expert mentors, to work in a community of practice, maintaining certain standards, group norms and values,
- True motivators for knowledge workers are being recognized and appreciated for their thinking. They must get credit for their achievements. They also require a stage, a forum, a social space to present and exchange ideas (Bukowitz, Williams, 2000).
- They want to take part in decision-making, to be heard and express own opinions. They need to be evaluated and have access to feedback on their results to be able to exercise effective self-control,
- They require flexible organisations, task-orientation, teamwork and democratic style of work and management,
- They require good ICT infrastructure, which allows them to freely access information, organise and process their knowledge, and freely communicate with others (Easterby-Smith, Lyles, 2006),

Thomas Davenport (2006) divides their needs into two groups:

- Need of autonomy – they are weary of obeying orders, think for themselves, work on their own, so their relation with managers must be based on trust; they are able to manage and organise their own effort; they receive the goal, choose the best way, and rarely can describe the way they work.
- Need to be engaged – emotional or intellectual engagement condition knowledge assimilation and development; efficient knowledge work is impossible without engagement – and that is impossible without trust and proper resources.

Knowledge workers assume certain functions and positions within organisations. Managers can be assumed to be knowledge workers, as can specialists or experts within the organisation. Large organisations evolve their own teams responsible for more efficient knowledge work. Applehans, Glove and Laugero (1999) name three functions, which can be assumed by knowledge workers within organisations:

1. Knowledge Officers – high-level executives who set the strategic directions for knowledge.
2. Knowledge Analysts – individuals charged with the specific knowledge-packaging efforts of identifying information needs and delivering appropriate knowledge, based on the strategic direction set by the knowledge officers.
3. Knowledge Authors – front-line providers of information, who Handle the day-to-day publishing as well as monitoring of information in their particular areas of expertise.

The next task is to identify knowledge workers in the economy and try to count them. If we wanted to name professions, which make up the group of knowledge workers, the list would be too long. Identifying them by professions, it is better to use main professional groups – which will be done below. We could also try to identify ‘knowledge industries’, such as high-tech manufacturing or high-knowledge services. But they also employ non-knowledge workers. And in any industry we can find knowledge-intensive companies. They come in two groups: the leaders, who dominate the market and lead by innovation, and start-ups, who enter the market with innovating ideas – often spin-offs of research or academic activity. Both seek their competitive advantage in knowing more than their competitors.

## **5. Knowledge workers in the world**

Due to a lack of an unequivocal and precise definition of a knowledge worker, it is impossible to precisely calculate their numbers in various countries. Regardless of the definition, though, it is undoubtful, that the biggest number of them are found in the most developed economies of USA, Europe and Japan. In the USA, they form – according to estimates – from 25 to 50 % of the working population (Davenport, 2006). Already in 1958, Fritz Mahlup, an American economist, judged knowledge workers to be one-third of the workforce. American Bureau of Labor Statistics (BLS) does not classify knowledge workers as a separate group, but their number can be discerned by putting together several categories of employees, which are used in BLS statistics. Davenport includes such categories, as: management, business and financial operations, information technology and mathematical disciplines, architecture and engineering, empirical and social sciences, law, medicine and health care, social services, education, training and librarianship, art, design, entertainment and sport, media.

In USA, about 36 mln. people, or 28% of employees, belong to these categories. As said, this classification is not exact: in the group so defined, we find professional sportsmen. But a great majority within these categories earn their living by thinking. Eubin and Huber, who applied less rigorous criteria (including e.g. public administration), counted 45 mln. knowledge workers as early as in 1980. Maybe the best measure is the number of managers, free vocations and technical specialists – who in 2003 composed about 34% of the working population. Another approach to estimation is to count the number of people with qualifications allowing them to perform knowledge work. In USA, about 25% of the employed are able to process highly or moderately complex information in mathematical or verbal form, and transform this information into knowledge. Applying still another set of criteria, Marc Porat calculated in 1977, that knowledge workers compose about 50% of all employed, and the sum of their earnings was higher, than that of the rest.

In Canada, knowledge workers comprise managers, free vocations and technical specialists, whoc comprised 25% of the working population in 2001, and only 11% in 1971. In the UK, research carried out on 28 mln. workposts showed, that 32% of them involved knowledge-based work and required at least a Bachelor degree.

## **6. Knowledge workers in Poland**

Now it is time to estimate the number of knowledge workers in Poland. We shall start with the narrowest estimate – professional researchers. Researchers are professionals engaged in the conception or creation of new knowledge, products, processes, methods and systems, and in the management of the projects concerned, in business enterprises, government, higher education, and private non-profit organisations. According to Eurostat, in 2004, there were 61 th. professional researchers in Poland. This is 0,42% of the working population in Poland, and exactly 5,00% of the total number of researchers in EU – which is better than expected, looking at the GERD index. In 1994 there were 47 th. researchers – a rise of 30% in 10 years, compared to 35% for EU in the same period. Unfortunately, at least 70% of Polish researchers work at universities – their number in businesses is almost negligible. In EU, the proportion of researchers in the working population is 1,2%, with a half of them in the business sector. The leaders – as usual – Finland (2,8%, 1,5% of that in business), Sweden (2,2%) and Germany (2,1%).

We can add to that the prospective researchers – the number of Ph.D. students. In 2004, there were 32 054 Ph.D. students in Poland, 35,7% of which were in empirical sciences and technology. They made up 8,00% of all Ph.D. students in EU (in EU, 37,7% of students are in empirical sciences and technology).

An indicator, that much more closely reflects the proportion of knowledge workers within the economy, is the HRST index. Human resources in science and technology is the percentage of the total labour force in the age group 25-64, that is classified as HRST, i.e. having either successfully completed an education at the third level in an S&T field of study or is employed in an occupation where such an education is normally required. For EU, the index was 29,2% in 2004. Poland is not far from that average, with 25,0%. But the leading countries are far ahead, with 39,9% for Sweden, 38,2 for Finland and 38,0 for Denmark. The 15% difference is a gap, which seems unbridgeable at least for one generation.

A different approach to approximating the proportion of knowledge workers is to count persons working in high- and medium-high-technology manufacturing and knowledge-intensive services. Such calculation includes all employes (even unskilled) in these industries, and excludes e.g. managers in other industries. Proportion of workers in these industries is presented in Table 1:

Table 1. Proportion of persons working in high- and medium-high-technology manufacturing and knowledge-intensive service sectors in Poland and EU.

	Employment in high- and medium-high-technology manufacturing			Employment in knowledge-intensive services		
	1995	2000	2004	1995	2000	2004
Poland	-	-	4.4	-	-	24.3
EU-25	-	5.8	5.7	-	29.2	33.1
Sweden	6.0	6.4	6.0	44.2	45.7	47.0
Denmark	6.1	5.4	5.0	39.0	42.1	42.3
United Kingdom	6.0	5.8	4.6	36.8	39.7	42.1
Finland	5.2	5.3	4.9	37.3	37.9	40.3
Netherlands	3.8	3.5	2.6	36.7	39.2	41.0
Germany	9.2	9.3	9.4	26.9	30.4	33.4
Ireland	4.3	3.5	3.8	29.2	31.7	33.4

Source: based on *Europe in figures. Eurostat yearbook 2006-07*, Eurostat 2007,

Data available for Poland, for 2004, shows, that 27,7% of the working population can be considered knowledge workers – compared to HRST of 25,0%. The EU average was 38,8%, and European leaders exceeded 45%, with Sweden reaching 53,0%. Here Poland reached just 71,4% of EU's average, while in HRST – 85,6%.

Polish Central Statistical Office publishes data on employment in different groups of professions. Table 2 shows employment in 2004, in two groups, which may be considered to comprise knowledge workers.

Table 2. Two main groups of knowledge workers in Poland, in 2004.

	Total	Public sector	Private sector
<b>RESEARCHED WORKPOSTS</b>	<b>6213,8</b>	<b>2725,1</b>	<b>3488,7</b>
<b>1. MEMBERS OF PARLIAMENT, HIGHER OFFICIALS AND MANAGERS</b>	<b>390,7</b>	<b>153,5</b>	<b>237,2</b>
in %	6,3	5,6	6,8
MANAGERS OF LARGE AND MEDIUM ORGANISATIONS	380,1	144,8	235,3
in %	6,2	5,3	6,8
General managers, executive managers and their deputies	123,3	48,2	75,1
Managers of internal organisational units in core activity	93,9	30,4	63,5
Managers of other internal organisational units	163,0	66,3	96,7
MANAGERS OF SMALL ENTERPRISES	1,5	0,4	1,1
in %	0,0	0,0	0,0
<b>2. SPECIALISTS</b>	<b>1220,8</b>	<b>873,7</b>	<b>347,1</b>
in %	19,6	32,0	9,9
SPECIALISTS IN PHYSICAL, MATHEMATICAL AND TECHNICAL SCIENCES	169,6	68,2	101,4
in %	2,7	2,5	2,9
Physicians, chemists and associated specialists	8,4	6,9	1,5
Mathematicians, statisticians and associated specialists	3,3	3,2	0,1
Information technology specialists	46,8	14,3	32,5
Engineers and associated specialists	111,2	43,9	67,3
SPECIALISTS IN NATURAL SCIENCES AND HEALTH CARE	113,1	93,5	19,6
in %	1,8	3,4	0,6
Specialists of biological sciences	7,3	7,0	0,3
Specialists of agriculture and forestry	15,1	12,7	2,4
Health care specialists (without nursing)	75,6	60,4	15,2
Nursing specialists	14,9	13,3	1,6
SPECIALISTS IN EDUCATION	552,7	532,3	20,4
in %	8,9	19,5	0,6
Teachers in higher education	81,9	69,3	12,6
Teachers of gymnasium and post-gymnasium schools	201,2	197,9	3,3
Teachers of primary schools and nurseries	204,1	201,2	2,9
Teachers of special schools	15,5	15,4	0,1
Other specialists in education and upvringing	49,9	48,5	1,4
OTHER SPECIALISTS	385,2	179,5	205,7
in %	6,2	6,6	5,8
Specialists in management and economics	283,1	90,0	193,1
Lawyers	25,2	22,1	3,1
Archivists, librarians and scientific information specialists	10,2	9,6	0,6
Specialists of social sciences	13,7	12,4	1,3
Specialists in art and culture	17,7	10,2	7,5
Public administration specialists	35,1	35,0	0,1

Source: based on *Struktura wynagrodzeń według zawodów w Polsce 2004*, Polish Central Statistical Office 2006,

Professional managers of different levels comprise 6,3% of the working population. Specialists are the largest professional group, with 19,6%. In total, 25,9% of workers belong to both groups. As mentioned earlier, this research did not comprise individual farmers and

the self-employed. Counting them in, the above group shrinks to 18,94%. There is a significant difference between the public and private sectors: the private sector only employs 16,7% of the two groups, while in the public sector they form 37,6% of workers. The imbalance is partly due to public education, with over 0,5 mln. employees, public healthcare system and public administration.

The research of the Polish CSO also includes data on employees' education. In the researched group of employed, 20,6% of them possessed a university degree of Master or higher, or Dr.med., and further 6,1% – the degrees of Bachelor, Engineer or equivalent. In total, 27,0% of employees have higher education – but can they be named knowledge workers, and does their work require them to have higher education?

Knowledge workers should be the best paid group of employees. This is confirmed by data in Table 3:

Table 3. Wages of knowledge workers in Poland, in 2004, according to the level of education and professional group.

RESEARCHED WORKPOSTS	Total	Public sector	Private sector
General:	2368,52	2527,63	2244,24
Education:			
Master degree or higher, or dr.med. or equivalent	3649,08	3244,08	4647,69
Engineer, Bachelor or equivalent	3262,85	2790,17	3617,86
Professional groups:			
Members of Parliament, higher officials and managers	5482,11	4854,15	5888,66
Specialists	3180,32	2992,89	3652,09

Source: based on *Struktura wynagrodzeń według zawodów w Polsce 2004*, Polish Central Statistical Office 2006,

The wages of the best educated group of employees were 54,1% higher than the average. Bachelors and engineers earned 37,75% more than the average. In professional groups, managers earned 231,5%, and specialists – 134,3% of the average. On the other hand, specialists in the public sector – in education or health care – earn considerably less. But together, managers and specialists take over 40,89% of all wages in the economy! Taking business sector alone, they catch over 50% of wages – business offers even better conditions for knowledge workers.

## 7. Labor market – threats to the development of the knowledge economy in Poland

In the forecasts of the “Poland 2000+” Forecasts’ Committee at the Polish Academy of Sciences, made to 2013 (the end of EU’s budget perspective) and 2025, specialists/ professionals/ knowledge-workers will be the fastest-growing group of employees. Their numbers should double between 2000 and 2025 (from 1 507 th. to 3 155 th.). Their number rises by 1/3 every 10 years. Within that group, professions with highest potential are IT specialists, business professionals, statisticians, financiers, sociologists, psychologists, media and communication specialists. The fastest growing industries are expected to be ICT, robotics, computer services, business consulting, PR and advertising.

A. Karpiński, secretary to the Forecasts' Committee, claims, that since Poland's accession to the EU, there arise conditions for a fall of unemployment to around the natural level within 10 years. He names five main factors working towards that (Karpiński (ed.), 2006):

- Quick rise and change in structure of domestic demand, aided by a jump in demand for housing.
- Broad use of EU funds will result in large capital investment and rapid development of workforce due to extensive training.
- The demographic pressure on unemployment is going to ease, since from 2010, the size of population in working age is going to fall.
- Due to the development of the service sector worldwide, there will be the opportunity to capture investments such as service centres for multinational companies.
- The labor markets of other EU countries will slowly open to Polish workers, and outward migration will force wage rise at home and rise in domestic consumption.

Unemployment may be falling, but still over 1,8 mln. people are registered in labor offices, and the unemployment rate, according to the ILO's definition, is 10,6%. Another important indicator is falling, too – although it already is the lowest among EU countries: the employment index is 52,8 % compared to the EU's average of 65,2. Emigration is intensifying. Business organizations alarm, that work shortages might shortly stifle Poland's economic growth. Companies meet more difficulty finding suitable employees. Quickly developing industries, such as IT, electronics or construction, suffer most – but others join, as well. In 2008 the demand for IT graduates will surpland the supply. And the rapidly growing construction industry is already missing ca. 200 thousand employees – and this is before the proper construction boom (not to mention stadiums, highways, airports and hotels to be built for the 2012 European Soccer Championships). Dramatic shortages can also be found in the public sector, e.g. police officers and nurses. Shortages of staff apply both to highly qualified graduates, and to qualified and non-qualified manual workers.

The reverse side of this may be favorable to knowledge workers: the shift from the employer's market to the employee's market. Employees have felt their power and position strengthened, and are starting to exercise their power and be more demanding. Which will hopefully lead to a change in corporate culture towards greater egalitarianism, democracy and individualism – which are features favourable of proficient use of knowledge workers. But it also results in a worrying rise in pay – over 10 % year-to-year since 2006, and a possible rise in inflation.

Consequently, we can name four factors hampering the development of the population of knowledge workers in Poland:

- proportion of the economically inactive people,
- emigration and brain-drain,
- maladjustment of the educational sector,
- social climate,

Any approximations of the proportion of knowledge workers within the economy, must be distorted, when over 47 % of adult population is outside the labor market. This has been the ongoing problem throughout the whole transformation. The level of employment has fallen by 4,2 mln between 1989 and 2005 – from 17,5 mln to 13,3 mln. One of the factors was

reduction of employment in agriculture, which amounts to 2,0 mln. Another reason was major overemployment and inefficiency in most of the industries. There were industries, in which the fall was to 15-40% of original employment – some of them were clearly relics and doomed in a market economy. Now, despite the fall of unemployment and rise in wages, the total number of economically active people is still falling. Who are the economically inactive? S.Golinowska (2006) names 4 groups:

- 29 % are young people in education. This may be perceived as encouraging, as majority of them are in higher education and will increase the number of knowledge workers. But two things counter that hope: firstly, universities have for the past few years been temporary refuge from the unemployment-ridden market and bleak prospects for young people, and secondly, the outburst of higher education in Poland has raised the numbers, but pushed down the quality of education.
- The second group are the (early) retired and people with disability pension. They often work part-time or in the 'grey economy'. Many of them also find work abroad, while still drawing state pensions.
- The highest part of the professionally inactive are the unemployed (over 31%). Among them are the long-term unemployed and those already discouraged from seeking employment at all. There is also a significant proportion of those, who work irregularly (seasonal jobs, short-term work) and illegally.
- Another 10% of the inactive are housewives, mothers and grandmothers caring for children and family.

It turns out from the above, that in fact a large proportion of the 'inactive' display activity, which does not fit into the term 'employment'. It may be the case, that the 47 % figure is, therefore, unnecessarily worrying, but on the other hand it is clear, that we cannot expect many of people composing it to enter the labor market as knowledge workers.

Emigration is another major threat to the knowledge economy in Poland.

It is reducing unemployment by 0,4-0,6% since 2004, but it is hardly any cause for satisfaction. The present wave of emigration is, unfortunately, to a great extent, a brain-drain. The recent research shows, that 43 % of the emigrants declare the will to stay abroad permanently (I.Dryll, 2007). This group is composed mainly of active, energetic young people. The average age of a migrant is 26 years and – which is important – he/she does not yet have a family. They are well-educated, many leave the country just after graduation. According to various estimates, from 600 thousand to 1 million Poles have left the country in the last three years. It is difficult to judge, what percentage of them leave permanently, what part leaves for 1-3 years to raise capital and come back, and what part finds seasonal or other temporary employment to supplement their income in Poland.

The phenomenon is a major threat to the future of the knowledge economy in Poland. We loose the most promising part of the workforce – the combination of dynamic and well-educated, which should be the catalyst of economic development and entrepreneurship. Poland looses the group of employes, who should in later years support the pension burden of the aging population. It is significant, that brain-drain is most vivid in the group of the most gifted youth. The brightest students use Erasmus to leave and stay abroad. The brightest graduates are not sufficiently appreciated and are not given opportunities suitable to their potential, which is connected with the misery of the R&D sector. Even the graduates of the secondary school International Baccalaureate (IB system), who have open doors to world's best universities, prepare themselves to study abroad as their first and natural choice.

There seems to be growing maladjustment of the educational sector to the labor market. First example are the manufacturing workers. Due to an inflow of foreign investment once again there is demand for qualified industrial workers. This is met with a sharp decline and neglect of vocational education after 1999, in favour of general high schools. Uncontrolled shutting down of vocational schools results in shortages in construction workers, mechanics, electricians, nurses, textile workers etc.

The extent of maladjustments in the Polish educational system provokes a claim, that it educates mainly for unemployment. Educational activity loosely corresponds with the needs of the market. Majority of both secondary schools and universities do not maintain close relations with local labor offices or business organisations, though in the last two years the trend is gradually changing. Private higher education is the exception, as it has had to be market-oriented from the start and offer programmes, which are perceived as attractive (though this often means a fad rather than a true market demand). Another factor adjusting education to market needs, is the huge popularity of part-time studies. Majority of students in Poland are working students, often with considerable professional knowledge and experience. Through their demands on the practical dimension of knowledge, they force a change of attitude on universities. This also signifies the existence of one of the pillars of a knowledge economy: the focus on constant, life-long learning. In Poland, it happened naturally: due to structural maladjustment of competences, thousands of working, middle-aged professionals have had to update or change their qualifications through additional degrees – and thus starting a degree over 40 has become understandable and natural.

But prof. Karpiński also sees maladjustment in the group of knowledge workers – key to modernisation and the new economy. Since 1989 technical studies were unpopular, and only in the last 2-3 years they are again promoted as the surest way to secure attractive and well-paid jobs in future. But new, narrow, technical specialties in the knowledge sector arise so quickly, that universities are not prepared to offer them fast enough to produce graduates, when demand appears. To overcome this, even quick reacting would have to be supplanted by careful forecasting in close cooperation with the industry. As experts say, among the 9-year-olds at school in the 90s, every second one will work in a profession, which does not yet exist.

A knowledge economy requires a knowledge society – and this requires mechanisms of knowledge circulation within a society. It requires a culture of high trust, openness to change, low barriers of communication, and an efficient set of social institutions facilitating knowledge transfer, such as schools, universities, training companies, media and publishing. And valuing knowledge above other things. Poland is still tailing in this respect. Mutual trust is low. People protect, what they know, even if they do not have to.

Surveys show, that the motivation of the current wave of emigration is not just economic. It is also the social climate abroad: healthier interpersonal relations, clearer appraisal and promotion criteria, more friendly and relaxed attitude to life. These factors are more important in the case of the best-educated group of emigrants – the knowledge workers such as IT specialists, engineers, financiers, doctors – who could earn a decent living in Poland, but for whom the social and intellectual climate is of higher value.

The social communication space in Poland is dominated by mistrust and hostility towards intelligent, educated people. It is attributable to the aggressive populism of the present government, and the medias' obsessive preoccupation with the political scene, which unnecessarily dominates the social debate. The ruling party's disregard for educated people (often labeled the 'lying elites') and open favouring of blind loyalty over independent competence, the strategy of 'ruling by scandals' – a never-ending campaign of dirty war on opposition and its own coalition partners instead of constructive resolving of real problems,



and the so-called ‘war on corruption: ‘regaining’ and founding new law-enforcement and anti-corruption agencies and undermining the authority of the justice system, while cynically taking over public institutions (like television) and using them to attack other parties and reap ‘historical justice’ – all three are destructive to the social fabric of interpersonal relations, which should support and frame the knowledge economy. Healthy separation of the economy and politics has protected the steady economic growth and transformation from the direct influence of politicians, but the indirect deterioration of social relations may turn to be much more harmful.

## 8. Conclusions

It is surely worthwhile to invest in knowledge workers. Over the past 20 years, the ratio of the market value to the book value of American companies doubled - which clearly shows knowledge as the source of economic success.

Poland has reached the stage of a developed industrial country – which is a major achievement in historical perspective. But the world leaders have already moved into the era of knowledge, and Poland is just at the door of the post-industrial age. Its advantages are a sizable proportion of well-educated knowledge workers (18 to 25%), strong economy, good education and fast-improving ICT system. Threats include underdeveloped R&D sector, brain-drain and unfavourable social climate. As incomes rise, Poland will lose competitive advantage as manufacturing centre, and be forced to move to a knowledge economy, or remain a periphery, contributing to Europe just the steady flow of educated emigrants and a market to sell to. It will continue to develop – the question is of direction. And the only way to enforce the direction towards a knowledge-driven economy must be through conscious decision, commitment and concerted effort of policy-makers and the whole society.

## References:

- Applehans W., Globe A., Laugero G., *Managing knowledge: practical-based approach*, Addison Wesley, 1999,
- Bukowitz W.R., Williams R.L., *The Knowledge Management Fieldbook*, Financial Time, Prentice Hall, London 2000,
- Davenport T., *Thinking for a living, How to get better performance and results from Knowledge Workers?*, Harvard Business School Press, Boston 2006,
- Drucker P.F., *Landmarks of Tomorrow*, Harper & Bros., New York 1959,
- Drucker P.F., *Is business letting young people down?*, Harvard Business Review, Nov/Dec 1965, Vol. 43 Issue 6,
- Drucker P.F., *Management and the professional employee*, **Harvard Business Review**, May/June 1952, Vol. 30 Issue 3, p84-90,
- Dryll I., *Szok na rynku pracy*, Nowe Życie Gospodarcze, 16/2007,

- Easterby-Smith M., Lyles M.A. (ed.), *Handbook of Organizational Learning and Knowledge Management*, 2006,
- Europe in figures. Eurostat yearbook 2006-07*, Eurostat 2007,
- Evans Ch., *Managing for Knowledge. HR's strategic role*, Butterworth-Heinemann, 2003,
- Golinowska S., *Czy brak polityki zatrudnienia to droga do społecznego wykluczenia?*, *Polityka Społeczna*, 11-12/2006,
- Horibe F., *Managing knowledge workers. New skills and attitudes to unlock Intellectual capital in your organization*, John Wiley & Sons, 1999,
- Karpiński A. (ed.), *Przyszłość rynku pracy w Polsce*, Komitet Prognoz „Polska 2000 Plus” PAN, PAN, Warsaw 2006,
- Knight T., *A strategic approach to KM*, *Knowledge Management*, Dec.2001/Jan. 2002,
- Kukliński A. (ed.), *Gospodarka Oparta na Wiedzy – wyzwania dla Polski XXI wieku*, OECD/Committee of Scientific Research, Warszawa 2003,
- Pinchot G., Pinchot E., *The rise and fall of bureaucracy*, in: Myers P.S. (ed.), *Knowledge Management and Organizational Design*, Butterworth-Heinemann, Boston 1996,
- Probst G., Raub S., Romhardt K., *Managing knowledge. Building blocks for success*, John Wiley & Sons, Geneva 2000,
- Seely Brown J., Duguid P., *The social life of information*, Harvard Business School Press, Boston 2000,
- Struktura wynagrodzeń według zawodów w Polsce 2004*, Polish Central Statistical Office 2006,
- Tampon M., *Motivating Knowledge Workers – the challenge for the 1990s*, in: Myers P.S. (ed.), *Knowledge Management and Organizational Design*, Butterworth-Heinemann, Boston 1996,
- Ziemkowski L. (ed.), *Wiedza a wzrost gospodarczy*, SCHOLAR, Warszawa 2003,

# **SOCIAL PROTECTION SYSTEM OF THE POPULATION OF REPUBLIC OF KAZAKHSTAN: CONDITIONS AND PROSPECTS**

**M.KH. TUSEEVA<sup>1</sup>,  
P.B. ISAHOVA<sup>2</sup>**

Social and economic reforms, which have begun in Kazakhstan, as well as in other CIS countries have influenced on all spheres of society's vital activity and have touched on all layers and groups of the population of republic. Today it is possible to speak about three stages of development of social policy in Kazakhstan

On the first stage (1992-1996) the course on socially focused market economy and decrease in rates of falling of life standards of the population has been proclaimed. Creation of new legislative base concerning social protection of the population has begun and bases for development of social partnership in such prior directions of activity, as employment of the population, a salary payments, social guarantees to citizens and social protection of the most vulnerable groups of the population have been incorporated.

Social support payments for indigents have got address character. The unemployment benefits have been transferred from the category of "grants" to the category of "material aid" paid from the funds of local budgets. In April, 1999 the legislation on benefits to the population has been changed. Benefits given previously were replaced by the social state payments to separate categories of the citizens, using natural benefits. Such policy had allowed not only to spend more rationally budgetary funds, to supervise execution of the state budget, but to achieve address giving of the social benefits and to providing equal access of citizens to the state social support also.

On the second stage (1997-1999) owing to growth of the economy there were opportunities for carrying out of active social policy. Created strategy of long-term development "Kazakhstan-2030" in which health, education and well-being of Kazakhstan citizens, struggle against poverty and unemployment have been declared as the major strategic tasks. Within the limits of realization of Strategy have been accepted a number of the important social programs, and practical actions on a labor protection, struggle against poverty and unemployment were undertaken. Among them:

---

<sup>1</sup> Professor Ph.D., University of International Business, Republic of Kazakhstan.

<sup>2</sup> Ph.D., University of International Business, Republic of Kazakhstan.

- Acceptance of the new legislative and normative legal acts, concerning struggle against poverty and unemployment;
- Pension system reforms;
- Realization of programs of population micro crediting and public works development;
- Assistance to development of small and average business;

Pension reform has begun in 1998. Kazakhstan became a first country in territory of the CIS which has begun systematic transition to stocker system of the population provision by pensions. Simultaneously with reforming, measures on increasing of the pension size, paid in solidary system of pension's provision, were undertaken.

Social support payments for indigents have got address character. The benefits on unemployment have been transferred from the category of "grants" to the category of "material aid", paid from the funds of local budgets. In April, 1999 the legislation on benefits to the population has been changed. Benefits given previously were replaced by the social state payments to separate categories of citizens, using natural benefits. Such policy had allowed not only to spend more rationally budgetary funds, to control execution of the state budget, but to achieve address giving of the social benefits and to providing equal access of citizens to the state social support also.

On the third stage (since 2000) a lot of important laws and the state programs are being accepted: Laws «On Labor in Republic of Kazakhstan », «About employment of the population in Republic of Kazakhstan», the Program on reduction of poverty for 2003-2005. Positive dynamics of growth on expenditures of the state budget on social programs is observed.

Table 1. Expenditures of republican and local budgets of RK on the social aid and social security for 1996-2006.

(Million tenge)

Year s	State Budget	Funding social protection		Republican budget	Funding social protection		Local budgets	Funding social protection	
		sum	%		Sum	%		sum	%
1996	280001	9212	3,2	196000	6860	3,5	84001	2352	2,8
1997	341871	13674	4,1	222216	7333,1	3,3	119655	6340,9	3,4
1998	377397	53618	14,2	266022	8797	3,3	156016	44821	2,9
1999	468423	159064	33,9	328573	140759	42,8	214974	18305	8,5
2000	602024	171065	28,4	396609	151033	38,1	303809	20032	6,6
2001	759610	186715	24,6	502490	156110	31,1	394054	30605	7,8
2002	834165	201415	24,1	541631	165389	30,5	394475	36026	9,1
2003	1026992	239230	23,3	773893	202043	26,1	479992	40145	8,3
2004	1287938	272333	21,2	995620	232998	23,4	622064	40039	6,4

2005	194614 6	345356	17,7	1537676	314710	20, 5	783483	34140	4,3
2006	215056 0	422423	19,6	1686342	390209	23, 1	1760351	42214	4,1

\*Source: [1. C.20-21, 2. C.11-13].

Stable economic growth has expanded financial opportunities of the state for an increase of expenditures on social needs. Last years is observed positive dynamics of expenditures growth of republican and local budgets on social programs.

In 2001 the Concept of social protection of population of Republic of Kazakhstan is accepted.

Acceptance of Conception of Public Social Security considered development the following components of social security of population:

- governmental payments from the budget for all citizens of the republic on the same level depending on social risks;
- mandatory social insurance (on the first step-in account of deduction of employers, in perspective in account of employees);
- accumulated pension system;
- social assistance and social state programs of support of definite category of citizens in account of budget facilities.

Accumulated pension system is improving. The amount of solidarity pension is increasing. From the 1<sup>st</sup> of January 2003 the amount of solidarity pension are increased on 12 %with account of forestalling temp of index growth of consuming prices.

Table 1- Social benefit receivers for 1996-2006

(thousand persons)							
Pointer	Pensioners	Economically active population	Number of population	Receivers of State social assistance	Specific weight of pensioners, %	Specific weight of economically active population, %	Specific weight of receivers of State social assistance, %
1996	2771,1	7489,5	14756,3	739,2	18,1	50,7	5,1
1997	2670,4	7440,1	14658,1	735,7	18,2	50,7	5,0
1998	1985,8	7052,6	14812,0	744,8	13,4	47,6	5,01
1999	1877,6	7055,4	14900,3	755,2	12,6	47,4	5,02
2000	1786,8	7107,4	14901,6	760,3	11,9	47,7	5,1
2001	1749,1	7479,1	14865,6	792,3	11,7	50,3	5,4

2002	1690,5	7399,7	14862,5	792,3	11,3	49,8	5,3
2003	1660	7657,3	14951,2	791,7	11,1	51,2	5,3
2004	1640,7	7840,6	15074,8	780,4	10,8	52,0	5,2
2005	1649,5	7901,7	15074,8	790,4	10,9	52,4	5,2
2006	1650,1	7908,3	15394,6	791,2	10,7	51,3	5,1

The specific gravity of pensioners in common amount of population is decreasing, the specific gravity of governmental benefit receivers remains on the level of 5 %. From the 1<sup>st</sup> of June 2003 is implementing the differentiated increasing of amount of pension payments depending on pensioners' labor contribution at simultaneous increasing of minimal pension from 5000 tg to 5500 tg. Increased pensions received more than 60 % from the whole amount of pensioners.

For stability of pension system are offered some measures, especially to expand the range of population by the services of accumulated pension system in account of development of transfer-agency activity in the market of pension services, disposal errors in system, appeared during optimization of pension accounts, effective use of opportunities of electronic data base. Also is need to do phased entrance of taxable preferences on payments in account of voluntary professional pension dues, to transfer voluntary professional pension dues into obligatory for branches with more harmful and dangerous labor condition. Entrance of obligatory professional pension dues, it can be done in account of own employer facilities-by relating the expenses of pension dues on cost price of product and their deductions at calculation of corporate income tax. In this case increases not only pension accumulation of employees, but also it becomes economically profitable of labor condition improving.

With the purpose of creation three-leveled system of social security of the population of the republic in April 2003 the following legislation "about mandatory social insurance" was accepted and from the 1<sup>st</sup> January 2005 the system of mandatory social insurance in following types of social risks: lost of working ability, lost of bread-winner and job is functioning.

Financing the system of social insurance is implemented in account of rate decreasing in social taxes until 3% and entrance of mandatory insurance deductions in amount of 3% from the income of employee. Moreover insurance payments on the first stage employers will bring. Personification of deductions on social insurance will increase motivation of employee to control the process of money transfer. Introduction of personification account of deductions on social insurance is one of the main conditions of reformation of social security system.

Addressed social assistance in the republic of Kazakhstan is executed in accordance with the Law "of state addressed social assistance" introduced in act from 1<sup>st</sup> of January 2002. The given law defined the circle of persons, having the right to receive state support in case of absence of income or low income. A criterion of rendering of addressed social assistance is the "poverty". The poverty in accordance with the Law "about living wage" serves as criteria for rendering of social assistance. It is defined in the Law as a border of income, established in the republic depending on economic opportunities. In 2000 and 2001 poverty had been establishing on the level of 30% from the living wage, on 2002 and 2003 – 40% from living wage. For receiving addressed social assistance persons with working ability age must been registered in empowered

bodies as unemployed. In connection with realization of the Law firstly for many years with the help of mechanism of addressed social assistance the “legalization” of unemployed people is happened.

In a structure of receivers of addressed social assistance on the 1<sup>st</sup> of January 2007 the most amounts are children – 60.3 %, unemployed-14.3%, persons busy by children care- 11.9%, working- 4.95%, invalids and pensioners – 2.8%, students-1.7%, self occupied-3% and other categories- 1.1%.

Equally with addressed social assistance housing assistance is paid, which is directed on offering material support for needy citizens for the compensations of expenses on housing-communal services and done in order with definite local executive organs.

Basic directions of development of social security system are based on the analyzes of international experience and modern conditions.

Nowadays social security system of the population of Kazakhstan is mixed and includes elements as in sympathy with, so personification system, as mandatory, also voluntary insurance and directed for provision of social security of the population from main risks, which person can face with during his life.

Guaranteed by state the level of social security is realized on the base of three-leveled level social security system.

Base social payments by old age; by invalidity; by lost of bread-winner are defined on the base of living wage and must provide its receivers the minimum level of support.

The second level of social support given for mandatory accumulated pension provision and mandatory social insurance.

The third level of social support is connected with development of schemes of voluntary social insurance, by formation of voluntary pension accumulations, insurance of responsibility of employer for bringing harm to life and health of employee at executing by himself working obligations.

In comparison with the system of social support, acting in Kazakhstan until the last period, transfer into multi-level system of social support has the following privileges:

- 1) additional levels of social security of employees of official economy sector are created;
- 2) to the social support, equally with budget, additional financing resources are attracted;
- 3) conditions for increasing personal responsibilities of citizens able to work for their own future and wealth of their family are created. Dependence on social payments from working activity of each, amounts and continuation of deductions enforce the fair character of social support system.
- 4) Multi-level system of social support influences positively on economic development, as such productive business in formal sector and legalization of working relations becomes beneficial.

In purposes of development of accumulated pension system in 2006 was conducted work in optimization of administrative payment system in accumulated pension system:

- payment procedure of mandatory pension dues is simplified;
- conditions, permitting to investor to realize the right of independently choosing of accumulated pension fund are created;
- on the base of “GCVP” united account center is created, where concentrated all information and cash flows of accumulated pension system.

Of investors, the number of which is 7 mln against 8.5 mln on the data base of accumulated funds. Nowadays in joint with pension funds the work is performing on removing 1.5 mln of doubled, tripled pension agreements.

Work on expansion of range by system of mandatory social insurance is done, consequently at the end of 2006 the amount of participants of mandatory social insurance system, for which even if once in time were paid social deductions in Fund, composes 4.5 mln people.

Social payments on loss of working ability, of bread-winner and job from the state fund of social insurance in 2006 received 9.5 thousand people.

From 2006 living wage legislatively attached by social normative base, which is used for establishing minimum amount of monthly income payment, base social payments and poverty.

On date of statistic Agency of the RK, volume of PM in 2006 was 8410 tg.

Half of population, having income below living wage decreased in third quarter of 2006 was 17.7% against 31.0% for analogical period in 2005.

In overcoming the poverty the special meaning has addressed social assistance. General expenses on rendering of addressed social assistance from the moment of its introduction (from 2002), was more than 3 billion tg. During 2006 addressed social assistance received more than 339000 persons on the sum of 3.4 billion tg.

Payments of extraordinary compensations are done for the persons, harmed from mass political repressions, nuclear testing on Semipalatinsk trial nuclear polygon.

Measures in expansion the net of medico-social institutions and improving of their financing are accepted. The net of boarding-school of less capacity (till 50 places) for old age people and disables, approximate to their living place are developing in oblasts.

Carries on the work in introduction of regulation system by labor security (MOT-SUOT 2001) and the standard OHSAS 18001: 1999 recommended by an International organization labor into Kazakhstan enterprises.

The following problems can be remarked:

- the amount of pension is increasing by phases, however in purpose of approaching their amount to the world standards are required accepting of further measures in problems at one with and base pensions.
- Are saved non-high level of pension asset income, insufficient temp development of voluntary pension accumulations, low level of informing the population about accumulative pension system and importance of conducting reforms.
- Is remarked low range of population by pension system. From 7 mln investors only 5 mln are the active investors. Such situation took place in mandatory social



insurance. For instance, the range of insurance system in Almaty oblast is 65%, South-Kazakhstan -70.1%. Zhambyl -80.1% and Kyzylorda -84%.

- In consequence of insufficient attention from the side of employers in provision of safe working conditions in comparison with 2005 on 18% increased the quantity of injured with death outcome. Their most amount is on mining-metallurgic industry and construction (53%). Given problems is necessary to solve in the frame of social partnership and increasing of social responsibility of an employer.

- In a labor market are saved inflow of low qualified foreign labor force, difficulties in employment of separate population group, tendency of exceeding the labor force supply over demand, training and retraining of personnel does not correspond with real economy requirements. This problem becoming more difficult in a background of Kazakhstan entrance into WTO.

Appears the necessity in solution of following problems.

In sphere of pension security:

- with account of possessed financial-economic opportunities and necessity in following to international principals of pension system, envisaging the establishment of income appointment percent not less than 40% must be entered offers of improving the level of pension payments.

- It is necessary to expand the range of population with the services of accumulated pension system and social insurance, to enter additional financial instruments.

- For provision of sufficiency of pension accumulations, equally with increasing the level of labor payment, it is necessary to enforce mechanism of employer participation in formation of additional level of pension accumulations.

- Development of voluntary pension accumulation scheme supposed to implement on a base of social partnership development and increasing of social business responsibility.

- In purpose of choice opportunity expansion for investors of APF and increasing of investment income is viewed as possible introduction of different pension plans.

- Measures lay ahead to accept in further improving the system of pension payments from APF and stimulating of annuity insurance.

In sphere of employment:

- it is necessary to expand business participation in creation of new working places, also for socially vulnerable population group and provision of employment of disable persons.

- To revise approaches and forms of work with unemployed youth and women, also independently employed population.

- To accept measures in formation of mechanisms, directed on protection of internal labor market and attraction into republic especially only high qualified foreign specialists.

In sphere of working relations:

- to realize the National program of deserved labor in the Republic of Kazakhstan on 2007-2009, accepted in joint with International Labor Organization and social partners of the Republic of Kazakhstan, the main task of which is to provide the legislative support for deserved labor and to increase the life quality of Kazakhstan citizens
- conduction of scientific-investigatory works on actual problems and labor protection, at first, in industrial sphere with high level of professional risk-coal and mining industry, in construction and agricultural complex.
- With the purpose of provision of work condition security in organizations should to continue the work in introduction of international standards by the system of labor security regulation.
- To continue the work in improving the system of employee labor payment of the budget sphere.

By our view, in purpose of developing the social security system of population of the Republic of Kazakhstan normative of social support and social serving should be improved, also living wage, of minimum income payment and minimal pension, which will permit to increase the life condition of population.

## **References**

Kazakhstan in the years of independence. Informational-analytical collection. Prepared by the Agency of the Republic of Kazakhstan in statistics. B.T. Sultanova. Almaty, 2006-380p.

Short statistical year-book of Kazakhstan. Under editing of Melshimbaeva A. Almaty, 2007-288p.

Isakhova P.B. Social transfers in system of social security of population//Karzhy-karazhat 2005, №6, p.41-50

# ECONOMIC SECURITY IN THE BLACK SEA REGION

ALINA DRĂGHICI<sup>1</sup>

## Abstract

Berry Buzan and the Copenhagen School proposed three new dimensions of security in order to complete it's the narrow political and military components. These are the economic, societal and environmental dimensions. The result is that economic factor came to be considered the building block of the other aspects of security. This idea is supported by NATO's new strategic concept (defined in 1991) stating that security and stability have political, economic, societal and environmental elements; and also by the EU's efforts of building the Common Foreign and Security Policy, were it applies economics, its strongest points, in the military security, one of its weakest points.

Ensuring a country's economic security considers the identification and management of dysfunctions, vulnerabilities, risks and threats to economic stability and strategic decisions independence concerning vital resources.

The paper will attempt to analyze the implications of applying the concept of economic security in the Black Sea extend area and highlight the link between the development model and interdependencies in international cooperation.

**Key words:** economic security, cooperation, Black Sea, energy.

**JEL codes:** F52, F59.

---

\* Assistant professor, PhD candidate, Department of International Business and Economics, Academy of Economic Studies, Bucharest, [alina.draghici@gmail.com](mailto:alina.draghici@gmail.com).

The security concept had, until the 1980's, a subsidiary role in geopolitical analyses, being particularly used in military strategic studies. In the 1980's we have certain dualisms like:

- Security – anarchy: security is the result of maintaining a balance of power or a hegemonic international system;
- Security – community: interest community creates security community structures, observing the proximity laws;
- Security – defense.<sup>2</sup>

Traditionally by referring to security, a statesman declares an emergency situation, demanding the right to use any necessary means to impede any threatening developments<sup>3</sup>.

The security concept became more complex, going beyond the narrow sense of military power equilibrium. Structurally there are two approaches to the security concept: the levels of action – individual, national and international; and the fields of action – military, political, economic and environmental<sup>4</sup>. Barry Buzan proposed enlarging the security concept so as to comprise the following five dimensions: military, political, economic, societal and environmental. “*Military security* concerns the game on two levels of states’ offensive and defensive capabilities and the states’ perception regarding everyone’s perceptions. *Political security* refers to states, governance systems, and ideologies (that ensure legitimacy) organizational stability. *Economic security* regards access to resources, markets and capital necessary for sustaining acceptable levels of wealth and power of the state. *Societal security* refers to the sustainability, in acceptable evolutionary conditions, of language, culture, religion, customs and national identity’s traditional patterns. *Environmental security* considers maintaining the local and global biosphere as an essential support of which all other human activities depend upon. These five sectors do not operate separately of each other. Each of them defines a focal point in the security problem and a way of defining priorities, but all are linked by a powerful connection network.”<sup>5</sup>

In the 1990's the Copenhagen School is created by Barry Buzan and other researchers that join him, using the analysis model he developed; the school had a major influence in security academic debates but also in developing security policies. During the NATO summit in Rome, 1991, the new security concept of the alliance was defined as “security and stability have political, economic, social and environmental elements”<sup>6</sup>.

---

<sup>2</sup> Buzan Barry, *Popoarele, statele și teama*, Editura Cartier, Chișinău, 2000.

<sup>3</sup> Weaver (1988) in Buzan Barry, Weaver Ole, de Wilde Jaap, *Security. A New Framework for Analysis*, Editura Lynne Rienner Publishers, 1998, Google Books, <http://books.google.com/books?vid=ISBN1555877842&id=j4BGr-Elsp8C&pg=PP1&lpg=PP1&ots=bKtfrZ4u18&dq=Security+a+new+framework+for+analysis&hl=fr&sig=ua1MVz62z74oVwGmnzO75oupae8#PPA21,M1>, p. 21.

<sup>4</sup> Eftimie Vasile, “Securitatea națională – O abordare comprehensivă”, *Neliniștile Insecurității*, coord. Troncotă Cristian, Editura Tritonic, Bucharest, 2005.

<sup>5</sup> Buzan Barry (1991) in Dan Dungaciu, *Moldova ante portas*, Editura Tritonic, Bucharest, 2005, p. 276.

<sup>6</sup> “The Alliance's New Strategic Concept”, July 1990, <http://www.nato.int/docu/comm/49-95/c911107a.htm#III>

Insecurity is at the other end of the spectrum, opposed to economic security. Gabriel Andreescu<sup>7</sup> considers simplifying the model that narrows the security of a state to the military strategic aspect and recommends identifying more security levels. It is interesting that when referring to the environmental, political and societal aspects he uses the term security; but for the economic one he opts for the term insecurity. The high economic interdependency degree allows efficient use of the economic instruments for penalty reasons. In Central and Eastern Europe, the author considers that profound economic restructuring and massive reorientation of the economic links transform the national economy in a fragile system, dependent of the international financial institutions policies or the ones of intergovernmental organisms.

The issues now raised by economic security<sup>8</sup> refer to way economic and politic stability can be maintained, the means to manage the wider distance among the rich and the very poor (that the free markets tend to generate). The liberals give the economy the first place in the spot lights, arguing that it is the base of social construction and the markets should be left to operate freely of state intervention. The state is necessary for ensuring the laws and the military and politic security and to support the social construction where the markets fail. Form this perspective, the main objective of economic security is to develop rules that ensure the free movement of production factors among the national economies.

The economic security discourse is mainly influenced by the liberal agenda, and consequently by trying to implement this agenda in trade, production and finance. The characteristics of the liberal ascendancy concentrate the economic security discourse on issues like instability and inequality. Concerns on instability raise questions on managing the internal and international problems determined by increasing the economic integration and liberalization degree. The concerns on inequality raise at national level questions about the state's role, and internationally issues on third world states disadvantageous position.

According to Berry Buzan, the following issues are on the economic security agenda<sup>9</sup>:

- The states capacity of maintaining military production capabilities in a global market, and in a wider sense, the relationship between the economy and state's military mobilization capacity;
- The possibility that the economic dependencies on the global market (especially the oil market) to be used for political purposes, or in a broader way, the issues on the security of delivery when the state abandoned the inefficient security of depending on its own forces with the efficient security of depending on external sources;

---

<sup>7</sup> Andreescu Gabriel, *Recomandarea 1201 și o rețea de stabilitate/securitate în Europa Centrală și de Est*, in "Studii internaționale", nr.3/ 1997.

<sup>8</sup> Buzan Berry, Weaver Ole, de Wilde Jaap, *Security. A New Framework for Analysis*, Editura Lynne Rienner Publishers, 1998, Goole Books, <http://books.google.com/books?vid=ISBN1555877842&id=j4BGr-Elsp8C&pg=PP1&lpg=PP1&ots=bKtfrZ4u18&dq=Security+a+new+framework+for+analysis&hl=fr&sig=ua1MVz62z74oVwGmnzO75oupae8#PPA21,M1>, p. 95-98.

<sup>9</sup> *Ibidem*.

- Fears that the global market will generate more losers than winners and will increase the existing inequalities (illustrated internationally, at one end of the spectrum, the fear of USA hegemony declining, and at the other end, the fear of developing countries of being marginalized and of financial crises; and nationally are represented by permanency of unemployment and increasing social polarization);
- The fear of (a) the dark side of capitalism and free trade represented by the illegal trade – especially drugs, that develop criminal groups and light weapons; (b) trade with certain significant types of military technology; and (c) pressure on the global environment done by industrialization and mass consumption;
- Fears that the international economy will go into crises under the influence of a combination of factors like political leadership, increase protectionist reactions and structural instability of the financial global system.

Another reality that needs thinking about is the need for an integrated approach<sup>10</sup> of these risks.

National security at the beginning of XXI century can not be approached nor at national or international levels, because in practice these things are tightly linked: corruption with money laundering, organized crime and terrorism. The subtle relations between these problems must be identified in order to solve the main issue. Another problem that could be a risk is the separate approach of the close and far conflict zones. Currently was identified a subtle communication system among the areas in which these risks operate – United States, South-Eastern Europe, Middle East, Afghanistan, South-East Asia. When stabilizing a zone like South-East Europe ignoring its effects somewhere else significant mistakes can be made in these multinational operations.

The main actors in the region are the neighboring countries with diverse affiliations – EU members (Romania, Bulgaria), candidate countries (Turkey), nonmember countries (Georgia, Russia and Ukraine); an array of international actors: EU, NATO, OSCE, USA and CIS (Community of Independent States). For now cooperation at the Black Sea materialized in the Black Sea Economic Cooperation, BLACKSEAFOR, GUUAM.

Historically the Black Sea was found at the confluence of the Russian, Ottoman and Persian Empires and was the main theatre of the “Big Game” played along its shores during the XIXth century. The contours of the Black Sea region established by the big European powers during the Crimean war and the First World War are still obvious today. The regions geopolitics’ is strongly influenced by external politics aspirations of the regional powers Russia and Turkey. The middle states Ukraine, Romania and Bulgaria are trying to insure security and stability by regional cooperation, especially by close relation with the European institutions. The small states Moldova, Georgia, Azerbaijan and Armenia are strongly affected by movement of the ex imperial powers in the area.

---

<sup>10</sup> Muresan Liviu, “Strategia securității naționale și politica externă după 11 septembrie 2001”, Scientific Communication Session “Securitatea națională la început de secol XXI”, organized by the Center of Security Strategic Studies, November 2001

Bruce Jackson argues that the same factors that transformed the Black Sea region in Europe's black hole are now justifying its placement as a central strategic interest today for Europe and the European Union<sup>11</sup>. These factors, even though presented by a US representative, synthesize the situation and the diverse interests in the area.

1. The Black Sea was for centuries the entry gate for the Middle East. The states in the region are neighbors of Syria, Iran and Iraq and the shores of Caspian Sea. USA will be successful in bringing democracy in the Middle East if it will contribute to building a Black Sea area secure, prosper and democratic.

2. The Caspian Sea energy reserves are becoming more and more important for US's European allies and for establishing the price of oil. Currently EU's member states are importing approximately 50% of their energy needs; until 2020 it is estimated that 70% of the energy consumption will be covered through imports. This increase of the energy needs is ensured by imports that will be transported to Europe using routes that will be crossing or bypassing the Black Sea – like the Baku-Tblisi-Ceyhan pipeline.

3. The Black Sea region is rapidly becoming part of Europe (Greece and the new EU member states – Romania and Bulgaria – are coming from this region; Turkey's accession to EU is estimated for 2014). The Black Sea west and south shores are NATO borders (Greece, Turkey, Romania and Bulgaria). The importance of the region was highlighted also at NATO summit in Istanbul in July 2004, where its essential role in the Euro-Atlantic security was recognized.

4. The most important and dramatic democratic changes take place in this area (the revolutions in Georgia and Ukraine).

5. The most dangerous fragments of the former Soviet Union are scattered along the northern shore. The frozen conflicts begin in Transnistria and continue in Abkhazia and South Ossetia in Georgia, in Chechnya and in Nagorno-Karabakh at the border of Armenia and Azerbaijan. In each of these conflict areas took place and might start again arm fighting and ethnic cleansing. In Transnistria, Abkhazia and South Ossetia are working trans-border criminal networks that destabilize the governments in the region and are a threat for Europe by trafficking arms, drugs and humans and for US also by its capability to sell arms and technology to its adversaries.

The European Security Strategy<sup>12</sup> synthesizes the threats to the European security as follows:

- The *energetic dependence* is a special preoccupation for Europe. Europe is currently the largest importer of oil and gas. Currently, approximately 50% of the energy consumption is covered by imports and it is estimated to get to 70% in 2030. Most part of the imports are coming from the Persian Gulf, Russia and North Africa;
- Terrorism undermines the openness and tolerance of European societies and represents an increasing strategic threat to the entire Europe. The most recent

---

<sup>11</sup> Jackson P., Bruce, "The Future of Democracy in the Black Sea Region", Romanian Journal of International Affairs, vol. X, 1-2/2005.

<sup>12</sup> European Security Strategy, "A Secure Europe in a Better World. European Security Strategy", Bruxelles, 12 December 2003, [http://ue.eu.int/ueDocs/cms\\_Data/docs/pressdata/en/reports/76255.pdf](http://ue.eu.int/ueDocs/cms_Data/docs/pressdata/en/reports/76255.pdf).

wave of terrorism is global by range and related to violent religious extremism. Its causes are complex and related to the pressure of modernization, cultural, political and social crises, and alienation of young people that live in foreign societies. Terrorism is part of the European societies, Europe being both a target and a base for terrorist activities.

- Proliferation of *arms of mass destruction* is probably the most important threat to European security. We are entering a period in which probably mass destruction arms race will take place in the Middle East. Also a serious threat is developing biological weapons, spreading the racket technology and attacks with chemical weapons and radiological materials.
- Regional conflicts. Violent or frozen conflicts that persist at Europe's borders threaten regional stability. They destroy human lives, social and physical infrastructures, threaten minorities, fundamental freedoms and human rights. Conflicts may determine extremism, terrorism and state failure; and create opportunities for organized crime. Regional insecurity may fuel the demand for arms of mass destruction. The most practical way to deal with the new threats, very often subtle and difficult to define, will ask for considering the older issues of regional conflicts.
- Weak government – corruption, power abuse, weak institutions and lack of responsibility – and civil conflicts erode the states from within. In some cases it determined state institutions collapse. States failure is an alarming phenomenon that undermines global governance and increases regional instability.

Europe is a main target for organized crime. This internal threat to European security also has an external dimension: transnational traffic of drugs, women, arms and illegal migration is an important part of criminal organization's activity. These could be linked to terrorist activities and, many times, are associated to weak or failed states.

The European interest presumes that the states at the borders of the Union toe well governed according to the European Security Strategy. In this respect, the neighbors engaged in violent conflicts, weak states where organized crime flourishes, dysfunctional societies or explosive increase of population at its borders raise problems for Europe. Former candidate countries accession increase the Union's security but they also bring it closer to the regions where most security issues are raised. Thus Europe proposes to promote a chain of well governed states at the eastern border and the Mediterranean Sea and to give more attention to the problems in the South Caucasus.

A short overview of the main actors of the political world, though in oil geopolitics more appropriately will be "centers of power"<sup>13</sup>, show differences but a common issue also. USA, EU and Japan have developed economies, national and international powerful financial institutions, settled democratic societies built on the principles of law and human rights; they also ensure a superior quality of life for all indicators. China and India are states with economies developing at high rates; financial stability; modernizing societies even though traditions have a strong influence and the quality of life is far from

---

<sup>13</sup> Dolghin Nicolae, „Geopolitica. Dependentele de Resursele Energetice”, in *Studii de Securitate și Apărare*, Volume 1, Editura Universității Naționale de Apărare, Bucharest, 2005.



that in first group of countries. The main common issue of these centers of power is dependence, especially of energy resources. This is mostly the reality that shapes the geopolitical behavior as well as the strategies content.

A special place among the centers of power belongs to Russia. It has features of the states in both the categories mentioned above; what sets her radically apart is the fact that it is not energy resources dependent, this independence also shaping its geopolitics and strategy.

In these conditions, oil geopolitics dominated the preoccupations of the world's governments and takes many shapes from multilateral cooperation, investments in the field, technical assistance, tenders, economic and financial help, privatizations, preferential conditions and so on, until expressions rather belonging to geostrategy being dominated by the military component, threats and force demonstrations, military presence and even armed violence.

Nowadays the main oil geopolitics actors are the USA and Russia. Each developed solid policies and strategies in this field. Their objectives are different but certain complementarities of these objective makes possible long term cooperation of the two, of course without excluding competition for the most favorable conditions.

USA's strategic objective is to ensure the long term resources necessary for maintaining the economic development rhythms, by guaranteeing access to resources and free shipment. It is a complex objective and fulfilling it requires decisive involvement in stabilizing volatile regions and enforcing security by encouraging the free market, the democratic values, transparency and predictability of the other actors' actions. Anyway the projects they are involved in are considered much cheaper investments than possible losses determined by energy flows dysfunctionalities.

Anyway the projects USA is embarking are considered much cheaper investments than the probable economic losses determined by dysfunctional energetic flows. USA see the Russian oil as a possible stable alternative to the oil of the Middle East, an unpredictable region were the steady supply could be affected by different events.

Russia also considers the entering of its oil on the American market a beginning for future economic consolidation and security building. That's why, on the long run the interests of two coincide, even though on the short run appear episodes of economic competition. The US are directly interested in the liberty of oil traffic in the Caspic Area and the Middle East, so they are actively involved in stabilizing the area, seeking in the same time to avoid a possible Russian oil transport monopoly formation.

Bearing in mind the theory of international relations, in order to have economic advantages, the states on the shores of the Black Sea should consider the followings: the control of the maritime coast; control of the maritime channels, control of the straits<sup>14</sup>. The states in the Black Sea region depend a lot of west European economic assistance essential for stimulating social and economic change; in most of these countries, in different proportions there are important obstacles: old mentalities, weak democratic traditions, corruption, international crime activities, illegal traffic of drugs, weapons and people.

---

<sup>14</sup> Maleşcu, Simona, "Tendințe geopolitice, geoeconomice și geostrategice regionale în zona Mării Negre", Colocviu Strategic, no. 13, 2005.

Developed economies depend on energy resources. The loss of access to resources could have destructive consequences. That's way an important part of external policies is preoccupied with the accessibility of pipelines and terminals, future pipelines projects and partnerships.

Referring to the energy resources, the states previously analyzed depend on the Russian oil and gas deliveries, which makes them particularly vulnerable. Thus Western Europe and the states on the west shore of the Black Sea are trying to open access to the energy resources of the Caspian Sea and Middle East in order to reduce the Eastern Europe, and EU in general, medium term dependency of Russia.

So far there is no strategy for the Black Sea. "Divergent interests, different affiliations make this region with very few cooperation traditions, historically speaking, to be difficult to place under a single efficient institutional coverage"<sup>15</sup>. In order to integrate this region Dan Dungaciu analyzes a series of projects implemented in other frontier regions of the EU, and particularly the Baltic Sea. According to the Italian analyst Fabrizio Tessinari<sup>16</sup> there can be identified three fazes of the cooperation process in the Baltic Sea area. There were three types of states in the region "the Old Europe" (Germany and the Nordic states), "the New Europe" (Poland and the Baltic states) and Russia. Considering the institutional affiliation there agendas did not always converge. Thus in the first period (1989-1992) was characterized by reviving and promoting a natural regionalism, by a small group of Scandinavian intellectuals; it indicated the potential for regional building. This faze was considered ended in 1992 once the institutional actors appeared – creation of the Baltic Sea States Council. The second faze, that lasted until 2004, was characterized by external and security policies becoming more European. Two types of discourses are identified form this period: the first one referred to the EU and NATO enlargement, the Baltic region being seen as the border of two quasi-empires – for the EU and NATO the enlargement was a way to create a safer Europe; for Russia it meant an invasion of its "close vicinity" and a threat for its security. The second discourse was determined by the by two initiatives ((*North European Initiative* – „soft security" cooperation, its agenda having the following priorities: promoting trade and business, state of law, building civil society, energy, environment and public health and *North Dimension Initiative* – that referred to five main issues: economic cooperation, infrastructure, natural resources, environmental protection, frontier cooperation), that led to increasing interdependencies by securing non-military aspects (unlike the first faze that focused on the military dimension). The third faze begun after 2004, when the security discourse was closely related to the political one and the interdependencies created are deepening.

Referring to the comparative analysis of the states in the two regions (the Baltic and the Black Sea) Dan Dungaciu<sup>17</sup> is underlining the fact that the conscious of belonging to a common region is not that strong as it was in the Baltic Sea and nor is it that homogeneous in Black Sea states (were they are grouping around regional actors like he EU, NATO and Russia). It is considered that this is an important aspect of a future cooperation process in the region. Also EU and NATO presence are much more reduced.

---

<sup>15</sup> Dungaciu, Dan, *Moldova ante portas*, page 292, Editura Tritonic, Bucharest, 2005.

<sup>16</sup> apud. Dungaciu, Dan, *Moldova ante portas*, pages 288-290, Editura Tritonic, Bucharest, 2005.

<sup>17</sup> Dungaciu, Dan, *Moldova ante portas*, page 288, Editura Tritonic, Bucharest, 2005.

In the case of the Baltic Sea the connection elements were non-military aspects of security; but in the Black Sea case together with these elements we have hard security issues (the frozen conflicts on the north shores) that amplifies the risks and are a proof of complex ethnic, frontier and social issues problems. Close ethnical and geographical location to Middle East and the Caspian Sea area, together with divergent interests increase the hard security issues.

## Conclusion

The economic security could become a stability pole in the area by attracting a growing interest of USA and EU for stabilizing and developing the area, but also from the states in the Black Sea region for economic development so as to not become dependent to extracting/processing and transporting oil, and thus vulnerable to the transfer of oil crisis from the developed countries to the periphery.

## References:

Andrescu, Gabriel, *Recomandarea 1201 și o rețea de stabilitate/securitate în Europa Centrală și de Est*, in "Studii internaționale", nr.3/ 1997.

Buzan Berry (1991) in Dan Dungaciu, *Moldova ante portas*, Editura Tritonic, Bucharest, 2005, p. 276.

Buzan, Barry, *Popoarele, statele și teama*, Editura Cartier, Chișinău, 2000.

Buzan Berry, Weaver Ole, de Wilde Jaap, *Security. A New Framework for Analysis*, Editura Lynne Rienner Publishers, 1998, Google Books, <http://books.google.com/books?vid=ISBN1555877842&id=j4BGr-Elsp8C&pg=PP1&lpg=PP1&ots=bKtfrZ4u18&dq=Security+a+new+framework+for+analysis&hl=fr&sig=ua1MVz62z74oVwGmnzO75oupae8#PPA21,M1>, p. 95-98.

Dolghin Nicolae, „Geopolitica. Dependențele de Resursele Energetice”, in *Studii de Securitate și Apărare*, Volume 1, Editura Universității Naționale de Apărare, Bucharest, 2005.

Dungaciu, Dan, *Moldova ante portas*, Editura Tritonic, Bucharest, 2005.

Weaver (1988) in Buzan Berry, Weaver Ole, de Wilde Jaap, *Security. A New Framework for Analysis*, Lynne Rienner Publishers, 1998, Google Books, <http://books.google.com/books?vid=ISBN1555877842&id=j4BGr-Elsp8C&pg=PP1&lpg=PP1&ots=bKtfrZ4u18&dq=Security+a+new+framework+for+analysis&hl=fr&sig=ua1MVz62z74oVwGmnzO75oupae8#PPA21,M1>, p. 21.

Eftimie Vasile, “Securitatea națională – O abordare comprehensivă”, *Neliniștile Insecurității*, coord. Troncotă Cristian, Editura Tritonic, Bucharest, 2005.

Jackson P., Bruce, “The Future of Democracy in the Black Sea Region”, *Romanian Journal of International Affaires*, vol. X, 1-2/2005.

“The Alliance's New Strategic Concept”, July 1990, <http://www.nato.int/docu/comm/49-95/c911107a.htm#III>

Maleşcu, Simona, “Tendințe geopolitice, geoeconomice și geostrategice regionale în zona Mării Negre”, Colocviu Strategic, no. 13, 2005.

Mureşan Liviu, “Strategia securității naționale și politica externă după 11 septembrie 2001”, Scientific Communication Session “Securitatea națională la început de secol XXI”, organized by the Center of Security Strategic Studies, November 2001

European Security Strategy, “A Secure Europe in a Better World. European Security Strategy”, Bruxelles, 12 December 2003, [http://ue.eu.int/ueDocs/cms\\_Data/docs/pressdata/en/reports/76255.pdf](http://ue.eu.int/ueDocs/cms_Data/docs/pressdata/en/reports/76255.pdf).

# ENERGY SECURITY: A CRITICAL ISSUE IN THE EUROPEAN ENERGY POLICY

ANA BOBIRCĂ<sup>1</sup>,  
PAUL-GABRIEL MICLĂUȘ<sup>2</sup>  
ȘTEFAN UNGUREANU<sup>3</sup>

## Abstract:

The topic of energy security has become an issue of high salience over the last few years. As fears about the stability of the world's energy resources grow, policymakers tend to merge the security concerns into the climate change policies that they are considering.

There are currently three major challenges of the global energy policy: the oil shock and higher prices, greater threats to security of supply, and climate change. Our paper seeks to bring an analytical perspective on these questions. To this end, it starts by individually analyzing the above-mentioned challenges at the EU level and by exploring strategies for meeting them. The paper subsequently concentrates on the European Emissions Trading Scheme (EU ETS), as the flagship of EU climate change policy, for a number of political, environmental and economic reasons. In the last part of the paper issues related to the climate change policy in Romania are addressed. The paper concludes with a review of the progress towards a single European energy market.

**Key words:** security, climate change, energy policy, carbon market, EU ETS

**JEL classification codes:** Q48, G18, F18

---

<sup>1</sup> Academy of Economic Studies, Faculty of International Business and Economics; e-mail: ana.bobirca@rei.ase.ro

<sup>2</sup> Academy of Economic Studies, Faculty of International Business and Economics; Romanian National Securities and Exchange Commission; e-mail: miclaus@rei.ase.ro

<sup>3</sup> Academy of Economic Studies, Faculty of International Business and Economics; e-mail: stefan.ungureanu@lycos.com

## 1. Introduction

Security is a multifaceted concept, with the national referent dominating security discourse. Large scale violent conflict is the concern that receives the most attention from policymakers, whilst developing military capability as a response to possible violent conflicts consumes large amounts of public resources. However, alternative risks to security and alternative referent objects (such as humans) are increasingly being considered. Among these risks are *energy supply and climate change*, as the two main elements of energy security topic and the core pillars of energy policy (Campbell, 1992; Dabelko and Simmons, 1997; Dalby, 1994).

As concern mounts over the impacts of growing demand, external dependency on energy supply sources, rising energy prices and global environmental change on economic, social and ecological systems, coinciding with a more fluid international security environment since the end of the Cold War, energy is increasingly being understood as a security issue.

The majority of interpretations of energy security focus on the way energy supply and environmental change issues may interact with the same national security concerns that dominated policy throughout the 20th century, in particular the way these may trigger violent conflict (Homer-Dixon, 1991; Kaplan, 1994; Myers, 1987). However, as recent developments in energy security research suggest, the concern with direct international conflict is misplaced, and the energy security impacts will take less direct and more multifarious routes (Lowi and Shaw, 2000).

Security is an accentuated discourse on vulnerability. Like vulnerability, its assessment requires considering the risk of exposure, susceptibility to loss, and capacity to recover. However, like vulnerability and risk, it is more socially constructed than objectively determined. The distinction is that security is attached to the most important of vulnerable entities – for example the nation (national security), basic needs (human security), income (financial security) and property (home security). The process of discursively ‘securitising’ vulnerable referent objects, and defining particular risks, is a political one (Waever, 1995).

Energy plays a vital role in our society, underpinning all areas of economic activity. The economic impact of supply disruptions can therefore be high and wide-ranging. This creates an incentive for governments to ensure that secure and reliable energy sources are readily available. A country’s energy security policy refers to measures taken to minimize the risks of supply disruptions below a certain tolerable level. Such measures ensure that a supply of energy is readily available and affordable to meet domestic demand. This, therefore, involves a quantity and a price parameter. But it also involves a time parameter: a sudden price hike will have very different effects on both society and the economy than a long-term price increase. Thus, the causes of insecurity in the energy sector include the risks related to the scarcity and uneven geographical distribution of primary fuels, as well as to the operational conditions and reliability of energy systems that ensure services are delivered to end users.

Climate change is a different energy policy driver from supply disruptions. Along with ozone depletion, it is one of the first truly global environmental concerns, and the first with major energy implications. Compared to the supply security policy drivers, it has emerged relatively recently as an energy policy driver of potentially great importance.

The first person to systematically argue that environmental change is a security issue was Richard Falk. Writing in 1971, when climate change was only a nascent concern, Falk outlined what he called “the first law of ecological politics” which is strikingly relevant for the issue of adaptation to climate change, namely: “there exists an inverse relationship between the interval of time available for adaptive change and the likelihood and intensity of violent conflict, trauma, and coercion accompanying the process of adaptation” (p. 353). This is a truism of contemporary climate change research: the faster the rate of change, the less time to adapt and the more “dangerous” climate impacts are likely to be. In 1977, Lester Brown explored the links between environmental degradation – including climate change – and security. His discussion particularly focused on food security, a subject which has subsequently received considerable attention from climate impacts researchers (for example Murdiyarto, 2000; Parry *et al.*, 1999; Sanchez, 2000; Wilkie *et al.*, 1999). After 1989, the argument that environmental change was a security issue for nations and people was increasingly made in both environmental and security journals. This must be considered in the context of dramatically improved relations between NATO and the former USSR, making conventional understandings of security less relevant. Simultaneously, environmental concerns were increasingly coming to the fore of national and international politics and policy (Dalby, 1992).

The accumulation over the course of the ‘70s and ‘80s of scientific evidence pointing towards the risks of enhanced climate change due to increasing anthropogenic greenhouse gas emissions led to a first international policy response in 1992, with the adoption of the United Nations Framework Convention on Climate Change. The Convention’s ultimate objective is to stabilize “greenhouse gas concentrations in the atmosphere at a level that would prevent dangerous anthropogenic interference with the climate system”. This was subsequently backed in 1997 by the Kyoto Protocol to the Convention which sets a timeframe for emission reductions in industrialized countries.

Accepting the above arguments that energy price hikes together with supply disruptions, on one hand, and climate change, on the other hand can be treated as security issues, this paper seeks to bring an analytical perspective on these questions. To this end, it continues by individually analyzing the above-mentioned challenges at the EU level and by exploring strategies for meeting them. The paper will subsequently concentrate (more specifically) on the European Emissions Trading Scheme (EU ETS), as the flagship of EU climate change policy, for a number of political, environmental and economic reasons. For the EU, emissions trading is one of the crucial pillars upon which both the EU’s climate change policy and the global regime should rest. Environmentally, the ETS is important because it covers almost half of the EU CO<sub>2</sub> emissions and more than a third of total greenhouse gas emissions. Economically, the ETS is important as it is the show case for applying this type of economic policy instrument in practice at large, cross-border scale, for CO<sub>2</sub> emissions. The purpose here is to give a comprehensive insight into the EU ETS and the climate change regulatory framework, as well as to identify the challenges the ETS faces and to either explore options and/or to identify the principle policy questions that emerge from the current state of the ETS. Market organization, trading practices, and the new financial assets introduced by the EU ETS will also be outlined. In the last part of the paper issues related to the climate change policy in Romania will be addressed. In developing a competitive domestic energy market, Romania is closely observing the energy policy of the European Union, with the aim of becoming a part of an integrated European market. The paper concludes with a review of the progress towards a single European energy market.

## 2. EU energy security challenges

For the past two decades Europe has focused overwhelmingly on the completion of the European energy market, and in particular on the liberalization of electricity and gas markets. This process is close to completion, subject to the last phases of market opening and a number of “difficult” cases. Europe’s energy is now supplied overwhelmingly by private companies competing in liberalized markets.

Though the internal energy market has yielded considerable benefits, it has been hampered by the fact that there is no integrated European market yet, but rather a string of national markets with bilateral connections (Helm, 2006; European Commission, 2007). Thus physical trade has been limited, and, as a result, Europeans have not reaped the benefits of a fully integrated internal market, and competitiveness has suffered.

This major gap did not matter so much in the ‘80s and ‘90s because most member states had excess capacity, and world energy prices were very low. But now it does matter, because the energy sector in Europe has changed fundamentally since. The decades of abundant low-priced fossil fuels, combined with the overhang of the power stations built in (or before) the ‘70s and early ‘80s, has given way to a new set of challenges: *the oil shock*, *security of supply* and *climate change* (Helm, 2005).

### (i) *The oil shock*

(a) The oil price shock from 2000 has resulted in sustained higher prices. The peak of world oil production is now within the planning horizon of the sector. Few new big reserves are being found, whilst the growth of demand from China, India and other fast developing countries will underpin prices. By 2030, the IEA (International Energy Agency, 2005) forecasts that world energy demand will rise by 60% from current levels.

(b) The gas price shock followed that of oil, and gas continues to be priced in contracts which are indexed to the oil price. With European supplies heavily concentrated in Russia and Norway, and new LNG (liquefied natural gas) supplies at a premium to pipeline gas, this linkage is likely to remain for the foreseeable future.

(c) Electricity prices have risen to reflect gas costs, since in most European countries, gas is the marginal fuel. The tightening supply/demand balance has also begun to be reflected in prices, which will have to sustain new investment.

Thus, the European economy, which has developed in the last two decades on the basis of low prices, will need to adapt to a very different set of assumptions.

### (ii) *Security of supply*

Recent increases in energy prices and a steady escalation in global energy demand — expected to rise by nearly 60% over the next 20 years — have led U.S. policy-makers to engage in a wide ranging debate over how best to address the country’s future energy requirements. Similarly, energy supply security has become a policy priority for the European Union (EU) and its 27 member states. Together, the United States and Europe represent the world’s largest energy



market. Although they produce approximately 23% of the world's energy, they consume almost 40% of the world's supply.

The EU imports about 50% of its energy needs. Barring significant changes, the European Commission expects this figure to rise to 65% by 2030. Europe's energy imports come primarily from Russia and the Middle East, where approximately 70% of global oil and gas supplies originate. Yet, the Middle East region is fraught with war, terrorism and politically unstable regimes. Iraq's oil production has not reached pre-war levels, and there is fear that terrorist groups could target pipelines and production facilities throughout the region. Iran has threatened to cut back oil production if forced to abandon its nuclear power program. With regard to Russia, recent political and economic behavior exhibited by Moscow has raised the dual specter of reliability and "energy politics."

High demand has also raised questions regarding the future availability of global oil and gas reserves. Although significant shortages are not projected for the next several decades, uncertainties over future exploration and production in areas such as Russia and the Middle East have raised concerns about long-term supply availability.

European concern regarding the security of its energy supply was first prompted by the Arab oil embargo of the early '70s. Since then, much of Europe has not faced any serious threat to the security of its energy supplies. The North Sea has provided oil and gas, whilst world markets in coal and oil have been benign. With the exception of the first Gulf War, the only threats have been internal and temporary, and focused largely on labor problems.

These conditions have now changed, and security of supply is threatened in a number of ways:

- (a) The external dependency on gas, notably from Russia, and the reliance on long pipelines through sometimes politically difficult territories.
- (b) The external dependency on oil supplies, with production increasingly concentrated in the Middle East.
- (c) Terrorist threats to key energy installations.
- (d) Network failures, due to the decades of asset sweating in the low return years of the '80s and '90s.
- (e) Aging oil refineries and power stations, and low investment in the last two decades.
- (f) Poor interconnections between European electricity and gas grids.
- (g) Lack of effective European-wide mechanisms for addressing security of supply risks and coordination of infrastructure investment.

Addressing the multi-dimensional security of supply problems will require a major investment program across Europe and much greater cooperation between member countries, and between the EU and its partners, notably Russia<sup>4</sup>. The International Energy Agency (IEA, 2005) estimates that close to \$16 trillion in new investments may be needed over the next 30 years to meet future global energy demand.

### *(iii) Climate change*

---

<sup>4</sup> The EU White Paper on security of supply sets out some of these issues (Commission of the European Communities, 2000).

Climate change was recognized in the EU back in the '80s, but the constraints have only begun to be felt in this decade. The EU has endorsed the ambition of stabilizing emissions of greenhouse gases, adopting specific Kyoto targets, and introduced the world's most advanced emissions trading scheme. It has also adopted a directive on renewables. These initiatives pose major challenges to Europe's energy sector, in particular:

- (a) The Kyoto targets, which in the context of global warming trends are modest, are nevertheless proving very hard for most member countries to achieve.
- (b) The majority of European electricity assets are based upon fossil fuels, and most are old and coming up to replacement.
- (c) Renewables technologies proved expensive relative to fossil fuels, adding to pressure on competitiveness.
- (d) The first generation of nuclear power stations are coming towards the end of their lives, taking out significant zero carbon emissions capacity, and some countries are considering a new wave of investment.

The Russia-Ukraine and Russia-Belarus oil and gas crises<sup>5</sup> have corresponded with increasing public calls for concerted European action on climate change, spurring European leaders to renew efforts to establish a more cohesive European energy policy. During their March 2007 summit, EU heads of state adopted a series of European Commission proposals that they expect will form the foundation of an "Energy Policy for Europe." The adopted measures are among a larger group of recommendations the Commission laid out in a March 2006 "Green Paper" and a more detailed action plan unveiled in January 2007. The Commission proposals focus on three broad interconnected goals: increasing European-wide energy security; enhancing sustainability; and fostering competition in Europe's internal energy market. Commission officials place particular emphasis on the links between energy security, energy efficiency, and an EU-wide reduction in carbon emissions.

In what some consider a reflection both of increasing public pressure to address global climate change and continued member state reluctance to cede national economic and foreign policy making authority, the EU's March 2007 agreement focused largely on Commission recommendations on sustainability. Member states did commit to take some steps toward further liberalizing the EU-wide energy market and have broadly endorsed increased foreign policy coordination on securing energy supplies. However, the EU's most far-reaching commitments focus on increasing energy efficiency, decreasing greenhouse gas emissions, and promoting the use of renewable energy and alternative fuels and associated technologies. Specifically, EU member states have committed to reducing total EU-wide carbon emissions by 20% compared with 1990 levels by 2020. They have also pledged to seek international agreement on a 30% reduction target by 2020 in a post- Kyoto Protocol international carbon emissions reduction

---

<sup>5</sup> In late December 2005, Russia's gas monopoly, Gazprom, temporarily suspended gas flows to Ukraine as part of a dispute over gas price increases. Within hours of the shut off, several European countries, including Austria, Italy, Poland, and Germany, reported drops in their own pipeline pressure by as much as 30%. The gas crisis lasted only a few days, and after Russia and Ukraine reached an agreement on gas prices, gas was flowing again. An almost identical dispute between Russia and Belarus with similar consequences for European countries, particularly Germany, occurred in early January 2007. This time, Russian oil pipeline operator Transneft shut down the Druzhba oil pipeline through which Germany receives 20% of its oil imports. Germany and the EU sharply rebuked Russia's decision, and Russia resumed oil delivery after three days of price negotiations with Belarus.

treaty<sup>6</sup>. In addition, the EU seeks a 20% increase in Europe-wide energy efficiency by 2020 and has mandated that 20% of all EU energy consumption come from renewable sources and 10% of transport fuel from biofuels by 2020. Member states are expected to agree on country-specific targets to achieve these Europe-wide goals by late 2007.

The challenge of climate change arises at the historical point when much plant needs replacing. This provides an opportunity to use this point of the investment cycle to invest in substantial non-carbon sources. Thus, both security of supply and the climate change challenges need to be met with major new investment.

### 3. The EU Emissions Trading Scheme

#### a. The carbon market: some conceptual issues

Carbon transactions are defined as purchase contracts or ERPA (Emission Reductions Purchase Agreements) whereby one party pays another party in return for GHG (greenhouse gas) emissions reductions or for the right to release a given amount of GHG emissions that the buyer can use to meet its compliance – or corporate citizenship – objectives vis-à-vis climate change mitigation (World Bank, 2006). Payment is made using one or more of the following forms: cash, equity, debt, convertible debt or warrant, or in-kind contributions such as providing technologies to abate GHG emissions.

There are several types of carbon assets currently traded on the market, created under international and national local regimes or through private contracts outside these legal frameworks. Most of these carbon assets share a common base – they are usually based on a common unit of one t CO<sub>2</sub> reduced, or an allowance to emit one t CO<sub>2</sub>. Emissions trading can be simplified to cover the creation and sale of these assets (Tang, 2005). Carbon assets derive mainly from the Kyoto Protocol and the EU ETS; thus they are statutory-based rights gaining their existence from statutes or treaties (Tang, 2005) (see table 1).

**Table 1. Carbon assets under the Kyoto Protocol and the EU ETS**

Carbon asset	Description
Assigned Amount Unit, AAU	Units that are issued to Annex I parties to the Kyoto Protocol; the amount of AAUs determine how much the Party is entitled to emit
Certified Emission Reduction, CER	Unit of emissions reductions created through CDM projects
Emission Reduction Unit, ERU	Unit of emissions reductions generated through JI projects
European Union Allowance, EUA	Units that are issued to liable installations under the EU ETS; represent an allowance to emit one tonne of carbon dioxide
Removal Unit, RMU	Unit of emissions reductions created through investments in sinks (deforestations, afforestation etc.)

<sup>6</sup> The United Nations Kyoto Protocol, to which the United States is not a party, is set to expire in 2012. European leaders reportedly see 2009 as the deadline for international agreement on a post-Kyoto treaty.

Carbon assets, mainly EUAs (European Union allowances), can be traded according to five basic financial structures: immediate (spot) settlements, forward contracts, futures contracts, option settlements, and swaps. Of these instruments, spot settlements, forwards, and futures are the most used at the moment; options and swaps are still in their emerging stage.

Carbon transactions can be grouped into two main categories:

- *Allowance-based transactions*, in which the buyer purchases emission allowances created and allocated (or auctioned) by regulators under cap-and-trade regimes, such as Assigned Amount Units (AAUs) under the Kyoto Protocol, or EUAs under the EU ETS. Such schemes combine environmental performance (defined by the actual level of caps set) and flexibility, through trading, in order for mandated participants to meet compliance requirements at the lowest possible cost;

- *Project-based transactions*, in which the buyer purchases emission credits from a project that can verifiably demonstrate GHG emission reductions compared with what would have happened otherwise. The most notable examples of such activities are under the CDM (clean development mechanism) and the JI (joint implementation) mechanisms of the Kyoto Protocol, generating CERs (certified emissions reductions) and ERUs (emissions reduction units), respectively.

There are several fragmented carbon markets, encompassing both allowances and project-based assets that co-exist with different degrees of interconnection<sup>7</sup>. These markets are developed to various degrees in different parts of the world, as national and regional policies themselves evolve. In 2006 and the first quarter of 2007, there were important regulatory developments in North America and Australia with initiatives to manage GHG emissions at least at regional levels.

By size and value, the Kyoto Protocol is the largest potential market and the EU ETS, a “tributary” scheme, which has spawned a thriving market in the trade of allowances and for the import of project-based reductions.

Buyers largely engage in carbon transactions because of carbon constraints (current or anticipated) at international, national or sub-national levels.

The main compliance buyers are: European private buyers interested in the EU ETS; government buyers interested in Kyoto compliance; Japanese companies with voluntary commitments under the Keidanren Voluntary Action Plan; U.S. multinationals operating in Japan and Europe or preparing in advance for the Regional Greenhouse Gas Initiative (RGGI) in the Northeastern U.S. States; power retailers and large consumers regulated by the New South Wales (NSW) market in Australia; and North American companies with voluntary but legally binding compliance objectives in the Chicago Climate Exchange (CCX).

There is also a growing retail carbon segment that sells emission reductions to individuals and companies seeking to offset their own carbon emission footprints.

---

<sup>7</sup> These interconnections arise mainly from competition between these different markets for the same type of offset credits (typically, CDM projects may be purchased by installations under the EU ETS, governments facing Kyoto commitment or Japanese companies with voluntary commitments under the Keidanren Voluntary Action Plan) and to a lesser extent, from trades of compliance instruments across schemes (for some time, EUAs were considered as a valid compliance instrument under the Chicago Climate Exchange).

## **b. The EU ETS as the largest carbon market**

The EU emissions trading scheme was launched on the 1<sup>st</sup> of January 2005 in the 25 EU member states to cap CO<sub>2</sub> emissions from heavy industry. The ETS was established through the implementation of the EU Directive 2003/87/EC: “establishing a scheme for greenhouse gas emission allowance trading within the Community” (EU, 2003). The ETS covers only CO<sub>2</sub> emissions from large emitters in the power and heat generation industry and only selected energy-intensive industrial sectors: combustion plants, oil refineries, coke ovens, iron and steel plants and factories making cement, glass, lime, bricks, ceramics, pulp and paper. A size threshold based on production capacity or output determines whether plants in these sectors are included in the ETS. More than 11,400 installations are included, accounting for about 45% of the CO<sub>2</sub> emissions in the EU, or about 30% of its overall greenhouse gas (GHG) emissions (EU, 2005). The ETS-Directive requires the member states to develop a national allocation plan (NAP) stating the total quantity of allowances and how they propose to allocate them.

Covering almost half of all EU CO<sub>2</sub> emissions, the EU ETS forms the centerpiece of European policy on climate change. Trade in these emission allowances gives value to reducing CO<sub>2</sub> emissions and has formed a market with an asset value worth tens of billions of euros annually. Putting a price on carbon has been an achievement of global significance, through the linkages to emission credits generated under the Kyoto mechanisms.

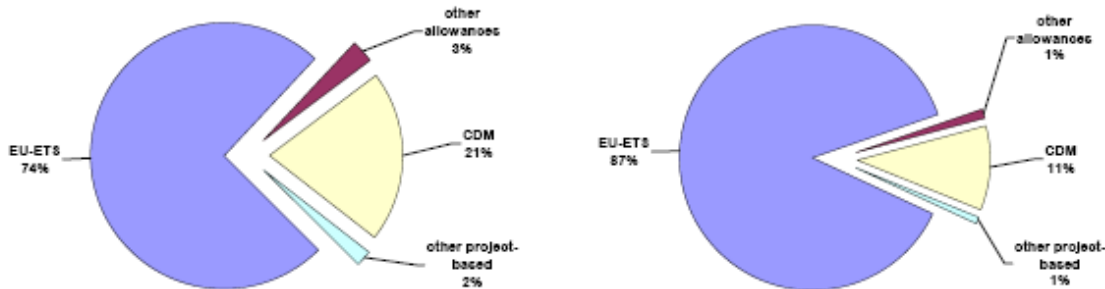
Like for any market, the key to prices is scarcity, and the price depends on both the absolute quantity of allowances available and expectations about the future. The most fundamental difference of emissions trading from any normal market is that the amount available depends directly on government decisions about allocations; and expectations about the future are largely expectations about future emission targets.

The legal framework of the EU ETS does not specifically regulate how and where the trading of carbon assets (mainly EUAs) takes place. There are three basic trading platforms through which companies that have obligations under EU ETS can trade their EUAs: bilateral trading, commodity exchanges, and over-the-counter (OTC) brokers. Around one fourth of the total traded volume of EUAs in 2005, 100 Mt CO<sub>2</sub>, corresponding to €1.8bn, was estimated to take place in the bilateral market (Point Carbon, 2006). At the moment, a majority of EUA trading takes place in exchanges or through wholesale or retail OTC brokers. The brokered and exchange market of EUAs in 2005 totaled to 262 Mt CO<sub>2</sub>, corresponding to €5.4bn (Point Carbon, 2006). Wholesale OTC brokers provide mainly EUA forward trading for companies and installations with defined contracts, established credit relationships with trading partners, and defined delivery dates. Retail OTC brokers, on the other hand, provide more customized transactions and flexible structures for buyers who seek to address their compliance shortfall (Capoor & Ambrosi, 2006). Over the last years, exchange platforms and auctions have increased their popularity over the OTC brokers. Exchanges simplify the transactions, reduce risks, and help make the trading prices more transparent (Capoor & Ambrosi, 2006). Currently six exchange platforms trade EUAs in the EU area. Of these exchanges, European Climate Exchange (ECX), Nord Pool, and Powernext have the biggest trading volumes, ECX having a share of 63 % of the traded volume (Point Carbon, 2006). Some of the exchanges also trade other commodities such as power (Nord Pool, Powernext), and several of the exchanges are preparing to trade CERs (Capoor & Ambrosi, 2006). In 2005, 79 % of the traded volume went through the OTC brokers, but the share of

trading through exchanges was approaching 50 % already in 2006 (Point Carbon, 2006; Capoor & Ambrosi, 2006).

In terms of economic scale, the European emission trading scheme is the biggest such scheme in the world by an order of magnitude (see figure 1).

**Figure 1. Shares of Volume (left) and Value (right) Transacted in the Carbon Market (2006 until September 30)**



Source: The World Bank, 2006

Actual verified emissions in 2005 were two billion t CO<sub>2</sub> – more than 3% below what had been allocated to countries that year. While as a whole, the scheme was “long”, six Member States (Greece, Austria, Ireland, Italy, Spain, UK) together were “short” by some 180 Mt CO<sub>2</sub>. On a sectoral basis, the power and heat sector was the only one with a shortfall, of about 35 Mt CO<sub>2</sub> (Kettner et al., 2007). Preliminary verified 2006 emissions data suggested a long market for 2006 as well, although less so, since caps were slightly tighter, while 2006 emissions were slightly higher than in 2005. This overall surplus together with the no-banking rule (rendering EUAs-I worthless beyond compliance year 2007) led to a steady price decline for EUAs-I through 2006. The decline continued as power and heat installations finished hedging their positions for Phase I.

Given the experience of Phase I, it was expected that the constraints on Phase II emissions would be tight, including in those newer members of the EU who enjoy a comfortable position *vis-a-vis* their Kyoto targets.

Decisions so far taken on 19 NAPs set, on average, the annual cap at 5.8% below 2005 verified emissions (adjusted for changes in the Phase II perimeter or boundary). Together with a tighter constraint, the penalty for non-compliance will rise from €40 currently to €100, and this remains on top of the obligation to cover any shortfall in that period.

One of the major changes in design between Phase I and Phase II is the inclusion of banking – which will bring market continuity to the EU ETS and possibly encourage additional abatement by installations depending on their current situation and their anticipations of future carbon price. In addition, the scope of the EU ETS has been extended with the inclusion of further installations by Member States. Another significant evolution is the introduction of aviation into the scheme for intra EU-bound flights (from 2011) and for all flights leaving or landing in the EU (from

2012). This is expected to reduce up to 183 Mt CO<sub>2</sub> emissions per year by 2020 in the fast-growing sector.

In 2007, the EU ETS saw over one billion allowances changing hands (1.101 million representing a three-fold increase over 2005) for a financial value of US\$24.4 billion or €18.7 billion (also up slightly more than three times from US\$7.9 billion in 2005 or €6 billion). This despite a drop in average EUA prices (down 10% from US\$24.70 in 2005, or €19, to US\$22.10 in 2006, or €17).

EUA transactions were mainly struck over-the-counter (with the London Energy Brokers Association, or LEBA, accounting for more than half the volumes). Virtually every month over the past two years saw an increase, on average, in the number of trades over the previous months. A year that saw the geographical scope of the EU ETS widen to include new member states of the EU (i.e. Romania and Bulgaria), also saw an increase in the number and type of participants (beyond the utilities that were the early players) and more complex transactions occurring (including, for example, options on EUAs and swaps between EUAs and CERs).

The January 27, 2007 announcement by the EU Commission on energy and climate change provided greater clarity concerning the future of a climate regime beyond 2012. However, many features for Phase III of the EU ETS still need to be drawn up – especially in the light of the key recommendations from the review process of the scheme: harmonization across member States or sectors (new entrants and exiting installations, allocations to installations among others) and linking to other mandatory cap and trade schemes.

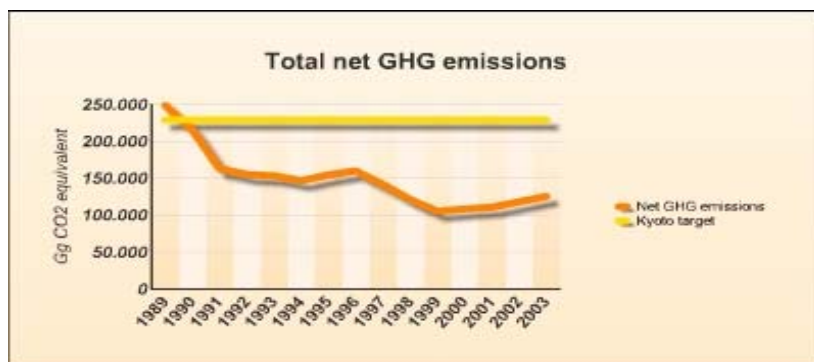
#### **4. The climate change policy in Romania**

Romania's current political outlook regarding climate change entails a pro-active approach, mainly shaped by the recent accession to the EU and the approximation of national policy to EU standards.

Important parts of Romania's commitment to reduce GHG emissions are already being implemented, such as the elaboration of the National Strategy on Climate Change (NSCC) adopted in 2005, and the action plan for the implementation of the strategy National Action Plan on Climate Change (NAPCC), also adopted in 2005, as well as the development of institutional capacity at the national level. Other provisions of the government program concerning climate change are under development, as is the Registry for Greenhouse Gases, updates of the GHG inventory, forecasts for future emissions, the development of new joint implementation (JI) projects, adaptation measures and others (Government program, 2005-2008).

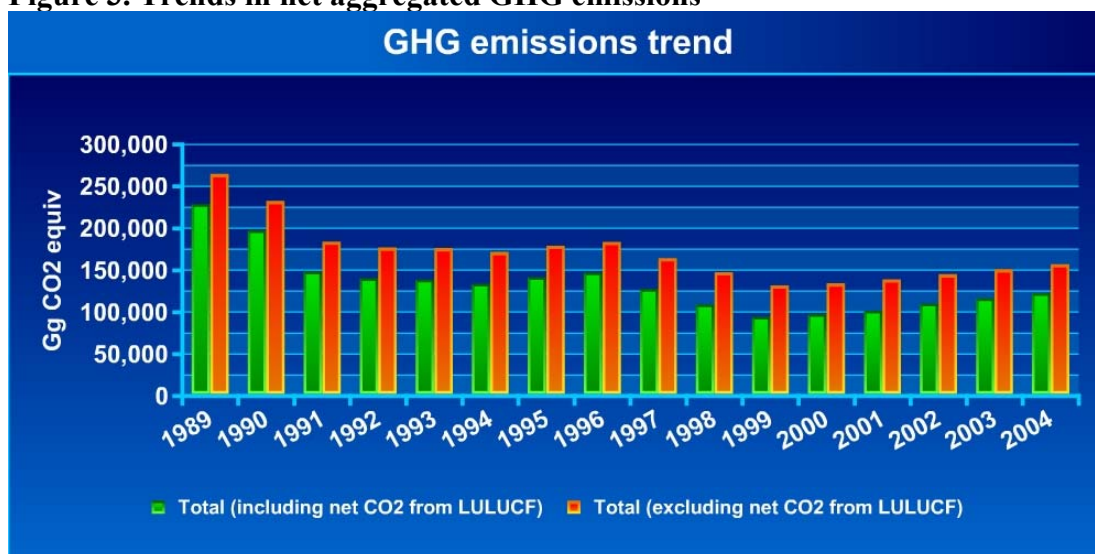
In accordance with the Kyoto Protocol, Romania has committed to reduce GHG emissions by 8 percent in the period 2008-2012 compared to the baseline year of 1989. Total GHG emissions decreased by 41 percent in the period 1989-2004, and net GHG emissions (taking into account CO<sub>2</sub> removals) decreased by 47 percent in the same period (see figures 2 and 3).

#### **Figure 2. Total net GHG emissions in CO<sub>2</sub> equivalent in the period 1989-2002**



Source: *National Inventory Report 2002*, Ministry of Environment and Water Management and National Research and Development Institute for Environmental Protection, 2004

**Figure 3. Trends in net aggregated GHG emissions**



Source: Romania — National Inventory Report 2006

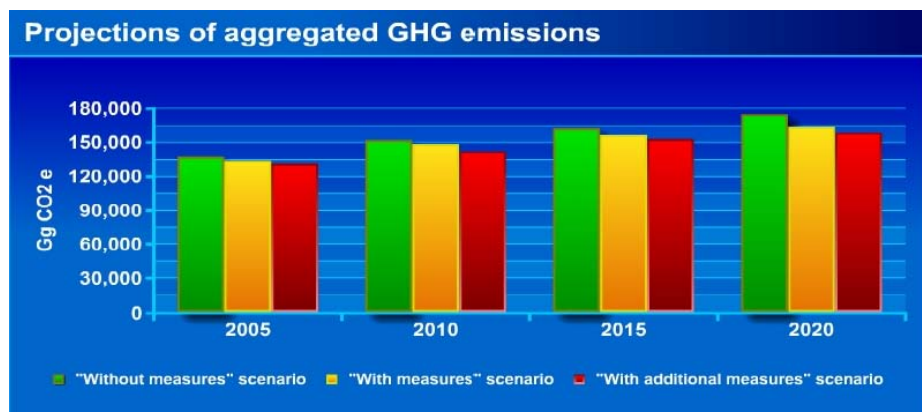
Projections for the period 2005-2020<sup>8</sup> show a great potential for Romania to reduce its GHG emissions. Three scenarios were used for calculating the projected GHG emissions, taking into account the macroeconomic and energy indicators for the period 1998-2020, together with the possible measures to reduce GHG emissions: without measures; with measures; and with additional measures (see figure 4).

The projections were based on calculations carried out using the Energy and Power Evaluation Program (ENPEP) developed by Argonne National Laboratory of the US Department of Energy (DOE) and distributed to Romania by the International Atomic Energy Agency (IAEA). The main models used are the Model for Analyses of Energy Demand (MAED), the Wiener Automatic Simulation Program (WASP), BALANCE and IMPACT.

**Figure 4. Projection of aggregated greenhouse gas emissions in Romania**

<sup>8</sup> Romania – Report on Demonstrable Progress in Implementing the Kyoto Protocol 2005, <[www.mmediu.ro/dep\\_mediu/schimbari\\_climatice](http://www.mmediu.ro/dep_mediu/schimbari_climatice)>





Source: Romania – Report on Demonstrable Progress in Implementing the Kyoto Protocol 2005

Macroeconomic and energy indicators for Romania for the period 1998-2020, together with possible measures for reducing GHG emissions, were used in order to estimate the projections of GHG emissions for the period 2005-2020. The starting point for the projections was the information included in the National GHG Inventory of Romania, submitted in 2003, and the provisional data for the 2004 submission.

The estimation suggests that the total GHG emissions level in 2020 for all scenarios will not exceed the aggregated net emissions level of the baseline year (1989) of 262,281.5 gigagram (Gg) CO<sub>2</sub> equivalents. Table 2 presents the projections for CO<sub>2</sub> removals for all scenarios, established on the basis of the GHG inventory submitted in 2004, also taking into consideration the various measures for the increase of carbon sequestration.

**Table 2. Projections of CO<sub>2</sub> removals (in Gg)**

Year	1998	1999	2000	2001	2002	2005	2010	2015	2020
<b>Scenario</b>									
Without measures	19,518.99	18,411.67	17,684.97	18,541.20	15,971.54	16,500	17,500	18,050	18,500
With measures	19,518.99	18,411.67	17,684.97	18,541.20	15,971.54	16,800	17,800	18,450	18,800
With additional measures	19,518.99	18,411.67	17,684.97	18,541.20	15,971.54	16,900	18,050	18,600	19,050

Source: Romania – Report on Demonstrable Progress in Implementing the Kyoto Protocol 2005

According to the provisions of Article 4.6 of the Framework Convention, and of the Fifth Session of the Conference of the Parties (COP), the baseline year for Romania for monitoring progress on climate change is 1989, which gives a figure of about 262,281.5 million tonnes of CO<sub>2</sub> equivalent. During the first commitment period (2008-2012), Romania will have to meet the 8 percent reduction level, meaning that no more than 241,000 tonnes of CO<sub>2</sub> equivalent can be released.

Romania has important reserves of AAUs for the period 2008-2012 that could be valued through the Kyoto Protocol mechanisms as well as through the ETS. The trends for 2020 show an increase in emissions, but all three scenarios are considerably below the level of the baseline year (1989).

With respect to the EU ETS, Romania, as a recent EU member:

- transposed the EU Emission Trading Directive (2003/87/EC) as well as the Linking Directive (2004/1014/EC) by June 2006;
- established a national registry by September 2006, this being one of the eligibility criteria for participation in the implementation of the Kyoto Protocol's flexible mechanisms and in the EU ETS. The purpose of the registry is to ensure the accurate accounting of the issuing, holding, transfer, acquisition, cancellation and withdrawal of assigned amount units (AAUs), removal units (RMUs), emissions reduction units (ERUs), and certified emission reductions (CERs), as well as the carry-over of these units. Furthermore, the Kyoto Registry should be combined with the EU ETS Registry required by the EU ETS Directive, resulting in a unique national registry.
- Prepared and submitted national action plans (NAPs) I and II for (informal) EC approval by mid-2006, in order to allow the start of trade as of January 1, 2007 and to submit the second NAP (2008-2012) for approval as requested by the directive;
- adopted legislation on monitoring and reporting by mid 2006; and
- adopted accreditation procedures for verifiers and institutional arrangements for registration of accredited verifiers by mid-2006.<sup>9</sup>

The implementation of the EU ETS would allow a large number of Romanian companies in the energy sector and general industry to participate in European emissions trading. Where emission reductions are realised, the participating companies can create additional revenues by selling surplus allowances on the market.

## **5. Concluding remarks**

Market failures are endemic to energy markets, and they are multiple. Energy policy is the design of a framework within which a number of different objectives can be met through markets, supported by appropriate instruments. For the last two decades of the twentieth century, these failures were largely masked by excess supply and low fossil-fuel prices. Since 2000, this context has gradually changed.

As we have outlined in this paper, Europe faces major security of supply and climate change challenges, and the myriad of current national energy policies as well as the underlying market structures are not fit for purpose. Europe requires major investment in its energy sector, after two decades of asset-sweating and cost reductions. This investment needs to meet not only the new realities of gas import dependency, particularly from Russia, but also the transformation from a high- to a low-carbon capital stock. To be fit for purpose requires a new European energy policy framework.

---

<sup>9</sup> The National Strategy on Climate Change and National Action Plan on Climate Change.

Energy policy in Europe – as elsewhere – has been chasing to catch up with the agenda of the 1980s and 1990s, and liberalization and fostering competition have been the main instruments. The latest policy proposals (European Commission, 2007) are aimed at completing that agenda. However, the world has moved on, and while competition might have many benefits, it cannot alone solve the other market failures. Recent fears over Ukraine and Belarus, combined with growing alarm over climate change, have begun to shift this complacency.

Despite these challenges and the interdependency of Europe’s energy market, remarkably after a decade and a half of trying to complete the internal energy market, Europe still consists of a set of national markets, many with national champions, connected together by a series of bilateral links. There is not yet much of a European market at all, and only the rudiments of a European electricity grid and pipeline network. This is reflected even in the EU Emissions Trading Scheme (EU ETS), which is very much national in its workings. This national, rather than European, physical structure of the market is reflected at the policy level too: almost all European countries have national energy policies, and indeed almost all are engaged in national energy policy reviews. In many of these cases, the European dimension has to date received scant attention. A national approach would not matter if the domain of the problems confronting energy markets remained national too. But a core characteristic of energy policy is that the objectives of security of supply and climate change are now, respectively, European and global. The former necessarily requires a European policy response, and the latter requires Europe to take the lead in gaining global agreement and reducing its own emissions. The other objective of the energy policy - competitiveness – is also better addressed at the European level through the economic efficiencies that arise from integrating energy markets and their networks.

#### References:

- Brown, L., “Redefining National Security”, *Worldwatch Paper No.14*, Worldwatch, Washington, 1977
- Campbell, D., “Writing Security: United States Foreign Policy and the Politics of Identity”, Manchester University Press, Manchester, 1992
- Capoor, K. & P. Ambrosi, *State and Trends of the Carbon Market 2006*, Washington DC, USA, 2006
- Dabelko, G., Simmons, P., “Environment and security: core ideas and U.S. government initiatives”, *SAIS Review* 17 (1), 127-146, 1997
- Dalby, S., “Ecopolitical discourse: 'environmental security' and political geography”, *Progress in Human Geography* 16 (4), 503-522, 1992
- Dalby, S., “The politics of environmental security”, in Kakonen, J., (Ed), *Green Security or Militarized Environment?* Aldershot, Dartmouth, 25-53, 1994
- Dower, N., “Peace and security: some conceptual notes”, in Salla, M., Tonetto, W., Martinez, E., (Eds), *Essays on Peace: Paradigms for Global Order*. Central Queensland University Press, Rockhampton, 18-23, 1995
- EU, Directive 2003/87/EC of the European parliament and of the council of 13 October 2003 establishing a scheme for greenhouse gas emission allowance trading within the Community and amending Council Directive 96/61/EC, 2003
- EU, Emissions trading: Commission approves last allocation plan ending NAP marathon, Press release 20 June 2005 (IP/05/762), 2005
- EU, EU emissions trading. An open scheme promoting global innovation to combat climate change, 2005

- European Commission (EC), EU Action against Climate Change. EU Emissions Trading – an Open Scheme Promoting Global Innovation. Brussels, Belgium, 2005
- European Commission (EC), EU Action against Climate Change. The European Climate Change Programme. Brussels, Belgium, 2006
- Falk, R., *This Endangered Planet: Prospects and Proposals for Human Survival*. Random House, New York, 1971
- Helm, D. R., *Energy, the State and the Market: British energy policy since 1979*. revised ed, Oxford, Oxford University Press, 2004
- Helm, D. R., “The Assessment: The New Energy Paradigm”, *Oxford Review of Economic Policy*, 21(1), 1-18, 2005
- Helm, D. R., and Hepburn, C., "Carbon Contracts and Energy Policy: An Outline", 2005
- Homer-Dixon, T., “On the threshold: environmental changes as causes of acute conflict”, *International Security* 16 (2), 76-116, 1995
- International Energy Agency, World Energy Investment Outlook 2005
- Kaplan, R., “The coming anarchy”, *Atlantic Monthly* 273 (2), 44-76, 1994
- Lowi, M., Shaw, B., (Eds), *Environment and Security: Discourses and Practices*. Macmillan Press, Hampshire, and St. Martins Press, New York, 2000
- Murdiyarso D., “Adaptation to climatic variability and change: Asian perspectives on agriculture and food security”, *Environmental Monitoring and Assessment* 61 (1), 123-131, 2000
- Myers, N., “Population, environment and conflict”, *Environmental Conservation* 14 (1), 15-22, 1987
- Parry, M., Rosenzweig C., Iglesias A., Fischer G., Livermore M., “Climate change and world food security: A new assessment”, *Global Environmental Change* no. 9, 51-67, 1999
- Point Carbon, “Carbon Market Europe”, a Point Carbon Publication (available at: <http://www.pointcarbon.com>), 2005
- Sanchez, P., “Linking climate change research with food security and poverty reduction in the tropics”, *Agriculture, Ecosystems & Environment* 82 (1-3), 371-383, 2000
- Soroos, M., *The Endangered Atmosphere: Preserving a Global Commons*. University of South Carolina Press, Columbia, 1997
- Tang, K., *The Finance of Climate Change. A Guide for Governments, Corporations and Investors*. Risk Books, London, UK, 2005
- The World Bank, “State and Trends of the Carbon Market 2006, Washington D.C. 2006
- Waever, O., “Securitization and desecuritization”, in Lipschutz, R., (Ed), *On Security*. Columbia University Press, New York, 46-86, 1995
- Wilkie, D., Morelli, G., Rotberg, F., Shaw, E., “Wetter isn't better: global warming and food security in the Congo Basin”, *Global Environmental Change* 9 (4), 323-328, 1999.

# AIRPORTS DRIVING ECONOMIC AND TOURISM DEVELOPMENT

CRISTIANA CRISTUREANU<sup>1</sup>

ANA BOBIRCA<sup>2</sup>

## ABSTRACT

*Globalization of the world economy is a key driver of air traffic growth. Cross-investment between European countries, as well as to and from the USA, Far East and the rest of the world is increasingly a feature of modern business, with mobility of labor as a growing factor.*

*The most important contribution of airports is the connectivity they provide, which allows the European economy and society to flourish. Air transport provides accessibility, which is essential in a modern economy and society.*

*The air transport sector is evolving rapidly to meet the changing needs of society as a whole. It is predicted that, despite recent global events, overall air traffic growth rates are likely to return to previous levels (5-6% per annum) in the medium term, driven in part by the growth in low cost services.*

*Transport is seen as an important factor in the economic and social integration of Europe, and an important indicator of the quality of life. Its significance will continue to grow with the enlargement of the European Union. The EU has recognized the importance of mobility to the social and economic development of nation states and also to the integration and realization of the Union. In addition, in remote regions, air transport fulfils a crucial social function, often connecting communities to essential services, such as hospitals and further education.*

*European airports are now widely recognized as having a considerable economic and social impact on their surrounding regions. These impacts go far beyond the direct effect of an airport operation on its neighbors, to the wider benefits that air service accessibility brings to regional business interests and to consumers. Airports provide the essential infrastructure to support regional social and economic growth; moreover, they are commercial entities in their own right, capable of generating returns on investment to the benefit of their shareholders, other stakeholders and to society as a whole.*

*It is also possible to identify 'air intensive' sectors of business. It is the financial and business services sectors which often make the greatest use of air transport and for whom **accessibility to air services** will have the strongest influence on location decisions.*

*Airports with available land are developing **business parks** to capitalize on the attractiveness of air service connectivity to businesses. Often these business parks are used by firms with some connection to the airport or aerospace industries. Otherwise they are chosen as locations for companies making intensive use of air transport. Examples include Cork, Hamburg, Nice and the 'Aviapolis' development at Helsinki Airport.*

*The use of **air freight** as a means of transport is increasing, particularly for high value, low weight goods, or those requiring urgent transport. OECD has estimated that up to a third in value of world trade in merchandise travels by air. That's why policy makers must better acknowledge the social benefits provided by airports in terms of the freedom to fly.*

---

<sup>1</sup> Professor PhD., Department of International Business and Economics, Academy of Economic Studies, Bucharest, Romania, E-mail: [cristiana.cristureanu@rei.ase.ro](mailto:cristiana.cristureanu@rei.ase.ro).

<sup>2</sup> Lecturer PhD., Department of International Business and Economics, Academy of Economic Studies, Bucharest, Romania, E-mail: [ana.bobirca@rei.ase.ro](mailto:ana.bobirca@rei.ase.ro).

Three years ago, a special issue of the *Geographical Journal* (British Royal Geographical Society) (Dodds and Siddaway, 2004) was devoted to the contemporary relevance of Halford J. Mackinder (1861-1947), a British geographer, politician and diplomat, on the centenary of his paper “The Geographical Pivot of History” (Mackinder, 1904). Mackinder formulated a subsequently much-repeated hypothesis (de Blij, 1967: 106; Taylor, 1989: 48) that was specifically directed at the statesmen then meeting in Versailles to redraw the map of Europe:

“Who rules East Europe commands the Eurasian core

Who rules the Eurasian core commands The World-Island (Eurasia and Africa)

Who rules the World-Island commands the World.”

The emphasis on Eastern Europe as the strategic route to Eurasia was interpreted as requiring buffer states to be established to separate Germany and Russia (Taylor, 1989: 48). Further elaborated during World War II, Mackinder’s hypothesis became one of the most intensively debated ideas of all time (Blij, 1967: 132; Blouet, 1987). Yet, Mackinder remained unimpressed by the potential importance of air power: “Some persons today seem to dream of global air power which will liquidate both fleets and armies....(but)...Air power depends absolutely on the efficiency of its ground organization” (Mackinder, 1943: 600).

Why are the above statements relevant to the contemporary transformation of European space and to international tourism? While since superseded by global perspective such as world-systems approaches (notably promoted by Wallerstein: 1974, 1976, 1979, 1984), Mackinder geopolitical ideas are significant (Gray, 2004) for the profound impacts that have been experienced in Eastern Europe for much of the twentieth century:

- In a Europe devastated by World War II, the EEC - today’s EU - was born out of the desire to prevent any further conflict on European soil;
- the Cold War that co-existed with the first three decades of the EEC/EC/EU witnessed markedly different models of domestic and international tourism being pursued in the continent’s two ideological blocs of East and West;
- the key aim of post-communist transition is EU membership and re-adoption of Western institutional norms;
- one of the most significant EU contributions to the transformation of European space and mobility has been, via Europe’s “freedom of the skies” legislation, the growth of low-cost airlines, the most effective and important of which do indeed follow Mackinder’s observation that air[line] power depends absolutely on the efficiency of ground organization, albeit facilitated most effectively by an extensive net of airports;
- With the enlargement of Europe and the greater travel distances involved, air transport has to play an ever more important role in the integration of Europe.

The present paper seeks to explain and expand on the specific **importance of Europe's airports** and their impact on social and economic development through the air travel industry. It also highlights the many key economic benefits accompanying airport development, as well as air travel contribution to the development of European destinations.

Information has been collected directly from airports statistics and through researching the most recent reports on economic and social impacts prepared for airports and other interested bodies. A list of those airports supplying data and reports is given in appendix A. We have supplemented this information from other reports where available. We have used the broad methodology and definitions from the "2000 ACI EUROPE Study Kit", as a basis for collating data for this study.

Airports provide air transport services through a complex interaction of resources and processes. Like other major industries, airports exert a significant economic impact on their surrounding areas, supporting employment, generating prosperity and **providing economic stability**. Regions or conurbations<sup>3</sup> served by more than one airport can benefit from competition and choice, so enhancing the economic benefits that airports can bring. Airports not only support employment directly on-site and in the surrounding areas, but also do so indirectly, in the chain of suppliers providing goods and services. In addition, the incomes earned in these direct and indirect activities generate demand for goods and services in the economy, which further supports employment.

In summary, we consider the overall economic impact of airports under the following headings:

- **direct** - employment and income that is wholly or largely related to the operation of an airport;
- **indirect** - employment and income generated in the economy of the study area in the chain of suppliers of goods and services;
- **induced** - employment and income generated in the economy of the study area by the spending of incomes by the direct and indirect employees; and
- **catalytic** - employment and income generated in the economy of the study area by the wider role of the airport in improving the productivity of business and in attracting economic activities, such as inward investment and inbound tourism.

## 1. Airports as national and regional economic hubs

Airports constitute necessary infrastructure for a wide range of economic activities. This wider economic role is known as the catalytic impact, arising from the effect that air service accessibility can have on the region served by the airport.

---

<sup>3</sup> large continuous built-up area formed by the joining together of several urban settlements. Conurbations are often formed as a result of urban sprawl. Typically, they have populations in excess of 1 million and some are many times that size.

Access to markets and external and international transport links is regarded as “absolutely essential” to businesses taking location decisions. The catalytic effect of an airport operates primarily through enhancing business efficiency and productivity by providing easy access to suppliers and customers, particularly over medium to long distances. Global accessibility is a key factor for business location and success in all regions of Europe.

Airports are increasingly developing as multi-modal interchange nodes. Their network positioning creates strategic advantages which enable them to ‘entice’ a broad range of economic activities, functioning as new development poles. This is evidenced by the development of **Amsterdam Schiphol** and **Paris Charles de Gaulle (CDG) Airports**.

Global accessibility can be important at a regional level as well as at a national level. For example, 31% of companies relocating to the area around **Munich Airport** cited the airport as the primary factor in their location decision. A survey of businesses in the **Hamburg** area found that 80% of the manufacturing companies reported air service connections as important to getting customers to look at their products. In 2002, it was reported that 93% of the top Irish companies used **Dublin Airport** for business travel. There is no reason to believe this proportion would have declined.

Where airports have good connectivity, this can act as a powerful magnet for companies. It is possible to identify ‘air intensive’ sectors of business, namely those sectors of industry that are most dependent upon air service accessibility: insurance, banking and finance, other means of transport, printing and publishing, petroleum and nuclear fuel, extraction, transport, communication, other business services, research and development, computer activities, precision and optical instruments:

- The Ile de France Region generates 30% of the French national GDP. Accessibility to **Paris CDG Airport** is a powerful factor in company location decisions, particularly for the large global companies headquartered in the Paris area, and for firms engaging in new high-tech, innovative, industries.

- Connections to Eastern Europe offered by **Vienna Airport** have enabled Vienna to provide the location for the East European headquarters of several global financial companies.

- The attractiveness of airports and their hinterlands is particularly strong for ‘high tech’ industries as evidenced by **Copenhagen** and **Nice Airports**.

Airports with available land are developing **business parks** to capitalize on the attractiveness of air service connectivity to businesses. Frequently, these business parks are used by firms with some connection to the airport or aerospace industries. Otherwise they are chosen as locations for companies making intensive use of air transport. Examples include **Cork, Hamburg, Nice** and the ‘Aviapolis’ development at **Helsinki Airport**.

The use of **air freight** as a means of transport is increasing, particularly for high value, low weight goods, or those requiring urgent transport. The Organization for Economic Co-operation and Development (OECD) has estimated that up to a third in value of world trade in merchandise travels by air.



Growth of air service access can enhance the growth potential of a region, which in turn will increase the demand for air travel, creating a ‘virtuous circle’ of growth. Airports also act as magnets for a wide range of economic activities. The effects are observed through the role of airports in:

- influencing company **location decisions** and **competitiveness**. The presence of an international airport can be a critical factor in:
  - attracting new **inward investment** from outside the area, and especially companies from overseas;
  - retaining **existing companies** in the area, whether they had previously been inward investors or indigenous operations;
  - securing the **expansion** of existing companies, in competition with other areas;
  - promoting the **export success** of companies located in the area by the provision of passenger and freight links to key markets;
  - enhancing the **competitiveness** of the economy, and the companies in it, through the provision of fast and efficient passenger and freight services; and
  - adding to the **quality of life** of citizens by enabling travel, notwithstanding local environmental implications.
- attracting business and leisure visitors and, hence, **inbound tourism** to the area, generating income and employment in the tourism industry. Tourism is the second main element of the catalytic impact. For the EU as a whole, tourism accounts for 5% of total employment and of GDP, and as much as 30% of the total external trade in services. Airports play a major role in making the development of inbound tourism possible. Many holiday destinations would not be easily accessible without air services, such as the **Spanish** and **Greek Islands**. Good air service connections are vital to their success as tourist destinations. Even for major European cities, air travel can account for a third or more of their foreign visitors. For example, almost 10 million visitors arrive in the Ile de France area by air via the **Paris Airports**, spending €3 billion.

## 2. Airports, vital to regional accessibility and social development

Air transport for passengers and freight is an essential component of the modern global economy. The social benefits contribute to the quality of life in Europe. The importance of air transport access has led many European countries, such as **France** and **Norway**, to introduce Public Service Obligations to ensure that essential services are maintained.

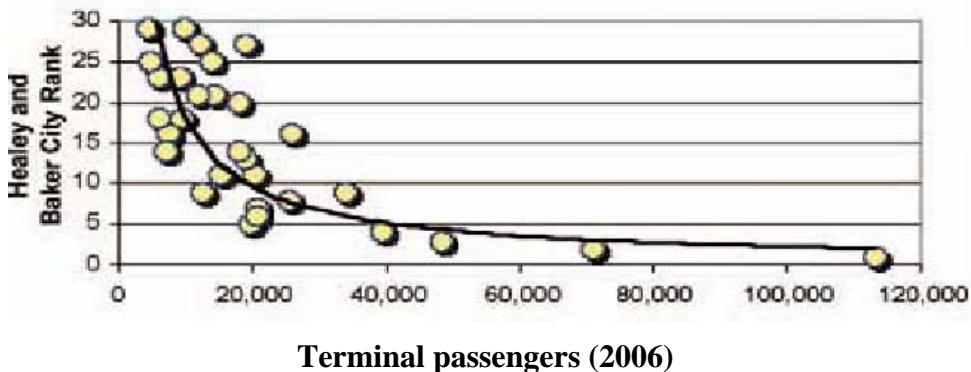
The social and economic importance of air transport in Europe will grow after the last EU enlargement. Although some airport economic impact assessments have attempted to quantify the catalytic impacts, this can be a difficult endeavor, as the wider impacts relate to the effect of airports on the operation of the whole economy. It can be quite intricate to isolate what is attributable to the airport and what is attributable to a wide range of other factors. Generally, the catalytic impacts, particularly business impacts, are best discussed in qualitative terms, illustrating the link between airports, access to air services and the

functioning of the wider economy. This includes other measures, such as the value or weight of exports by air as a proportion of total national exports, journey time savings as a result of the opening of a new airport, or the development of new capacity or services at an existing airport. The qualitative approach to the discussion of the catalytic impacts can draw on a wide range of other evidence that does not measure the specific impact of airports, but of the overall business location factors. These studies include:

- surveys of attitudes to business locations, such as the annual Healey and Baker survey of Europe’s top business cities;
- surveys of key business location factors, such as the work undertaken by the University of Reading in the UK; and
- surveys of the impact of airports on company location decisions, such as work on Hartsfield International Airport in Atlanta.

The 2002 **Healey and Baker survey**<sup>4</sup> demonstrates that external transport links remain an important component of company location decisions. In this most recent survey, availability of qualified staff is now regarded as the most important factor. Access to markets and external and international transport links were also regarded as “absolutely essential” to businesses making location decisions. Although air transport links are not explicitly included as a measure in the survey, there is a good correlation between the number of passengers handled by an airport and the ranking of the city for external transport links.

**Figure 1. Correlation between airport passengers and the attractiveness of city external transport links.**



Source: *Cheshire and Gordon, Centre for the Study of Advanced European Regions, University of Reading (2007).*

<sup>4</sup> Source: Cheshire and Gordon, Centre for the Study of Advanced European Regions, University of Reading (1993).

A similar survey in Ireland showed that for large multi-national companies based in Ireland, air and sea facilities were the sixth most important factor in their overall competitive performance.

The measures which apply to the attraction of new companies and businesses will also apply to the ability of indigenous businesses to operate competitively and will thus impact more widely on the performance of the economy. It is clear that air service accessibility will have an important influence on wider economic growth. This can apply at a national, regional, sub-regional or local level. Oxford Economic Forecasting estimated that the impact of aviation growth on the output of the UK economy was of the order of £550 million per year. This equated to approximately 3% of the trend increase in GDP over and above the direct contribution of the air transport industry.

A key example of a single airport operating at a national level is the **Schiphol Mainport** concept. For many years, the airport at Amsterdam Schiphol and the sea port at Rotterdam have been regarded as the main drivers of the economic growth of the Netherlands as a trading nation. National policies towards the development of the Airport and the national airline KLM have specifically promoted Schiphol's role as a global hub airport in order to maximize the number of destinations served from the airport, underpinned by connecting passenger traffic. In this way, the network connectivity of the Netherlands has been maintained and enhanced, facilitating the transition of the economy into a modern industrial structure, driven by high technology companies. Schiphol itself is being developed as an 'Airport City', providing a counterweight growth pole to the city of Amsterdam itself. In particular, the airport area is developing as a logistics centre, continuing Schiphol's role in facilitating trade.

At a national level, the number of direct air service connections is regarded, for example, as a key measure of the competitiveness of the Swiss economy. It has been estimated that passengers would be prepared to spend between €87 and €115 more for a direct flight from Zurich Airport compared to an indirect routing. From this information, it was estimated that the value to the Swiss economy of having direct routes from Switzerland was €773 million in 2002. The same study noted that high value, banking, information technology, type firms were prepared to pay a premium to locate near to Zurich Airport, or the city centre, whilst logistics firms were also attracted to the areas close by, in part due to convenient road, as well as air access. The lack of national connections is illustrated by the studies undertaken also in Switzerland, examining the impact of the loss of direct services from **Zurich Airport** on the Swiss economy, following the demise of Swissair.<sup>5</sup> This suggests that there is a role for concerted regional planning to ensure that the benefits of the airport can be exploited by optimizing the opportunities for high value business location.

Airports can act at a regional as well as at national level. A study for **Frankfurt Airport** in 1999 was set out to estimate the overall impact of the Airport on the regional economy of Hesse. This paper specifically looked at the impact of improved air connections on the productivity of the wider economy.

---

<sup>5</sup> York Aviation Study: *The social and economic impact of airports in Europe*, jan. 2004, p 23

In other cases, the development of air services may follow the development of the local economy. For example, the purchase of Renault Truck by Volvo in 2001 is creating demand for air travel between **Gothenburg** and **Lyon**, which is presently being satisfied, in part, by air taxi services. For **Hamburg Airport**, there is synergy between the role of the airport and that of the port. Air service connections are also vital to cities holding a large number of trade fairs. Examples of this activity include **Düsseldorf Airport**, **Hanover Airport** and **Birmingham Airport**. Intercontinental links can be particularly important in this regard. In Düsseldorf's case, there have been innovative developments by Privatair flying business class only services from the airport to New York and Chicago, in response to market needs.

Air travel is essential for many companies to function. A survey in 2003 at **Dublin Airport** found that 93% of the top Irish companies used Dublin Airport for business travel, with on average 108 business trips per annum per company. Even a relatively small airport, like **London City**, can have a very substantial economic impact related to concentrations of local business activity. London City provides short haul European connections to the financial and business centre in the 'City of London'. As such, it has a wider economic impact, greater than its scale of operations would indicate.

Connectivity and access to air services is even more important in more remote parts of countries, which may not have other location advantages. The area around Ireland's **Shannon Airport** has a high proportion of multi-national manufacturing firms, with a high reliance on air transport. Improved surface access links between the airport and its catchment area are seen as important to unlocking the full economic potential of the airport.

One way of measuring the linkage between business and air service accessibility is through an examination of the expenditure of companies on air transport. This information can often be obtained from national or regional input-output tables.

### 3. Air freight

There is also evidence that air transport accessibility can assist innovation in a region. Companies using high technology often have a high demand for air travel and for shipping products and components by air freight. As a result, airports can assist regions in establishing clusters of these companies, with consequent benefits for the competitiveness of the local economy.

Globalization of manufacturing, coupled with the need for increased productivity has meant that supply chain logistics are critical to business success. Companies are no longer willing to hold large quantities of unproductive stock and there is a growing need for just in time deliveries of goods from suppliers and to the end customers. The use of air freight as a means of transport is increasing - particularly for high-value, low-weight goods, or those, such as medical products, requiring urgent transport. For example, air freight accounted for 39% by value of Irish exports in 2001. These goods tend to be primarily technology intensive, high value goods. For Austria, 5.5% by value of exports

were carried by air. For the UK, the equivalent percentage is 20% by value. Globally, OECD estimates that up to a third in value of world trade in merchandise travels by air.

Express freight activity is characterized by being high valued added and is the fastest growing sector. It is increasingly important to the **manufacturing sector**, using the night period to deliver goods for next day use in assembly or to the customer.

The integrated service provided by the operators adds to the efficiency and productivity of other industries by relieving them of the burden of organizing transport. Moreover, the use of express delivery enables companies to minimize inventories of stock and increases the productivity of capital. The express industry *“offers European businesses a service which gives them the opportunity to streamline their supply chains, leading to reduced delivery times, faster responses to market needs, reduced stockholding and savings in warehousing.”* (Cheshire and Gordon, Centre for the Study of Advanced European Regions, University of Reading, 1993, *The Production of Space*) In addition, the development of express freight hubs at airports can represent substantial investments in their own right, with accompanying wider economic impacts. For example, the Fedex hub at **Paris CDG Airport** represents an investment of over €200 million. A study in France found that express freight services are frequently used by 44% of businesses, including 74% of large companies. 44% of shipments were finished goods, 14% parts and 22% raw materials. Next day delivery is seen as vital by 60% of users, with 20% of companies saying that express delivery was critical to achieve 25% or more of their sales. Failure to allow continued growth in night shipments, including those by air, could put at risk 205,000-465,000 employees in the French industry as a whole, €105,000 of exports and €6 million of GDP.

#### **4. The direct and measurable impact of airport activities**

Airports support employment directly on-site and in the surrounding area, but also indirectly in the chain of suppliers providing goods and services. In addition, the income earned in these direct and indirect activities generate demand for goods and services in the economy, which supports further employment.

In 2004, we estimate that **total on-site employment at airports reporting traffic to ACI EUROPE was around 1.2 million**. In addition, we estimate that there are a further 0.2 million direct airport related jobs located off-site at Europe’s airports. Nearly two-thirds (64%) of employment comes from airlines, handling agents and aircraft maintenance, with the remainder split between airport operators (14%), in-flight catering, restaurants and bars and retailing (12%), air traffic control and control agencies (6%), freight (1%) and other activities such as fuel companies and ground transport operators (3%).

The evidence suggests that European airports currently support, on average, around **950 on-site jobs per million passengers (workload units) per annum**. This is lower than the number observed in 1998 (the ‘typical’ 1000 jobs per million passengers ratio), indicating the success of measures taken by airports to reduce costs and increase productivity, despite increases in security measures. Other factors include the

development of *no-frills* carriers and the drive towards lower costs throughout the industry, particularly in the airline sector, resulting in productivity improvements across the board. They are vital to the development of remote regions of the Europe. Quite simply, without air service access, many regions in Europe would be denied participation in the modern world. This would have profound ‘quality of life’ implications. There are many examples of airports engaging in programs to ensure that their positive social impact is maximized. Such programs include initiatives in education and training, as well as local cultural and sporting programs.

Airports can make a substantial contribution to the overall economy of the areas that they serve, when the combined effect of their direct, indirect and induced impact is taken into account. Estimates vary in the range 1.4-2.5% of GDP, excluding tourism impacts. It was estimated that, in 2004, operations at **Vienna Airport** contributed 2.2% to the economy of Burgenland, Lower Austria and Vienna, or 1% of national Gross Domestic Product (GDP). A study for Aéroports de Paris has estimated that activity at the Paris airports accounts for 2.5% of the GDP in the Île de France and 2% of regional value-added. **Tallin Airport** has estimated that the total of its direct, indirect and induced activity accounts for 7.42% of national GDP, including tourism expenditure. On a similar basis, the impact of the **Rome Airports** in the Lazio area is estimated to account for 10.1% of the region’s economic value, although this included substantial tourism impacts.

Restricting airport capacity or pricing off air travel demand could have severe economic or social consequences. Studies suggest that failure to increase capacity to meet demand could **reduce GDP at a national or regional level by 2.5 to 3%**, taking all impacts into account, although this will be heavily dependent upon the level of restrictions applied. Based on forecast growth in passenger and freight traffic at Europe’s airports, direct employment at airports is expected to grow by almost 200,000 jobs between 2001 and 2010. However, restricting growth in demand, through limits on capacity or other means, would have the effect of reducing this growth in jobs, while more severe restrictions could result in a net loss of direct jobs as productivity improvements negate the benefits of traffic growth.

## **5. Airports driving tourism development**

For the EU as a whole, tourism accounts for 5% of total employment and of GDP and as much as 30% of the total external trade in services. If transport and distribution trades are included, the figures rise to 20 million jobs and 12% of GDP. Tourism is expected to be a growth sector in the EU economy with as much as 25% growth in employment anticipated over the next 10 years. Globally, it is estimated that tourism accounts for 195 million jobs and 7.6% of total employment in 2007.

Tourism is an increasingly important sector in the economies of many European countries. For some countries, air transport is the principal means by which tourists access the country.

Four of the EU countries are amongst the top ten world tourist destinations, along with 3 of the new EU Member States: France, Poland, Spain, Hungary, Italy, Czech Republic, United Kingdom.

Whilst for some EU countries, there is a negative balance of payments in tourism (greater expenditure by residents abroad than by inbound visitors), for others there is a significant direct positive contribution to the economy. The EU acknowledges, nonetheless, the social benefits of tourism: *“Tourism’s economic contribution is not the only indicator of beneficial impact. Travel and leisure activities are also social factors, since tourism is no longer an activity for the privileged few, but rather a widespread experience for the great majority of EU citizens.”*

Albania, Austria, Bulgaria, Croatia, Cyprus, Czech Republic, Estonia, Hungary, France, Greece, Italy, Liechtenstein, Lithuania, Malta, Portugal, Slovakia, Slovenia, Spain, Switzerland and Turkey all maintain balance of payments surpluses in tourism. Other countries earn over €10 billion a year from tourism, including Austria, France, Germany, Greece, Italy, Spain, Switzerland and United Kingdom.

In the European periphery, tourism and its economic impact is relatively unstable. South-eastern Europe (much of former Yugoslavia, Albania, Moldova) and much of the former Soviet Union has stagnated or even declined. Private sector under-funding and infrastructural shortcomings have persisted. The semi-periphery with core potential comprises: the Baltic States, fuelled by low cost carriers, 2004 accession and current Western curiosity and investment, Bulgaria and Croatia showing mass market resurgence and foreign investment in businesses, land and property and, in the last place, Romania, unattractive from foreign TO point of view.

Traditionally, charter carriers have played a major role in facilitating the development of tourism in Europe: much inbound tourism has been driven by charter flights, particularly from the Northern European countries to the Mediterranean area. In 2005, UK-Spain was the largest country to country air passenger flow in Europe, accounting for 11.5% of all passengers carried. In 2005, Europe’s charter airlines flew almost a million flights in the European airspace. They employed over 50,000 people and carried 118 million passengers to their destinations, using a 650-strong fleet of aircraft Low-cost, no frills carriers are now opening up new markets to tourism and accelerating the growth in tourism, even in traditional markets, such as UK-Ireland.

Airports play a major role in facilitating the development of inbound tourism. This is particularly the case for more remote or island destinations. For example, 70% of foreign tourists to the United Kingdom arrive by air, 21% of all foreign tourist arrivals in Greece travel through **Athens Airport** and 32% of foreign tourists to the Lisbon area arrive through **Lisbon Airport**. **Vienna Airport** plays a key role in tourism to Austria. Approximately 37% of visitors to Vienna travel by air, remaining for an average of 4.7 days and spending around €130 per day for leisure travelers and €126 per day for business travelers.

Unlike broader catalytic impact, tourism impacts are relatively easier to quantify and, hence, are included in some airport economic impact studies through detailed investigations into the nature and contribution of tourism. One example where a detailed quantification of tourism impact has been carried out is **Nice Airport**, which treated

tourism impact as an indirect impact of the airport. This showed that, at a regional level, tourism expenditure from visitors arriving by air can be significant. This research focused on identifying the specific regional impact of visitors using the airport. Of the 8,997,193 passengers that used Nice Airport in 2000, 1,995,630 were overseas visitors, traveling for either business or leisure purposes, and staying within the Alpes-Maritime Region. Each of these visitors stayed an average of 7.9 nights and spent €93 per night.

**Figure 2 Tourism regional income due to an airport**



Source: York Aviation Study: *The social and economic impact of airports in Europe*, Jan. 2004

Tourism arrivals by air are vital especially to island economies. For example, over 80% of tourists arriving at Greek islands such as Crete, Rhodes and Corfu travel by air. The development of tourism, and the benefits it brings, would not have been possible **without the development of direct air service connections**.

The advent of no frills carriers is particularly stimulating the development of new tourism markets based around short breaks and flexible low-cost travel arrangements. Such developments are often strongly supported by the communities in the vicinity of these smaller airports, because of the overall benefits to the local economy.

## 6. Conclusions

Tourism is irrevocably bound up with the concept of security. Tourist behavior and, consequently, destinations, are deeply affected by security perception and the management of safety, security and risk. Although “Tourism as a Force for Peace” has been a popular positive message relayed by the industry, consultants and some academics in recent years, the reality is that tourism has very little influence on peace and security issues, at least at the macro level, and that tourism is far more dependent on peace than peace is on tourism.



**Airports** play a major role in making the development of inbound tourism possible. Tourism can generate substantial income and employment in Europe's regions. Whilst it is not possible to attribute this income and employment, directly or indirectly, to the existence of an airport, it constitutes however, another powerful contribution to the **catalytic impact**. Even for major European cities, **air travel can account for a third or more of their foreign visitors**. The advent of low cost carrier services is accelerating the development of tourism in many places.

The most important role of airports is related to the connectivity they provide, to education mobility, to rising standards of living and quality of life, which allow the European economy and society to flourish.

Policy-makers must better acknowledge the social benefits provided by airports in terms of the freedom, safety and security of movement ..... and Mackinder was right: "*Air power depends absolutely on the efficiency of its ground organization*".

## Appendix A

Summary of information received	
Airport	Reports
Aberdeen	y
Amsterdam	y
Athens	
Baie Mare	
Bergamo (Orio al Serio)	
Birmingham	y
Bournemouth	y
Brussels	y
Budapest	
Cardiff	y
Copenhagen	
Cork	y
Dublin	y
Dusseldorf	y
East Midlands	y
Edinburgh	y
Exeter	y
Frankfurt	y
Glasgow	
Gothenburg	
Hamburg	y
Hannover	y
Helsinki	y
Humberside	y
Klagenfurt	
Koltsovo	
Larnaca	
Leeds/Bradford	y
Limoges	
Lisbon	y
Ljubljana	
London Ashford	
London City	y
London Gatwick	
London Heathrow	
London Luton	y
London Stansted	
Lyon	y
Maastricht	
Malmö	
Manchester	y
Milan Malpensa	y

Munich	y
Nice	y
Norrkoping	
Paris (CDG + ORY)	y
Rome (FCO + CIA)	y
Rostock	y
Shannon	y
Stockholm (ARN + BMA)	y
Stuttgart	
Tallinn	y
Toulouse	
Vaxjo	y
Vienna	
Zurich	

# **THE POLISH MARKET OF PRIVATE EQUITY AND VENTURE CAPITAL INVESTMENTS IN 2001 – 2006**

**IZABELA PRUCHNICKA-GRABIAS<sup>1</sup>**

## **Introduction**

Although only a small fraction of corporate investments is financed through venture capital, research on venture capital is both important and challenging.<sup>2</sup> Private equity means buying shares in companies which are not listed on any exchange. Thus, these are investments on the private capital market. Their characteristic feature is usually mid-term and long-term character and the fact that the investor involves in managing the company that he co-finances. If such investments are made in early development stages of companies, they are classified as venture capital. However, many publications use these two names (venture capital and private equity) as substitutes. The author also uses this terminology.

The aim of the paper is to show the sector structure of pe/vc investments in Poland as well as its changes in 2001 – 2006. The author also presents some examinations on benefits from this kind of investments. These studies let conclude that venture capital investments in Poland are diversified into different sectors, which is a positive effect. However, they also pay attention to the problem of attracting pe/vc investments as a significant part of the future development of the Polish economy.

## **Venture Capital Characteristics**

The modern venture capital industry was born in the United States in 1946 and developed apace throughout the next 60 years.<sup>3</sup> Venture capital invests in start-up companies anywhere from initial financing to last financing before an exist is in sight. Most start-ups have

---

<sup>1</sup> Ph.D., Warsaw School of Economics

<sup>2</sup> J. Vauhkonen, Essays on Financial Contracting, Bank of Finland Studies E:30, 2004, p. 7.

<sup>3</sup> R.Pearce, S. Barnes, Raising Venture Capital, John Wiley & Sons, Ltd, Chichester 2006, p.15.

medicore or poor performance, but those that succeed may provide outstanding returns.<sup>4</sup> Thus, venture capital on one hand can be a profitable business, but on the other hand it is connected with a high level of risk, low liquidity, as well as low flexibility as far as inflows and rates of return are concerned. This means that if an investor decides for a venture capital, he or she must be aware of the fact that it may not bring the results assumed earlier and what's more, there is a high probability that it will not. Chances are better when one invests in sectors with wide perspectives.

According to A. Metrick, a venture capital has five main characteristics:

1. A venture capital is a financial intermediary, meaning that it takes the investors' capital and invests it directly in portfolio companies.
2. A venture capital invests only in private companies. This means that once the investments are made, the companies cannot be immediately traded on a public exchange.
3. A venture capital takes an active role in monitoring and helping the companies in its portfolio.
4. A venture capital's primary goal is to maximize its financial return by exiting investments through a sale or an initial public offering (IPO).
5. A venture capital invests to found the internal growth of companies.<sup>5</sup>

In order to define a venture capital in a more precise way, it would be interesting to emphasize what venture capital is not. As S. Bloomfield states, venture capital is not:

- secured – there is no guarantee of recovery of the investment in the event of failure of the business;
- time limited – while there is a horizon (typically three to five years) for the calculation of the rate of return available to the investor, there is considerable uncertainty as to that being achieved;
- certain – the investment is always at the risk of market forces and managerial capability;
- liquid – once in it is very difficult to get the money out again readily;
- suitable for a “core” investment policy – venture money is capable of high rewards but is not intended for the provision of basic and safe returns.<sup>6</sup>

Many years of experience and scientific research in different countries show that companies strengthened with venture capital beat their competitors: they develop quicker than others, increase employment and introduce more innovations.

According to the research of companies benefiting from venture capital in EU countries:

- 90% of such companies increased the employment. They created on average 46 new jobs. Because the majority of them are small and medium enterprises, the growth was high, often a few times bigger than before.

---

<sup>4</sup> L. Tvede, *Business Cycles. History, Theory and Investment Reality*, Third Edition, John Wiley & Sons, Ltd, Chichester 2006, p. 386.

<sup>5</sup> A. Metrick, *Venture Capital and the Finance of Innovation*, John Wiley & Sons, New York 2007, p. 3.

<sup>6</sup> S. Bloomfield, *Venture Capital Funding. A Practical Guide to Raising Finance*, London and Sterling, VA, London 2005, p.22.

- More than 90% of companies admit that without venture capital they would develop less quickly or they would even cease to exist.
- Almost 60% of companies admit that their profits growth rate was higher than in competitive firms.<sup>7</sup>

Studies have shown that private equity is good for economies in the medium-term. In particular, this is attributed to the strong alignment of interests between Private equity General Partners and portfolio company managements. Private equity General Partners recognise that appropriate financial engineering does not in isolation provide longer term value creation.<sup>8</sup> Some authors proved that there is a positive correlation between venture capital and profits generated by companies, their innovation, as well as good effects for the whole economy.<sup>9</sup> Besides, there are many publications that prove that venture capital influences knowledge creation in companies. Thus, taking all above mentioned factors, it is indisputable that venture capital has many good sides to companies and to the economy itself.

It should be noted that investors can't jump in and out of existing private equity funds at will. Most of these funds will require approval of their investors, and an investor who wants to enter an existing private equity fund during an emerging bull market may only be able to do so if he can find someone else who wants to leave, and if the fund approves the change of ownership of the shares.<sup>10</sup>

As far as a private equity fund makes a decision to invest in a company and the company decides to take advantage of financial means offered by the fund, partners negotiate terms of agreement which specifies their relations and conditions of cooperation. Funds usually want a wide range of collateralisation because they want their money to be spent in a reasonable way and their investment not to lose its value. Sometimes it happens that the company considers fund's requirements as too rigid. Generally, the more motivated the company is, the more strict conditions it will accept.

Besides, future partners should agree at the beginning the terms of ending their cooperation. Plans of the company may be different. Some companies intend to take other firms over or launch new products into the market. Some others plan to develop much enough to be taken over by competitive corporations. There are also firms that want to start quotations on the domestic or even foreign stock market. It is important then both for the company and for the venture capital fund to set all the details and to be aware of the final goal. As soon as it is realised, the fund will finish the investment and starts to look for another one. The contract usually specifies what time is needed to achieve the assumed results and usually it is about ten

---

<sup>7</sup> Statistical Yearbook 2002, Polish Private Equity Association, Warsaw 2003, p.4.

<sup>8</sup> Private Equity Going Public, Global Private Equity Report 2006, PriceWaterhouseCoopers, p.9.

<sup>9</sup> See f.ex. A. Brav, P. Gompers, Myth or Reality? The Long-Run Underperformance of Initial Public Offerings: Evidence from Venture and Non-Venture Capital-Backed Companies, *Journal of Finance* 52(5), 1997, p. 1791 – 1821; D. Engel, The Impact of Venture Capital on Firm Growth: An Empirical Investigation, ZEW Discussion Paper 02 – 02, 2002; D. Engel, M. Keilbach, Firm Level Implications of Early Stage VC Investments: An Empirical Investigation, ZEW Discussion Paper 02 – 82, 2002; R. Fehn, T. Fuchs, Capital Market Institutions and Venture Capital: Do They Affect Unemployment and Labour Demand? *Applied Economics Quarterly* 50(4), 2004, p. 393 – 422.; T.Hellmann, M. Puri, The Interaction between Product Market and Financing Strategy: The Role of Venture Capital, *Review of Financial Studies* 13(4),2000, p. 959 – 984; S. Kortum, J. Lerner, Assessing the Contribution of Venture Capital to Innovation, *Rand Journal of Economics* 31(4), 2000, p. 674 – 692; J. Lerner, Boom and Bust in the Venture Capital Industry and the Impact on Innovation, *Federal Reserve Bank of Atlanta Economic Review*, Fourth Quarter 2002b; W.L. Megginson, K.A. Weiss, Venture Capitalist Certification in Initial Public Offerings, *Journal of Finance* 46(3), 1991, p. 879 – 903.

<sup>10</sup> L. Tvede, *Business Cycles. History, Theory and Investment Reality*, Third Edition, John Wiley & Sons, Ltd, Chichester 2006, p. 388.

years, however it may be set differently if it is necessary. For the venture capital fund the whole thing is to achieve the assumed rate of return in the specified period of time.

## **The Analysis of Venture Capital Investments Structure in Poland**

This part of the paper analyses pe/vc investments in Poland by sector both in total values and as a percent of the total. At the beginning, the amount of investments is examined, whereas in the next part the author makes studies on the number of companies benefiting from vc/pc.

Traditionally, venture capital investments have been concentrated in two broad sectors: health care and information technology (IT), where the latter sector is defined to include the communications, semiconductor, software, and hardware industries. This concentration is no accident: because venture capitals invest in small companies with the potential to quickly grow large, they need to look for business with large, addressable markets.<sup>11</sup> If we look into the structure of Polish investments, it can be noticed that according to the United States tendencies, venture capital is the most strong in a telecommunications/media sector and other computer related sectors, however as far as health care is concerned, venture capital is present in this sector, however it is not as noticeable as in the former branches. It should be stressed that the distribution of investments by sectors is diversified and changes all the time, although telecommunications/media is the most important sector in all analysed years i.e. from 2001 to 2006. Another significant sector, where pe/vc goes to, is consumer related and other manufacturing. These three mentioned earlier sectors are steadily the most important receivers of venture capital. Sectors where vc/pe is rarely present are: industrial products and services, biotechnology, other electronics-related or industrial education.

As far as the total pe/vc investment is concerned, it was about the same level in 2001 – 2004, however in 2005 it decreased suddenly by almost four times to 153 981 million PLN to increase again in 2006 to 293 723 million PLN, which was by two times only.

Speaking about the structure of investments, in 2001 the investments in the telecommunications and media sector were 46,4% of all venture capital investments, which is an impressive number (see table 2). If one analyses the value of venture capital investments in 2001 – 2006 (see table 1), it is easily noticeable that their values fluctuate. In 2002 investments in the telecommunications/media sector decreased dramatically to 63 080 million PLN in comparison with 2001 when they reached 256 146 million PLN, to increase again in 2003 but they weren't still as impressive as two years earlier. In 2004 they went up again to 199 306 million PLN, which was the effect of Poland's joining the European Union, however in 2005 they went down back to 8 606 million PLN, having the minimum level in the whole examined period. In 2006 they were almost twice as much as a year earlier, but they still did not achieve the 2001 level.

The second sector where venture capital investments are most developed is consumer related sector which in the best 2005 year accounted for almost 19% of the total value of investments. The amount of venture capital investments in this branch in 2001 was 49 020 million PLN and grew suddenly to 159 373 million PLN in 2002 in order to note a small down movement in 2003 reaching 148 959 million PLN and a dramatic reduction in 2004 to 23 835 million PLN. In 2005 venture capital investments in consumer related sector grew more than twice in comparison to the previous year, however this tendency did not last for a long time because in 2006 their volume was zero.

---

<sup>11</sup> A. Metrick, *Venture Capital and the Finance of Innovation*, John Wiley & Sons, New York 2007, p. 17.

Another important venture capital sector in Poland is other manufacturing that in 2005 had an almost 25% share in the total value of investments. Venture capital investments in this sector were in 2001 at the level of 80 463 million PLN. They were decreasing in 2002 – 2003 in order to increase in 2004 to 77 790 million PLN and diminish again in 2005 to 38 209 million PLN. In 2006 they increased up to 60 633 million PLN but they were still lower than in 2001, 2002 or 2004.

Table 1. PE/VC investment in Poland by sector [million PLN]

PLN (thousands)	Amount of Investment					
	2001	2002	2003	2004	2005	2006
Telecommunications/media	256 146	63 080	173 719	199 306	8 606	164 977
Computer Related	4 379	17 408	523	0	28 376	0
Other Electronics-related	0	2 668	6 858	0	0	0
Biotechnology	0	2 194	0	0	0	0
Medical/Health-related	27112	16 165	27 082	4 770	114	3 046
Energy	4 157	31 058	30 419	16 626	0	9 219
Consumer related	49 020	159 373	148 959	23 835	65 785	0
Industrial Products and Services	2 389	7 689	0	943	0	0
Chemicals and Materials	34 890	0	7 826	10 202	0	0
Industrial Automation	0	8 290	0	0	0	0
Other Manufacturing	80 463	72 049	17 247	77 790	38 209	60 633
Transportation	0	27 243	5 425	4 285	9 675	7 460
Financial Services	2 517	5 368	138 605	97 767	3 216	41 437
Other Services	90 921	14 681	6 388	48 600	0	103
Agriculture	0	0	150	2 367	0	0
Construction	0	26 257	8 780	103 067	0	5 001
Other	307	0	13 581	0	0	1 847
<b>Total Investment</b>	<b>552 301</b>	<b>453 522</b>	<b>585 561</b>	<b>589 558</b>	<b>153 981</b>	<b>293 723</b>
<b>Subtotal High-Tech</b>	<b>185 634</b>	<b>36 181</b>	<b>181 105</b>	<b>199 306</b>	<b>36 983</b>	<b>164 977</b>

Source: prepared by the author on the basis of European Venture Capital Association data.

Table 2. The amount of PE/VC investment in Poland by sector as a percent of the total

PLN (thousands)	%					
	2001	2002	2003	2004	2005	2006
Telecommunications/media	46,4	13,9	29,7	33,8	5,6	56,2
Computer Related	0,8	3,8	0,1	0,0	18,4	0,0
Other Electronics-related	0,0	0,6	1,2	0,0	0,0	0,0
Biotechnology	0,0	0,5	0,0	0,0	0,0	0,0
Medical/Health-related	4,9	3,6	4,6	0,8	0,1	1,0
Energy	0,8	6,8	5,2	2,8	0,0	0,0
Consumer related	8,9	35,1	25,4	4,0	42,7	3,2
Industrial Products and Services	0,4	1,7	0,0	0,2	0,0	0,0
Chemicals and Materials	6,3	0,0	1,3	1,7	0,0	0,0
Industrial Automation	0,0	1,8	0,0	0,0	0,0	0,0



Other Manufacturing	14,6	15,9	2,9	13,2	24,8	20,7
Transportation	0,0	6,0	0,9	0,7	6,3	2,5
Financial Services	0,5	1,2	23,7	16,6	2,1	14,1
Other Services	16,5	3,2	1,1	8,2	0,0	0,0
Agriculture	0,0	0,0	0,0	0,4	0,0	0,0
Construction	0,0	5,8	1,5	17,5	0,0	1,7
Other	0,1	0,0	2,3	0,0	0,0	0,6
<b>Total Investment</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>
<b>Subtotal High-Tech</b>	<b>33,6</b>	<b>8,0</b>	<b>30,9</b>	<b>33,8</b>	<b>24</b>	<b>56,2</b>

Source: prepared by the author on the basis of European Venture Capital Association data.

If one looks at the number of companies in pe/vc investments in Poland (see table 3), conclusions about the most and least important sectors are almost the same as in the case of investment volume which was deeply analysed in the earlier part of the text and tendencies in the analysed years differ a little. To be exact, when one analyses the number of companies in pe/vc investments in Poland, it turns out that the two most important sectors are telecommunications and consumer related (as in the case of the analysis of the value of investments) whereas the third most significant sector are other services, although its role decreased year by year. If one interprets it in per cent of the total (see table 4), the biggest share has telecommunications/media sector (varying in different years from 17,6% to 37,3%. The second reward can be given to consumer related accounting for 5,9% to 28% percent in different years, and the third place goes to other services whose share ranges from 0 to 21,6% of the total number of companies benefiting from vc/pe.

Table 3. The number of companies in PE/VC investment in Poland in real numbers

PLN (thousands)	Number of Companies					
	2001	2002	2003	2004	2005	2006
Telecommunications/media	21	21	13	6	7	7
Computer Related	3	9	1	0	4	0
Other Electronics-related	0	3	1	0	0	0
Biotechnology	0	1	0	0	0	0
Medical/Health-related	3	3	2	1	1	1
Energy	1	4	1	1	0	0
Consumer related	3	12	7	5	7	5
Industrial Products and Services	2	4	0	2	0	3
Chemicals and Materials	1	0	1	6	0	0
Industrial Automation	0	1	0	0	0	0
Other Manufacturing	4	9	6	2	1	3
Transportation	0	4	1	1	2	2
Financial Services	4	1	5	7	2	5
Other Services	12	8	1	1	0	1
Agriculture	0	0	1	1	0	0
Construction	0	5	4	1	0	1
Other	1	0	4	0	1	9
<b>Total Investment</b>	<b>57</b>	<b>86</b>	<b>48</b>	<b>34</b>	<b>25</b>	<b>37</b>

<b>Subtotal High-Tech</b>	<b>22</b>	<b>16</b>	<b>15</b>	<b>6</b>	<b>11</b>	<b>7</b>
---------------------------	-----------	-----------	-----------	----------	-----------	----------

Source: prepared by the author on the basis of European Venture Capital Association data.

Table 4. The number of companies in PE/VC investment in Poland as a percent of the total

PLN (thousands)	%					
	2001	2002	2003	2004	2005	2006
Telecommunications/media	37,3	24,4	27,1	17,6	28,0	18,9
Computer Related	5,9	10,5	2,1	0,0	16,0	0,0
Other Electronics-related	0,0	3,5	2,1	0,0	0,0	0,0
Biotechnology	0,0	1,2	0,0	0,0	0,0	0,0
Medical/Health-related	5,9	3,5	4,2	2,9	4,0	2,8
Energy	2,0	4,7	2,1	2,9	0,0	0,0
Consumer related	5,9	14,0	14,6	14,7	28,0	13,5
Industrial Products and Services	3,9	4,7	0,0	5,9	0,0	0,0
Chemicals and Materials	2,0	0,0	2,1	17,6	0,0	0,0
Industrial Automation	0,0	1,2	0,0	0,0	0,0	0,0
Other Manufacturing	6,9	10,5	12,5	5,9	4,0	8,1
Transportation	0,0	4,7	2,1	2,9	8,0	8,1
Financial Services	6,9	1,2	10,4	20,6	8,0	5,4
Other Services	21,6	9,3	2,1	2,9	0,0	13,5
Agriculture	0,0	0,0	2,1	2,9	0,0	0,0
Construction	0,0	5,8	8,3	2,9	0,0	2,7
Other	2,0	0,0	8,3	0,0	4,0	2,7
<b>Total Investment</b>	<b>100,0</b>	<b>100,0</b>	<b>100,0</b>	<b>100,0</b>	<b>100,0</b>	<b>100,0</b>
<b>Subtotal High-Tech</b>	<b>38,6</b>	<b>18,6</b>	<b>31,3</b>	<b>17,6</b>	<b>44,0</b>	<b>18,9</b>

Source: prepared by the author on the basis of European Venture Capital Association data.

As Schertler, using panel data techniques proves, countries with a high amount of total knowledge capital are likely to generate more business start-ups in high-technology industries than countries with a low amount of knowledge capital. This is because the founder of a high technology start-up must be highly skilled and because the founders need employees who are highly skilled, as well.<sup>12</sup> This may mean that rather poorly developed venture capital sector in Poland results from low expenditures on research and development. If they are not increased, it will be difficult to stimulate it in a long run.

Moreover, venture capital is influenced by macroeconomic factors. This problem was examined by Paul A. Gompers and Josh Lerner on the basis of the United States in 1972 – 1994.<sup>13</sup> The authors conclude that the most important factors are those that influence demand. Decreasing rate of income tax resulted in the increased amount of capital possessed by venture capital funds. The interesting matter was the fact that this rule applied both to institutions paying taxes and to those which are tax-free like pension funds or foundations. Demand for venture capital is created thanks to the development of the whole economy. It

<sup>12</sup> A. Schertler, Knowledge Capital and Venture Capital Investments: New Evidence from European Panel Data, German Economic Review 8(1), 2007, p.66.

<sup>13</sup> P.A. Gompers, J. Lerner, What Drives Venture Capital Fundraising?, NBER Working Paper No. 6906, 1999.

helps to create new companies which then use venture capital. Supply depends for example on risk free interest rate. If interest rates are rather high, venture capital investors are not eager to risk more than that. This may be one of the reasons for poor development of domestic venture capital in Poland. However, interest rates have been going down for a few years, which gives optimistic views for the future.

### Venture Capital Divestments in Poland

Venture capital funds take up the investment in order to achieve certain, specified earlier goals and as soon as it is done, they set new challenges or exit the investment in order to find another firm which will allow them to realise expected rates of return. Divestments are natural in this field. It should be then emphasised that divestments are a normal part of the whole investment process and can not be interpreted differently. Their analysis in 2001 – 2006 provides with conclusions concerning the most popular types of exiting the investments by venture capital funds.

Table 5. Divestment by Polish PE/VC fund managers at historical cost in 2001 - 2006 [million PLN].

Type	2001	2002	2003	2004	2005	2006
Trade sale	96	161	47,0	123,8	74,1	19,0
Write-Off	No data	No data	62,0	77,5	8,1	0,0
Stock Exchange	11	98	109,0	108,8	22,0	74,8
Loan Repayment	No data	No data	2,0	20,4	0,3	17,2
Sale to Another VC Fund	7	22	18,0	16,8	1,1	21,1
Sale to Financial Institution	No data	No data	0,0	10,0	0,6	0,0
MBO	No data	No data	151,0	39,4	1,3	4,4
Other	28	8	117,0	5,4	8,1	3,5
Total	142	289	506	402,1	115,6	140

Source: prepared by the author on the basis of European Venture Capital Association data.

The total sum of divestments was growing from 2001 to 2003 and in 2004 started to fall down in order to increase in 2006 again (see table 5). In 2001 the most popular method of exiting the venture capital investments were trade sales. They accounted for 67,6% of exits. The least popular method in this period were sales to another venture capital fund which were equal to 4,9% of the total. In 2002 these were also trade sales that were the most popular method of divestments, accounting for 55,7% of total exit value. Management Buy Outs were the most important way of exiting the investment in 2003 accounting for 29,8% of all exits. In 2004 these were again trade sales which accounted for 30,8% of the total divestments. The same tendency was observed in 2005 when trade sales were responsible for 64,1% of all

divestments. In 2006 the majority of exits (exactly 53,4%) were done by stock exchanges. Generally, it can be concluded that the most popular way of exiting venture capital investments in Poland in 2001 – 2006 were trade sales.

## **Concluding Remarks**

Literature shows certain proves for positive effects of benefiting from venture capital/private equity investments. What's interesting, L.Bottazzi and M. Da Rin<sup>14</sup> show there is no evidence of positive effect of venture capital on the growth of companies whereas the same authors<sup>15</sup> prove later that firms benefiting from venture capital increase their sales faster after they go public.

Besides, R. Pearce and S. Barnes notice that experimental learning of the nature and consequences of risk and the necessity of its professional management lies behind much of a venture capital's behaviour towards investment opportunities. Facing these likely attrition dynamics, the venture capital recognises that each company he or she backs statistically only has a 20-30 % chance of being successful (in fact, it has been demonstrated by academics that even the most successful companies in high growth sectors statistically have a less than 12% chance of success – neatly demonstrating how allying with a venture capital can improve an entrepreneur's chances of success).<sup>16</sup>

In well-developed countries, these are also governments that make efforts to stimulate such investments. For example, V. Kannianen and Ch. Keuschnigg emphasize that venture capital investing has attracted much governmental interest in the past decade owing to the importance of venture capital in funding small-technology firms and the perceived importance of these firms to economic growth. Many governments have in fact launched initiatives designed to strengthen their domestic venture capital industries and thus give a boost to their high-technology sectors.<sup>17</sup> It should be a core issue for the Polish government to take care of attracting venture capital to small and medium companies but unfortunately it is not. It could give a solid base for further development of Polish firms and thus the whole economy. Good sources of venture capital are pension funds. Their investment horizon is long and it is certain that the financial means possessed by these institutions grow and will substantially grow in the future. The Polish government could help in this process.

As it was shown, venture capital investments are present in Poland in different sectors of the economy. Their values are not impressive but this type of investments develops gradually. The reason for anxiety is the fact that the majority of venture capital investments in Poland comes from foreign investor. The important factor for further development of pe/vc investments in Poland is to intensify domestic sources of venture capital financing. One of the most significant barriers to small and medium enterprises is the lack of financial means for conducting small business projects. Vc/pe funds whose place of origin is foreign generally do not deal with projects worth less than 2 million Euro. It means that creating small local funds

---

<sup>14</sup> L. Bottazzi, M.Da Rin, *Venture Capital in Europe and the Financing of Innovative Companies*, Economic Policy 34, 2002a, p. 229 – 269.

<sup>15</sup> L. Bottazzi, M.Da Rin., *Europe's New Stock Markets*, Discussion Paper 3521, Center for Economic Policy, London 2002b.

<sup>16</sup> R.Pearce, S. Barnes, *Raising Venture Capital*, John Wiley & Sons, Ltd, Chichester 2006, p.32.

<sup>17</sup> V. Kannianen, Ch. Keuschnigg, *Venture Capital, Entrepreneurship, and Public Policy*, Seminar Series, Massachusetts Institute of Technology, Cambridge-Massachusetts-London 2005, p. 69.

in Poland, capitalized by domestic institutional investors, would be a golden mean to this situation.

To sum up, venture capital can contribute to the dynamic development of companies and the economy itself. Thus, attracting it to Polish firms should be a core issue both for their managers and for the government.

## References

- S. Bloomfield, *Venture Capital Funding. A Practical Guide to Raising Finance*, London and Sterling, VA, London 2005.
- L. Bottazzi, M. Da Rin, *Venture Capital in Europe and the Financing of Innovative Companies*, *Economic Policy* 34, 2002a.
- L. Bottazzi, M. Da Rin, *Europe's New Stock Markets*, Discussion Paper 3521, Center for Economic Policy, London 2002b.
- A. Brav, P. Gompers, *Myth or Reality? The Long-Run Underperformance of Initial Public Offerings: Evidence from Venture and Non-Venture Capital-Backed Companies*, *Journal of Finance* 52(5), 1997.
- D. Engel, *The Impact of Venture Capital on Firm Growth: An Empirical Investigation*, ZEW Discussion Paper 02 – 02, 2002.
- D. Engel, M. Keilbach, *Firm Level Implications of Early Stage VC Investments: An Empirical Investigation*, ZEW Discussion Paper 02 – 82, 2002.
- European Venture Capital Association Yearbooks 2002 – 2007.
- R. Fehn, T. Fuchs, *Capital Market Institutions and Venture Capital: Do They Affect Unemployment and Labour Demand?* *Applied Economics Quarterly* 50(4), 2004.
- P.A. Gompers, J. Lerner, *What Drives Venture Capital Fundraising?*, NBER Working Paper No. 6906, 1999.
- T. Hellmann, M. Puri, *The Interaction between Product Market and Financing Strategy: The Role of Venture Capital*, *Review of Financial Studies* 13(4), 2000.
- Internet pages of Polish Private Equity Association, 2007.
- V. Kannianen, Ch. Keuschnigg, *Venture Capital, Entrepreneurship, and Public Policy*, Seminar Series, Massachusetts Institute of Technology, Cambridge-Massachusetts-London 2005.
- S. Kortum, J. Lerner, *Assessing the Contribution of Venture Capital to Innovation*, *Rand Journal of Economics* 31(4), 2000.
- J. Lerner, *Boom and Bust in the Venture Capital Industry and the Impact on Innovation*, Federal Reserve Bank of Atlanta Economic Review, Fourth Quarter 2002b.
- W.L. Megginson, K.A. Weiss, *Venture Capitalist Certification in Initial Public Offerings*, *Journal of Finance* 46(3), 1991.
- A. Metrick, *Venture Capital and the Finance of Innovation*, John Wiley & Sons, New York 2007.
- R. Pearce, S. Barnes, *Raising Venture Capital*, John Wiley & Sons, Ltd, Chichester 2006.
- Polish Private Equity Association Statistical Yearbooks, Warsaw 2002 – 2006.
- Private Equity Going Public, *Global Private Equity Report 2006*, PriceWaterhouseCoopers.
- A. Schertler, *Knowledge Capital and Venture Capital Investments: New Evidence from European Panel Data*, *German Economic Review* 8(1), 2007.
- L. Tvede, *Business Cycles. History, Theory and Investment Reality*, Third Edition, John Wiley & Sons, Ltd, Chichester 2006.
- J. Vauhkonen, *Essays on Financial Contracting*, Bank of Finland Studies E:30, 2004.

# ROMANIAN HIGHER EDUCATION – A VIEW FROM THE INSIDE

MARIANA NICOLAE<sup>1</sup>

## Abstract

The present paper looks at the Romanian higher education from a cultural perspective with a view of identifying stakeholder expectations from a system that has to become competitive in order to align itself to European Union standards of quality.

The paper will be structured along the following lines:

- An exploration of Romania's higher education cultural profile
- Issues of Romanian economic higher education as perceived by its customers

The paper explores higher education issues in Romania as a new member state of the EU by analyzing some of the challenges for Romanian education providers as compared to the objectives laid out by the European Union in view of the changes of its economic paradigm expected to take place in the future twenty years. How effectively does Romanian higher education compete on the European market in providing quality services for its customers, on the one hand, and in defining itself as knowledge creator on the other? Are Romanian policy makers clear about the strategy along which to reform the system?

**Key words:** cultural profile, higher education, standards of quality, market positioning.

---

<sup>1</sup>Ph.D., The Bucharest Academy of Economic Studies, [mariana.nicolae@rei.ase.ro](mailto:mariana.nicolae@rei.ase.ro)

Romanians have had a soft spot for Western Europe in their hearts for a long time<sup>2</sup>. Even if in the early '90s this translated mainly in discussing the benefits or costs of an eventual accession in all social strata, from government officials, politicians, intellectuals, business representatives to the simplest and most unassuming people, in the remotest areas of the country, the focusing of these national debate took place slowly and it was only by 2000 that there was a relative “consensus on the only viable alternative for Romania’s political orientation in international relations. Besides the already mentioned emotional reasons, rooted in the identification of Romanians as Europeans, there are also objective benefits justifying Romania’s orientation”<sup>3</sup>. Romanians have been among the most optimistic of the peoples of Europe concerning the worth and the viability of the European construction having waited for the moment when the country becomes a full member with a sometimes too naïve eagerness and hopes for a miraculous settlement of long pending problems.

## 1. Background

The questioning of national identities, the deconstruction of historical and social mythologies, the discussion of the national stereotypes evident in various fields of activity, the building of a marketable image for entire nations or countries are no longer unusual, exotic topics nowadays for the business, political, social and academic worlds. It is therefore natural that Romanian scholars would engage themselves on such quests<sup>4</sup> in order to position the country and its people not only on the European market, but mainly among the member states where Romania still has to find its desired image, voice, brand or, expressed differently, its added value to the European Union.

*Cheap and well-trained labour force, good language skills, highly disciplined labour, flexible frame of mind* are only a few of the stereotypes in the Euro discourse of the pre-accession period. This is the way both Romanian official brochures describe the key elements of the Romanian market to potential investors and the way foreigners who have set up businesses in Romania explain why they chose this part of the world and how they had been successful. On the other hand, the well-trained labour force is a product of an education system generally criticised for being a continuation of the communist education system and for not adjusting fast enough to the values and vision of EU higher education.

The paper will explore higher education issues in Romania as a new member state of the EU by analyzing some of the challenges for Romanian education providers as compared to the objectives laid out by the European Union in view of the changes of its economic paradigm expected to take place in the future twenty years. How effectively does Romanian higher education compete on the European market in providing quality services for its customers, on the one hand, and in defining itself as knowledge creator on the other? Is the international discourse that is meant to contribute to the ideals of a unified, peaceful, and flourishing Europe really a dialogue? Are Romanian policy makers clear about the strategy along which to reform the system? The paper will attempt to answer these questions or at least discuss the various alternative answers that may appear.

---

<sup>2</sup> Djuvara, N., 2002, p. 163-170, 178-182.

<sup>3</sup> Miron, D., 2002, p. , 264.

<sup>4</sup> See Boia, L., 2002, p.63, Djuvara, N., 2002, as well as Luca, A., 2005.

## 2. Exploration of Romania's higher education cultural profile

Cultural profiles have become fashionable in the second half of the last century when a massive number of studies started to be devoted to explore, define and make use of the effects of culture upon social behaviour and development. Academics and students of many countries and traditions have become engrossed in this quest and the results can be found in the flow of books, studies, essays and articles that fascinate all those interested to find out why we are as we seem to be and how we can predict and, therefore, prescribe a pattern of behaviour for most people in most situations. This is how students in Romania, or Hungary, or Slovakia for that matter, have come to know a lot about how Americans, Japanese, Arabs (sic!), British, Latinos (sic!), French, etc. are expected to react in a certain situation, but not much about how their own fellow country people do things in specific situations.

In the first edition of Hofstede's *Cultures and Organizations* (1991) Romania is on none of the maps of the well-known indices and only twice mentioned in the text. In the 2005 edition, however, Romania made it to Hofstede's maps, which gives enthusiasts of cultural profiles the backing of a well-known guru for claims on how Romania *behaves* culturally. Hofstede also mentored one of the first cultural studies of the Romanian employee, a study done by Luca (2005) who based her research on Gallup polls and her own experience as an intercultural facilitator. Other studies on Romania are scarce and superficial, but the media discovered a subject of great interest for the general public and, therefore, many articles and discussions on the Romanian "ways of doing things" have appeared lately both in the written press and on radio and television.

To attempt to draw the cultural profile of higher education in Romania is both simple and very complex. Simple as legislation and regulations spell out the framework in which higher education institutions, processes and people should be moving, and complex as the system has been in a long and controversial process of reform. The Romanian education system has been under continuous changes and improvements in various domains and at all levels, according to economic, social, political and cultural changes identified within society. Still the *National Strategic Reference Framework for 2007-2013(NSRF)* produced by the Romanian government clearly points out that the "the skills gap between the educational provision and demand of a knowledgebased economy remains significant" (p.35). Since 2005 tertiary education has been structured into three cycles in agreement with the Bologna process which Romania adopted from the very beginning. Some of the main reform actions are related to quality assurance and management. The enrolment rate into university education increased from 27.7% in 2000-2001 to 40.2% in 2004-2005. The increasing participation in university education is explained by the development of private university education, development of university networks and increased interest for university education due to larger labour market absorption of highly educated people and lower unemployment risk for university graduates.

According to the latest report<sup>5</sup> of the Ministry of Education, Romania has at present 56 state accredited higher education institutions (49 civilian state higher education institutions and 7 military universities), 29 private accredited higher education institutions, 28 private accredited higher education institutions authorized to function temporarily and 6 postuniversity academic schools (p.5).

---

<sup>5</sup> Romania National Report, London 2007, <http://www.edu.ro/index.php/articles/c788/>



Higher education is perceived by the majority of the population as the most realistic chance of Romania's development, as the promise for the better future of one of the less developed and most abused by the communist regime countries in Europe. This explains, perhaps, why the discussions about education are more heated in Romania than they usually are elsewhere, and why a system of education that is so acutely underfinanced and generally struggling with its inner demons (called reform) is deemed responsible for whatever social unhappiness appears particularly in times of economic recess. Romanian higher education has to adapt to the requirements of the Bologna process, particularly since the country has become part of the European Union, not only formally which it already has, but in real terms by coping with the pressures that the universities from the rest of the EU set on the market both in terms of competition and quality standards and mainly, with the pressures that students as customers, more sophisticated than ever, raise for higher education. This is a particularly threatening area for the future development of Romanian higher education as marketing, with a special focus on promotion and selling, has not been a part of its mission in the centrally planned social and economic development of the country. Relatively suddenly Romanian universities had to wake up to the constraints of decreasing, in real terms, state financing and to the fierce competition from the private education area, on the one hand, and the international educational markets on the other. As some of the recently undergone research has pointed out the discourse of complacency and self-praise has ended and, in the face of competition, "Romanian higher education institutions (HEIs) need to carefully plan their actions, and better manage their scarce resources" (Niculescu, 2006).

Chiper (2006) finds that the communication style of Romanian higher education management has recently changed trying to acquire a more business and professional image, particularly under the pressures of the pre-accession period and, at present, full membership status in the EU. "Universities have started to give more attention to their public discourse, which is now perceived as an instrument of attaining competitive advantages, as creator of added value and as the means to construct and promote institutional image and identity" (Chiper, 2006, p.722). However, Chiper considers that the updated discourse of Romanian universities does not match their actual organizational behaviour, in other words that although "the vocabulary of Romanian universities has been "Westernized," local practices and mentalities are hard to alter" (idem, p.722) that is the *culture of higher education, irrespective of whether we look at the private or state owned sector, is still very traditional, autocratic and self-centred.*

If for the 1990s higher education reform in Romania was mainly intended to facilitate access to higher education studies, under the pressures of the market basically, the new millenium brought about the realization of new goals for the reform in terms of improving the quality of education and of scientific research, of decentralising the academic and financial management and of encouraging academic and social partnerships. The development strategy of Romanian higher education, defined for the period 2002-2010, is focused on the compatibility assurance between Romanian higher education system and other European systems.

Like the majority of higher education institutions worldwide (Daniel, 2002) Romanian universities have concerned themselves with the following general aspects of the reform actions envisaged by the Bologna Declaration, which Romania signed in 1999: quality assurance, qualifications, reorganisation of the teaching process, the promotion of the integration of the Romanian higher education system within the European systems and international co-operation. Progress has been made, but there is still much to be done in order to have changes internalized

and made operational in the system. The 2007 Report on Romania<sup>6</sup> perceives the following main challenges for the Romanian higher education (p.20) for the near future: 1) the establishment of the NQF (National Qualifications Framework), based on learning outcomes and described in terms of knowledge-competences-skills; 2) the separation of the HEIs: for education, for research, for education and research<sup>7</sup>; 3) the passage from teaching to learning based education paradigm; 4) the assessment of all the HEIs and of all the study programs; 5) increase the funding for higher education, allocated in accordance with their quality; 6) the portability of scholarships; 7) the training of the trainers; 8) the establishment of the of Sustainable Development Education Strategy.

The above challenges, among which the second and third seem to be, in the opinion of the author of the present study, the most sensitive ones, are the natural results of the educational policies the EU puts forward for its member states to implement. In its document entitled *From Bergen to London*<sup>8</sup> the Commission presents the nine policies that are necessary to update the agenda of European universities and make them truly competitive internationally: 1) break down the barriers around universities in Europe; 2) ensure real autonomy and accountability for universities; 3) provide incentives for structured partnerships with the business community; 4) provide the right mix of skills and competencies for the labour market; 5) reduce the funding gap and make funding work more effectively in education and research; 6) enhance interdisciplinarity and transdisciplinarity; 7) activate knowledge through interaction with society; 8) reward excellence at the highest level; 9) make the European higher education area and the European research area more visible and attractive in the world.

“The university, as a centre of teaching and research, is a genuinely European invention and, with a few exceptions, the existence of the university was inspired by and confined to European cultural, economic and political dominance for a long period of time.” (Trends in Higher Education, p. 5) However, Europe has lost its dominance as a destination for international students in favour of the US and not even the international tensions and the terrorist activities have changed that. The very fashionable at the moment university rankings give a clear image of the shift in the importance of universities in today’s complex world. Therefore, the road to the implementation of the nine needed policies is long and convoluted as European universities are no longer in a position to achieve their full potential by offering Europe their input for its growth and more jobs. Besides having lost in the increased international competition for talented academics and students, they still miss out on dynamic research agendas and on generating the critical mass, excellence and flexibility necessary to succeed. These failures are the result of an excessive multi-layered bureaucracy coupled with insufficient funding<sup>9</sup>.

It is rather obvious that Romanian universities mirror, on another scale and intensity, the problems and challenges universities across Europe have to meet. The discourse of Romanian university management needs to be more realistic and present the true perspectives of the changes higher education goes through in the EU.

---

<sup>6</sup> Romania National Report, London 2007, <http://www.edu.ro/index.php/articles/c788/>

<sup>7</sup> Such a separation is less the result of administrative classification, therefore imposed external regulations, and more the natural division brought about by the universities’ own profiles developed along their historical existence.

<sup>8</sup> <http://ec.europa.eu/education/policies/educ/bologna/report06.pdf>

<sup>9</sup>See introduction (p.2) to “Delivering on the Modernisation Agenda for Universities: Education, Research and Innovation” [http://ec.europa.eu/education/policies/2010/doc/comuniv2006\\_en.pdf](http://ec.europa.eu/education/policies/2010/doc/comuniv2006_en.pdf)

### **3. Romanian economic higher education: competing internationally**

In a highly developed and sophisticated service economy the concept of customer and customer care are very developed. Almost anyone can be a customer in a certain situation and as such the philosophy of customer satisfaction is important and relevant for the quality of the service provided. In Romania it is only relatively recently that the mainstream academic discourse admitted the reference to education as a service offered on a market that tends to be less centrally controlled by the government through the Ministry of Education and is becoming freer mainly under the international pressures. In the use of the present paper the term customer refers to students, in all cycles of education and coming from both national and international environments.

The issues dealt with further on will be mainly from business higher education with a focus on the author's institution which is the Faculty of International Business and Economics (FIBE)<sup>10</sup> of the Bucharest Academy of Economic Studies (BAES). To better understand the institutional context, the services provided and the variety of its customers it is important to give a brief outline of the BAES.

BAES is one of the most important economic universities in Romania and, at the same time, one of the oldest being set up by royal decree in 1913. The fundamental goal of the BAES is to educate future economists, to carry out continuous education programmes as well as scientific research.

According to its own presentation leaflet<sup>11</sup>, BAES is and intends to remain the most prestigious institution of tertiary economic and public administration education in Romania and to rank among the leading universities in Europe, due to the content and topicality of its learning processes, its innovation, dynamism, and its involvement, through strategic partnership relationships, in the national and international economic environment.

BAES is one of the largest higher education institutions in Romania with well over 46,280 students enrolled in its faculties and colleges in the academic year 2006-2007. The academic staff includes 950 full-time, highly qualified members, out of whom 379 professors and readers.

The Bucharest Academy of Economic Studies has adopted the principles of the Bologna Declaration which, essentially, lead to the development of a European Higher Education Area to increase mobility and ever closer cooperation in the field of academic training and research. In this respect BAES has partnerships with over 50 well-known universities abroad in order to gain recognition among the prestigious economic institutions worldwide. Enjoying a good reputation worldwide, the Bucharest Academy of Economic Studies has been in demand from overseas students for Bachelor's courses, doctoral studies, specialisation and exchange of experience. Most undergraduates and doctoral students are from Albania, Angola, Azerbaijan, Belgium, Bulgaria, China, Columbia, Congo, Croatia, Egypt, Gabon, Germany, Greece, Iran, Lebanon, Macedonia, Great Britain, Morocco, Nigeria, the Moldavian Republic, Russia, the USA, Syria, Sweden, Turkmenistan, Ukraine, and Yemen. In the academic year 2004/2005, over 600 foreign undergraduates were enrolled in the various schools of the BAES as well as more than 180 foreign doctoral students. These figures point to the need of a well organised department for

---

<sup>10</sup> [www.rei.ase.ro](http://www.rei.ase.ro)

<sup>11</sup> <http://www.ase.ro/site/despre/socrates/brosura.asp>

international students, with clearly communicated procedures and with staff who is well trained in intercultural communication and speaks relevant foreign languages or at least English.

The Department for International Relations of the BAES caters mainly for outgoing Romanian students. The Department as such has only one person, a junior instructor, working in it under the monitoring of one of the vicerectors of the university and transferring all the actual work to the faculty management. The incoming, international students, and their number has been rising lately, are in the care of the same International Relations and European Integration Department<sup>12</sup>, where there is a small group of administrative staff (3 or 4) to deal with the various issues of the international students. One of the main complaints of students is the difficulty in communicating with the Department and the lack of reliable and updated information on the university website. In a time in which most internationally looking universities have a visible, multilingual and user friendly website, the BAES has a relatively complicated way of structuring its information and very little to offer to international prospects. Even the name of the BAES is ambiguous for international students. If for Romanian prospective students the Academy of Economic Studies is a well-established, prestigious brand, for international students the term *academy* in the university title is relatively disconcerting as it does not show the true status of a university. The term *academy* in English<sup>13</sup> refers to either a school which is usually above the elementary level and is very often a private high school or to a high school or college in which special subjects or skills are taught (police academy, music academy, L'Oréal Academy, etc.). In Romanian<sup>14</sup>, however, the term academy is listed in the dictionary, true only as its third meaning, as “școală de învățământ superior” (that is higher education institution). For the international positioning of the BAES, however, the present name, even if a brand in Romania, is not an asset. This explains why the English version of the university web page ([www.ase.ro/engleza/index.asp](http://www.ase.ro/engleza/index.asp)) has been optimized for search engine as Economic University Bucharest, while the main banner on the website gives the following explanation: *Bucharest Academy of Economic Studies, The University was established by Royal Decree on April 6, 1913.*

In spite of this positioning weak point, the BAES is looking forward to implement one of its main objectives which is attracting international students and has taken steps in creating the required institutional and administrative framework<sup>15</sup> in order to achieve this objective. There are two schools, out of the nine faculties of BAES, which offer full instruction in foreign languages: Business Administration (in foreign languages) and International Business and Economics. At the Faculty of International Business and Economics (FIBE), education at bachelor level is based on a curriculum that combines core subjects that are fundamental to the field of economics with specialty and service disciplines. This, hopefully, ensures the development of competencies and specific skills in the domain of bilateral and multilateral economic diplomacy as well as the negotiating and unfolding of international financial and commercial transactions. FIBE offers full programs of studies in both English and Romanian as the primary language of instruction. Moreover, English is a mandatory subject for all the students attending the Faculty. The unique selling point of FIBE as compared to the other schools of the BAES is the wide array of elective

---

<sup>12</sup> [http://www.ase.edu.ro/engleza/despre/departamente/euro\\_integration.asp](http://www.ase.edu.ro/engleza/despre/departamente/euro_integration.asp)

<sup>13</sup> <http://www.merriam-webster.com/dictionary/academy>

<sup>14</sup> <http://dexonline.ro/search.php?cuv=academie>

<sup>15</sup> BAES Strategy for 2004-2008, p. 6, “Dezvoltarea și diversificarea unor servicii universitare de calitate, având costuri acceptabile, orientarea lor către specificul societății informaționale, ... lărgirea spectrului clienților ... lansarea unor oferte de pregătire pentru cetățenii străini.”

[http://www.ase.ro/site/despre/management/fisiere/pdf/planuri/strategia%20\\_ASE.pdf](http://www.ase.ro/site/despre/management/fisiere/pdf/planuri/strategia%20_ASE.pdf)

foreign languages and business communication courses that are offered which comprise French, German, Russian and Spanish (second foreign language) as well as optional courses of Arabic, Italian, Japanese, Portuguese and Turkish (third foreign language).

Higher education all over the world is indeed in a period of profound transformations, the same as the world is in its economic, social, technological and cultural environments. Various competing paradigms are at work, and estimations and predictions are difficult to make as to the most appropriate directions to follow. However, the best way to deal with this uncertain and uneasy period of change and transformation is to acquire a knowledge of the various models, to get into partnerships and cooperation in the field of higher education, to know more and to reflect more on the complexity and diversity of the world in order to be able to make better sense about it and communicate points of views in spite of the differences in institutional communication styles and patterns.

#### **4. Services provided by Romanian HEIs. The BAES**

A discussion of services provided by HEIs can be complicated by the fact that universities offer both academic and non-academic services (student accommodation, catering on campus, conference and research facilities, counseling, etc.). For academic services Romanian universities are constantly trying to adapt to market requirements. The curriculum in the higher education institutions in Romania has undergone complex changes and it continues to be updated to the standards of European and American models<sup>16</sup>. But the politics of change triggered mainly by the Bologna process made the current situation in BAES to be characterized mostly by the teaching of theory, no real focus on practice and entrepreneurial education.

For example, the teaching of communication is part of this overall change. However, there are not enough opportunities for meaningful communication, such as writing and speaking for students: no more oral exams and the written exams are in their great majority multiple choice tests. Even in the students' research session, a once a year, very popular event, in which undergraduate students present the research they did under the supervision of a member of the academic staff, they are not given the opportunity to speak for more than three to five minutes. So much for public speaking for Romanian students of business who will need to compete in a tough business environment to "sell and buy" contracts! Besides general, abstract courses on communication and negotiation there is no course on public speaking and debate. As there is no "writing centre", either.

The lack of a "writing centre" makes it difficult for students and tutors/supervisors to go through the process of dissertations and theses writing. The lack of formal style of Romanian end-of-cycle assignments is notorious, even if some very few steps have started to be made especially by individual tutors and/or faculties.

The rest of this section will refer to some issues of institutional communication as part of the services HEIs are supposed to offer. One of the important aspects of higher education communication is the way institutions address their various publics. The educational market is

---

<sup>16</sup> Nicolae, M., Enache, M., *Romanian Higher Education – the First Lessons as a European Union Member State*, BAES Publishing House, June 2007.

highly competitive today and first impressions count more than ever. The Erasmus mobility programme has provided many Romanian students with the opportunity to study abroad. When they come back they start to put pressure on their home institution by demanding higher quality services both of the academic and non academic type. At the same time Erasmus brought a significant, though much lower, number of European students to study in the BAES, particularly in the Faculty of International Business and Economics, which provides full time tuition in English. The international students studying in FIBE complain not of the lack of comparable resources to their home institutions, as might have been expected, but mainly about the lack of effective institutional communication, the lack of clear, transparent procedures, easily available in international languages. The difficulty of accessing information, the lack of dynamism in updating the existing information on the university website are other types of complaints. In 2007, the year of Romania's joining the EU, a university of the size of the BAES, with more than 46 000 students had its webpage only in Romanian, although the previous university year (2005-2006) it used to have an English version as well. There was some basic information about the university, its history and very general, not updated information on its faculties and programmes.

Another issue is the obsolete, pretentious, highly unintelligible, digressive discourse that Romanian universities generally maintain in comparison with their counterparts around the world. For example, the mission statement of the BAES is presented in 155 words compared to the Harvard Business School, which expresses its mission only in 10 words or the Haas School of Business of the University of California, Berkeley, which uses only three words. European universities, in declared competition with the American ones, follow the same communication patterns trying to concentrate and make their discourse more marketable, but against a background of European identity. The Judge Business School of the Cambridge University expresses its mission in 18 words, while INSEAD in Fontainebleau, France, does it in 7 and the London School of Economics seems to be more verbose putting into the 48 words on its webpage both its mission and the history of the school<sup>17</sup>.

Chiper (2006) considers that although most universities have developed a mission statement, the awareness of a collective mission does not really exist within Romanian HEIs. In other words, the vision of a particular university is little known, or fully ignored. "Indeed, there are well written texts targeted towards the "extramural" world but there is little communication and interpretation of the vision inside the institution. The institutions own culture is rather weak, and staff cooperation and dialogue are also low." (Chiper, p. 9) Chiper goes on to conclude that Romanian universities will have to match their already tuned in discourse to the general EU higher education themes with appropriate organizational behaviour materialized in more interest in both research and in standards of quality in teaching, more accountability and commitment to the educational process and better staff-student communication.

---

<sup>17</sup> Nicolae, M., Enache, M., *Romanian Higher Education – the First Lessons as a European Union Member State*, BAES Publishing House, June 2007, p. 7.

## 5. Conclusions

1. Romanian HEIs are on the right track in adapting their institutional discourse to the inter/national educational market demands. What is still needed is a match of their mentalities and practices to their updated discourse.
2. Focus on quality and external monitoring of the academic and non-academic services is an important step forward to create an organizational culture in which customer value becomes essential.
3. One of the main roles of Romanian universities is to invest in communication and marketing research as a means to foster increased cooperation at both national and international levels for the benefit of their diverse stakeholders.

## References

- Amariei, R., *Educatia si sanatatea se pot sufoca de prea multi bani*, <http://www.capital.ro/index.php?a=25343&shift=1>, retrieved from [www.capital.ro](http://www.capital.ro) on 29 Oct., 2006
- Boia, L., *Două secole de mitologie românească*, Humanitas, București, 2002, ISBN – 973-50-0232-9
- Chiper, S., *The discourse of Romanian universities*, Journal of Organizational Change Management, Vol. 19 No. 6, 2006, Emerald Group Publishing Limited ISSN 0953-4814
- Djuvara, N, *O scurtă istorie a românilor povestită celor tineri*, Humanitas, București, 2002, ISBN – 973-50-0242-6
- Duffy, M., *England, The Making of the Myth from Stonehenge to Albert Square*, Fourth Estate, London, 2002, ISBN 1-84115-167-x
- Hofstede, G., *Cultures and Organizations, Software of the Mind, Intercultural cooperation and its importance for survival*, HarperCollinsPublishers, UK 1991
- Hofstede, G., Hofstede, G.J., *Cultures and Organizations, Software of the Mind*, McGraw-Hill, USA 2005
- Luca, A., *Employeescu, O scurtă caracterizare a angajatului român*, Editura Interact, 2005
- Luca, A., *Studiu despre valorile si comportamentul romanesc din perspectiva valorilor culturale* <http://www.training.ro/docs/studiu2.pdf>
- Miron, D. (coord.), *Economia Uniunii Europene*, Editura Luceafărul, București, 2002, ISBN – 973-85399-8-6
- Nicolae, M., *Integrarea europeană – economie, instituții și comunicare*, in the volume “Economie, instituții și integrare europeană”, Editura ASE, 2007, ISBN 978-973-594-954-9
- Niculescu, M., *Strategic positioning in Romanian higher education*, Journal of Organizational Change Management, Volume 19 Number 6 2006 pp. 725-737, Emerald Group Publishing Limited ISSN 0953-4814
- Romania National Report, London 2007, <http://www.edu.ro/index.php/articles/c788/>
- Delivering on the Modernisation Agenda for Universities: Education, Research and Innovation, 2006, [http://ec.europa.eu/education/policies/2010/doc/comuniv2006\\_en.pdf](http://ec.europa.eu/education/policies/2010/doc/comuniv2006_en.pdf)
- [http://www.cariereonline.ro/index.php?m=article&article\\_id=291](http://www.cariereonline.ro/index.php?m=article&article_id=291)

# **RURAL SPACE PLANNING AS A TOOL FOR NATURAL RESOURCE MANAGEMENT IN SLOVENIA**

**ANDREJ UDOVČ<sup>1</sup>**

## **Abstract**

Regulated spatial planning is in large number of countries primarily concentrated on urban areas, while the rural areas are less strictly planned, especially in the context of natural resource development. As Slovenia is a small county with very limited spatial conditions for non restricted development planning (ie. flat, no geographical or/and environmental restrictions), the idea of more or less detailed spatial planning in rural areas was adopted already in early 70es. The reason for starting with this kind of planning was mainly connected with the competition between urban and industrial development planning and agriculture for the best lands. In the paper we discuss the development of methods of rural spatial planning, present effects of past approaches on usage of rural space and the proposal of the future rural areas planning models.

**JEL classification codes:** R52 – Land Use and Other Regulations

---

<sup>1</sup> Biotechnical faculty University of Ljubljana, andrej.udovc@bf.uni-lj.si.



## **Introduction**

Before establishing an independent state, Slovenia had a comprehensive social planning system, which contained, in addition to economic and social aspect, also a spatial aspect. When Slovenia gained independence in 1990, a special law cancelled social planning. Only spatial components of the national and local social plans were in force until the adoption of new spatial planning and management regulations in 2003. And right now the changes of actual spatial planning situation are again going on and they are in discussion between ministries and experts.

Adopted prior to independence (year 1986), the existing national spatial plan was the key development framework document for the period 1986-2000<sup>2</sup>. It spatially defined long-term goals and guidelines for economic and social development within the socialist self-management system. It included guidance on the development of towns and settlements; spatial planning, design, development and protection of the agricultural land and forests; protection and improvement of the human environment and conservation and the promotion of conditions of work, living, culture and recreation (Eliot, Udovč, 2005).

With the national spatial plan in place, it was the absence of instruments for the supervision of the location of activities, and for monitoring the implementation of adopted spatial planning documents, which caused ineffective implementation of otherwise well-considered goals of spatial development, planning, and management. All this also began to reflect with regard to space. Particularly outstanding in the wide range of identified issues are big differences in spatial development of regions, uneven urban development associated with the shortage of land policy, and housing policy instruments, suburbanization pressures along motorways, uncontrolled dispersed building construction, a large share of illicitly-built structures, degraded urban and other areas, the decline of old industrial towns, unplanned and deficient renewal of old city cores, inadequate infrastructure in settlements, unsolved waste management issue, restructuring of rural areas due to a changed role of agriculture, extensive forestation overgrowing of farmland, inadequate transport links despite well spread out road network, insufficient emphasis on rail transport, and an inadequate network of public means of transport, inadequate systems solution of the protection of farming land also within settlements, no respect for and observance of regulations on spatial planning and management, the absence of regional level as an intermediate link between state administration and local government, a shortage of suitable personnel, and disassociated work of various sectors. All this subsequently lead to a graduate loss of the best agricultural areas and with it a loss of the best food and fibre production potentials.

## **Spatial planning system in Slovenia**

In the existing system of spatial planning and management in Slovenia, the state prepares laws, policies, and other instruments, that are adopted by the National Assembly or the Government of RS. They define the spatial planning system and provide strategic spatial development objectives and guidelines, which all provide frameworks for spatial planning at the regional and local levels. In addition to the spatial development laws and strategic documents, the state also has the

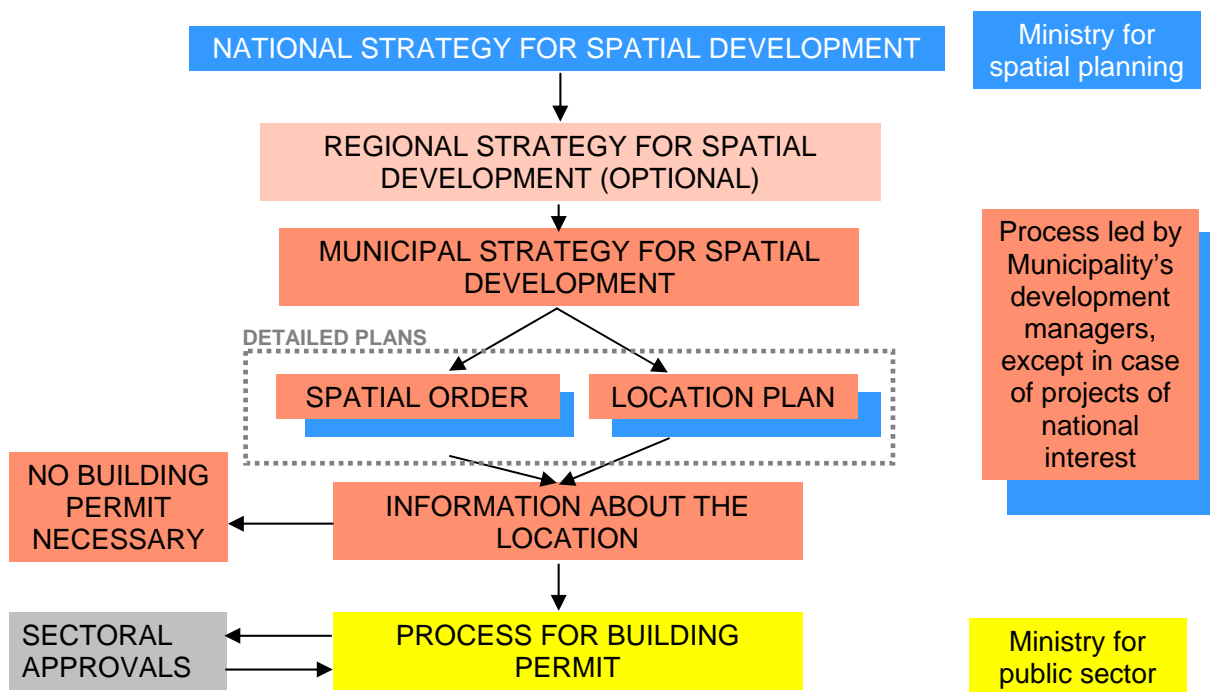
---

<sup>2</sup> Official Gazette of the S. R. Slovenia 1/86, 41/87, 12/89, 36/90, 27/91, 72/95, 11/99

authority to perform measures concerning spatial development activities and construction, which are of national importance.

Local communities have the original right to spatial management and planning of their territories, with exception of spatial development activities which are under direct jurisdiction of the national state. A local community is obliged to perform activities in the field of spatial planning and management, as well as planning pursuant to the adopted laws, standards, and criteria. Their principal task in connection with spatial management and planning is concern for rational, mixed, and sustainable land use, as well as economical use of land plots in accordance with the principles of high quality living, working, recreation, and a healthy environment. In decision-making procedures, they are responsible for the direct participation of all the involved and interested parties. They also care for and maintain the identity of the community by considering and protecting the natural and built characteristic features.

## SPATIAL PLANNING LEGISLATION IN SLOVENIA

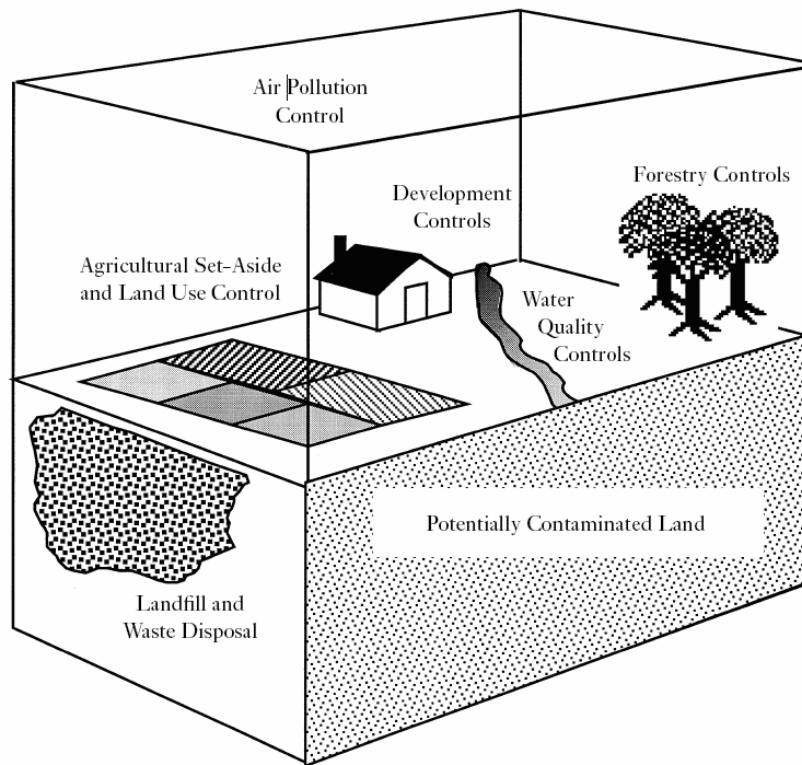


Picture 1: Spatial planning legislation in Slovenia (Cotič, 2005).

### Concept of integrated spatial planning of rural areas

To achieve a holistic and sustainable development of rural areas at spatial planning all development potentials have to be harmonized: population, settlements, agriculture, forestry, hydrology, recreation, ecology and nature protection. The available space must be planned and managed holistically, to achieve efficient spatial planning. Such spatial planning means

cooperation between sectoral specific planning and general planning, what means that there must be an adjustment made between spatial functions (traffic, recreation, lodgings, agriculture, ...) and functional patterns (ecological aspect, socio-economic aspect,...). Especially ecological aspect is gaining on its importance with the natural environment becoming limited good. (Prosen, 1993).



Picture 2: Land use control (Platt, 1975)

Integrated spatial planning comprises more planning methods including ecological and landscape planning, physical planning of space use or land use planning. The land use planning is used to protect agricultural land, as limited and irreplaceable natural good. Physical planning bases on natural characteristics of specified areas. Land is in this case considered as resource for demand satisfaction. Regarding the natural production characteristics of land an usage plan is made, which secure different areas for different sectors (agriculture, forestry, settlement, traffic, ...) In this purpose the land is divided into infertile land, forests and arable land (fields, gardens, meadows, orchards, vineyards, pastures, ...) (Prosen, 1993: 25).

Integrated spatial planning was in the past due to enforced socialist planning not implemented. In the system of socialist planning the rural areas were planed by interested individual sectors (i.e. agriculture, water management...). First in the second half of the nineties the socialist planning started to be substituted by integrated spatial planning what forced also the agriculture to more actively involve into the spatial planning of rural areas, as the efficient integrated spatial planning is only possible when all actors participate in the process.

Traditionally within the socialist planning system in rural areas twofold spatial planning was present: planning of builded space and protection of agricultural land. The right to build goes to

everybody who owns land in a rural area, where building is possible pursuant to the land use of the Municipal Spatial Order or spatial arrangement set out in the local detailed plan.

The systematic protection of agricultural land is in Slovenian spatial planning present since early 70es. In 1973 the first Agricultural land act (UL. SRS 26/1973) was passed which determined which land is permanently protected as production resource for agriculture. Since then in all Slovenian spatial legislation the protection of agricultural land is explicitly included.

The law defined three types of agricultural land areas, which are even nowadays still used:

- areas where agricultural land is permanently designated for agricultural use only, and where in the rule its purpose can't be changed,
- areas where agricultural land can be used for non agricultural purposes, if those are in congruity with community spatial plan,
- areas where agricultural land can be used for other with agriculture connected activities (farm tourism, rural tourism, drinking water reservation, nature protection areas).

The reasons for such protection were to secure the minimum needed extent of available natural resources for food production in the case of distorted supply. Among all agricultural land the special concern was and still is given to the areas which are having the highest natural production potential. Such pieces of land can be changed into other usages only, if some other agricultural land is developed to compensate the lost production potential.

To operationalise the adopted legislation, in a whole country a categorization of agricultural land on the basis of its natural and spatial characteristics was done in late 70ies.

### **Rural space categorization systems**

All categorization systems of spatial units existing in Slovenian spatial planning system are based on certain valuation approach, which can base either on monetary or non monetary values. In this context at planning rural space the planning must beside taking in consideration agriculture as well consider other economic sectors (valued in monetary terms with generated income opportunities) and landscape, environment, preservation of settlements (often valued in non monetary terms).

Because of this, also the valuation of rural space for agriculture is divided into two groups:

- valuation regarding economic goals of agricultural production, and
- valuation regarding the protection of agricultural land as natural resource.

Existing rural space valuations, and on them based classifications, were primarily based on protection of agricultural land as natural resource, and their goals were to preserve as much agricultural land in cultivation as possible. Within this paradigm for the most valued agricultural land are considered:

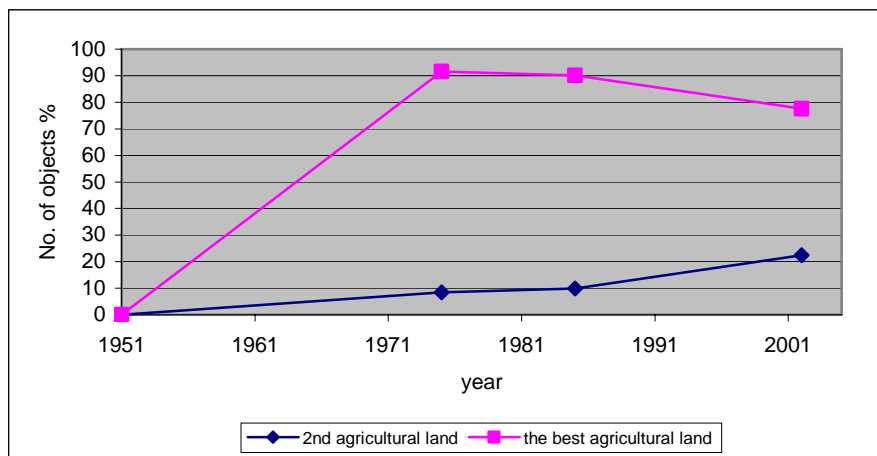
- plots of land where there are no or very few agro technical limitations regarding the cultivation of known agricultural plants and usage of modern agricultural technologies,

- plots of land which can be improved with certain agro technical operations (hydro- and agro ameliorations, irrigation) for intensive agricultural production,
- plots of land which form bigger complexes,
- plots of land which are suitable for intensive plantations (orchards, vineyards),
- complexes of plots which are suitable for horticultural production.

All such land is categorized as 1<sup>st</sup> (the best for agricultural production) or 2<sup>nd</sup> category of agricultural land, and was protected by Agricultural land act (UL.SRS 26/1973) against other forms of spatial use. The other agricultural land allocated in categories from 3 to 6, was allowed to be allocated to other spatial uses by local municipality spatial documents.

### Effects of past rural space planning systems

The regulated use of agricultural land for non agricultural purposes has been affecting the spatial development in rural areas as it can be seen from the picture 3, which shows the trends in building up of agricultural land in period 1951-2001. As we can see has the introduction of Agricultural land act in 1973 redirected the building processes from best agricultural land to other categories of rural space, but it could not completely stop it.

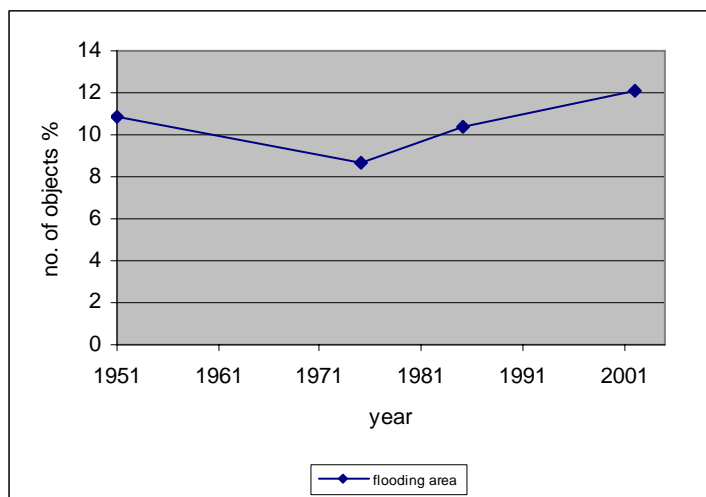


Picture 3: Trends in building of residential housings on agricultural land in municipalities of Medvode, Vodice, Trzin, Mengeš, Domzale between years 1951 and 2001 (Prosen et al, 2005)

But the positive effects of restrictions put on building on agricultural land had also some unwanted consequences, among which are disperse buildings, non permitted building, use of non agricultural rural land with higher degree of natural importance and building in areas with higher degree of natural hazards risks, as can be seen from picture 4.

Big spatial problem in rural areas connected to changes in agriculture also represent the abandonment of production on agricultural land, which is than because of limited availabilities for other spatial usages (even temporal) left fallow. A the moment the analysis show that about 4% (cca 48.000 ha) of agricultural land is under the process of overgrowing and about 100.000 ha

(5% of total area of R Slovenia) was already because of this processes already converted back into forests in last half of a century. The problem is considerable, because the process is not present only on marginal hilly agricultural land, but also in flatlands on the best agricultural land. One of the reasons for such development is also lying in the small parcel structure of agricultural holdings, and to change this is one of the future tasks of new spatial planning of rural areas.



Picture 4: Trends in building of residential housings in flooding areas in municipalities of Medvode, Vodice, Trzin, Mengeš, Domzale between years 1951 and 2001(Prosen et al, 2005)

Continuing we represent some expert assessments of influences of restricted usage of agricultural land on spatial development of rural areas (Prosen et al, 2005). In the survey 198 experts from fields of agriculture, spatial planning and rural development were questioned. The table 1 shows the results of a question asking if all land plots, which are categorised as the best agricultural land, are also such in reality.

Table 1: Answers on the question “Are, by your opinion, all land plots, which are categorised as the best agricultural land, also such in reality?” N=198

	%
Total	100
As the best agricultural land are classified predominately the best agricultural land plots	36.9
As the best agricultural land are classified all agricultural land plots, also bad agricultural land	29.8
The quality of agricultural land was not the criteria for classification as the best agricultural land	27.8
Don't know	4
Yes, as the best agricultural land, only the best agricultural land plots are classified	1.5

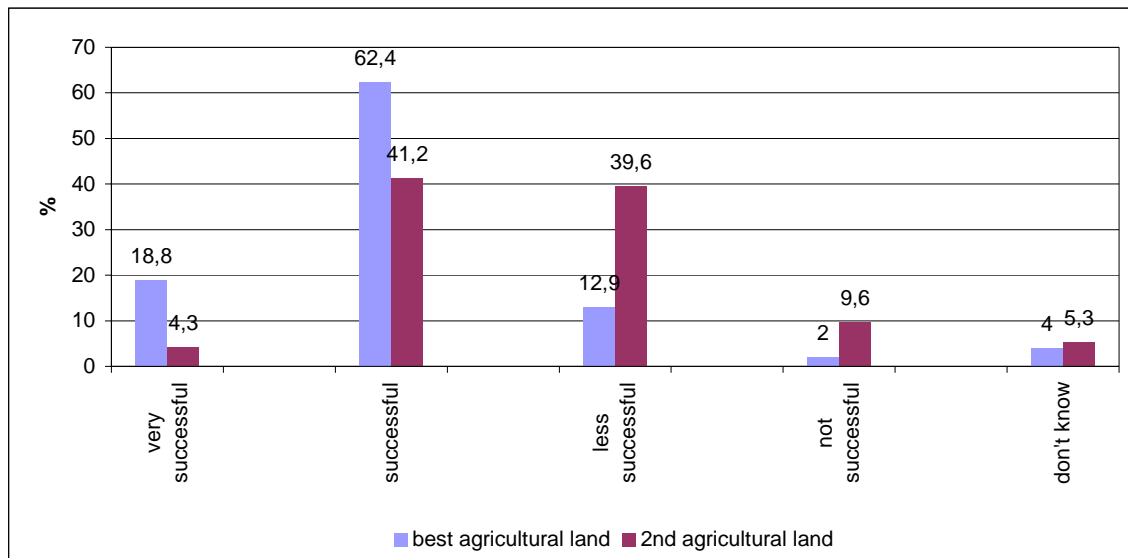
The results show, that more then half of questioned experts doubts, that only the best agricultural land was categorised as such. Firm about this are only 1.5% of them. This answers show that the system was considered very doubtful and probably even abused in number of cases. From this we

can conclude that in the future the classification of the best and most needed agricultural land must be better defined and also more strictly followed.

Table 2: Answers on the question: “How was by issuing the building permit the actual quality of agricultural land considered?”

	%
The permits were issued only for interventions on non agricultural land	8.0
The permits were issued only for interventions on non agricultural land and low quality agricultural land	20.9
The permits were issued predominately for interventions on non agricultural land and low quality agricultural land	36.8
Quality of agricultural land had small influence on issuing the permits	14.4
Quality of agricultural land had no influence at all on issuing the permits	5.0
Don't know	14.9
Total	100.0

The results show that the issued the permits were in majority of cases connected to land quality and in the rule the permits were not issued for interventions on agricultural land. Only in small percent the issuing of permits was not connected to the land quality. This answers are in concordance to the assessment how effective was the protection of the best agricultural land (picture 5).



Picture 5: Expert assessment of protection of agricultural land against spatial development

Even if more than half of asked experts think that the system of protection was not good, almost all (81 %) agree that the system was effective in protection of the best agricultural land. Regarding protection of other agricultural land the assessment is already more in favour of failure. This answers might indicate, that even if the system of protection was not very popular and sometimes even not strictly implemented, it has delivered good results in achieving the set goals. The authorities did not give up under pressure for building up agricultural land. The

situation is different when considering building up of public infrastructure, but here the dilemma between protection and development plans is always present and not in favour of agriculture.

The main problems that experts identified as negative development from existing agricultural land protection is the collision between Slovenian ideal of owning a house in nice rural area near the city and scarcity of such locations. The solutions will have to be searched in better planned organized building ground development in periurban areas.

Generally speaking, the survey showed some major differences between groups of experts. The agricultural experts were predominately very positively assessing the development, while the architects and planners were more often connecting unwanted spatial developments, as scattered settlements, lack of building grounds, non permitted building, with the strict protection of agricultural land.

### **New suggested approach in rural space planning**

As this classification was predominately based on pedological characteristics of plots, it proved itself as unsuitable and too rigid for integrated spatial planning of rural areas. In modern agricultural production beside soil quality, also other factors (accessibility, plot size, distance to pollution sources, transport infrastructure, water availability...) influence the decisions where the agricultural production and of what kind will take place. In 90es, in spite existing protection, also the trend of developing the best agricultural land for building grew steadily and because of this a novel approaches to classifications for rural space was demanded. In this context a proposal for new spatial planning strategy in rural areas was developed which:

- more precisely defines the best agricultural land, where the definition is basing on more agronomical parameters and also make spatial reference for their locations,
- spreading of settlement directs in areas with lower quality of land or into forests; settlements which don't have such space in its' hinterland should not be planed for further spreading (the use of best agricultural land should be permitted only exceptionally in case of building traffic, municipal or state level infrastructure, share of the rent earned by developing agricultural land should be transferred to improve the remaining agricultural land),
- minimize the transfer of agricultural land from farmers to non farmers and
- establish databases for better control over transactions with agricultural land.

Those strategic starting points were first time used by preparation of a spatial development strategy for the city of Ljubljana (Kovačič et al, 2003). Within this project the open space in rural areas was classified in three categories:

(1) areas of intensive agricultural production with highest production potential,

(2) areas where agricultural production is limited due to lower production potential of the land or existing environmental and spatial constraints and we can experience mixture of different usages and agriculture might even be of secondary importance,



(3) areas where the agricultural land can be, due to bad or restricted development opportunities for agriculture, transferred to other spatial usages.

Each of this category can be the further internally structured regarding its suitability for agricultural production or level of needed protection. In the case of planning the agricultural usage of rural space the proposed categories are:

1. areas of protecting agricultural land with highest degree of production potential,
2. areas of protecting agricultural land,
3. areas of possible alternation of usage, and
4. where needed, areas of improvement of agricultural space.

### **Areas of protecting agricultural land with highest degree of production potential**

Those are the areas where agricultural production development is planned and agricultural usage of land is preferred. Those areas have the highest possible protection against the change of usage. The characteristics of areas that are evaluated for this category are:

- productivity of agricultural land,
- extensiveness of land plots,
- possibilities to form bigger production units (concentration of estates), and
- feasibility of using agricultural machinery.

In such areas limiting factors can be protection of drinking water springs and catchments, nature protection, vicinity to settlements and roads (transportation, collision of interests, airborne pollution...) and possibilities to create new cultural landscapes. In those areas all agro technical operations and measures are possible (merger of land units, drainage, irrigation and agro ameliorations).

### **Areas of protecting agricultural land**

Those are areas where agricultural production has some limitations either due to lower production potential of the land, or other impeding factors (natural, drinking water catchments...). Here agricultural production faces some limitations in its development. This does not mean, that having agriculture there is not important and due to this the agricultural land subject to less protection, rather opposite. In such areas agricultural production represents important element of cultural landscape (natural and cultural heritage, preservation of settlements, tourism...), but as economic activity it is of secondary importance. Mixing of usages and activities is in those areas more obvious and acceptable and in this category we categorise also special geographical position for production of special cultures as fruits, grapes and perennial vegetables and in special cases even small gardening. Possible subcategories within this category are:

- areas of special geographical conditions for production of special cultures,

- areas of nature protection,
- areas of landscape protection, and
- areas of landscape heritage protection.

The characteristics of such areas that are evaluated for this category are:

- moderate suitability for agricultural production,
- exceptional landscapes (cultural quality, symbolism, identity),
- natural and cultural heritage,
- areas of specific ecological sensible landscapes (difficult production conditions, low level of natural resources renovation),
- areas of natural resources protection, etc.

### **Areas of possible alternation of usage**

This category includes two types of areas. First type are areas, which could be, because of low suitability for agricultural production (low soil quality, remainder of land within urban areas, polluted land, high degree of agricultural land abandonment and its overgrowing with natural forests...), left to other usages either to develop them or to use them as protective areas (ie. protective vegetation stripes...). The other type are areas where agriculture represents a so called influential space on other economic activities (ie. mixture of agricultural and forestry usage).

### **Areas of improvement of agricultural space**

In the past some not well planed agricultural measures caused the degradation of space due to wind erosion, landscape degradation, draining wetlands... The new development calls for improving such areas with either ecological measures (renaturation) or agro technical – especially irrigation for securing the future potential agricultural production.

For small scale planning (on the level of individual parcels) the above mentioned methodology proved to be too rough. So in cases when there is a mixture of different land usages planed within one small area a precise location of each of the usages is determined on the basis of valuing selected natural factors (geological foundation, hydrological conditions, soil type...), which are stable and they are on a small scale determining which land has higher production potential for agriculture, and as such is the most valuable for securing the potential for future food and fibre production.

### **Conclusions**

As the most important experience, learned from rural space planning and agricultural land protection in last few decades in Slovenia, we can name the fact that system of protection of agricultural land can't be dealt with separated from entire problem of rural space planning. Even

if protection of agricultural land might seem to be more of strategical agronomical problem of long term insurance of food and fibre production, this is not the case. Rural space use is wider system and changes in one sector have long term influence on others. Often first effects are noticeable in agricultural sector itself, with higher pressure on the best agricultural land, because the wide protection of all agricultural land brings to importance other factor then land production quality itself, what can then lead to general non rational use of rural space.

So to be able to secure the needed natural resources in rural areas the integrated rural space planning systems have to be used, which represent the only sustainable long term approach to successful and sustainable rural development.

## References

PROSEN, A., 1993 *Sonaravno urejanje podeželskega prostora*. 1. natis. Ljubljana: Katedra za prostorsko planiranje na Fakulteti za arhitekturo, gradbeništvo in geodezijo, 180 p.

ELLIOTT, C., UDOVČ, A., 2005 Nature conservation and spatial planning in Slovenia: continuity in transition. *Land use policy*. [Print ed.], vol. 22, p. 265-276,

KOVAČIČ, M., UDOVČ, A., PERPAR, A., MASLO, G., 2003 *Strateške usmeritve razvoja kmetijstva, gozdarstva in dopolnilnih dejavnosti na območju mestne občine Ljubljana*. Ljubljana: Inštitut za agrarno ekonomiko, Biotehniška fakulteta, Oddelek za agronomijo: Mestna občina Ljubljana, Oddelek za gospodarske dejavnosti in turizem.

Cotič, B. 2005 Spatial Planning System in Slovenia.

Source: [www.usaidspira.ba/docs/konferencija/drugi/Spatial\\_Planning\\_System\\_in\\_Slovenia.ppt](http://www.usaidspira.ba/docs/konferencija/drugi/Spatial_Planning_System_in_Slovenia.ppt)

Agricultural land act, Official Gazette of the SR. Slovenia 1973

PROSEN, A., MARUŠIČ, J., KOVAČIČ, M., UDOVČ, A., PERPAR, A., MIVŠEK, E., HUDOKLIN, J., KOSMATIN FRAS, M., VUGRIN, M., BOVHA, D., GROS, A., BARKOVIČ, J., PESEK, Grega., 2005 *Vrednotenje normativnega sistema varovanja kmetijskih zemljišč in opredelitev novih možnih javnih modelov : dopolnjeno končno poroč. proj. v okviru CRP "Konkurenčnost Slovenije 2001-2006"*. Ljubljana: Univerza v Ljubljani, Fakulteta za gradbeništvo in geodezijo - Katedra za prostorsko planiranje: Univerza v Ljubljani, Biotehniška fakulteta: IGEA, razvoj, svetovanje in storitve s področja geografskih informacijskih sistemov.

Platt, R., 1975 Land use contrlre: Interface of law and geography. Association of American Geographers, Resource paper, Washington, no 75.1.

# MSA AS THE ASPECT OF EUROPEAN MARITIME SECURITY

**MAREK GRZYBOWSKI<sup>1</sup>**  
**RYSZARD K. MILER<sup>2</sup>**

## **Abstract**

*Fear of terrorist interruptions has already affected the marketplace. Before 9/11, inventory had consistently trended downward as technology enabled just-in-time manufacturing and delivery of products. A significant breakdown in the maritime transport system would send shockwaves throughout the world economy. In fact, under the worst-case scenario, a large attack could cause the entire global trading system to halt as governments scramble to recover. Drastic and inefficient solutions may be put in place, such as the complete closure of some ports and duplicative and lengthy cargo checks in both originating and receiving ports.*

*The size of the maritime security challenge is as daunting as the terrible consequences of a serious attack. Maritime security involves hundreds of ports, thousands of miles of coastline, tens of thousands of commercial and private crafts, and millions of shipping containers. The maritime domain is truly global in nature, encompassing every ocean and the peoples and property of many nations.*

*This paper presents the idea of Maritime Security Operations (MSO) as an European inter-agency (military – civilian) latest response on maritime threat seen from wider perspective. Six strategic actions MSO requires to achieve synergy of civilian and military maritime security activities to address all maritime threats are pointed as well as four related Lines of Development (LoDs) to be taken forward by a partnership of European military and civilian authorities in order to create MSO Standard Operational Procedures.*

---

<sup>1</sup> Gdnya University Poland

<sup>2</sup> Gdnya University Poland

## **INTRODUCTION**

Maritime Security Operations (MSO) are defined as those measures performed by the appropriate civilian or military authorities and multinational agencies to counter the threat and mitigate the risks of illegal or threatening activities in the maritime domain. They may be acted upon in order to enforce law, protect citizens and safeguard national and international interests<sup>3</sup>.

Developing these operations will focus on terrorism, proliferation, narcotic trafficking, illegal migration, piracy and armed robbery. They might also include smuggling, the protection of national resources, energy security, the prevention of environmental impact and safeguarding sovereignty<sup>4</sup>. In defining these activities, it is to be understood that the lead in the majority of issues is not a military remit but that a successful strategy for an increasingly secure maritime domain lies in a coherent civilian and military partnership<sup>5</sup>.

## **THE MARKET**

Maritime transport is of fundamental importance to Europe and the rest of the world. To put this in perspective, over 90% of European Union external trade goes by sea and more than 1 billion tones of freight a year are loaded and unloaded in EU ports. This means that shipping is the most important mode of transport in terms of volume. Furthermore, as a result of its geography, its history and the effects of globalization, maritime transport will continue to be the most important transport mode in developing EU trade for the foreseeable future<sup>6</sup>. Below are listed some of the most important EU maritime transport indicators.

---

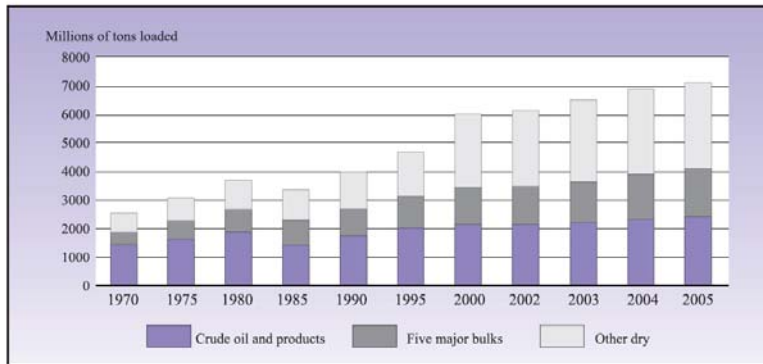
<sup>3</sup> <http://tide.act.nato.int/mediawiki/index.php> - 10.09.2007.

<sup>4</sup> White House, Office of Homeland Security, National Strategy for Homeland Security, 2002, at [www.whitehouse.gov/homeland/book/nat\\_strat\\_hls.pdf](http://www.whitehouse.gov/homeland/book/nat_strat_hls.pdf) (October 29, 2004), pp. 15–46.

<sup>5</sup> Bill Coffin, "Rough Water," *Risk Management*, Vol. 50, No. 3 (March 2003), p. 10.

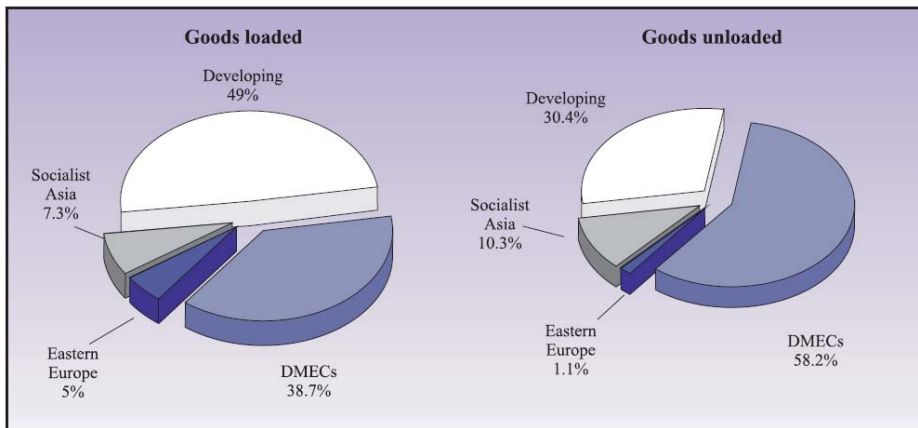
<sup>6</sup> Review of Maritime Transport, 2006. Report by the UNCTAD sekretariat, UN, New York and Geneva, 2006 pp. 16-69

Table 1. International Seaborne Trade In Selected Years



Source: Review of Maritime Transport, various issues.

Table 2. World Seaborne Trade By Country Groups (percentage share in tonnage, 2006)



Source: Compiled by the UNCTAD secretariat on the basis of data supplied by reporting countries and other specialized sources.

Table 3. Estimated Cargo Flows In Major Trades Routes (millions of TEU)

Year	Trans-Pacific		Asia-Europe		Transatlantic	
	Asia-USA	USA-Asia	Asia-Europe	Europe-Asia	USA-Europe	Europe-USA
2004	12.4	4.2	8.9	5.2	1.7	3.2
2005	13.9	4.3	9.9	5.6	1.8	3.3
% change	12.1	2.4	11.2	7.7	5.9	3.1

Source: Compiled by UNCTAD secretariat from *Containerisation International*, October 2005, p. 5.

In this context, European citizens have the right to expect their maritime passenger and goods transport to be safe, secure and clean. So, in support of these goals, and particularly in the wake of the *Erika* and *Prestige* oil tanker accidents, the set up of EMSA<sup>7</sup> (under Regulation (EC) N° 1406/2002 of 27 June 2002) is one of the key EU level initiatives aimed at improving the situation.

There has always been a requirement for appropriate levels of security on board ships and in ports. However, since the attacks on September 11th 2001 in New York, and following subsequent major incidents in Madrid and other cities, protection against terrorist actions has become a major concern around the world, including in many EU Member States. This concern has resulted in the allocation of significantly more resources and expertise to security issues than in the past.

The majority of terrorist surveillance, and response measures, set in place throughout the EU have been as a result of action at Member State level. These include measures to protect against terrorism in the maritime sector which vary significantly across the EU. In order to address the main issues for the EU as a whole, Directive 2005/65/EC was approved by the European Parliament and Council in October 2005. The primary objective of the Directive is to ensure that, as far as possible, appropriate levels of ship and port related security are provided in all Member States<sup>8</sup>.

The new International Maritime Organization's (IMO) International Ship and Port Facility Security (ISPS) Code became effective July 1, 2004—the first multilateral ship and port security standard ever created. The code requires all

---

<sup>7</sup> EMSA – European Maritime Safety Agency is the EU level provider of technical support in implementing Directive 2002/59, and this includes the following responsibilities: Provision of support to the European Commission in the development of the SafeSeaNet project, which is a pan-European electronic information system which deals with ship movements and cargoes. Management of SafeSeaNet and organisation of follow-up issues in cooperation with Member States' maritime administrations. Coordination of activities aimed at organising places of refuge around the EU coastline for ships in distress. Provision of technical support to the European Commission in its work in proposing amendments to Directive 2002/59. Monitoring of developments in IMO and IALA on long distance Automatic Identification Systems (AIS). Participation in regional meetings concerning the above items (eg HELCOM, Bonn Agreement, etc.). Participation in the work of the IMO ad-hoc working group on the engineering aspects of Long Range Identification and Tracking of Ships (LRIT). Access to the Shore based Traffic Monitoring Infrastructure Database (STMID).

<sup>8</sup> In order to achieve the fullest protection possible for maritime and port industries, port security measures should be introduced, covering each port within the boundaries defined by the Member State concerned, and thereby ensuring that security measures taken pursuant to Regulation (EC) No 725/2004 benefit from enhanced security in the areas of port activity. These measures should apply to all those ports in which one or more port facilities covered by Regulation (EC) No 725/2004 are situated.

nations to submit port facility and ship security plans, making port security a shared responsibility of all nations and shipping authorities<sup>9</sup>.

Security measures are being layered onto the global maritime industry at significant cost. The burden on owners of ship-related security measures is estimated at over \$1.3 billion initially and nearly \$800 million annually thereafter<sup>10</sup>.

Port security costs have been more difficult to estimate because of the uncertainty regarding the hiring of new security personnel and system-wide procedural changes resulting from advance notification rules recently mandated by United States Customs and Border Protection. Additionally, the industry may see long-term effects if new security requirements make maritime careers seemingly less rewarding, thereby reducing the pool of potential candidates.

## **THE THREAT**

The sea has already been used for terror attacks by boats armed with rockets, machine guns and other small arms, water borne improvised explosive devices and as an enabler for terrorist attacks. It is conceivable that a renegade ship such as an LNG (Liquefied Natural Gas) carrier could even be employed as a weapon near the centre of population. Continued use of the sea for logistic support to terrorism through the movement of arms, personnel or funds is substantiated by evidence. The maritime environment provides a potential conduit for CBRN (Chemical, Biological, Radiological, and Nuclear) material, both for the small high technology items, but also for larger items associated with weapon delivery. Other threats include cross-border illegal migration, which is forecast to increase significantly, and criminal activity including narcotics, human trafficking and piracy, all of which is increasing in sophistication and volume. These factors impact Europe's physical and economic security either directly or indirectly<sup>11</sup>.

---

<sup>9</sup> Donald Bowersox and David Closs, "Friction Economy," *Fortune*, February 3, 2003, pp. 104–110.

<sup>10</sup> Organization for Economic Co-operation and Development, "Security in Maritime Transport." [www.oecd.org/statisticsdata/0,2643,en\\_2649\\_34367\\_1\\_119656\\_1\\_1\\_1,00.html](http://www.oecd.org/statisticsdata/0,2643,en_2649_34367_1_119656_1_1_1,00.html) (October 29, 2004)

<sup>11</sup> For more information related to the piracy see: Michael Richardson, "The Pirates Who Could Sink East Asia," *South China Morning Post*, January 9, 2004, at [www.glocom.org/special\\_topics/](http://www.glocom.org/special_topics/)



In the European theatre of operations, nations are conducting MSO today as part of routine, peacetime duties in response to the threats mentioned above. Traditionally referred to as ‘Constabulary’ tasks, these operations are generally either conducted independently by member states’ navies and/or civilian maritime agencies in order to enforce legal powers and safeguard sovereignty or as part of multi-national military operations, which aim to safeguard common defence and security interests. In addition, there are a plethora of military and civilian initiatives at various stages of maturity which are seeking to enhance maritime domain awareness in parts of Europe<sup>12</sup>.

A European inter-agency approach to MSO would better safeguard common prosperity and security interests by protecting and supporting legitimate activities while countering the threat of current and emerging terrorist, hostile, illegal or dangerous acts within the maritime domain. By ensuring freedom of navigation and commerce, it would also promote regional, and contribute to global, economic stability and protect maritime trade as the heart of the regional and global economy<sup>13</sup>.

## ACTIONS REQUIRED

---

*asia\_rep/20040113\_asia\_s45/* (November 2, 2004). For an analysis of possible terrorist threats to one of chokepoints—the Strait of Malacca—see John Brandon, “Terrorism on the High Seas,” *International Herald Tribune*, June 5, 2003, p. 1.

Also Bruce B. Stubbs, “The Coast Guard and Maritime Security,” *Joint Force Quarterly*, No. 26 (Autumn 2000), pp. 95–99.; Margaret Wrightson, “Maritime Security: Progress Made in Implementing Maritime Transportation Security Act, But Concerns Remain,” testimony before the Committee on Commerce, Science, and Transportation, U.S. Senate, GAO–03–1155T, September 9, 2003, at [www.gao.gov/new.items/d031155t.pdf](http://www.gao.gov/new.items/d031155t.pdf) (November 2, 2004), p. 7.

For an up-to-date list of sources about modern maritime piracy, consult the bibliography compiled by the U.S. Naval War College Library, at <http://www.nwc.navy.mil/library/3Publications/NWCLibraryPublications/LibNotes/libModernMaritimePiracy.htm>. Political groups commit acts of piracy in order to gain publicity and extort hostage money.;

International Chamber of Commerce, “Piracy Takes Higher Toll of Seamen’s Lives,” January 28, 2004, at [dockwalk.com/issues/2004/march/piracy1.shtml](http://dockwalk.com/issues/2004/march/piracy1.shtml) (November 2, 2004). The International Maritime Bureau is a division of the International Chamber of Commerce.

<sup>12</sup> <http://tide.act.nato.int/mediawiki/index.php> - 10.09.2007.

<sup>13</sup> Organisation for Economic Co-operation and Development, “Security Maritime Transport,” at [www.oecd.org/statisticsdata/0,2643,en\\_2649\\_34367\\_1\\_119656\\_1\\_1\\_1,00.html](http://www.oecd.org/statisticsdata/0,2643,en_2649_34367_1_119656_1_1_1,00.html) (October 29, 2004). Estimates of global maritime commerce vary. For example, according to Bill Coffin, trade rose from 2.5 billion tons of cargo in 1970 to 5.5 billion tons in 2002, accounting for about 95 percent of international trade. Coffin, “Rough Water,” p. 10

MSO requires at least six strategic actions to achieve synergy of civilian and military maritime security activities in a co-ordinated effort to address all maritime threats:

- a. Political willingness at the national and international levels to develop an inter-agency approach to MSO. Given the civilian/military nature of this work, it will need to be taken forward outside a single institutional structure with the broad political backing of nations, international organisations and multinational agencies. It will be necessary to invigorate existing national and multi-national governance mechanisms to ensure that the real and potential benefits of MSO to European nations are fully understood<sup>14</sup>.
- b. International and Inter-Agency Cooperation. The benefits or the necessity of an international, inter-agency approach have been demonstrated over the world. The co-ordination of an inter-agency approach requires detailed work but it would need to involve international actors such as the EU (and its constituent agencies), NATO, United Nations International Maritime Organisation (IMO) as well as law enforcement authorities, in line with their responsibilities. The commercial sector would also need to be involved.
- c. The need to maximize maritime domain awareness. There are numerous ongoing initiatives within Europe, both civilian and military, which aim to create a comprehensive maritime surveillance capability and to share information. A strongly favoured near term approach for multinational co-operation on maritime domain awareness is to create a simple, unclassified picture of maritime activity based on information easily accessible and disseminated through IMO standards such as among others, the Automatic Identification System (AIS).
- d. The deployment of layered maritime security from the high seas to territorial waters, including littoral areas and port facilities. Nations currently monitor and act primarily within their territorial waters. Yet many of the threats originate in international waters where surveillance and powers to act are more limited. Effective MSO relies on the co-ordinated ability to maintain a comprehensive picture of

---

<sup>14</sup> John C. K. Daly, "The Terrorism Maritime Threat," United Press International, December 29, 2003.

maritime activity which encompasses territorial and international waters, and to act accordingly<sup>15</sup>.

- e. The need to embed security into commercial practices. With most of world trade travelling by sea, the maritime environment delivers many goods and services that are essential for society's needs. As the need for hydrocarbon-based energy grows, the need to safeguard maritime-related traffic will become more acute. Co-operation and partnership with commercial shipping agencies will be vital in order to progress a holistic approach to MSO which meets mutually agreed aims.
- f. The need to promote the necessary jurisdictional arrangements for effective MSO. National responsibilities extend from coastlines to the outer edge of territorial waters with another nation's unit unable to enter territorial waters without obtaining permission. Outside territorial waters, UNCLOS<sup>16</sup> allows nations' military and law enforcement vessels powers to act in specific instances (e.g. to board vessels suspected of piracy). The Proliferation Security Initiative (PSI) is an example of how nations, through Ship Boarding Agreements, permit the interdiction of Flag State ships in prescribed circumstances. While there is welcome progress in providing greater maritime enforcement powers as part of amendments to the IMO SUA<sup>17</sup>, the ability of ill-disposed elements to exploit weaknesses in the system remains.

## **THE STRATEGY**

The proposed approach for implementing a European, inter-agency strategy to MSO envisages four related Lines of Development (LoDs) to be taken forward by a partnership of European military and civilian authorities. LoDs respectively address inter-government, inter-ministry and multinational co-operation including as follow:

- Legal issues - Diplomatic and Co-operation LoD;
- Information exchange and maritime picture sharing - Information LoD;

---

<sup>15</sup> U.S. Congress, House of Representatives, "Maritime Transportation Security Act of 2002," Conference Report 107-777, at [thomas.loc.gov/cgi-bin/cpquery/?&db\\_id=cp107&r\\_n=hr777.107&sel=TOC\\_1236&](http://thomas.loc.gov/cgi-bin/cpquery/?&db_id=cp107&r_n=hr777.107&sel=TOC_1236&) (October 29, 2004), p. 4.

<sup>16</sup> United Nations Convention on the Law of the Sea.

<sup>17</sup> Convention on the Suppression of Unlawful Acts at Sea

- the operational contribution - Operational LoD;
- the participation of the commercial shipping sector - Economic LoD<sup>18</sup>.

The aims of mentioned above LoDs are:

- **Diplomatic and Co-operation LoD** - to promote national inter-ministry, inter-governmental and multinational co-operation for MSO in support and in the remit of UN, EU and NATO endeavours along with other actors involved - taking full advantage of existing frameworks.
- **Information LoD** - to ensure that existing maritime-related information exchange initiatives, both national and organisational, and at all levels, are examined to explore how networks might be linked, relevant information exchanged, and maritime pictures improved through a more coherent and efficient approach.
- **Operational LoD** - to contribute towards existing Security Strategies, encouraging maritime domain awareness, mutual understanding and the capability development required within nations in order to deliver an optimised operational contribution to MSO.
- **Economic LoD** - to encourage a better mutual awareness and understanding of how the commercial shipping sector might contribute to and benefit from MSO, most notably in the energy sector.<sup>19</sup>

And the objectives for the aims are:

- **Diplomatic and Co-operation LoD** - to create the appropriate environment to promote the civilian-military aspects of co-operation, information sharing and maritime surveillance and to co-ordinate the participation and actions of all organisations and member states.
- **Information LoD** - to transform live data into an information-led approach facilitating decision-making by appropriate national authorities responsible for and directing MSO.
- **Operational LoD** - to achieve a common concept of use of military assets in MSO amongst European maritime nations.
- **Economic LoD** - to embed necessary enabling elements of MSO within commercial practices<sup>20</sup>.

---

<sup>18</sup> “Marine Insurers Contemplate Increased Security Regulations,” Claims Magazine, December 1, 2003, at [static.highbeam.com/c/claims/december012003/marineinsurerscontemplateincreasedsecurityregulations/index.html](http://static.highbeam.com/c/claims/december012003/marineinsurerscontemplateincreasedsecurityregulations/index.html) (October 29, 2004), p. 12.

<sup>19</sup> <http://tide.act.nato.int/mediawiki/index.php> - 10.09.2007.

## CONCLUSION

To meet the threats of the global security environment it needs a strong and enduring partnership between civilian and military authorities. This approach would build on separate initiatives already in place and the respective strengths of countries, NATO and the EU as well as any other relevant body such as the IMO. Of course, there are numerous hurdles to overcome in bringing such an approach to fruition such as gaining agreement on the perception of the threat, the scope of MSO activities, the willingness to share information and the international jurisdictional arrangements required for effective action.

However, the timely fusing of maritime information, much of which is unclassified, would be the initial priority. Incremental gains in information sharing could allow operational co-operation to develop in slower time as mutual confidence builds. For an inter-agency approach to work it must draw together the strengths of the numerous organisations involved in addressing maritime security. The output would need to be seen as a valuable data to Governments, the commercial sector and the public. It must enable better use of limited resources to address the omnipresent, multi-national threat in the maritime domain.

During the next 20 years, maritime commerce will likely become an even larger and more important component of the global economy. The main elements of this transformation will probably include continued growth in the seaborne shipment of energy products, further adoption of containerized shipping, and the continued rise of mega ports as commercial hubs for transshipment and deliveries.

The challenges for maritime security are complex and growing. Addressing vulnerabilities, ensuring access to the maritime domain, and maintaining economic competitiveness while protecting “western world” interests from sea-based attacks will be no easy task for EU civilian and military authorities. The strategic nature of the challenge requires a strategic response. The next steps in that response must include further development of the MSA concept and maximizing the number of participating nations.

---

<sup>20</sup> Donald Bowersox and David Closs, “Friction Economy,” *Fortune*, February 3, 2003, pp. 104–110.

## References

- “Marine Insurers Contemplate Increased Security Regulations,” *Claims Magazine*, December 1, 2003, (October 29, 2004)
- Bill Coffin, “Rough Water,” *Risk Management*, Vol. 50, No. 3 (March 2003)
- Donald Bowersox and David Closs, “Friction Economy,” *Fortune*, February 3, 2003
- EU Directive 2005/65/EC - Enhancing Port Security.
- EU Regulation (EC) No 725/2004 - Enhancing Ship and Port Facility Security.
- [http://ec.europa.eu/transport/maritime/safety/2005\\_package\\_3\\_en.htm](http://ec.europa.eu/transport/maritime/safety/2005_package_3_en.htm)
- <http://tide.act.nato.int/mediawiki/index.php> - 08.09.2007.
- <http://tide.act.nato.int/mediawiki/index.php> - 10.09.2007.
- <http://www.emsa.europa.eu/end185d007d003d001.html>
- John C. K. Daly, “The Terrorism Maritime Threat,” United Press International, December 29, 2003.
- Organization for Economic Co-operation and Development, “Security in Maritime Transport.” Organisation for Economic Co-operation and Development, “Security Maritime Transport,” (October 29, 2004)
- Review of Maritime Transport, 2006. Report by the UNCTAD Secretariat, UN, New York and Geneva, 2006
- U.S. Congress, House of Representatives, “Maritime Transportation Security Act of 2002,” Conference Report (October 29, 2004)
- White House, Office of Homeland Security, National Strategy for Homeland Security, 2002, at [www.whitehouse.gov/homeland/book/nat\\_strat\\_hls.pdf](http://www.whitehouse.gov/homeland/book/nat_strat_hls.pdf) (October 29, 2004)

# ***CHALLENGES FOR THE EUROPEAN ENERGY MARKET***

**LIVIA ILIE<sup>1</sup>**

**ALEXANDRA HOROBET<sup>2</sup>**

## **Abstract:**

The changes and uncertainties that appear at the beginning of this century, is bringing Europe, as well as all other regions, in front of new challenges, especially in what concerns energy. The competitive landscape of the energy market is reshaped by a combination of trends: macroeconomic, social and business trends; and, of course, environmental trends. There are difficult strategic, organizational, operational, technological choices to be made in the context of changing climate, high demand of energy, high costs. And in this context, one should not forget a necessary partnership between Russia and Europe. Despite the apparent differences, both parties need the other more than they like to admit.

The paper aims to identify and analyze the major issues that develop in the energy market at the global level and the alternatives companies and governments have to take into account in order to face the challenges of the coming decades. Those that will make the right choices on the energy issues will make the difference in the market.

**Keywords:** energy, energy security, environment protection

---

<sup>1</sup> Senior Lecturer Phd., “Lucian Blaga” University, Sibiu, Romania.

<sup>2</sup> Senior Lecturer Phd., Academy of Economic Studies, Bucharest, Romania.

## INTRODUCTION

We are living times of change and uncertainties. Fundamental changes are taking place in the world today, and this is not only in the energy field. In this respect it is worth to mention:

- Changes in the geopolitical structures at the beginning of the '90s. The geopolitical structures that were inherited after the world war were fundamentally changed in early '90s from centralized economies to market driven systems.
- Effects of globalization. At the global scale the effects of globalization start to be felt.
- Extraordinary technological development. Technology is progressing at an extraordinary pace, putting in motion revolutionary changes.
- Acceleration of the world trade based on market policies. The lines between countries, markets are less visible.

In this general framework, we can identify specific major events that are shaping the energy sector:

- First oil shock 1973-74, that put in danger for the first time the energy consumer countries, so that they realized that the highly dependence on the Gulf oil is becoming risky. In 1973, several Arab nations, angered at U.S. support of Israel in the 1973 Arab-Israeli War, instituted an oil embargo against the United States and Holland. The Arab oil embargo came at a time of declining domestic crude oil production, rising demand, and increasing imports. The embargo was accompanied by decreased OPEC production, and with minimal global excess production capacity available outside OPEC, created short-term shortages and price increases.
- Oil price collapse in 1986. Faced with declining world oil demand and increasing non-OPEC production, OPEC cut output significantly in the first half of the 1980s to defend its official price. The sharp drop in crude oil prices pushed U.S. petroleum demand steadily higher in the second half of the decade. From 1985 to 2000, demand climbed from 15.7 million barrels per day to 19.5 million barrels per day.
- Accident at Chernobyl that took place on 26 April 1986 is the worst nuclear power plant accident in history and the only instance so far of level 7 on the International Nuclear Event Scale, resulting in a severe nuclear meltdown. The accident brought to attention the risk involved by the nuclear power energy. The accident raised concerns about the safety of the Soviet nuclear power industry, slowing its expansion for a number of years, while forcing the Soviet government to become less secretive. The now-independent countries of Russia, Ukraine, and Belarus have been burdened with the continuing and substantial decontamination and health care costs of the Chernobyl accident
- Environmental concerns and sustainable development, that leads to the World Conference at Rio de Janeiro in 1992, also known as the Earth Summit. Government officials from 178 countries and between 20,000 and 30,000 individuals from governments, non-governmental organizations, and the media participated in this event to discuss solutions for global problems such as poverty, war, and the growing gap between industrialized and developing countries. The central focus was the question of how to relieve the global



environmental system through the introduction to the paradigm of sustainable development. This concept emphasizes that economic and social progress depends critically on the preservation of the natural resource base with effective measures to prevent environmental degradation.

- Technological changes brought improvements in efficiency and cost reductions both for exploration and production.
- Energy demand changes as a reflection of the evolving economic structures of the global economy.

Looking to the energy sector, several emerging trends can be observed. Oil is cheaper than previously predicted and the discovery of additional reserves is technically feasible. The nuclear power has lost its momentum in Europe. Renewable energy technologies start to become more accepted. New organizational structures for gas and electricity utilities are experienced.

The demand for energy continues to grow. Even if the energy intensity of many products is down, energy consumption is increasing due to increased travel and leisure, greater competition in industrial markets, developing countries are looking for similar achievements.

The challenge is to understand the implications of these substantial shifts in geopolitical, social, economic and energy structures. The greatest need is for common understanding of the driving forces and shaping factors that determine evolving geopolitical relations, competitiveness and environment.

## 1. MAJOR TRENDS AFFECTING THE ENERGY SECTOR

What will make the world of 2015 different of today? Many researchers tried to identify the trends for the energy sector. They can be synthesized in six major factors that will shape the future energy sector:

1. **Shifting centers of economic activity.** Growth in demand for energy is moving from developed to developing countries, especially Asia – China and India 's oil demand will double from 2003 to 2020. Resources will be generally produced farther from the points of consumption. Important macroeconomic shifts are taking place in regions. Middle East expands also in other sectors than oil. The example of Dubai is obvious in this sense. Dubai emerged as a leading aluminum producer due to access to cheap energy and the proximity to the Asian and European markets. Global connectivity will bring greater market liquidity, more globally priced commodities. On the other hand more complex supply chains and geopolitical events will make prices more volatile.
2. **Rising demand, rising environmental concerns.** Due to accelerating economic growth especially in developing countries, the consumption of natural resources and energy will grow at an unprecedented rate – the impact is the need for massive investment in these industries to build production capacities. China, India, Russia and Middle East are making efforts to build power generation plants to meet growth in demand. According to International Energy Agency, the oil industry will need to invest 4.3 billion dollars until

2030. All this brings the question of energy security. Moreover, the environment is becoming more important for business: growing pressure to reduce greenhouse gas emissions. This brings to attention the renewable sources of energy like wind and solar power. By the end of 2020, renewables can provide more than 10% of electricity. In addition to the supply-side measures, there will be changes on the demand-side: world energy consumption could be reduced up to 25% by 2020 using energy more efficient, without compromising consumers' comfort. The solution is a concerted global effort to increase energy productivity (amount of output achieved per each unit of energy consumed). But market forces alone can not produce these outcomes due to information gaps, market-distorting subsidies, and inadequate financing infrastructure. To overcome these barriers, policy makers should make the price and use of energy more transparent, create new market-clearing and financing mechanisms, and selectively implement demand-side energy policies, while also encouraging demand-side innovation by companies.

3. **A changing consumer landscape.** A polarization in many markets is taking place: premium segments and no-frills offering – 1 billion new consumers in the developing world. Even if these consumers will have less spending power than the consumers in the developed countries, they have similar demands and access to global brands.
4. **The battle for talent.** The human factor, the talent will be in the future as important as the strategies for outsourcing today. Global labour markets are opening new sources for talent on the other hand there are many talent-intensive industries. In developing countries there are 33 millions university-educated professionals, more than twice as in the developed countries. The boom in the resource industries is asking for a huge demand of engineers and technical staff. The oil sector is looking worldwide for talented engineers to develop new technologies. The demand for petroleum engineers and project managers that can handle complex capital projects could double over the next decade.
5. **Emerging industry structures.** New structures are emerging due to changing market regulation and technology development. In the upstream, more economies of scale predominate, compared to the midstream where benefits of size are less clear. It is also place for small niche companies across the value chain of the energy sector (for example biomass technologies). As they will develop giants will tend to acquire these innovators. The combination of industry restructuring opportunities, growth attracted the interest of private equity that invested, for instance only in 5 years (between 2000 and 2005) up to 64 billions dollars.
6. **Business in the spotlight.** Everywhere, businesses are in the spotlight of societies: corporate responsibility, environment protection. Their large size, government corruption in unstable regions, their high profiles in local markets as monopolists represent issues for controversies in the societies. Energy companies must improve their policies in terms of safety and environmental protection.

All these trends put a lot of demands on companies and their management in the energy sector. Exploiting the shifts of fundamentals of competition will be an issue of survival in the coming decades.

## 2. ENERGY SUPPLIERS FOR EUROPE

Looking closer to Europe and its suppliers, one can identify Southern and Eastern countries of the Mediterranean and the Middle Eastern region to be of particular importance for the energy future of the European Union, and this for several reasons:

- as providers of energy from domestic resources
- as important energy transit routes
- as increasing importance as energy consumers

The Arabian Gulf region will continue to be the largest of Europe's suppliers of oil (potentially for gas, too). Gas production will increase consistently in North Africa (supplier of gas for Southern Europe). Former Soviet Union and Central and Eastern Europe gas is increasingly important both as domestic fuel and as vital export for Western Europe.

Overall gas is the fuel gaining most market share and it appears likely to continue to do so. Different fuels at different times dominated the fuel mix:

- in the '50s the king was the coal
- in the '60-'70s oil occupied the high ground
- following the first oil shock, urgent effort was made to diversify the energy supply and massive investment was made in nuclear power
- today, is the turn of gas to lead the energy investment

Current decades provide a wider fuel choice than before and the challenge is to maintain it in the new millennium.

### **Russia – an important player**

Looking to Russia's energy sector, some important characteristics should be considered:

- Russia has the world's largest natural gas reserves
- Russia has the second largest coal reserves
- Russia has the eighth largest oil reserves

Having these resources and taking into account China's rapid economic growth, India, the turmoil in Middle East, Russia's energy industry has bright prospects. Disruptions to world energy markets could be partially offset by increased Russian production. But this needs huge investments to increase production capacity: domestic capital and foreign one. Professor Morris Adelman from MIT pointed out in 2005 in *The Economist* "if the Arabs don't sell us oil, somebody else will". The somebody else could be Russia. The Russian oil industry may gain from the recent world developments. It has the oil needed by growing economies, however it will need to expand its production capacity to take advantage of the economic opportunities.

When in January 2006, Russia cut off flow of gas to Ukraine, there were alarm bells for European Union – despite the apparent differences between Russia and Europe, both sides need the other more than they care to admit. Europe has few economic alternatives for its energy needs.

For the western Siberian gas, the proximity and ability to pay of Europe makes it the most lucrative customer for Russia's gas. On the other hand, major European energy companies can be allowed to invest in Russia's energy sector to help develop the sector. Having these goals, action should be taken at different levels:

1. Russia and EU should implement regulatory reforms to reduce risk and facilitate investment.
2. Risk can not be totally eliminated and reforms will take years, so businesses and governments must seek ways to manage the remaining risk.
3. Working together to create more transparency in the market regarding supply, infrastructure capacity, changes in demand.

## **CONCLUSION**

The trend toward globalization appears to be well established, the internal market in energy and transport is progressing towards completion, technology is improving quickly and environmental issues remain at the heart of energy policy especially as regards climate change. Energy security remains a major issue too.

There are difficult strategic, organizational, operational, technological choices to be made in the context of changing climate, high demand of energy, high costs. And in this context, one should not forget a necessary partnership between Russia and Europe. Despite the apparent differences, both parties need the other more than they like to admit.

### **References:**

Directorate General for Energy (DG XVII), Energy in Europe – European Energy to 2020. A scenario approach, Special issue, Spring 1996

McGee, R.W, Prospects for Russia's oil industry, Andreas School of Business working papers, September 2005

Farrell, D., Nyquist,S., Rogers, M.C, Curbing the growth of global energy demand, The McKinsey Quarterly, July 2007

Bozon, I.J., Campbell, W., Lindstrand, M., Global trends in energy, McKinsey Quarterly, No.1, 2007

Bozon, I.J., Campbell, W, Vahlenkamp, T., Europe and Russia: charting an energy alliance, McKinsey Quarterly, No.4, 2006

[www.iea.org](http://www.iea.org)

# THE TERRITORIAL DIMENSION OF THE COHESION POLICY

**DELIA IONICĂ<sup>1</sup>**

**Scientific Adviser: PhD Mihai Korca<sup>2</sup>**

## **Abstract**

This paper will focus on exploring the territorial dimension of the cohesion policy of the EU as it was stated in the Community Strategic Guidelines on Cohesion, as being the capacity of the cohesion policy to adapt to the particular needs and characteristics of specific geographical challenges and opportunities. In this respect, the main territorial disparities, which led the EU decision factors to promote the territorial guidelines of the cohesion, will be emphasized. Particular attention will be paid to the various policies with impact on the territorial cohesion, as well as to the place of the territorial development on the European Agenda, namely the European Spatial Development Perspective and the Territorial Agenda of the European Union. In the end, the Romanian approach of the territorial cohesion will be presented in the framework of the programming period 2007-2013.

**Key words:** territorial features, disparities, cohesion

**JEL classification code:** F15 – Economic integration

---

<sup>1</sup> PhD Candidate, Academy of Economic Studies, Faculty of International Business and Economics, *e-mail:* [delia\\_ciorogariu@yahoo.com](mailto:delia_ciorogariu@yahoo.com).

<sup>2</sup> Professor PhD., Dean of the Faculty of International Business and Economics, Academy of Economic Studies, Bucharest

## I. INTRODUCTION

### What is “territorial cohesion”?

Economic and social cohesion is an expression of solidarity between the Member States and the regions of the European Union. The cohesion represents both a development objective of the European Union as set as such in the Art. 2 of the EU Treaty and a European policy with specific implementation instruments and clear guidelines, as they were defined for the period 2007-2013.

This status of cohesion is the result of a parallel evolution with the one of the European Union. It started with the identification of the need to “to promote economic and social cohesion and solidarity among the Member States” in the Art. 2 of the Rome Treaty and of the “aim at reducing disparities between the levels of development of the various regions and the backwardness of the least favoured regions or islands, including rural areas” in the Art. 158 of the same Treaty.

Based on these needs, the first steps were dedicated to the creation of social measures at European level, complementing the national ones, by instituting the European Social Fund, to the supporting of the population of rural areas, through the European Agricultural Guidance and Guarantee Fund (EAGGF), and later one, to addressing the specific structural problems of the regions, through the European Development Regional Fund (ERDF).

Thus, the regional policy has been defined with the aim at ensuring the balanced development throughout the European Union, reducing the structural disparities between regions and promoting equal opportunities for all citizens.

After being identified in the Single European Act (1986), the Treaty establishing the European Union promotes the *economic and social cohesion*, particularly the reduction of the disparities between the levels of development of the various regions and the backwardness of the least favoured regions or islands, including rural areas. In this regard, the Treaty states that both the national economic policies and European ones shall be conducted and coordinated in the way of strengthening the economic and social cohesion.

At the beginning, the economic and social cohesion has been built on the need of supporting the real convergence of the regional economies, as the most important territorial imbalance in the European Union is that between the less developed regions and the rest. Therefore, the core of the cohesion was represented by the regional policy, which is focused mainly on the NUTS II regions<sup>3</sup>. Only the measures oriented towards the cross-border cooperation have implied measures at the level of NUTS III regions.

However, the designing of the intervention measures aiming at addressing the regional disparities should take into account the specific features of the different parts of the regions, the diversity of the territory not only the regional economic and social indicators. It has to be taken into account that the main purpose of the NUTS classification is a statistical one and does not reflect the internal divergence existing within the regions. In the Second Cohesion Report it is recognised

---

<sup>3</sup> According to the Regulation (EC) No 1059/2003 of the European Parliament and of the Council of 26 May 2003 on the establishment of a common classification of territorial units for statistics (NUTS), the size of NUTS II regions shall lie in the population threshold of 800,000 – 3,000,000.

that the *spatial disparities in the Union reflect a more complex reality than indicated by differences in income and employment between regions*<sup>4</sup>.

The upsurge in interest and work in the spatial planning field, intensified in the 1990s, has drawn attention on the importance of using spatial planning in achieving the cohesion objectives, by taking into account the diversity of the EU territory. The decision makers (namely the spatial planning ministers of the Member States) started an intergovernmental work which was aimed at designing a non-binding spatial framework to provide a guide for the public policy making with territorial impact at all spatial scales, from the Community level to the regional and local levels. The result of this initiative was the adoption of the European Spatial Development Perspective (ESDP), by the informal Council of Ministers responsible for spatial planning and regional policy in Potsdam in 1999. The ESDP sets out policy guidelines for all Member States, regions and local authorities as well as for the Commission.

Promoting the “territory” as a new dimension of the European policy, the ESDP identified three main aims regarding the territorial development: *a polycentric urban development and a new relationship between urban and rural areas; equal access for all European regions to infrastructure and know-how and prudent management of the natural and cultural heritage.*

The adoption of the ESDP represented the beginning of the debate surrounding the concept of territorial cohesion and the evolution of a spatial dimension to the policy-making of the EU. As a result, the territorial dimension of the cohesion was introduced in the reform of the cohesion policy for 2007-2013, in the Community Strategic Guidelines for Cohesion and a Territorial Agenda of the European Union has been agreed on the occasion of Informal Ministerial Meeting on Urban Development and Territorial Cohesion in Leipzig, May 2007.

## **II. EUROPEAN TERRITORIAL DISPARITIES**

Before analysing the policy solutions identified in the main EU strategic documents, it is important to highlight the territorial facts which have led to raise the awareness on the great diversity of the EU territory and on the disparities therefore induced. In this respect, of analysing the territorial disparities, one of the main recommendation of the ESDP was “*the institutionalisation of a “European Spatial Planning Observatory Network”(ESPON), which should facilitate the exchange of information between the spatial research institutes of the Member States and the political co-operation between national spatial development authorities and the Commission.*

The ESPON and European Commission studies have provided the information on territorial divergences which have been highlighted in the Economic and Social Cohesion Reports and in the Interim Territorial Cohesion Report. The territorial imbalances emphasized in these studies and presented below relates both to the European level itself and to the regional and local levels.

---

<sup>4</sup> European Commission, *The Second Report on Economic and Social Cohesion*, 2001, pg. 5

### *Concentration of activity and population in Europe as core-periphery feature*

One of the traditional features of the EU territory is the high concentration of the economic activity in a core part of the Union, the so called “the traditional economic core” of Europe. Some studies refers to this area as being the “triangle”<sup>5</sup> extending from North Yorkshire in the UK to Franche-Comté in France and Hamburg in Germany, while others names it as being the so-called “pentagon”<sup>6</sup> delimited by London, Paris, Milan, Munich and Hamburg. Approximately 46,5% of the EU27 GDP is concentrated in this area, which covers only 14% of the territory and accounts about one third of EU citizens<sup>7</sup>.

However, one of the conclusion of the Forth Cohesion Report is that “the economic prosperity in the EU is becoming less geographically concentrated”, due to the emergence of new growth centres such as Dublin, Madrid, Helsinki, and Stockholm, but also Warsaw, Prague, Bratislava and Budapest.

If at the EU level, the status of the economic concentration starts to become a polycentric one, the core-periphery continues to manifest, however, at the level of the national territories of the EU Member States. The capital city regions concentrate the national economic activity throughout the regions, with the exception of Berlin and Dublin. According to the Forth Cohesion Report, the capital region’s share of national GDP increased by 9%, while their population grew by 2%, between 1995 and 2004. Moreover, in 2004, capital city regions produced on average 32% of the GDP in the country where they were situated, while they accounted for just 22% of population.

### *Urban areas as potential growth centres for regional competitiveness*

The role of urban areas as potential growth centres for regional competitiveness it is identified in the official documents as being one of the main territorial features of the EU territory. The metropolitan regions, cities and other urban areas play an important economic role, as localisation of the variety of activities, firms and institutes of higher education. Cities are home to change based innovation, spirit of enterprises and economic growth. Also, they are concentrating 80% of the European citizens and over 60% of the population in the European Union lives in urban areas of over 50 000 inhabitants<sup>8</sup>. In this respect, the urban areas are key driving forces for economic development as well as social cohesion and environmental improvement.

Taking into account the theory of urbanisation<sup>9</sup>, the urban system in Europe is characterised by to trends: suburbanisation (in 90% of urban agglomerations, population in the suburbs grew by

---

<sup>5</sup> *The Second Report on Economic and Social Cohesion* (2001), pg. 24

<sup>6</sup> *The Third Report on Economic and Social Cohesion* (2004) and *The Interim Territorial Cohesion Report* (2004)

<sup>7</sup> *The Territorial State and Perspective of the European Union*, ESPON, 2006

<sup>8</sup> Communication to the Council and Parliament ‘*Cohesion Policy and cities: the urban contribution to growth and jobs in the regions*’.

<sup>9</sup> According to the theory of urbanisation differential, all city systems ideally undergo various phases in their development, passing through a complete cycle of urbanization (polarisation), polarisation reversal and counter-urbanisation. These various stages of urbanisation have been conceptualised in terms of urbanisation (population increase of the city’s core), suburbanisation (increase of the ring, decrease of the core), disurbanisation (decrease of core and ring), and re-urbanisation (increase of core, decrease of ring).



more than in the core city, with few exceptions) – according to *the Fourth Cohesion Report* - and counter-urbanisation, i.e. a flow of people down the urban ladder from larger to smaller urban settings – according to the *Interim Report of the Territorial Cohesion*.

### *Specific urban-rural relationship*

According to *The Territorial State and Perspective of the European Union*, up to 80% of the European territory can be characterised as rural or semi-rural, if it is considered the low influence of cities in these areas and the more rural land-use and low population density.

The urban-rural relationship differs widely throughout EU, with the effect of a growing urban-rural interdependence. The most frequently urban-rural relationships are as follows:

- rural areas situated near urban areas and tend to become part of the urban system due to the suburbanisation process and the boundaries tend to become blurred, the relationship being dynamic and complex; R&D activities are increasingly located in attractive semi-rural/semi-urban environments in the proximity of large towns;
- cities and towns located in urban areas represents development poles in these areas by valorisation of local assets while using the modern technologies; agriculture is carried out in an increasingly industrialised fashion, which means that traditional environmental values connected to rural environments are disappearing and the industries are relocating from urban to rural settings on a large and global scale;
- rural areas, especially in remote areas, facing demographic challenges as population ageing and loss of working-age people, especially better-educated younger people.

### *Regions with geographic handicaps and other constraints*

Islands and archipelagos, mountain and peripheral areas - including the ‘outermost’ regions - are an important part of the Union and share many common physical and geo-morphological characteristics and economic disadvantages. These regions generally suffer accessibility problems which make their economic integration with the rest of the Union more of a challenge.

Border regions present another category of territorial issues, often suffering from problems of accessibility and lack of economic opportunities because of the fracture created by an international frontier. With the creation of the single market, backed by cross-border cooperation programmes supported by European funds, for the most part, existing internal border regions no longer show significant differences in income per head and unemployment compared to the Union as a whole, the main problem areas being in the east along frontiers with third countries.

### *Other European territorial features*

The above presented disparities are only the most important and visible features which characterises the EU territory, being the traditional issues raised when the territorial development comes into discussion. The analyses produced under the EPSON and EC initiatives underpinning the new *EU Territorial Agenda* reveal a wider range of factors which influence the structure of the EU territory. The new approaches and developments highlight as territorial issues: innovation and R&D activities (concentration of R&D expenditure in large metropolitan areas, in the core of Europe and the Nordic Countries); risk management (dealing with both technological and natural hazards – floods, droughts, fires, climate change or accidents); Information and Communication Technologies; transport and energy (different accessibility degrees throughout the EU territory and by transport mode, with the concentration of road and rail accessibility in the core of Europe, while the air accessibility shows a more polycentric development, need of stable energy supply and different import dependencies between the Member States, high sensitivity to energy price in the New Member States), environment, nature and culture.

### **Policies with Territorial Impact**

In most cases, the objectives of EU policies - as defined in the Treaties – do not have a spatial character. Yet they have a significant impact on the territory of the EU. The spatial impact depends on the specific method of intervention - whether it is of a financial (e.g. income support, regional and horizontal structural measures, sectoral measures such as research programme financing), legislative (e.g. competition rules, market liberalisation, environmental legislation, market-based instruments) or planning (e.g. trans-European transport and energy networks) nature. EU planning directives, for instance the directive for the establishment of a coherent integrated biological network, intervene in land use. In addition, a number of Community policies directly influence the behaviour of economic players. Moreover, their actions are partly determined by market forces, which are in turn reinforced by the Single Market.

The spatial effects of Community policies do not automatically complement each other, in line with a more balanced regional development. Nor do they automatically correspond to the development concepts of regions and cities. Without a reciprocal fine-tuning process, they can unintentionally aggravate disparities in regional development if they are exclusively geared towards specific sectoral objectives.

The following are the most important treaty headings providing the European Commission with the basis for action with implications for spatial development in the EU: EU cohesion policy, the Common Agricultural Policy (CAP), Community Competition Policy; Trans-European Networks (TEN); environment policy; Research and Development policy; energy policy, fishery policy.

### **III. EU POLICY SOLUTIONS TO ADDRESS THE TERRITORIAL IMBALANCES**

As mentioned in the *Introduction*, the result of the territorial debates concluded in highlighting and promoting the territorial dimension of the cohesion in the Community Strategic Guidelines for Cohesion 2007-2013 and in the adoption of the Territorial Agenda of the European Union in Leipzig, May 2007.

Based on the highlights of the *Third Cohesion Report* regarding the territorial disparities, the *Community Strategic Guidelines for Cohesion 2007-2013 (CSG)* tries to address the territorial imbalances in order to promote the harmonious development of the EU regions.

The Cohesion Policy for 2007-2013 can be characterised through a more developed territorial orientation of the interventions, as it has been before, by promoting the territorial dimension of cohesion in the CSG, the indicative framework for the intervention of Structural and Cohesion Funds and through establishing a special objective under this policy – “The European Territorial Cooperation”.

Taking on board the territorial dimension, the CSG promotes the importance of geographical circumstances in concentrating financing resources and will help to develop sustainable communities and to prevent uneven regional development from reducing overall growth potential. It will also represent a part of the effort to attract the European territory to contribute to the growth and jobs agenda.

Such an approach also requires that the specific problems and opportunities of urban and rural areas may need to be addressed as well as those of particular territories such as cross-border and broader transnational areas, or regions suffering from other handicaps due to their insularity, remoteness (such as the outermost or Arctic regions), sparse population or mountainous character.

After a short and scarce description of some territorial problems, the CSG establishes the guidelines which should be promoted in order to enhance the territorial cohesion. These guidelines cover the following issues:

- The contribution of cities to growth and jobs;
- Support the economic diversification of rural areas, fisheries areas and areas with natural handicaps;
- Territorial cooperation – cross-border cooperation, transnational cooperation, interregional cooperation.

The last guideline represents the essence of the newly created objective – *the European Territorial Cooperation (ETC) objective*. Therefore, the aim is to promote the strengthening of *cross-border cooperation* through joint local and regional initiatives, strengthening *transnational cooperation* by means of actions conducive to integrated territorial development linked to the Community priorities, and *strengthening interregional cooperation* and exchange of experience at the appropriate territorial level. The ETC objective is financed from ERDF, while the cooperation along the external borders of the Community will entail the additional use of the instruments of the Community's external assistance, in particular a European Neighbourhood and Partnership Instrument (ENPI) and the Instrument for Pre-Accession (IPA). Thus, the cohesion policy is not the single tool used to achieve the territorial cohesion, and the European neighbourhood policy and the enlargement policy.

This objective is not something innovative at the European level, even if represents a new approach of the cohesion policy. The cooperation as policy option was promoted within the ESDP: “In applying the policy options, Member State government and administrative agencies as well as EU services should consider, at an early stage, sectoral and spatial conflicts and timing difficulties and set the right priorities. This requires new ways of cooperation, which according to the ESDP’s principles should be on a voluntary basis. [...] The ESDP recommends three levels for spatial cooperation: the Community level, the transnational/national level, the regional/local level.”<sup>10</sup>

Overall resources for the ETC objective amount to 2,52 % of the total resources allocated under Cohesion Policy (approximately EUR 7.750 billion in 2004 prices) and this amount is distributed as follows between its three types of intervention: 73.86% for the financing of *cross-border cooperation*; 20.95% for the financing of *transnational cooperation*; 5.19% for the financing of *interregional cooperation*, cooperation networks and exchange of experience between regions.

### **Territorial Agenda of the European Union**

After agreeing on the ESDP as being a policy framework for the Member States in 1999, without establishing any new responsibilities as the Community level, the decision makers felt the need of more pragmatic cooperation framework in the field of spatial development. Taking into account the impact of enlargement and the challenge of achieving the Lisbon objective in such wide variety of territorial imbalances, the ministers responsible for spatial planning and development, together with the European Commission, presents the *Territorial Agenda of the European Union – Towards a More Competitive and Sustainable Europe of Diverse Regions*, which represents an action-oriented political framework for future cooperation of the Member States , having as future task: strengthening territorial cohesion.

The spatial development decision makers have agreed on the following priorities to be promoted in order to achieve the territorial development of the EU territory:

1. Strengthening the polycentric development and innovation through networking of city regions and cities
2. Promotion of new forms of partnership and territorial governance between rural and urban areas
3. Promotion of regional clusters of competition and innovation in Europe
4. Strengthening and extension of Trans-European Networks
5. Promotion of trans-European risk management including the impacts of climate change
6. Strengthening of ecological structures and cultural resources as the added value for development

In addition to the ESDP, the Territorial Agenda is provided with a special chapter referring to the implementation of the Territorial Agenda. This chapter foresees actions and responsibilities for the European institutions and the EU Member States, as well as specific activities for the

---

<sup>10</sup>*European Spatial Development Perspective*, pg. 35

ministers themselves. A special attention it is paid to the programmes promoted under the ETC objective of the cohesion policy, emphasising the importance of those facilitating analyses and studies referring to territorial cohesion (ESPON 2013 and URBACT II). The ministers commit themselves to integrate the political priorities of the Territorial Agenda and the territorial aspects of the CSG 2007-2013 in the national, regional and local development policies.

#### **IV. TERRITORIAL COHESION IN ROMANIA**

Romania, as Member State, is benefiting of an important allocation of the Structural and Cohesion Funds for the period 2007-2013. In this respect, a strategy for the implementation of the cohesion policy in Romania has been developed in the National Strategic Reference Framework (NSRF), based on the guidelines established by the European Commission in the *Community Strategic Guidelines for Cohesion*.

Under the NSRF, four thematic priorities and a territorial priority have been identified, based on the analysis of the current situation performed by the national authorities. The territorial development priority responds both to the Convergence and Territorial Cooperation objectives, and is meant to address the territorial disparities identified at the level of the Romanian territory.

Until recently, Romania's land and urban planning policy has been somehow separated from the economic planning but the prospect of EU accession has fostered an integrated approach of the development process. In October 2005, the Romanian Government initiated and approved the guidelines of the *Strategic Concept of Spatial Development and Integration into the European Spatial Structures 2007-2025 (SCSD)*.

The guiding lines of the SCSD focus on the orientation of national efforts towards creating a Romania capable of defining and taking responsibility for its future development and the role it can play in the EU and globally. Having in mind the ESDP, the Lisbon Agenda and the Gothenburg Strategy, the SCSD facilitates the valorisation of Romania's potential at regional, inter-regional, national, cross-border and trans-national levels, based on polycentric development, balanced accessibility to physical and knowledge infrastructures, new urban-rural relationships and the proper management of natural and cultural patrimony.

An important dimension of the planning and implementation of the national and regional development policy is the territorial dimension. For Romania, an efficient spatial and land use planning is an important factor for ensuring sustainable development and integration into the European economic development structures.

The key regional disparities issues identified within the socio-economic analysis of the National Development Plan 2007-2013 are: increasing development disparities between Bucharest-Ilfov Region and the other Regions; unbalanced development between the eastern and the western parts of the country; concentration of chronic under-development in the East, on the border with Moldova and in the South, along the River Danube; existence of important intra-regional disparities that reflect a mosaic pattern of the economic development and within some regions the coexistence of underdeveloped areas with relatively developed areas; decline of the small and medium-sized towns, especially of the mono industrial towns, generated by the industrial restructuring; socio-economic decline of many large urban centres and the diminishing of their role they have on the development of adjacent areas; insufficient local experience in the

management of the regional/local development programmes.

The territorial strategy of the NSRF responds to the territorial development needs of Romania and aims to ensure the coherence of the investments and strategic actions planned, as well as to achieve the highest impact in terms of economic and social development.

Thus, the NSRF will seek to contribute to stopping and hopefully reversing the widening trend of regional development disparities in line with the National Strategy for Regional Development and the development strategies of the eight NUTS II Regions, by improving infrastructural conditions, business environment and the human capital for facilitating economic growth. In the process, a special attention will be given to the development and valorisation of the local and regional capital and to maximizing the competitive advantages of the regions.

The strategy will have a polycentric approach by targeting the development of the national urban network. Urban areas act as engines of economic growth for regions and sub-regions, and especially for the surrounding rural areas. Therefore, the strategy seeks to provide the necessary conditions for tapping the urban potential and enhancing the contribution of cities to growth, jobs and social cohesion in the regions.

Within this framework, the NSRF strategy will target development of existing or emerging growth poles/corridors. It will seek to create the conditions for concentration of development in areas around the poles/corridors as well as an efficient connection network at regional, national and trans-European level. The dynamic regional poles will be reinforced through improved accessibility and interconnectivity, better conditions for living and for business development, more efficient use of the human resources and better governance.

According to the Romanian NSRF, the territorial cohesion in Romania will be promoted by orienting the financial intervention towards the following priorities:

- *Regional cohesion*, by stimulating the areas with growth potential and helping the lagging behind ones, including rural areas. In this context, the strategy will give high importance to promoting a polycentric approach to development and to enhancing the role of urban centres as regional drivers.
- *Sustainable urban development*. Within the polycentric approach of development, the role of the urban centres will be reinforced, by promoting the investment in physical regeneration, environment and social services and the support for improvement of entrepreneurship in the urban centres, but be also a special attention will paid to the revitalization of suburbs and some neighbourhoods (districts) with socio-economic and environmental problems.
- *Sustainable Rural Development*<sup>11</sup>. The overall national strategy aims to apply a multifunctional model for the agricultural and rural development by promoting a balanced development of both the agricultural and non-agricultural functions of the rural areas.
- *Promote European Territorial Cooperation*, which respond to the ETC objective. The general principles of the strategy for the ETC programmes are to ensure effective social and economic integration in the border areas and increased activity and accessibility to the

---

<sup>11</sup> This strategy will be supported mainly through the interventions of the European Agricultural Fund for Rural Development (EAFRD) and European Fisheries Fund (EFF), as well as through the Structural and Cohesion Funds, under a coordinated approach.

Romanian regions within Europe. In this respect, the strategy will focus the resources as follows:

- *Cross-border Cooperation.* Under this sub-priority, Romania will participate, jointly with its neighbours, to the following operational programmes:
  - on the internal borders (CBC Hungary–Romania Operational Programme (OP) and CBC Romania- Bulgaria OP)
  - on the external borders (IPA CBC Romania – Serbia OP, ENPI CBC Romania – Ukraine – Moldova OP, ENPI CBC Hungary – Slovakia – Romania – Ukraine OP, ENPI CBC Black Sea Basin OP)
- *Transnational Cooperation.* Romania is participating to the South East European Space (SEES) Transnational Cooperation OP, next to other seven Member States (Austria, Bulgaria, Greece, Italy, Slovenia, Slovakia and Hungary) and eight non-Member States (Albania, Bosnia&Hertegovina, Croatia, Moldova, Montenegro, Serbia, Ukraine). The general objective is to strengthen cohesion, competitiveness and stability by enhancing cooperation and improving integration by ensuring sustainable development in SEES.
- *Interregional Cooperation.* Romania will participate as partner or Lead-partner in joint projects proposed within all four new programmes promoted under this sub objective: 1. *The Interregional cooperation programme (INTERREG IVC) - Contributing to the “Regions for Economic Changes”* intends to link regions and cities with comparable problems and opportunities with the end to promote the transfer of know-how and the exchange of experience among government and regional agencies and equivalent. 2. *The URBACT II Programme – Integrated urban development transnational exchange* is an European network for exchange of experience on key urban policy fields for the achievement of the European strategy aims and will allow European cities to learn from each other. 3. *The ESPON 2013 Programme* aims to support the reinforcement of regional policy with studies, data and observations of development trends and to build a European scientific community in the field of territorial development. 4. *The INTERACT II Programme - INTERREG Animation Cooperation and Transfer* has a wide geographical scope covering the 27 Member States and neighbouring countries involved in the ETC Objective programmes. The core mission of the INTERACT II Programme is to identify, to describe and to spread good governance approaches and practices of cross-border, trans-national and interregional cooperation across the EU.

## V. CONCLUSIONS

The territorial cohesion has become one of the subjects which are most frequently used by the European officials and in the official documents. This happened in the context of enlargement which made the EU territory more diverse than ever, with more imbalances which need to be addressed through specific measures.

After the adoption of the ESDP and institutionalisation of ESPON, the various studies and analyses underpinned the strategic approach of the territorial cohesion which has been further developed. The recognition of the importance of this dimension of the cohesion has led the high

representatives of the EU to add the territorial cohesion to the economic and social cohesion in the draft EU Constitutional Treaty in 2004 and to take it over in the new *Draft Treaty amending the Treaty on European Union and the Treaty establishing the European Community*.

## References

- \*\*\*\*European Commission, *The Second Report on Economic and Social Cohesion*, 2001
- \*\*\*\*European Commission, *The Third Report on Economic and Social Cohesion*, 2004
- \*\*\*\*European Commission, *The Fourth Report on Economic and Social Cohesion*, 2007
- \*\*\* European Commission, *Interim Territorial Cohesion Report*, 2004
- \*\*\*\*Council Decision No 702 on “*Community Strategic Guidelines on Cohesion*”, 2006
- \*\*\*\**Territorial Agenda of the European Union – Towards a more competitive and sustainable Europe of Diverse Regions*, Inform Ministerial Meeting on Urban Development and Territorial Cohesion, May 2007
- \*\*\*\**European Spatial Development Perspective - Towards Balanced and Sustainable Development of the Territory of the European Union*, Informal Council of Ministers responsible for Spatial Planning in Potsdam, May 1999
- \*\*\*\*The territorial State and Perspective of the European Union, ESPON, 2006
- \*\*\*\*Communication to the Council and Parliament, *Cohesion Policy and cities: the urban contribution to growth and jobs in the regions*, 2006
- \*\*\*\**National Strategic Reference Framework 2007-2013 for Romania*, [www.fonduri-ue.ro](http://www.fonduri-ue.ro), 2007



# **THE SOCIAL RESPONSIBILITY OF THE COMPANY – FACTOR OF SUPPORTING THE EUROPEAN ECONOMIC DEVELOPMENT**

**ANDREEA-DANIELA GANGONE<sup>1</sup>**

## **Abstract**

The experience of the developed countries has drawn our attention to the fact that a company cannot develop efficiently from an economic point of view unless it develops socially, at the same time. As organizations managed to understand this, they have also started to take on social obligations, in close relation to their economic objectives. At present, the taking on of social responsibilities has become a fundamental aspect in the society of organizations because the modern organization has, and even more, must have social power.

Thus, the success of the Romanian organizations on the large European market essentially depends on their capacity of understanding and integrating in their activity, efficiently and operatively, responsibilities towards society. This aspect is all the more important given that, through their social objectives, the organizations will always exceed the limits of the local communities in which they act. Practically, the social results of the organizations, regardless their origin, British, Italian, French or Romanian, have European impact, not a local one, and they represent one of the most important factors of supporting the European economic development, on long term.

**Keywords:** social responsibility of the organization, social power, social objectives, social results, durable development

**JEL classification:** M14 - Corporate Culture; Social Responsibility

---

<sup>1</sup> Assistant Professor, PhD. Candidate, “Constantin Brâncoveanu” University, Pitești, Romania, andreeagangone@yahoo.com.

The central element of the classical economic theory was the fact that the organizations had a single responsibility – the economic efficiency. For many decades this principle has represented the essence of the mission of the economic organizations that have carried out their activity starting from the premise that they had to satisfy a single category of interests – those of the shareholders.

This economic mentality led to what we call today “the period of wild capitalism,” respectively to an abusive behavior of the organizations on their employees, consumers, environment, and society, in general.

More important is the fact that this behavior has generated the aggravation of some social and environmental issues, and has caused the appearance of some new ones and it will not be possible to solve them, not even on long term.

But the becoming aware of the effects caused by this type of behavior has led to substantial mutations in the economic theory and practice, mutations that essentially refer to the fact that the organizations have not only economic responsibilities, but also other types of responsibilities, among which the most important are the social and ecological ones.

On the other hand, the lack of ecological and social responsibility of organizations, in their effort of achieving their economic objectives, combined with economic-social dynamism, has determined the growth of the citizens’ expectations, and governments are no longer able to meet these expectations on their own.

This apparent failure of the government of meeting the pressing social requirements has determined the society to focus its attention towards other social actors, namely the economic organizations, starting from the premise that these have the moral duty and the economic capacity of contributing to the growth of the society’s welfare, to the mutual benefit of these.

A new concept in the economic theory was outlined based on this change of mentality, namely the concept of social responsibility of the organization.

I say social responsibility of the organization and not corporate social responsibility, as this concept is most often mentioned in the specialized literature, because, in my opinion, this does not only refer to the activity of the big transnational corporations, although their international activity obviously generates infinitely more problems with a non-economic character, and thus, infinitely more non-economic responsibilities, but also the activity of any economic organization, regardless its sphere of action.

The concept of social responsibility of a company has its roots in the practice of the American firms, one of the first companies that has answered positively to the new social expectations being the McDonald’s company, which in the ‘50s had adopted in its activity the *give back to the community you are part of principle*.

Subsequently, this way of approaching the economic through the point of view of the social has become a genuine business philosophy for more and more companies around the world.

In the specialized literature, the concept of social responsibility of the company has quite a large number of definitions that, although formulated from different perspectives, support the same basic idea according to which the organizations’ activity must lead to meeting the expectations of all the partners interested in this activity, regardless their nature.

For example, there are specialists who consider social responsibility as being that type of management that takes into consideration the economic and social effects of its decisions [Boone E. L., Kurtz D. L., 1992, p. 38].

The concept of the organizations' social responsibility has also been defined as being the managers' obligation of undertaking actions that protect and improve both the welfare of the society, seen as a whole, and the company's interests [Certo C. S., 2002, p. 76].

Other authors consider that the social responsibility is the well-established obligation of a company, beyond its legal obligations or those imposed by the economic restrictions, of pursuing the long-term objectives that are in the interest of the society [Popa I., Radu F., 1999, p. 258].

Finally, social responsibility was also defined as a specific way of making decisions according to some standards in order to have favorable effects on those interested in the company's activity [Puiu Al., 2004, p. 145].

In my opinion, generally speaking, the social responsibility represents the degree of empathy shown by an organization in relation with the partners, financially or non-financially, directly or indirectly interested in its activity.

According to the definition given by the European Commission, in order to be socially responsible, an organization must integrate into its actions and strategies the social and environmental issues related to the interactions in which it is involved [Diaconu B., Oancea D., 16 – 22 April 2007]

The year 2000 marked an accentuation of the European Union's preoccupations for ensuring the social responsibility of its organizations. Thus, on one hand, there was a growth in the importance of the volunteer side of the social responsibility practices, the organizations being encouraged to take on extra ethical and social responsibilities as compared to what the law stipulated.

On the other hand, there have been attempts to surpass the classic charitable behavior, based on donation, and the creation of some relationships equally profitable with the market and the social environment, on long-term, was encouraged [Diaconu B., Oancea D., 16 – 22 April 2007].

Romania's integration into the European Union generated, among our co-nationals, hopes, more or less justified, regarding the raise of the level of living and of the life quality. On the other hand, most of the Romanian economic agents see our country's accession to the European Union as a source of serious difficulties that will lead, in the end, to the disappearance from the market of the business that will not succeed to meet the new requirements.

Indeed, the fears of the Romanian companies are justified, because the fields considered as being the most important for ensuring the economic success in the European companies are seen as unimportant or non-profitable by the Romanian entrepreneurs.

Nowadays, the most obvious difficulties for the Romanian companies are those related to the administration of the material and financial resources, being in correlation with an emphatic preoccupation to protect the natural environment. Concomitantly with the solving these difficulties, the Romanian managers will have to take into consideration the consumers more than in the last 15 years, by carrying out economic activities in such a way so that it does not affect the integrity or security of the latter.

On medium-term, it is also expected to have positive changes in what concerns the observance of the employees' rights and liberties, an aspect that involves the necessity of drafting some new personnel policies and, obviously, the growth of the company's general costs.

On long-term, the Romanian companies will have to re-think the entire business philosophy in the terms of an extended responsibility that will include not only the investors, clients or employees, but the entire Romanian community.

But nowadays the companies' social responsibility, a very fashionable topic in the developed countries and object of some complex enactments, remains something unknown to most of the Romanian economic agents.

Nevertheless, it can be seen that the year 2000 represented a key moment in the Romanian economy, regarding the growth of social responsibility of the economic agents.

Thus, if in the first decade of free economy, most of the Romanian companies only focused on the issue of survival, and most of the business people only focused on the short-term profit, after the year 2000 we can identify a series of companies that have reconsidered their mission and objectives from the perspective of the social responsibility.

Nowadays, in Romania, the issue of the companies' social responsibility, far from being ignored, is regarded with interest. Although the terminology of the term is not well understood by everybody, on the list of the consumers' expectations the requirements regarding the correctness of the price policy occupies an important place, as well as health protection, good working conditions, getting involved with the community's problems, and environment protection [Brady A., [www.csr-romania.ro](http://www.csr-romania.ro), 28 January – 4 February 2007].

In this regard, an opinion poll made by **BMG** in 2005 on 160 companies having an activity in Romania, emphasized the fact that the sums donated by these companies over the years 2003 and 2004 varied between 500 Euros and 2 million Euros, the uncontested leaders in this field being Romtelecom, with 1 million Euros allotted during the 2 years, and the Romanian Commercial Bank, with 2 million Euros [Biz Magazine, nr. 103/2005].

Most of the companies that answered the opinion poll stated that they intended to invest at least as much in the social field and in the future, and seven of them stated that they would considerably increase the funds allotted to the responsibility towards society.

More concretely, the Romanian economy can provide nowadays enough examples of companies with mature social policies, with complex charitable strategies and with real social results.

But most of these companies are branches of some organizations with international activity that have imported the charitable strategy promoted on the origin market, but not as an answer to the pressure of the market or to the requirements of the public, but as an integral part of their entire corporate strategies.

For example, **McDonald's** company entered the Romanian market in 1995 when it opened the first restaurant in Bucharest. In 1998 the Foundation for Children Ronald McDonald was founded, adopting the western model, a foundation that entirely overtook the carrying out of charitable actions.

The first important program of the company was "**Operation Smile**," carried out in 1999 when McDonald's sponsored the arrival of an international team of plastic surgeons who operated on almost 200 children with facial congenital malformations [Capital, No. 40/2003].

Another important project of the foundation was "**Millennium dreamers**" accomplished in 1999, a project that compensated the initiatives of almost 2,500 children worldwide who enjoyed a trip to Disney World Resort in the USA. Ten children with ages between 10 and 14 left from Romania, accompanied by a parent.

In order to win this prize the children wrote an essay in which they described what they have done for the community where they lived. The company's preoccupations continued in the following years with the same intensity.

The initiatives of McDonald's company are really praiseworthy, especially if we take into consideration the fact that between 1995 – 2003 it did not have profit.

Philip Morris Romania offered another interesting example, when the company took over the factory from Otopeni. In collaboration with the city hall from Otopeni, the company came to know the social problems that the community dealt with and chose an original method to contribute to the improvement of the situation.

Philip Morris Romania founded a *Canteen for the Poor* in which one hundred under-privileged people continue to eat today, every day, people selected from widows with more children who live on family allowance, war veterans, handicapped people who live on pittance social allowances [Evenimentul zilei (The Event of the Day), 22 October 2002].

**Shell Romania** company initiated in 2002 a project financed by the Shell foundation with the sum of \$330,000, a project that aims to encourage young people with ages between 18 and 30 to start their own business. The project is called "*You really can,*" and it is carried out together with the Center for Economic Development and it is meant for a three-year period [Capital, No. 44/2003].

A praiseworthy initiative was also adopted by **Coca-Cola Romania** company which, in 2003, mobilized around 250 employees from all the cities in which it has branches and factories: Bucharest, Ploiești, Timișoara, Oradea, and Constanța, and the employees worked to recondition some parks, paint fences, clean and rearrange the playgrounds for children [Capital, No.29/2003].

The Coca-Cola company actually imported the social practices also carried out on the origin market, among which we can count the willingness to volunteer of its own employees.

In fact, in the present case, the company's financial effort was minimum, because the willingness to volunteer is considered to be the least expensive form of social involvement, but which leads to the best results in terms of image. Moreover, through offering to volunteer the team spirit is formed and the employees' loyalty towards the company they work for is increased.

**Connex/Vodafone** company has invested till now approximately 3,5 million dollars in social projects, with the help of Sirois Foundation, founded after the western model. Among the social programs financed by this company, the program **Connex for the future** was, by far, the most important; the company estimated an investment of approximately 7 million dollars for this social initiative till 2007.

The program presupposes a donation of 1 cent from Connex/Vodafone company for each 10 minutes used in telephone calls within the same company. The funds collected this way will be allotted for financing some social projects chosen by the clients of Connex company, projects that will vary from one year to another.

Among the social projects initiated with the help of collected funds we can also count the campaign "Clean Seaside," launched in the summer of 2005, a campaign that includes two main components:

- *Gleaning the wastage*, that is made by placing special storage bins that allow the selective collection of wastage, and which are placed on the beaches of the seaside resorts. Moreover, volunteers from the Mare Nostrum organization carry out

demonstrative actions of cleaning the beaches in which they involve the tourists, and they monitor weekly the degree of cleanliness of the beaches.

➤ **The information caravan**, a mobile eco-center that moves every weekend from one seaside resort to another. The volunteers of the Mare Nostrum organization offer the tourists information about how to keep the beaches clean and about the importance of recycling the wastage for the protection of the natural environment.

The amount of money annually invested by Vodafone in this project exceeds 50,000 Euros, an amount of money spent to produce the storage bins, the logistics needed for carrying out the project, printing informative flyers and posters, and purchasing the prizes offered for the beach contests [[www.csr-romania.ro/resurse-csr/studii-de-caz.html](http://www.csr-romania.ro/resurse-csr/studii-de-caz.html) – *Clean seaside*, 07 March 2007].

**Softwin** company chose an even more interesting way to its responsibility towards the Romanian community. Softwin carries out the program called *A day for society*, which represents a rendering responsible social campaign that involves the employees' offering to volunteer who, on that day, dedicate their time and experience to a charitable cause [Capital, No. 29/2003].

In parallel with this project, Softwin organizes each year, on holy days, various charitable activities.

For example, in 2003, the company purchases a few hundreds paintings made by the students from "Constantin Brâncoveanu" school in Bucharest and included them in the employees' holy day gifts. The funds obtained this way by the school were reinvested in modern endowments, while the children's paintings are now in some important people's offices.

The social involvement of the Romanian companies greatly differ from that of the foreign companies, in the sense that they do not act based on some plans and strategies integrated in the whole policies of the company and, because of this, their efforts do not present a positive continuity.

On the other hand, the efforts of the Romanian economic agents show, many times, a better anchorage in the reality of the life of the Romanian society, and here I especially think about the social involvement of European Drinks.

More specifically, **European Drinks** company has shown over the past years a constant concern for supporting some under-privileged communities from Romania [Capital, No. 43/2001].

In 2001, European Drinks was co-sponsor of the charity concert-show *Musica Generosa*, organized by the Stare circus Bucharest, the funds collected being donated to the hospitals in Timișoara.

The company donated important quantities of water and food products in the areas damaged by the floods, and the sums of money donated annually by the company for charitable purposes constantly exceed a hundred thousand lei.

Another approach belongs to **Arctic** company, the leader of the Romanian electric appliances market, which launched a program of social responsibility called *Believe in U*, meant to support the students from the most important universities in Bucharest and Târgoviște in order to develop a successful career [[www.csr-romania.ro/resurse-csr/studii-de-caz.html](http://www.csr-romania.ro/resurse-csr/studii-de-caz.html) – *The program "Believe in U" initiated by Arctic: answers to the students' questions concerning the career*, 23 April 2007].

The program is accomplished by Arctic in collaboration with For People, a company specialized in development techniques, and with Synovate, an institute specialized in marketing research.

Within this program, Synovate has carried out a study in order to identify the students' expectations concerning their own professional career, based on which the specialists of the Arctic company, in collaboration with the students, will look for solutions for the problems that the young people may encounter in the moment of getting a job.

Over the time, the social efforts of the Arctic company have been directed towards the very diverse social causes, among which one can notice the precise problems of endowing some hospitals with electric appliances, sponsoring some charitable events organized by non-profit organizations, or by founding the internet school from Găești, endowed with modern calculation technology.

The change of mentality of the Romanian organizations has occurred, at least in the first phase, under the demonstrative effect of the transnational companies from our country that proved that they could increase the profit and the success on the market directly proportional with the improvement of their relationships with the community.

The business practice from Romania can draw our attention nowadays to plenty of examples of responsible behaviors towards society. Nevertheless, the business environment does not abound in factors that can favor this type of behaviors.

In the first place, *the lack of funds from the state* cannot be compensated by the funds donated by companies, and thus money is always insufficient.

Moreover, *the motivations* for which companies and natural persons make donation are mostly emotional ones (mercy, compassion), probably normative ones (the neighbor did the same thing), and much too little mutual ones, that is to get a direct or indirect benefit for the donation [Biz Magazine, No. 103/2005].

Obviously, one of the breaks against assimilating the social responsibility in the activity of the Romanian companies is *the Romanian business people's mentality*, who in most cases have developed their business in an individualist manner.

One can see all over Romania residential areas with extraordinary villas, superb gardens and streets full of garbage. Practically speaking, the local community does not exist. Moreover, the business people are considered stars of the local community in which they live and it is natural for the people to expect a favor from them, no matter how small for the respective community [Pleter O. T., 2005, p. 525].

I believe that the most important factor for stopping the private social initiatives nevertheless remains *the lack of legislation in the field*, as there are no stipulations regarding the granting of some fiscal facilities to the companies that allot a part of their profits with the purpose of solving some social requirements.

The present fiscal code only stipulates that any natural or legal person can direct 2% from the income tax towards a non-profit organization favored by the state, an absolutely insufficient stipulation [Capital, No. 30/2003].

On the other hand, the outspread of the social responsibility concept in more and more organizations from the Romanian economy has generated controversies referring to the ethical character of their involvement in the life of the community.

One can ask the question if these companies have the right to a positive image and to other benefits generated by social responsibility. There are enough examples that can be given in this regard. It seemed interesting to me to call attention to a recent case.

The *No to tobacco* campaign was presented to the public from Romania as the biggest anti-smoking campaign up to that moment, being an initiative of the Romanian Pneumology Society, of the “Pure Air” Association and of the Health Ministry [Capital, No. 10/2004].

The campaign was based on an advertising video presenting Claudiu Bleont, Liana Stanciu and Radu Nicolau telling the story of how they had given up smoking using the power of will. Cristian Țopescu urged us to follow their example and offered us a phone number and an Internet address where we could get further information.

The National Commission of the Audio-Video granted this project the status of “social campaign,” and thus the national television and radio stations from Romania broadcast it for free. Furthermore, the above-mentioned stars agreed to use their image free of charge in the service of such a noble goal.

But many Romanians do not know that this social campaign actually represented a hidden promotional campaign meant to promote a medicine of the GlaxoSmithKline company, namely the Zyban medicine.

The phone number presented in the advertising video actually sent certain medical offices that invariably recommended the Zyban cure.

It is true that Zyban was back then the only medicine of this type on the Romanian market, but the way in which it was “promoted” is at least debatable.

It is obvious that this type of deceitful practices would not have even been mentioned on the company’s origin market where the strongly restrictive legislation would have squared away the campaign from the start. Subsequently, the National Commission of the Audio-Video banned the broadcast of these advertising videos.

***In conclusion***, the companies’ social responsibility, a very fashionable topic in the developed countries and object of some complex enactments, remains something unknown for most of the Romanian economic agents.

This situation is fundamentally generated by the lack of experience of the Romanian companies and of the Romanians in general, concerning taking on responsibility towards society, peers, corroborated with ignoring the mutually advantageous character of approaching business from a social point of view.

The best argument in this sense is the fact that the Romanian organizations refuse to do something for society blaming the lack of money, or when they have such initiatives they are only satisfied to make donations, giving as much money as they can, without monitoring the way this money is spent and without expecting a benefit from it.

The question that is probably asked by many Romanian business people is the following: ***Why do we also have to be socially responsible?***

The answer to this question is obviously complex and it has to be approached from a threefold perspective, namely the social responsibility as moral obligation, and social responsibility as necessity and social responsibility as source of economic competitiveness.

Thus, the incumbency of taking on social responsibility in the Romanian companies is, first of all ethical, in the sense that the Romanian society places at the disposal of its economic agents the resources they need but it also expects them to use the resources responsibly, to the mutual benefit.



For this reason, the Romanian companies' efforts of social responsibility will not be efficient until they have as basis a whole of realistic ethical standards, confirmed by their members' daily behavior.

Related to this aspect, I consider that the most efficient way of forming an ethical behavior is the training of the future employees and investors, starting even from school. The ethical businessperson must be formed starting with the university period when the learning of the business techniques and practices must be combined with the grounding of some sound and realistic principles of ethics in business.

Secondly, the integration of the social responsibility in the objectives and strategies of the Romanian companies, and not only, is supported by the world's need to survive.

The economic organizations must become aware of the extremely dangerous situation generated by the lack of some ethical and social principles associated to the wild capitalism, and they also must act more responsibly towards the natural environment and people in order not to lead humanity to collapse.

Lastly, if the first two arguments are not enough to convince a more skeptical economic agent, it is important to understand the fact that being responsible towards society represents, for an organization, an important source for creating and maintaining some competitive advantages that should not at all be neglected.

Furthermore, in a highly competitive market, such as the European one, the Romanian organizations will have to meet the expectations of some educated and very pretentious consumers.

Thus, I consider that the success of the Romanian organizations on the large European market essentially depends on their capacity to understand and to efficiently and operatively integrate into their activity certain responsibilities towards society.

This aspect is all the more important given that the organizations, through their social objectives, will always exceed the limits of the local communities where they act. Practically, the organizations' social results, regardless if they are British, Italian, French, or Romanian, have a European and not a local impact, and they represent one of the most important factors for sustaining the long-term European economic development.

I also consider that taking on social responsibility creates business opportunities since they facilitate establishing some strategic partnerships with other organizations that have the same business philosophy, but also with governmental institutions and agencies that are very interested in starting an association in order to meet the pressing social requirements.

Nevertheless, the Romanian companies must understand that if they are happy to imitate the strategies of some transnational companies, they will not obtain the same positive results and that a social responsible behavior will bring benefits only if it is built on the Romanian social realities and on the expectations of the Romanian public.

## References:

- Boone E. L., Kurtz D. L. – *Contemporary business*, Third Edition, The Dryden Press, New York, 1992
- Certo C. S. – *Modern management*, Teora Publishing house, Bucharest, 2002
- Pleter O. T. – *Business administration*, Cartea Universitară Publishing house, Bucharest, 2005
- Popa I., Radu F. – *International management*, Economic Publishing house, Bucharest, 1999
- Puiu A. – *Management. Comparative analyses and studies*, Independența Economică Publishing house, Pitești, 2004
- Brady A. – *Corporate social responsibility in Central and East Europe*, [www.csr-romania.ro](http://www.csr-romania.ro), 28 January – 4 February 2007
- Diaconu B., Oancea D. – *More questions than answers: corporate responsibility in Romania*, [www.markmedia.ro](http://www.markmedia.ro), 16 – 22 April 2007
- Capital – *A social campaign dupes the press*, No. 10/2004
- Capital – *Social micro credits offered by a private company*, No. 44/2003
- Capital – *Fast-food restaurants work together for the community*, No. 40/ 2003
- Capital – *The exchequer discourages the involvement of the companies in social projects*, No. 30/2003
- Capital – *The companies' employees work for the under privileged people*, N0.29/2003
- Capital – *People start the engines of the market economy*, No. 43/2001
- Biz Magazine – *Social responsibility*, Cover Story, no. 103/2005
- [www.csr-romania.ro/resurse-csr/studii-de-caz.html](http://www.csr-romania.ro/resurse-csr/studii-de-caz.html)

# INCREASE OF NATIONAL COMPETITIVENESS ON BASIS OF INNOVATION

SAMAZHAN UMIRZAKOV<sup>1</sup>

## Increase of national competitiveness on basis of innovation

Recently innovation activity has become the integral part of economic development of the Republic of Kazakhstan, based on introducing new ideas, scientific knowledge, technologies and types of products to various spheres of production and society management. Apart from cluster initiative some aspects of diversification have been worked out as well. The program on organizing and developing the National Innovation Systems was affirmed for 2005-2015 years. The main objective of its program is to organize innovation systems of open type using both country and foreign scientific potential.

Objective of the paper is to determine the role and place of innovations in the achievement of competitiveness of the country.

In the process of research the following methodology was used: analysis and generalization of the state program development realization and innovative activity until 2015 year.

In the course of study and analysis of innovative processes the main problems, preventing these processes were revealed.

The industry – innovation development strategy of the Republic of Kazakhstan is affirmed by the President's Decree of the Republic of Kazakhstan of 17 May N 1096 and aimed on one hand at achieving stable development of the Republic of Kazakhstan by means of branch economy diversification and on the other hand ignoring raw oriented development where innovation is considered to be as a major factor in competitiveness of the national economy.

One of the main characteristics of today's technological revolution is creation and wide spread of territorial scientific – production systems. Scientific parks, innovation technological centers, innovation incubators and other similar structures, oriented to rapid realization of scientific research results into HOBYSO techniques, technology and materials, considered to be the main science efficiency factor and the integration of its parts with production.

Ranking the most and the least complexity the techno parks structure can be presented in the following way: incubators, technological parks, technopolicies, science and technology regions.

Technological park is responsible for profitable experimental-production transfer and it operates from the trial-construction and experimental work to organization of serial production of new products (learning to handle new technology), having almost guarantee demand in the market. The techno park organization realizes know-how, produces new products (in small batches) or takes part in its serial production. On this stage the main role is business support. Today there are three pilot regional techno parks. They are: "Algoritm" Ltd

---

<sup>1</sup> Professor, PhD, University of International Business, Faculty of Management and Economics, Almaty, Kazakhstan, E-mail: umirzakov@uib.kz

in Uralsk (mechanical engineering and metal working for oil producing industry), UniScienTech Ltd in Karaganda (mining metal, chemistry and ecology) and “Almaty regional techno park”( construction, new materials, power engineering).

To improve economy diversification of the country apart from Almaty, four more techno parks are going to be opened. The first project is going to be launched in Ust-Kamenogorsk, administrative center of the Eastern part of Kazakhstan, then in Shimkent, Petropavlovsk and Astana.

Techno park in the Eastern part of Kazakhstan will deal with the innovation development in mining metal industry and the production of new metal, its “colleague” in the Northern part of Kazakhstan will be specialized in mechanical engineering and agriculture products re-making, the project in the Southern part of Kazakhstan of oil-processing and metallurgy industry are supposed to be developed, and in free economic zone, in Astana, the agrarian sector, construction and food industry are supposed to be developed.

All in all under the construction of the Information Technology Park (ITP) 340 hectares are given in Alatau settlement. This land partly belongs to the settlement and partially to Almaty region. The construction of the Park started two years ago and in August of this year the first part of this project has been put into operation. The total area of premises and structures is 18.000square metres. There are office-premises for 360 people, a dining room for 5000 seats; production modulus N1 and N2 with total area equals 9.000 square metres, engineering and telecommunication systems, car parks, basketball, volleyball and badminton pitch. Of course, not only beautiful offices and ready production premises must attract future participants of the project. As a free economic zone (ITP) has a number of advantages, for example, tax remissions. Corporate tax will be reduced by half as to land and assessed tax the participants are tax free and realization rotation services are free from VAT. Besides they are free from customs duties for import goods and they have privilege financing by institutes of development.

Generally as the world practice shows the matter is not only in that. Techno parks play a very important role in the IT development of the company situated on its territories. But companies get reduction in overhead expenses and especially in administrative expenses. In special economic zones it is possible to establish contacts with other companies unofficially and to build relationships with customers and suppliers, also with banks and venture capitalists getting access to financing.

IT has an access to the scientific organization and scientists here and they have a good opportunity to have a consultation on different issues. And finally may get area for placing firms in case of its growth or vice versa its reduction.

It is supposed that 20% of its area stands out for business-incubator placement. Business-incubators support newly established firms and firms, being on the initial stage of development. In one case they are the techno parks’ core and in another one they operate as independent organizations. For entrepreneur beginners, who suffer from lack of financing, incubators give privilege conditions lower than market prices. Business-incubators are so popular for entrepreneurs that its number has already increased from several tens to 575 joined into the National business incubator association. In the world all in all there are 200 independent operating business incubators. After the USA they have become the most popular in the Western Europe.

In accordance with legislation PIT has many ancestors: The Government, institutes of development, private companies and also higher establishments and scientific research institutes. All above mentioned organizations will choose and establish a new management

company, which will be responsible for the whole PIT activity, when the complex is put into operation. Its duties will be: continuation of construction and accomplishment of its establishments and territory, supplying them with telecommunication, office, laboratory and metrology equipment.

Firms aspiring to take part in PIT must meet several requirements. Three of them are a must. There is the registration in tax agencies in free economic zone; the absence of structure divisions; and also 90% of total revenue got from different activities that meet the requirements of establishing free economic zone. These activities are: projections, elaboration, implementation, trial and software production, hardware database; creation of new information technologies on the basis of artificial immune and neuron system, doing scientific and research work and trial-construction work in the sphere of information technology.

We can easily notice that most of our computer firms don't meet these requirements. Unfortunately nowadays these firms only buy, sell and re-sell hardware and software equipment, produced in China and Taiwan and as to domestic production it is only on initial stage. But the idea of free economic zone supposes that PIT will become a kind of generator in new technological policy in industry effective tools in new project realization:

World leading companies in the sphere of IT (information technology) and communication companies are drawn in techno park work; memorandum about cooperation has been signed with Microsoft, Hewlett Packard, Siemens, Cisco Systems, Tales, LG, Sun Microsystems, Samsung and other world leaders in this field.

Kazakh versions issue of Windows Office and participation in IT park are being planned within the frame work of this memorandum. Taking part in the state project, software giant, together with Hewlett Packard, is planning to create the expertise centre directly in the techno park.

It is planned to install very powerful HP server. Microsoft is going to install its more up to date software; in particular it is 64 bit server operation version of Window Server 2003 system, and 64 bit SQL version of Server 2005. There are only a few of such servers in the Republic of Kazakhstan and only large corporate customers have such servers. The expertise centre will be very helpful because our Kazakhstani companies-software programmers will have free access to this server.

In the techno park, besides the expertise centre, Microsoft is planning to open the study centre, working in two directions. The first is the courses for clients how to use the program products; today the consumers show interest in the complex server products.

The second direction of the study centre will be the courses especially for Kazakhstani software designers.

In the IT park, laboratories and joint venture premises producing the first in RK LCD monitors and PDP and LCD TV sets will be allocated. The starting capital is \$ 10 million, out of which 40% are paid by the National innovation fund, 35% by Glotinvest and 20% by Singaporean DS Multimedia LTD PTE.

But, alongside with all these positive aspects, Kazakhstani techno parks face a range of problems.

They can be divided according to the degree of its influence into:

- general, indirectly affecting techno park performance in the frame work of the state innovation policy realization.

- specific, directly and negatively influencing techno parks' work.

General problems can include:

Firstly, lack of investments in the main capital of processing enterprises. Intensification of the problems is caused by such reasons as:

-considerate share of investments is put into raw material sector

-the main part of economic activity income in the Republic falls on natural resources mining, which is export oriented. A large part of income is concentrated in the hands of foreign investors.

Secondly, the absence of modern mechanisms of introducing technological innovations to the market.

Today the scientists of Kazakhstan have a lot of projects, based on the ideas and results of many years' researches. But the problem is how to introduce them into production and there are only few selling of them.

Foreign projects remain more preferable according to their quality features and under corresponding financial opportunities are often used by our enterprises.

Thirdly, the absence of effective demand for advanced technologies and industrial innovations in the domestic market.

According to the world experience, science and science-technical activities refer to the sphere of service and their products are in the market demand. However at present the Kazakhstani market of scientific services and scientific products is not developed well enough. Today the Kazakhstani market is not ready to the full extent to pay for services of home scientists and designers.

Fourthly, lack of production potential.

To the specific problems refer:

Firstly, lack of highly qualified workers.

At present, the vital problem for Kazakhstan is the lack of specialists able to react quickly and professionally to the state innovation policy. In connection with it, the innovation development in Kazakhstan needs to establish the whole system of innovation control, directed to management level increase, the process of transforming of science-technical projects into ready made innovation product, attractive for an investor, producer and consumer; it can be done only by specially prepared and trained specialists-innovation managers. It's impossible to provide effective and dynamic work of techno parks without neither modern educational system nor modern managers. There is no doubt that the first priority is development of technical specialties, that is great deficiency, and staff is drawn from abroad.

Secondly, lack of expenses in the private sector on techno park development.

Low level of attracting private investment system into applied researches and science is a large drawback in Kazakhstan innovation system, according to the world experience; precisely they are one of the main factors of techno parks development. Further more, lack of private investments in innovations results in fact that the part of innovation technologies and products, developed by state scientific centres, is left unclaimed as it doesn't meet the specific needs of industrial enterprises.

Thirdly, lack of innovation university autonomy.

Today Kazakhstani institutions of higher education can't solve the problems of establishing small and joint companies together with productive sector, which consequently would become the main element in the technological system of parks being created in our republic. It takes a long time of coordination and permission from Ministry of Education and Science and from state property and privatization Committee of RK.

Fourthly, absence of information about market condition of new technological innovations. Lack of such information makes difficulties for Kazakhstani researchers and producers who are planning producing new products, i.e. techno parks' scientists and designers don't have the opportunity to exactly evaluate the situation and to compare the planned showings with techno-economic showings of a similar production. So, not having enough information about the level of market competition, home producers have to work under the condition of so called "dark" competition.

Fifthly, absence of techno parks, oriented to raw material processing. Speaking about the development of mining branches in Kazakhstan, in particular, about oil chemical branch, it is necessary to emphasize that the potential, our republic has (it is rich in oil, gas), is not fully realized. Well, hydrocarbon raw material processing volume at oil-refining plants in Pavlodar, Atyrau, Shimkent is only 55 %; it means that 40-50% of their production power is used. Meanwhile, in the developed countries this index is equal to 98%. Under the support of the Government of the Republic of Kazakhstan some definite measures are being taken to improve oil-chemical complex, large domestic and foreign companies are taking part in this process.

Under the modern conditions of scientific –technical development, entrepreneurs, who are initiators of new projects, large production companies and government clearly realize that rejection of the investment to the innovation mastering would be large financial losses in practice. That's why they have taken the way of creating such economic mechanisms which would on the one hand help to introduce the latest STP achievements into production and on the other hands would make it possible to bring to minimum the financial risk of some separate investors.

One of such mechanisms is risky (venture) innovation financing. Venture mechanism has played an important role in realization of many large innovations in different spheres of activity. Some companies, starting their growth with the help of risky financing, in a comparatively short time have become dealers of the main STP directions.

At the same time, many founded long ago large industrial companies widely use venture mechanism at financing to strengthen their own scientific-technical potential, diversification of production , revealing and mastering the most perspective scientific-technical projects, developed both in the home country and abroad.

These home venture funds also began financing such projects as Silan technology elaboration and organization of experimental industrial production of high-quality silicon. The cost of the project is 65, 1 million KZT; development of centres which can provide wide range of services in IT. The cost of the project is 54 million KZT - elaboration and creation of experimental industrial specimens of a new heat vortex generator. The project cost is 112, 2 million KZT; building of a new ferrosilicoalluminium factory. The project cost is 522 million KZT; production of heat-insulated materials from basalt fiber. The project cost is 186, 2 million KZT.

At the same time, the national innovation fund nowadays realizes several innovative projects such as: organizing of pharmaceutical complex for production of home antitumor drug "Arglabin". The total cost of the project is about \$ 1 billion, including the share of the fund –

338, 4 million KZT. Industrial capacity – 2 million ampoules a year entering forecasted capacity to 2008; organizing of the production of cast-iron through method of non-coke creation on the basis of innovation process Romelt. Annual output is 34 560 tons, environmental safety production; production of modern universal log recorders “Geoscan” in complex with bore-hole gadget. The total project cost is 1, 9 billion KZT, share of the fund – 658 million KZT.

The situation with venture funds is not as good as it seems. New and potential techno parks always need financing, especially in early stages of its development. But without stable financial basis they cannot rely on means from such traditional resources as bank credits or investment of securities in public financial markets. That is why the only solution of financial problems for new techno parks is to find venture investor.

However, there are some legislative norms and states, which prevent the development of investment share and venture funds in Kazakhstan. For example, prohibition for buying enterprise shares not having proper rating even if it is paying enterprise. Nowadays, it is a problem of going out from the project for Innovative fund: according to the inner regulations, the fund has 49% share, but the joint-stock company law allows buying the society only 29% of shares at the expense of its capital.

The absence of venture funds leads to such serious problems as:

- lack of experience of innovative projects commercial development;
- absence of financing of innovative projects by commercial banks;
- shortage of means to protect the intellectual property.

As a whole there are all necessary prerequisites for transition to innovative way of development in Kazakhstan. They are- rich natural resources which supply almost all home requires in raw materials and energy resources; presence of great considerable industrial capacities to start science production; cheap workforce with its high level of education; well developed science potential; presence of several technological structures.

Moreover, some elements of innovative infrastructure have already been applied, such as technological parks, with the object of creation of necessary conditions and favorable environment for the development of country’s economy on a basis of achievements in science and technology, to form balanced industrial infrastructure and phased substitution of raw component’s part in GDP to high-technological export.

However, in spite of intensive application of techno parks and presence of powerful industrial and scientific potential, there is no intensive implementation of foreign experience in Kazakhstan, when techno parks are created attached to the large scientific center and stimulate the development of new companies, involved into scientific technological business. Nowadays, techno parks are places of concentrated standard infrastructural support where companies rent premises but not places of enterprises support, based on new technologies.

Their main function is to raise competitiveness of business in spite of its branch direction and, as a result, the absence of the main factor - creation and introduction of innovations.

Consequently, all above-mentioned problems need urgent and efficient decision. In this connection it is necessary to realize the complex state support, based on the formation of necessary conditions for the development of techno parks’ net, oriented on creation and application of IT and high-tech production. Financing of risky entrepreneur business projects is hardly to call a new economic phenomenon. Almost every investment of private funds into different organizations on order to get profit inevitably. These home venture funds also began



financing such projects as Silan technology elaboration and organization of experimental industrial production of high-quality silicon. The cost of the project is 65, 1 million KZT; development of centres which can provide wide range of services in IT. The cost of the project is 54 million KZT - elaboration and creation of experimental industrial specimens of a new heat vortex generator. The project cost is 112, 2 million KZT; building of a new ferrosilicoaluminium factory. The project cost is 522 million KZT; production of heat-insulated materials from

As a conclusion we can say that effectiveness of innovations introduction depends on removal of the revealed problems and development of a complex program.

## References

- Nazarbaev, N.A. "To overcome raw material orientation". In: *"Kazakhstan's truth"*.
- The Ministry of Trade and Industry: "The program on formation and innovative system development of the Republic of Kazakhstan for 2005-2015 years". *Decree of the Government of the Republic of Kazakhstan of December 21, 2004*.
- The law "About state support of innovative activity". *Decree of the Government of the Republic of Kazakhstan of June 30, 2005, № 651*.
- Mushaeva A. D. "Analysis of modern condition of technological parks development in the Republic of Kazakhstan". In: *Analytic, 2006-№1*.
- Kembayev, B.A. "The scientific information providing of innovative activity of the Republic of Kazakhstan". In: *Kazakhstan Association of IT companies, 2006*.
- Bukagaliev, A.S. "Financial infrastructure of innovative activity was formed with creation of venture funds in Kazakhstan". In: *Kazakhstan today of November14, 2006*.

# FOREIGN EXPERIENCE OF COMPETITIVENESS INCREASE IN THE ECONOMY OF KAZAKHSTAN

GULNARA NURMUKHANOVA<sup>1</sup>

## **Abstract**

Increase of innovative activity in the economic development of a state has direct impact on competitiveness of enterprises and the state as a whole. Innovative development is aimed at the achievement of steady growth of the country as well as further dynamic development of society and economy.

**Key words:** innovation, innovative process, innovative enterprise, competitiveness, innovative infrastructure.

---

<sup>1</sup> Associate Professor, PhD, University of International Business, Department of MBA Program, Almaty, Kazakhstan, email: [gnurmukhanova@uib.kz](mailto:gnurmukhanova@uib.kz)

## **Foreign experience of competitiveness increase in the economy of Kazakhstan**

Steady growth of any national economy at the present stage can be provided only on the path to its innovative development. The strategy of industrial and innovative development of the Republic Kazakhstan for 2003-2015 years is aimed at achievement of steady development of the country by diversification of branches of economy and deviation from raw orientation of its development. At the same time innovations are defined as the major factor defining competitiveness of the national economy; full use of innovations for the further dynamical development of economy and society is possible if the state will carry out purposeful innovative policy.

The objective of the paper is to illustrate that it is possible to obtain the increase of economy competitiveness only in conditions of making innovative processes more active in the economy of the country.

In the process of research the following methodology was used: comparison, observation, analyses, appraisal (Delphi technique), and program and target method.

The result of the research is substantiation of widening scientific potential, development of innovative enterprise, creation of multilevel innovative infrastructure, also the creation of financial infrastructure, providing financing of innovative processes.

The results of the market analysis of innovative activity at the industrial enterprises of Kazakhstan for the last 3 years (where innovations were understood basically as innovations of improving and local or branch character) have shown, that the share of expenses on purchase of intellectual property rights (know-how, patents, licenses, etc.) in total amount of investments is only 0,8 %. The situation becomes complicated as there are no elements of estimated infrastructure for innovative sphere, typical for any developed economy. Such infrastructure gives an opportunity for wide layers of economic agents to have an objective picture of actual state of affairs in different spheres of economy and its real capitalization, thereby, receiving proved information to make investment decisions.

At present the innovative infrastructure in Kazakhstan consists of existing subjects created with assistance of state budget means (republican, local budgets, means of organizations with state participation), and also service development institutes, established by the state. The list of basic functions carried out by subjects of innovative infrastructure includes:

- services assisting the process of organizational and legal formation of innovative development subject;
- complex of business-services (complex consulting);
- informative and communicative provision
- providing with access to the equipment for general use - laboratory, industrial;
- complex of educational services;
- technology transfer;
- representative services (establishment of partnership ties).

The existing infrastructure does not provide the necessary level of interaction between its subjects and is not a system of complex organizations providing all list of services, necessary in the process of activity and interaction of innovative system participants. Quality and quantity of innovative infrastructure organizations, presented in Kazakhstan, don't satisfy the

specific character of innovative development of our republic, it is characterized by following:

- territorial dispersal of regions, having innovative potential, and insufficient coverage of innovative infrastructure of regions;
- the necessity of infrastructure support creation as the process of branch, as well as regional innovative development;
- rather low quantity of innovative initiatives at the first stage of industrial and innovative development of Kazakhstan, not demanding plenty of innovative infrastructure objects in one region;
- necessity of observance of the cost expediency principle and its conformity to the potential of the state budget;
- choice of the most optimal forms of innovative infrastructure organizations to except duplication of separate functions by them.
- actual absence and sharp necessity of information provision system creation of all elements interaction and participants of innovative system.

The economic mechanism of any system regulation is a system combination of principles, problems, methods, organizational structure, elements of management agents, legal and infrastructural provision. The economic mechanism of innovative activity regulation is not an exception. In the course of analysis, estimation is conducted to work out technological alternatives under the following schemes:

- estimate of scientific and technical resources;
- estimate of production factors;
- estimate of financial (investment) resources;
- selection of technological alternatives;
- choice and substantiation of alternatives for realization.

The innovative system is subdivided into the following basic subsystems; each includes such elements as:

1) Scientific potential, the necessary factor for innovative development, is formed by the creation of developed sphere of applied researches, carrying out "operational development" of fundamental development up to the level of commercial application. It includes:

- state scientific organizations - national science centers, scientific research institutes, higher educational establishments, project institutes;
- scientific organizations attached to national companies, laboratories attached to large enterprises;
- private scientific research institutes and project institutes;
- small and middle enterprises; engaged in scientific research
- scientific brainpower and individual inventors;
- material and technical base.

Today the scientific potential of the country is presented by scientific organizations of Ministry of Education and Science, branch ministries, private research organizations, and

centers of research in the directions of scientific researches, exercising economic vision rights, coordinating activity of institutes of corresponding description, also scientific research institutes which are under the jurisdiction of national companies. All actions on development of the scientific and technical potential of scientific researches must be based on the following principles:

- Financing of R & D on grant basis,
- Co- financing of R & D with private sector,
- Independence of scientific and technical examination,
- Change of organizational structure of scientific institutes, including stimulation of privatization of the scientific research institutes, engaged in applied science.

2) Innovative enterprise, providing development of connecting (intermediary) role between scientific - technical and industrial spheres. The ultimate goal of innovative business is the development of enterprise which can react to the current market situation efficiently and adjust the repetition work of competitive high technology production of new generation and increased demand at the world standards level. It includes:

- business-angels;
- enterprises;
- innovative managers.

Important directions of innovative enterprise development for the nearest prospects will be: creation of manpower training system and retraining of personnel in the field of innovative enterprise, including higher education, post higher education, also abroad, and short-term courses, seminars, round-table discussions to improve qualification of already working managers with state participation in financing of such programs.

Stimulation of innovative enterprise should be concentrated on following directions:

- further perfection of tax system with the purpose of creation of favourable conditions to conduct innovative activity by all subjects, irrespective of the form of ownership and financing;
- development of cluster strategies, directed at creation of specialized knowledge networks of and its commercialization - territorial zones of new technologies development;
- development of systems of information exchange and access to data, regulations, databases, etc., necessary in innovative activity;
- assistance in the development of business and information services market for innovative activity - finance and law consulting, patent protection, etc.;
- stimulation of joint innovative enterprises creation by foreign investors;
- assistance in the creation of business associations, promoting simplification of dialogue between state and private business;
- increase of efficiency of state ownership use to make innovative activity more active by transfer of unused working area and resources under the creation of innovative infrastructure elements;

- creation of product standardization system and system of certification of technological processes, goods and services;
- creation of innovative risks insurance mechanism;
- development of managerial and entrepreneur culture, etc.

3) Multilevel innovative infrastructure, defining a complex of interconnected industrial, consulting, educational and informational structures, serving and providing conditions for innovative activity realization. It consists of the following elements:

- national technological parks;
- regional technological parks;
- technological business-incubators, etc.

Technological parks (techno parks) and technological business-incubators should become the basic organizational institutes of innovative infrastructure of Kazakhstan, having organizational structure, financial, peopleware and logistical support, necessary and sufficient to provide assistance to all stages and processes of innovative development. According to foreign experience, a small and middle enterprise in the innovative sphere is the first mass and the most dynamic structural component of innovative potential of industrially advanced countries. Small and middle innovative firms are technological leaders in infant industries of economics, opening new segments of the market, developing new production, raising science linkage, competitiveness of production and thereby promoting the formation of new technological structure.

One of the most effective mechanisms of development and support of small innovative enterprises is the process business- incubation i.e. the process of favorable conditions creation for innovative projects at the earliest, risky stages of its development, when it is difficult to define the probability of success and fast development of technological companies. In accordance with the Strategy of industrial and innovative development of the country up to 2015, in the period up to 2007 year it is supposed to create not less than 12 specialized technological business-incubators in the various regions of the republic consisting of technological parks attached to leading technical, agrarian and medical higher educational institutions of Kazakhstan and 8 educational centers attached to techno parks. From the point of view of innovative project management, the creation of technological business-incubators network will allow:

- to concentrate the necessary material resources for grant financing of the scientific-research funds of hi-tech enterprises in the area of technological business-incubators;
- to make administrative decisions effectively, which allow to reduce duration of innovative cycle;
- to lower the level of overhead maintenance costs of infrastructure;
- to reduce the quantity of bureaucratic procedures in the process of making investment decisions;
- to optimize the managerial structures of innovative enterprises;
- to create conditions for knowledge transfer in innovative system.

The most acceptable for conditions of innovative development of the republic is the division of techno parks into elements and participants of scientific research, according to levels of their influence:

- national scientific and technological parks;
- regional technological parks.

The national scientific and technological parks are created to provide accelerated development of branch, region, and area of knowledge which are priority for social and economic development in accordance with provisions of statutory legal acts. To stimulate innovative activity of national scientific and technological parks, the territory is given the status of special economic zones in accordance with legislation of the Republic Kazakhstan. Regional techno parks are created with the purpose of definition, revelation and development of innovative potential, innovative ability of the region, maintenance of region's economy need in innovative products. In the field of regional techno parks development it is necessary to create four regional techno parks in the following regions to achieve maximum national effect in stimulation of innovative activity:

- The East Kazakhstan region
- The South-Kazakhstan region
- the North-Kazakhstan region
- Astana city
- Almaty city.

Cluster form of innovation activity should play a large role in innovative process to make it more active at present stage of economy development of Kazakhstan. This form leads to creation of special form of innovation – «the cumulative innovative product». Such innovation is the product of several firms' activity or research institutes that allow accelerating their distribution over interrelations network in general regional economic space. Besides variety of different sources of technological knowledge and communications facilitates combination of factors of competitive advantages achievement and becomes a precondition of any innovation. Cluster unification on a basis of vertical integration forms not a spontaneous concentration of various technological inventions but the certain system of new knowledge distribution and technologies. Thus, the most important condition of effective transformation of inventions into innovation, and innovations into competitive advantages is the formation of stable connections between all cluster participants.

4) Financial infrastructure, providing complex financing of research-and-production, educational processes in the sphere of is innovative-technological development, which is based on combination of various mechanisms of direct and indirect state support of innovative enterprise and infrastructure. It consists of the following elements:

- state institutes of development;
- venture funds;
- enterprises;
- sole proprietors;
- banks of the second level; and others.

The state should influence demand and venture capital, as well as its supply. The state stimulation of venture capital supply will be carried out by:

- participation in the creation of venture funds;

- creation of conditions for institutional investors participation and financial institutions in venture investment;
- assistance in individual investors' network development;
- maintenance of the venture investments liquidity;
- partnership in R&D financing with private capital and innovative projects;
- creation of the state system of insurance investments in realization of innovative projects;

If the state stimulation will cover all above-mentioned measures at the initial stage, in the future, in the process of "exit" of state from venture funds and companies, the given means will be directed towards financing of applied R&D and elements of innovative infrastructure. The state stimulation will be mainly carried out in the form of R&D financing and also in indirect form (taxation, etc.).

In conformity with the Strategy of industrial and innovative development of Kazakhstan it is supposed to bring the size of produced added value in high technology and hi-tech branches from 2 billion tenge in 2000 year to 126, 6 billion tenge by 2015 year (more than 60 times as much) with growth of science services and scientific-innovative activity from 24 billion tenge in 2000 year to 157 billion tenge in 2015 year (6 times as much). The volume of science services and scientific-innovative activity (where researches and development enter) will increase in 2, 7 times by 2015 year in comparison with 2000 year in comparable prices. By 2010 year it is supposed to increase financing of science up to 2 % from gross national product (and in 2015 year up to 2, 5-3 %) in comparison with 0, 2 % now. Thus, we notice, Kazakhstan (as some developed countries, for example, Australia or Canada) has quite appreciable competitive advantages in certain resources, it influences any planned and carried out policy and it should be considered and used to provide competitiveness of the national economy.

As planning implement in the economic mechanism of management of investment activity, the program target approach has received further development. Financing of scientific researches is carried on a basis of legislatively fixed program target principle through the formation and realization of target scientific and technical programs, within the limits of which the scientific organizations receive a state order to carry out research and development. The program target financing of scientific research and scientific technical programs is carried out on the competitive basis. It is obligatory to make the state scientific and scientific technical independent examination of offered programs and results of scientific researches. The program target method of financing of applied R&D should be based on the following principles: concreteness of purposes, problems and contents of the scientific and technical program; openness of the researches results.

At present stage within the limits of the program target method, the formation and realization of the following scientific and technical programs is carried out:

- fundamental researches on that limited number of priority science directions, scientific and technical progress which have a purpose to receive essentially new knowledge about natural and social systems and development of the scientific basis of economy system transformations, steady development of society, culture and science;
- republican target scientific and technical programs as the major means of the state scientific and technological policy realization, capable to concentrate scientific and



technical potential on general priorities of industrial-technological and social economic development;

- applied (branch, inter-branch and regional scientific and technical) programs which are concrete and complex inter-branch directions of the scientific technical activity, applied and promotional researches and developments;
- priority programs of the scientific researches for the region;
- projects of Science Fund having a purpose to stimulate "risky " and perspective fundamental and applied researches within the limits of certain priority directions and to promote the development of scientific researches in regions.

Transition of the national economy to innovative way of development is impossible without susceptibility of all society to innovations and sufficient number of staff, able to manage innovative processes and realize innovations. Despite of available scientific and technical potential, the absence of enterprise, carrying out the basic kinds of innovative activity in Kazakhstan, such as creation of innovative product and intermediary services connected with promotion of innovative product in the market, is one of the reasons of low innovative activity in the country.

As conclusion we can say that in order to increase innovative activity in Kazakhstan it is necessary to consider the following factors:

1) Scientific potential, the necessary factor for innovative development. It includes:

- state scientific organizations - national science centers, scientific research institutes, higher educational establishments, project institutes;
- scientific organizations attached to national companies, laboratories attached to large enterprises;
- private scientific research institutes and project institutes;
- small and middle enterprises; engaged in scientific research
- scientific brainpower and individual inventors;
- material and technical base.

2) Innovative enterprise, providing development of connecting (intermediary) role between scientific - technical and industrial spheres. It includes:

- business-angels;
- enterprises;
- innovative managers.

3) Multilevel innovative infrastructure, defining a complex of interconnected industrial, consulting, educational and informational structures, serving and providing conditions for innovative activity realization. It consists of the following elements:

- national technological parks;
- regional technological parks;
- technological business-incubators, etc.

4) Financial infrastructure, providing complex financing of research-and-production, educational processes in the sphere of is innovative-technological development, which is

based on combination of various mechanisms of direct and indirect state support of innovative enterprise and infrastructure. It consists of the following elements:

- state institutes of development;
- venture funds;
- enterprises;
- sole proprietors;
- banks of the second level; and others.

## **References**

Porter, M.E., “International competition”. In: *International Relations*, Moscow, 1993.

Lynch, M. “Emerging Markets Research”. In: *Republic of Kazakhstan*, (March, 2001).

Emelianov, S.V. “American Experience of the national competitiveness increase”. In: *The USA and Canada: economy, politics, culture*, (2002, № 11).

“The Program on formation and development of the national innovative system of the Republic of Kazakhstan for 2005- 2015 years”. *Government regulation of April the 25, 2005, N 387*.

“The strategy of industrial and innovative activity of the Republic of Kazakhstan for 2003-2015 years”. *Decree of the President of the Republic of Kazakhstan of May the 17, 2003 N1096*.

# THE CONVERGENCE DEGREE OF INNOVATION POTENTIAL OF ROMANIAN ECONOMY, BY COMPARISON WITH THE DEVELOPED ECONOMIES OF THE EU MEMBER STATES

CAMELIA OPREAN<sup>1</sup>  
CRISTINA TĂNĂSESCU<sup>2</sup>

## Abstract

In this paper we analyze the convergence degree of innovation potential of Romanian economy, by comparison with the developed economies of the *economical and monetary union*, on one hand, and with the last wave of integration countries – in most cases, economies in process of development, therefore with an economical development trajectory like our country – on the other hand. The *European Innovation Scoreboard (EIS)* is the instrument developed at the initiative of the European Commission, under the Lisbon Strategy, to evaluate and compare the innovation performance of the EU Member States. The EIS includes innovation indicators and trend analyses for the EU Member States, plus the two new Member States: Bulgaria and Romania, as well as for Croatia, Turkey, Iceland, Norway, Switzerland, the US and Japan. The Summary Innovation Index gives an “at a glance” overview of aggregate national innovation performance. It measures 5 key innovation dimensions: Innovation drivers, Knowledge creation, Diffusion, Applications and Intellectual property.

**Keywords:** innovation, Summary Innovation Index, research, knowledge creation

**JEL classification code:** O31

---

<sup>1</sup> Lect. univ. dr., Faculty of Economic Sciences, University “Lucian Blaga” of Sibiu; e-mail: camelia.oprean@ulbsibiu.ro

<sup>2</sup> Conf. univ. dr., Faculty of Economic Sciences, University “Lucian Blaga” of Sibiu; e-mail: cris\_tanasescu@yahoo.com

The growth of Romania's productivity and competitiveness on the global markets have to be sustained by politics of easy firms' access to the research-development results, through: innovation and technological transfer; access to specialized services – as information, intellectual and industrial property – and participation to the international network; development of entrepreneurial culture and of innovation; growth of firm level research; strengthening connections between the business community and the one of education and research.

In USA and Japan the economical and research sectors are highly connected, but in EU there is a *real gap* between the economical sector and the one of applicative research. For our country, is a challenge to catch up the European developed economies, or even more than that, through a convergent economy, based on knowledge, and most important, able to generate knowledge. Therefore, the adoption of strategies which could stimulate new ideas and technologies represents an obligation for every European country.

The main reason of this research is the fact that process of knowledge creation is most rewarding in the present international economic context, characterized by global economy globalization. Any invention or innovation which could be brevetted is a competitive advantage on the global emergent markets, implying huge profitable effects.

Competitiveness within the European Union is closely tied to its position in the domain of innovation and transmitting new technologies. For a better understanding of the factors that contribute to the success of innovation in the European Union we use the benchmarking as an instrument to identify the best methods. The method allows the appreciation of a country, region or enterprise's performances compared with its competitors.

As an answer to the challenge of the European Council in Lisbon, there have been used some of the performance indicators as reference points to provide the people who take decisions with relevant information referring to each country's achievements in terms of innovation, business development and utilization of new technologies. The information related to the innovation activity made by EU enterprises is assured by a special statistic investigation/inquiry/survey: **Community Innovation Survey (CIS)**. The data and the information provided by this investigation are at the basis of the evaluation of the partial and synthetic innovation indicators.

**The System of innovation indicators** used by the EC countries and the candidate countries (*European Innovation Scoreboard - EIS*) is the main statistic instrument used by *European Trendchart on Innovation*, elaborated as a reply to the initiative from Lisbon in March 2000. It was implemented in 2001 and continuously perfected, thus it became a main reference point for the decisions referring to innovation policies and economic analysts, as well. The number of the indicators used increased from 20 to 25, trying to find various aspects of the innovative process. These indicators are capitalized under different forms: individually, five synthetic indicators that cover the key dimensions of the innovation and a composite one that unites in a standard form all the partial indicators, offering a synthetic evaluation of the innovation that affords regional and international comparisons.

The elaboration of a complex system of innovation indicators has been a long process, developed in many stages.

The first step was the **indicator identification**, potentially relevant for the investment process, capable of directing the decisions making of economic policy according to the Lisbon objective. There has been elaborated a first list of 52 innovation indicators, selected in terms of relevance

and data availability. These indicators have been organised in 5 blocs/bodies: innovation drivers (human resources), knowledge creation, innovation and entrepreneurship describe the input of the innovational process, while the applications and the intellectual property refer to output.

The second step is the selection of final indicators so that to avoid redundancies and strongly correlated indicators. At this stage there has been made a statistic analysis of the relation among the five blocs of indicators and among the indicators in each bloc. The correlation matrix made for each bloc of indicators allowed the identification of indicators that had a strong correlation, and the statistic analysis of the main component was used to identify the key- factors in each group.

After the first two phases there remained 25 indicators. The selection was based on the following principles (Sandu, Steliana; Ioan-Franc, Valeriu; *Creativitatea și inovarea – experiențe europene*, publicat în *Studii și cercetări economice – vol. 44-45*, Academia Română, Institutul Național de Cercetări Economice, Centrul de Informare și Documentare Economică, București, colecția 2007, p. 9):

- redundancy: if there are two or more indicators that offer similar information, we select only one;
- political impact: when two indicators are strongly correlated and offer an important political message, both indicators are selected ;
- availability: in many countries available indicators for many countries are preferred and those that can be obtained from the existent database;
- when two indicators are redundant, the one that is included in the previous lists is kept.

The database was completed with absent information using regression techniques.

It is possible to obtain a general view relating to the innovation evolution of each country by synthetising the partial indicators in a **summary innovation index**. It is much easier to analyze the variation of a synthetic indicator than to look for common tendencies of partial indicators' evolution. The synthetic indicator is useful for countries' hierarchy, discrepancies' evidence and in the decision making process. However, the construction of a synthetic indicator is not free of difficulties, and the methodological problems that appear have to be solved accordingly to eliminate the danger of misinterpretation or results manipulation. The list of partially used indicators is frequently revised. For example, in the EIS 2005 list of partial indicators, the indicator "the penetration rate of simultaneous telecommunications" replaces "the access to Internet", the indicator "the weightings of innovative enterprises financed by public sources" replaces "direct expenses (research-development) of companies financed by public sources", and the indicator "national patents per a million citizens" disappears.

The reunion of partial indicators in a summary innovation index and subindexes corresponding to thematic groups presumes a calculation algorism that starts from standardizing the primary data. The primary indicators are represented in different unit measures (for example, % results on a million people) which do not permit their direct summing up. Bringing the primary indicators to a common measure unit is done by using **the minimum-maximum standardization method** that can be applied in two steps as it follows:

1. The standardized value is determined (between 0 and 1) of each primary indicator with the relation:

$$y_{ij} = \frac{x_{ij} - \min(x_j)}{\max(x_j) - \min(x_j)}$$

where:  $y_{ij}$  - standardized value of indicator  $j$  for country  $i$  ;

$x_{ij}$  – value of indicator  $j$  for country  $i$ ;

2. The calculation of synthetic index as arithmetical mean (weighted or simple) of the standardized value of constitutive indicators:

$$I_i = \frac{\sum_{j=1}^m q_j y_{ij}}{\sum_{j=1}^m q_j}$$

where:  $I_i$  - innovation synthetic index for country  $i$ ;

$q_j$  - weight indicator  $j$ .

In most of the cases, to simplify the partial indicators – that composes the summary index – receive equal weightings. In case of complementary indicators (for example when the data for innovative and noninnovative companies are available) weightings of sum 1 are used.

The European Innovation Scoreboard (EIS) covers the 27 EU Member States (Bulgaria and Romania joined the EU on 1 January 2007. However, the EU25 mean is used throughout this report to reflect average EU performance as all of the underlying analyses were performed in 2006 when only EU25 mean data was available from Eurostat and other data sources), Croatia and Turkey, the associate countries Iceland, Norway and Switzerland, as well as the US and Japan. The indicators of the EIS summarise the main elements of innovation performance.

The EIS 2006 almost fully adopts the 2005 methodology with the exception of some few changes, for example:

- Removal of the indicator measuring the share of university research and development expenditures financed by the business sector;
- The indicator on public research and development expenditures is now defined as the sum of government and university research and development expenditures only.

**The groups of innovation indicators** that form EIS (2006 variant) refer to two main themes: inputs and outputs. Innovation inputs (that include three dimensions) and outputs (two groups) will be presented briefly as it follows.

• **INPUT 1: innovation drivers**

This group of five indicators measures the structural conditions that assure the innovative potential using information related to the quality of work resources mainly:

1. science and engineering graduates per 1000 population between 20 and 29 years old;

2. population with higher education (any kind of posthighschool education), per 100 population between 25-64 years old;
3. broadband penetration rate: the extension rate of telecommunication lines (number of lines at 100 citizens);
4. participation in permanent education (life-long) learning (% people between 25-64 years old);
5. youth education attainment level (% people between 20-24 years who graduated at least highschool).

- **INPUT 2: knowledge creation**

The four indicators in this group measure the investments in human factor and in research – development activities, considered as key elements of the knowledge – based economy:

6. public research-development expenditures as percent of Gross Domestic Product (GDP);
7. business research-development expenditures as percent of Gross Domestic Product (GDP);
8. share of medium high-tech and high-tech research-development expenditures (% of manufacturing research-development expenditures);
9. share of enterprises that are financed for innovation and research-development from public sources;

- **INPUT 3: innovation and entrepreneurship**

This group of six indicators measures the efforts done for innovation at a microeconomic level.

10. sum of small and medium enterprises (SMEs) that have a domestic (in-house) innovation activity (% of the total number of SMEs);
11. innovative SMEs that cooperate with others for innovation (% in the total number of SMEs); SMEs prove a much more flexibility than the big companies, in all their activities, and by cooperating with other units they can become more powerful, having at the same time the advantage of reduced size and local presence. Industrial clusters are part of this category (for example technological parks) that create conditions for a mutual stimulation of ideas and knowledge;
12. innovation expenditures as percent of turnover; this indicator is calculated as a ratio between the sum of total innovation expenditure for enterprises (in-house research-development and outside the enterprise, product and process innovation, buying of patents and licenses, industrial design, innovation marketing etc.) in the total turnover (including the enterprises with no innovation activity);
13. early-stage venture capital (venture capital investment is defined as private equity raised for investment in companies), as percent of GDP ;
14. information and communication technology expenditures, as percent of GDP;
15. number of SMEs who introduced an organizational innovation in the total number of SMEs; the indicator refers to SMEs that use new or significantly improved knowledge

management systems, a major change to the organization of work within the enterprise, significant modifications in their relations with other firms or public institutions.

- **OUTPUT 1: applications**

The five indicators from this group measure the performance, expressed in terms of labour and business activities, and their value added in innovative sectors, mostly in high-tech domains:

16. the percent of employees in high-tech services (post and telecommunication, information technology – IT, research-development services) in the total workforce;
17. exports of high technology products, as a share of total value of exports;
18. sales of new products to the market (or significantly improved products), as percent of turnover;
19. sales of new products to the firm, but already on the market, as percent of turnover;
20. employment in medium-high and high-tech manufacturing, as percent of total workforce; this indicator refers to the activities in the following domains: chemicals, machinery, office and electrical equipment, telecommunications and related equipment, precision instruments, automobiles and other transport.

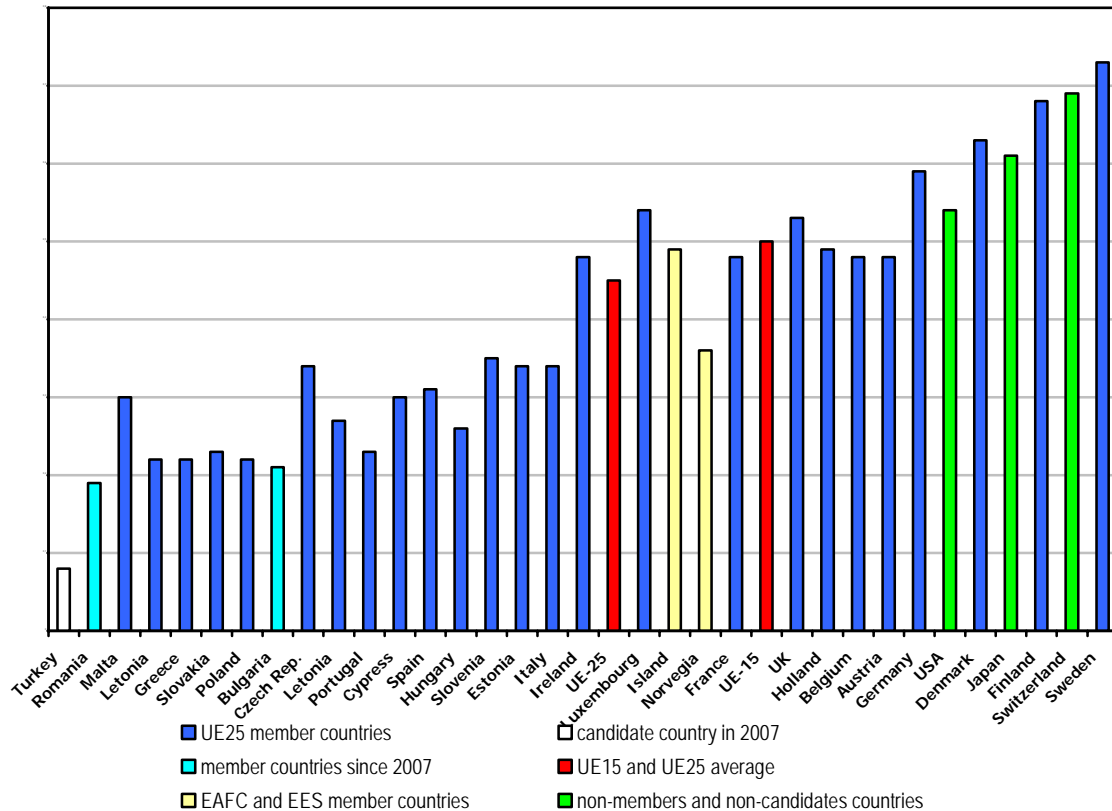
- **OUTPUT 2: intellectual property**

The following five indicators from this group measure the achieved results in terms of successful know-how.

21. number of patents applied for at the European Patent Office (EPO), per million population; high class patents comprise: computers and automatised equipment for business; genetic engineering and microorganisms; aviation; communication; semiconductor; laser;
22. number of patents granted by the US Patent and Trademark Office (USPTO) per million population;
23. number of triad patents (filed at the EPO, the Japanese Patent Office-JPO and the USPO) per million population;
24. number of new community trademarks per million population;
25. number of new community designs per million population.

The summary innovation index calculated as arithmetical mean of the standardized values of these partial indicators (according to the previous algorithm) permits the identification of relative places in innovation of the EU countries, and of candidate countries as well, those countries that joined in the last wave (figure no.1).





**Figure 1. The Summary Innovation Index in 2006 in the EU countries and the candidate countries**

(Source: EUROSTAT, *The European Innovation Scoreboard Indicators*, and CIS 4. Note: EAFC– European Free Trade Association; EES –Economic European Space/area).

Starting with the increase of the synthetic innovation indicator for each country, we can analyze the innovative performance that identifies four big groups of countries: *the innovation leaders*, that have an over average level of synthetic index, and a rapid growth as well; *the intermediary countries*, that have a reduced level (about the average) of synthetic index; *countries where the synthetic innovation index is increasing*, but its level is under average and *the group of countries under the average level of EU*, as level and the dynamic of the synthetic innovation index, as well.

Figure 2 shows the Summary Innovation Index on the vertical axis and the average growth rate of the Index on the horizontal axis. Countries above the horizontal dotted line currently have an innovation performance above that of the EU25. Countries to the right of the vertical dotted line had a faster average increase in the Index than the EU25.

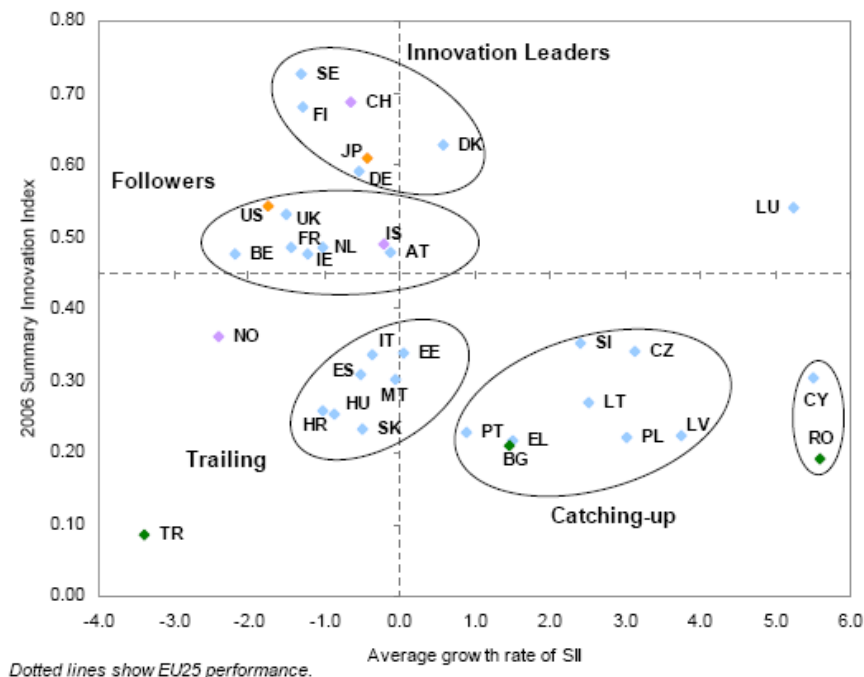
Based on their Index score and the growth rate of the Index, the countries included in the analysis can be divided into four groups or clusters:

- Sweden, Switzerland, Finland, Denmark, Japan and Germany are the *innovation leaders*, with Index scores well above that of the EU25 and the other countries. The lead

of the innovation leaders has been declining compared to the average of the EU25, with the exception of Denmark.

- The US, UK, Iceland, France, Netherlands, Belgium, Austria and Ireland are the *innovation followers*, with Index scores below those of the innovation leaders but above that of the EU25 and the other countries. The above EU25 average innovation performance of the innovation followers has been declining. Also, the gap of the innovation followers with the innovation leaders has on average slightly increased.
- Slovenia, Czech Republic, Lithuania, Portugal, Poland, Latvia, Greece and Bulgaria make up the group of *catching-up countries*, with Index scores well below that of the EU25 and the innovation leaders, but with faster than average innovation performance improvement.
- Estonia, Spain, Italy, Malta, Hungary, Croatia and Slovakia seem to be *trailing*, with Index scores well below that of the EU25 and the innovation leaders, and innovation performance growth which is either below or only just above that of the EU25.

Cyprus and Romania form a separate fifth cluster of fast growing, catching-up countries. Cyprus being one of the smallest EU countries and Romania starting from very low levels of innovation performance, this cluster is less robust than the other clusters, and is therefore not considered to be a real cluster. Luxembourg, Norway and Turkey do not fit into any of these groups.



**Figure 2. The Summary Innovation Index in 2006 and trends**

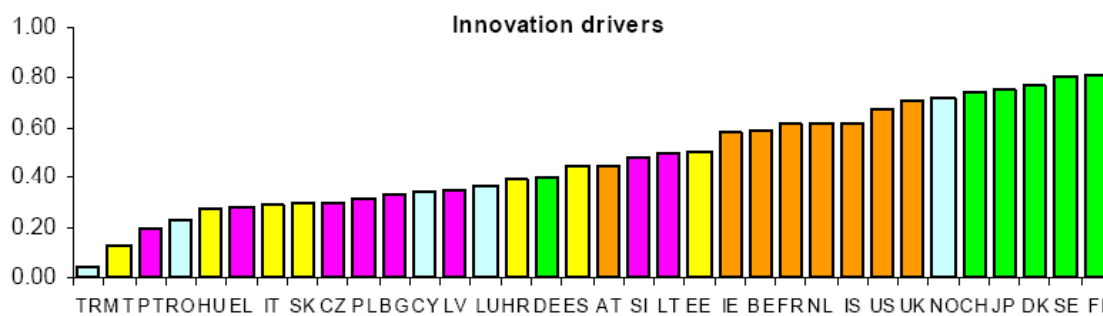
(Source: EUROSTAT, *The European Innovation Scoreboard 2006*, and *Pro-INNO Europe*)

Current performance as measured by the Summary Innovation Index is shown on the vertical axis. Relative to EU25 growth performance of the Index is shown on the horizontal axis. This

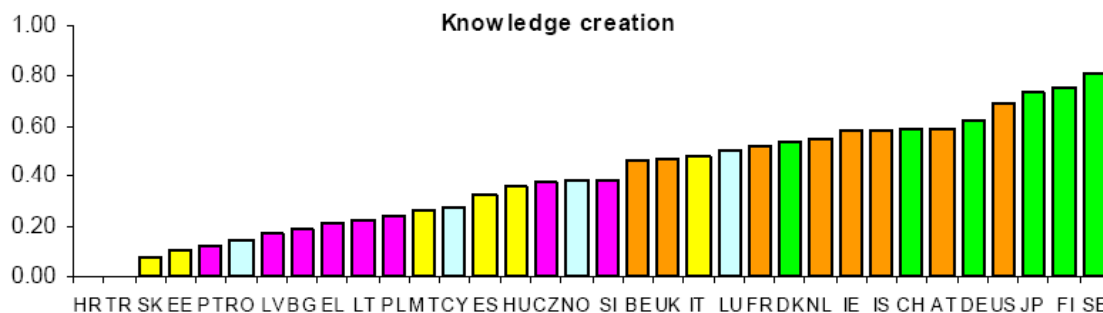
creates four quadrants: countries above both the average EU25 trend and the average EU25 Index are forging ahead from the EU25, countries below the average Index but with an above average trend performance are catching up, countries with a below average Index and a below average trend are falling behind, and countries with an above average Index and a below average trend maintain their lead but are growing at a slower rate.

Figure 2 suggests that there is a *process of convergence* in innovation performance in Europe: the catching-up countries are closing the gap with the EU25 and both the innovation leaders and followers are experiencing a relative decline in their innovation lead with the EU25. This relative decline is a straightforward result of the rapid increases in innovation performance in the new member states.

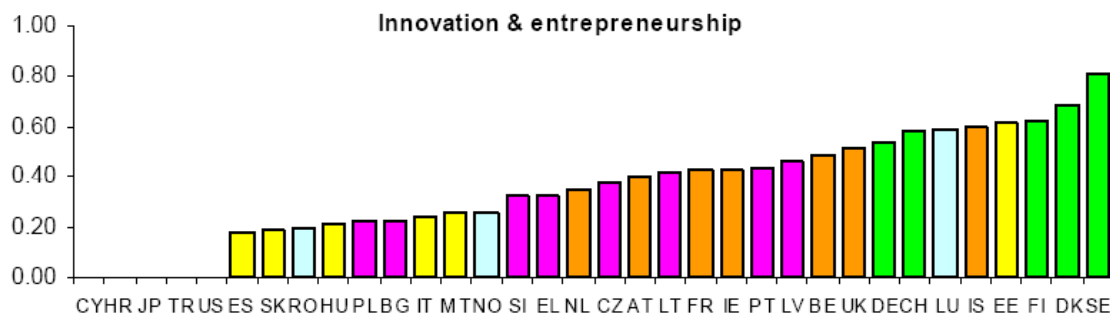
The analysis can be studied thoroughly with the help of sub-indexes calculated on blocs of indicators for the year 2006. The figures below (Source: *EUROSTAT, The European Innovation Scoreboard 2006 – Pro INNO Metrics Europe*) show the ranking of countries for each of the 5 dimensions, from worst to best performer:



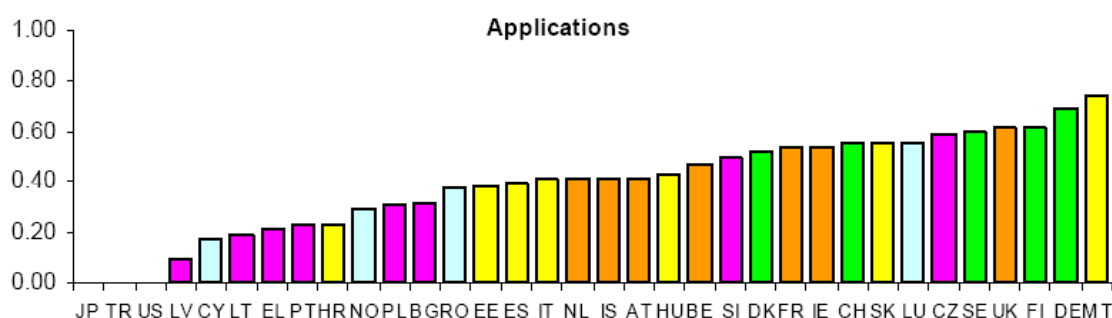
**Figure 3. The synthetic index of Innovation drivers in 2006**



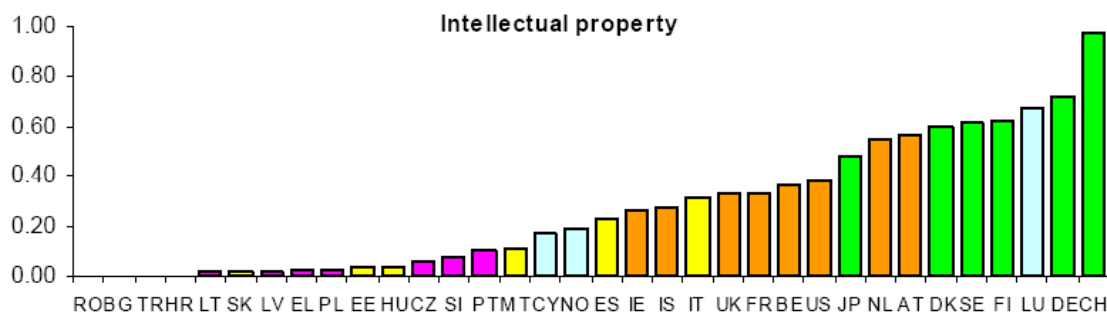
**Figure 4. The synthetic index of Knowledge creation in 2006**



**Figure 5. The synthetic Innovation and entrepreneurship index in 2006**



**Figure 6. The synthetic index of innovation Applications in 2006**



**Figure 7. The synthetic index of Intellectual property in 2006**

*Abbreviations used in graphs:*

- **EU – European Union:** AT-Austria; BE-Belgium; DK-Denmark; DE-Germany; EL-Greece; ES-Spain; FI-Finland; FR-France; IE-Ireland; IT-Italy; LU-Luxembourg; NL-Holland; PT-Portugal; SE-Sweden; UK-England;
- **ACC – The countries that became members of the EU in 2004 :** CZ-Czech Republic; EE-Estonia; CY-Cyprus; LV-Letonia; LT-Lithuain; HU-Hungary; MT-Malta; PL-Poland; SL-Slovenia; SK-Slovakia;
- **ACC I – The countries that became EU members in 2007:** BG-Bulgaria; RO-Romania;
- **CC – Candidate country:** TR-Turkey;
- **Other countries:** IS-Island; NO-Norvegia; US-USA; JP-Japan; CH-Switzerland; HR-Croatia.

The analysis of innovation subindexes allows the identification of weak points of the member countries. It has been demonstrated that the resources for the support of less performant areas of innovation are more beneficial compared to the use of the same resources for stronger domains. This suggests that a balanced policy, which supports the harmonious development of all innovation domains is more efficient.

Generally, there is a concordance between the place of a country in the hierarchy based on the summary index and the place it has according to the subindex values. There are some significant exceptions. Germany and Austria are performing relatively worse in Innovation drivers, the Netherlands in Innovation and entrepreneurship, and the Netherlands, Austria and Iceland in Applications. Of the stagnating countries, Estonia is among the best performers in Innovation and entrepreneurship and Malta in Applications.

**The innovation indicators elaborated by EUROSTAT are used by the Romanian statistics.**

In figure 8 the relative place of Romania is presented (% in the average level EU-25) in 2005, referring to the innovation indicators, the indicators referring to SMEs have an important place.

Romania's place is not favorable compared to the average of EU referring to SMEs innovative capacity. The only indicators Romania is superior to the average is the SMEs weightings that introduce the nontechnological progress and the new products for the market, as weightings in the turnover, while at the expenses weightings with communications technology in the GDP exceeds the average level slowly.

There is a rising tendency of the disparity/difference at indicators «weightings in GDP of direct expenses of the companies» and «patents request».

On the other hand, there is a favourable trend of reducing the disparities at the rapid rising indicators than the EU average: the employees' weightings in top domains, the number of the graduates, the weightings of research-development public expenses in GDP, etc.

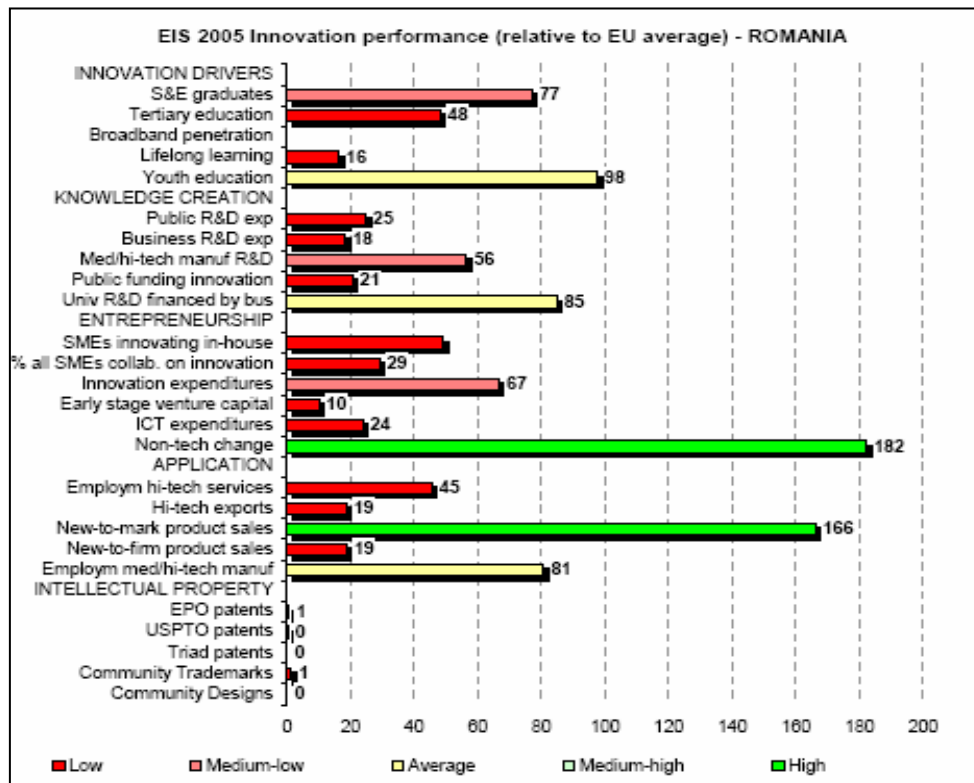
The synthetic innovation index and the partial innovation indicators in Romania compared to the EU average level presents Romania in an unfavorable place referring to innovation capacity. However, Romania is among the groups that are in a process of disparity recovery confronted by the EU average level. This position illustrates, on one hand, the tendency of economic rise mostly based on cheap labour hand, and on the other hand, the low level of the infrastructure and of innovational mechanisms that are in a primary stage of development.

Most of the partial innovation indicators present a reduced tendency of disparities. Except the expences for information technology and communications, tertiary education, direct expenses of companies and EPO patents, which are on an unfavorable trend.

The evolution of main partial innovation indicators shows:

- positive tendencies for permanent education, research-development of public expenses (relating to the governmental decision to rise to 1% the weightings in the GIP of research-development public funds), *high-tech* EPO and USPTO patents;
- moderate rising tendencies in the number of university graduates;
- worsening tendencies for the EPO patents and the companies research expenses (related to the reduced innovational potential of companies, the strong tendency to import

equipment and technologies from abroad, the reduced request for domestic research-development and the orientation mostly to commerce and services).



**Figure 8. Romania’s place in EU referring to partial innovation indicators**

(Source: EUROSTAT, New Cronos, CIS 3 and Pro INNO Europe, Country Report-Romania)

The innovative profile of Romanian firms is still very low: over 80% of non-innovator firms, next to approximately 10% of intermittent innovator firms and a small percentage of strategic innovator, adopter and modifier firms. Innovative firms account for less than a fifth of the country’s total number of active firms and workforce, and for about 42% of the total turnover of active firms. Innovative firms are predominantly SMEs (83,4%) and operate mainly in industry (73%), while the rest are active in services (trade, real estate, transport and communications). This situation is to a large extent the result of a very low level of public funding of innovation, with only 10% of innovative firms receiving funding, and very low levels of innovation expenditures, which don't exceed 3% of innovative firms’ turnover. Although significant progress has been made in order to foster the weak innovation culture in the country, further measures are needed to increase application of research – development results by business and to turn innovation into a driver of national competitiveness.

The distribution of innovative companies on regions points out that many of them are in Bucharest. These indicators show a reduced innovative capacity, explained by the insufficient development of innovative infrastructure and of diffusion instruments, which slows the rhythm of economic development considerably. Although progress towards innovational system

consolidation has been made, firm methods are needed to amplify the research-development results application and transformation of the innovational process in a motor of national competitiveness.

#### References:

- Sandu, Steliana;  
Ioan-Franc, Valeriu      *Creativitatea și inovarea – experiențe europene*, publicat în *Studii și cercetări economice – vol. 44-45*, Academia Română, Institutul Național de Cercetări Economice, Centrul de Informare și Documentare Economică, București, colecția 2007
- Schiemann, M.      *SMEs in Europe - candidates countries, Luxemburg, Eurostat, 2005*
- \*\*\*      *Sources and Resources for EU Innovation, Statistica in Focus, Eurostat, ianuarie, 2007*
- \*\*\*      *EUROSTAT: NewCronos, The third community innovation survey (CIS 3, CIS 4), The European Innovation Scoreboard Indicators*
- \*\*\*      *Pro INNO Europe, INNO Metrics, European Innovation Scoreboard 2006, "Comparative Analyses of Innovation Performance"*
- \*\*\*      *Pro INNO Europe, European Trend Chart on Innovation, Romania, 2006*
- \*\*\*      <http://trendchart.cordis.lu/Scoreboard/scoreboard.htm>
- \*\*\*      <http://www.proinno-europe.eu>
- \*\*\*      <http://epp.eurostat.ec.europa.eu>

# REAL EXCHANGE RATES AND COMPETITIVENESS: A COMPARATIVE ANALYSIS OF CEE COUNTRIES

ALEXANDRA HOROBET<sup>1</sup>

LIVIA ILIE<sup>2</sup>

LUCIAN BELASCU<sup>3</sup>

## Abstract

Unexpected fluctuations in exchange rates represent a matter of concern for all businesses nowadays as the volatility in exchange rates impacts businesses' cash flows, revenues and expenses, and eventually is reflected in the company's risk-return profile. Companies' exposures to exchange rate risk have considerably increased in the past decades, given the boost in international operations and the continuous diversification of businesses' activities at the global level. Despite the attention that businesses display to nominal exchange rates changes, it is the real exchange rate that should be of more concern to corporate managers, since they induce changes at the level of the competitiveness of the business. Our paper comparatively analyzes the exposure to changes in the nominal and real exchanges rates of the local currencies that companies from a number of four Central and Eastern European countries (Romania, Hungary, Czech Republic and Poland) and investigates the nature of the relationship between stock market performance and exchange rates in the four countries under consideration.

**Key words:** exposure, exchange rate risk, Central and Eastern Europe, co-integration, Granger causality

**JEL classification codes:** F23, F31, G15

---

<sup>1</sup> Academy of Economic Studies Bucharest, Faculty of International Business and Economics, 13-15 Mihai Eminescu, Bucharest, alexandra.horobet@rei.ase.ro.

<sup>2</sup> University Lucian Blaga of Sibiu, Faculty of Economic Sciences, 17 Calea Dumbravii, Sibiu, ilieliv@yahoo.com.

<sup>3</sup> University Lucian Blaga of Sibiu, Faculty of Economic Sciences, 17 Calea Dumbravii, Sibiu, lucian\_belascu@yahoo.com.



## I. Introduction and theoretical considerations

Unexpected fluctuations in exchange rates represent a matter of concern for all businesses and particularly for those involved in international business, since the generalized adoption of floating exchange rates, at the beginning of 1970's. The volatility in exchange rates impacts businesses' cash flows, revenues and expenses, and eventually is reflected in the company's risk-return profile. At the same time, the increased globalization process that took place in the last decades has made exchange rates an issue that cannot be ignored by any company, no matter its degree of international involvement. Works in the field of international finance consider exchange rate risk as one of the most relevant components of financial management in modern times, since companies' exposures to exchange rate risk have considerably increased in the past decades, given the boost in international operations and the continuous diversification of businesses' activities at the global level.

In international finance research, corporate exposure to exchange rate risk is built upon the impact of exchange rate changes on a number of key-elements: shareholder's wealth, firm's assets and liabilities or company's financial position. Adler and Dumas (1984) define exposure to exchange rate risk as the change in the value of the firm induced by changes in exchange rates. This is one of the broadest definitions of exposure, followed by others, more specific. Eiteman, Stonehill and Moffett (2004) measure exposure by the potential change in company's profitability, its net cash flows and market value, determined by exchange rate changes. Holland (1993) locates foreign exchange exposure at the level of companies that own assets abroad, thus ignoring companies that operate in a purely national environment. Another definition is provided by Shapiro (2002) that understands by exchange rate exposure the degree to which a company is affected by exchange rates changes. Beyond the mere definition, international research demonstrates a higher homogeneity with regard to the exchange rate exposure types that a company faces. Depending on the moment in time when exchange rates change, a company might face: (1) *transaction exposure*, that arises whenever the firm commits or is contractually bounded to make or receive a payment at a future date denominated in a foreign currency; (2) *translation exposure*, arising from the need to globally consolidate the financial reports of a multinational company, starting from affiliates' reports denominated in various currencies; and (3) *economic exposure*, seen as the change in the firm's present value as result of changes in the value of the firm's expected future cash flows and cost of capital, induced by unexpected exchange rate changes. As opposed to transaction and translation exposure, a firm will be confronted with economic exposure to exchange rates when unanticipated real, not only nominal exchange rate changes, have a non-zero effect on its expected future cash flows<sup>4</sup>. Two main mechanisms that generate economic exposure can be identified: a conversion effect – given the lower amount in home currency that will be obtained after converting the same amount in a foreign currency at a lower exchange rate; a competitive effect – given the change in the firm's competitive position that follows an asymmetric sensitivity of its revenues and expenses to exchange rate changes.

Empirical evidence on corporate exposure to exchange rate risk is almost entirely concentrated on the case of companies originated from developed countries, given the higher data availability for performing tests. At the same time, in most studies, the impact of nominal exchange rate changes, as opposed to real exchange rate changes is tested, following the rationale that inflation rates are small and that any change in the nominal exchange rate level will directly generate changes in the real exchange rate level. Albeit this might be true for

---

<sup>4</sup> Other terms used for economic exposure are operating exposure, real exposure and competitive exposure.

developed countries, traditionally displaying low inflation rates, in the case of less developed countries, where inflation rates are higher, the connection between nominal and real exchange rates is not as direct. Jorion (1990) examines US multinational corporations exposure to exchange rate risk for a 17 years period and concludes that share prices of these companies are not systematically influenced by changes in nominal exchange rates, but further research on American multinationals conducts to mixed results: Bartov and Bodnar (1994) and Choi and Prasad (1995) confirm Jorion's findings, while Allayannis (1996), Miller and Reuer (1998), Gao (2000) and Koutmos and Martin (2003) seem to detect a more significant link between the American companies share prices and changes in the nominal exchange rate of the dollar against various currencies. Research in the field also identifies lagged exposures, as well as asymmetric responses of share prices to changes in the dollar value. Outside the United States, Glaum et al. (2000) investigate German companies' exposure to changes in the nominal exchange rate of the German mark against the dollar during 1974-1997 and find it as being significant. Their result is confirmed by Entorf and Jamin (2002), which identify the company's degree of involvement into international business and the level of the exchange rate as being two important factors in explaining the exposure. Dutch companies have been researched by De Jong et al. (2002) that find more significant exposures in phases of the Dutch guilder depreciation, after investigating 117 companies over a 5-year period (1994-1998). Doukas et al. (2003) examine the relation between the rate of return on a number of 1079 Japanese companies' shares and unexpected changes in the Japanese yen exchange rates between 1975 and 1995 and find significant exposures, which are higher in the case of multinational and exporting companies, being also positively linked to the degree of international involvement of the firm, on one hand, and negatively linked to the firm's size and its financial leverage. British companies also display significant exposure, according to El-Masry (2003), but depending to a large extent on the industry. As mentioned above, less developed countries were less interesting for researchers: to our knowledge the only study released so far – Kyimaz (2003) – investigates Turkish companies for the period 1991-1998 and finds significant exposures to exchange rate risk, but also variable in magnitude from one industry to another.

The concept of exposure to exchange rate risk represents the microeconomic level of analysis for what concerns the linkages between stock prices and exchange rates. The macroeconomic perspective is built on the assumption that stock prices reflect real economic activity and affect exchange rates through the increase in the demand for real money and, subsequently, the value of domestic currency. The relation between exchange rates and stock prices at the macroeconomic level may be sensitive to the exchange rate regime in force. Economic theory suggests that currency appreciation under a floating exchange rate regime reduces the competitiveness of countries' exports and, consequently, is expected to have a negative effect on the domestic stock market. Conversely, for a country relying on imports, an appreciation of the domestic currency lowers input costs and may generate a positive effect on the stock market.

The research undertaken on the macroeconomic linkages between stock prices and exchange rates uses advanced econometric, such as bivariate and multivariate cointegration methods, Granger causality tests and GARCH models. The countries and regions are diverse and the results are also mixed, no definite conclusion being possible to be drawn from them. Kim (2003) investigates the existence of long-run equilibrium relationships among the aggregate stock price, industrial production, real exchange rate, interest rate and inflation rate in the United States, applying Johansen's cointegration methodology. For 1974-1998 he finds that the S&P500 index is positively related to the industrial production but negatively related to the rest of the variables. At the same time, the research indicates that stock prices are driven to

a significant extent by innovations in the interest rate. Dong et. al (2005) examined six emerging Asian countries over 1989 and 2003 and found no cointegration between their exchange rates and stock prices, but they detected bi-directional causality in Indonesia, Korea, Malaysia and Thailand. Except for Thailand, the stock returns show significantly negative relation with the contemporaneous change in the exchange rates, which implies that currency depreciations generally accompany falls in stock prices. Ibrahim (2000) studies the interactions between the foreign exchange market and the stock market in Malaysia and his results indicate that despite the lack of a long-run relationship between the exchange rate measures and stock prices in bivariate cointegration models, there is evidence of such long-run relations in multivariate models that include M2 money supply and foreign reserves. Pacific Basin countries were studied by Phylaktis and Ravazollo (2005), which examine the long-run and short-run dynamics between stock prices and exchange rates and the channels through which exogenous shocks impact on these markets by using cointegration methodology and multivariate Granger causality tests. For the period 1980-1998, their results suggest that these markets are positively related and that the US market acts as a leading factor for these links. Moreover, the links between the stock prices and exchange rates were found to be determined by foreign exchange restrictions. Gunduz and Abdalnasser (2004) investigate the causality between the exchange rates and stock prices in the Middle East and North Africa region before and after the Asian financial crisis and they find uni-directional Granger causality from exchange rates to stock prices for Israel and Morocco before and after the crisis, and for Jordan after the crisis. Additionally, no relationship is identified between the two variables for Egypt. Another interesting research was developed by Murinde and Poshakwale (2004) that investigate price interactions between the foreign exchange market and the stock market in a number of three European emerging financial markets – Hungary, Poland and Czech Republic – before and after the adoption of the euro. Using daily observations on both stock prices and exchange rates, they find that for the pre-euro period stock prices in these countries uni-directionally Granger cause exchange rates only in Hungary, while bi-directional causality relations exist in Poland and Czech Republic. After the euro adoption, exchange rates uni-directionally Granger-cause stock prices in all three countries. The authors interpret these results as being consistent with the dynamic nature of the transition process, suggesting that causality is much easier to detect as the markets become more integrated with the EU.

Our research analyzes both the microeconomic and macroeconomic perspectives on the linkages between stock prices and exchange rates for a number of four Central and Eastern European countries – Czech Republic, Hungary, Poland and Romania. The paper is structured as follows: Section II presents an important conceptual distinction between nominal and real exchange rates, Section III specifies the data and the research methodology, Section IV outlines the results of our research and Section V concludes.

## **II. Nominal and real exchange rates**

Analogous to concerns with the effects of inflation in the domestic setting on nominal versus real price levels, the effects of relative inflation rates between the home economy and the foreign economy matter for the exchange rate between the two countries. When the foreign inflation is higher and the home inflation does not change, the foreign currency would be expected to depreciate against home currency. Although the foreign currency will cost less now in home currency terms, this does not necessarily imply that the real value of goods and services purchases across borders decreased. The explanation resides in the fact that the

increase in foreign prices for goods and services has exactly offset the decline in the value of the foreign currency, given higher inflation rates abroad than at home. Another way of expressing this phenomenon is to say that purchasing power remains the same in the two countries. In this case, while the foreign currency has undergone a nominal depreciation, it has not undergone a real depreciation. Therefore, what eventually matters for purchasing power between any two countries is not the simple change in the nominal exchange rate, but the change in nominal rates after adjustments for the changes in the relative inflation rates between the two countries have been made. The *real exchange rate* can be defined as the nominal exchange rate that takes into account the inflation differentials among the countries. When a currency appreciates in real terms, its purchasing power abroad has increased; when it depreciates in real terms, its purchasing power abroad has decreased. The importance of the real exchange rate to international business and finance research stems from the fact that it can and it is widely used as an indicator of relative competitiveness in the foreign business of a country.

Because of this important role it plays in an economy, the real exchange rate has been one of the most debated issues both in theory and practice. The debate over the real exchange rate is observable at the definition level, on one hand, and at the test level, on the other hand. Since the purpose of this paper is to link real exchange rates with changes in the competitiveness level, we will briefly review only the definition debate, as it is revealed by the existing calculation methods and interpretation of real exchange rates.

The various definitions of the real exchange rate can be categorized under two main types: the first type is linked to the theory of purchasing power parity, while the second is based on the distinction between the tradable and non-tradable goods. Although they may coincide in some special cases, applying these two types of definitions typically leads to different results.

According to Purchasing Power Parity (PPP), the real exchange rate can be defined as the nominal exchange rate, adjusted by the ratio of the foreign country price level to the domestic country price level. Mathematically, we write

$$q_{HC/FC} = \frac{S_{actual}}{(P^{HC} / P^{FC})} = S_{actual} \times \frac{P^{FC}}{P^{HC}}$$

where  $q_{HC/FC}$  designates the real exchange rate,  $S_{actual}$  represents the current exchange rate (spot rate), while  $P^{HC}$  and  $P^{FC}$  stand for the general level of prices in the home country and the foreign country, respectively. In terms of this definition, the benchmark level of the real exchange rate equals 1, while a value higher than one can be interpreted as a real appreciation of the foreign currency. The reverse is true when the real exchange rate has a value lower than 1.

The definition on the basis of tradable and non-tradable goods takes the relative price of the tradable and non-tradable goods in a specific country as an indicator of the country's competitiveness level in the foreign trade. The rationale behind this definition is related to the fact that cost differential between the countries are closely related to the relative price structures in these economies. Under the assumption that the prices of tradable goods will be equal around the world, the real exchange rate can be mathematically represented as

$$q_{HC/FC} = \frac{P_t^{HC}}{P_n^{HC}} = S_{actual} \times \frac{P_t^{FC}}{P_n^{FC}}$$

where  $P_t^{HC}$  and  $P_t^{FC}$  denote the domestic and foreign prices of the tradable goods respectively, while the prices of the non-tradable goods are represented by  $P_n$ . Under the terms

of this definition, a decline in the real exchange rate indicates a real appreciation of the domestic currency. Given an unchanged price structure in a country, a higher relative price of non-tradables leads to a decrease in the country's level of competitiveness against its trade partners. In practice, applying the second definition proves complex (it can only be made by considering the ratio of the prices of exportable or importable goods to the prices of the non-tradables) and for this reason the first definition is widely used.

Although more used, the PPP-based definition of the real exchange rates raises the issue of the price index employed in the computation. The wholesale price index (WPI) and the consumer price index (CPI) are two of the leading indices that can be used in these calculations, other alternatives being the gross domestic product (GDP) deflator and producers price index (PPI). All these indices support criticism. The most important criticism to the real exchange rates calculated by using the WPI is that the commodities included in this index are formed of tradables that are similar in nature and, therefore, their prices are not expected to differ substantially when measured in a common currency. Consequently, the changes in the real exchange rate calculated using the WPI would not sufficiently indicate the changes in a country's competitiveness level. The same criticism applies for the PPI as well: although in theory the PPI includes the prices in the services sector – categorized as non-tradables –, in practice such an index includes the prices in the primary and secondary sectors, which are categorized as tradables. On the other hand, the main problem with the real exchange rates calculated by using the CPI is that this index includes the non-tradable commodities, while the main problem with the GDP deflator is that the time series is not available on the monthly basis.

Apart from bilateral nominal and real exchange rates, international financial statistics operates with the concepts of nominal effective and real effective exchange rates. The *nominal effective exchange rate* of a country (NEER) or, equivalently, the “trade-weighted currency index” of the country aims to track changes in the value of the country's currency against the currencies of its main trading partners. The *real effective exchange rate* (or, equivalently, the “relative price and cost indicators”) aims to assess a country's competitiveness in terms of prices and costs against its main competitors in international goods and services markets. The existing literature employs a wide range of prices to calculate real effective exchange rates, such as: consumer price index (CPI), GDP deflator, industrial production prices index (PPI), nominal unit labour costs for the total economy or for the manufacturing industries, and the ratio between the prices of tradable and non-tradable goods. As an indicator of international competitiveness, the real effective rate is best to be used over a long-run horizon. Still, despite its widespread use, this indicator has some disadvantages. Specifically, the concept of international competitiveness is difficult to be measured at the economy level, as the indicator does not take fully into account the competition at firm level that includes factors such as product quality, innovation and reputation. Nevertheless, the use of real exchange rates may be explained by the fact that firms' international performances are highly influenced by macroeconomic evolutions, particularly in emerging countries.

The methodologies used for the computation of the effective exchange rates differ between the International Monetary Fund, European Central Bank and OECD. In our research we have used the rates calculated according to the European Central Bank methodology. Specifically, the NEER is calculated as a weighted geometric average of the bilateral exchange rates against the currencies of trade partner countries and reported as an index; a rise in the index indicates a strengthening of the currency in nominal terms. The REER corresponds to the NEER deflated by nominal unit labour costs for the total economy and consumer prices (CPI/HICP); a rise in the index signifies a real appreciation of the currency and, by consequence, a loss of competitiveness.

### III. Data and research methodology

The research employs two sets of data on each of the four countries – Czech Rep., Hungary, Poland and Romania -, over the January 1999 – June 2007 period. The first set of data covers monthly values of local stock market indices, denominated in the local currencies. In order to track the performance of stock exchanges in the region we have used the MSCI (Morgan Stanley Capital International) indices for Czech Rep., Hungary and Poland and the BET-C index of Bucharest Stock Exchange for Romania. For what concerns the exchange rates data, we have used the nominal and real effective exchange rates of the local currencies (Czech koruna, Hungarian forint, Polish zloty and Romanian leu) computed against the euro-13 area countries and the main 41 trading partners. Data on nominal and real effective rates were collected from the database of the Directorate General for Economic and Financial Affairs of the European Commission.

In order to identify the relevance and magnitude of corporate exposures to changes in the exchange rates in these countries, we have used simple regressions such as

$$y_{it} = \alpha_i + \beta x_{it} + \varepsilon_{it} \quad \text{and} \quad y_{it} = a_i + bz_{it} + \omega_{it}$$

where  $y_{it}$  represents the monthly change in the stock market index of country  $i$ ,  $x_{it}$  denote the changes in the nominal effective exchange rates of the domestic currency of country  $i$ ,  $z_{it}$  indicate the changes in the real effective exchange rates of the domestic currency of country  $i$ , and  $\varepsilon_{it}$  and  $\omega_{it}$  are regression residuals. Changes in stock market indices and exchange rates are all computed as first differences of monthly logarithmic values. Also, a lagged relationship between the variables was estimated, of the form

$$y_{it} = \alpha_i + \beta x_{t-1,i} + \varepsilon_{it} \quad \text{and} \quad y_{it} = a_i + bz_{t-1,i} + \omega_{it}$$

In all regressions, the regression coefficients ( $\beta$  and  $b$ , respectively) indicate the sign and magnitude of the respective market overall exposure to exchange rate risk: the higher the value of the coefficient, the higher the exposure; a positive sign of the coefficient implies that a nominal or real appreciation of the domestic currency results in an increase in the value of the stock index and, consequently, in an increase in the value of the equity of companies in the respective country; a negative sign of the coefficient shows that a nominal or real depreciation of the domestic currency is reflected in a decrease in the value of the index and, by means of consequence, in a decrease in the value of the companies in the country under consideration.

The other direction of our research aimed at identifying significant interactions between the stock exchange performances and exchange rates and was developed using two different but complementary methodologies: a cointegration test and a Granger causality test. The concept of cointegration was first developed by Engle and Granger (1987), and it considers the case of variables that are I(1) and are included in a regression. Engle and Granger advanced the idea that sometimes the regression of two I(1) variable might not be spurious, but meaningful, in case the two variables are cointegrated. Generally, if  $y_t$  and  $x_t$  are two I(1) processes, then, in most of the cases,  $y_t - \beta x_t$  is also a I(1) process for any number  $\beta$ . Nevertheless, it is possible that for some  $\beta \neq 0$ ,  $y_t - \beta x_t$  is not an I(1), but an I(0) process, with constant mean, constant variance and autocorrelation that depends only on the time distance between any two variables in the series, and it is asymptotically uncorrelated. If such  $\beta$  exists, the series  $y_t$  and  $x_t$  are said to be cointegrated and  $\beta$  is called the cointegrating parameter. Economically speaking, cointegration of two variables indicates a long-term or equilibrium relationship between them, given by their stationary linear combination (called the cointegrating

equation). We test for the existence of cointegration between the stock market indices and the exchange rates using the methodology developed by Johansen (1988) and Johansen and Juselius (1990).

The Granger causality test (Granger, 1969) was developed as a more efficient approach as compared to the basic correlation tool, which does not imply causation between correlated variables in any significant sense of the word. The Granger test addresses the issue of whether the current value of a variable  $y - y_t$  - can be explained by past values of the same variable -  $y_{t-k}$  - and then whether adding lagged values of another variable  $x - x_{t-k}$  - improves the explanation of  $y_t$ . As such, the variable  $y$  is said to be Granger-caused by  $x$  if the coefficients on the lagged values of  $x$  are found to be statistically significant. The statement “ $x$  Granger causes  $y$ ” does not necessarily imply that  $y$  should be seen as the effect or results of  $x$ , as the Granger test measures only precedence and information content on variable  $y$ , and does not indicate causality in the common sense of the word.

In our research we performed bivariate Granger causality tests on stock exchange logarithmic returns and first logarithmic differences in exchange rates, using the standard methodology proposed by Granger (1969, 1986) and Engle and Granger (1987). In order to test for Granger causality among the stock market index  $x_t$  and exchange rate  $y_t$  we estimated the following equations:

$$\Delta \ln y_t = c + \sum_{i=1}^k \delta_i \Delta \ln y_{t-i} + \sum_{i=1}^k \beta_i \Delta \ln x_{t-i} + \varepsilon_t$$

$$\Delta \ln x_t = g + \sum_{i=1}^k \phi_i \Delta \ln x_{t-i} + \sum_{i=1}^k \gamma_i \Delta \ln y_{t-i} + \omega_t$$

and performed an F test for joint insignificance of the coefficients  $\beta_i$  and  $\gamma_i$ ,  $i=1 \dots k$ . The null hypothesis was that  $x_t$  does not Granger cause  $y_t$  or  $y_t$  does not Granger cause  $x_t$ . Therefore, when the null hypothesis is rejected this indicates a presence of Granger causality. For each pair of stock market index and exchange rate we performed two Granger causality tests in order to identify unilateral causation ( $x_t$  causes  $y_t$  or  $y_t$  causes  $x_t$ ), bilateral causation ( $x_t$  causes  $y_t$  and causes  $x_t$ ) or no causation.

An important issue linked to the specification of the Granger causality tests is worth mentioning. As shown by MacDonald and Kearney (1987), Miller and Russek (1990) and Lyons and Murinde (1994), the Granger causality tests are well specified if they are applied in a standard vector autoregressive form to first differenced data only for non-cointegrated variables. Statistically, the presence of cointegration excludes non-causality between the variables under consideration. Therefore, if two variables are found to be cointegrated, then there must be causality in the Granger sense between them, either uni-directionally or bi-directionally. We approached this issue by performing cointegration tests between relevant variables and excluding from the application of the Granger tests those pairs of variables that were found to be cointegrated.

#### IV. Results

Before applying the research methodologies presented in Section III above, we tested all variables for the presence of unit root, using the Augmented Dickey-Fuller procedure. The

test indicated that indices levels and exchange rates were all non-stationary, while their first differences were stationarity at 1% or 5% level of significance. These results made the application of the cointegration test on indices and exchange rates levels relevant, as well as the Granger causality tests on first differences.

Table 1 below presents the results of the contemporaneous exposures of stock markets in the four countries under analysis to nominal and real exchange rate risk.

**Table 1. Contemporaneous exposures of stock markets**

<i>Dependent variables</i>	<i>Independent variable</i>	<i>Exposure coefficient</i>	<i>T-statistic</i>	<i>P-value</i>
CZRET	CZREERR13	0.954444	1.725135	0.0876
HURET	HUNEERR41	1.116029	2.191603	0.0308
HURET	HUNEERR13	1.234269	2.527224	0.0131
HURET	HUREER13	1.002548	2.104760	0.0378
HURET	HUREER41	0.911044	1.808469	0.0736
PLRET	PLNEERR41	1.095328	3.036402	0.0031
PLRET	PLNEERR13	0.989120	2.947287	0.0040
PLRET	PLREERR13	0.897579	2.753831	0.0070
PLRET	PLREERR41	1.005932	2.869918	0.0050

Note: CZRET, HURET and PLRET designate the first difference in stock market indices from Czech Rep., Hungary and Poland, respectively. The column *Independent variables* refers to the first differences in nominal effective or real effective exchange rates of the respective currencies, either including the 13 euro-area member countries, or the main 41 trading partners.

Our results indicate that three of the markets (Czech Republic, Hungary and Poland) are exposed to changes in nominal and/or real exchange rates. Romania's capital market, on the other hand, does not seem to be exposed to exchange rate risk. For all the markets that were found to be exposed to currency risk, the regression coefficients are positive, which shows that the stock market reacts positively – by increasing in the overall value of the stocks traded – to nominal and real appreciations of the local currency. In terms of nominal exposure to exchange rate risk, only the stock markets from Hungary and Poland respond to changes in the exchange rate, when the latter is measured against the 13 euro-area members and the main 41 trading partners of the countries. This indicates that investors from these countries see a strengthening of the local currencies in nominal terms as positively influencing the value of companies traded in the market. For what concerns exposure to real exchange rate risk, all three countries' stock markets react in the same manner: since regression coefficients are positive, this means that a strengthening of the local currency in real terms, which generally indicates a loss in the country's competitiveness, has also a positive impact on the companies' values. It is also interesting to note that no statistically significant exposures were identified when we used 1-month lagged regressions, which proves that investors in these markets are quickly incorporating in the stock markets' returns any changes in exchange rates and do not take into account when constructing the stock prices and returns the past values of exchange rates.

Turning to the second objective of our research – testing for the presence of significant links between stock markets and exchange rates -, we performed a cointegration test on stock market indices and nominal effective and real effective exchange rates (all as logarithmic values). This test had two main purposes: the first one was to observe the presence of a long-



run relationship between the stock market and the foreign exchange markets, and the second was linked to the application of the Granger test, as explained in Section II of the paper. Table 2 presents the results of the cointegration tests and allows us to observe that no long-term relationship exists between the stock market performance and exchange rates in all of the countries considered. On the other hand, for two of the markets – Hungary and Romania – cointegration tests indicate the existence of such a long-term link between the stock market and the nominal exchange rate: in case of Hungary, the link involves only the nominal effective rate of the forint against the euro-area member countries, while in case of Romania the connection engages both nominal effective rates.

**Table 2. Results of the cointegration tests (1 lag)**

<i>Stock markets and nominal effective exchange rates</i>			<i>Stock markets and real effective exchange rates</i>		
	<i>Trace</i>	<i>Eigen</i>		<i>Trace</i>	<i>Eigen</i>
CZINDEX – CZNEER13	3.5763	0.0347	CZINDEX – CZREER13	4.3294	0.0423
CZINDEX – CZNEER41	3.2616	0.0268	CZINDEX – CZREER41	3.1832	0.0298
HUINDEX – HUNEER13	16.1320**	0.1489**	HUINDEX – HUREER13	5.5419	0.0516
HUINDEX – HUNEER41	13.0792	0.1193	HUINDEX – HUREER41	6.3072	0.0520
PLINDEX – PLNEER13	7.9798	0.0727	PLINDEX – PLREER13	8.8705	0.0817
PLINDEX – PLNEER41	6.2281	0.0584	PLINDEX – PLREER41	6.0544	0.0587
ROINDEX – RONEER13	18.8993**	0.1398**	ROINDEX – ROREER13	3.7384	0.0366
ROINDEX – RONEER41	22.9335*	0.1701*	ROINDEX – ROREER41	6.1241	0.0591

Note: \* indicates significance at 1% level, and \*\* at 5% level.

Following the cointegration tests, we performed Granger causality test in the standard vector-autoregressive form for variables that were not found to be cointegrated. Therefore, we excluded from such tests the pairs HURET-HUNEERR13, RORET-RONEERR13 and RORET-RONEER41. Based on the Akaike criterion, all Granger tests were performed using one lag on both explained and explanatory variables. Table 3 below presents the results of the Granger tests, only for the pairs of variables where a causality relationship was identified.

**Table 3. Results of Granger causality tests**

<i>Null hypothesis</i>	<i>F-statistic</i>	<i>Probability</i>
HURET does not Granger Cause HUNEERR41	2.90597	0.09145
HURET does not Granger Cause HUREERR13	4.80576	0.03076
HURET does not Granger Cause HUREERR41	4.11650	0.04521
PLRET does not Granger Cause PLNEERR13	8.17406	0.00520
PLRET does not Granger Cause PLNEERR41	8.35569	0.00474
PLRET does not Granger Cause PLREERR13	7.51254	0.00730
PLRET does not Granger Cause PLREERR41	7.60122	0.00697

The first important observation that needs to be made with respect to Granger causality tests is that all causal relationships are unilateral, from the stock markets to the exchange rates. Only investors from Hungary and Poland consider the past information on companies' performance relevant for the exchange rates, while investors from Czech Republic do not consider such information as relevant. At the same time, there is no information transmission from the exchange rates to the stock market, which might indicate that the market adjusts quicker to evolutions in the foreign exchange market and, therefore, testing for such a high lag is irrelevant. Also, since no bilateral causation relationships were identified, it seems that in those four markets the two markets do not serve as reciprocal information channels for each other.

## **V. Conclusions**

Our paper approached the linkages between the stock market and the foreign exchange market in the case of four Central and Eastern European countries – Czech Republic, Hungary, Poland and Romania – from both a microeconomic and a macroeconomic perspective. The main findings suggest that in three of these countries (Hungary, Poland and Romania) exchange rates and stock market performance are related, although differently from one country to another. As such, in Hungary and Poland the information embedded in stock market returns is integrated into the local currencies' nominal and real values, while in Hungary and Romania a long-term relationship between the stock market performance and the nominal effective exchange rate is identified. On the other hand, the microeconomic perspective sheds light on the fact that the overall's market exposure to nominal exchange rate risk is present only in Hungary and Poland, while exposure to real exchange rate risk is identified in all countries except Romania. Possible explanations of these findings may be related to diversification of exchange rate risk among companies, given the systematic nature of this risk, as well as to hedging activities of local companies.

## References

- Allayannis, G. (1996), "Exchange rate exposure revisited", *University of Virginia Working paper*
- Bartov, E., Bodnar, G. (1994), "Firm valuation, earnings expectations, and the exchange-rate exposure effect", *Journal of Finance* Vol. 49, No. 5, pp. 1755-1788
- Choi, J., Prasad, A. (1995), "Exchange rate sensitivity and its determinants: A firm and industry analysis of U.S. Multinationals", *Financial Management*, Vol. 24, No. 3, pp. 77-88
- De Jong, A., Ligterink, J., Macrae, V. (2002), "A Firm-Specific Analysis of Exchange-Rate Exposure of Dutch Firm" *Erasmus Research Institute of Management Working Paper*
- Dong, Shuh-Chyi, Yang, Sheng-Yung, Wang, Alan T. (2005) "The Dynamic Relationship and Pricing of Stocks and Exchange Rates: Empirical Evidence from Asian Emerging Markets", *Journal of American Academy of Business*, Vol. 7, No. 1, pp. 118-123
- Doukas, J.A., Hall, P.H., Lang, L.H.P. (2003), "Exchange Rate Exposure at the Firm and Industry Level", *Financial Markets, Institutions & Instruments*, Vol. 12, No. 5, pp. 291-346
- Eiteman, D., Stonehill, A., Moffett, M. (2004), *Multinational Business Finance*, Addison-Wesley Publishing Company
- El-Masry, A. (2003), "The Exchange Rate Exposure of UK Nonfinancial Companies: Industry-Level Analysis" *Manchester Business School Working Paper*
- Engle, Robert F., Granger, Clive W.J (1987), "Co-integration and Error Correction Estimates: Representations, Estimation and Testing", *Econometrica*, Vol. 55, No. 2, pp. 251-276
- Entorf, H., Jamin, G. (2002), "Dance with the Dollar: Exchange Rate Exposure on the German Stock Market", Working Paper, available at <http://ssrn.com/abstract=341320> [Accessed 10.09.2007]
- Gao, T. (2000), "Exchange rate movements and the profitability of U.S. multinationals", *Journal of International Money and Finance*, Vol. 19, pp. 117-134
- Glaum, M. & Brunner, M. & Himmel, H. (2000). The DAX and the Dollar: The Economic Exchange Rate Exposure of German Corporations. *Journal of International Business Studies*, 31(4), 715-724
- Granger, Clive (1969), "Investigating Causal Relations by Econometric Models and Cross-Spectral Methods", *Econometrica*, Vol. 37, No. 3, pp. 424-438
- Granger, Clive (1986), "Developments in the Study of Cointegrated Economic Variables", *Oxford Bulletin of Economics and Statistics*, Vol. 48, No. 3, pp. 213-228
- Gunduz, Lokman, Hatemi-J Abdunnasser (2004) "On the Causal Relationship Between Stock Prices and Exchange Rates: Evidence from the MENA Region", *Be Kent University and University of Skövde Working Paper*, Istanbul and Skövde
- Holland, J. (1992), *International Financial Management*, Routledge, London
- Ibrahim, Mansor H. (2000), "Cointegration and Granger Causality Tests on Stock Price and Exchange Rate Interactions in Malaysia", *ASEAN Economic Bulletin*, Vol.17, No. 1, pp. 36-47
- Johansen, Soren (1988), "Statistical Analysis of Cointegration Vectors", *Journal of Economic Dynamics and Control*, Vol.12, pp. 231-254
- Johansen, Soren, Juselius, Katarina (1990), "Maximum Likelihood Estimation and Inferences on Cointegration – With Application to the Demand for Money", *Oxford Bulletin of Economics and Statistics*, Vol. 52, No. 2, pp. 169-210
- Jorion, P. (1990), "The exchange rate exposure of U.S. multinationals", *Journal of Business*, Vol. 63, pp. 331-345
- Kyimaz, H. (2003), "Estimation of foreign exchange exposure: an emerging market application", *Journal of Multinational Financial Management*, Vol.13, pp. 71-84
- Koutmos, G., Martin, A. (2003), "First- and Second-Moment Exchange Rate Exposure: Evidence from U.S. Stock Returns", *The Financial Review*, Vol. 38, pp. 455-471

- Lyons, S.E., Murinde, V. (1994), "Cointegrated and Granger causality testing of hypothesis on supply lending and demand following finance", *Economic Notes*, Vol. 23, No. 2, pp. 308-316
- Kim, Ki-ho (2003) "Dollar exchange rate and stock price: evidence from multivariate cointegration and error correction model", *Review of Financial Economics*, Vol. 12, pp. 301-313
- MacDonald, R., Kearney, C. (1987), "On the specification of Granger-causality tests using the cointegration methodology", *Economics Letters*, Vol. 25, pp. 149-153
- Miller, K., Reuer, J. (1998), "Firm strategy and economic exposure to foreign exchange rate movements" *Journal of International Business Studies*, 29(3), 493-514
- Miller, S.M., Russek, F.S. (1990), "Co-integration and error correction models: the temporal causality between government taxes and spending", *Southern Economic Journal*, Vol. 57, No. 1, pp. 221-229
- Murinde, V., Poshakwale, S. (2004) "Exchange Rate and Stock Price Interactions in European Emerging Financial Markets Before and After the Euro", *Working Paper Birmingham Business School, University of Birmingham*
- Phylaktis, Kate, Ravazzolo, Fabiola (2005), "Stock prices and exchange rate dynamics", *Journal of International Money and Finance*, Vol. 24, p. 1031-1053
- Shapiro, A.C. (2002), *Multinational Financial Management*, Sixth Edition, Prentice Hall, Upper Saddle River, New Jersey

# THE IMPROVEMENT OF ECONOMIC BUSINESS MANAGEMENT – COMPETITIVENESS GROWTH FACTOR

FLORENȚA CÎRCEAG\*

## Abstract

By 2000 two things have become clear. First, the roots of international competitiveness lie in the microeconomic fundamentals of an economy. Macro-economic factors play a role in creating the environment for competitiveness but are not sufficient to enhance prosperity. Second, international competitiveness results from firm level choices that produce distinctiveness, not from replicating the choices of other firms, regions or nations. Now more than ever we live in a world that moves at a bewildering speed. Innovation is an important topic in the 21st century. Innovation management has become a compulsory path to sustained enterprise growth. In today's society, intellectual capital has replaced the more traditional meaning of the capital needed for success in business or in life. Knowledge management is now recognized as the management of the 21<sup>st</sup> century, therefore understanding knowledge management processes and factors leading to its success or failure is an important key to help managers identify and understand what is required to make knowledge management work.

**Key words:** competitiveness, innovation, knowledge management

**JEL classification codes:** M29

---

\* Assistant Professor, Ph.D. student; “Constantin Brâncoveanu” University of Pitești, The Faculty of Management Marketing in Economic Affairs, Râmnicu Vâlcea; e-mail: florenta\_vl@yahoo.com

Despite the fact that the interest in and concern with human activities' scientific management and at the same time aiming at providing their rational character have been present since long in the past, management as a science became clear quite recently, in the 19<sup>th</sup> century and developed and improved in the 20<sup>th</sup> century by world-wide specialists' efforts. One can certainly state that management is not a new notion. Napoleon used to practice management when dealing with his armies. Old Egyptians applied management when building pyramids. The gardeners that built the famous Babilon Suspended Gardens did not dig or seed at random, as they thought it was good. They had a plan<sup>†</sup>.

The term "management" is taken from the English language, yet its source is the Latin word "*manus*" which means "hand" and involves handling, the concept having become famous in social-economic sciences to the same extent that the practice of organizations' scientific leadership has become known in social life. One can assume that the occurrence of the term "management" was mainly in US schools, the term being taken in many European languages as such. The emergence of management as a science of leading is historically connected to a set of phenomena, namely<sup>‡</sup>:

- the partial separation of capital administration from its property and, in this context, the increase in specialists' role in managing economic-social activities;
- production concentration and centralization;
- technical-scientific progress that is rapidly taking place;
- the expansion of production specialization and cooperation both at national and international level.

Management has emerged, developed and improved especially in the economic field, but it has gradually imposed itself in other fields of activity, too, such as: politics, administration, culture, education, due to the fact that an economy's performance level and size are significantly influenced by leadership quality. The concept of "management" is seen both as a practical activity with direct reference to an entity's leadership and as a science of leading for conveying the theory of that field. There are several definitions in specialized literature, of which:

- ⇒ management is the function by means of which things can be accomplished by others<sup>§</sup>;
- ⇒ management is the set of means by which goals are reached by organizations<sup>\*\*</sup>;
- ⇒ management is the conscious process by which a man's or a group's actions are coordinated for achieving organizational goals<sup>††</sup>;
- ⇒ management is the process that pursues the accomplishment of organizational objectives by efficiently coordinating the supply, allocation and use of organizational human

---

<sup>†</sup>Crainer Stuart – "75 of the Best and 21 of the Worst Managerial Decisions Ever Made", Teora, Bucharest, 2002

<sup>‡</sup> Puiu Al. – "Management. Comparative Analyses and Studies", Second Edition, Independența Economică, Pitești, 2004, p. 15

<sup>§</sup> Koontz H., O'Donnell C. – "Principles of Management", Mc. Graw-Hill Book Company, New York, 1968, p.5

<sup>\*\*</sup> Beckett J. – "Management Dynamics. The New Synthesis", Mc. Graw-Hill Book Company, New York, 1971, p.8

<sup>††</sup> Duncan W. J. – "Management: Progressive Responsibility in Administration", Random House Business Division, New York Toronto, 1983, p. 7

and physical resources and maintaining the organization in a dynamic balance with its environment<sup>††</sup>;

⇒ management means work with and by other people with a view to meeting organizational goals efficiently, using limited resources in the context of changing environment<sup>§§</sup>;

⇒ management is the process to meet organizational goals with and by people as well as other organizational resources<sup>\*\*\*</sup>;

⇒ according to Larousse French encyclopaedia, management is the science of an enterprise's leading techniques;

⇒ as a science, management means studying the leading process with a view to systemizing and generalizing certain concepts, laws, principles, rules, setting certain management systems, methods and techniques in order that they lead to increasing the activities' efficiency with certain objectives<sup>†††</sup>;

⇒ the purpose of management as a science is to explain management nature and traits as a process, practical activity, with a view to drafting a structured knowledge set on that activity, in order to train managers and orient their activity<sup>†††</sup>.

By comparing the above definitions, one can assert that there is a wide acceptance of the fact that management has three main characteristics, namely:

- it represents a process or a series of ongoing or interrelated activities;
- it focuses on achieving organizational goals;
- goals are met by working with and by means of people.

As a conclusion, management is a set of activities developed with a view to ensuring the normal and efficient functionality of economic systems by one or several people, those activities rendering science. Management emerges as a "bordering" economic science that uses methods and techniques typical of other sciences and adjusts them to its own character.

The world economy has entered an era of total competition. Competitiveness, the challenge of the third millennium, has become a central preoccupation of both advanced and developing countries in an increasingly open and integrated world economy. The OECD has defined competitiveness as "the degree of which a company can, under free and fair market conditions, produce goods and services which meet the test of international markets, while simultaneously maintaining and expanding the real incomes of its people over the long term". Competitiveness is a multidimensional concept. It can be looked at from three different levels: country, industry, and firm level. At the firm level, competitiveness is the ability to provide products and services more effectively and efficiently than relevant competitors. This means sustained success in international markets without protection or subsidies. Measures of competitiveness at the firm level include firm profitability and measures of cost and quality, the exports or foreign sales of the company divided by output, and regional or global market share. Performance in the

---

<sup>††</sup> Phatac A. V. – "International Dimensions of Management", Second Edition, PWS-Kent Publishing Company, Boston, 1989, p. 3

<sup>§§</sup> Kreitner R. – "Management", Fifth Edition, Houghton Mifflin Co, Boston, 1992

<sup>\*\*\*</sup> Certo S. – "Modern Management. Diversity, Quality, Ethics and Global Environment", Teora, Bucharest, 2002, p. 23

<sup>†††</sup> Burduș E., Căprărescu G. – "Principles of Organizational Management", Editura Economică, Bucharest, 1999, p. 16

<sup>†††</sup> Ursachi I. – "Management", ASE, București, 2001, p. 10

international marketplace provides a direct measure of the competitiveness of the firm. At the industry level, competitiveness is the ability of the nation's firms to achieve sustained success versus foreign competitors, without protection or subsidies. Measures of competitiveness at the industry level include the overall profitability of the nation's firms in the industrial sector, the trade balance in the industry, the balance of outbound and inbound foreign direct investment, and direct measures of cost and quality at industry level. At the national level, competitiveness means citizens' ability to achieve a high, and constantly rising, standard of living. In most countries, the standard of living is determined by productivity, which deploys national resources and the output of the economy per unit of labor and/or capital employed. A high and rising standard of living for all nationals can be sustained only by the continuous improvement of productivity, either through achieving higher productivity in existing businesses or through successful entry into higher productivity businesses.

The term competitiveness refers to the capacity of enterprises to adapt quickly to change, exploit their innovation potential and develop high-quality products. Enterprises are no doubt the main engines of a country's competitiveness. In an era of increasing globalization and trade and investment liberalization, economic business continues to be a key actor in the diffusion of managerial, technological, and financial resources which provide and foster positive economic, social and environmental benefits, wherever it operates. More importantly, successful and competitive economic businesses have learned that good management is good business.

In modern society whose dominant and irreversible trend is globalization, management is and will be a highly interesting and important field with the following main coordinates:

- *global, integrating vision to solve problems*, according to which solving managerial issues should be done in two ways, on one hand within the organization, among its constitutive subsystems, departments and activities, and on the other between an organization and its external environment where it develops its activities;

- *interdiscipline*, as management is a field that continually attracts new elements from other sciences, adjusting and using them according to the requirements of social-economic entities' leading activity;

- *provisional feature*, which means the need to set up and define further action directions, taking account of the changes that might occur in the external environment where an entity functions, and the main goals that must be met;

- *the growth of managerial dynamism* rendered by a significant increase in change occurrence mainly due to rapid technical and scientific progress;

- *enhancing the purpose character of managerial actions*, as all managerial fields must have a logical purpose, thus ensuring the achievement of organizational general objectives;

- *management universalness* which means there are several types of management : agricultural management, building management, banking management, financial management, insurance management and, very frequent lately, educational management, as there is a permanent transfer of managerial concepts, principles, techniques and instruments from the industrial field to all the other fields of life and human activities;

- *professionalizing the manager function* as at world level there are numerous schools, institutions, training and coaching centers for leading people, famous business schools where they train the managerial elite of the future.



All that is to be found in what P. Drucker calls « the new traits of management » that clearly define contemporary management : management generalness, as it is present in all fields of social-economic life; innovation development as an essential feature of modern management; management orientation to the ongoing increase in the productivity of intellectual and physical labour; management pursuit of the cultural, political and social traditions of every country, of countries' growth conditions.

In modern society, management is the main factor that helps increase the efficiency of developed activities, becoming a leading force of economic growth that mainly relies on the enterprising and innovation spirit, intellectual capital replacing the traditional meaning of the capital needed for life or business success.

The term “knowledge management” was first used publicly in late 80's. A few years later, after 1995, the sector of knowledge-based management recorded a major recovery, which is now recognized as 21<sup>st</sup>-century management, therefore knowing the factors and processes that lead to its success or failure is the key which helps managers identify what it takes to make it work. Society's fast and complex growth illustrates more than enough that technological, social or economic changes largely depend on both the quality of information and the ability to manage it correctly and efficiently. The idea that high efficiency and greater success may come from knowledge-based management, that it opens the way to performance and competition for organizations has made knowledge-based management a key-concept in the development of organizations, an essential strategic issue in their survival in modern society. In a society that depends on information, as well as on the numeric growth of organizations (as the result of increased communication and social relations complexity), knowledge seems to be the only power that guarantees social, economic and democratic progress that does not fade away in time. To many organizations, the orientation towards capturing and acquiring knowledge means the confirmation of certain functional maturity complying with the essence of the informational society they are related to. The need to manage knowledge seems to be a natural issue as a result of long discussions about the role and importance of the intellectual capital valuation process in post-capitalist society. In this context, knowledge-based management includes the identification and localization of intellectual values within an organization, the generation of new knowledge in order to emphasize competitive advantages, the entire access to corporate information, the dissemination of positive practices and the access to technologies that code and use information. *Knowledge* is generally defined as *the power to understand and perceive the essence of facts, the valuation of certainties and information* acquired in the form of experiments or teachings. In such organizations' functioning, the basis is rendered by the generically set processes, namely *innovation* (creating new knowledge), *learning* (acquiring new knowledge) and *partnership interactivity* regarding knowledge<sup>§§§</sup>. Being a relatively new management field, knowledge-based management is concerned with managing processes and resources, regarding not only production relations, but also the ratio between people and the purpose of their work oriented to the creation, dissemination and assessment of knowledge needed to achieve an organization's development strategies. Yet, many public organizations and companies have been relying on old-fashioned concepts and techniques. Knowledge-based management, as a subdiscipline of the new concept of “knowledge economics”, is a new management method that pursues changing the good points of an organization's personnel into a superior competitive strength as compared to other similar organizations. Focusing upon using the intellectual professional potential in

---

<sup>§§§</sup> Drucker P. – „The New Society of Organizations”, Harvard Business Review, 1992

activities that use individual and external knowledge, knowledge-based management gives value to organizations, makes them special, increases their individual value. Exceeding the mere collection and handling of data in order to get information, knowledge-based management process refers to the acquisition, creation, preservation and implementation or re-utilization of knowledge, its fundamental objective being the valuation of an organization's knowledge resources and ability in order to give it the opportunity to learn and adapt to its ever-changing environment\*\*\*\*.

Knowledge-based management pursues the exploitation of organizational members' intellectual resources with a view to meeting the organization's goals and objectives. In this respect, Lewis Platt, the former CEO of Hewlett Packard, stated that "in the torment of world economy, knowledge is the convertible currency of large enterprises", thinking that "only the companies that succeed in capturing, storing and implementing what their employees know will be successful". Knowledge-based management is nowadays a vast field meant to ensure that the right information should reach the people who need it in order to make good decisions, as intelligence and creation, innovating ideas and information flow rapidness represent a significant competitive advantage. Among the most popular practices of knowledge-based management are the following:

- setting up data bases made up of: positive practices, expertise managers, customers' profiles, market evolutions, organization processes, legislative changes, business histories etc.;
- knowledge mapping by information structuring and organization according to a certain rule/informative tree or specialized data bases;
- making up teams to gather new knowledge, a good one including as many reference disciplines as possible, information managers/librarians, informatics specialists, intranet specialists, documents and information lists managers, human resources specialists;
- the active management of knowledge process which involves gathering, classifying, storing and disseminating information ;
- developing « knowledge centers »<sup>††††</sup> that aim at disseminating and transmitting positive practices needed to increase the outcome of acquired information;
- installing collaborative technology : intranet or groupware in order to improve the rapid access to information, including the one by interpersonal communication ;
- assigning a person in charge of managing knowledge initiative. There is a popular practice of assigning such a responsible person within large organizations, called Chief Knowledge Officer<sup>††††</sup>, whereas in small companies such a person might be appointed from among the people holding positions in the Boards of Directors.

Knowledge-based management aims at: the improvement of decision making; the reintegration of corporate experience; the increase in innovations number; the transformation of information into knowledge; the acquisition of new knowledge. It supports organizations' efficiency growth for

---

\*\*\*\* Davenport Th., Prusak L. – „Working Knowledge; How Organizations Manage What They Kno”, Harvard Business School Press, Boston, 2000

†††† Resource centers represent, according to the definition used by the Model of Booz Allen & Hamilton, “a contact center for the collection, structuring and dissemination of information”, [www.trendmonitor.com](http://www.trendmonitor.com)

†††† Do You Need a CKO? Insight No.27, [www.skyrme.com](http://www.skyrme.com)

social and economic development up to the level where that factor becomes the essential element in producing added value and also the overall prosperity of world economy.

In modern society, under the impact of the continuously fast rate of scientific, technological, educational, cultural and last but not least economic and managerial changes, the three concepts – management - knowledge-based management – competitiveness – have acquired new meanings and have increasingly become one of the invisible forces that economic practices should take into account in order to achieve organizations' efficiency, development and upgrading, involving the economy in general, aiming at the material and spiritual progress of society.

Globalization and changes in the world economy over the last years have raised new challenges for firms, industries and countries. The popularity of the concept of competitiveness is clearly demonstrated by the fact that there is an increasing interest around the issue of competitiveness benchmarking at the country level as well as the policies through which governments can enhance national industrial competitiveness. Competitiveness has become a key term in economic theory, in the last decades. Management is perhaps the key variable among the many that influence enterprise competitiveness. It is management that is responsible for creating competitiveness through the ability to produce ever-higher quality at lower cost.

Globalization of the economy has radically altered the nature of competition-both domestic and international. Economic growth and international competitiveness are increasingly dependent on the generation and transfer of knowledge and technology. Knowledge management has become a source of sustainable competitiveness into the knowledge based society. In the landscape of modern business, companies are persistently striving to create mechanisms for differentiating themselves from their competitors within given markets. Firms must be able to deliver high quality goods and services on time and in the correct quantities – all at competitive prices. Developments in trade during the last decade have brought the concept of “international competitiveness” to the attention of policy makers and technical cooperation agencies. The notion of international competitiveness denotes the capacity of a country, region, economic sector, business enterprise or a single product to maintain its market position despite of the presence of other suppliers. European business needs to respond to the urgent challenge of raising productivity and generating more added-value in the context of increasing international competition. The international competitiveness of modern economies is linked increasingly to their ability to generate, adapt and use new knowledge. Science and technology are considered to be key factors contributing to achieving sustainable development, prosperity and economic growth. In the contemporary global economy, driven as it is by technological innovations, European Union identifies competitiveness with high levels and rapid growth of productivity, along with high levels of employment. The prosperity and viability of nations and firms now appear to be intricately linked to their ability to achieve and sustain international competitiveness.

Whether for a micro-enterprise, a small business or a medium or large enterprise, "management" has always been and always will be a key factor in ensuring its viability and competitiveness. Today's environment is dynamic and complex. The importance of advanced and new technologies in enhancing productivity, and in improving quality and competitiveness, is widely accepted. The pressure to manufacture high-quality products or provide high-quality services that meet the specifications and demands of consumers has led to a systemic approach to the management of technology. Many companies today rely on advanced technologies to achieve high precision, maintain tolerance, and provide high value-ended services and products.

## References

- Crainger Stuart – “75 of the Best and 21 of the Worst Managerial Decisions Ever Made”, Teora, Bucharest, 2002
- Puiu Al. – “Management. Comparative Analyses and Studies” , Second Edition, Independența Economică, Pitești, 2004, p. 15
- Koontz H., O’Donnell C. – “Principles of Management”, Mc. Graw-Hill Book Company, New York, 1968, p.5
- Beckett J. – “Management Dynamics. The New Synthesis”, Mc. Graw-Hill Book Company, New York, 1971, p.8
- Duncan W. J. – “Management: Progressive Responsibility in Administration”, Random House Business Division, New York Toronto, 1983, p. 7
- Phatac A. V. – “International Dimensions of Management”, Second Edition, PWS-Kent Publishing Company, Boston, 1989, p. 3
- Kreitner R. – “Management”, Fifth Edition, Houghton Mifflin Co, Boston, 1992
- Certo S. – “Modern Management. Diversity, Quality, Ethics and Global Environment”, Teora, Bucharest, 2002, p. 23
- Burduș E., Căprărescu G. – “Principles of Organizational Management”, Editura Economică, Bucharest, 1999, p. 16
- Ursachi I. – “Management”, ASE, București, 2001, p. 10
- Drucker P. – „The New Society of Organizations”, Harvard Business Review, 1992
- Davenport Th., Prusak L. – „Working Knowledge; How Organizations Manage What They Kno”, Harvard Business School Press, Boston, 2000
- Resource centers represent, according to the definition used by the Model of Booz Allen & Hamilton, “a contact center for the collection, structuring and dissemination of information”, [www.trendmonitor.com](http://www.trendmonitor.com)
- Do You Need a CKO? Insight No.27, [www.skyrme.com](http://www.skyrme.com)

# THE ROMANIAN RURAL ECONOMY – A RESOURCE OF GROWTH AND REGIONAL COOPERATION, OR A SOURCE OF CONFLICTS AND INSECURITY?

GHEORGHE SĂVOIU,<sup>1</sup>  
CAMELIA MANEA,<sup>2</sup>  
CONSTANTIN MANEA<sup>3</sup>

## Abstract

In an attempt to answer such a delicate question, we try to present the characteristics of Romanian rural economy, underlining its political, social, demographic, cultural, and even religious specificity. It is a thorough analysis of the diminution of the force and impact of the rural traditions, of the inflexion in the dynamics of rural overpopulation, of the reduction of the aversion in comparison with the urban, which confers a new identity to the Romanian countryside. The rural economy is also made up of the aggregation of the peasant's economic behaviour and attitudes. The new rural-urban relationships change the identity-perishability antinomy. We try to use statistical arguments and to establish some important axes of the new programmes and projects, apt to reveal through the urban-rural convergence and through the downgrading of the discrepancies between the two kinds of environment.

**Key words:** rural economy, rural-urban convergence and discrepancies, statistical indices and arguments.

**JEL classification code:** R13.

---

<sup>1</sup> Senior Lecturer, PhD, University of Pitești, Romania, e-mail gsavoiu@yahoo.com.

<sup>2</sup> Senior Lecturer, PhD, University of Pitești, Romania, e-mail camelia\_manea2005@yahoo.co.uk.

<sup>3</sup> Senior Lecturer, PhD, University of Pitești, Romania, e-mail camelia\_manea2005@yahoo.co.uk.

## I. Introduction

The Romanian rural community, whose relative weight was prevalent before 1986, was structured around the axis of the village as a phenomenon of special economic and social complexity, defined by its own demography, by the traditional precincts of the village, as the passive geographic area where the peasant dwellings were set, and the farming land, as the active geographic area where the villagers' working places were spread. Hence, saying that a significant part of an economy like that of Romania is rural or traditional, or that the individual who runs a rural husbandry, and not a business in the economic sense proper, i.e. the farmer / villager, is its principal element, does not automatically explain why this traditional *rurality* still persists, and which is the distinctive mark of the villager who allowed it to be so longevous. The main studies conducted on rural economy are focused on three directions. The first – specifically economic – direction belongs to Virgil Madgearu, who expounded it in his 1940 book *Evoluția economiei românești după războiul mondial (The Evolution of the Romanian Economy After the World War)*. The second, a predominantly statistical one, is that adopted by Nicolae Georgescu-Roegen, which was presented in *The Encyclopaedia of Romania*, volume III, entitled *The National Economy*, published in 1940; subsequently, its orientation was biologically and entropically derived, as presented in his 1960 *Teoria economică și studiul economiei agrare (The Economic Theory and the Study of Agrarian Economy)*. The third direction is traced culturally, ethically and economically by Mircea Vulcănescu in his work *Prolegomene sociologice la satul românesc (Sociological Prolegomena to the Romanian Village)*, republished in 1997; it was rounded off from a demographical perspective by Anton Golopenția, through his *Complete Works*, republished in 2001, and from a sociological perspective by the prominent members of the sociological school, through their works and papers issued as a result of the monographic campaigns, in *the Journal of Romanian Sociology*, between 1937 and 1943.

Twelve characteristic features of the Romanian rural communities in the 20<sup>th</sup> century can be revealed, in a synthetic sketch:

1. The economic relationships based on constraint; the social relationships of dependence in the production system of the Romanian rural husbandry were relatively limited.
2. As the incentive provided by the exchange having as an object the products was comparatively absent, a natural tendency was noted to limit the production of goods to those meant for self-sufficient-consumption. It can be said that, at best, most of the production was used either to the producers' benefit, or to pay back their debts, as it was intended for neither exchange nor gain.
3. Although the control exerted on the production means was decentralized, the peasants remained the rural cultivators whose surpluses were transferred to a group of elderly people, initiators or descendants of the village or the main precincts of the village, a group who used those surpluses for themselves, but also to redistribute them towards those who were unable to produce, but had to get food and sustain themselves, and the transfer took place in exchange for various services. That group generated the funds destined to old traditions (viz. the series of ceremonial rituals), which underlined the economic, religious and cultural solidarity of Romanian rural community.
4. Still the Romanian peasant was a farmer / land cultivator as well as an animal breeder holding a long-term relationship with the urban area. There was no urban milieu without a rural milieu, and neither will their be in future, unless the urban succeeds in taking over the function of land cultivator and of breeder of stock through the agency of the modern agricultural farm, based on relationships determined by the equilibrium between demand and supply, with ensuing profit, or

on the existence of state subsidies, in those cases where this is imposed by the intervention of the state. The Romanian peasant was also compelled to maintain a supplementary relationship of equivalence between his own demand and the requirements of the urban milieu, thus being under inherent pressure meant to preserve the right balance with respect to his limited resources.

5. The Romanian rural economy centred round the family, the kinship relations, and its whole structure and organization was determined by the size and the coordination between the consumption needs and the number of the hands (i.e. the labour-worthy members). This is what can account for the importance of rural overpopulation, which used to connect the density of the village population with its agricultural land area during the pre-war and inter-war periods. The symptoms characteristic of agrarian overpopulated territories were: *“the fragmentation of the farming land, the high prices the plots of land were sold or leased for, emigration, the spreading out of the connected agricultural occupations, low salaries, low agricultural income reports, receding commons-land, pasture, and individual plot areas, diminution of the livestock, and decrease in gross incomes”* (Virgil Madgearu, 1940, p. 25).

6. Out of the typology of the eco-types as systems of energy transfers from the natural environment to the human milieu, one can distinguish the paleo-technical one, marked by the use of human and animal labour force, and the neo-technical one, based on the energy supplied by fossil fuels and technology. The eco-types of rural economy represented ecologic adaptations by the village inhabitants, materialized in a number of transformations of the products, and a set of means intended to attract the inorganic sources of energy into the productive process. In the Romanian paleo-technical rural ecotype, both the farmer / cultivator, and the non-cultivator lived together being sustained by the same crops. The relative degree of using a certain plot of land through time generated a whole series of subclasses of paleo-technical eco-types [1], whose fundamental distinctness is given by the area of land used, the duration of vegetation specific to the stated tilled plant, etc. Out of the five types of village paleo-technical eco-types, only three held a major significance in Romania's rural economy, all over its historical and traditional cultural evolution: the system of burning vegetation (also called, in Romanian “pârjol, arșiță, jariște”), short-term fallowing / upturning of the land, or the peasant system of lay land (followed by fertile crops when on fallow land, and less fertile ones on ploughed and seeded fallow land, and then by abandon in the after-cultivation by seeded fallow land, and the self-sown plant stages), and the hydraulic system (Stahl H.H. and Stahl H.P., 1968, p. 20-26). These pure ecological eco-types, turned to account in the peasant husbandry, allowed the villagers to preserve high quality soils until the advent of forced chemical fertilization and mechanization of agricultural crops in rural cooperatives. The eco-type centred on the cooperative hydraulic system was impossible to continue as a result of the destruction of the irrigation installations (a consequence hard to imagine of the restoration of private property against the background of the deteriorated property instincts of an absenteeist cooperative type). On a broader European plane, the Romanian rural eco-type combined elements of the Mediterranean eco-type with elements of the trans-Alpine or continental one. The neo-technical eco-types, resulting from the second agricultural revolution that took place at the end of the 18<sup>th</sup> century appeared in Romania's rural economy as late as the 20<sup>th</sup> century, being maintained on restricted areas, and aimed at tilling arable land all through the year, systematic multiplication of plants and animals, introducing new crops, coming from other regions of the world, and the growing tendency of regional specialization of certain crops (e.g. specialized horticulture, viticulture and pomiculture), introducing new implements, such as the iron plough drawn by two horses, the threshing machine, the harvesting machine, furrowing machines, introducing steam engines, and a new

kind of agricultural management including the optimal dimensioning and dividing properties, which transformed agriculture into an economic enterprise pursuing maximization of production. The predominant neo-technical eco-type gradually becomes the mixed agriculture type, where both plants and animals are grown (and raised, respectively) for commercial ends.

7. “Although the form of property is relevant for the manner in which a peasant ecosystem is organized, serving as a model for the social relationships, what is decisive in order to prefigure the profile of a system of rural economy is the way the holders of power use that model” (Eric Wolf, 1970, p. 57). Three types of property have affected the peasantry: the patrimonial property, where the control over the inhabitants of that land is held by the owners of the land as such, the acquired property, where the land cannot be inherited, but is guaranteed for the authorities, who collect the taxes from the peasantry (Max Weber, 1947, pp. 378-381), and commercial, where the land is considered the private property of the land-holder, an entity which can be sold or bought in order to get a profit. Collecting rural taxes was the usual form of acquired property in the Romanian rural economy of the past century, and it dominated the inter-war period, jointly with the commercial property. After the process of co-operativization, i.e. from 1962 till 1989, the new type of property can be defined as administrative property, borrowing some characteristics from the acquired property, with the state holding the supremacy over the land, and the produce obtained being taxed by the state by means of a hierarchy of officials, while generating a rapid development of the state-run farms, which are led by a group of technicians trained by the state, and leaving little room for the private farms. Cereals are cultivated collectively, while each worker also possesses a small private plot, where they till their subsistence crop or the perishable produce that can be sold on the local market. The economic reality showed that, at the same time, the private lots allotted or not taken over from the cultivators proved more productive than the collective farms called *state-run agricultural farms*.

8. The Romanian rural husbandry joined together several family nuclei, and implicitly several generations. The educational aspects and the common life of the different generations were permanently favoured. An extended husbandry centred on a numerous family nucleus did not automatically generate well-being. The extended husbandry characterized the well-to-do villagers, those belonging to the rural middle classes, who owned land. The conclusion is that the accumulation of labour in a husbandry was an immediate consequence of the peasant husbandry's economic well-being. The head of the household / husbandry had to relatively persist in time, as his replacement by one of the members of the younger generations was regulated by strict customary laws / rules, which controlled the transfer of the resources and of their administration, from the elder to the younger individual. In the Romanian rural economy, for a long period of time co-existed the transfer of the resources towards a single inheritor, or the *indivisible heritage* (preponderantly towards the first-born sibling, and more recently to the last born sibling, who undertook the obligation of looking after their parents), with the transfer involving more than one inheritors, or the *divisible heritage* (which was dominant to the profit of maintaining the unity of the husbandry). The rights ensured only to the male individuals represented the most common situation, as compared with that of the general inheritance, where the daughters received compensation in the form of a dowry.

9. In the Romanian monographic research, the characterization of the economy, and especially of the village structure, identifies two fundamental types: the structural-economic type, and the homogeneous-unitary type. Both typologies are however the expression of a closed economy, of a rural type, characterized by the poor use of currency in the exchange relationships. “If we



understand by the economy the set of the implements used by a group to achieve their aims, village life is much more an-economic than that in towns and cities. The ethic prices are indissolubly linked to the economic ones... Hence, if a commodity is cheaper on the town market, the individual who does not make it at home, but buys it passes for an “unthrifty” man, and is railed at by his fellow-villagers.” (Mircea Vulcănescu, 1997, p. 186).

10. In the studies of ethic and rural economic typology, the dependence of the rural community was analyzed by means of the village’s economic balance, which delimited, through the balance surplus, an autarkic or closed village from a village defined by commercial exchanges that were concluded, with a deficit or a surplus, with other rural regions or urban activities.

**An illustration of the increased dependency of the village on the market**

Table no. 1

No	Category	Village Import	VillageExport	
I.	Money	+ n <sub>1</sub>		Increased dependency means: $\Delta = \text{village import} - \text{village export} > 0$ $\Delta = (n_1 + n_2 + n_3) - (n_4 + n_5 + n_6) > 0$ (deficit in the external relations in the village analyzed)
	Products			
II.	-maize	+ n <sub>2</sub>	+ n <sub>4</sub>	
	-fruit and vegetables		+ n <sub>5</sub>	
	-other products		+ n <sub>6</sub>	
III.	Services	+ n <sub>3</sub>		

Source: Mircea Vulcănescu, *Prolegomene sociologice la satul românesc*, Ed. Eminescu, București, 1997, p.108

The questions asked by the economists and the statisticians of the Romanian monographic school identified quite numerous paradoxes of the rural economy, be it autarkic or isolated. “The traditional character of the customs of an irrational nature bring forth a normal question, ‘Does the law of the minimal effort still preside over the activity of a closed economy?’, ‘Does the need of maximal production still exist? What for – just taxes and debts?’” (Mircea Vulcănescu, 1997, p. 101-109).

11. If Virgil Madgearu concentrated on rural demographic pressure, on the correlations between the density and the farming land, or rural living standards, natural growth and emigration, rural density and structure according to the residential environments, emitting a number of predictions and estimations with a historical character, which in today’s context are superannuated, the sociological school had already developed and detailed the demographic analysis of the rural economy starting from the prevalent principle of the multi-causality of a statistical type, as can be seen in the example presented in the following table:

Table no. 2

	Village	Plasa / Sub-district	Județ / County / District	Historical region	Romania
Natality / Birth rate					
Mortality / Death rate					
<i>The maximal demographic level</i> defines the limit of the population that can find favourable life conditions within the economic situation of the village					
Causal demographic analyses					
Emigration	Abortion	Lack of land	Education	Traditions of occupation	

Source: The monographic model of the campaign carried out in the village of Șanț, in the Năsăud county, in 1935

12. Maybe the most realistic economic contribution with respect to the rural economy belongs to Nicolae Georgescu-Roegen. Virtually dismantling the theory of rural overpopulation in Romania, finding that agrarian economy still remains a reality without a theory, identifying no fundamental taxonomy of the villages centred around a certain evolutionary function-force, but on purely topographical criteria (villages situated in the hilly, plain, or mountain regions), around the predominance a typical crop or agricultural activities (e.g. cereal-growing, fruit-growing, vegetable-growing, viticultural, stock-breeding villages) and the location of the village inner precincts (in a compact or dispersed manner), studying and detailing the anatomy of the village, indivisible through blood relationships, village situation and activities, and starting from the specific geographic conditions, he remarked that *“agriculture will long represent a primordial economic activity for some communities, which will not be able to develop along the guideline specific to the industrialized nations”* (Nicolae Georgescu-Roegen, 1976, p. 214).

The Romanian village remains dominated by the flows of property, by the repartition of the usufruct, and not by the principles of marginal productivity, relatively inoperative in the last century, but which can represent major landmarks of the new agricultural policies in a Romania that has completely outgrown the sphere of agrarian overpopulation.

Pointing out to the complexity of the rural economy, in addition to the lack of an economic theory and a set of data with an acceptable degree of coverage, the sociological school noticed, through the voice of its most remarkable researchers, *“There no such thing as THE Romanian village, there only are Romanian villages”* (Henri Stahl, 1946, p. 40). Hence then the obsessively informational appetite of the monographic school in connection with ensuring statistical, economic, cultural, religious, etc. data, i.e. the succinct presentation – so necessary – of this component of the contemporary Romanian agrarian economy, of the rural residential milieu, in comparison to the urban one.

## **II. Demographic, economic and political realities of the contemporary Romanian rural economy**

The significant rural dimension of the national economy constitutes an economic and social reality with important consequences, to be continued in the period that will mark Romania’s actual integration into the European Union. Though there are copious arguments at a

demographic, economic and political level, only as few as twelve aspects have been selected and presented below, which synthetically reflect both the specificity, the weight and the main disparities between the rural and the urban residential milieu / environment.

I. The forced cycle of urbanization, to be noticed between 1948 and 1992, was followed by inertial recoil of *rurality*, as the population of this residential milieu, which saw a mostly descending dynamics after 1930, developed upwards during the transition period, in an abnormal loop, slowly consumed after approx. 15 years:

### Population according to the last 7 censuses, and on January 1<sup>st</sup> 2007, by residential milieus

Table no. 3

Census	Total population	No. of inhabitants, out of which in:		Weight of residential milieu:	
		Urban	Rural	Urban	Rural
29 December 1930	14280729	3051253	11229476	21.4	78.6
25 January 1948	15872624	3713139	12159485	23.4	76.6
21 February 1956	17489450	5474264	12015186	31.3	68.7
15 March 1966	19103163	7305714	11797449	38.2	61.8
5 January 1977	21559910	9395729	12164181	43.6	56.4
7 January 1992	22810035	12391819	10418216	54.3	45.7
18 March 2002	21680974	11435080	10245894	52.7	47.3
1 January 2007*	21565000	11915000	9650000	55.25	44.75

Source: www. insse.ro \* In keeping with the data presented during the INS conference, on September 20, 2007.

II. The rural dominant component of the localities has been stabilized, and it belongs to the interval between 2,000 and 5,000 people, immediately below the modal level of the urban localities, situated between 5,000 and 20,000 inhabitants, although there is no possibility of comparing their infrastructure and specific services, from any standpoint.

III. With a sharp increase in the ageing rate of the population, synthesized in the weight of the respective section, which is greater by 10% in the 65, and over 65 years age-groups, with a life expectancy virtually two years lower, and a mortality rate, both general and infantile, higher by nearly 50%, with an illiterate population 3.3 more numerous than that in the urban milieu – a category that holds a weight of nearly 4.5 % out of the total population aged 10 and more, the rural population is still defined, in its majority, by the Romanian villager's traditional husbandry, and to a much smaller extent by the modern agricultural farm.

IV. With twice the ratio of activity and of occupation along the lower educational segment, the rural population experiences only one third of the ratio of urban unemployment, within the same segment of low educational level, in accordance with the date recorded in the AMIGO inquiry, in the first trimester of the year 2007.

## The ratio of activity, occupation and unemployment, in keeping with the AMIGO survey

Table no. 4

%

	Total	out of which, in keeping with the educational level:		
		Higher	Medium	Lower
<i>Ratio of activity</i>	61.7	87.8	68.3	41.6
- urban milieu	61.1	88.1	66.2	25.6
- rural milieu	62.6	84.5	72.1	51.4
<i>Ratio of occupation</i>	57.2	85.0	63.1	37.6
- urban milieu	56.2	85.4	60.7	20.7
- rural milieu	58.6	80.7	67.6	47.9
<i>Ratio of unemployment BIM*</i>	7.0	3.1	7.5	8.0
- urban milieu	8.1	3.0	8.3	18.3
- rural milieu	5.8	4.3	6.2	5.4

Source: www. insse.ro \* According to the data presented during the INS conference, on September 20, 2007.

V. The house specific to the rural milieu is situated, as a rule, singularly within a dwelling building, mostly erected over the interval between 1945 and 1970, and endowed with water supply installations and sewers in a low proportion, under 15%, with gas supply installations – under 10%, and central heating installations – nearly 2%.

VI. The general budget of the rural households strikes through the prevalent weight of the incomes in kind and resulting from agriculture, and also through the high amount of self-sufficient consumption, still lying around 1/3 of the total expenditure, as well as the low percentage of money spending, taxes and imposts.

## The Level and Structure of the Expenses of the Romanian Households, according to the ABF 2006 survey

Table no. 5

	Total spending lei (RON)	out of which, in %:			Consumption out of own resources (%)
		Money spending	out of which:		
			Consumption spending	Taxes and imposts	
Total	1305	83.0	62.5	13.5	17.0
Urban	1459	92.5	69.9	17.5	7.5
Rural	1104	66.8	49.8	6.6	33.2

Source: www. insse.ro

Approached typologically, the money income of the rural husbandry reflects a net salary level of only 72,4% of the national average as on the 1<sup>st</sup> July 2007 (viz. 753 lei / RON as compared to 1,040), and a pension level of 38,4% of the average state-administered social welfare pension at the end of the first semester of the same year (viz. 140 lei / RON as compared to 365).

VII. Starting from the hypothesis of the contribution of the rural residential milieu to the formation and the dynamics of the prices for food products (identified as rural export), and that of the urban milieu, especially within the range of the non-food products (identified as rural import), we can redefine a rural-to-urban price shears (PS), starting from the detailed PCIs (i.e. price consumer indices), as follows:

$$PS = (1 - IRSN) \times 100 = \frac{I_{\text{non-food goods}}^P - I_{\text{food goods}}^P}{I_{\text{non-food goods}}^P} \times 100 = (306347.26 - 223759.08) : 306347.26 = 0.27$$

(respectively 27%) over a 17 year period, starting from the PCI values in June 2007, as compared to October 1990, for food commodities (223,759.08%), and for non-food commodities (306,347.26%). A price shears of the rural husbandries actually reflects the village-dwellers' much bigger effort, resulting from the territory distribution of inflation, as their incomes, low as they are, additionally lose substance by approximately 27% more than those in the urban milieu, as a consequence of the much steeper increase in the price of the non-food goods. The tradition of the price shears, maintained in the national economy to the detriment of the rural milieu, is also recorded and assessed between 1929 and 1938, oscillating between a minimum of 23.35 and 36.2 % (Virgil Madgearu, 1940, republished in 1995, p. 61, and Nicolas Georgescu-Roegen, 1943, republished in 1997, p. 81).

VIII. The structure of the gross national product by categories of resources reveals an oscillating contribution of the aggregate of activities like agriculture, sylviculture, fishery and pisciculture, which abruptly augmented from 14.4% in 1989, to 21.8% in 1990, at the expense of a GNP which decreased by an average of 7% in the first two years, as well as an industry which has been continuously re-structured, losing 50% of its structural contribution, in favour of the field of the services. Since 1994, the dynamics and the rate of that contribution have been clearly and firmly descendant, as the aggregate of activities described above has been plummeting towards 11%. The agricultural activity, dramatically subject to cyclicality, has decreased, in point of specific weight in the make-up of the GNP, to 8,1%, and, over the first semester of the year 2007, to 3.4%, against the background of a drought which will surely diminish it further.

IX. The villager's economic behaviour has evolved from an involuntary inactivity imposed by the limited character of the soil resources and the farming equipment (Nicolas Georgescu-Roegen, 1960, p. 264) to adopting a strategy centred around working so as to stay poor in order to avoid the excesses of the urban fiscal system, the socialist agrarian policies aimed at proletarianization, and the random distribution the property of an absenteeist kind, typical of forced cooperativization campaigns, and, over the past 17 years or so, to a transition from the agrarian communism, with its imposed forms of collective and communitarian property, to the private land property. The tradition of rurality, re-born again and again, created the feeling that *the peasants form the most durable class* (Oswald Spengler, 1929, p.26), and *when the last peasant on earth disappears, the last human will disappear, too, and, with him, the human species* (Petre Țuțea, 1993, p.105). The topic was obsessively revisited during the 20<sup>th</sup> century, in economics, sociology and philosophy, as an assertion in support of authenticity [2] and traditionality, being expressed as early as the first post-2000 years, right in the middle of a new Romanian transition.

X. After the year 1990, once with the completion of the five electoral cycles, the split of the national economy into two distinct parts, defined by the residential criterion: an urban Romania, on the rise, with a strong liberal component, which expects from the state opportunities rather than support and assistance, and a conservative rural Romania, typically represented by people in

the 65 years-and-over age group, as well as people living under the poverty threshold, who need to be supported, not only to develop their husbandries, but mostly in order to survive. The elections to come will surely add another variable of political division, in accordance with the electorate's preference for an excessively presidential, or an excessively parliamentary Romania. Econometric modelling becomes almost impossible when the structure of rural economy is, as can be easily noticed, rapidly changing, which is an obvious thing when it comes to nations and countries in transition. The current state of agriculture is due to the countless changes in the agricultural politics. The political factors having a major negative influence are still acting on Romanian agriculture, continuing to generate the under-use of the existing production factors as well as poor complementarities. The turnouts in the 2004 parliament election, cumulated at hourly intervals offer significant differences between rural and urban (final information: 60.84 % urban, and only 54.41 % rural).

XI. The religious structure recorded by the 18 March 2002 census reflects a strong concentration within the class of the Orthodox denomination. The diversity of the denominational weights is a little higher than that recorded by the 7 January 1992 census, but much smaller if compared to the data of the 1930 census, although the information is not rigorously comparable. The rural environment includes 86.2 % Orthodox population, as compared to 87.2 % in the urban areas.

XII. After the year 1999, the totally irrational or aberrant economic behaviour generated a rural crime rate slightly diminished (cca. 15% less) as to the urban environment: the number of those convicted by definitive decisions of the court, as on the 1<sup>st</sup> January 2006, was 30,146 in the rural localities, as against 35,536 in urban areas, except for the category of the offences against the individual, where the number of the villagers convicted is double that of the town-inhabitants convicted.

### **III. Most Recent European Point of View for the Romanian Rural Economy**

The most recent survey on the structure of agricultural holdings in Romania was carried out in February and March 2006 on a sample basis, and the reference date of the farm structure survey for livestock, structural data and organic farming was 31 December 2005.

There are some distinguished signs of post transition Romanian rural economy[3], from european point of view (Benoist György and Marquer Pol, 2007, p. 1-7):

1. About 1.24 million agricultural Romanian holdings had an economic size of at least 1 ESU (European Size Unit).
2. A strange trend of concentration of the average area of holding (from 8.8 ha in 2003 to 8.4 ha in 31 december 2005).
3. The real Romanian holding is made of means less than one AWU (annual work units). Among 1.24 million agricultural Romanian holdings, 55% made use of less than one AWU, while only 9% made use of 2 or more AWUs;
4. The modern holding means only 1% in Romanian rural Economy (from 1.24 million agricultural holdings just 1% used 100 ha or more, and 74% used less than 5 ha agricultural area).

5. Nearby 69 % from Romanian holdings produce mainly for their own consumption (*subsistence farming*).
6. Romanian rural Economy in traditional point of view is so aged, full of women and alternative, that it will disappear in a short period of less than one generation (among the 1.24 million sole holders: 20% were women, 71% were aged 55 or more, and only 4% were younger than 35 years, 16% had another gainful activity as their major occupation).

Perhaps after 20 years, no more traditional rural economy will be found in this part of Europe. But who is able now to use these statistical arguments and to establish some important axes of the new programmes and projects, revealing through the Romanian rural -European agricultural economy and convergence and through the downgrading of the discrepancies between the two kinds of organizing farms and working the land?

#### IV. Conclusions and Final Remarks

A natural, fundamental conclusion can be inferred to the effect that the structural changes that are about to occur in the 2007-2027 period can trigger a series of processes of social alienation by certain segments of the population living in the rural areas, who suffer significant, far-reaching mutations as compared to the situation in the past century. The advent of comparatively high unemployment (if compared with the usual rate), and its rising evolution in the rural economy, determined by the general re-structuring, viz. the restriction of maintaining the inflation indices at acceptable levels, the price shears for the agricultural products coming from the rural areas in comparison with the prices of the industrial goods coming from the urban areas, the lack of resources destined to the degraded or non-existing rural infrastructure will even influence in a negative manner the *vulnerable* components of the traditional peasant society, will cause increasing outward migratory flows, and also an ascending criminal behaviour, expressed as both impact and indicators, migrating from the offences directed against the individual towards those directed against the patrimony. Though the identification and the attempts at evaluating and turning to account Romania's competitive advantages in the European Union confer to agriculture a priority position through the fields of ecological agriculture, centred around natural food produces, viticulture, as a resource for the wine industry, horticulture and nature pharmaceutical products, etc., the concrete preoccupations and programmes are insufficient within the rural space.

Yet the attraction exerted by the Romanian village seems not to have ceased. Villages continue to animate the younger generations, who are exploring, and trying to identify their cultural roots, which are probably located in plain or mountain villages, along river meadows or on hill slopes, in outspread groups of houses or in isolated homes, gathered together or spread like flocks of birds, or in groves. The Romanian rural economy still remains both a resource of economic development, or else of regional collaboration, and a source of conflicts and insecurity.

#### Notes

[1] The classic paleotechnical eco-types are: the systems of lasting turning-up / fallowing, or fallowing through burning (cleaning by fire, and then tilling by means of hoe), the systems sectorial turning-up / fallowing (the land under crop is divided into two or more sectors, which are cultivated for two or three years, and left to go into fallow

for another three or four), the systems of turning-up / fallowing over a short period of time, or of Eurasian cereal agriculture (the land, cultivated with the plough drawn by animals for one or two years is re-used after another year meant for regeneration), systems of permanent cultivation, or hydraulic systems (centred around building mechanisms supplying water), and systems of permanent cultivation of the favoured plots (which turns to account alternative plots, in combination with the sporadic utilization of the less productive plots).

[2] In view of which idea, the realism of Lucian Blaga's statements becomes all the more suggestive and revealing: *"The Romanian village, in spite of its poverty and all the shortcomings which came to drill into it through the grievous concourse of the centuries, is to an exceptional extent worth of the epithet of genuineness... This should not be understood as a desire to maintain ourselves within the village achievements."*

[3] Some methodological information becomes obviously necessary. For each activity on a farm (for instance wheat, or cow), a *standard gross margin* (SGM) was estimated, based on the area (or the number of heads) and a regional coefficient. The sum of such margins in a farm is its economic size, expressed in *European Size Units* (ESU). 1 ESU is equal to 1200 euros. Each farm is classified in the community typology by its economic size and its type of farming, depending on the share of each enterprise in its economic size. Depending on the level of aggregation, farms are grouped into 8 to 70 types. *Annual work unit* (AWU) is equivalent to a worker employed on a full time basis for one year. In Romania it is 1960 hours (245 working days of 8 working hours per day). *Livestock Unit* (LU) is equivalent to a dairy cow. The number of animals (number of heads) is converted into LU using a set of coefficients reflecting the feed requirements of the different animal categories. *Subsistence farming* refers here to all farms below 1 ESU economic size. Note that the number of farms cannot be compared between countries due to the differences in coverage of FSS.

## References:

- Benoist György, Marquer Pol - *Agriculture and fisheries - Statistics in focus*, EUROSTAT, 2007
- Bădescu, Ilie, Cucu-Oancea, Ozana, -*Dicționar de sociologie rurală*, Editura Mica Valahie, București, 2005
- Georgescu-Roegen, Nicolas, -*Teoria economică și studiul economiei agrare*, in the vol. *Energy and Economic Myths: Institutional and Analytical Economic Essays*, Pergamon Press Inc., New York, 1976
- Golopenția, Anton, -*Ultima carte*, Editura Enciclopedică, București, 2001
- Golopenția, Anton, -*Opere complete vol. I, II*, Editura Enciclopedică, București, 2001
- Gusti, Dimitrie (coord.), -*Enciclopedia României*, Monitorul Oficial și Imprimeriile Statului, Imprimeria Națională, București, 1940
- Gusti, Dimitrie, -*Sociologia națiunii și a războiului*, Editura Floarea albastră, București, 1995
- Gusti, Dimitrie, Herseni Traian, Stahl, Henri, -*Monografia. Teorie și metodă*, Editura Paideia, București, 1999
- Madgearu, Virgil, -*Evoluția economiei românești după războiul mondial*, Ediția I 1940, reeditată, Editura Științifică, București, 1995
- Max, Weber, -*The Theory of Social and Economic Organization*, New York: Oxford University Press, 1947
- Pricopie, Vasile -*Recunoașterea internațională a Școlii Gusti*, Editura Tritonic București, 2004
- Spengler, Oswald, -*The Decline of the West*, vol. II, New York Knopf, 1929
- Stahl, Henri, -*Sociologia satului devălmaș românesc*, Institutul de științe sociale al României, București, 1946
- Stahl, Henri, -*Tehnica monografiei sociologice*, Editura SNSPA, București, 2001
- Stahl, Henri și Stahl Paul - *Civilizația vechilor sate românești*, Editura Științifică, București, 1968



- Trebici V. (coord.) -*Mică enciclopedie de statistică*, Editura Științifică și Enciclopedică, București, 1985
- Țuța Petre, -*321 de vorbe memorabile*, Editura *Humanitas*, București, 1993
- Wolf, Eric, -*Țăranii*, Michigan University, 1970, reeditată la Ed.Tehnică, Chișinău, 1998
- Vulcănescu, Mircea -*Prolegomene sociologice la satul românesc*, Editura *Eminescu*, București, 1997
- Vulcănescu, Mircea -*Școala sociologică a lui Dimitrie Gusti*, Editura *Eminescu*, București, 1998
- \*\*\*-*Agricultural Statistics*, data 1995-2004, Luxemburg, Office for Official Publications of the U.E, 2006
- \*\*\*- *Caracteristicile principale ale exploatațiilor agricole – Date generale*, Ed. INS, București, 2006.
- \*\*\*- *Caracteristicile principale ale exploatațiilor agricole –Regiuni de dezvoltare și județe*, Ed.INS, București, 2006
- \*\*\* -*Din istoria statisticii românești. Culegere de articole*, Editura D.C.S., București, 1969
- \*\*\*- *National Methodological Report – FSS 2005 (available on request on NSI web: www.insse.ro)*
- \*\*\* -*Revista Sociologie românească*, an V, Editura Institutului de Științe Sociale al României, București, 1937-1942 și 1943, nr. 1-6
- \*\*\* -*Sociologie Românească*, vol III, nr. 1,Ed. *Polihrom*, București, 2005

# EUROPEAN CHALLENGES FOR ISLAMIC BANKS

AIOANEI SORINA<sup>1</sup>

## Abstract

The paper briefly review the growth in Islamic Finance, implications of the Islamic banking in Europe and challenges to be met, in terms of compatibility with local banking markets, product development and strict anti-money laundering rules. The paper analyses also the hawala remittance system and the negative association with the Islamic banks. This type of funds transfer is often related with illegal remittances, money laundering and financial crime. As acting as European banks, newly established in Europe Islamic banks, as new comers, will have to face the critics about their possible link with terrorism support and money laundering

**Keywords:** hawala, interest- free, money laundering

**JFL classification code:** G15 – International Financial Markets

---

<sup>1</sup> Aioanei Sorina is Financial Institutions Director in a German Bank in Romania, PhD Student at Academy for Economic Studies in Bucharest ,email:sorina\_aioanei@yahoo.com, tel: 0040722284853

## Introduction

Every religion, irrespective of time, has played an important or even a critical role in the development of the society and also in the economic activity. The understanding of religion is often distorted by the outsiders' eyes. This is the case of Islam and linked to it is also the understanding of Islamic Financial Services (IFS), which are more and more seen as a particular threat for the Western civilization. Islamic Financial Services came to the attention of the economists, investors and analysts, as the Islamic banks started to open in Europe, targeting Muslim and non-Muslim population.

Islamic banking, and generally Islamic Financial Services are a growing phenomenon, which came into existence to meet the needs of the devout Muslims around the world, who have the main wish to observe the Koran and Sunne.

More than 40 years ago the first Islamic bank Mit-Ghamr was established in Egypt and 15 years ago Iran and Pakistan opted for Islamic banking System. In the last decade, a large number of Islamic banks or Islamic financial institutions were emerged in many countries. As a result of the increased interest in this large transactions, many Western banks started open their branches or subsidiaries in Islamic countries. Following the experience gained in the previous years, there is no doubts that non-interest based financial transactions are viable and feasible, and more and more interesting for western investors.

There is a generally well accepted fact, that Islamic Financial Services Industry (IFSI) is the fastest growing component of the financial services industry, in terms of the availability of the new products and also in the geographical spread. Islamic banking clients are not limited only to Middle East areas, but they are spreading across Europe, Asia and the US.

Currently, the IFSI consists of the following types of institutions:

- a) Islamic banks ,including full-fledged Islamic banks, Islamic subsidiaries and “Islamic windows” of conventional banks
- b) Islamic insurance and reinsurance companies or *takaful* and *retakaful* operators
- c) Islamic capital markets
- d) Islamic non- bank financial institutions, including Islamic leasing, factoring, finance companies, Islamic microfinance companies, etc.
- e) Islamic financial infrastructure including settlements systems, regulators and supervisors, rating and external assessment institutions

At least 75 countries have institutions performing Islamic Financial Services on their territory. The world Muslim population is approximately 1.6 billion <sup>2</sup>and Islam is considered to be the fastest growing religion in the world. So, the very high-speed development of the Islamic Financial Services could be explained by the size of the market on the one hand and by the increasing wealth of the regions dominated by Islam, i.e. Middle East.

The current assets in Islamic Banking segment alone are estimated at over \$ 500 billion. The annual market capitalization of the stocks meeting the Dow Jones Islamic Market Index Criteria

---

<sup>2</sup> Information downloaded on 6<sup>th</sup> September 2007 from [www.islamicpopulation.com](http://www.islamicpopulation.com)

in Islamic countries is estimated at \$ 300 billion. Corporate and sovereign *Sukuk* bonds amounting to around \$18 billion<sup>3</sup> have been issued till present day. The growth and development is more spectacular taking into account that in the '90s the IFS were in a nascent stage of its formation.

This rapid growth shows the demand for Islamic financial products in the global financial markets and consequently the demand for such services increased.

The IFS offered previously for retail business, expanded to new areas like private equity, structured products, project finance or mutual funds. For some countries the share of Islamic banking assets in total banking assets is still at very low level, despite the very aggressive development, with a penetration level of 15 up to 22%. The five countries with the largest Muslim population in the world: Pakistan, Indonesia, Egypt, Bangladesh and Turkey are still at very low level of development of the Islamic financial industry. For some countries the ratios of the IFS are improved by the large international players like, Citibank, UBS, HSBC, Deutsche Bank or BNP which entered recently into these markets.

All have entered the sector within last 10 years and their move coincides with the rise in oil prices, as it happened 3 decades ago. Islamic Financial Institutions bloomed when the oil boom ensured them wealth.

Religious fervor and oil prices are on the rise again and now many western bank or companies are highly interested to do banking business in accordance with Shari'ah and to attract millions of potential clients.

On the other side there are Islamic banks opening branches or subsidiaries in Europe or US, and they are "forcing" the authorities to find some ways to integrate these services into the global financial system.

To the requests for the acceptance of these new types of financial institutions we shall add the more concerns for ethical investments of a large community in the world, which are similar to the Shari'ah concerns of the Islamic finance.

Many financial products were developed and meet the specifications of investments in ethical products or socially responsible services. The optimists consider this like a precursor of the shape and form of global finance in the coming decades. It is true that there are a lot of conventional banks, similar with the Islamic banks, which do not enter in business partnership with companies involved in activities like gambling, prostitution, alcoholic liquor, narcotics, etc. There is no international financial institution which will agree to grant loans to banks which will credit such a/m activities and ethical and socially responsible finance are becoming popular in the Western world (Wilson, 1997).

But, speaking at present about globalization and assimilation of the Islamic banks by the conventional ones, I consider being too early. As more and more we hear about Ethical finance in the western world, we should consider Islamic investments as a potential opportunity to the conventional financial services.

---

<sup>3</sup> Information downloaded on 1<sup>st</sup> October 2006, from [www.lmcbahrain.com](http://www.lmcbahrain.com)

When analyzing majority of the products, we notice common features for both types of systems and the final result is basically the same. The client receive a credit card in a conventional or Islamic mode, leasing or *ijara* is the final result, the same in case of *sukuks*. Like in the limited case of conventional banks, not extended to Islamic ones, the banking products are almost all “invented” already. It will harder be to develop a new product. But the difference is done by the marketing and targeted clients, as far as all products have the same basic features.

## **Islamic Finance, Shari’ah Principles and AML**

When speaking about Islamic banks, Islamic Fund, *Sukuk* (Bonds), *takaful* (Islamic insurance), the discussions seem to gravitate to one issue, namely the Shari’ah guidelines or Shari’ah principles.

However, the Islamic financial markets do not deal with Divine rules alone and the operational aspects of the Islamic markets can be considered.

Shari’ah principles are applied to all aspects of the Islamic life, including financial services, enabling individuals and companies to adhere to these principles in their investment activities. We can summarize the list with the main requests of Shari’ah:

- No interest (*riba*) will be charged or paid. Avoidance of interest has been abused by those who merely seek to be considered Islamic bankers. Many convert interest into capital gains and find a Koranic justification. The rules were tightened progressively as they have been in tax avoidance.
- Avoidance of risk (*gharar*), means that trading of risk or sale of something not yet obtained, must be avoided
- Trade related business only will be financed .There are western similar instruments, involving commercial papers and bankers’ acceptance, which also have to be trade related. We must mention here that many of the developing countries, having strict exchange control regimes, insist that all overseas financing or foreign exchange transactions to be trade- related.
- Part of the income must be given to charity (*zakat*)
- An ethical investment, meaning that investments in certain activities are not permitted (*halal*).These includes production of alcohol, tobacco, pork, gambling and weapons.
- The concept of profit sharing business is the base of each credit contract.
- The principles are religious and generally are concerned how the income is generated, wealth’s distribution in society or how the profit and loss are shared.

The Islamic principles of sharing risks and rewards, joint partnership in the wealth creation by lender and borrower, through substituting equity for debt, is a possible positive solution that promotes entrepreneurship and creativity. Usually this model is transformed into a partnership through risk sharing and sharing of the profit and loss.

It doesn't mean that investments with financial institutions are necessarily speculative. More than that, Islamic banks are structured to retain a different status between shareholders' capital and clients' deposits, in order to ensure correct profit sharing according to Islamic principles. Islamic investors are motivated in their choice of investments by almost the same criteria as their western counterparts. The search for acceptable investments is balanced by natural risk-aversion. In the same way, Islamic borrowers also have a reluctance to give away a share in the profits of their enterprise. The most Islamic banks take the form of one type mark-up or other, rather than profit sharing.

Investing according to Shari'ah principles requires trained scholars, with a good understanding of Islamic Law and very good knowledge of the financial markets.

Another requirement is standardization of the accounting and auditing principles. The Accounting and Auditing Organization for Islamic Financial Institution (AAOFI) has about 140 members from 30 countries and developed 68 standards, including 30 Shari'ah standards. However, as it is explained in the recent documents of Islamic Research and Training Institute<sup>4</sup>, there is still more to be settled, as far as Shari'ah is an interpretative law that has variance among countries and people. At present, there is no Islam-wide authority that says what is *haram*(prohibited) and what is *halal*(accepted) and like in the Western banking moving from one tax jurisdiction to another, the Islamic product developers can go from one scholar to another to get the approval of their product, as it is compliant to Shari'ah.

In addition to normal audits, Islamic banks have to conduct Shari'ah review of their transactions and to check the compliance. It is supposed they will see any funds used for prohibited activities. Unfortunately this beneficial feature was not yet widely disseminated and used as a tool for the prevention of the money laundering.

As the Islamic banks are engaged in partnerships with their clients, within the profit-loss sharing framework, they have to know their clients, their sources of funds and their business. Thus, the Islamic banks are in a better position to identify and prevent the suspicious transactions of their clients.

In the last few years were many articles, opinions, etc related to the *Hawala*. I would like to describe it with more details for a better understanding of the link of *hawala* with the anti money laundering guidelines and also with the Islamic banks, if any links with the last ones exist.

Hawala was originating in the Middle East and means in Arabic "transfer". We may say that hawala was practically the first banking system established by the Phoenicians and than used by the Jewish immigrants in Europe. Hundreds of years ago, merchants were forced to hide and to transfer their wealth in more secure regions and they started to establish a trust- based network. Many experts believe that *hawala* was established in the modern era by the immigrants, sending money from Europe or from Dubai and Bahrain in their countries in Asia and Africa. The system was also used to avoid bans on gold imports into South-East Asia. This system was developed and improved and now we can say *hawala* is an informal, parallel, illegal remittance system based on honor and performance among a large network of dealers, which are primarily located

---

<sup>4</sup> Ten-year Framework and Strategies ,Islamic Financial Services Industry Development, A Joint initiative of IRTI and ISDB, 2007, downloaded from [www.irti.org](http://www.irti.org) on July 2007

in Middle East, Asia and Africa. In many countries, like India, Sri Lanka, Philippines and Bangladesh, the system was eradicated.

When comparing a bank transfer with *hawala*, anybody from the Muslim users can say the system is trustful, timesaving and costless.

In this system, a client gives an amount of money to a dealer and also the details referring to the recipient. The *hawala* dealer contacts another dealer in the city and country, where recipient is located and gives deposit instructions for the funds. He also retains a small commission and promise to effect the payment at a later date.

There is no written document in the transaction, which is merely done based on honor than on documents. For most people, despite the existence of a multitude of banks, either conventional or Islamic, *hawala* is a convenient, fast, cheaper and safe remittance system.

Today, most of the *hawala* transactions are taking place in the rich Middle East countries, by sending money to the Asian countries, origin countries for most of the immigrants. The reason for domiciling most of the *hawala* transactions here is that there is a large population of expatriates workers and because especially Dubai is the large gold market for India and Pakistan.

Irrespective how efficient or trustful would be *hawala* put a shadow from the AML point of the credibility of the banks operating in these countries. Quite often we've read opinions (Ramachandran, R., 2007) related to the close link of the Islamic banks with *hawala*, which logically it does not make any sense as far as the banks and *hawala* are "competitors" on the transfer funds market.

There are of course operations, which can indicate the existence of a *hawala* transaction. This bank operation can be done not only using Islamic banks, but conventional banks for some certain transactions. In the paper<sup>5</sup> published by Interpol General Secretariat on January 2000, there are detailed explanations of the routes, mode and even registrations of the *hawala* operations.

After carefully analyzing all these procedures, I couldn't prove any link with the Islamic banks, except the case when the initial transfers to the first *hawala* dealer are routed through a bank, which we must say could be a conventional or an Islamic one. The first transfer should be identified as a money laundering operation as the amount is unusual for the previous activity on the account, if it is not a document based payment, if the account shows a significant deposit activity previous to the transfer, mainly in the form of cash or checks. All these indicators can appear in a conventional or Islamic account and there is no difference in the obligations of the compliance officers to report the suspect transaction.

So, anti- money laundering in the sense of the fight against any activity which refers to "cleaning" of the profits generated by illegal activities has to be regulated in any country.

Know your customer (KYC) is a term used for the customer identification process which helps banks or any financial institutions to identify and prevent suspicious transactions.

Banks are aware about AML and KYC policy and they implemented strict controls for money laundering.

---

<sup>5</sup> Jost, P, Sandhu, H.S., "The hawala alternative remittance and its role in money laundering", published by Interpol General Secretariat ,Lyon, 2000

As it results from the detailed analysis of the Islamic banking products, due to the specific requirements for considering “*halal*” transactions, we may say that Islamic banks should have more abilities to know their clients than conventional banks.

When Islamic banks start to establish in Europe, they have to know that they have to obey the AML rules, already established by the international banking community. As Michael Foot, Managing Director of the UK Financial Services Authority mentioned<sup>6</sup> “There will also need to be the usual guards against misuse of a bank for purposes of financial crime and terrorism. But I see no reason why the conditions they will need to be met for shari’ah compliance need to be more difficult than for a conventional bank the key task of “knowing your customer” which is at the heart of most good safeguards for banks against financial crime.”

### **European Challenges of the Islamic Financial Services**

Growing Muslim communities internationally has led to the request for more Islamic banking services. Much progress was made in UK for launching Islamic products from an UK authorized and established Islamic bank. This is expected to be followed by similar initiatives among 20 million Muslims in Europe, US and Canada. UK made important steps in making allowances such as abolishing the double stamp duty on Islamic mortgages. In Europe the main challenge will be to make the Islamic mode of financing widely accepted among a constituency which transcends Muslim communities. Still the main concern is the European countries like Germany or France is either not interested or even reluctant to agree with the establishment of the Islamic financial institutions despite the fact that as Khan (1986) noted, the appearance of interest-free based transactions are not an alien subject for western economies.

The global Islamic finance sector is growing year by year. Islamic banks are able to offer new and innovative products, but there are challenges to be met, especially when they have to compete in Europe with international sophisticated and experienced banks. Definitely, the Islamic banks had a fierce competition in their own countries, as many international banks open “Islamic windows “there, but the challenges they have to face are mostly the same in their origin countries or in Europe( I would say even more in Europe ,and I’ll explain later on):

- Shortage of experts in Islamic banking, I refer here to executive specialists not to scholars
- Tax regimes not meeting the needs of Islamic products
- Lack of uniform rules in credit analysis
- Lack of relevant of accounting and auditing standards for Islamic banks. Basel II and IFRS changes will act as catalysts to improve the quality and consistency of disclosure of the Islamic financial institutions.
- Enhancement of product development, according to the market needs, taking into account the offers of conventional banks. I insist on the fact that Muslim population in Europe, having at least a medium living standard level, applied already to conventional banking products. They opened accounts in European banks, because they needed it and they did

---

<sup>6</sup> Michael Foot, Managing Director of the UK FSA, Second International Islamic Finance Conference Dubai, Sept.2003,downloaded from [www.fsa.gov.uk](http://www.fsa.gov.uk) on 23<sup>rd</sup> July,2007



not wait for a potential establishment of an Islamic bank. We do not have to forget the 2 generations families living in Europe, who were using the conventional banking services for many years. It is quite difficult now, irrespective of their religiosity, to shift to another bank without comparing the cost, the quality and diversity of services of the two banks. Management of the Islamic banks in Europe and not only have to be more creative, developing product variations and enabling their banks to compete with their conventional peers.

- Improvement of corporate governance and risk management. Worth to be mentioned here that definitely Shari'ah board should be totally separated by the Risk Committee.
- Shortage of Shariah scholars. Shari'ah principles are set forth by qualified religious scholars. There are estimations of the existence of about 250 clerics, and they have to provide to all Islamic financial institutions support to product development according to Shari'ah rules. General practice states at a Shari'ah committee consists of three or more scholars, but in fact these scholars, due to their limited number serve more committees. Therefore, Shari'ah clerics need more trained scholars that combine an understanding of Islamic law, Islamic economics and global financial markets
- Strict Anti-Money Laundering rules, which have to be observed

In his paper<sup>7</sup>, Sayyd Tahir noted as a challenge innovation to create “financial instruments yielding stable income flows for orphans, widows, pensioners and other weaker segments of the society.” Like in other papers or articles, there are mixes among the challenges for the Islamic banking and those of Islamic religious institution. In my opinion there is clearly a need for separating the social life's requests from those of banking or, generally Islamic financial services. For the above mentioned issue, the Muslims and not particularly those dealing with the banking sector, have a specific instrument “zakat”, which is used and must be used by every religious Muslim. Including this issue on a list with possible challenges will complicate more the Islamic banking system, adding to it components which belong to social assistance activity and not banking.

## Conclusion

There is a certain need for designing the new financial architecture of Europe, which should promote the strong infrastructure for better global integration of both conventional and Islamic finance. Both types of institutions will have to work together with the supervision and regulatory bodies, national or European, for ensuring a free, fair and transparent market. Providing banking services in conformity with Shari'ah rules will enhance the accessibility of a significant part of population to financial services and should have positive implications for social justice and economic development.

Due to their specificity, Islamic banks need to invest more in their research for new products in order to ensure a proper financial risk management, resource mobilization at a competitive price and a proper balance sheet management through securitization.

---

<sup>7</sup> Sayyd Tahir is professor of Economics in Islamabad .His paper “Future of Islamic Banking” was prepared for the course on Islamic Banking in Tehran, on 2-6 March 2003

## References

Foot, M., Second International Islamic Finance Conference Dubai, Sept.2003, downloaded from [www.fsa.gov.uk](http://www.fsa.gov.uk) on 23<sup>rd</sup> July, 2007

Jost, P, Sandhu, H.S., "*The hawala alternative remittance and its role in money laundering*", Interpol General Secretariat, Lyon, 2000

Khan, M., "*Islamic Interest-Free Banking: A Theoretician Analysis*" IMF Staff papers No.33, pp 1-27, 1986

Ramachandran, R., "*The origins of AML*", [www.gtnews.com](http://www.gtnews.com), 23<sup>rd</sup> August 2007

Tahir, S., "*Future of Islamic Banking*", 2003, downloaded from [www.irti.org](http://www.irti.org) on June 2007

Wilson, R., "*Islamic Finance and Ethical Investment*", International Journal of Social Economics, Vol.24, pp 1325-1342, 1997

***DECISIONS ABOUT THE FUTURE OF THE EUROPEAN UNION: AN  
APPROACH FROM A ROMANIAN PERSPECTIVE***

**RAMONA DUMITRIU<sup>1</sup>  
RĂZVAN ȘTEFĂNESCU<sup>2</sup>**

**Abstract**

The European Union reached a turning point when it has not only to fructify the opportunities of the new market opened by globalization, but also to face significant threats such as the ageing population, the competition from the Asian producers and the dependence on the energetic resources placed in politically unstable regions. This situation implies decisions about the reforms of the political institutions, the future enlargements and the elaboration of a common external policy. The experience from the past proved that, in making such decisions, it has to be taken into consideration the public opinion, which sometimes is not favorable to the radical changes. The position of Romania, with its representation in the European institutions, will certainly influence the strategic decisions regarding the future of the E.U. In this paper we will analyze this position, using both information from the Government strategies and the results of our investigations regarding the way some aspects of the integration are perceived.

**Key words:** institutional reform, enlargement, foreign affairs

**JEL classification codes:** F 15

---

<sup>1</sup> Faculty of Economic Sciences, University "Dunărea de Jos" Galați, Romania

<sup>2</sup> Faculty of Economic Sciences, University "Dunărea de Jos" Galați, Romania

## **1. Introduction**

The evolutions from the last years made the present circumstances of the European Union (E.U.) development very different in comparison with the ones from the creation moment. After the recent enlargements the E.U. became to have 27 members, overstretching considerably its absorption capacity and creating some coordination difficulties. There are some significant threats that have to be faced. The ageing population and the high unemployment endanger the state social insurance system from some countries. The significant competition from the Asian producers threatens the European companies. Moreover, the dependence on the energetic resources from the politically unstable regions makes the European economies vulnerable against the evolutions from these areas. Besides these threats it is also present the opportunity of entering on new markets open in the last years in the context of globalization. As a consequence, the policies and institutions adjustment to the new conditions became necessary. Such an attempt is quite complex because of the clashes of opinions between the members of the E.U. regarding the changes that must be accomplished in certain fields, such as:

- the European institutions reform;
- the E.U. enlargement;
- the foreign policy.

The role that Romania will have in adopting solutions for these problems is quite difficult to anticipate. On one side, the adhesion of Romania is quite recent and it was accompanied by some safeguard clauses. On the other side, its population of 22, 3 millions (4, 51 % from the E.U. population) gives the right to a significant representation in the E.U. institutions. In order to anticipate the position of Romania in the decisions concerning the future of the E.U., the present authorities attitudes (resulted from the official documents) over the discussed problems could be taken into consideration. The public opinion perceptions regarding the decisions over the E.U. future that should be adopted are also important (Cojanu, Birsan, Muresan and Aristide, 2006, pages 7 – 10). These perceptions will be evaluated in this article on the base of an own investigation that was realized in the period March – May 2007, with the participation of 160 students from the “Dunarea de Jos” University – Galati. We considered the students being parts of a well educated and informed category that could offer signs about the Romania population attitudes. As methods of investigation we used the classical questionnaires and the focus group technique. Although the results of our investigation can not be generalized for the whole community of students from Romania, these could be useful in order to understand some public opinion perceptions.

## **2. The position of Romania in the decisions making about the future of Europe**

Decisions regarding the E.U. are settled by certain treaties. The European Council, that puts together the state or Government leaders of the E.U. members, establishes the general social, economic and political views. The legislative initiatives come mainly from the European Commission grouping, for now, commissioners from all the member states. Theoretically, a commissioner must do his duty independently, without receiving instructions from his

government. Presently, the Council of the European Union is the main legislative institution, that includes representatives (ministries or state secretaries) designed by the member states. According to the adopted European Treaties, the decisions must be approved by the Council of the European Union with simple qualified majority (each country having a number of votes correlated with its size) or with unanimity of votes. The European Parliament has also an important role in decision – making from E.U. as the control function of the European Commission. Each country from the E.U. has a number of places in the European Parliament correlated with its size.

Now, it must be obtained the unanimity of the Member States for the decisions with a significant impact on the future of E.U., being a very complex approach. In the situation of big clashes of opinions it may come to long negotiations, such it happened in the case of the Reform Treaty. This experience showed that opposition of one country could block for long time the decisions adoption, although the big contributors at the E.U. budget have a dominant position in the negotiation process in the end. For the moment, it is considered that Germany and France, countries with significant contributions to the E.U. budget and with a massive representation in the European decisional institutions, have an alliance that succeeds, generally, to impose its points of view.

A proposition concerning the future Reform Treaty stipulated that the basic decisions to be approved with qualified majority instead of unanimity. It is expected that such an evolution to strengthen the position of the present alliance between France and Germany.

The considerable population of Romania gives an important representation in the decisional institutions of E.U. that should be taken into account in the European construction. However, at least for the moment, it can not play a big role in this process. Romania adhered to the European Union only at 1<sup>st</sup> of January 2007 and it is yet conditioned by certain safeguard clauses. Moreover, its contribution to the E.U. budget is not significant.

An important aspect of adopting the strategic decisions for the E.U. consists in the degree a government must take into consideration the public opinion from its country. The mandate in the Council of the European Union for the vote regarding important decisions may be gained by a resolution of the Parliament or by referendum. On one side, it is easier to obtain a resolution of the Parliament but it may induce to the citizens the perceptions their opinions are ignored, amplifying the Euroscepticism. On the other side, the approval by a referendum is not sure for a government, this being proved by the failures of a Constitution for the E.U approval from France and Holland.

In the situation of Romania, the public opinion has, in general, a favorable attitude regarding the belonging to the E.U. This fact was confirmed by our investigation on 160 students who considered, in unanimity, that positive effects of the Romania adhesion to the E.U. exceed the negative ones. In order to evaluate the students' perceptions concerning the impact of the adhesion, they were asked to mention their first thought about the E.U. It resulted the greatest part perceive the E.U. with positive effects, such as the free mobility of the European citizens, the living standard increase or the access to the European funds (see table 1).

Table 1 - Students answers regarding their first thought about the E.U.

<b>Opinions</b>	<b>Number of answers</b>	<b>Weight</b>
Free mobility of the European citizens	74	46,3 %
The national identity lost	2	1,2 %
The living standard increase	59	36,9 %
Access to the European funds	20	12,5 %
No answer	5	3,1 %
<b>Total</b>	<b>160</b>	<b>100 %</b>

From the group interviews it came out a position of inferiority students allots to Romania in comparison with the other countries from the E.U. The explanation consists in the behind situation regarding some important aspects such as: justice, living standard, civilization degree or fight against corruption. When they were asked to mention the number of years Romania needed to reach, for these aspects, the level from the Western Europe, the answers of the students offered a quite pessimistic image. The majority evaluated at over twenty years the gap between Romania and the Western Europe (see table 2).

Table 2 – Students opinions regarding the number of years Romania needs to reach the level of the Western Europe for some social – political aspects

<b>Aspect</b>	<b>Number of answers</b>		
	<b>Under 10 years</b>	<b>Between 10 and 20 years</b>	<b>Over 20 years</b>
Justice	32	55	73
Living standard	16	48	96
Civilization degree	22	47	91
Fight against corruption	17	43	100

This perception of inferiority makes the students consider that, at least for now, it would not be desirable that Romania adopt a very strong position in the decisions over the future of the E.U., even if there could be harmed some of its interests. In any case, in their opinion, Romania should not threaten to block the institutional reform (the way Poland did) or the future enlargements.

### **3. Decisions regarding the institutional reform**

All the countries from the E.U. accepted the necessity of adapting the European institutions to the present stage of integration. However, there are some clashes of opinions over the ways these institutions efficacy could be increased. A disputed matter is represented by responsibilities distribution between the national authorities and the E.U. institutions. A concentration of the responsibilities at the level of the European institutions could lead to the economic policies efficacy increase, but this could be perceived by the public opinion as a national sovereignty decrease. In the conditions of the Euroscepticism increase from some countries this problem must be approached with a lot of cautiousness. Generally, the public opinion is more sensitive at the

changes forms than at the changes fund. From this reason, it is recommended that institutional reform proposals to be formulated in a manner that spares the susceptibilities.

Another important aspect of the institutional reform is the change of the unanimity condition into the qualified majority in order to adopt the major decisions for the future of the E.U. It is obvious that unanimity of the member states could make very difficult the E.U. management. However, for the small countries there is a fear that unanimity replacement with the qualified majority could signify their voices would not be heard in the European Union Council. In this context, the approval in the Parliaments from these states of giving up to the unanimity condition could be quite difficult.

In Romania the authorities support, at least by their declarations, the French – German alliance position towards the institutional reform. This may be considered as a precautious policy, adequate to the sort of vulnerable position Romania has in the present in the E.U. As it concerns the public opinion it must be considered the fact that a big part of it is quite little accustomed to the E.U. institutions role. In order to evaluate the opinions of some better informed categories, the 160 students were asked about the attributions transfer from the Romanian authorities to the European ones. It resulted the preferences are quite balanced distributed between the alternative of a significant transfer of decision power towards the European authorities and the one of maintaining the attributions at the national level (see table 3).

Table 3 – Opinions of students regarding the attributions transfer from the Romanian authorities to the European ones

<b>Opinions</b>	<b>Number of answers</b>	<b>Weight</b>
Favorable to the Romanian authorities attributions transfer	80	50 %
Unfavorable to the attributions transfer	77	48,1 %
No answer	3	1,9 %
<b>Total</b>	<b>160</b>	<b>100 %</b>

During the group interviews the students favorable to a significant transfer of the attributions to the European authorities justified their option by the lack of competence and the corruption of the Romanian authorities. The students who prefer the attribution maintenance at the national level explained they were afraid the European authorities could not understand the problems of Romania. Still, they mentioned they considered not indicated, in the present circumstances, the representatives of Romania to oppose frankly to the attributions transfer. As a conclusion, the results of our investigation seem to indicate the fact the institutional reform of the E.U. will not come up against a major opposition from the public opinion from Romania.

#### **4. Decisions regarding the enlargement**

A big number of countries (some of them from outside Europe) expressed their desire to become members of E.U. There are countries that could represent important markets for the E.U. producers. Moreover, many countries have a population with an age average quite reduced, that could counteract the population aging effects from the Western Europe. Nor there must not be neglected the geo-strategic positions of some potential candidates (Busek and Mikulitsch, 2005,

pages 161 – 166). However, the decision regarding the future enlargements is under some significant constraints.

The massive adhesions from the last years overstretched the E.U. absorption capacity and they contributed to the Euroscepticism increase. Many new members were countries with a low living standard in comparison with the average level of the E.U. and they needed consistent financing. Moreover, the flows of immigrants that followed the adhesion aroused partially the hostility of the public opinion from the Western European countries. The citizens from these countries are also sensitive to the cultural differences that separate them from the population of the potential candidates. Most of the E.U. old members are countries with a solid democratic tradition and they belong to the Western civilization with Catholic and Protestant majority (Huntington, 1998, pages 23 – 42). On the other hand, most of the countries that want to adhere have a quite recent democratic experience and they have an Orthodox or Muslim majority population. Especially the adhesion of a Muslim country, in the context of Islam terrorism worsening, could arouse the worry of the E.U. public opinion.

The potential candidates for the enlargement belong to three important geographic areas: the Balkans, the Eastern Europe and the Caucasus. In the Balkans the countries expressing their wish to adhere are: Albania, Bosnia – Herzegovina, Croatia, Macedonia, Montenegro, Serbia and Turkey. For Albania, Bosnia – Herzegovina, Montenegro and Serbia the democratization and the economic reform processes did not reach stages for taking into account the adhesion in the near future. Croatia, Macedonia and Turkey gained the status of candidate for the adhesion to the E.U. In the case of Croatia, a small country with a Catholic majority population and with a living standard that exceeds the one of some E.U. members, it would not be overstretched the capacity of absorption and it would not be amplified the Euroscepticism. The admission of Macedonia, a country where the Orthodox and Muslim religions prevail and the living standard is inferior to those from the E.U. members, could amplify the Euroscepticism. Moreover, there are some suspicions regarding the lack of control from the democratic institutions over the Army and its big population would qualify it for a massive representation in the European institutions.

From Eastern Europe, Moldova and Ukraine want to adhere to the E.U. Yet, their political and economical situation does not justify their hope to a fast adhesion. Besides that, the two countries have Orthodox majority population, so their accession could be regarded with hostility by some citizens from the Western Europe.

In the Caucasus area Armenia and Georgia expressed, for now, their intention to adhere. Both have Orthodox majority population, a low living standard, so their accession could favor the Euroscepticism. Anyway, their position next to rich in oil areas makes them attractive targets for the enlargements.

In the present circumstances, it is expected that the potential candidates not be admitted too soon in the E.U, with the exception of Croatia. However, the E.U. authorities must consider the fact a frank rejection or a too long delay could arouse the population hostility in these countries. From this reason it would be desirable as a remedy the intensification of the E.U. economic and political support for these states.

For the future enlargements there are also aimed countries that did not yet express clearly their intention of adhesion to E.U. The accession of some countries with a high living standard and that belong to the Western civilization (Norway, Island, Liechtenstein, Switzerland a.s.o.) would increase the economic and political force of the E.U. without escalating the Euroscepticism or



without overstressing the absorption capacity. Besides these countries, the admission of Kazakhstan or Azerbaijan could be a guarantee against some future energetic crises. For these countries some promotional policies could be elaborated in order to convince the population about the adhesion benefits.

In the case of Romania, the government joined the majority from E.U., considering welcome the graduate enlargements. For the public opinion from the country a sensitive matter is the situation of Moldova Republic. This could create in the future a certain pressure for the Romanian authorities to a massive support of this country accession in the European Union.

During our investigation the 160 students were asked if, in their opinion, the new members' accession in the E.U. would be favorable for Romania. More than half of them answered new enlargements would be good for Romania and 40 percent of them answered there would not be favorable (see table 4).

Table 4 – Opinions of the students regarding the effects of new enlargements for Romania

<b>Opinions</b>	<b>Number of answers</b>	<b>Weight</b>
New enlargements would be favorable for Romania	83	52 %
New enlargements would not be favorable for Romania	64	40 %
No answer	13	8 %
<b>Total</b>	<b>160</b>	<b>100 %</b>

The students who consider the new enlargements would be favorable for Romania explained their opinions by the advantages of new markets. They think it would be desirable in the near future countries from the West Balkans to adhere, this making easier the communications of Romania with the South and South – West of Europe. However, they do not think the Romanian government should act in order to rush any enlargement. All the students showed hostility towards the accession of Turkey in E.U., motivating this country is too far from the European culture. Most of the students consider that for the moment Moldova Republic is not ready to become a member of the E.U. The students considering that new enlargements would not be favorable for Romania declared the new members of E.U. would become some serious competitors for the foreign direct investments and for the European financing. However, the students consider it would not be well that Romania opposes frankly to the new accessions, because this position would damage the international relations of our country.

## **5. Decisions regarding the foreign affairs**

The transition to unitary foreign affairs policy of the E.U. members is a disputed matter. The requirements for a substantial clear policy of the members concerning the international problems came both from inside and from outside E.U. In order to reach this purpose, in the rejected European Constitution it was proposed the creation of the post called “Union Minister for Foreign Affairs”. Anyhow, it became obvious such a measure is unpopular in some countries, being perceived as harming the national sovereignty. From this reason, in the Reform Treaty it is used the name “High Representative of the Union for Foreign Affairs and Security Policy”. The

person established for this post could represent E.U. only in problems where there is an agreed policy between all member-states. This could mean that in the future it will be quite difficult for E.U. to elaborate a coherent foreign affairs policy. Now, the E.U. Member States have to face three important problems of foreign affairs policy: the relations with the U.S.A., the relations with Russia and the situation from the Middle East.

During the Cold War, the threat represented by Soviet Union forced the countries from the Western Europe to have a foreign affairs policy similar to the one of U.S.A. Most of these were members of NATO, where the first position of U.S.A. was undisputed. However, beginning with the '60s the relations from the East and the West defrost decreased continuously the Soviet threat, stimulating the differentiation of some Western countries (especially France) foreign affairs policies in relation with the U.S.A.

The fall of the Communist regimes from the Eastern Europe imposed a new approach of the relations with this area. It was rethought the role of NATO taking into consideration the new threats it had to face. Generally, the present members of E.U. supported U.S.A. in the conflicts from the Gulf, in the conflicts with Yugoslavia and Afghanistan. The latest war from Iraq led to major clashes of opinions in E.U. regarding the intervention of U.S.A. On one side the biggest part of the E.U. members supported U.S.A. politically and military, on the other hand the president Jacques Chirac and the chancellor Gerhard Schroeder disapproved the U.S.A. intervention. Their attitude, approved by the public opinion with increasing anti – American feelings, provoked a strong reaction from the U.S.A. officials. However, in the last years the elections from France and Germany brought the power to Nicolas Sarkozy and Angela Merkel. The two leaders seemed to be closer by the president Bush than their predecessors so that it is expected to be improved the relations of France and Germany with U.S.A.

Romania is considered by U.S.A. an allied in the conflict from Iraq and the declarations of the Romanian authorities indicate the interest for the privileged relations maintenance. From this reason, it is expected that Romania supports the cooperation between E.U. and U.S.A in the foreign affairs policy. However, from the group interviews with the students it resulted they were not too favorable to this attitude. Many of them are not pleased with what they perceive to be an American hegemony in the Euro-Atlantic affairs. Some of them explained that U.S.A. and E.U. (competitors from the economic point of view) will become, inherently, rivals in the foreign affairs policy. Quite a lot of students expressed their anti – American feelings that seem to be stimulated by the war from Yugoslavia and by the intervention in Iraq.

After the adhesion of Poland and of the Baltic States E.U. has now a common border with Russia. The relations with this country are dominated by the deliveries of oil and gases and by the attempts of Russia to maintain its spheres of influence. The Russian gas and the oil are sold in attractive conditions although some deliveries interruptions from the past aroused worry among the E.U. countries. There are fears regarding the Russia using the oil and gases deliveries as a mean of pressure on E.U. The attempts of Russia to maintain its spheres of influence are in contradiction with the intentions of some countries from these areas of adhesion to E.U. (Ciascai, 2006, pages 27 – 34). In the past the development of relations between Russia and E.U. was undermined by the situation of the Russian minority from the Baltic countries and by the Russian - Polish commercial dispute.

In the present, Romania imports big quantities of oil and gases from Russia. During our investigation most of the students mentioned the main obstacle for the Russian – Romanian

relations development is represented by the situation from Moldova Republic, where Russia wants to maintain its influence. This is also the main reason for the students not being very favorable to the political cooperation between E.U. and Russia.

The situation from the Middle East is a preoccupation for E.U., in the context of the implications it could have on the oil price and on the Islam terrorism. Until now E.U. participated, together with U.S.A. and Russia, to attempts of solving the crises from this region.

The United States of America are allied with Israel but Russia supports some radical Muslim states. The privileged relations the present leaders of France and Germany have with the president Bush could indicate the E.U. policy regarding the Middle East would be similar to the American one. Anyway, the big weight the Muslims have in the electorate of some Western European could lead to a more moderate position.

Romania was the only member of the Pact from Warsaw that, after the Six Days War from 1967, did not interrupt the diplomatic relations with Israel. In the same time it succeeded to maintain good relations with many Arab countries. The contacts it had with both parts made Romania contribute significantly to the preparation of Agreements from Camp Davis. This experience could be used in the negotiation of new agreements for Middle East.

During our investigation the 160 students were asked about their opinion regarding the E.U. policy to Middle East. It resulted they support a moderate policy, rejecting the idea of E.U. participation to a new military intervention in the area.

## **6. Conclusions**

This article had as subject the approach from a Romanian perspective of the decisions regarding the future of Europe. In the context of the Euroscepticism intensity from the last years, in these decisions – making the public opinion must be seriously taken into consideration. In our article, in order to understand the Romanian public opinion perceptions regarding the European problems we used the results of an investigation of 160 students.

In the present, the important decisions for the future of E.U. must be adopted in unanimity by the member states representatives. This situation makes that theoretically the small and the big countries to be equal as it concerns the strategic decisions making. Anyhow, the experience proved that practically the countries with big population and that are big contributors to the E.U. budget succeed to impose their points of view. The transition to the strategic decisions making by qualified majority could amplify the role of these countries. The considerable population of Romania offers a significant representation in the European institutions. However, being just a small contributor to the E.U. budget and the safeguard clauses that threat its quality of E.U. member does not allow it to play a big role in conceiving the future of Europe, at least for the moment. From our investigation among students we conclude they perceive a certain inferiority of Romania in comparison with other members and they consider it would not be desirable our country to adopt a strong position in the strategic decision about E.U.

About the institutional reform of E.U. it must decide upon the attributions distribution between the national authorities and the European ones. The Romanian government does not oppose, at least by declaration, to give up a significant part from its attributions in the favor of the European

institutions. Our investigation among students revealed half of them are favorable to an important transfer of attributions from the Romanian authorities to the European ones. Even those who are not favorable to this transfer do not consider that Romania should oppose frankly.

Concerning the decisions upon the future enlargements, it is expected that, excepting maybe Croatia, the new adhesions will not happen too soon. The Romanian government is favorable to some graduate enlargements. More than half of the students consider the new enlargements would be favorable to Romania but none of them thinks the government should act to urge them. After the European Constitution rejection it is obvious it will be difficult to get a unitary foreign affairs policy for E.U. Anyway, it is desirable the member states have similar positions in the important international problems. From our investigation among students it resulted they were favorable to some moderate positions and they did not agree the participation of E.U. to military interventions.

For now, it is not expected in the decisions regarding the future of Europe the Romanian authorities to have radical positions, as it was the case of Poland with the occasion of Reform Treaty debate. Such an attitude is caused both by the reduced economic force and by the safeguard clauses still available and by the quite favorable perceptions of the public opinion about the integration.

## References

Blanchard, O., *The Economic Future of Europe*, Working Paper 10310, NBER, Cambridge, February, 2004, accessed at <http://www.nber.org/papers/w10310> in June 2007

Busek, E. and W. Mikulitsch, *Uniunea Europeană și drumul spre Răsărit*, Iași, Institutul European, 2005

Ciascai, G., *Entre Balkans et Orient: l'approche roumaine de la PESC*, Institut de Securite de l'Union Europeene, 2006, accessed at <http://www.iss.europa.eu/occasion/occ65.pdf> in June 2007

Cojanu, V. , M. Birsan, L. Muresan and O. Aristide, *Elemente ale unei strategii post-aderare pentru Romania*, Institutul European din Romania, Studiul nr. 7, 2006 accessed at [http://www.ier.ro/PAIS/PAIS3/RO/ST.7\\_RO\\_Final.PDF](http://www.ier.ro/PAIS/PAIS3/RO/ST.7_RO_Final.PDF) in June 2007

Huntington, S. P., *Ciocnirea civilizațiilor și refacerea ordinii mondiale*, București, Editura Antet, 1998

\*\*\* Guvernul României, *Strategie post-aderare 2007 – 2013*, accessed at <http://www.guv.ro/presa/integrare/12/strategie-post-aderare.pdf> in June 2007

# CUSTOMS RISK MANAGEMENT IN THE EUROPEAN UNION

EMILIA IORDACHE<sup>1</sup>

ALINA VASILICA VOICULET<sup>2</sup>

## Abstract

In the latest decade, the major reorientation of the customs policy in the EU consisted in shifting the emphasis from the fiscal role to the function of protecting and ensuring security within the community. The suitable and proactive administration of risks at community level is compulsory if one wishes to decrease the challenge caused by expansion referring to the customs union, the progress related to security issues and reaching a balance as to customs clearance implementation. The customs model of risk management at community level integrates various elements of a global approach. To minimise the occurrence of risks, customs can use risk management as a technique to more effectively set priorities and more efficiently allocate resources necessary for maintaining a proper balance between controls and facilitating legitimate trade. In the present context of Romania's strategic geographic localization, it is an urgent need to apply external frontier integrated management, leading to Romania's perfect integration in the application of the European Neighbourhood Policy.

**Keywords:** risk management, risk analysis, the integrated management of external frontiers, customs

**JEL classification codes:** F15

---

<sup>1</sup> Lecturer PhD., "Constantin Brâncoveanu" University of Pitești, Romania.

<sup>2</sup> Lecturer PhD., "Constantin Brâncoveanu" University of Pitești, Romania.

## **Introduction**

The 2005 European Commission work programme admits that “security is one of the primary expectations of European citizens”. In concrete terms, the Commission intends to focus on a common approach to border control. EU citizens will be better protected against security threats through a coordinated response at the external borders of the European Community. The customs authorities of the 27 Member States play an important role in the fight against cross-border crime and terrorism. Customs expertise in controlling goods, backed up by the use of modern IT systems and an efficient risk assessment, is vital to detect illegal goods such as drugs, explosive materials or nuclear and chemical weapons.

## **Aspects of Customs Fraud**

In the last decade, the role of customs has significantly changed from the collection of customs duties to the protection of citizens due to reduced duty rates and increased concerns for safety and security. The main task of customs nowadays in all administrations is the protection of citizens and their interests while facilitating legitimate trade.

The so called "security amendments" to the Community Customs Code which entered into force in April 2005, provide the legal framework for the measures introduced in the EU Customs Security Programme:

- Traders are required to provide customs authorities with information on goods prior to import to or export from the European Union (Pre Arrival/Pre Departure Declarations);
- Reliable traders will benefit from trade facilitation measures through the Authorised Economic Operator (AEO) programme;
- Introduction of a mechanism for setting uniform Community risk-selection criteria for controls, supported by computerized systems.<sup>3</sup>

These three approaches are interlinked and will provide enhanced security through a combination of measures; the provisions came into force in 2007. The European Community is expecting more security and more facilitation from these rules as for example the use of advance electronic information and electronic systems for risk analysis will enable customs to identify high risk cargo bound for Europe at an early stage in the logistical process. With the new security initiative, Customs will be enabled to carry out more targeted controls on high risk shipments by means of automated systems as well as new technologies.

The protection of the Community's financial interests and the fight against fraud are areas of shared responsibility between the Community and the Member States.

---

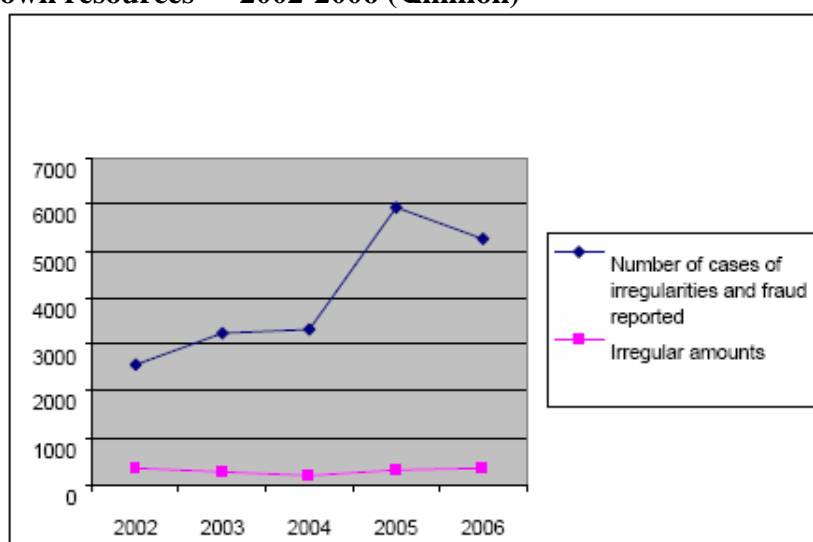
<sup>3</sup> *Supply Chain Security: EU Customs' role in the fight against terrorism*, [www.europa.eu.int/comm/taxation\\_customs/customs/policy\\_issues/customs\\_security](http://www.europa.eu.int/comm/taxation_customs/customs/policy_issues/customs_security), 03.05.2007

**Table 1 – Number of irregularities and amounts<sup>4</sup> – 2006**

TOTAL 2006			
Area	Number of irregularities reported	Total estimated financial impact of irregularities, including suspected fraud (€million)	Estimated financial impact of suspected fraud (€million)
Own resources	5 243	353	134.39 (~0.94% of the total amount of own resources in 2006 <sup>4</sup> )
EAGGF Guarantee Section	3 249	87	29.8 (~0.06% of the total allocations)
Structural Funds and Cohesion Fund	3 216	703	157.56 (~0.41% of total allocations)

As far as own traditional resources are concerned, in 2006, the number of cases of fraud and irregularities reported (exceeding €10 000) was down 12% on 2005 (from 5 943 to 5 243), but the amount affected by irregularities rose by over 7% (from €328 million to €353 million)<sup>5</sup>. The goods most affected by irregularities in 2006, as in previous years, are tobacco products and TVs. The figures for sugar, fish, glass and glassware and optical instruments were down on 2005, whereas meat, engines and parts, inorganic products and oils and fats were all up. The textile sector remained relatively stable, involving €10.3 million in duties.

**Graph 1: Number of irregularities reported and estimated financial impact in the area of traditional own resources<sup>6</sup> – 2002-2006 (€million)**



<sup>4</sup> Protection of the financial interests of the Communities – Fight against fraud – Annual report 2006, [SEC(2007)930], [SEC(2007)938], Commission of The European Communities, Brussels, 06.07.2007 COM(2007)390, 30.07.2007, (5)

<sup>5</sup> idem, (7)

<sup>6</sup> idem, (7)



As part of a sound control system, appropriate assessment and management of risk help ensure that taxpayers' money is spent properly when implementing policies. This area is currently being developed within the Commission as well as in Member States, to ensure proactive protection of financial interests, prevention and targeted action.

For some years the Commission has used risk management not just in relation to expenditure but more generally too. Acknowledging the need for a common approach to risk management, the Commission has taken a number of steps since 2006. The objective is to improve the decision-making process, to increase effectiveness and to strengthen the reliability of management systems. In this context, Commission departments now have a common methodology for analysing risk and choosing the right response. In the latter part of 2006, a pilot study was carried out to test a structure meant to improve risk management for several departments and bring about more effective management by grouping services. That structure is to be put on a permanent footing in 2007.

At national level all Member States have rules in their budgetary procedures to help managers to assess and manage the financial risks involved in awarding grants and public contracts, in particular to verify the reliability of potential beneficiaries.

The new financial rules introduced in 2006 require to national administrations establish effective internal control systems and perform the necessary inspections on the EU funds they manage. This means providing information and reporting each year on controls and audits.

Approximately half of the Member States have general national guidelines (instructions or good practices) or rules on risk assessment and management in specific fields.

The national customs authorities have for a long time been using risk analysis to identify potential illegal activities and to target controls more effectively. Over the years coordination at European level has improved the effectiveness of actions taken by the national authorities. In 1997 the Commission presented an action plan for transit in Europe to combat transit fraud more effectively and in 2001 it drew up a revised regulatory framework which included the introduction of a new computerised transit system (NCTS). Following the special report of the Court of Auditors No 11/2006, the Commission took the necessary measures to ensure that, from 2007 onwards, it could access NCTS data concerning sensitive goods for the purposes of risk analysis, so that it could promote strategies for targeted physical controls of goods in transit.

The Commission also continued to improve the ConTraffic system, which provides an overview of container traffic. The system enables a container's itinerary to be monitored so that suspicious consignments can be identified. With a new web interface launched in 2006 and a database with over 220 million entries relating to more than 4.4 million containers, the system has been used by national authorities to help them combat fraud more effectively, particularly through joint customs operations carried out in 2006.

In December 2006 the Commission adopted a Regulation<sup>7</sup> amending some of the implementing provisions of the Community Customs Code. The Regulation also provides for the application of common risk criteria and common priority control areas and sets out standards for the harmonised application of customs controls in specific cases.

---

<sup>7</sup> Commission Regulation (EC) No 1875/2006 of 18 December 2006 amending Regulation (EEC) No 2454/93 laying down provisions for the implementation of Council Regulation (EEC) No. 2913/92 establishing the Community Customs Code (OJ L 360, 19.12.2006)

## **Customs Definition of Risk Management**

"Risk" means the likelihood that something will prevent the application of Community or national measures concerning the customs treatment of goods.

To minimise the occurrence of risks, customs can use risk management as a technique to more effectively set priorities and more efficiently allocate resources necessary for maintaining a proper balance between controls and facilitating legitimate trade.

Risk management can therefore be defined as a technique for the systematic identification and implementation of all the measures necessary to limit the likelihood of risks occurring.<sup>8</sup> International and national strategies can be effectively implemented by collecting data & information, analysing & assessing risk, prescribing action and monitoring outcomes.

## **The Elements of The EU Risk Management Process**

Risk management must not be seen as a static process but as an interactive process in which information is continuously updated, analysed, acted upon and reviewed.

What is Risk Management?

- Good management practice
- Process steps that enable improvement in decision making
- A logical and systematic approach
- Identifying opportunities
- Avoiding or minimising losses

Risk Management is the name given to a logical and systematic method of identifying, analysing, treating and monitoring the risks involved in any activity or process.

Risk Management is a methodology that helps managers make best use of their available resources.

Who uses Risk Management?

Risk Management practices are widely used in public and the private sectors, covering a wide range of activities or operations. These include: Finance and Investment, Insurance, Health Care, Public Institutions, Governments. Effective Risk Management is a recognised and valued skill.

How is Risk Management used?

The Risk Management process steps are a generic guide for any organisation, regardless of the type of business, activity or function.

The basic process steps are:

---

<sup>8</sup> *Standardised Framework For Risk Management In The Customs Administrations of The Eu*, EU Commission, DG Taxation and Customs Union, [www.europa.eu.int](http://www.europa.eu.int), p.3

1. Establish the context
2. Identify the risks
3. Analyse the risks
4. Evaluate the risks
5. Treat the risks

‘Risk’ is dynamic and subject to constant change, so the process includes continuing:

6. Monitoring and review and
7. Communication & consultation

## **The Risk Management Process:**

### **1. Establish the context**

The strategic and organisational context in which risk management will take place.

For example, the nature of your business, the risks inherent in your business and your priorities.

### **2. Identify the risks**

Defining types of risk, for instance, ‘Strategic’ risks to the goals and objectives of the organisation.

- Identifying the stakeholders, (i.e., who is involved or affected).
- Past events, future developments.

### **3. Analyse the risks**

How likely is the risk event to happen? (Probability and frequency?)

What would be the impact, cost or consequences of that event occurring? (Economic, political, social?)

### **4. Evaluate the risks**

Rank the risks according to management priorities, by risk category and rated by likelihood and possible cost or consequence.

Determine inherent levels of risk.

### **5. Treat the risks**

Develop and implement a plan with specific counter-measures to address the identified risks.

Consider:

- Priorities (Strategic and operational)
- Resources (human, financial and technical)
- Risk acceptance, (i.e., low risks)

Document your risk management plan and describe the reasons behind selecting the risk and for the treatment chosen.

Record allocated responsibilities, monitoring or evaluation processes, and assumptions on residual risk.

## 6. Monitor and review

In identifying, prioritising and treating risks, organisations make assumptions and decisions based on situations that are subject to change, (e.g., the business environment, trading patterns, or government policies).

Risk Management policies and decisions must be regularly reviewed.

Risk Managers must monitor activities and processes to determine the accuracy of planning assumptions and the effectiveness of the measures taken to treat the risk.

Methods can include data evaluation, audit, compliance measurement.

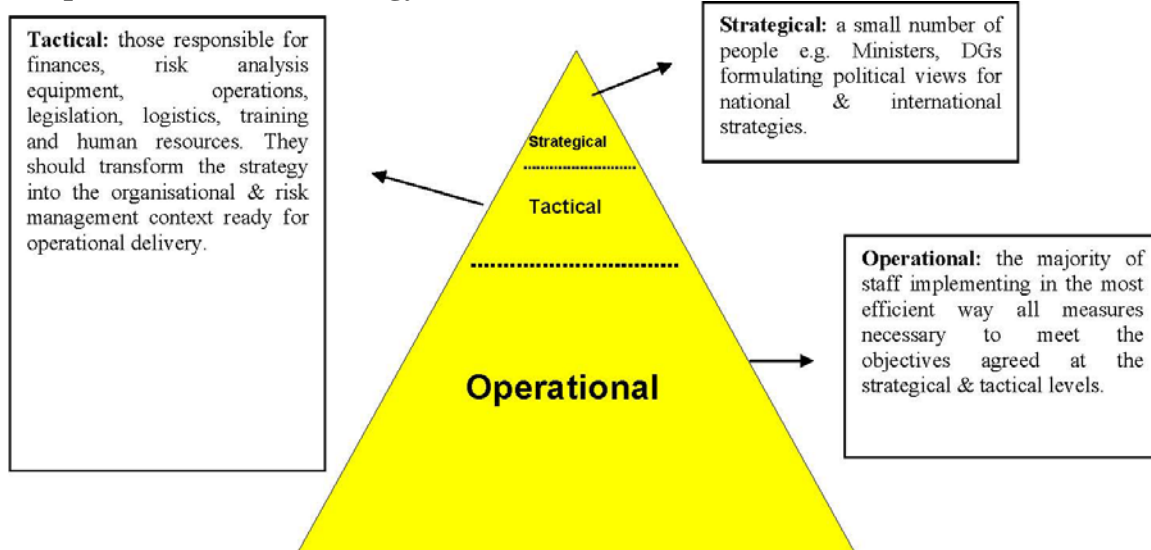
## 7. Communicate & consult

### Risk Management in Customs

Customs administrations have turned increasingly to Risk Management as an effective means of meeting national objectives. Administrations provide facilitation while maintaining control over the international movement of goods and persons. Risk management helps in matching Customs priorities to resources. International Organisations encourage and support the adoption of modern Customs control techniques, using Risk Management principles.

Risk management within Customs can be **strategic**, **operational** or **tactical**.

#### Graph 2 The levels of strategy



**Strategic:** Risks to Customs goals and objectives, e.g., prohibitions and restrictions, (social or economic), health, revenue, environment.

- usually longer term strategies

**Operational:** Decisions and action plans on measures taken to deal with the assessed risks. Deployment of resources; monitoring and review.

- medium term strategies

**Tactical:** Used by officers at their workplace, to deal with immediate situations, working within set parameters and to approved procedures.

- short term strategies

Why you should use Risk Management:

- Economic benefits, by facilitating the movement of goods, ships, aircraft and people – when rated low risk.
- Makes more effective use of existing skills and experience – giving better results.
- Improves the quality of Customs controls – information and accountability.

The process helps Administrations focus on priorities and in decisions on deploying limited resources to deal with the highest risks.

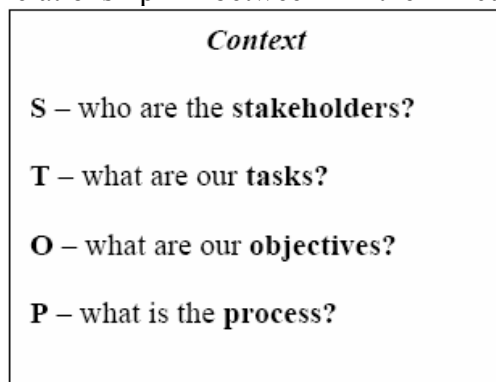
How do you use it in Customs?

Where do you start?

The first step is to look at your Customs context.

- What is the role of Customs?
- What are your national priorities and the expectations of the government and the public?
- What is the nature of your operational environment?

In step 1 the context is the environment in which the risk management process is performed. A range of factors such as resources, political & legal objectives and social aspects influences the context. The acronym S.T.O.P (above) is a summation of how to establish the context; more detail is given below. The result of this element should be a description of the relationship between the customs organization and its environment.



Today, customs administrations are required to provide extensive facilitation while ensuring that the international movement of goods, means of transport, luggage and other goods carried by or on persons are appropriately controlled. The level of risk is determined in the context of the national and international priorities set for customs administrations. Customs are responsible for the implementation of Community regulations relating to external trade, but not only for duty or trade regulation purposes, but also for environmental, anti-dumping, consumer protection, cultural and agricultural purposes. These responsibilities are a main feature of the strategic context established by customs administrations.

The **strategic context** can be defined by thinking about the following question:

**WHAT ARE CUSTOMS EXPECTED TO ACHIEVE?**

Many customs organizations have mission statements, long term visions or high-level control priorities and strategic objectives that can provide the answer to this question. It is within these documents that the future direction for customs is set and which leads to consideration of the organizational and risk management context.

The **organizational and risk management context** can be defined by thinking about the following question:

**HOW CAN CUSTOMS ACHIEVE THE STRATEGIC OBJECTIVES?**

Senior managers, technical and analytical experts provide the answer to this question and with that define the organizational & risk management context. They assess & understand the strategic context in the light of the organisations capability to deliver the strategic objectives. They then consider risk management of the strategy by taking into account the need to balance costs, benefits & opportunities, resources and equipment. They may need to prioritise certain strategic objectives or seek additional resources to tackle important objectives. The key issue here is the accurate assessment of the capability to deliver the strategic objectives. They need to consult widely with stakeholders and operational staff before implementing a risk management plan. They also need to consider the extent to which they need to monitor outcomes (element 4) and ensure that the capability to assess the effectiveness of the strategy exists or can be put in place. It may be the case that the measure of success is an improvement in the level of compliance, or an increase in the number of detections. If this is so, a benchmark should be established from which improvements can be measured.

The organisational structure necessary for establishing strategy, organising the risk management context and delivering results is shown below and is fairly typical in many countries.

The next steps in the Risk Management process are to: **Identify the risks; Analyse the risks; and Evaluate the risks.**

Who does the Risk Assessment?

Responsibilities must be allocated:

- Appoint a Risk Management champion with appropriate qualifications, including experience and analytical skills.
- Form a Risk Management Committee, representative of operational areas.
- Conduct Risk Management Workshops.
- Determine operating procedures.

Sources of information for Risk Assessments:

1. Identify commodity or control risks; e.g., high duty rates or quantity controls, the demand for prohibited goods, such as drugs, pornography, traffic in CITES wildlife.
2. Research existing databases and records on commodity and trader histories.
3. Evaluate current procedures to identify potential control weaknesses.

This step of the risk management process can be complex. Some member states prefer to view this step in greater detail and use a subprocess.

## **Identify risk data**

In this step information is vital. All available information should be examined as potential sources of risk data, evaluated for accuracy and where appropriate, be made available to the operational service. The information can also be valuable for legal departments to help them consider changes to legislation. Sources of information for this element of the process can be trade flows, declarations rendered, payments made on time/debt on file and new or changed legislation. The experience of operational staff should also be seen as a source of information as well as the results of their control actions. Information in TARIC, laboratory reports are useful sources. The risk data should then be analysed.

Using the risk data, and assessment of the risks in each aspect of the context should be undertaken. There are two main ways to view this, by analysing **proven risk** and by analysing **potential risk**.

Proven risk is historical fact, an irregularity has occurred and the organisation has a record of the incident and the facts surrounding the case. Lists of these risks can be analysed against current data to see if conditions surrounding the risk currently exist. If yes, an assessment of the likelihood and consequence of the risk should be undertaken (see below).

Potential risks are risks that have not yet been uncovered but are suspected. For example the development of a new commodity to which the owner assigns their Trade Mark®, may become the target of others wishing to breach the owners intellectual property rights. These risks should also be analysed against current data and if the conditions for the risk exist, an assessment of the likelihood & consequences should be undertaken.

Exchange of risk information between member states is an additional source of information, this is an important aspect to help equivalence of controls and to counter emerging threats rapidly.

Analyse the risks in terms of likelihood and consequence. The analysis should consider how likely an event is to happen and, if it were to happen, what are the potential consequences and their importance. Combining these elements will produce an estimated level/weighting of the risk in the next step of this element.

## **Weighting the risks**

There are different types of ranking systems. The assessment into HIGH, MEDIUM, and LOW is widespread. Although ranking in three levels is widespread, it can be defined in only two levels (high and low) or if desired it can be more than three levels. The output of this element in the risk management process should be a prioritised list of risks and the future treatment action specified.

*High risks* are generally likely to arise and have severe effects. Treatment actions for these risks should be highly visible to senior management and possibly agreed in control plans. In exceptional cases where a control is not acted upon, the reasons for not acting should be documented and made transparent to those responsible for assessing the risk.

*Medium risks* may be less likely to arise, or have less severe effects, but not necessarily both. Also with medium risks it is recommended to document the reasons for not acting.

*Low risks* are acceptable risks that can be assessed by standard or routine procedures or even where no action is necessary.

A consistent strategic approach, based on common criteria, understanding, methodology and procedures that applies across all areas of the risk management exercise should minimise

unnecessary subjectivity in the decision process. The consistent use of inputs including criteria, procedures and data will promote the production of comparable outputs, such as identified risks that are prioritised according to a common measurement scale. Logical categorisation of risks is considered necessary to set level of priority for assessing the identified risks.

### Evaluate the risks

After identifying and analysing the risks, you can evaluate.

What is the likelihood of the risk event occurring?

- Almost certain
- Likely
- Moderate
- Unlikely
- Rare?

What is the consequence if the risk event occurs?

- Extreme
- Very high
- Moderate
- Low
- Negligible?

You need to describe or to quantify exactly what the ‘Likelihood’ and ‘Consequence’ terms means to you. This helps in ensuring a consistent approach in future risk assessment and review and monitoring. It promotes a common understanding within the Administration.

After establishing ‘Likelihood’ and ‘Consequence’ you can use a table like this to set a level of risk

**Table 2 Level of risk<sup>9</sup>**

	Extreme	Very high	Moderate	Low	Negligible
Almost certain	Severe	Severe	High	Major	Moderate
Likely	Severe	High	Major	Significant	Moderate
Moderate	High	Major	Significant	Moderate	Low
Unlikely	Major	Significant	Moderate	Low	Very low
Rare	Significant	Moderate	Low	Very low	Very Low

You must define what these risk levels mean to you.

<sup>9</sup> Risk Management, www.unctad.org, 30.10.2006



## **Treating the risks**

Low and very low level risks can normally be accepted, subject to on-going monitoring. All other risks are included in the management plan. The plan catalogues the risks, the level of risk, and describes a treatment. The treatment is the action proposed, (and perhaps the resources allocated).

A common method of treating risks is to develop risk profiling and targeting systems. This means – in the case of goods – selecting transactions for specific checks, according to trader, agent, origin of goods, commodity code, duty rate, routing, value, etc.

Risk Profiles are developed as a means of putting risk management into practice at the Operational level. A Risk Profile is normally specific to a Customs office. It describes:

- The risk areas
- Assessment of the level of risk
- The countermeasures adopted
- Activation date and review dates
- Means of measuring effectiveness.

Using the profile information, consignments of goods, means of transport and people are targeted. The profile information is used as the basis for Selection Criteria.

Selection Criteria: documents received and processed by Customs, i.e., cargo and passenger manifests, goods declarations, are compared against the Selection Criteria



Selections are made by manual checks of documents, or by using automated systems. Selected transactions or movements are subject to the actions detailed in the profile or plan, e.g., physical examination, audit, etc.

## **Monitor & Review**

The initial assessment made of the existence and level of risks must be evaluated on a regular basis. You need to measure the effectiveness of risk profiles and update as necessary.

- Reliable reporting of examination results
- Compliance measurement activities
- Feedback from the business community
- Results analysis and data comparisons.

## Customs Role in External Borders' Integrated Management

The main responsibility of customs authority resides in goods clearance. However, in the current context characterized by the occurrence of new threats, customs has a major role in fighting those threats related to the goods that trespass community frontiers.

In December 2001, the European Council of Laeken required "the Council and the Commission to define the cooperation mechanisms among the services in charge of external frontier control and to analyze the conditions where a common external frontier control might be set up"<sup>10</sup>. In reply to that requirement, the Commission drafted an **integrated European strategy to manage external borders**, having as **main objective** *the improvement of security and controls at external borders facilitating legitimate trade and people movement*. At that particular time, they thought that customs clearance policies do not adequately meet the increasing security-related concerns. In addition, new members' accession to the EU does nothing but increases risks regarding security.

### Main Threats to Community's Security and Safety Criminal or terrorist threats that can be:

- **direct** – they involve the deliberate intention to bring forbidden goods into a country, such as explosives, nuclear weapons, biological or chemical weapons;
- **indirect** – they involve smuggling or illegal merchandise trade (drugs, cigarettes, alcohol, fake goods) with the purpose to supply or finance terrorist organizations or organized crime groups.

#### ➤ **Risks for consumers' security and safety**

- **Health risks:** threats to bio-security; for example, unauthorized contaminated products imports (the expansion of ESB cases was due to contaminated beef imports) or imports of products which contain genetically modified organisms. In terms of consumption, intoxicant products and other drugs can be included in this category.

- **Risks related to dangerous products:** there are risks of certain goods that are counterfeit or not in compliance with the Community's security regulations (for example, medicines, food products or various tools – lighters, detachable parts etc.).

➤ **Environment-related and sanitary risks:** these types of risks especially occur with species of flora and fauna becoming extinct, with radioactive substances or sick animals that illegally cross frontiers.

➤ **Public health risks:** the illegal trade in weapons and drugs.

Customs units play a central role in controlling the goods traded abroad and thus they can spot illegal goods as well. Allowing customs administration to take that function involves a re-assignment of customs tasks under the form of rationalizing controls at external borders; this aspect is essential as the new member states must implement the community customs legislation right away. The Schengen acquis is to be applied at the accession time, too, yet the Council must necessarily make a decision to suspend internal frontiers controls for the new member states. One should not forget that the member states in charge of external frontiers management are responsible for the Union's security as a whole, not only for the respective country's. For that reason, the same treatment applied to the main security risks at any spot of an external frontier means the community's concern, not a nation's.

---

<sup>10</sup> Commission des Communautés Européennes, Communication de la Commission au Conseil, au Parlement Européen et au Comité Économique et Social Européen, *Le rôle de la douane dans la gestion intégrée des frontières extérieures*, Bruxelles, 24.07.2003, COM(2003) 452 final, 2003/0167 (COD), [www.europa.eu.int](http://www.europa.eu.int), (42)

The controls and work methods in the customs field have been redirected in order to ensure the Community and its inhabitants' protection; that reorientation finds itself within the general and integrated framework of managing external borders, which has led to new organizational structures, and cooperation and coordination mechanisms among the services involved (customs units, police, sanitary-veterinary authorities, consumers' protection authorities). Therefore, the pursued orientations have been<sup>11</sup>:

## **I. Rationalizing customs controls' tasks at border units:**

### **1.1 Distribution of customs tasks between domestic and frontier positions:**

- based on defining and selecting priority risks;
- by developing control methods to allow that task distribution (for example, subsequent controls);
- by adjusting the facilities in trade so that they could comply with the security and safety criteria.

**1.2 Rendering the goods supply logistics chain secure**, especially by developing and improving the techniques to monitor goods and transportation means.

## **II. Implementing a common approach of goods-related risks and using a common cooperation and compliance mechanism.**

**III. Ensuring a proper level of human resources and equipment at external frontiers**, this objective having in view:

**3.1 To supervise the provision of necessary resources in order to ensure a high security level at external borders**, which involves:

- member states' provision of the necessary customs personnel availability and training; for training they can resort to "Vama 2007" programme, in the annex;
- the definition (at community level) and the provision (at national level) of the minimal necessary equipment;
- the analysis of community budget possibilities to finance equipment acquisitions to the extent that treaties allow;
- the identification of situations where an increased synergy with other customs services or expensive customs equipment at specialized frontier units might determine scale economies.

**3.2 Typical actions to allow the candidate countries to benefit from the best practices in the customs field** (for example, making up mixed teams).

**3.3 Making up rapid reaction teams when it comes to unexpected risks.**

**3.4 The community level inventory, development and implementation of the best work practices for external frontiers' security**, based on the experience acquired at national and community level.

**3.5 Drafting common steps to train and making up the organizing framework to train people in the field of external frontiers management for merchandise control.**

**IV. Ensuring a legal framework that could include security into the customs field** involves:

---

<sup>11</sup> idem, (56-58)

- the adjustment of normative acts and regulations in order to integrate the development of risk management;
- the promotion of agreements to share responsibilities among coterminous countries;
- the enhancement of cooperation with third countries.

#### **V. Enhancing cooperation with the police and other authorities having competence at external frontiers.**

In June 2002, two important political initiatives were launched: **"E-Europe"** and **"Improved Regulation"**. The initiative for **"Improved Regulation"**, which is one of the White Paper agreements on European governance, aims at simplifying European legislation in order to cut down the costs additional to business management in Europe and to strengthen the juridical security for citizens.

In this context, customs is a key field: giving incentives to proper electronic data transmission by common interfaces will allow the operators to avoid submitting a large number of statements containing similar or identical data to various frontier agencies. Moreover, all the requirements on imports or exports (at sanitary, environmental or health level) could be transmitted through a single entry or exit spot.

Traditionally, customs' most important role used to be to perceive customs rights and variable issues regarding agricultural products, therefore to supply the Community's budget; its participation in the Romanian VAT and excise collection still remains a major task. Consequently, customs also plays a leading role in globalization to countries' and companies' competitiveness as it has a large significance in foreign trade control and management.

Companies as well as overall society have great expectations concerning customs leaderships.

#### **➡ What are the society's expectations from customs leaderships?**

In addition to their traditionally fiscal role, customs leaderships are very important in protecting the society:

- customs stimulates the Union's economy when the latter needs protection (against dumping or counterfeit goods);
- it protects the society's economic interests by fighting against customs fraud (in the field of its own resources, of VAT and excises) and by ensuring that the commercial policy instruments are correctly applied (export replevins, anti-dumping fees, export and import licences);
- it protects public health (the interdiction and control over dangerous substances: drugs, hormones, dioxine);
- it preserves the environment (wastes, radioactivity) and the species becoming extinct (the CITES Convention);
- it contributes in the regional integration by promoting preferential commercial relationships among countries and regions.

#### **➡ What are companies' expectations from customs leaderships?**

When managing the logistics chain, the delivery term has considerably shortened due to informatics applications; if the customs process does not take part in that circuit, then the latter becomes an impediment to commercial flows. In relation with those new facts, companies' expectations are connected with the advantages they get, in particular higher efficiency, better services and increased productivity. The transport costs, regulatory

framework, information access facility, operations' predictability up to its completion (especially various frontier controls) – all these factors participate in creating companies' competitive advantage and new opportunities.

Modernizing and simplifying customs legislation lead to cutting down companies' customs costs and strengthening citizens' juridical security, and allow companies to obtain maximum advantages from the possibilities provided by informatics procedures and single market.

The **E-Europe** political priority, the EU's expansion and the ideas related to security impose an efficiency improvement of customs procedures and controls. That firstly involves a better distribution of roles between the customs units situated at the external frontier of the Union and those inside the community's customs territory. Controls at external frontier should concentrate on products' security and acceptance aspects; commercial and fiscal controls within countries are facilitated by the possibility to resort to the information included in the accounting balance sheets of an exporter or importer.<sup>12</sup>

## Conclusions

International trade is an essential driver for economic prosperity. The global trading system is vulnerable to terrorist exploitation that would severely damage the entire global economy. As government organizations that control and administer the international movement of goods. Customs administrations are in a unique position to provide increased security to the global supply chain and to contribute to socio-economic development through revenue collection and trade facilitation.

Securing the international trade supply chain is only one step in the overall process of strengthening and preparing Customs administrations for the 21<sup>st</sup> Century. Customs also have the authority to refuse entry or exit and the authority to expedite entry. Customs administrations require information about goods being imported, and often require information about goods exported. They can, with appropriate legislation, require that information to be provided in advance and electronically. Given the unique authorities and expertise, Customs can and should play a central role in the security and facilitation of global trade. However, a holistic approach is required to optimize the securing of the international trade supply chain while ensuring continued improvements in trade facilitation.

Modernized Customs administrations use automated systems to risk manage for a variety of issues. In this environment, Customs administrations should not burden the international trade community with different sets of requirements to secure and facilitate commerce, and there should be recognition of other international standards.

For customs administrations there is always an element of risk in controlling and facilitating the movement of goods. The extent of controls to ensure compliance with the laws and regulations that Customs are responsible for enforcing should be proportionate to the level of assessed risk.

In modern customs control techniques the process of risk management is an important aspect. It helps to determine where the greatest areas of exposure to risk exist, and supports management decisions on how to allocate limited resources effectively.

---

<sup>12</sup> Iordache, E., "The Reorganization of Customs Practices – A Part of Romania's Accession to the EU", Doctorate Paper, The Academy of Economic Studies Bucharest, The Faculty of International Business and Economics, Bucharest, 2007, (178)

The current stage of EU customs policy development has helped emphasize the function to prevent risks related to the security and safety of community citizens.

**References:**

*Supply Chain Security: EU Customs' role in the fight against terrorism*, [www.europa.eu.int/comm/taxation\\_customs/customs/policy\\_issues/customs\\_security](http://www.europa.eu.int/comm/taxation_customs/customs/policy_issues/customs_security), 03.05.2007

*Protection of the financial interests of the Communities – Fight against fraud – Annual report 2006*, [SEC(2007)930], [SEC(2007)938], Commission of The European Communities, Brussels, 06.07.2007 COM(2007)390, 30.07.2007, (5)

Commission Regulation (EC) No 1875/2006 of 18 December 2006 amending Regulation (EEC) No 2454/93 laying down provisions for the implementation of Council Regulation (EEC) No. 2913/92 establishing the Community Customs Code (OJ L 360, 19.12.2006)

*Standardised Framework For Risk Management In The Customs Administrations of The Eu*, EU Commission, DG Taxation and Customs Union, [www.europa.eu.int](http://www.europa.eu.int), p.3

Risk Management, [www.unctad.org](http://www.unctad.org), 30.10.2006

Commission des Communautés Européennes, Communication de la Commission au Conseil, au Parlement Européen et au Comité Économique et Social Européen, *Le rôle de la douane dans la gestion intégrée des frontières extérieures*, Bruxelles, 24.07.2003, COM(2003) 452 final, 2003/0167 (COD), [www.europa.eu.int](http://www.europa.eu.int), (42)

Iordache, E., “The Reorganization of Customs Practices – A Part of Romania’s Accession to the EU”, Doctorate Paper, The Academy of Economic Studies Bucharest, The Faculty of International Business and Economics, Bucharest, 2007, (178)

# TERRITORIAL NETWORKS - A SOLUTION FOR REGIONAL PROBLEMS?

LUIZA RADU<sup>1</sup>,  
MĂDĂLINA ISTRATE<sup>2</sup>,

## Abstract

Regional policy implementation proved that the micro and macro-economy elements cannot be separated because there are a various number of issues that need the integration of the two economic fields at the regional level. Moreover, the experience of the last decades in the European Union reveals that local/ regional development depends not only on endogen resources, but also on the approach to the global economy, on the capacity of developing relations with other regional systems in areas such as: exports, tourism, productive investments, technological transfer.

**Key words:** regional policy, territorial networks, partnership, development

**JEL classification code:** R 58

---

<sup>1</sup> PhD. Candidate, expert, Ministry of Development, Public Works and Housing, Member of the National Association of Regional Sciences, [luiza.radu@mdlpl.ro](mailto:luiza.radu@mdlpl.ro),

<sup>2</sup> PhD. Candidate, councilor, Ministry of Development, Public Works and Housing, Member of the National Association of Regional Sciences, [madalina.istrate@mdlpl.ro](mailto:madalina.istrate@mdlpl.ro),

## **Introduction**

The regional development policy, which represents an assembly of concepts, principles, aims and objectives, instruments and concrete methods for its implementation – is realized through the synergic action of governmental and non-governmental bodies that cooperate within an established institutional framework. Moreover, the regional policy is based on planned and promoted measures by the local and central public administration authorities, in partnership with different actors (public and private), in order to ensure a sustainable and dynamic economic and social development through and efficient use of local and regional resources for the final objective of the regional development accomplishment.

The regional policy of the European Union entitled the regions and those institutions that represent their interest. Regional policy determined the necessity that the European Commission should define the regions so as to allow a balanced socio-economic development and to serve as a basis for the Communities decision-making process regarding the priorities development resources allocation.

At the European Union level is considered that the optimum level of territorial structures for the design and implementation of the regional policy measures is corresponding to NUTS II in the Nomenclature of the Statistic Territorial Units of EUROSTAT. The territorial level NUTS II, associated with the territorial level represented by Region, is the conception, implementation and evaluation framework of regional development policies and social and economic cohesion programmes, representing meanwhile information collecting framework needed in the monitoring process, accordingly with the European regulations.

There is a general trend of regionalizing within the territorial organization of the European States, under a diversity of institutional forms. The region represents the most important innovation of the territorial administration systems in the last decades, which was basically undertaken, in a very short period of time, even if in different degrees, by all the European countries.

The scope in which these regions were created is similar to the one in the other member states - to support the bigger communities to solve their problems, which exceed the financial resources available at county level. The development regions represent the territorial structures in which the national policy of regional development is being implemented and evaluated.

The regional development policy, together with other factors – globalization process or the competition for localization determined the emergence of regional networks, which promote the resources mobilization and regional potential capitalization.

## **Regions and territorial networks**

The networks can be defined in many ways, the terminology being used in various fields of activity such as chemistry, neurology, architecture, cybernetics. Today everything seems to be part of a network. Even if the network concept is widely used, clarifications are needed because everything gives the impression of relations, connections, associations, cooperation, etc.



As a general definition, the network describes a process where two or more participants or groups of participants work for a common goal having the same vision. This process is not based on formal contracts, but on trust, partnership and the conviction that the interested persons will obtain benefits (Sprenger, 2001).

According to Glas (1995) a network consists of three basic elements: actors (that perform activities and control resources), activities (that can be for the transformation of resources or for connecting actors and shaping relations) and resources (having as main characteristic the interdependency).

Moreover, the international literatures defines the regional networks as a cooperation between the business environment, governmental organizations, research institutes and universities, intermediary bodies, etc. Business and public networks are integrated components of the “regional networks” system.

The decision of setting-up regional networks can be determined by many factors: competence lacking in the existing institutions, requirements regarding the new partners, the missing of the local funds and resources, the increasing of the importance of soft factors for localization. Also, the setting-up of the regional networks can take a variety of forms, depending on the origin and the number of partners, the initiative rationale and the network objectives. The form of partnership within the territorial networks is influenced by the institutional framework, by the specific problems of the regions, but especially by the targeted objectives.

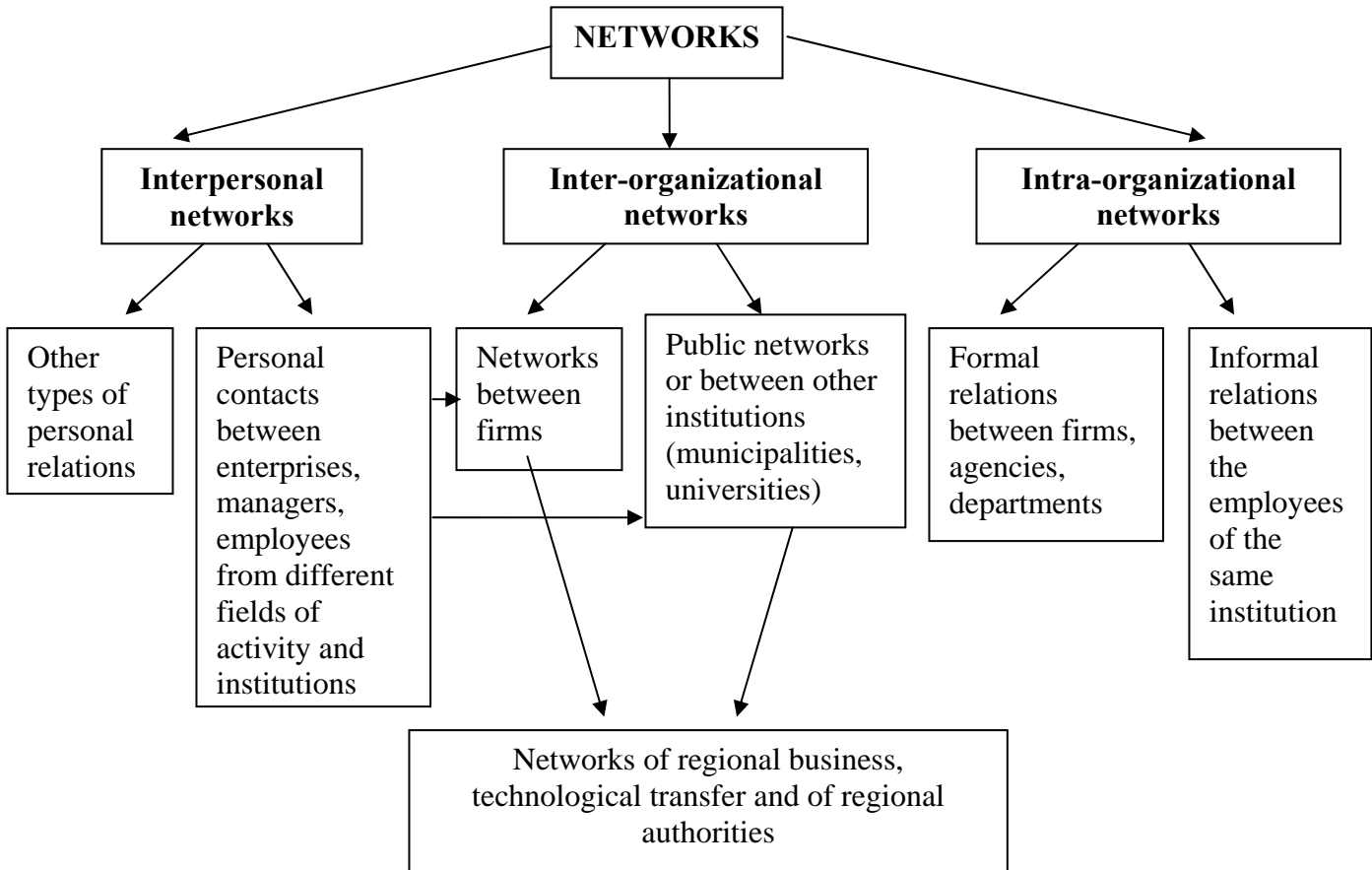
Within the territorial networks the participation is on volunteer basis, the members being representatives of different social levels (business, trade and industry chambers, governmental bodies and other public institutions, research institutes, universities, social groups), and the relations are based on equal rights, dialogue, consent and compromise, targeting a win-win situation for all the participants in the network. It should be mentioned that the participants in the network do not have the authority and power to act upon or to penalize the others, the premises of successes being the mutual trust and learning from each other.

In regional policy field, the network had various form of setting-up accordingly to the specific reasons of the partners for cooperation, as well as localization in certain areas. The European Union practice identifies regional cluster initiatives, regional centres of environmental excellence, regional employment and environmental protection initiatives, Agenda 21 initiatives as being types of regional networks.

Regional clusters represent a form of cooperation among production and services companies, research institutes, training institutions that can provide complementary services to the members. The regional centres of environmental excellence aim to develop the research competences and to increase the economic application of research and development results. The regional employment and environment initiatives supported by the European Commission through the “territorial employment pacts” aim to implement coordinated measures for securing the employment and creating new jobs. Agenda 21 initiatives encourages the implementation of the concept of sustainability within the economic activities.

The development of the territorial regional networks was encouraged by the European Union policy that promotes the partnership in the implementation of the projects financed through Structural Funds.

Through the involvement of a broad group of participants, a wider range of expertise is available for use during the programming cycle of Structural Funds programmes. This can help to improve the effectiveness of programme development, monitoring and evaluation. By contributing their specific knowledge on a certain subject or region, their awareness of potential project applicants, partners can improve programme effectiveness by raising the efficiency of project selection. Generally speaking, a widely drawn partnership leads to greater commitment and ownership of programme outputs, and hence to a direct interest in the success of the programme.



**Fig 1. Types of network and relations among**

Source: Institute for Structural Policy and Economic Development, [www.isw-online.org](http://www.isw-online.org)

The participation of regional and local authorities and that of civil society helps to legitimize the decision-making process by counterbalancing any specific political or other influence. Regional and local authorities, socio-economic partners and civil society can contribute also to the transparency in decisions and decision-making processes through their involvement and through their channeling of information.

The network success depends on the dynamic process of development. Every regional network must take into consideration the requirements of a development process under the influence of the conditions when it was created (initiators, regional conditions, legal framework).

## **Implementation of regional policy through territorial networks**

The fast economic changes represent a challenge for the local actors, and the existence on a market in a permanent change determines the cooperation among them. Moreover, the economic changes from the regional and local level determine the adaptation of the local production system to the request of the international economic competition. Thus, the open of local economies to the interregional and international markets determine the setting-up of local cooperation, an important stage for implementing commune actions at interregional level.

A modern regional economic policy must be characterised by a territorial approach, rather than sectoral or functional, by integrating different economic elements (research, training, transport, etc.). The open of local economies and the new forms of economic integration of firms and local actors justify the transition from an approach of economic concentration and sectoral specialization to territorial and intersectoral integration one.

Thus, there can be two types of regional interventions and even complementary. One of them is referring to the concentrated intervention in individual systems of local production. Within these, the local authorities can establish detailed guidelines or sectoral programmes through which to define the eligibility and selection criteria for the beneficiaries and projects. In this case will be done an ex-post selection of specific plans, promoted and cofinanced by local actors.

Regional and local administration can encourage the projects implementation in strategic areas that need a local approach and allow the strengthening of local authorities' role:

- Involving in setting-up new firms and encouraging the entrepreneurship;
- Encouraging the production diversification and reconversion for specialized industrial areas;
- Know-how transfer and promoting the long life learning process;
- Promoting a sustainable development through territorial planning and network transport improvement.

Therefore, the economic policy should not only sustain the initiatives having as objective the improvement of local productive systems, but also to promote activities with important regional impact, such as: regional integration of different local production systems, investments for research and development within innovative projects implemented at regional level, interregional and international cooperation in production areas.

Another type of intervention, characterized by a bottom-up approach, can promote regional action programmes with an important strategic character and encourage the setting-up of regional innovation systems and the conversion of regional production systems according to the "learning region" model. In this case the participants will not implement isolated projects, but will participate within a network to implement one single project. Thus, the partners' selection must be made ex-ante and not ex-post, based on criteria as: the actors' involvement in different regional sectors, the capacity to ensure original and qualified contributions in project implementation. The promoting of the own regional development policies by the local public administration authorities but also by the regional structures starts from the premises that nobody knows better the real necessities of these collectivities but themselves and the ones elected to represent them.

Traditionally, through the regional policy, is granted financial support for less developed regions, in order to reduce the regional disparities. But, even in these conditions, the regional policy must be implemented by taking into consideration the competitive advantages, by using different instruments. Thus, by the promoted measure will be created services centres for small and medium enterprises, incubators for new innovative firms, technological parks, will be developed the relations between firms and research institutes. Even in this case, there is recommended the collaboration between regions confronted with development disparities and the developed ones. Moreover, the regional policy, must promote not only cohesion and territorial integration of regions, but also to encourage the set-up of networks between firms or strategic alliance at interregional level. Especially for the less developed regions, the new investments are not always sufficient, so that must be encouraged the economic partnership and firms cooperation. These involve a financial involvement of entrepreneurs.

<b>Economic advantages</b>	<b>Socio-cultural advantages</b>	<b>Ecological advantages</b>
<ul style="list-style-type: none"> <li>– Finding and using the regional development potential</li> <li>– Increasing the regional added value</li> <li>– Increasing used of synergies effects through cooperative planning</li> <li>– Reducing the reaction time to regional structural problems</li> <li>– Development of new services and products</li> </ul>	<ul style="list-style-type: none"> <li>– People affected become participants</li> <li>– Are supported the regional initiatives, creativity and cultural identity</li> <li>– Solving the regional conflicts is supported by intermediary structures</li> </ul>	<ul style="list-style-type: none"> <li>– Increased importance of environmental regional problems</li> <li>– Increased regional responsibility</li> <li>– Improvement of the regional resource cycle</li> <li>– A better integration of the environmental dimension into regional development by ex-ante evaluation, indicators, project selection.</li> </ul>

**Table1. Anticipated advantages of regional networks**

Source: Sprenger, 2001

Moreover, the territorial networks can represent a solution for the regional development problems that could not be solved or for which were proposed inadequate solutions by the traditional institutions. It contributes to the competitiveness increase and unemployment decrease by using the regional social capital potential, as well as by involvement of different groups of regional actors. In addition, the involvement of partners contributes to the development of institutional capacity at sector and territorial levels. Through the involvement of local or regional authorities, their institutional capacity has been strengthened, their awareness on European structural policy has been extended, and a more effective dialogue between the different authorities has been established. The participation of the different actors contribute to the drawing –up of innovative projects that responds better to the community problems improving the evaluation and the monitoring process, dissemination of best practices and obtained results, creating opportunities for reinforcing innovation. The private sector must also actively involve both with financial and human resources. Thus, can be developed a partnership culture by encouraging organizations to see the local development as a responsibility for the people that live in the area.

## References:

Cappellin, R., "The governance of regional networks in the process of European integration", *The CD-ROM Collection of Papers of the 41<sup>st</sup> Congress of European Regional Science Association*, Zagreb, 2000

Fischer, M., "The new economy and networking", in M. Fischer (editor), *Innovation, networks and knowledge spillovers*, Springer Verlag, Berlin, 2006

Glas, G., „Industrial networks, regional orientation, cultural aspects and policies”, *Collection of Papers of the 35<sup>th</sup> Congress of European Regional Science Association*, Denmark, 1995

Radu, L., Constantin, L., "Territorial development and networking – the role of partnership", 2007

Sprenger, R.U., *Inter-firm Networks and Regional Networks*, NSS ADAPT, Bonn, 2001

\*\*\*European Economic and Social Committee – "Partnership for implementing the structural funds", 2003

\*\*\*European Commission "Territorial State and Perspectives of the EU Document – Towards a stronger European territorial cohesion in the light of the Lisbon and Gothenburg ambitions", Bruxelles, 2006

\*\*\*Thematic Evaluation of the Structural Funds - Contributions to the Lisbon Strategy, Danish Technological Institute, Denmark, February 2005

# **THE EUROPEAN UNION IN A CHANGING WORLD: GLOBALIZER OR GLOBALIZED?**

**FLORIN D. SALAJAN<sup>1</sup>**

## **Abstract**

This paper analyzes the influence of the globalization processes on the European Union's viability in today's transformative world. Its main theme of discussion is the tension between an EU that may appear to be threatened by globalization and an EU that may be construed as an active factor of globalization. This paper maintains the view that while global forces exert significant political, economic, social and cultural pressures on the EU's member states' ability to remain viable entities of governance, the EU as the embodiment of pooled sovereignty can not only protect the European nation-state from demise, but it can also strengthen it by representing it on the world stage through the legitimacy conferred upon it by the member states. The conclusion offered here is that the EU acts predominantly as a globalizer, even though it is itself exposed to the processes of globalization, and that it can stand as a model of governance from which other regions of the world may seek inspiration.

**Key words:** European Union, Europeanization, globalization, governance, regionalism.

---

<sup>1</sup> Columbia University, 525 West 120<sup>th</sup> Street, New York, NY 10027, USA; fds24@columbia.edu; 212-678-3000.

## Introduction

Dreaded by some, celebrated by others, there is no escaping globalization in any kind of discourse today. From politicians to business people, from academics to students of all ages, from the ever-present media to the man on the street, just about anyone has heard, talked or written about it. Blamed or credited, depending on the stance one takes, for the need to reform, for competition, for economic changes, for richness and poverty, for the spread of digital technologies, for changes in social habits, for the way in which we learn and teach, for the ills and the thrills it generates, for ups and downs of all sorts, for abundances and shortages, or for just about anything our minds can fathom, globalization has been a driving concept in thinking about these themes.

But why talk about globalization here? Primarily because the term globalization consistently appears in EU official documents and parlance as a rationale for promoting needed programs, projects or actions subscribing to the larger narrative of developing a globally competitive organization on all fronts. If it is technology, education, business, industry or social measures, globalization is the all-inclusive motivator for persuading the multitude of actors, but especially member states' governments, into action. To be sure, it must not be inferred from here that individual governments are ignoring the global trends, quite the contrary. But the EU institutions are concerned with fusing the fragments into a strong whole able to cope, as a unitary mechanism, with the pressures from global competitors. Because of the unique relationship between the member states and the EU institutions, an incursion into the realm of globalization and its relevance for the contemporary functioning of the nation-state (or simply *the state*)<sup>2</sup> is a theme that has to be subjected to theoretical scrutiny at this point.

The discourse on globalization has expanded to the point that there is virtually no electronic medium, TV newsreel, journal, newspaper, academic publication or government document that doesn't make reference in one way or another to globalization in any field of inquiry. My intent here is not to fully engage in a minutely detailed epistemological analysis of globalization. The field is enormously varied, interpretations run through the lenses of the full gamut of economic, political or social theories and the complexity of the notion itself renders it rather unwieldy for an elaborate discussion that could fit in the space of an article. As Scholte (2000) puts it, "the only consensus about globalization is that it is contested" (p. 39). I am rather focusing on some of the key aspects that I believe make it relevant for the subject at hand here, namely the relevance of the nation-state in the context of contemporary global trends.

The root cause of much of the confusion, frustration and disorientation surrounding globalization in our times stems from the difficulty of pinning down the term itself to a general accepted understanding. Its significance is put to the test, with some calling it a phenomenon or a process, others thinking of it as an ideology, yet other denying its existence altogether. Some have attempted to bridge this divide by employing two terms instead of one. Thus, *globalization* and *de-globalization* are processes whose axes of representation are projected in terms of action and distance. They are the movers in a "state of the world involving networks of interdependence"

---

<sup>2</sup> I will use the terms *nation-state* and *state* interchangeably, though there is a fine difference, in my view, between the two. *Nation-state* has an affective connotation which implies the presence of a nation or people with its institutions as an interactive unit in which "subjects" and "rulers" are bound together by a shared commitment to the upholding of the nation's distinctive character. *State* is devoid of the emotional linkage to a cultural pattern of behavior, being more oriented towards maintaining the rule of law and acting as the guardian of the universal rights interests and obligations of all entities under its dominion.

called *globalism* (Keohane & Nye, 2000, p. 2). This dichotomy, however, may render the debate on globalization even hazier than it needs to be, as the term globalization is generally understood (or perhaps misunderstood, depending on interpretation) to comprise both notions. Steger (2003, p. 7) and Scholte (2003, p. 87) mention *globality*, as a derivative term of globalization. While the former uses it to refer to a “social condition” that encompasses a wide array of “interconnections,” the latter perceives it as a set of “circumstances where territorial space is substantially transcended.” Everyday media and globalization literature rarely ponders the distinction between these notions, however, opting instead to stick with *globalization* as the sole term of reference. I will not embrace here a hard definition of globalization, but I find both Keohane & Nye’s and Steger’s positing useful in expressing my view that globalization, in general terms, is a manifestation of multi-sectoral forces exerting push or pull actions across distances on entities throughout an interconnection of systems. I also drew some inspiration for this formulation from Giddens’ (2003, p. 60) dialectic relation between “local involvements” and “interaction across distance” without necessarily submitting to his interpretation of globalization.

### **Dimensions of Globalization**

More often than not, globalization is assigned a whole range of dimensions in the academic discussions. Each dimension appears to be split right down the middle with two camps trading contradictory messages across the dividing line. The most frequent of all and probably the easiest to identify, is the economic dimension. It seems to be the instinctive association to and the primary driving force (if not fundamental for the hardcore economists) globalization for many authors. Those who see the acceleration of transactions across economic systems as irrefutable proof of the presence of globalization, are usually enthusiastic free-traders who consider that unbridled trade, liberal economics, deregulation, minimal government interference, promotion of foreign direct investment, free movement of capital, etc. constitute the recipe for success in the countries of the global economy. For them, international financial institutions, such as World Trade Organization, International Monetary Fund or World Bank are “the pride of progressive architectural design regarding the management of the world economy” (Bhagwati, 2004, p. 23) and Coca Cola refrigerators in the “lonely desert outposts” selling the popular soft-drink stand as “temple[s] to consumerism, choice, global integration and corporate organization” (Moore, 2003, p. 43). On the other hand, there are those who oppose this picture of progress via free-trade by arguing that there is nothing new about globalization or that we are witnessing the end of globalization. James (2001) points to the “globalization backlash” of the late nineteenth century to the run up of the Great War as an indication that globalization is not characteristic of our contemporary world (p. 6). Saul (2005) concurs with this cyclicity, but nuances it with the broken promises of the elites’ global economic designs which rendered richness in some quarters but reduced the collective wealth of ordinary citizens (p. 24). In driving home the same point, Rugman (2000) calls globalization a “myth” and considers that the bulk of the global economic trade is confined to a space he calls the “triad” (p. 22), formed by the economies of the United States, European Union and Japan, with much of the rest of the world being left out of this share of the global economic pie.

Politics is the next subject in the globalization debate. It is usually concerned with governance and territoriality tied into the question of the locus of political control at global level. Here again we see two main diverging perspectives. On one side of the coin we have those who propose



that policy-making has shifted from the traditional governing bodies of the nation-states to the supranational, suprateritorial, intergovernmental (not in the sense in which it applies to EU politics) or, more simply put, international level. The first example that is immediately contemplated is that of the European Union, which has come to be recognized, even by many economists for whom Europe as body-politic is an afterthought, as a new kind of political organization embedded in globalization. The United Nations, with its Security Council and the General Assembly, is considered an international political force, particularly through its subsidiary bodies entrusted with guaranteeing international law (International Criminal Court or the International Criminal Tribunals for the former Yugoslavia and Rwanda). The Council of Europe or the Organization for Security and Cooperation in Europe (OSCE) also serve some of these functions, though at a regional level. International economic bodies such as the WTO, IMF or World Bank are also considered as branching out into the political realm, as many of the economic policies that come out of these organizations have deep impacts on the politics of many developing countries. Other entities, such as International Non-Governmental Organizations (INGO) have been attached increased significance in recent times for influencing national government decisions on various issues. On the other side of the coin we see the defenders of the sovereign right of national governments to manage, control and represent the interests of the state both internally, as well as externally. This view seemed to fade away in the aftermath of the Cold War, but it has gained fresh confidence within the last few years given America's new reassertion and projection of political and military power employed in the defense of national security interests.

The socio-cultural dimension entertains the idea of societal transformations and cultural interconnections that are brought about through the dispersion of social habits and culturally iconic traditions specific to some places to the rest of the world. For those who support this type of globalization, there are benefits to be gained from the diffusion of models of social practices or programs from those locations in which they are proven to be successful to other parts of the world that could benefit from them. For others, the concern is that this application of models cannot be performed without adaptation to local conditions, since cultural traditions may not be compatible with aspects of social models developed in culturally different environments. The debate is not as sharply polarized in partisanship terms as is the case with more concrete notions such as politics or economics, but being immersed in a naturally shapeless and fluid medium like culture or society, it is fraught with the difficulty of extricating and making sense of key elements from the entangled web of the socio-cultural mosaic. The discussion usually revolves around dissecting the meaning of powerful influences of cultural icons promoted, not coincidentally, through economic means. Commercial brands with instant recognition (Coca Cola, McDonalds, Nike, IBM are just some of the examples that easily come to mind) are perceived by many critics as the vehicles of the imposition of a western consumer culture on world locales without due consideration of the impact on local people's cultural traditions. Benjamin Barber's (1995) "McWorld" concept captures this condition and visualizes the uniformization of the global cultural space, through manipulating the images, sounds, messages, propaganda, desires and (im)morals of a culture that is everyone's and yet no one's. The "infotainment tele-sector," as Barber names it, fills every nook and cranny of every cultural universe, de-localizing and imperiling age-old local customs and arts. Yet, at the same time, resistance to the imposition of alien cultural constructions on parochial cosmoses manifests itself at every turn, even if the chances of survival of rituals or ways of life, for instance, in the face of the pop culture monolith are slim. Not everything in this realm needs to be marked by gloom

and doom though. While many cultures sense the threat of extinction, others are able to extract or adapt some of the elements of the dominating western values and transpose them to local conditions (Inglehart, 2003, p. 131). Those that are indeed endangered to lose their identity are the smaller communities that, in the first place, suffer from a dwindling of their generational pool. But then, they may well be fated to disappear altogether, a consequence that may not be attributed to western cultural imperialism.

Environmental concerns have entered global consciousness thanks to the relentless efforts of the scientific community and advocacy groups (Greenpeace is the most notorious of them all) in urging governments around the world to foster cleaner lands, waters and skies. A superficial reading of any daily news source would place global warming or climate change, for example, to the heart of globalization and impart the sense of urgency that is often uttered through the media outlets about the need for action in coping with this pressing matter. This environmental dimension, while having deep ramifications in multiple aspects of life, particularly in the fundamental level of society's very existence, is intrinsically linked to the human activity in the economic realm (Keohane & Nye, 2000, p. 5). Industrial activity, development and growth are principal "culprits" in such environmental ills as air and water pollution, soil degradation, oil spills or ozone depletion. But farming techniques (whether in the developed or developing countries), human consumption, traffic congestion or waste (mis)management are also factors with huge consequences for the environment. That is why sustainability in economic development programs, be it in agriculture or industry, is always associated with environmental protection, so that growth is not pursued at all costs without the implementation of measures to prevent hazardous spills or unnecessary pollution of any kind that can damage the planet's ecosystem.

Another component of globalization ponders international security arrangements, proliferation of weapons and projection of military power, acute issues today particularly in the conditions of an international military order in which the United States has unmitigated supremacy. If during the Cold War a nuclear standoff between the US and USSR was at once a threat to and a deterrent of each superpower's actions, the collapse of the Soviet Union left the US exposed to the uncertainties of not knowing how to wield its immense military might. The perceived threat of unconventional warfare has forced international security arrangements, like NATO, to reconsider their missions. Set up as a common defense umbrella for the US and its western European allies to confront potential Soviet aggression, NATO had to redefine its role to take on uncharacteristic duties such as peacekeeping, while also moving from a defensive to a more offensive philosophy particularly when it comes to its members countries' cooperation in combating terrorism or actions of "rogue states" that could potentially be involved in supporting terrorism.

There are many other facets to globalization, but I would like to finally give due consideration to education and computer technology as features that have daily relevance to our contemporary life. Education is crucial in acquiring the knowledge and skills from which one benefits over the course of one's life. If the ancient Chinese, Indians or Egyptians with their universities or the Europeans with the modern conception of degree-granting universities (the oldest European university in existence today is the University of Bologna, founded in 1088), recognized the value and power of formal education, it makes sense to keep education in the same high regard today. How can we conceive of a relationship between education and globalization? In the sense that education generates human capital for use in the global economy or for using universally recognized digital technologies for learning new skills or accessing information, at

the general level, we may speak of global education. But formal education does not easily lend itself to generalizations of the sort that would render it global. Schools and universities are embedded in national cultures normally residing on territorially confined states (Boyer, 1996, p. 51). Essentially, institutions of formal education are the vehicles for the preservation and perpetuation of national culture and a fundamental feature of the modern state is its unconditional, expected financial and logistical support of its educational system. No global educational system is on the horizon.

At the same time, the proliferation of information and communication technologies have enriched the global societal landscape by transforming the way governments, businesses, corporations, armies, individuals in general, etc., communicate and use information. Sure enough, ask what the source of globalization is and chances are that the first answer you get is ICTs, the internet or the World Wide Web. Any government agency, commercial firm or university today that does not have a web address is out of step with the rest of the world and can pass as a non-existent entity in some respects. It goes without saying that the educational system is both the promoter of ICTs as well as the environment in which skills to use them are imparted. After all, in our society, it is those individuals who are educated that are able to make effective use of technologies for professional, recreational or commercial purposes.

### **The Nation-State and the Pressures of Globalization**

Within all these dimensions, the state acts as the common denominator given that it represents a space in which various interactions originate and are transmitted, parceled out through borders that separate national territories. It is often argued in the globalization literature that the role of the state in regulating social, economic or political activity has diminished in recent years, particularly when the subject is viewed from the perspective of commerce and telecommunications. There are visible signs, however, that the nation-state has shown remarkable resilience in what we perceive as the tumult of deep global transformations. I am of the opinion that the state remains the most viable alternative, as a manageable unit of territorial governance, to any envisioned global arrangement. That the state has been affected by borderless economic and financial transactions is undeniable, but it has not led to the dissolution of the state as the container of political, social, cultural, ethnic and national values of a populace within its territory. Even in the sophisticated EU with its transfers of authority from national to supranational institutions, national determination and the recognition of many sovereign rights of states are as valid as ever. Sassen (1996), for instance, apart from contending that economic activity and the emergence of the “electronic space” have induced extraterritorial pressures on the authority of the nation-state, questions the ability of national governments to control the entry of foreign citizens on the territories under their jurisdictions. I would argue that if there is one policy that is not subject to extraterritorial influences brought about by globalization is immigration and citizenship. States still reserve overwhelming, and, in many cases exclusive, command over the inflow of foreign nationals, be they visitors or workers. The United States is a prime case in point especially considering the view of the rest of the world that globalization is essentially an American phenomenon. The rules for almost any foreign national seeking entry into the US are some of the most stringent in this so-called global open society of ours. Only a privileged few have the right to set foot on American soil without the need to obtain a visa. Citizens of 27 mostly rich, industrialized countries included in the US Department of State’s

Visa Waiver Program<sup>3</sup> can avail themselves of this possibility for tourist purposes only. When it comes to the right to work in the American labor market, visas are automatically imposed and the rules for obtaining them are even more cumbersome. Canada is the only other country whose citizens have more generous entry terms for visiting, studying and working, but that is a consequence of a historical tradition of close friendship between the two North American neighbors. This fact alone refutes many of the arguments embracing the notion of a new global order in which people can freely move or settle anywhere with the state being powerless in forestalling such tendencies. Canada, while more welcoming of immigrants than the United States, is equally in charge of controlling its immigration flows, with yearly quotas established for the admittance of foreign nationals seeking to obtain permanent residence. Australia, with its insularity, makes no exception to imposing and maintaining strict immigration criteria. Japan, the epitome of technological modernity is ironically one of the most traditionally closed societies, fiercely guarding its national heritage, still reluctant to let foreigners in for reasons other than short-term employment. Securing Japanese citizenship for someone not born in Japan is almost an impossible endeavor. Even in the European Union, this experiment in globalization for some, the entry of third nationals (any nationals of a non-member state) is strictly regulated. As with many other policies in the EU, control over immigration is a dual responsibility of the national governments and the supranational institutions. The latter, however, are entrusted only with ensuring uniform technical standards (e.g., design of the visa stickers, duration of stays, etc.), while the former have the ultimate say in setting entry quotas or in the decision to allow anyone to enter a particular member state's territory. It is not rare that some member states are irked by the actions of others to allow foreigners to settle on their own territories. In the spring of 2005, Spain came under sharp criticism from some member states over the Spanish government's decision to grant amnesty to up to 700,000 illegal immigrants present in the country.<sup>4</sup> Germany and other countries feared that, once regularized, these immigrants would be free to move to other parts of the EU, putting a strain on national labor markets or on the generous social welfare and healthcare programs of some member states. This is an illustration of EU's immigration duality in the globalization age. The EU's philosophy of fostering free movement of people seems to apply mainly to the natural born citizens of its member states. When it comes to immigrants who attain the citizenship of a member state, such ideals are quickly forgotten under the urgency of protecting the social and economic rights of the natives.

Statehood is a salient and attractive proposition for many ethnic groups which see themselves as trapped in foreign lands. The resilience of the state has been, in my view, seriously underestimated. Suter (2003) suggested that the Westphalian system of nation-states has run into problems, but then again, it has never been free of problems or challenges to begin with. I would seriously contradict his view that "the future belongs to globalization" (p. 147). Contrary to the popular belief that globalization has eroded the appeal of the nation-states, these have only grown in numbers. Global governance is a "delusion."<sup>5</sup> The nation-state gives ethnic groups supreme recognition of historical claims of attachment to a certain territorial space. It relieves them of the stigma of peoples not considered worthy of living in their own lands or of the oppression of the master nation in a forced federation (e.g. the Russians in Soviet Union or the

---

<sup>3</sup> Visa Waiver Program (VWP). *U.S. Department of State*. Retrieved January 21, 2006, from [http://www.travel.state.gov/visa/temp/without/without\\_1990.html#2](http://www.travel.state.gov/visa/temp/without/without_1990.html#2).

<sup>4</sup> Spain's immigration amnesty ends. (May 7, 2005). *BBC News*. <http://news.bbc.co.uk/2/hi/europe/4526177.stm>.

<sup>5</sup> Jacques, M. (2004, November 12-18). Strength in numbers: Despite globalization, nation states are not in decline. *The Guardian Weekly*, pp. 6.

Serbs in Yugoslavia). We need look no farther than Europe to understand that statehood or nationhood is a coveted prize, which pales in comparison to any promised borderless, amorphous global economic order. This invention of Old Europe is still the dream of such ethnic or national groups as the Kosovars or the Basque in Modern Europe. They may never achieve total independence, but Montenegro, the uneasy partner of Serbia in the last living relic of former Yugoslavia, Serbia-Montenegro, is almost certain to achieve this status in a referendum scheduled for 2006.<sup>6</sup> Elsewhere in the world, Taiwan's barely veiled attempts to declare independence are evidence of the struggle of a nation to achieve the self-realization of a unit in a system of equals. Tiny East Timor's success in securing independence from Indonesia, granted under UN patronage (ironically the paramount ideal of world governance for global governance proponents), attests to the allure of statehood, even in today's globalized world. In Africa, Somaliland's secession from Somalia's lawless, failed state<sup>7</sup> or the Sahrawis' continuous confrontation with Moroccan authorities to have Western Sahara recognized as their land<sup>8</sup> are further testimony to the appeal of the nation-state. These cases breathe life into Hall's view that the "globalization thesis is desperately provincial in that it ignores the need for much of the world to have a state in the first place" (2000, p. 76).

Before I conclude this section, I would like to recapitulate and give a little nuance to specifics of some of the dimensions under discussion here. Transnational corporations (TNC) are perceived as entities breaking down barriers and locating in various corners of the world with little resistance from the governments of the nation-states in which they operate, facilitated by extensive communication networks through which they can exchange data nearly instantaneously (Scholte, 2003, p. 86). The liberal thinkers on globalization, or the optimists, would have us believe that the business interests of the TNCs are much more powerful than the political considerations of the nation-states for the latter to stand in the way of the former (Robinson, 1998, p. 574). Their commercial interests are overwhelming the capacity of governments to impose restrictions on TNCs since that would spell the end of investments by such companies in the respective countries. In consequence, we are witnessing the erosion of the state's power to regulate its market as it sees fit and at the same time a weakening of the role of the state as an actor in the global economy (Strange, 2003, p. 131).

By the same token, the telecommunications sector, which is inextricably linked to the global markets not only as a product, but also as a means of mediating commercial flows, is seen as a catalyst for the transnational disintegration of borders that normally stand in the way of social or political contact (Rifkin, 2004, p. 191). Specifically, the new digital communications technologies (the microcomputer, the Internet, the World Wide Web, satellite relays, cellular phones, etc.) permeate the social, political, cultural and commercial facets of nation-states, contributing to the formation of transnational networks of interests that are independent of the influence of the nation-state (Castells, 1996, p. 171).

While there is some truth to that claim, the reality is murkier than the optimists tend to believe. It must be conceded to the liberal thinkers that the nation-state, under the pressure of the globalizing forces, has lost some of its powers in regulating and governing over issues that previously had been its exclusive jurisdiction, like the flows of goods and capital, currency fluctuations, pricing, which are now free of the encumbrances of strict governmental controls,

---

<sup>6</sup> Montenegro picks national symbols. (July 13, 2004). *BBC News*. <http://news.bbc.co.uk/2/hi/europe/3889355.stm>.

<sup>7</sup> Somalia: A state of utter failure. (December 17, 2005). *The Economist*, p. 46.

<sup>8</sup> Western Sahara: Give it another try. (September 24, 2005). *The Economist*, p. 56.

especially since they are conducted in real time with the use of advanced micro-computing technologies. The skeptics argue that TNCs and financial institutions, however, do not operate solely in the virtual territory of monetary and stock exchange transactions (Giddens, 2003, p. 63). They need to have the guarantee that their investments and exchanges will be protected legally by the governments of the countries in which they operate (Sil, 2003, p. 286). As Wade (1996, p. 61) indicates, “companies are rooted in national home bases with national regulatory regimes.” It is here that the state shows its resilience, despite the optimists’ argument that it has become an obsolete and cumbersome structure.

Political and social processes are to some extent also subjected to networks of interested groups running above and/or below governmental controls. It may be true that in some domains these interest groups are able to completely bypass the state in achieving their objectives, however, when it comes to the protection of the framework within which their activities unfold, in a territorial sense, the nation-state is the primary guarantor of legal processes (Rifkin, 2004, p. 216). NGOs, human rights groups, educational institutions, grass-roots organizations may each band together for a common goal in various ways, but essentially through some of the same communication networks that the financial institutions and TNCs employ, challenging the state in courts of supraterritorial jurisdiction, like the International Court of Justice, the European Court of Human Rights or the European Court of Justice (the latter with jurisdiction only in the EU). When it comes to the application of court decisions in national legislation, these are often times subject to interpretation from and may be overruled by national courts.

To illustrate the role of the educational system and its impact on national development in the context of new digital technologies, taking my cue from Castells (1996, p. 356), I will contend that the universities are the very first units of innovation that precede any real technological revolution. It is in the labs and testing rooms of universities that pilot projects for the invention of new forms of technologies unfold (e.g., ARPANET, later the Internet, setup in 1969 at UCLA), often times through grants received via various channels from government funds. These innovations regularly end up as patented inventions, later entering the process of mass production for the various purposes for which they were devised, ultimately benefiting the public at large. Castells calls the creative environments that the universities represent “*milieux of innovation*,” as a telling symbol of their intrinsic vocation for technological progress. In addition, not only are universities centers for innovation, but they are the frontrunners in the promotion of the new technologies, especially ICT, as the students are the ones who are most likely to use communications technologies for academic, research or recreational purposes and thus contribute to the diffusion of ICT outside the walls of their academic institutions (p. 391). It follows, then, that there exists a dual relationship between the educational system and communication technologies, each one feeding off of and supporting the other. The prestige of the nation-state in the international arena is partly dependent upon the quality of technologies developed, tested and implemented by universities. Meanwhile, the state tends to protect its investment in innovation by fostering a climate favorable to research and development and by encouraging the patenting of technologies to reflect their national origin. Since, as mentioned above, the educational system is embedded in the national culture, the nation-state is the direct contributor and, at the same time, the main beneficiary of the advancement of ICT through education. These dynamics ensure that the state enjoys political and cultural continuity by benefiting from a pool of skilled professionals and a technological base that is conducive to national progress.

The significance of the debate between the optimists and the skeptics is that it underlines an evident split between those who believe that the state is an outdated entity and those who think that it is still a powerful actor in the global economy and society. Whichever view is considered, it is evident in one way or another that the state has not lost its relevance in the whirlwinds of the deep economic, political and social transformations that we are now witnessing.

### **A Globalized or a Globalizing European Union?**

At the risk of sounding too ambiguous, for now, I will give a simple answer to the question above: both scenarios apply. This may appear to contradict my own statement in the previous section about the buoyancy of the nation-state in the face of globalization even if it is part of an organization such as the EU. In the remainder of this paper, however, I will explain this apparent contradiction and provide a definitive answer at the end.

The European Union is not the typical territorial construction comparable to any nation-state in existence today. It is a loose assembly of member states which pooled together a degree of their sovereignties so that interests that cannot be resolved by states alone are referred for resolution to the supranational level. It is a unique structure that essentially overarches the relationships among its constituent member states. If we consider again Giddens' two key elements in the dynamics of globalization, "local involvements" and "interaction across distance," the EU does have the attributes of a globalizing force. In the geophysical sense, the EU spans exponential combinations of distances among its distinctive component units. Linking point A with point B with point N in a commonly shared space creates the impression of a globalizing actor, because it breaks down the barriers of the traditional international order by eliminating physical borders among its member states that stay in the way of free movement of people, goods or services. In the socio-politico-cultural-economic sense, it stimulates a vast array of interactions that occur within its space. Decisions taken in one location of the union can have an impact on other locales in the shared space because they are filtered and then diffused through the supraterritorial mechanisms imposed over the myriad of segments forming this mosaic-like structure.

But this may simply be construed as regionalization or "Europeanization," since these manifestations are confined to a number of members in a relatively constrained continental area. If the EU's influence were only limited to its internal environment, then it would be plausible to call it as such. In fact, the EU has a tremendous ability to project its political values and economic strength outside its frontiers. Talking of EU's clout in the world, Leonard (2005, p. 54) speaks of a "Eurosphere" which counts no less than 109 countries, including the current member states. Accordingly, apart from the countries that are already scheduled to join it, are in membership talks with it or have been granted candidate status by it, the EU's zone of influence extends into the Western Balkans, the former Soviet Union, North Africa, the Middle East and Sub-Saharan Africa. Whether offering the prospect of membership, trade agreements, development aid, structural funding, education exchange schemes, even peacekeeping operations, the EU weighs more in the balance of global dynamics than it gets credited for. Taking education as a non-political example, I would point to one of the oldest educational programs that the European Commission has promoted. TEMPUS,<sup>9</sup> set up in 1990 and renewed

---

<sup>9</sup> EUROPA-Education and Training-The Tempus programme.  
[http://europa.eu.int/comm/education/programmes/tempus/index\\_en.html](http://europa.eu.int/comm/education/programmes/tempus/index_en.html). Retrieved January 22, 2006.

three times since then, is a program oriented towards cooperation between the EU and the countries of the “Eurosphere” in the field of higher education. Through the projects designed within the program, the EU seeks to grant technical assistance for modernization of the higher education practices (e.g., good university management, quality assurance, etc.) in the partner countries, to develop academic “people-to-people” networks for exchange of expertise, to foster mutual cultural understanding, to provide training and assistance for academics teaching in participating countries and to help universities disseminate knowledge outside their institutions.

This is a socio-cultural facet of the EU’s soft power, but Europe has even more powerful tools at its disposal, particularly in the economic domain, to persuade entities into compliance with its norms, extending its reach across the Atlantic and thwarting the intentions of some of the most recognizable American corporations. When in 2000 a \$45 billion merger between American avionics manufacturers GE and Honeywell was approved by the US Department of Justice’s Anti-Trust Division, none of the executives in the two companies had any inkling that they were violating stringent EU competition regulations. Because GE was financing deals for airplane manufacturers in Europe, the merger had to be approved by the Directorate General for Competition, the antitrust branch of the European Commission. To the surprise of the American CEOs, the then Commissioner for competition, Mario Monti, rejected the alliance over concerns that the two corporations could engage in “bundling” services into securing deals from prospective clients, whereby GE would demand that the contracting European parties agree to buy Honeywell components before any deal could be concluded (Reid, 2004, p. 102). In the event, there was no recourse to Monti’s decision and what would have been the biggest industrial merger in history went sour before it even took shape.

In another high profile case that highlights the EU’s pull in the global market is the €497 million fine imposed on Microsoft in 2004 by the European Commission for the software giant’s abuse of its position on the software market. Microsoft was found in breach of EU antitrust laws for bundling the popular Media Player for audio-video files in the Windows operating system package sold in Europe.<sup>10</sup> One year later, the EU deemed that Microsoft had not fully complied with its demands and it warned that it would levy a daily fine of up to €2 million if the latter would fail to take corrective measures.<sup>11</sup> It must be conceded that to some degree these rulings may have a flavor of political jockeying in that the EU, as a unitary whole, is attempting to position itself as a an actor on equal footing with the United States on the world stage. But this significance should not be overstated, as the Commission has not hesitated to penalize European corporations that run afoul of its orders, such as pharmaceutical companies Roche<sup>12</sup> and Bayer<sup>13</sup>.

Europe’s emergence as a global power does not become obvious solely from a show of its legalistic muscle. For instance, its presence in the form of investments in America’s industrial, financial and service markets, is just as prominent as America’s presence in Europe. Rifkin (2004) provides an impressive list of the European giants that have gained a significant market

---

<sup>10</sup> Microsoft hit by EU record fine. (March 25, 2004). *CNN.com*.  
<http://www.cnn.com/2004/BUSINESS/03/24/microsoft.eu/>.

<sup>11</sup> EU threatens Microsoft with daily fine over competition ruling. (December 22, 2005). *EUBusiness*.  
<http://www.eubusiness.com/Competition/051222105047.jwvoo8xa>.

<sup>12</sup> EU Commission issues fine in citric acid case. (December 5, 2001). *Roche-Corporate Media News*.  
<http://www.roche.com/media-news-2001-12-05-e.pdf>.

<sup>13</sup> EU fines likely for Bayer and Chemtura. (December 19, 2005). *Indymedia Cambridge, UK*.  
<http://www.indymedia.org.uk/en/regions/cambridge/2005/12/330280.html>.



share in the US economy in recent years. It is an interesting dynamic that makes one wonder why anti-globalization advocates never pick on Europe's Bertelsmann, the multimedia and publishing giant, as the embodiment of global capitalist imperialism, but prefer to bash McDonalds or Coca-Cola as the icons of economic and cultural homogenization. I think it has to do with the popular identification of America's economic policies as the extension of its politico-military arm which projects the image of a country bent on racking up profits and advantages of many sorts at any costs without showing sensitivity for other actors' interests or grievances. Europe, in turn, is less obtrusive and rarely sparks such visceral reactions because it chooses not to assert its power through military means, but rather through persuasion, negotiation and cooperation. Many people are clueless about the ways in which a corporation like Bertelsmann touches their lives, from the newspapers, magazines or books they read to the movies they watch or video games they play, and have no idea that they are indulging in products promoted by a European seller. But McDonalds is immediately associated in anyone's consciousness with American hegemony, even though local outlets are actually owned and operated locally by Frenchmen, Brazilians, Kenyans, Filipinos, etc.

In political terms, the EU has yet to be as firmly established as a global power as it is in economic realm. It is, however, quietly and gradually emerging as a political actor in world affairs, but it still has a long journey ahead of it. In issues such as environmental protection or enhancing the rule of law, many countries, particularly in the developing world, follow the EU's lead, because they already count on or know that they can look forward to further development funds if they emulate the EU in such matters as the Kyoto Protocol or the International Court of Justice. The promise of financial aid and equitable economic offers are much more enticing proposals than sword brandishing, coercion or bullying which, unfortunately, so often accompany American foreign policy. In some respects, the EU is still tentative in its political endeavors, such as its involvement in the seemingly intractable conflict between the Palestinians and the Israelis, in engaging Russia over its handling of the war in Chechnya or in dealing with Iran's nuclear program because it lacks the unified voice of a common foreign policy. A constitutional treaty would have endowed the EU with more political clout abroad, but it is still possible for it to achieve such status even in the absence of a constitution. Another way in which EU has a political global appeal is its model of pooled sovereignty. As I explained in the previous section, some ethnic groups within Europe seek sovereignty in a system that is moving away from the "classical conception of external sovereignty" (Keohane, 2002, p. 744). In the recent Canadian election campaign, however, the Bloc Quebecois's candidate, Duceppe, referred to the EU as a model that could be emulated by Canada, should Quebec achieve its decades-long aspiration for independence if the French Quebecer separatists have their way in a future referendum.<sup>14</sup>

Militarily, the EU is indeed a dwarf on the global stage, but the question is whether it needs to become a military power. The EU's philosophy of spreading and maintaining peace, human rights and the rule of law contradict the doctrine for the use of force. The Yugoslav wars, the Kosovo conflict and the American invasion of Iraq highlighted not only a deep split within the union as to what the appropriate response should have been but also the reluctance to commit

---

<sup>14</sup> English debate transcript. (December 16, 2005). CBC-Canada Votes 2006 – Voter Toolkit. [http://www.cbc.ca/canadavotes/voterstoolkit/debate\\_trans.html](http://www.cbc.ca/canadavotes/voterstoolkit/debate_trans.html).

\*Quebec came close to separating from Canada in a 1995 hair splitting referendum that caused deep divisions among Quebecers.

troops for combat operations. The EU would rather send forced arms for post-war peacekeeping operations, but usually only with the UN's stamp of approval. It has taken a greater role in its immediate vicinity, as in Macedonia or Bosnia-Herzegovina, but has not ventured farther than that. Obviously, member states of the EU have sent troops to Iraq, but doing so only enforces the power of the states in controlling their means of coercion and particularly highlights the lack of a coherent European common foreign policy. The US is still the uncontested military global power, and the EU, for the time being, can do very little in trying to reign in America's penchant for the use of brute force.

What about the threat globalization poses to EU's vibrancy and continued influence in the world? In recent months, a string of leaders in the EU have rushed to expose the looming problems that the EU has to confront in dealing with globalization. A healthy dose of apprehension about global events is a good means to keep policy-makers connected to the outside world and engaged in proposing solutions to the problems of the European public. Ranging in tone from wary to bold, statements on globalization have been on high officials lips since the failed referenda in France and the Netherlands. Fearing that the lack of a constitutional arrangement for Europe would leave it vulnerable to global pressures, leaders have adopted a mix of hand-wringing and morale-boosting approaches to push governments into action. Prime Minister Blair gravely spelled out the need for Europe to have a "vision on how to meet the challenges of globalization" and that "Europe needed to embrace globalization."<sup>15</sup> The optimistic Danish premier, Anders Fogh Rasmussen saw in globalization an "opportunity for everyone, not a threat" and urged the Europeans to "tackle globalization on the offensive."<sup>16</sup> The pensive Commission chief, José Manuel Barroso in a similar vein, highlighted the EU's potential and pondered that "even the biggest states don't have the leverage to manage globalization, but the EU can add strength that no individual state shows."<sup>17</sup> Not coincidentally, all these statements came in the preceding days of an EU high level ministerial meeting in the fall of 2005, after a summer which saw Europe's constitutional future cast into doubt. The textile "war" with China, following a surge in exports from the Asian manufacturer that led to EU's strict enforcement of the quotas agreed for Chinese garments,<sup>18</sup> only heightened the anxiety about Europe's ability to stave off competition from emerging markets and protect its high-paying manufacturing industries from the pressures of remote low-cost manufacturing powerhouses.

This sudden awareness of and urgency about globalization is rather comical and misplaced in channeling efforts to carry out economic programs or reforms. Neither does it do much good for the public's comfort with the whole notion of radical changes necessary in order to appease a menacing outside force that has no palpable shape or concrete conceptual substance. The problem should not be presented as a helpless Europe pitted against the merciless globalizing world. Europe, after all, is itself a globalizer, as my brief analysis above shows. Instead, the leaders of Europe should focus on the need to change Europe from within, to convince the public that embracing reform is a catalyst for the future sustainability of Europe's economies and social models, not because China or India loom large on the horizon. In all fairness, China and India

---

<sup>15</sup> Bilefsky, D. (2005, October 27). Blair says EU must modernize or lose out. *International Herald Tribune*, pp. 1.

<sup>16</sup> Rasmussen, A.F. (2005, October 25). Europe needs to embrace reform. *International Herald Tribune*, pp. 6.

<sup>17</sup> Barroso urges EU unity in the face of globalization. (October 26, 2005). *EUPolitix.com*.

<http://www.eupolitix.com>.

<sup>18</sup> EU warns China over textile export explosion. (March 17, 2005). *EUBusiness*.

<http://www.eubusiness.com/Trade/050317153653.lfdogpvs/view?searchterm=china%20textile%20quota>.

should pose some concern for Europe's leaders. Europe's governments should keep their guard up when it comes to economic competition from these two countries. But China and India are nowhere near the standards embodied by Europe's main "rival" targets, the US and a Japan re-awakening from a decade-long economic slump.<sup>19</sup> It is in relation to these partners in the triad that the EU should conceive of its power of innovation, transformation and growth. China and India, together accounting for one third of Earth's population, the first an autocratic political system, the second a large somewhat dysfunctional democracy, have deep internal problems that shadow their rise in the global economy. The biggest of all is poverty, a veritable "political bomb," as Saul called it (2005, p. 206). China's lax enforcement of environmental regulations and atrocious industrial standards, particularly in the mining sector (reminiscent of the disorganization that plagued the Soviet Union) are further obstacles in the long-term sustainability of its economic growth. India's sectarianism undermines the manageability of its democratic structure and though it excels in the high-tech industry, it has not been too successful in establishing a diverse industrial sector that can truly make it a global power. Their positions in the United Nations Conference on Trade and Development's *Trade and Development Index* country ranking illustrate the overall shortcomings of the two "rising powers." China shows up on place 51, well below the lowest ranked EU member, tiny and "poor" Latvia (36), and even below soon-to-be member Bulgaria (42). India is even further down the ranks, at number 90.<sup>20</sup> As Saul points out, China and India are firm believers in the "rigid defense of the Westphalian system of national sovereignty" (2005, p. 207), having as primary objectives the safeguarding of national political and economic interests which doesn't make them any less vulnerable to globalizing forces than countries in the Western world. Furthermore, they trade more with one another than with the rest of the world (p. 209), in a pattern that resembles the triad dynamics to which I alluded above, which makes them regional, more so than global players.

### **A Model of Governance for the Rest of the World?**

What does all this say about the possibility of other regions to emulate the EU as a model of political and economic governance? Its appeal for the emergence of other regional arrangements is real, but the materialization of such scenarios is riddled with enormous difficulties. In Asia, nationalistic rivalries and the absence of even shared democratic values that underline the European ethos prevent a close rapprochement of the Asian countries in a union similar to the EU. Suffices to mention China's resentment of Japan (the two major players in the region) over the historical interpretation of past events to conclude that Asia lacks an integration duo such as the Franco-German engine was in the EU. In Africa, the dismal economic situation, the chronic poverty and underdevelopment, the continued tribal warfare and the presence of failed states in the Sub-Saharan region, each and all put together, make it impossible to transpose even a remote semblance of a European-style union. Most of Central and South America's profligate, corrupt or repressive governments (with the relatively happy exceptions of Chile and Costa Rica) coupled with guerilla warfare and illicit narcotics production squander any remote opportunity of such a union taking root. It can be safely concluded that the EU is destined to remain a unique integrational masterpiece borne out of conditions and circumstances specific to a time and place

---

<sup>19</sup> Watts, J. (2005, November 25-December 1). The sun also rises. *The Guardian Weekly*, pp. 17.

<sup>20</sup> UNCTAD. The Trade and Development Index: Country ranking. Retrieved December 26, 2005 from <http://www.unctad.org/Templates/Page.asp?intItemID=3582&lang=1>.

that cannot be replicated in full elsewhere. However, the EU can still serve as an ideal to which other regions could aspire. And if not fully imitable, at least some of its core values are still universal precepts that, in the right environment, can flourish.

In essence, the EU acts as an attraction pole for those who share its set of ideals and values, but its distinctiveness from past unions attempted in history, is that it does not resort to coercion to spread those ideals and values. Too often, however, Europe is oblivious to its global peaceful power of attraction. If it is to endure as a guiding beacon, I would say that the EU has to look within its borders to find the sources of its malaise and discontent that stay in its way towards an even greater role in the global order. By way of conclusion, if I had to answer the question I posed in the title of this article, I would say that Europe is more of a globalizer than a victim of globalization. This should play to Europe's advantage if its leaders will know how to use the political mechanisms, economic force and the potential of its reservoir of educated and technologically savvy Europeans.

## References

- Barber, B.R. (1995). *Jihad vs. McWorld*. New York: Times Books.
- Bhagwati, J.N. (2004) *In Defense of Globalization*. Oxford: Oxford University Press.
- Boyer, R. (1996). The Convergence Hypothesis Revisited: Globalization but Still the Century of Nations? In S. Berger & R. Dore (Eds.), *National Diversity and Global Capitalism*, 29-59. Ithaca: Cornell University Press.
- Castells, M. (1996). *The Rise of the Network Society*. Malden: Blackwell Publishers.
- Giddens, A. (2003). The Globalizing of Modernity. In D. Held & A. McGrew (Eds.), *The Global Transformations Reader: An Introduction to the Globalization Debate*, 60-66. Cambridge: Polity Press.
- Hall, J.A. (2000). Globalization and Nationalism. *Thesis Eleven*, 63, 63-79.
- Hall, J.A. (2003). Nation-States in History. In T.V. Paul, G.J. Ikenberry, & J.A. Hall (Eds.), *The Nation-State in Question*, 1-26. Princeton, NJ: Princeton University Press.
- Held, D. & McGrew, A. (2003). *The Global Transformations Reader: An Introduction to the Globalization Debate*. Cambridge: Polity Press.
- Inglehart, R. (2003). Technological Change, Cultural Change and Democracy. In R. Breton & J.G. Reitz (Eds.), *Globalization and Society: Processes of Differentiation Examined*, 129-137. Westport: Praeger Publishers.
- James, H. (2001). *The End of Globalism: Lessons from the Great Depression*. Cambridge: Harvard University Press.
- Keohane, R.O. & Nye, J.S. (2000). Introduction. In J.S. Nye & J.D. Donahue (Eds.), *Governance in a Globalizing World*, 1-41. Cambridge: Visions of Governance for the 21<sup>st</sup> Century.
- Keohane, R.O. (2002). Ironies of Sovereignty: The European Union and the United States. *JCMS*, 40(4), 743-765.
- Leonard, M. (2005). *Why Europe Will Run the 21<sup>st</sup> Century*. New York: Public Affairs.

- Moore, M. (2003). *A World Without Walls: Freedom, Development, Free Trade and Global Governance*. Cambridge: Cambridge University Press.
- Reid, T.R. (2004). *The United States of Europe: The New Superpower and the End of American Supremacy*. New York: The Penguin Press.
- Rifkin, J. (2004). *The European Dream: How Europe's Vision of the Future is Quietly Eclipsing the American Dream*. New York: Jeremy P. Tarcher/Penguin.
- Robinson, W.I. (1998). Beyond Nation-State Paradigms: Globalization, Sociology, and the Challenge of Transnational Studies. *Sociological Forum*, 13(4), 561-594.
- Rugman, A. (2000). *The End of Globalization*. London: Random House.
- Sassen, S. (1996). *Losing Control? Sovereignty in an Age of Globalization*. New York: Columbia University Press.
- Saul, J.R. (2005). *The Collapse of Globalism: And the Reinvention of the World*. Toronto: Viking Canada.
- Scholte, J.A. (2000). *Globalization: A Critical Introduction*. Basingstoke: Palgrave.
- Scholte, J.A. (2003). What is "Global" about Globalization? In D. Held & A. McGrew (Eds.), *The Global Transformations Reader: An Introduction to the Globalization Debate*, 60-66. Cambridge: Polity Press.
- Sil, R. (2003). Globalization, the State and Industrial Relations: Common Challenges, Divergent Traditions. In T.V. Paul, G.J. Ikenberry & J.A. Hall (Eds.), *The Nation-State in Question*, 260-287. Princeton: Princeton University Press.
- Steger, M.B. (2003). *Globalization: A Very Short Introduction*. Oxford: Oxford University Press.
- Suter, K. (2003). *Global Order and Global Disorder*. Westport: Praeger Publishers.
- Wade, R. (1996). Globalization and Its Limits: Reports of the Death of the National Economy are Greatly Exaggerated. In S. Berger & R. Dore (Eds.), *National Diversity and Global Capitalism*, 60-88. Ithaca: Cornell University Press.

# **THE ROLE OF THE EU COMMON AGRICULTURAL POLICY ON THE FREE TRADE AGREEMENT – THE CASE OF MERCOSUR**

**MARIJANA CRISTINA PASATOIU<sup>1</sup>**

## **Abstract**

This article is touching upon the role of Common Agriculture Policy (CAP) on the free trade negotiations between the EU and Mercosur, which has turned out to be quite problematic for the decision-making and for the development of member countries of Mercosur. The theme researched is socially enquired and explained from two different theoretical approaches (economic nationalism and neo liberalism) that analyse how states act in relation to trade, power and hegemonies. The theoretical analysis addresses empirical data relating to both the trade relations between the two regional players as well as the history of the CAP in order to demonstrate the traditional role that agriculture holds within the EU and its indirect impact and influence towards free trade negotiations.

The article is placing under criticism the decision-making and the contradictory policy of the EU in its free trade negotiations with Mercosur.

**Key words:** Common Agricultural Policy, Free Trade Agreement, Mercosur

**JEL classification code:** F – International Economics – F5 – International Relations and International Political Economy

---

<sup>1</sup> Associated Assistant. PhD researcher. Faculty of Economics Craiova. E-mail: [pasatoiu cristina@yahoo.com](mailto:pasatoiu cristina@yahoo.com).

## **Introduction.**

The Cooperation relations between the Mercosur and European Union hold a rich-long historical background which dates back from 1991, soon as the Asuncion Treaty was signed in between the members of the Mercosur free trade area. The EU economic cooperation interest was strengthened by the US initiative of creating the biggest trading block – Free Trade Area of Americas (FTAA) becoming a common strategy (both of EU as well as Mercosur ) to counter weighting the US hegemony and dominance.

In spite of the strong US influence in the region, it is important to stress that EU stands as the biggest recipient of agricultural products from Mercosur region. The FTAA was perceived as a threat to Community interests and generated the official recognition of the cooperation interest by signing in 1995 the Interregional Framework Co-operation Agreement – which put on the agenda as a main objective to establish a free trading area in between the two trading blocks.

If agreement would have been reached between the two trading blocks, it would have resulted to the creation of the biggest free trading area with nearly 700 million consumers, covering a surface of 12 million km<sup>2</sup>. However, in spite of all these development opportunities the results of over 20 rounds of negotiations are non-conclusive as far as the agreement is being hampered by the discussions over the agricultural issues and concessions over public procurement and services.

The EU haunts two different political strategies; as a member in the WTO on the international level, they advocate free trade and liberalization but on the other hand they still try to protect their own markets as we can still see in their common agriculture policy (CAP). The current discussion about signing the Free Trade Agreement is the best evidence for the cleavage in the EU because it is contrary to the CAP.

The puzzling question, which is also brought under research in this article is that: if EU declares that it wants to support the development of the Mercosur, how come the negotiations related to agricultural issues, which could lead to further development of Mercosur, still lag behind?

## **Theoretical approach to the subject.**

There is an ongoing discussion in international relations about neo-realism and neo-liberalism and their relevance in the international politic economy. According to Keohane the political realism and neo-realism is deeply embedded in western thought. It is important to have that in mind before it is possible to understand and criticize our own tradition of thinking about international relations. Keohane argues that it is important to examine prevailing assumptions that might be taken for granted. Another important thing according to Keohane is also that world politics and values changes over time, so there is no guarantee that a theory will remain valid in the future<sup>2</sup>. I have chosen some of the main principles, which I think are important for this article. Afterward I will discuss the critical theory opposed to the two orthodox theories.

---

<sup>2</sup> Keohane, Robert. O. (Edit.) (1986): “Neorealism: and its critics”. Columbia University Press. New York, pp.4-5.

## Anarchy and State

The neo-realists and neo-liberal institutionalists share the assumption that the world system is anarchical and that the definition of anarchy does not mean chaos but the absence of a political world authority. They emphasise the importance of anarchy as a determinant for the behaviour of international politics. In comparison to the realist view, the neo-liberal institutionalists advocate for a world government or international institutions like the WTO, IMF and WB.

While the neo-realists, according to the neo-liberalists view, overemphasize the importance of anarchy, the neo-realists argue, that the neo-liberal institutionalism underestimates the impact of survival of the nation as motivation for state behaviour. The two theories focus on different issues, where realism and neo-realism emphasise state interests, national security and power among states, the neo-liberalists focus on international trade and international relations. In contrast the critical approach focuses more on transnational social forces and power relations in the global capitalist production system (Gill & Law 1988 p. 78). Neo-realists argue that the state is the key actor in international relations. Its main goals are to maximize its power, state interests and security. The neo-liberalists also think that the state is the main actor in international relations, but beside this, they argue that other actors, like international organizations, INGO's or Trans National Companies are important as well. The state, in the neo-liberalists view, should provide a framework for free trade for example laws for protecting property rights.

Taking these assumptions into account, one of the critics against neo-realism and one of its weaknesses is that it underestimates the importance of other actors in the international system.

The theory does not comply with the present situation, where states are becoming more permeable, because of the multitude of relationships across borders that do not involve states. The states have no longer control over the transnational actions. Another neo-liberal critic of the state-centric theories is that there is an increasing interdependence among states, e.g. through trade and environmental issues. Also the neo-liberalists' criticize neo-realism in arguing that the states are becoming less concerned with power and security and more concerned with economic growth and social security and welfare in the state.<sup>3</sup>

Colclough and Manar argue that neo-liberalism reinforce the position of authoritarian forms of production with arguments for strongly centralized state power, even when it provides non-democracy<sup>4</sup>.

According to Nye and Keohane, realism is not adequate anymore, because it no longer can be assumed that interstate relations always are most important. The decisions and actions of non-state actors can affect our lives as much or even more than the decision of states. It can no longer be assumed that the states have the power to regulate the non-state actors.<sup>5</sup>

---

<sup>3</sup> Grieco, Joseph. M. (1993): "Anarchy and the limits of cooperation: A realist critique of the newest liberal institutionalism". In Baldwin, David. A. (1993): "Neorealism and neoliberalism, the contemporary debate". Columbia University Press, p.119.

<sup>4</sup> Colclough and Manor (1998), p.55.

<sup>5</sup> Brown, Chris (2001), pp.38-39.



Not considering other actors to be important in IR, the neo-realists also have trouble accounting for the changes in the world politics, where international organization and non-state actors are playing a still bigger role.

According to Keohane, if neo-realism wants to remain an adequate theory in IR it has to take into account the limitations of anarchy. But it also has to consider the changes in functional capabilities of governments, the role of information and the importance of international institutions and regimes. The strength of realism lies in analyzing the behavior of states. The realist theory would be adequate for this; because it concentrates on why the states do as they do, with focus on the national interests and the survival of the nation. Another strength of realism is that the complexity of the world is reduced to manageable proportions; however this is not giving a true picture of the world as it looks today.

### **Cooperation and Gains in International Relations**

Like the neo-realists, neo-liberalists are interested in maximizing their interests through cooperation between states, but the Neo-realists think *“it is harder to achieve, more difficult to maintain and more dependent on state power”*<sup>6</sup>. Neo-liberalists argue that cooperation is not difficult to achieve when the states have mutual interests. They stress the absolute gains from cooperation, while the Neorealists focus on the relative gains. This means that the neo-liberalists emphasizes on the long-term relations, whereas the Neo-realists look upon the short-term relationship and the gain relative to other states’ gain in the system<sup>7</sup>.

### **Mercantilism and Economic Liberalism**

In International Political Economy the realist view, mercantilism, argues that in the relationship between economics and politics is decisive, because it is the political decisions that guide the economic interests. They underestimate the importance of the economics, which they call low-politics and put emphasis on power, interest and security, which fall under high-politics. According to Brown this distinction between high and low politics does no longer count, because what were once low politics are now high politics of IPE.<sup>8</sup>

Looking upon the market the two theories take on different assumptions. The economic liberalists argue that the market economy is an autonomous sphere of society. Economic liberalists do not take into account the social domain of the state; they concentrate on trade conditions and competition without considering if the country is competitive.

Economic liberalism believes that the cooperative economic relations will give a positive-sum game, where all states gain.<sup>9</sup> The mercantilists argue that the nature of economic relations is the zero-sum game, where one state's loss is another state's gain.

---

<sup>6</sup> Baldwin, David (1993), p.5.

<sup>7</sup> Jackson & Sørensen (2003), p.179.

<sup>8</sup> Brown, Chris (2001), p.147.

<sup>9</sup> Jackson & Sørensen (2003), p.192.

## Critical Approach

Some of the deficiencies related to mainstream theory in IR, is the fact that they underestimate the concept of the state. The state has been regarded *a priori* as a singular concept in IR. Liberals emphasise the separation between states and markets. Politics is not to engage on the issue of market relations, therefore liberals disregard the interventionist state. Both realists and liberalist see the state as the main actor in an anarchical system. Marxist theories confront this postulate by introducing the state in a state/society complex, which has opened up for a variety of notions of the state in a more complex system<sup>10</sup>. The state is not just considered as a mere actor, but emphasis is placed on the actions made by the state and the underlying forces related to these actions. This is one of the principal strengths of Marxists theories in general. In the ahistorical worldview of realism, states are ever present given elements of world order but they are not subject to fundamental change. The strength of the critical theorists in contrast see different forms of state and world orders, which conditions of existence, principles and norms vary over time. The state is thus changeable over time and enters into constantly different contexts<sup>11</sup>.

## Common Agricultural Policy (CAP) and its influence towards free trade negotiations.

In order to provide an understanding of the current situation in the negotiation process between the EU and Mercosur emphasis is placed upon the EU position on the negotiations and the challenges. This requires some understanding of how the relationship between the domestic agricultural policy and the trade policy of the EU has developed. Skogstad points out that the institutional context within which trade policy is developed limits the flexibility that trade negotiators poses in the negotiation rounds. Within this context, the institutional and legal context of agriculture in the EU causes seriously *problematiques* to negotiation-process between the EU and the Mercosur<sup>12</sup>.

Agro-industrial groups within Europe are highly protectionist orientated and are lobbying against the further deregulation of markets. The farmer's organizations play an important role in this group. The lobbying against further opening the sensitive markets intensified greatly after the signing of the EMIFCA (European Union Mercosur Interregional Cooperation Framework Agreement) in 1994 and the European Commission's actions to obtain a negotiation mandate:

*“The major argument of agricultural interest groups against such a mandate had been that an engagement in concrete negotiations would have overloaded the EU agenda with respect to the pending reform of the Common Agricultural Policy (CAP), the issue of expanding the EU to the east and the fiscal discipline imposed by the monetary Union”*<sup>13</sup>

---

<sup>10</sup> Cox, Robert W. (1981), p.127.

<sup>11</sup> Sinclair, Timothy J. (1996): “Beyond international relations theory: Robert W. Cox and approaches to world order”. In: Robert Cox (1996), *Approaches to world order*. Cambridge University Press: Cambridge, pp.5, 7.

<sup>12</sup> Skogstad, Grace (1994), p.247.

<sup>13</sup> J3rg Faust (2004): “The European Union's Trade Policy towards Mercosur”. Working paper PEIF-7. See: <http://ies.berkeley.edu/pubs/workingpapers/PEIF-7-MERCOSUR.pdf>

Some of the member states are represented by heavy agriculture economies dependent on subsidies from the EU to keep production cost artificial low and in this way secure their competitive power. They are not interested in signing the agreement due to fear of losing competition on the European market in case there will be an opening for price competing products from low price producers, as in our case Brazil. This policy is strongly influenced by the mercantilist point of view where key issue is the protection and wealth of each state. They argue that it can be necessary to manipulate economic policies to maximize own interests. An example could be the subsidies that the EU poses on agricultural products and high tariffs on import goods.

The actions taken by the EU towards its agricultural policies do not favour developing countries; the institutional settings of the European agriculture are highly traditional and not value-free, but instead rooted in the conception of agriculture as a traditional part of Europe. It is a very sensitive area of production that gives rise to international conflicts in trade relations being also the key disagreement issue that is keeping the EU – Mercosur negotiations on hold for over a decade.

### **EU and Mercosur; the path followed by the two regional blocks towards a FTA**

EU started to show an interest in Mercosur, just few months after the signing of the Asuncion Treaty. *“The creation of Mercosur in 1991 favoured the EU’s preference for dealing with group of countries rather than on a purely bilateral basis<sup>14</sup>”*

The first formal political dialogue with Mercosur, started in May 1992 with the signing of the Inter institutional Cooperation Agreement between the Commission of the EU and the Mercosur Council.

In 1994 the European Commission and the governments of Mercosur member countries, agreed to start negotiating an interregional framework agreement. The negotiation talks took place during two rounds, in Brussels and Montevideo. After these rounds, the Commission presented the European Council the proposal for the European Union Mercosur Interregional Cooperation Framework Agreement.

The framework Agreement was signed by the Council members and the presidents of the Mercosur member countries in December 1995. The agreement took into consideration, not only trade in goods but also investment, property rights, service liberalization, government procurement, etc<sup>15</sup>. The ratification process by the parliaments of each actor involved was slow and lasted four years.

Meantime, a parallel process took place, and this was the European Commission lobbying for a tariff negotiation mandate in the European Council. After years of disagreements and discussions, mostly on the agriculture and industrial sectors, the mandate for negotiations was finally obtained

---

<sup>14</sup> J6rg Faust. *The European Union’s Trade Policy towards MERCOSUR*. Working paper PEIF-7. See: <http://ies.berkeley.edu/pubs/workingpapers/PEIF-7-MERCOSUR.pdf>

<sup>15</sup> European Commission . *Interregional Framework Cooperation Agreement between the European Community and its Member States, of the one part, and the Southern Common Market and its Party States, of the other part*. [http://europa.eu.int/comm/external\\_relations/mercotur/bacground\\_doc/fca96.htm](http://europa.eu.int/comm/external_relations/mercotur/bacground_doc/fca96.htm)

in September 1999<sup>16</sup>. An important thing to mention is that the decision was not a unanimous one. There were four commissioners that voted against the EU negotiation mandate, among them, the Commissioner for Agriculture – Franz Fischler<sup>17</sup>.

The further negotiations took place during the 1<sup>st</sup> Summit between Heads of State of the European Union, Latin America and the Caribbean, which took place Rio de Janeiro in June 1999 and had as main objective to set up a “strategic association” between the two regions. EU objective was to “*establish itself as a new actor of the international politics, and to reinforce multipolarity and multilateralism, given the growing hegemonic position and unilateralism by the US*”.<sup>18</sup>

The second Summit in Madrid in May 2002 between the heads of state and of Government of Mercosur and the EU, took place in Madrid, and had as main goal to “*intensify and deepen the existing political, economic, trade and co-operation relations between the two regions, in line with the Interregional Framework Co-operation Agreement*”<sup>19</sup> signed in 1995. During the summit the main discussions were focusing on further strengthening the political dialogue on matters of mutual interest on the international agenda, among others; sustainable development and peace and stability, conflict prevention, confidence and security building.<sup>20</sup>

The 3<sup>rd</sup> Summit in Guadalajara in May 2004 touched upon the same old subjects, without any progress in dealing with most arduous issues such as agriculture. The enlargement of the EU had an important impact on the general lack of political enthusiasm coming from the EU.

A progress in the negotiations failed to show itself even after the EU enlargement with 10 new member states ended, the only decision made being that to set a new deadline for the signing of the Agreement by May 2006, before the Doha Round talks of the WTO, deadline that as again not met when Brussels decided to wait for the results of the Doha Round multilateral negotiations. The WTO talks, which are focused on one of Mercosur main interest: farm subsidies and access to the rich countries agricultural markets the farm subsidies in rich countries and access to those markets have also been grounded for over a year due to the reticence of developed countries to comply with the demand from the so called G-20 to be more flexible regarding the agriculture controversy.

In conclusion the biggest divergent issue and most arduous in the negotiations is represented by the agricultural chapter, more specifically the protectionist policy promoted by the EU through its Common Agricultural Policy. “*This issue is increasingly dominating the agenda of trade negotiations, and the possibilities of deepening the agenda of the trade negotiations, and the possibilities of deepening and balancing trade links between the two blocs will largely depend on progress in this area*”<sup>21</sup>

---

<sup>16</sup> J6rg Faust. *The European Union’s Trade Policy towards MERCOSUR*. Working paper PEIF-7. See: <http://ies.berkeley.edu/pubs/workingpapers/PEIF-7-MERCOSUR.pdf>

<sup>17</sup> Ibid .

<sup>18</sup> Andrea Ribeiro Hoffmann, Closer, or further away from the “strategic partnership”? – Analysing the impact of EU enlargement to EU-Latin American Relationship. <http://home.iscte.pt/~ansmd/elas/RibeiroAndrea.pdf>

<sup>19</sup> European Commission, *Second meeting of Heads of State and of Government of the European Union and of Mercosur. Joint Communiqué*, [http://europa.eu.int/comm/external\\_relations/mercosur/ass\\_neg\\_text/ma05\\_02.htm](http://europa.eu.int/comm/external_relations/mercosur/ass_neg_text/ma05_02.htm)

<sup>20</sup> Ibid.

<sup>21</sup> G. A. Valadao. *The costs of Opting Out. The EU Mercosur Agreement and the FTA of the Americas*, Chap3. pp 96. Chaire Mercosur . 2004.

## Analysis.

There seems to be two reasons for the EU interests in the Latin American region: The political interest, seen primarily as being in opposition to the US control and to make the region more independent. Taking dependency into consideration this can be seen from different angles, which we will elaborate on in progress. The economic reason, if it should be taken into consideration, could be the large consumer market that Mercosur represents; however another and more obvious one must be the EU companies' possibility to get into the Brazilian market of recourses and cheap labour force. Looking at the different initiatives coming from the EU it is clearly seen that they represent contrasting elements.

Therefore there are several reasons for the results of the latest negotiations between EU and Mercosur, showing that Mercosur no longer represent as great a priority for EU as earlier, this could also be due to the decisions and actions internal in the EU. The forthcoming question must then be what are the reasons for Mercosur not to signing the FTA agreement?

Mercosur and its member countries have a long history of interdependency with other states. According to the neo-liberal theory of interdependency every country gains but one state will always be more dependent on the trade relation than the other. This situation does not represent a sustainable future for a developing country or region and could be seen as one of the reasons for Mercosur's avoidance for not signing the FTA.

Further more Mercosur's interest in striking a deal with EU is placed within the liberalization and easier access to the agricultural market, and as the Brazilian Ambassador to the EU in 1996, Jorio Dauster, mentioned in one of his speeches: *"if the issue of agriculture does not have a priority there will be no negotiations ...In the present conditions, the creation of a free trade area between the EU and Mercosur is not absolutely essential"*<sup>22</sup>.

Despite the promised benefits for both sides, there are few chances for significant changes to occur in the EU's protectionism in its agricultural sector which would favour Mercosur. Considering this, Mercosur countries should be more concerned that the signature of an agreement based on limited market access concessions for few products is not an important step forward. Mercosur needs a more valuable package-deal which could also provide instruments to protect its industry and embryonic services sectors which are important for the bloc members to go beyond the position of mere exporters of agricultural products.

During the Cardoso period there were several other aspects connected to this new way of thinking about the role of a region in international relations; however one could be the wish for less dependency on the US, as the EU states that they want to help the region get more independent. This can be seen in the way that Mercosur cooperate with other countries such as Africa and Asia in trade relations. It can also be seen in the results of Brazil not wanting to sign the FTAA due to another unequal deal, where Brazil imports more from the US than they export to the US.<sup>23</sup> In this case, the signing of the FTA with EU, Mercosur will not renounce to its demands, and will not sign an agreement for a Free Trade Area between the two regions, unless the EU comes with a equal proposal for easier access of Mercosur' agricultural products the following quote explains the tendency within Mercosur: *"the Mercosur countries would not be likely to remove*

---

<sup>22</sup> Gazeta Mercantil Latinoamericana, 27 October to 2 November 1996, p.3.

<sup>23</sup> Williamson, John (2003), p.112.

*their own barriers to European exports in sectors such as steel and textile without a compensation equal to their agricultural exports*<sup>24</sup>”

Until now the expectations of Mercosur in terms of economical relations with Europe were not fulfilled. The gains they expected from trade with European Union are lagging behind, because Mercosur member countries cannot export the products, as the EU has a comparative advantage due to the protectionist measures imposed by the common Agricultural Policy of EU, so even though EU says that they want to help promote economic development they do not give Mercosur a fair chance to do so by their high subsidies.

## References

Keohane, Robert. O. (Edit.) (1986): “Neorealism: and its critics”. Columbia University Press. New York, pp.4-5.

Grieco, Joseph. M. (1993 ): “Anarchy and the limits of cooperation: A realist critique of the newest liberal institutionalism”. In Baldwin, David. A. (1993): “Neorealism and neoliberalism, the contemporary debate”. Columbia University Press, p.119.

Sinclair, Timothy J. (1996): “Beyond international relations theory: Robert W. Cox and approaches to world order”. In: Robert Cox (1996), *Approaches to world order*. Cambridge University Press: Cambridge, pp.5, 7.

Jörg Faust. *The European Union’s Trade Policy towards MERCOSUR*. Working paper PEIF-7. See: <http://ies.berkeley.edu/pubs/workingpapers/PEIF-7-MERCOSUR.pdf>

European Commission . *Interregional Framework Cooperation Agreement between the European Community and its Member States, of the one part, and the Southern Common Market and its Party States, of the other part*. [http://europa.eu.int/comm/external\\_relations/mercosur/bacground\\_doc/fca96.htm](http://europa.eu.int/comm/external_relations/mercosur/bacground_doc/fca96.htm)

Jörg Faust. *The European Union’s Trade Policy towards MERCOSUR*. Working paper PEIF-7. See: <http://ies.berkeley.edu/pubs/workingpapers/PEIF-7-MERCOSUR.pdf>

Andrea Ribeiro Hoffmann, Closer, or further away from the “strategic partnership”? – Analysing the impact of EU enlargement to EU-Latin American Relationship. <http://home.iscte.pt/~ansmd/elas/RibeiroAndrea.pdf>

European Commission, *Second meeting of Heads of State and of Government of the European Union and of Mercosur. Joint Communiqué*, [http://europa.eu.int/comm/external\\_relations/mercosur/ass\\_neg\\_text/ma05\\_02.htm](http://europa.eu.int/comm/external_relations/mercosur/ass_neg_text/ma05_02.htm)

G. A. Valadao. *The costs of Opting Out. The EU Mercosur Agreement and the FTA of the Americas*, Chap3. pp 96. Chaire Mercosur . 2004.

Gazeta Mercantil Latinoamericana, 27 October to 2 November 1996, p.3.

Manuel Cienfuegos Mateo, Implications of European Union Enlargement for Euro-Mercosur relations, [http://selene.uab.es/\\_cs\\_iuee/catala/obs/working\\_ocasionals\\_archivos/beyond%20the%20enlargement/n\\_Cienfuegos.pd](http://selene.uab.es/_cs_iuee/catala/obs/working_ocasionals_archivos/beyond%20the%20enlargement/n_Cienfuegos.pd)

---

<sup>24</sup> Manuel Cienfuegos Mateo, Implications of European Union Enlargement for Euro-Mercosur relations, [http://selene.uab.es/\\_cs\\_iuee/catala/obs/working\\_ocasionals\\_archivos/beyond%20the%20enlargement/n\\_Cienfuegos.pd](http://selene.uab.es/_cs_iuee/catala/obs/working_ocasionals_archivos/beyond%20the%20enlargement/n_Cienfuegos.pd)

# THE ORIGINS OF EU AND THE FLIGHT FROM LIBERALISM

MIHAI-VLADIMIR TOPAN<sup>1</sup>

## Abstract

In this paper I try to refute the thesis that European integration – the way the European states embarked upon with the creation of The European Coal and Steel Community – was indispensable for the preservation of peace among the continent's nations. The main line of argument is that, instead, the integration process was a logical consequence of the reluctance of states to renounce domestic interventionist policies inherited from the war (and interwar) period. The beginnings of European integration are usually presented under the form of a dilemma: integrate or fight. I believe that this is a false alternative, and that the dilemma was actually a “trilemma”: integrate, fight or return to the sound policies of free trade and laissez-faire. Liberalism, that is.

**Keywords:** interventionism dynamics, European integration, European Coal and Steel Community

**JEL:** F15; F5; B53.

---

<sup>1</sup> Lecturer, PhD Candidate, International Business and Economics Department, Academy of Economic Studies – Bucharest, mihai.topan@rei.ase.ro

## **Integrate or Fight: a Genuine Dilemma?**

Should anyone question the benefits of European integration, he is in for some taboos, the long period of peace on the continent being among the most important of them (and especially the idea that the only way conducive to it was to initiate European intergovernmental and supernational integration). Opinions such as the following are already a well established “common good”:

The creation of the European Union will go down in history as one of the most remarkable achievements of the twentieth century. In the space of just forty years – less than two generations – Europeans fought two appalling wars among themselves, finally appreciated the dangers of nationalism and the futility of violence, and sat down to design a system that would make it inconceivable that they would ever take up arms against each other again. (McCormick, 1999, p. xii)

And moreover,

The results have been substantial. A body of treaties and laws has been agreed and a set of institutions has been created that have altered the political, economic and social landscape of western Europe, changed the way Europeans relate to each other, redefined the balance of power in the world by creating a new economic superpower, and helped bring Europe the longest uninterrupted spell of peace in its recorded history. (McCormick, 1999, p. xii)

Even the official discourse of EU itself centers upon such a claim that it was first and foremost the urge not to fight each other anymore that made the European founding states join the ECSC (European Coal and Steel Community) after the Schumann Declaration (9<sup>th</sup> of May, 1950) and the Treaty of Paris (18<sup>th</sup> of April, 1951):

The aim, in the aftermath of World War Two, was to secure peace between Europe’s victorious and vanquished nations and bring them together as equals, cooperating within shared institutions.<sup>2</sup>

In the same place, it is also written:

...a new kind of hope emerged from the rubble of World War Two. People who had resisted totalitarianism during the war were determined to put an end to international hatred and rivalry in Europe and create the conditions for lasting peace. Between 1945 and 1950, a handful of courageous statesmen including Robert Schuman, Konrad Adenauer, Alcide de Gasperi and Winston Churchill set about persuading their peoples to enter a new era. New structures would be created in Western Europe, based on shared interests and founded upon treaties guaranteeing the rule of law and equality between all countries.<sup>3</sup>

Again, one should bear in mind is not the fact that EEC (later EU) structures happened to bring peace to the continent, but that they were *indispensable to the maintenance of peaceful relations*.<sup>4</sup> Such wording is used by Schumann himself in his famous Declaration.<sup>5</sup> And the idea is also present in the text of the European Coal and Steel Community treaty<sup>6</sup>.

---

<sup>2</sup> See *The EU at a Glance* (the “Europe in 12 lessons” chapter, “Lesson 2”) material available on-line at [http://europa.eu/abc/12lessons/lesson\\_2/index\\_en.htm](http://europa.eu/abc/12lessons/lesson_2/index_en.htm).

<sup>3</sup> Idem, “Lesson 1”, available at [http://europa.eu/abc/12lessons/lesson\\_1/index\\_en.htm](http://europa.eu/abc/12lessons/lesson_1/index_en.htm)

<sup>4</sup> On his way to find the text of the Schumann Declaration, the reader will encounter such a bold claim at [http://europa.eu/abc/symbols/9-may/index\\_en.htm](http://europa.eu/abc/symbols/9-may/index_en.htm).

<sup>5</sup> See the Declaration text at [http://europa.eu/abc/symbols/9-may/decl\\_en.htm](http://europa.eu/abc/symbols/9-may/decl_en.htm)

<sup>6</sup> The first words of the preamble of the treaty sound as follows: “Considering that world peace may be safeguarded *only* (underlining mine) by creative efforts equal to the dangers which menace it; convinced that the contribution which an organized and vital Europe can bring to civilization is *indispensable* (underlining mine) to the maintenance of peaceful relations; etc...”. See the ECSC Treaty at <http://www.ena.lu/mce.cfm>.



Now one can only wonder why such an (exclusive) alternative? Is it true that Europeans at the end of World War II had only two options – fight each other some more or integrate institutionally into a structure such as ECSC, or later EEC (and now EU)? Because if such a statement were true, than the case for European integration would be compelling, and all those “euroskeptics” just a bunch of unreasonable (even dangerous, unpatriotic and unhuman) critics.

The thesis of the present author is that the mentioned alternative was (and still is) a false one and that at least one other solution was available for a war ravaged Europe: the return to liberalism. More on that later. Moreover, the problems that plagued European nations at the end of the wars were caused by the reluctance to give up the massive government intervention previously deemed necessary for war purposes. When contemplating the beginnings of Europe, it is vital to bear in mind the tremendously interventionist context, with countries such as Britain on the verge of socialism (and Germany having been there already). Otherwise, all the “impending” needs of the moment (intergovernmental cooperation or even integration) appear to be meaningless to the honest researcher.

## **1. Interventionism: National and International**

I believe that an understanding of the beginnings of the European process of integration presupposes familiarity with the theory of interventionism, both domestic and international. To this we now turn.

The first instance in which interventionism can be contemplated, is the national scene. And here, one general form of interfering with the economy is *price controls*, while, in particular, governments can hamper the market for certain goods, money or labor, and at the same time face unavoidable consequences pertaining to international trade (commodity imports and exports), international payments and international labor force migration. More on these later.

Maybe one of the best descriptions of how price controls disturb the market and cannot be a durable solution to any problem is provided by Mises (1995, p. 39 and the following), who contemplates the situation where a government institutes a maximum price for milk. The declared purpose is, of course, to better the access of the needy to this vital product. Moreover, for such a measure to be effective, the fixed maximum price has to be below the one that would have otherwise been set by the unhampered market forces of supply and demand.

Now, what happens? In Mises’ own words:

On the one hand, the lower price of milk increases the demand for milk; people who could not afford to buy milk at a higher price are now able to buy it at the lower price which the government has decreed. And on the other hand some of the producers, those producers of milk who are producing at the highest cost – that is, the marginal producers – are now suffering losses, because the price which the government has decreed is lower than their costs...And as he cannot take losses in milk, he restricts the production of milk for the market. (Mises, 1995, p. 45)

Thus the government’s interference with the price of milk will result in less milk than there was before, and at the same time there will be greater demand. Some people who are prepared to pay the government-decreed price cannot buy it. Another result will be that anxious people will hurry to be first at the shops. They have to wait outside. The long lines of people waiting at shops always appear as a familiar phenomenon in a city in which the government has decreed maximum prices for commodities that the government considers as important. (Mises, *ibidem*)

Such an outcome is not a very glorious one, so the government will try to step in and fix the problem once more. At this point it should be observed that the governmental authority is at the point where every instance of intervention puts it: that of choosing between the scrapping of the previous intervention(s) and the cumulation of new interventions. Discard old interventions or intervene some more – this is the dilemma<sup>7</sup>.

So, in the case of milk above, the government might intervene with a system of rationing, which would not be a genuine solution, as it would imply arbitrary decisions and it would not fundamentally solve the main problem: the lower quantity of milk available. (Not to speak of consequences such as the “need” to create a governmental body to supervise the functioning of the quota system and to prevent the development of black markets etc.)

One other – seemingly more promising – solution would be to try to create better production conditions for those who supply milk to the market. Fixing maximum prices (of course, below the free market level) for their inputs would be a possible way to solve the problem. But the same kind of problems will now arise, only on a different market. And so on. Therefore, the government will have to choose between a return to the free market or all-round price-fixing which is one and the same thing with socialism. We contemplate here the classical argument against interventionism: its *inherent instability*.

One unpleasant (from the point of view of governments) factor hampering governmental efforts to “correct” market inefficiency or injustice is the world market. Assuming that the former maximum price fixing for milk was undertaken in the context of free imports of milk, a situation will follow in which national milk producers will be at a disadvantage (as they presumably had the higher prices, or were more dependent on them than foreign competition). Therefore, in order to make the price control more acceptable to its own national producers, a government will have all the political reasons to depart at the same time from the previous free trade regime (or, from a relatively freer regime, if such is the case)<sup>8</sup>.

Should the government desire to engage in fixing the exchange rate between the national currency and foreign currencies, an additional intervention on the money and capital market is necessary (various form of capital and foreign exchange control, quotas, conditions for purchase etc.) so as to make such exchange rate fixing effective. Again, a seemingly domestic business has consequences at the international level, slowly secluding the national market from the world market.

The same reasoning applies to protection for workers by means of minimum-wage laws and migration problems. When a government tries to better the lot of its domestic workers by means

---

<sup>7</sup> This fact should make it clear that interventionism is no genuine “third economic system”, apart from socialism and capitalism, as renouncing previous interventions means approaching capitalism and cumulating new ones pushes the economy towards socialism. One way to syntetise this aspect of interventionism is to speak of its *inherent instability*. Thus, thinking of the consequences of consistent interventionism, Hayek could speak of a “road to serfdom”.

<sup>8</sup> Such a connection between domestic interventionism and protectionist policies can be very well contemplated in many other instances. A subsidy, for example, given to domestic producers for various reasons (“structural problems”, “infant industry reasons” etc.) will be much more effective in enhancing the position of the supported companies if doubled by protection from foreign competition. (Otherwise, under free trade conditions, depending on the height of foreign companies’ profits, the government might see its subsidy compensated by price reductions of imported products.)

of fixing a minimum wage (above the free market level, of course; otherwise it would have no effect), it should at the same time preclude foreign immigrants from countries with lower wage levels to enter the domestic labor market and enjoy the benefit of this fixed (higher) wage – thus replacing national workers, who remain unemployed. The same thing happens: domestic interventionism implies logically the need for supplements of protectionist measures (immigration barriers in this case), which disconnect the economy from the world markets and lead it more and more towards relatively higher levels of autarky.

The conclusions of the previous paragraphs can be well summarized by the words of Hans Sennholz:

Policies of government planning and welfare and the disintegration of the world economy into heterogeneous national units are two aspects of the same phenomenon. ...every welfare measure by a national government bears inescapable effects on foreign relations and the international exchange of goods. (Sennholz 1955, p. 1)

A disintegrated international order with nation states insulated from each other in different degrees of autarky has multiple disadvantages. Chief among them – from the point of view of governments, but not only – is the higher and higher cost of each governmental interventionist measure. Maintaining the internal market of, let's say, coal secluded (absolutely or relatively) from the world market implies lower level of efficiency in coal production. As this product is an input in numerous other lines of production, coal protection leads to higher production costs in all sectors which use coal. Should some of these sectors be exporting ones, the government indirectly impairs the country's exports, which, in their turn require governmental intervention for support. This – no matter the means: subsidy, preferential exchange rates etc. – has effects on foreign markets, prompting foreign governments to deal with the problems they now face (ensuring further obstacles in front of the said exporters: higher tariffs, quotas etc.).

Long before extreme levels of autarky (which implies very low levels of efficiency and standards of living) governments will foresee the possibility to cooperate so as to render their particular instances of intervention more fruitful. This leads to *international interventionism*: intergovernmental cooperation for feasible intervention purposes. If governments manage to intervene in concert, then they will no longer hamper each other's policies. For instance, if governments manage to reach an "international agreement" concerning coal production – agreement involving quotas (production, export and import) or even prices – then the situation at home becomes (at least on the short run) more manageable. The proportions of the feasible domestic intervention are in a way preset. Of course, the more a government is inclined (ideologically or pragmatically) towards interventionism, the more it will find it useful to cooperate with foreign governments on each and every possible aspect of the economy. At this moment a general impression that "union", "integration", "cooperation" is necessary sets in.

Judging from the openly declared purposes of various forms of international cooperation, one is under the impression that this phenomenon can only be a beneficial thing. Nevertheless, the eye of the trained economist must spot the fact that such phenomena are the necessary consequence of problems raised at the international level by domestic protectionist policies of all sorts: welfare schemes, trade barriers, money and capital movement controls etc. Therefore, an economist perspective on such schemes is not at all as glorious as that of the politician.

Last, but not least, one should not be under the impression that international cooperation solves the dilemmas of domestic protectionism and that's that. The instability argument against interventionism applies both to the domestic and the international level. While on the short run cooperation means feasible intervention, on the long run it sets the world economy on a path to world socialism.

What happens if states fail to cooperate and at the same time refuse to abstain from further intervening in their economies? Well, assuming (unrealistically) very pacifist ideologies on the part of all states, a situation is begotten where the world consists of autarkychal states, completely insulated from each other, with (very) low levels of productivity and standards of living. Everything consumed must be produced at home. Of course this means that many of the goods now familiar will never get to be produced.

More probably, the other possible outcome – given the fact that there are no more viable economic ways to cooperate with the other states through free trade and free markets – is war: the use of the political means<sup>9</sup>. This was the path of Germany (see Mises, 1944) towards World War II, as an economy oriented toward production for war purposes precluded the possibility of sufficient internal food production and presupposed a constant flow of different types of natural resources from abroad (not all available – at all, or in sufficient amounts – on the domestic market).

To sum up, states that embark systematically on interventionist policies, face – at the international level – a “trilemma”: to maintain interventionism and advance more and more rapidly towards autarky or, more probably, war; cooperate on an international level (international interventionism and planning) so as to render interventionism more feasible; to return to free trade and laissez-faire, renouncing interventions – this way “reintegrating” the world market but with no “positive” elements of governmental intervention (intergovernmental or supernational).

From most presentations of the beginnings of Europe, the third option is left out – more or less deliberately. If it is left out of the picture, it follows naturally that European states were facing the “fight or cooperate” alternative. But if the third option is included, one can immediately see that there would have been at least one other way to peace and prosperity, besides European integration. Only because the ideological climate of the era was profoundly anti-liberal, was the cooperation among European states seen as indispensable for peace.

In the last part of this chapter I would only want to draw attention to the fact that at the end of the World War II, the European countries who were to become the founders of what would in our days has become the European Union were indeed highly interventionist – with decades of interventionist policies behind them. The first half of the twentieth century can be called the “international economic disintegration era”.

It is usual to consider the nineteenth century (and even the era up to 1913-1914) as the “liberal century”. In the words of Sennholz:

It was a century of individual freedom and decreasing international restrictions upon the movement of men, goods, and capital. The world economy was an interdependent system, on the way to economic unification which makes political unification irrelevant. It was an era of unprecedented success. (Sennholz 1955, p. 2)

---

<sup>9</sup> In the terminology of Franz Oppenheimer. See Franz Oppenheimer, *The State. Its History and Development Viewed Sociologically*, New York, B. W. Huebsch, 1922, p. 24 and the following.

This period is even seen as “the first globalization” period, with the world integrated by free trade and open borders. The other important ingredient of the liberal century was the gold standard, which meant a *de facto* monetary integration of the world.

Things started to change visibly (even though elements of change can be observed well into the nineteenth century with the policies of the German Reich under Bismark) around the beginning of the Great War (which some even explain by the resurgence of protectionist and interventionist ideologies). In the words of the same author:

The liberal century was followed by the age of economic and social planning. And, again, ready plans for international unification and government cooperation followed the early symptoms of disintegration and international conflict. (ibidem)

To grasp the point of the present author, the reader should bear in mind instances of interventionist (sometimes even socialistic) policies such as: the Hindenburg Plan, the great German inflation, the *Zwangwirtschaft* of Hitler, the fascist system of Italy (with institutions such as IMI (Istituto Mobiliare Italiano) and IRI (Istituto per la Ricostruzione Industriale), with powerful syndicates/unions and the corporations system and with more decisive steps towards autarky after the Ethiopian episode and the problems with the League of Nations) and also with the equally protectionist regimes of France and England (especially after 1930, which prompted F. A. Hayek to write *The Road to Serfdom*). At the end of the World War II, exchange controls, capital transfer restrictions and controls, tariffs and quotas of all sorts, migration barriers were a common thing in Western Europe. Under these circumstances the need for intergovernmental cooperation seemed vital.

To those above can be replied that, in the end, Europe undertook – with the creation of ECSC – a decisive step toward free markets. But was it really so?

## **2. Was the European Coal and Steel Community (ECSC) a step towards freer markets?**

At a first glance – and under the mediatic assault of the EU propaganda machine – the ECSC is a seemingly free market, although the founders were reluctant to such straightforward wording. The preferred version was the concept of “common market”<sup>10</sup>. The supposed liberal spirit of ECSC is present in the famous Article 4, which states<sup>11</sup>:

The following are recognized to be incompatible with the common market for coal and steel, and are, therefore, abolished and prohibited within the Community in the manner set forth in the present Treaty:

- (a) import and export duties, or charges with an equivalent effect, and quantitative restrictions on the movement of coal and steel;

---

<sup>10</sup> Whether this common market is one and the same with the free-market, or it differs – and in what regards – it is never said. Clarity is not a virtue in politics.

<sup>11</sup> See the *Treaty constituting the European Coal and Steel Community*, available on-line at <http://www.ena.lu/mce.cfm>.

- (b) measures or practices discriminating among producers, among buyers or among consumers, specifically as concerns prices, delivery terms and transportation rates, as well as measures or practices which hamper the buyer in the free choice of his supplier;
- (c) subsidies or state assistance, or special charges imposed by the state, in any form whatsoever;
- (d) restrictive practices tending towards the division of markets or the exploitation of the consumer.

Nevertheless, this free-market orientation is so powerfully amended by a host of other provisions of the treaty that it remains practically empty. In the words of the same Hans Sennholz, the European Coal and Steel Community amounted to no less than *socialization of the coal and steel industries* of the ratifying countries. As a general overview of the scheme, he has to say the following:

The European Coal and Steel Community reverses the production structure and abolishes the social function of ownership, i.e., its employment in the best possible way for the consumers' benefit. It is the institutions of the Community that are defining the general objectives of production (Art. 5). They decide on the financing of production programs and on construction and operation of production facilities. They control investments and financial assistance and may prohibit enterprises to resort to capital and money markets to finance their expansion programs (Art. 54-56). Having decided what shall be produced and who shall produce it, the institutions of the Community are to regulate or influence general consumption (Art. 57). The High Authority not only may establish a system of production quotas but also consumption priorities, and it may determine the allocation of the coal and steel resources among consumers (Art. 58-59). It may fix maximum and minimum prices for goods consumed in the territory of the Community as well as for goods exported to other countries (Art. 60-64). It may restrict the importation of coal and steel and thus decrease the supply for consumers (Art. 71-75). Finally, having regulated production, fixed prices, and allocated quotas of consumption, the institutions of the Community may determine the costs of production by deciding wage rates and other benefits to labor employed in the coal and steel industries (Art. 68). In all these economic decisions it is the High Authority or other institutions of the Community that are sovereign. The public, the consumers, no longer control the production process. Through buying or abstention from buying they no longer determine the price and market structure. The Treaty constituting the European Coal and Steel Community has put the consumers in the care of supranational trustees. (Sennholz 1955, p. 248-249)

It is no surprise then that a handful of interventionist states decided to join steel and coal production under such a scheme, which cannot – even euphemistically – be called a free market.

### 3. Concluding remarks

In this paper I have tried to refute the thesis that European integration – the way the European states embarked upon with the creation of The European Coal and Steel Community – was indispensable for the preservation of peace among the continent's nations. The main line of argument was that, instead, the integration process was a logical consequence of the reluctance of states to renounce domestic interventionist policies inherited from the war (and interwar) period. The beginnings of European integration are usually presented under the form of a dilemma: integrate or fight. I believe that this is a false alternative, and that the dilemma was actually a "trilemma": integrate, fight or return to the sound policies of free trade and laissez-faire. Liberalism, that is.

One more thing: the present author believes that the essential "trilemma" confronted EU at every step undertaken towards what should eventually be a European super-state, and still confronts it today. As they embarked – seemingly to avoid war – on international interventionism and

planning, the European states are heading towards European socialism. Therefore the genuine option of liberal policies is still relevant.

## References

Anderson, Benjamin M., *Economics and the Public Welfare. A Financial and Economic History of the United States, 1914-1946*, Liberty Press, Indianapolis, 1979.

Kantor, Myles B., *The European Union's American Pedigree: Lessons from the Other Side of the Atlantic*, Journal of Libertarian Studies, Vol. 16, No. 1 (Winter 2002), pp. 45-59

McCormick, John, *Understanding the European Union. A Concise Introduction*, Palgrave, New York, 1999

Mises, Ludwig von, *Economic Policy: Thoughts for Today and Tomorrow*, Free Market Books, Irvington NY, 1995

Mises, Ludwig von, *Omnipotent Government: The Rise of Total State and Total War*, Yale University Press, New Haven, 1944

Röpke, Wilhelm, *International Order and Economic Integration*, D. Reidel Publishing Company / Dordrecht-Holland, 1959

Rothbard, Murray N., *Man, Economy, and State with Power and Market*, The Ludwig von Mises Institute, Auburn, Alabama, (no date)

Sennholz, Hans F., *How Can Europe Survive?*, D. Van Nostrand Company, Inc., New York, 1955

# AN ANALYSIS OF THE RISK MANAGEMENT IN THE CASE OF TERRORISM

GABRIELA PRELIPCEAN<sup>1</sup>  
MIRCEA BOSCOIANU<sup>2</sup>

## **Abstract**

The management of crises caused by terrorist attacks proved an insufficient capacity of the governments to manage extreme risks in most of the recent cases. After the '90s, the philosophy of terrorism changed and it therefore requires immediate governmental intervention. The mega terrorism that occurred on the private insurance markets triggered the loss of the functionality character. A financial analysis of the terrorism processes, considered as catastrophic risk, by using the risk theories, risk management and financial risks is proposed. This kind of analysis should include the specific aspects of the terrorism processes. Also, an insurance system based on the public-private partnership against the catastrophic risk is proposed. It will be demonstrated that the main problem is the assessment of risk in the very low demand for this type of risk coverage.

**Key words:** terrorism, risk management, governmental intervention, insurance, public-private partnership

---

<sup>1</sup> “Stefan cel Mare” University of Suceava, Romania, [gabrielap@seap.usv.ro](mailto:gabrielap@seap.usv.ro).

<sup>2</sup> Military Technical Academy, Bucharest, e-mail: [mircea\\_boscoianu@yahoo.co.uk](mailto:mircea_boscoianu@yahoo.co.uk)



## **Introduction**

The events of September 11<sup>th</sup> and March 11<sup>th</sup> have determined participants in insurance and reinsurance markets to drastically re-evaluate their estimates of potential insured property losses from terrorist attacks. In order to analyze the dynamics of the insurance-reinsurance market response (a possible explanation for the significant flows of new capital directed to the reinsurance industry) it is necessary to discuss the terrorism risk in the context of risks normally handled on the insurance/reinsurance markets, the role of the government in resolving insurance/ reinsurance supply problems related to terrorism and the general principles that a government terrorist program should adhere to and provide a critical view on the present inefficiency of the proposals on this market.

The evaluation of alternative forms of governmental intervention implies an analysis of the factors which motivate them. The theory provides the evaluation background of the specific market dysfunctions that motivate the intervention. In this paper is proposed a comparative analysis of different forms of governmental intervention. It is important to combine economic theory instruments with the insurance industry and with the government, because, sometimes it is suggested that there are many differences between the economic theory and institutional structure; the economic theory shows that the assumptions are in conflict with the institutional reality. Institutions frequently seem to act independently from economic objectives. In this paper, the analysis strategy begins from the analogy between the insurance markets of terrorism and of natural calamities.

In the specific literature there are intense discussions about the management of the catastrophic risk.

The potential loss caused by catastrophes requires a specific capacity of the insurance market; the market seems to be insufficient. An example could be the failures on the insurance market after the major natural disaster: hurricane Andrew. The hurricane Andrew caused losses which were less than the established average estimates of each day: the catastrophic events brought out losses of 100 billion dollars or more to the insurers, which can cause the collapse of the insurance market. The ART transactions (alternative risk transfer) appeared, as an instrument for avoiding the collapse was necessary. These transactions appeared at the same time because of the increasing number of catastrophes at the end of the 80's and at the beginning of the 90's. These transactions transferred the catastrophic risk to investors by means of the insurance market. An important segment of the papers published on the subject of the catastrophic risk management focuses on ART and their potential of covering the catastrophic risk (Lewis, Murdock, 1999).

The role of the government in managing (reducing and covering) the terrorism risk has grown after 9/11. This development was required by the fact that the insurance companies from all over the world cancelled their insurance policies with the companies of air transport and with the airports. The terrorist attacks from New York and Washington have caused a reconsideration of the exposure to losses in air traffic, as the insurance companies were compelled to offer coverage for all these events. The aircrafts without sufficient coverage of the obligations were not allowed to take off, and the air traffic was in danger of ceasing its activity. Confronted with this scenario, many governments offered state guarantees for the airline companies of those countries. Many states participate, in different ways, at settlements, introduced for covering the risk of terrorism, for dividing the risk. This led to political debates which considered the advantages and the disadvantages of the governmental intervention in these states in the insurances industry for the risk of terrorism (Priest, 1996).

Finally, the problems of the protection against natural catastrophes (as demonstrated by the floods of August 2002 in Europe) concern not only the type of supply, but also the type of

demand. The floods of August 2002 in Central Europe proved that the problems of the catastrophic risk management did not occur only from the point of view of the offer, but also from the point of view of the demand for covering the losses. One can notice that just a few of the victims of the floods had an insurance against these losses and, moreover, in Germany, the density of insurances against this kind of hazard was very low (Schwartz, Wagner, 2002). As a result, the political strategists took into account the development of the bases for compulsory insurance against fundamental risks such as floods and storms.

### **Terrorism risk vs. natural catastrophic risk**

The distinctive characteristic of the two forms of extreme risk (natural disasters and terrorism – both accompanied by considerable losses) refers to the uncertainty caused by the human intervention. The actuarial methods of evaluating the risk of terrorism are not developed enough in the field and represent an objective for subsequent research; the effect created by the interdependence of the terrorism risk will also be analyzed through the general pattern of interdependent security.

The effects of extreme natural disasters such as hurricanes, typhoons, floods and earthquakes represent a serious threat to human life, properties, local communities and the economic growth of the entire nation.

The considerable damage caused, among others, by hurricane Andrew in Florida in 1992, by the Northridge earthquake in California in 1994, by the Kobe earthquake in Japan in 1995, by the Kocaeli earthquake in Turkey in 1999, by the Lothar and Martin storms in Europe in 1999, the Bleuj and Gujarata earthquakes in India in 2001, the tropical storm Allison in the USA in 2001, the floods in Germany in 2002, the tsunami in Indonesia in 2004, hurricane Katrina in the USA in 2005, all these have challenged the capacity of the insurance and reinsurance market and underlined the decreasing possibilities of covering the catastrophic risk.

Because of the increasing number of natural disasters which occurred during the last years, the risks triggered by the constant interaction between human activities and the environment are diverse, varied and often catastrophic because of their consequences. The development of a crisis plan, with specific targets as a response to the strategy, needs proactive contributions from the economic national and international players involved: governments, public officials, international organizations, financial institutions and private entities.

The nature of the risk, the probability of loss, and the possible amount of the damage and the capacity of absorbing the consequences of the damage depend on the individual attitude towards risk. Under reasonable circumstances and equal access to information, the economic players can calculate the value of the risk based on the amount of the damage and the possibility of the disaster to happen. The decision must be taken on the basis of this evaluation of the risk. Consequently, the economic players can display the following types of behaviour: *aversion to the risk, preference for the risk, neutral to the risk.*

The mechanism of the traditional insurance has four phases: *evaluation of the risk* (by statistical and probabilistic analyses); *transfer of the risk* (the transfer of the negative consequences by means of insurance policies); *creation of common funds of risk* (placing homogeneous, yet independent, risks in a common fund, allowing insurers to diversify the risk and to benefit in accordance with the law of big numbers); *allotment of the risk and the correct evaluation of the risk allowances.*

Because the amount of foreseen damage increases, the financial ability of the insurers to cover them can be seriously affected. In the event of financially differentiated exposure level, the insurers may become themselves averse to risk. In this context, co-insurers and re-insurers have the right of preference, before the first insurers, who are eager to give a part of the assumed risk in exchange for the money already collected.

The traditional insurance agreements can be of two types: *proportional treaties (agreements)* (in which the re-insurers take a share of the risk transferred by the first insurers) and *treaties of stop loss type* (in which the re-insurers take a bigger share of the risk according to a certain index).

Everybody agrees with the fact that, in order to be insurable, the risk must be predictable, based on past experience and statistical calculus. The majority of the problems appear when: there is *some generalized uncertainty* – which can undermine the ability of the insurer to correctly evaluate the risk; or there are *asymmetric pieces of information* – in the advantage of prospective insurances, generating distortions and problems in connection with *the adverse selection* and *the moral hazard*.

The traditional mechanism of insurance is not capable to cope with the risk of natural catastrophes, as the predictability of the risk, its space diversification and the financial capacity of the market show serious limitations. The amount of the foreseen losses and the asymmetric information influence the predictability of the risks, and the evaluation needs the conjugated efforts of the groups of insurers and re-insurers. We must underline the fact that the way the information is distributed and the concentration of the market needs a correct and fair approach of the antitrust policies and of the competitive ones.

The considerable losses caused by the natural catastrophes in the last years caused a temporary absence of the reinsurance of catastrophe because of the shortage of supply and the withdrawal from the market of the catastrophic risk (Holzhen and Lechner, 1998). Apart from this, natural disasters can cause even more serious losses (60 billion for hurricane Andrew, 100 billion for the earthquake from California (Durbin, 2001) and 160 billion for hurricane Katrina).

All these brought about chain reactions which can cause the insolvency of the reinsurance market. Moreover, a significant part of the capacity of the reinsurance market is not available because of liquidity (Cummins, 2002).

Consequently, other solutions are necessary, such as *the ART solution (alternative transfer of the risk)*. The stress was first of all placed on the instruments which could facilitate the direct transfer of the risk using the financial market, by means of the famous bonds. The capacity could have been increased if the bond issues had brought important funds from investors who were not active in the field of insurance. The solution of the transfer of the risk towards the capital market can be observed since 1992. The Chicago Board of Trade (CBOT) introduced as instruments, at the end of 1992, *the catastrophic index and the options of catastrophic risk* (Durbin, 1996). The CBOT options weren't very successful on the capital market, and therefore, after a few years, the transfer of the risk on the capital market was performed by using the titles negotiated outside the stock exchange, for example: *cat bonds*, instruments which made possible the direct transfer of the risk towards the investors. If the transactions with titles of risk have technical parameters which describe the intensity of the catastrophic event, as the intensity of an earthquake on the Richter scale, the force of a hurricane etc., the speculation could be completely excluded. The utility of these parameters appears when they are correlated with the consequences of the insurance of the event.

A case of ART is the “*trigger*” model that can be used if the number of combinations of possible parametric achievements and the results are not known for each case, if they are not explicitly specified, where the procedure for determining the compensation is the following: if the event occurs, a simulation based on the observed parameters is made and this generates an estimate of the losses for the real portfolio of the owner.

The entire capacity of the re-insurance market is not sufficient for covering the catastrophe risk and the demand for the ART solution is justified by the assumption that there is a limited offer for the traditional instruments of hedging. This element requires the increase of the capacity of financing a risk that can be generated either by the extension of the capital funds owned by the insurance industry or by entries on the insurance market.

There exist many ways to transfer of the risk towards the financial market. The economic evaluation of each instrument depends mainly on the specific plan chosen and on the institutional characteristics. The risk securities depend on fundamental random variables and offer an instrument for covering the moral hazard. From the financial mathematics point of view the coverage of the insurance/reinsurance can be completely correlated with the loss, it induces changes in the clients’ behaviour and the analysis of this phenomenon can be performed by using *models of the evaluation of the interdependent security*. The evolution of the risk bonds, in the case of the capital market, does not directly depend on the specific loss; the loss is correlated with a set of random variables. A specific element is basis risk that represents the difference between the loss and the coverage; another aspect is the so-called cost of transaction, imposed by the market of the respective instrument, and represents a difference between the risk securities and the reinsurance.

The risk of the insurance is not correlated or is low correlated with the risk of the market, which means that the price of the bonds could include reduced premiums of risk. Another potential advantage of the bonds of catastrophic risk is the fact that *the risk of non-payment* can be elegantly avoided. As disasters determine a significant risk of insolvency for the reinsurance companies which are active on the market; their agreements are subject to the risk of non-payment. This is correlated with the possibility of accumulated losses, typical for catastrophic events. The threat of accumulating losses brings about a strong correlation between the portfolios of the first insurers and the compensations from the portfolio of agreements of the re-insurers. For a first insurer, this brings about an increase of the risk of non-payment or of the risk of loan as related to the reinsurances of catastrophic risk. The bonds are not greatly affected by the risk of non-payment. The funds invested in titles of catastrophic risk are collected in advance, which means that the loan risk of the first insurer is reduced to the risk of non-payment corrected with the investments made by the endorser (Laster and Ratim, 2001). However, the titles of risk associated with the insurances did not have the expected success on the market. The fastest increase in the volume of transactions of these financial instruments was at the end of the 90’s when the premiums of reinsurance grew (Durbin, 2001).

The impact of the future major disasters on the market of reinsurance and the impact on the price can bring about a new growth in the volume of the market of the titles of catastrophic risk (known as a technique of private management of risk, combined with a component of the public management of risk). The coverage generated by risk bonds could be an interesting alternative to the solution of the traditional insurance.

Kunreuther (2002) suggests the incorporation of the risk bonds in the approach of the public – private partnership. The involvement of the government usually appears after the catastrophes which cause shock on the level of the industry of insurances and of reinsurances. The growth of the price of reinsurance in the event of a natural catastrophe induces, for a certain period of

time, a negotiation and a segmentation of the market of the risk bonds which the re-insurers must reconsider in their own portfolios.

The legal framework and the various means of the government intervention are different from one country to another and the comparative analysis allows for the better understanding of the complex managerial process in this field. Many states have implemented the complex government strategy for the management of risk. The most important institutional agreements imply public-private partnerships, such as: France – the diagram of compensation in the event of national disasters CAT; Spain – Consorcio de Compensación de Seguros; USA – National Flood Insurance Program – NFIP; California – California Earthquake Authority (CEA); Florida – Florida Natural Catastrophe (Hurricane) Fund; Hawaii – Hawaii Hurricane Relief Fund (HHRF); New Zealand – Earthquake Commission (EQC); Japan – Japanese Earthquake Reinsurance (JER); Turkey – Turkish Catastrophe Insurance Pool (TCIP); Norway etc.

### **Terrorism risk and the insurance-reinsurance markets**

Terrorism risk is not materially very different from other risks that are handled by insurance and reinsurance markets, but questions have been raised about the feasibility of financing such a large event through insurance/reinsurance markets. Events of this nature may be more efficiently handled through capital markets via financially engineered instruments such as catastrophic bonds. One risk for the involvement of the government in the terrorism insurance market is that it would potentially discourage the development of these private market alternatives.

The uncertainty of this risk is another feature of terrorism coverage that initially seems different from other catastrophic risks. This fact makes it difficult for insurers to estimate the probability and severity of loss. Nevertheless, the insurance industry has provided coverage for other uncertain events which lacked statistical reliability such as political risk insurance and satellite launches. The private market can develop pricing for terrorism coverage as it has for other uncertain and unique risks. Therefore, any governmental involvement should not discourage private industry from returning to this market.

The management of crisis caused by the terrorist attacks proved an insufficient capacity of the governments of administrating the extreme risks in most of the recent cases. In this case, the necessity, the mechanisms and the means of the initial government intervention are justified.

The risk of terrorism is social and requires an immediate and urgent governmental intervention. The mega terrorism caused the loss of the functionality character on the private insurance markets. The insurance against terrorism may be limited according to the CBNR type of attack (chemical, biological, nuclear, and radiological). Russel (2002) shows that the intervention of the state is an absolutely necessary answer. Kunreuther and Michel Kerjan (2004) have shown that the international terrorism presents a set of strictly specific characteristics, which amplifies the importance of the public sector. Priest (1996, 2003) agrees that the governmental intervention on the insurance market is not desirable. Robert Merton (2004) shows that the institutional structure must act in the sense of the elimination of the first incorrect effects and of roughness of the market, ignored in most of the economic models. The institutional structures most act so that the economic models to be universally applied even when a simple comparison of the models hypothesizes and of the real institutions suggests something else.

This approach shows that even if the countries are different in their institutional structure (prices and traditions), a single analysis framework should be valid for the accomplishment of the economic objectives.

*The empirical knowledge on the private antiterrorist markets is very limited, as the governmental interventions dominate these markets in most countries (the public-private system in which a substantial part of the risk is governmentally sustained).*

The management plans in which the government might have an insurance role (Kunreuter, 2004, OECD, 2004) take into account reinsurance for the high level risks. The most evaluated insurances against terrorism are in France (GAREAT), Germany (EXREMUS), U.K. (Pool RE) and U.S.A. (TRIA). The concept of *possible creditor* is connected with ex-post payments of the bonuses (Jaffe, Russel, 2003) and is applied for the terrorism coverage if the governmental agency, most probably The Central Bank, is relieving credits to insurance companies that need cash.

### **The new challenges facing insurers in managing extreme events**

There are two important implications for insurance companies that operate in catastrophic insurance; the companies cannot limit losses or their variation through *portfolio diversification policies*; the annual rate of losses (refunds reported on the total of the collected rate) is extremely volatile based on extremely high values. The result is that insurance companies must have remarkable capital and foreign currency reserves to confront such events. The governments through have a strategic advantage tax links and dominate the majority of the world market. The insurance industry admits that following a catastrophic attack there are a lot of companies that can go bankrupt and need urgent governmental support. In many countries the insurance against terrorism is based on government participation.

The magnitude of the last terrorist attacks requires new thinking about managing terrorism risk. In the next years after the terrorist attacks there was considerable demand from insurance against these events from many businesses, but little coverage available. A new appreciation by insurers of these risks led them to charge higher prices for coverage in a non typical market.

This fact led the US Congress to vote the TRIA (Terrorism Risk Insurance Act) in November 2002 and insurers are now required to offer insurance against terrorism as a separate endorsement to an existing commercial policy. Firms can voluntary purchase this coverage and each insurer is financially responsible for a certain portion of the loss as a function of its total premiums written. The terrorist coverage is available, but the demand for such protection has been low, because the business men feel that a future terrorist attack will not happen to them and because they perceive the premium to be too high.

This type of risk is unlikely to occur, even if it can trigger devastating consequences, such as the reluctance on the part of the potential risk transfers to incur the high cost associated with them. For insurers, low frequency and high impact risk is difficult to sell. The challenge is to help stakeholders to understand this nature of low frequency, high impact event and appreciate correctly the transfer of these risks.

The access to risk capital is very limited both for the elementary insurers and for the insurers. The limited access to necessary capital can lead to bankruptcy (wreck risk). Besides the common character of catastrophic risks, the terrorism risk has the unique characteristic that it is produced by human intervention. The impact of this characteristic is essential, regardless of

the type of intervention required a critical analysis. For example, the government seems to have superior information regarding the possibility and location of a future terrorist attack, a fact that justifies why private companies avoid covering these risks. It is also possible that terrorists will not choose to attack an insured target, a fact that increases the private companies' ability in offering insurance against terrorism.

The initial decision of governmental intervention after a major attack starts from the next motivations: the government has the best information regarding the characteristics of future attacks; as a result of private insurance market failure against terrorism there can be major macro-economical losses (the government intervention can diminish these losses – Russel, 2002); regardless of the immediate macro-economic effects, if a subsequent attack is produced there would exist a serious regress regarding the initial intervention.

### **Means of intervention on catastrophic insurance markets**

An initial way of intervention refers to the *initiatives regarding the market's functionality boost-up* (re-creation of private markets not the creation of a public substitute). In order to organize an analytical background of intervention forms, it is useful that *the micro-markets* (through which selling policies and damages application appear) and *the risk insurance functions* are distinguished. Many current governmental interventions represent public-private corporations, with the private markets based on the functioning of the market microstructure, while the government is responsible for insurance functions. Alternative market microstructures mechanisms will be analyzed with the attention focused on alternative means to improve risks and the way this is divided between the public and the private sectors. Key mechanisms observed in different governmental interventions start from the following: dividing the risk between the government, the investors on the capital market and insurance companies; there are mandates for the involvement in the governmental plan; how the government accomplishes cost subsidizing for the insurance offered; which are the limitations covered at terrorism risk levels; maximum limits regarding the exposure of insurance companies and government; the private companies' part in assigning standards and risk policies; provisions adopted at the end of the participation.

The *optimal methods of governmental intervention in the insurance market against terrorism* starts from the following aspects: what should be the global extension of government participation; which should be the duration of the intervention (necessary for the private capacity to remake, or the long term approach that reflects fundamental market failure); what is the governmental financial intervention modality (elementary insurers, last instance re-insures, last instance ex-post creditors).

### **The limits of governmental intervention on the market**

It is very difficult to determine the fact that through its intervention, the government cancels the purpose of private insurance. The possibility that government interventions can diminish private companies' interest can be analyzed starting from the *moral hazard* principle in which the insurance provision transfers to the market players the ability of engaging a higher risk. On the other hand, insurers use *a risk based price setting* especially to co-interest the insured parts to take their own measures to diminish risks. Given the public nature of terrorism risks, some efforts will be influenced by other factors other than strictly defined economic

initiatives. Individuals generally anticipate governmental intervention in case of a catastrophic event, regardless of the governmental program. For example in the USA this part is insured by FEMA (Federal Emergency Management Agency). The Victim Compensation Fund, created after September 2001, is a governmental compensation method.

*The failure of catastrophic risks on private markets leads to another way of governmental intervention* that is a valid worldwide characteristic. In case of natural disasters the fundamental impediments regarding the mobilization of large sums are due to: accounting restrictions; provision taxation; taking over risk; re-insurance when confronted with similar capital problems (Frott 2001); the transfer mechanisms failure of the catastrophic risks on the capital market (a standard evaluation procedure doesn't exist), there are no protection mechanisms against hedging risks: the lop-sided risk characteristics; the catastrophic risk liabilities (cat bond) didn't achieve their purpose.

The involvement of the human factor in terrorism makes this risk more difficult to ensure. The main effects introduced by human nature are: the government has better ways of obtaining information than the private markets: if the insurance rates reflect the detailed ratings, then they only count on the information that is directly available to the private insurance firms (a more precise evaluation could only be made by using the governmental information, and this ambiguity concerning the limited access to information leads to higher rates); the governmental disposition to act *as the last instance insurer* influences the credibility of the programs that aim at stopping the terrorist attacks from the beginning; the terrorists will choose the targets strategically and their strategy includes target selection based upon the insurance level (Kunreuther, Michael Kerjan 2004); the action that the individuals and firms take in order to understate the damages that result from a terrorist attack depend on the strategy that the terrorists will choose when they select the targets.

*The macroeconomic effects* of the terrorists attacks are higher than those caused by natural disasters, as the direct losses can be more considerable and the failure in stopping the attack will be seen like a governmental failure; the terrorists' goal is to maximize the global impact on the economy.

## **Conclusions**

The magnitude of the last terrorist attacks requires new thinking about managing terrorism risk. This type of risk is unlikely to occur, even if it can trigger devastating consequences, such as the reluctance on the part of the potential risk transfers to incur the high cost associated with the risk transfer.

The paper presented the analogy between terrorism risk and natural catastrophe risk, the catastrophic events insurance/reinsurance market, the possibilities to transfer risk to capital markets, the means of governmental intervention in the catastrophic insurance market, and the limits imposed on the intervention in catastrophic insurance market.



## References

- Cummins, J. D., N. A. Doherty, and A. Lo, "Can insurers pay for the 'big one'? Measuring the capacity of an insurance market to respond to catastrophic losses", *Journal of Banking and Finance*, 26: (2002) 557-583
- Cummins, J. D., D. Lalonde, and R. D. Phillips, "The Basis Risk of Catastrophic-Loss Index Securities", *Journal of Financial Economics*, 71 (2004)
- Durbin, D. (2001), Managing Natural Catastrophe Risks: The Structure and Dynamics of Reinsurance, *The Geneva Papers on Risk and Insurance*, (2001): 26: 297-309
- Holzhen, T., and R. Lechner, The global reinsurance market in the midst of consolidation, *Sigma* no. 9/1998, Swiss Re, Zurich
- Jaffee, D. and T. Russell, "Markets Under Stress: The Case of Extreme Event Insurance," in R. Arnott, B. Greenwald, R. Kanbur, and B. Nalebuff (Ed.), *Economics for an Imperfect World: Essays in Honor of Joseph E. Stiglitz*, MIT Press, 2003
- Kunreuther, H. C., The Role of Insurance in Managing Extreme Events: Implications for Terrorism Coverage, *Risk Analysis*, 22: (2002): 427-437.
- Kunreuther, H. and E. Michel-Kerjan, "Dealing with Extreme Events: New Challenges for Terrorism risk Coverage in the US," Working Paper 04-09, Risk Management and Decision Process Center, University of Pennsylvania, April 2004.
- Kunreuther, H. and M. Pauly, "Neglecting Disaster: Why Don't People Insurance against Large Losses", *The Journal of Risk and Uncertainty*: 28-1 (2004): 5-21
- Laster, D., and M. Raturi, Capital market innovation in the insurance industry, *Sigma* no. 3/2001, Swiss Re, Zurich, 2001
- Merton, R. and Z. Bodie, "The Design of Financial Systems: Towards a Synthesis of Function and Structure," *National Bureau of Economic Research Working Paper* No. 10620, June 2004.
- Munich Re ART Solutions, Risk Transfer to the Capital Markets - Using the Capital Markets in Insurance Risk Management, Munich, 2001
- Prelipcean, G., "Politicile CDI in fata noilor amenintari asimetrice de securitate. Un model al terorismului international", Sesiune de informare pentru Programul National de Cercetare-Dezvoltare-Inovare in domeniul Securitatii si Apararii, Bucuresti, 29 martie 2005
- Prelipcean, G. and M. Boscoianu, "Some aspects about the direct government intervention into the terrorism insurance market", NAV MAR EDU, Constanta, 2005
- Prelipcean, G., M. Boscoianu, and M. Lupan, "An overview of the methodologies and politics of crisis management", Conferinta Strategii XXI: Spatiul sud-est European in contextual globalizarii, Universitatea Nationala de Aparare, Bucuresti, 12-13 aprilie 2007
- Priest, G., "The Government, the Market, and the Problem of Catastrophic Loss," *Journal of Risk and Uncertainty*, vol. 12, no. 2/3: (1996): 219-237.
- Russel, Thomas, "The Costs and Benefits of the Terrorism Risk Insurance Act: First Look," *NBER Insurance Conference paper* 2003, available at <http://www.nber.org/confer/2003/insurance03/russell.pdf>.

# **ANALYSIS OF FAILED STATES: SOME PROBLEMS OF DEFINITION AND MEASUREMENT**

**VALENTIN COJANU,<sup>1</sup>  
ALINA IRINA POPESCU<sup>2</sup>**

## **Abstract**

It has become a common claim that the gravest dangers to world security are no longer military threats from rival great powers, but rather transnational threats emanating from poorly governed countries.

Since the end of the Cold War, the international community has become increasingly preoccupied with the phenomenon usually named “state failure”, because state failure causes a wide range of humanitarian, legal, and security problems. Recent examples of failed states are familiar to all of us, from the total collapse of state institutions in Somalia and the disintegration of the former Yugoslavia to the varied crises in Rwanda, Haiti, Liberia, Congo, Sierra Leone, and Afghanistan. But how can we measure or define if a state is a “weak” or a “failed” state?

Due to the importance gained by this issue, several international organizations (World Bank, The Fund for Peace) and national institutions (U.S. National Security and the Commission on Weak States, United Kingdom’s Department for International Development) performed several surveys in this respect. This paper aims to identify and to analyze the ways to measure state failure and concludes with commentaries drawn on a contrasting perspective of three most renowned attempts (e.g. the Transformational Index of the Bertelsmann Foundation, the Governance Index of the World Bank, and the Failed States Index of the Foreign Policy Council).

**Keywords:** failed states, security, development

**JEL Classification:** F52, O19

---

<sup>1</sup> Professor, Ph.D., Department of International Business and Economics, Academy of Economic Studies, Bucharest, Romania, [cojanu@ase.ro](mailto:cojanu@ase.ro);

<sup>2</sup> Lecturer, Ph.D., Department of International Business and Economics, Academy of Economic Studies, Bucharest, Romania, [alina.popescu@rei.ase.ro](mailto:alina.popescu@rei.ase.ro).

## 1. The concept of “failed states”

There is a growing recognition of the threat to international security posed by failed and fragile states, often marred by serious internal conflict that also has the potential of destabilising neighbouring states and providing ungoverned territory that can provide safe haven for terrorists. The inability of their governments to provide basic services is considered a significant contributory factor. Poorly performing developing countries are linked to humanitarian catastrophes; mass migration; environmental degradation; regional instability; energy insecurity; global pandemics; international crime; the proliferation of weapons of mass destruction, and, of course, transnational terrorism.

Academics and policy-makers have been interested in state failure since the beginning of the 1990s. The concept of state failure was popularised by Madeleine Albright and others at the United Nations in the early 1990s (Gross, 1996), although the political scientist Robert H. Jackson was writing about a similar topic – under the label of ‘quasistates’ – even before 1990 (Jackson, 1987).

Other important early works on state failure include Helman and Ratner’s “*Saving Failed States*”, which was published in 1993 in *Foreign Policy* and argued for UN conservatorship in failed states (Helman and Ratner, 1993), and Kaplan’s influential 1994 *Atlantic Monthly* article, “*The Coming Anarchy*”, which described state failure in West Africa and darkly predicted that it would spread throughout the world (Kaplan, 1994).

Zartman’s (1995) edited work “*Collapsed States*” is the earliest book devoted entirely to state failure & collapse, while Gross (1996) attempted to construct a ‘taxonomy’ of failed states in 1996, placing them in *five categories*: ‘anarchic’, ‘phantom’, ‘anaemic’, ‘captured’, and ‘aborted’.

More recently, Baranyi and Powell (2005) argue that “conceptions of state fragility, weakness and failure converge around two ideas”. **First**, fragility refers to certain states’ inability and/or unwillingness to provide essential public goods like protection from external threats, rule of law and basic social services to most of their citizens. **Second**, fragility is a matter of degree - ranging from states that have ceased to exist in all but name and cannot provide protection or welfare to anyone, to certain states that can deliver most public goods to most of their citizens.

Despite the large body of scholarly writings on the subject, ***there is no agreement on the definition of state failure***. The most widely accepted definition is that offered by Zartman (1995), who defines failure as occurring when “***the basic functions of the state are no longer performed***”.

Patrick (2006) considers that “state strength is a relative concept and can be measured by the state’s ability and willingness to provide the fundamental political goods associated with statehood: *physical security, legitimate political institutions, economic management, and social welfare*”. Many countries have critical gaps in one or more of these four areas of governance. In effect, they possess legal but not actual sovereignty. In the ***security*** realm, they struggle to maintain a monopoly on the use of force, control borders and territory, ensure public order, and provide safety from crime. In the ***economic*** arena, they strain to carry out basic macroeconomic and fiscal policies or establish a legal and regulatory climate conducive to entrepreneurship, private enterprise, open trade, natural resource management, foreign investment, and economic growth. In the ***political*** sphere, they lack legitimate governing institutions that provide effective administration, ensure checks on power, protect basic rights

and freedoms, hold leaders accountable, deliver impartial justice, and permit broad citizen participation. Finally, in the *social* domain, they fail to meet the basic needs of their populations by making even minimal investments in health, education, and other social services.

Leading thinkers such as Fukuyama (2002) have said that, “since the end of the Cold War, weak and failing states have arguably become the single-most important problem for international order.” In Washington, Secretary of State Condoleezza Rice declared that nations incapable of exercising “responsible sovereignty” have a “spill-over effect in the form of terrorism, weapons proliferation, and other dangers” (quoted by Garfinkle, 2003).

In the United Kingdom, the Prime Minister’s Strategy Unit has advocated a government-wide approach to stabilizing fragile countries (PMSU, 2005), and Canada and Australia are following suit. The United Nations has been similarly engaged; the unifying theme of one series of proposals for the UN reform was the need for effective sovereign states to deal with today’s global security agenda. Kofi Annan remarked before the Council on Foreign Relations in New York in 2004 that, “whether the threat is terror or AIDS, a threat to one is a threat to all.... Our defences are only as strong as their weakest link.” (Annan, 2004)

Recent studies were conducted by Patrick (2006), Krasner and Pascual (2003), Clemens and Moss (2005), François and Sud (2006), Malek (2006) and others. All agree that **state failure** causes a wide range of humanitarian, legal, and security problems.

Among the **international agencies / bodies** involved in the creation of a strategy applicable to failed states we can mention: the World Bank, USAID, the OECD DAC, AusAID, DFID, and selected UN agencies. Most of these agencies/bodies are leaders in the community of donors working on fragile states, and all have strong policies regarding failed states. Many studies were conducted by specialists from these organisations.

The report of the US-government-commissioned *State Failure Task Force*, one of the most extensive studies of state failure, links state failure to widespread internal conflict that further destabilises an already shaky regime (State Failure Task Force, 2000). It may be argued that weak or failed states provide opportunities for actors outside the government – whether religious fundamentalists, disaffected citizens, or merely opportunists seeking power – to attempt to seize the state apparatus by violent means. According to the State Failure Task Force (2000), the internal conflict can take various forms:

- **Revolutionary wars.** Episodes of sustained violent conflict between governments and politically organised challengers that seek to overthrow the central government, to replace its leaders, or to seize power in one region.
- **Ethnic wars.** Episodes of sustained violent conflict in which national, ethnic, religious or other communal minorities challenge governments to seek major changes in status.
- **Adverse regime changes.** Major abrupt shifts in patterns of governance, including state collapse, periods of severe elite or regime instability, and shifts away from democracy towards authoritarian rule.
- **Genocides and politicides.** Sustained policies by states or their agents, or, in civil wars, by either of the contending authorities, that result in deaths of a substantial portion of a communal or political group.

Recently, Malek (2006) considers useful to assume the existence of the state monopoly over all of the national territory a central factor of a state’s effectiveness. In an effective state, there are neither separatist parts nor any areas “liberated” by rebels or regions constantly controlled by guerillas, warlords, and neighbouring countries, etc. “The division of a country’s territory is clearly indicating the failure of a state – in contrast to categories like its legitimacy in the

view of the population, the effectiveness of institutions, bureaucracy, corruption, and the functioning of the legal system, etc.” (Malek, 2006). As those are mainly subject to individual perception and bound to various traditions and customs, they are much more difficult to be operationalized and assessed.

**Table 1. Characteristics of strong and weak or failed states (Malek, 2006)**

<b>Characteristic</b>	<b>Strong state</b>	<b>Weak / failed state</b>
State monopoly on use of force	exists	more or less absent
Sovereignty of state	high	low
Quality of democracy	high	low
Legitimacy of state and citizens' loyalty to it	high	low
Security	high	low
State control of territory	exists	more or less absent
State control of borders	exists	more or less absent
Effectiveness of institutions, infrastructure and bureaucracy	high	low
Disposition of means of physical violence	concentrated in the hand of the state and of persons authorized by it	illegally also in the hand of non-state players
Corruption and crime	low	high or out of control
Legal order	reliable	unreliable and ineffective
Economy	functioning	in more or less deep crisis
Demographic changes	slight and under control	considerable and out of control, enormous streams of refugees, mass emigration

### **Effects of failed states**

In their paper “Promoting Stability and Development in Fragile and Failed States” François and Sud (2006) identified a series of **effects of failed states**:

#### ***Domestic effects***

The domestic effects of state failure and collapse are severe. “When the state cannot or will not fulfil its core functions, citizens suffer”. State collapse is especially devastating, as the total disintegration of public authority usually leads to violent contestation over who will control the state and obtain the benefits that international recognition brings.

Citizens flee in massive refugee flows. The effects of civil war persist for years after the war ends; these include increased mortality rates, inflated military spending, capital flight, loss of social capital, and low economic growth (World Bank, 2003).

#### ***Neighbourhood effects***

State failure and collapse also have strong regional effects. First, state failure itself can be contagious. The civil war that often accompanies state failure and collapse can easily spill over into neighbouring countries, leading to failure in those countries. Civil wars often ‘cluster’, as exemplified by Central America in the 1980s and the Balkans and African Great Lakes in the 1990s (World Bank, 2003). Secondly, state failure has large negative effects on economic growth in neighbouring countries. A recent World Bank study estimates that states sharing a border with a fragile or failed state – a ‘low-income country under stress’ or LICUS in the World Bank’s terminology – have economic growth rates that average 1.6 percentage points lower than those in states which are not neighbouring (Chauvet and Collier, 2005).

Finally, another enormous regional cost of state failure is the spread of malaria and HIV/AIDS that accompanies refugee flows (World Bank, 2003).

## *Global effects*

As the world becomes more and more interdependent, the global threats posed by state failure and collapse increase. When states lose control over what goes on within their borders, the result is ‘ungoverned spaces’. These lawless areas allow drug production and trafficking, international terrorism, and other global crime to flourish. Co-ordinated action on the part of the international community is essential to curb the global risks of failed states.

## **2. Defining and Identifying Failed States: Problems of Measurement**

There is no consensus on the precise number of weak and failing states. According to Patrick (2006), “the Commission on Weak States and U.S. National Security estimates that there are between 50 and 60; the United Kingdom’s Department for International Development classifies 46 nations with 870 million inhabitants as “fragile”; and the World Bank treats 30 countries as LICUS<sup>3</sup>.”

The World Bank has identified about 30 “low-income countries under stress,” whereas Britain’s Department for International Development has named 46 “fragile” states of concern. A report commissioned by the CIA has put the number of failing states at about 20.

*These divergent estimates reflect differences in the criteria used to define state weakness, the indicators used to gauge it, and the relative weighting of various aspects of governance.* The remainder of this section will contrast and discuss three of the most reputed measurements of the degree of state failure.

**A.** One of the most comprehensive and well-respected system for evaluating state performance is the **World Bank’s “Governance Indicators”**. The WGI cover 213 countries and territories and are based on several hundred variables produced by 25 different sources, including commercial data providers. (Kaufmann et al., 2006)

Since the 1990s, development researchers and practitioners have focused on “good governance” as both a means of achieving development and a development objective in itself. The World Bank has defined “good governance” as “epitomized by predictable, open and enlightened policy making; a bureaucracy imbued with a professional ethos; an executive arm of government accountable for its actions; and a strong civil society participating in public affairs; and all behaving under the rule of law.” (World Bank, 1994)

In response to the growing demand for measures of the quality of governance, a number of aggregate governance indicators have been produced, such as the World Bank’s Worldwide Governance Indicators (“WGI”).

The WGI rank countries with respect to *six aspects of good governance: Voice and Accountability, Political Stability and Violence, Government Effectiveness, Rule of Law, and Control of Corruption*. These indicators have been used by researchers as explanatory variables and by United States policymakers to allocate enormous aid packages.

Most recently, the indicators were defined as:

1. *Voice and Accountability (VA)*, the extent to which a country’s citizens are able to participate in selecting their government, as well as freedom of expression, freedom of association, and free media.

---

<sup>3</sup> Low-Income Countries Under Stress (LICUS)

2. *Political stability and absence of violence (PV)*, perceptions of the likelihood that the government will be destabilized or overthrown by unconstitutional or violent means, including political violence or terrorism.
3. *Government effectiveness (GE)*, the quality of public services, the quality of the civil service and the degree of its independence from political pressures, the quality of policy formulation and implementation, and the credibility of the government's commitment to such policies.
4. *Regulatory quality (RQ)*, the ability of the government to formulate and implement sound policies and regulations that promote private sector development.
5. *Rule of law (RL)*, the extent to which agents have confidence in and abide by the rules of society, and in particular the quality of contract enforcement, the police, and the courts, as well as the likelihood of crime and violence.
6. *Control of corruption (CC)*, the extent to which public power is exercised for private gain, including both petty and grand forms of corruption, as well as "capture" of the state by elites and private interests.

The indicators are not absolute measures of governance, but are measures of a country's relative rank with respect to that indicator. The indicators have been produced for 1996, 1998, 2000, 2002, 2004 and 2005 with global coverage, albeit with some missing values. Six papers have been written presenting the data sets. Most are published as World Bank Working Papers, but one has been published in a peer-reviewed journal.

Table 2 lists the 44 countries that rest in the bottom quintile, ranked from weakest (Somalia) to strongest (Algeria).

**Table 2. Bottom Quintile of Aggregate Governance Rankings**

Somalia (weakest)	Cote d'Ivoire	Venezuela
Iraq	Nigeria	Guinea
Myanmar	Laos	Togo
Democratic Republic of Congo	Angola	Azerbaijan
Afghanistan	Equatorial Guinea	Bangladesh
Liberia	Tajikistan	Cuba
Haiti	Republic of Congo	Iran
Zimbabwe	Belarus	Nepal
Turkmenistan	Chad	Libya
Sudan	Yemen	Syria
North Korea	Solomon Islands	Sierra Leone
Uzbekistan	West Bank/Gaza	Guinea-Bissau
Burundi	Pakistan	Cameroon
Central African Republic	Ethiopia	Comoros
	Eritrea	Algeria (strongest)

*Source:* Kaufmann, Kray, and Mastruzzi, *Governance Matters IV*, 2005

From the listing presented in Table 2, we can observe that *weak states are not necessarily poor states*. Accordingly, the fifth quintile includes several lower-middle-income countries, such as Venezuela, and excludes a few very poor countries, such as Gambia and Niger.

This definition of state weakness differs from that adopted by the *World Bank* and *OECD/DAC* donors, which restrict the category "fragile state" to very poor countries that are eligible for the bank's concessional (International Development Association) window and that score lowest on the bank's Country Policy and Institutional Assessment indicators. That approach, although consistent with the poverty reduction mandate of aid agencies, is overly

restrictive for policy analysts and officials interested in the security implications of weak governance across the entire range of developing countries.

**B.** To present a more precise picture of the scope and implications of the problem, **the Fund for Peace**, an independent research organization, and Foreign Policy have conducted a global ranking of weak and failing states<sup>4</sup>.

Using 12 social, economic, political, and military indicators, they ranked 60 states in order of their vulnerability to violent internal conflict. For each indicator, the Fund for Peace computed scores using software that analyzed data from tens of thousands of international and local media sources from the last half of 2004.

The resulting **index (Failed States Index)** provides a profile of the new world disorder of the 21st century and demonstrates that the problem of weak and failing states is far more serious than generally thought. About 2 billion people live in insecure states, with varying degrees of vulnerability to widespread civil conflict.

The **indicators** used by The Fund of Peace in composing the **Failed State Index** are:

***I. Social Indicators***

1. Mounting Democratic Pressures
2. Massive Movement of Refugees or Internally Displaced Persons creating Complex Humanitarian Emergencies
3. Legacy of Vengeance-Seeking Group Grievance or Group Paranoia
4. Chronic and Sustained Human Flight

***II. Economic Indicators***

5. Uneven Economic Development along Group Lines
6. Sharp and/or Severe Economic Decline

***III. Political Indicators***

7. Criminalization and/or Delegitimization of the State
8. Progressive Deterioration of Public Services
9. Suspension or Arbitrary Application of the Rule of Law and Widespread Violation of Human Rights
10. Security Apparatus Operates as a "State Within a State"
11. Rise of Factionalized Elites
12. Intervention of Other States or External Political Actors

Source: <http://www.fundforpeace.org/web/>

The FSI was first introduced in the July/August 2005 issue of Foreign Policy magazine. In 2005, it rated 75 countries; in 2006, the Index was expanded to include 146 countries. The 2007 Failed States Index (FSI) ranks 177 countries based on their social, economic, and political pressures.

**C.** The **Bertelsmann Transformation Index (BTI)** examines the political management of change on the way to a market-based democracy. To this end, the index provides *two rankings* and *two trend indicators*, which present the results of the comparative analysis. **The Status Index** shows the state of development that a country had achieved on the way to democracy and a market economy by the beginning of 2005.

The Status Index's overall result represents the mean value of the scores for the dimensions "Political Transformation" and "Economic Transformation".

---

<sup>4</sup> [www.foreignpolicy.com](http://www.foreignpolicy.com)



The score for "Political Transformation" is obtained by calculating the mean value of the ratings for the following criteria:

- Stateness
- Political Participation
- Rule of Law
- Stability of Democratic Institutions
- Political and Social Integration

The score for "Economic Transformation" is obtained by calculating the mean value of the ratings for the following criteria:

- Level of Socioeconomic Development
- Organization of the Market and Competition
- Currency and Price Stability
- Private Property
- Welfare Regime
- Economic Performance
- Sustainability

*The Management Index* classifies the quality of transformation management in the countries examined between 2003 and 2005. The trend indicators provide information on the direction of development in terms of democracy and a market economy in each of the countries examined from 2001 to 2005.

The study embraces 119 developing and transformation countries worldwide.

The **Methodology** for the BTI is represented by qualitative assessments by experts. Relying on 58 qualitative & quantitative indicators, experts on the country in question have, for each of the 119 countries, examined in detail to what extent the total of 19 criteria have been met. The BTI methodology has been slightly modified due to experience gathered in compiling the 2003 BTI and to other suggestions. The adjustments have been aimed at improving the BTI, its precision and its differentiation, without altering the objectives of the study or putting the comparability of the data at risk. With this aim in mind, the number of criteria and questions has been slightly reduced. The score forming the basis of the two indices is now derived from 58 separate questions — not from criteria as in 2003. To differentiate more precisely between the various countries, the results for the Status Index are also shown on a 10-point scale in the 2006 BTI — as opposed to a 5-point scale as in the 2003 BTI. The trend indicators for democracy and a market economy are shown separately in order to more clearly illustrate successes and setbacks in development. The level of difficulty in the Management Index was calculated with the aid of quantitative data.

Assessment efforts of the presented Indices present common components, such as: political and social issues. Still, major differences exist.

More particularly, The World Bank has developed sets of indicators focusing on *measuring governance* and has created metrics to track how well rule of law is being established in transitional societies and to identify the quality of life.

In addition to political indicators, economic indicators are almost all the time considered. Relevant approaches to measuring economic factors can be found both in The Fund of Peace and Bertelsmann assessment methodologies. In addition, The Bertelsmann Transformation Index assesses the quality of transformation management in the examined countries.

The framework is structured around determining conflict drivers and state/society capacities across five different “*pillars*” of analysis: Politics and Stable Democracy, Security, Rule of Law, Economic Sustainability, and Social Well-Being. Addressing the five pillars of analysis from both conflict drivers and capacity growth perspectives, the central judgment is determining the point at which the drivers of conflict have been sufficiently reduced and the institutional capacity of the state has sufficiently grown that the level of outside assistance can begin to be reduced.

All of these metrics approaches have been individually and manually crafted over time. Methodologies were continuously adapted and improved. This was done to address some difficulties of measurement, and assessment errors. Even the authors of the indicators have tried to draw attention to the large standard errors of the estimates – caveats that have been largely ignored.

### 3. Conclusions

This paper aims to create a comprehensive approach to the issue of economic development as influenced by the real-world problem of state weakness (see Cojanu and Popescu, 2006). Accordingly, it has been produced a synthesis of the theories on “failed states” and the range of policy ramifications.

It has been suggested that a set of indices may be used to present a diagnosis of the problem, the first step in devising strategies for strengthening weak and failing states. The more reliably policymakers can anticipate, monitor, and measure problems, the more they can act to prevent violent breakdowns, protect civilians caught in the crossfire, and promote recovery. Continuous monitoring of the measures, using the same assessment methodology, can inform decision making on strategies and programs.

At the same time, policymakers must focus on building the institutional capacity of weak states, particularly the “core five” institutions: military, police, civil service, the system of justice, and leadership. These are assessed in different ways by different authors and organizations. Still, the aim remains more or less the same: building strategies to strengthen failed states in the best possible way.

### References:

- Annan, K., (speech, Council on Foreign Relations, New York, December 16, 2004). See High-Level Panel on Threats, Challenges and Change, *A More Secure World: Our Shared Responsibility*, p. 9, 2004.
- Baranyi S., and Powell, K., *Fragile States, Gender Equality and Aid Effectiveness: A Review of Donor Perspectives*, The North-South Institute, For the Gender Equality Division (YWD), Policy Branch Canadian International Development Agency (CIDA), 2005, [http://www.nsi-ins.ca/english/pdf/Gender\\_FS\\_Paper\\_Donor\\_Perspectives.pdf](http://www.nsi-ins.ca/english/pdf/Gender_FS_Paper_Donor_Perspectives.pdf).
- Bertelsmann Stiftung, *Bertelsmann Transformation Index, 2006*, <http://www.bertelsmann-transformation-index.de/37.0.html?&L=1>.
- Chauvet, L., and Collier, P., *Development Effectiveness in Fragile States: Spillovers and Turnarounds*, 2005, <http://www.eldis.org/static/DOC16180.htm>.
- Clemens, M., and Moss, T., *Costs and Causes of Zimbabwe’s Crisis*, CGD Notes, July 2005, <http://www.cgdev.org/content/publications/detail/2918/>.
- Cojanu V., and Popescu A.I., *A Developmental Perspective on Conflicts in South-Eastern Europe*, Romanian Journal of European Affairs, 2007.

François, M., and Sud, I., *Promoting Stability and Development in Fragile and Failed States*, Development, Policy Review Vol. 24, Issue 2, page 14, 2006.

Fukuyama, F., *State-Building: Governance and World Order in the 21st Century* (Ithaca, N.Y.: Cornell University Press, 2004), p. 92. See John J. Hamre and Gordon R. Sullivan, "Toward Postconflict Reconstruction," *The Washington Quarterly* 25, no. 4, 85–96, 2002.

Garfinkle, A., *A Conversation With Condoleezza Rice*, *American Interest* 1, no. 1 (Autumn 2005): 47–50. See Richard Haass, "Sovereignty: Existing Rights, Evolving Responsibilities" (speech, Georgetown University, Washington, D.C., January 14, 2003), <http://www.state.gov/s/p/rem/2003/16648.htm>.

Gross, J.G., *Towards a Taxonomy of Failed States in the New World Order: Decaying Somalia, Liberia, Rwanda and Haiti*, *Third World Quarterly* 17:3, 1996.

Helman, G.B. and Ratner, S.R., *Saving Failed States*, *Foreign Policy*, 89, 3-20, 1993.

Jackson, R.H., *Quasi-States, Dual Regimes, and Neoclassical Theory: International Jurisprudence and the Third World*, *International Organization* 41 (4), 519-49, 1987.

Kaplan, R.D., *The Coming Anarchy*, *Atlantic Monthly* 273 (2) : 44-65, 1994.

Kauffmann, D., Kray, A., and Mastruzzi, M., *Governance Matters IV: Governance Indicators for 1996–2004*, Washington, D.C.: World Bank, 2005.

Krasner, S.D., and Pascual, C., *Addressing State Failure*, *Foreign Affairs* 84, no. 4 (July/August 2005): 153–163; USAID, *Fragile States Strategy* (Washington, D.C.: USAID, February 2005); Robert Zoellick, "CAFTA Is a Win-Win," *Washington Post*, May 24, 2005.

Malek M., *State Failure in the South Caucasus: Proposals for an Analytical Framework*, *Transition Studies Review* 13 (2): 441–460, 2006.

Prime Minister's Strategy Unit (PMSU), *Investing in Prevention: An International Strategy to Manage Risks of Instability and Improve Crisis Response*, London: PMSU, 2005.

State Failure Task Force, *State Failure Task Force Report: Phase III Findings*, McLean, VA: Science Applications International Corporation, 2000.

Stewart, P., *Weak States and Global Threats: Fact or Fiction?*, The Center for Strategic and International Studies and the Massachusetts Institute of Technology, *The Washington Quarterly*, 29:2 pp. 27–53, 2006.

World Bank, *Breaking the Conflict Trap: Civil War and Development Policy*, Washington, DC: Oxford University Press for the World Bank, 2003.

Zartman, I.W. (ed.) *Collapsed States: The Disintegration and Restoration of Legitimate Authority*, Boulder, CO: Lynne Rienner, 1995.

<http://www.foreignpolicy.com>

### Failed States List (Fund of Peace)

#### 2007

177 states were included in the list, of which 32 were classified as "alert", 97 as "warning", 33 as "moderate", 15 as "sustainable". The worst 20 states are shown below. For the entire ranking see List of countries by Failed States Index. Change in rank from 2006 is shown in parentheses.

- |                                       |                                                   |                                       |
|---------------------------------------|---------------------------------------------------|---------------------------------------|
| 1. <a href="#">Sudan</a> (0)          | 8. <a href="#">Afghanistan</a> (+2)               | 15. <a href="#">Uganda</a> (+6)       |
| 2. <a href="#">Iraq</a> (+2)          | 9. <a href="#">Guinea</a> (+2)                    | 16. <a href="#">Bangladesh</a> (+3)   |
| 3. <a href="#">Somalia</a> (+4)       | 10. <a href="#">Central African Republic</a> (+3) | 17. <a href="#">Nigeria</a> (+5)      |
| 4. <a href="#">Zimbabwe</a> (+1)      | 11. <a href="#">Haiti</a> (-3)                    | 18. <a href="#">Ethiopia</a> (+8)     |
| 5. <a href="#">Chad</a> (+1)          | 12. <a href="#">Pakistan</a> (-3)                 | 19. <a href="#">Burundi</a> (-4)      |
| 6. <a href="#">Côte d'Ivoire</a> (-3) | 13. <a href="#">North Korea</a> (+1)              | 20. <a href="#">Timor-Leste</a> (N/A) |
| 7. <a href="#">Congo</a> (-5)         | 14. <a href="#">Burma/Myanmar</a> (+4)            |                                       |

Source: [http://www.fundforpeace.org/web/index.php?option=com\\_content&task=view&id=229&Itemid=366](http://www.fundforpeace.org/web/index.php?option=com_content&task=view&id=229&Itemid=366)

#### 2006

146 states were included in the 2006 list, of which 28 were classified as "alert", 78 as "warning", 27 as "moderate", 13 as "sustainable". The worst 20 states are shown below. Change in rank from 2005 is shown in parentheses.

- |                                       |                                                   |                                        |
|---------------------------------------|---------------------------------------------------|----------------------------------------|
| 1. <a href="#">Sudan</a> (+2)         | 8. <a href="#">Haiti</a> (+2)                     | 15. <a href="#">Burundi</a> (+3)       |
| 2. <a href="#">Congo</a> (0)          | 9. <a href="#">Pakistan</a> (+25) <sup>[21]</sup> | 16. <a href="#">Yemen</a> (-8)         |
| 3. <a href="#">Côte d'Ivoire</a> (-2) | 10. <a href="#">Afghanistan</a> (+1)              | 17. <a href="#">Sierra Leone</a> (-11) |
| 4. <a href="#">Iraq</a> (0)           | 11. <a href="#">Guinea</a> (+5)                   | 18. <a href="#">Burma/Myanmar</a> (+5) |
| 5. <a href="#">Zimbabwe</a> (+10)     | 12. <a href="#">Liberia</a> (-3)                  | 19. <a href="#">Bangladesh</a> (-2)    |
| 6. <a href="#">Chad</a> (+1)          | 13. <a href="#">Central African Republic</a> (+7) | 20. <a href="#">Nepal</a> (+15)        |
| 7. <a href="#">Somalia</a> (-2)       | 14. <a href="#">North Korea</a> (-1)              |                                        |

Source: <http://fundforpeace.web.cedant.com/programs/fsi/fsindex2006.php>

# **AID AND MIGRATION: SUBSTITUTES OR COMPLEMENTS? GLOBAL PATTERNS AND EUROPEAN PERSPECTIVE**

**JEAN-CLAUDE BERTHÉLEMY<sup>1</sup>,  
MONICA BEURAN<sup>2</sup>,  
MATHILDE MAUREL<sup>3</sup>**

Second draft, 7 October, 2007

## **Abstract**

This paper examines the determinants of migration from developing, emerging and transition economies to developed countries, using a recent dataset on bilateral migrations. It tests whether such global patterns may explain East-West migration within Europe. It contributes to the debate on foreign policy coherence by studying the complementarities that may exist between migration and foreign financial assistance, suggested by the strong positive correlation that is observed between aid and migration. This correlation is studied in a simultaneous equations model, which analyses both the consequences of migrant lobbying on aid allocation and the positive influence of foreign assistance policy on migration. We find also that growth of income in developing countries may stimulate rather than dampen emigration from these countries, when their income is below a threshold of about US\$4600 per capita in PPP. Hence, foreign assistance cannot be considered as an instrument to reduce migration pressure from relatively poor countries. These conclusions are particularly relevant in the context of the policy debates on the European enlargement. From a policy viewpoint, at least three patterns of East-West European migration should be differentiated: from the relatively rich new members of the European Union, from relatively poor countries in the Balkans, and from other relatively poor but remote Eastern European countries.

The authors thank participants at the conference Social Security and Labour Mobility in the Enlarged EU, Fudan University, Shanghai (China), 14-15 September 2007, for helpful comments.

---

<sup>1</sup> Centre d'Economie de la Sorbonne, University Paris 1, France.

<sup>2</sup> Centre d'Economie de la Sorbonne, University Paris 1, France.

<sup>3</sup> Centre d'Economie de la Sorbonne, University Paris 1, France.

## **1- Introduction**

In the globalization process, movements of labour have been to some extent liberalized, with a doubling of the share of international immigrants in the population of developed countries between 1970 and 2000, although this liberalization has been modest and resisted by a number of governments. Confronted with non-desired international immigration pressure, some governments are tempted to raise various barriers to international labour movements. However, such policies have two potential shortcomings. First, they stimulate illegal immigration, which in some countries, particularly in Europe, is hard and costly to prevent, and can create in turn severe social and political tensions. Second, they are possibly inconsistent with other foreign policy instruments that are used in vis-à-vis countries of origin of potential immigrants, notably development assistance policies.

Specifically, in Europe, it would be inconsistent to assist neighbouring countries in their development and to prevent migration of workers from the same neighbours. The development of Southern neighbours of Europe is dramatically hampered by excess labour supply, notably in Mediterranean countries. In Central and Eastern Europe, job destructions during the transition process has stimulated emigration flows to Western Europe; the political will of progressive integration of these transition economies into the European Union would have been inconsistent with harsh policies vis-à-vis Europeans migrating from East to West.

More generally, immigration policy is a core concern in the whole debate that has emerged in OECD countries about the coherence of their foreign policies vis-à-vis developing and transition economies (OECD, 2006). Trade opening, facilitation of international investment, foreign aid and migration controls form a complex mix of policies that cannot be considered in isolation. They interact with each other, and to be efficient they must be designed and implemented in a coherent manner.

Several aspects of the policy coherence debate have been already considered in the previous literature. Substitutability or complementarities between trade and factor movements is an old theme in the international economics literature since the seminal work of Mundell (1957), but a theme that has also been revisited with new results, suggesting possible complementarities between labour flows and trade in particular (Markusen, 1983). Schiff (2006) provides a recent survey on recent developments in this literature.

In this paper, we consider another aspect of the policy coherence debate, namely whether aid and migration policies are substitutes or complements. To our knowledge very few empirical papers have answered precisely these questions. Lucas (2004) looks at aid data to check whether aid flows concentrate mainly on migrant-sending countries; Stalker (2000) reveals some correlation but argues that former colonial ties have the main influence. This question is particularly relevant from a policy perspective in Europe, since the European Commission has for long time implemented assistance policies toward countries that were in the process of being integrated in the European Union. "Structural Fund" policies have played a key role in the integration on Ireland, Greece, Portugal and Spain in the European Union, and a similar policy is now implemented in favour of new members of the European Union in Central and Eastern Europe. Of course, these policies have similarities with foreign assistance that is given to other neighbours of Europe, notably Southern Mediterranean countries, in the context of the Barcelona process.

One major difficulty faced by researchers in this area is the lack of good data on migrations. In this paper, we take advantage of the recent release by the World Bank of an update of the global data base of the Development Research Centre on Migration, Globalisation and

Poverty, which consists of a 226x226 matrix of origin-destination stocks by country (see Parsons et al., 2007, for a complete description of the database). This dataset provides however only one point observation in time, for the year 2000, which creates a major limitation on quantitative research that can be done with it. In particular we have not enough information to study precisely intra-European migrations alone, both because the number of observations of migration between Central/Eastern Europe and Western Europe is limited, and because the process of migration in Europe is relatively recent, insofar as it has started on a large scale only after the end of the Cold War, and is probably still ongoing. For this reason, we have chosen to start our enquiry by looking at global patterns of migrations from developing, emerging and transition economies to developed countries, that we will call henceforth “South/North” migration. Subsequently, we test whether parameters estimated for the whole “South/North” migration behaviours apply also to European East/West migrations. We find indeed some differences, but also a number of commonalities between the European East/West migrations and the whole “North/South” migrations.

The paper is organized as follows. In section 2, we describe our main data and provide some stylised facts on “South/North” migration. In section 3, we present our analytical framework. In section 4 we estimate our model on “South/North” migrations. In section 5, we study the specificities of European East/West migrations and derive from our estimations some lessons for the analysis of European integration policies. We conclude in section 6.

## **2- Data and stylised facts**

Since we have chosen to work on “South/North” migration only, our main data source is a matrix of stock of migrants from 187 sending countries, which are developing, emerging and transition economies, to 22 OECD member countries (the members of the Development Assistance Committee of the OECD), estimated for the year 2000. We consider whether these migrations are influenced by economic, geographic, demographic and cultural factors. We pay particular attention to the interaction that may exist between foreign assistance policy and migrations. Data sources are detailed in Appendix 1.

Table 1 shows the overall geographical structure of international “South/North” migrants. The largest destination of migrants is Northern America, which corresponds to the fact that United States and Canada are by nature immigration countries, like Australia and New Zealand. These four “western offshoots” have been historically major destination of migrants, given the small size of their native population. The “old” Europe is the second largest destination, well above developed Asia and Oceania (made of Japan and of Australia and New Zealand, which attract many migrants but are demographically small countries compared to Japan). The vast majority of immigrants in Northern America come from the neighbouring Latin America (notably from Mexico), while immigrants in Western Europe are diversified, coming from the neighbouring Central and Eastern Europe and Africa and the Middle East, but also from Asia (principally from former colonies in South Asia and Indochina, and to some extent from China).

Table 1: Migrants in proportion of total "South/North" migration

	Northern America	Developed Asia & Oceania	Western Europe	Total
Africa & Middle East	4.4%	0.8%	18.4%	23.9%
Latin America	31.2%	0.9%	4.3%	36.4%
Developing Asia & Oceania	14.2%	3.6%	6.6%	24.2%
Central & Eastern Europe	4.7%	0.7%	10.0%	15.5%
Total	54.6%	6.0%	39.4%	100.0%

Source: Authors' computations

The relative weights of the different regions of origin are however very different, Asia being much more populated than Africa and Central & Eastern Europe. For this reason, it is useful to consider also ratios of migrants divided by population of origin. Table 2 provides this information. It shows that people who migrate the most are citizens from Latin American countries (mostly Mexican immigrants in the United States), and then citizens from Central and Eastern European countries. Africans migrate less, although significantly, to Western Europe, and Asians much less.

Table 2: Migrants in proportion of population of country of origin

	Northern America	Developed Asia & Oceania	Western Europe	Total
Africa & Middle East	0.3%	0.0%	1.1%	1.4%
Latin America	3.0%	0.1%	0.4%	3.4%
Developing Asia & Oceania	0.2%	0.1%	0.1%	0.4%
Central and Eastern Europe	0.8%	0.1%	1.6%	2.5%

Source: Authors' computations

Hence, it seems that distance plays a major role in migration behaviours: people tend to migrate to neighbouring countries or regions. Historical ties and cultural factors, such as common languages, probably play also a significant role, as suggested by the large number of immigrants coming from former colonies. In Europe, 35 percent of immigrants come from former colonies.

Considering the purely economic determinants of migration, a standard intuition, consistent with the seminal Harris and Todaro (1970) model, is that migration is positively influenced by the income per capita in the country of destination, relative to the income per capita in the country of origin. Stylised facts do not confirm this intuition. The correlation between GDP per capita and immigrants per capita in developed countries is insignificant (Figure 1). The correlation between GDP per capita and emigrants per capita in developing, emerging and transition economies is significantly positive, rather than negative, at the 2% significance level. This positive correlation masks however a more complex pattern: there is a positive correlation for relatively low levels of GDP per capita and a negative correlation afterwards. This hump-shaped pattern can be related to the existence of costs of migration, which reduce migration possibilities in poor countries. Migration costs include a lot of elements, from geographical distance - closer countries being more open to two-ways migrations - to common language, and historical ties implying overall knowledge of the destination country's habits. While some estimates exist (Martin, 2006), they are too scarce to be used in an econometric analysis. The reasons offered for migration humps include also demographic factors (Hatton and Williamson, 1998, 2002), industrial restructuring, and higher returns to remittances and migrants' networks.



Faini and Venturini (1993) relate the evolution of migration observed in Europe from the 1960s to the 1980s to this migration hump framework; they find a negative relation between migration and development for Greece, Portugal and Turkey, but not for the more advanced Spain or Italy. Clark *et al.* (2002), studying immigration to the United States between 1971 and 1998, find a negative relationship between income and migration from middle-income and high-income countries that reverses for low-income countries. Cogneau and Gubert (2005) highlight that Mali and Mexico are two countries where most migration comes from regions not classified as among the poorest.

Figure 1: immigration and GDP per capita in destination countries

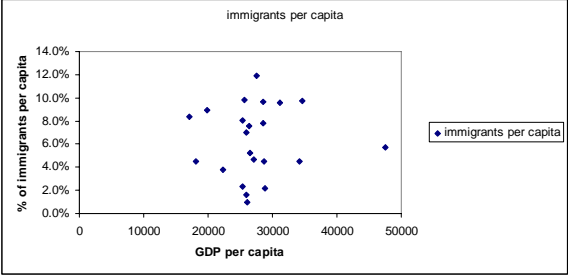
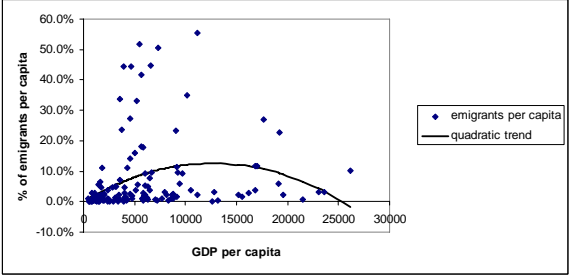


Figure 2: emigration and GDP per capita in origin countries



Source : Authors' computations

Aid may influence migration indirectly through its impact on income, but we have to consider also the existence of direct links between migrations and foreign aid. In the aid allocation literature, there is a standard argument, developed by Lahiri and Raimondos Møller (2000), saying that immigrants act as a lobbying force, in developed countries, in favour of development assistance allocation to their home countries. Stylised facts are consistent with this view. In most cases, countries that belong to the first quintile of aid recipients of a donor country are by far the main sources of immigration in that donor country: on average, immigrants coming from such countries that are the main beneficiaries of donor aid allocation policies account for 44 percent of total immigrants in donor countries, and this ratio is well above 50 percent in all donor countries but the United States and European Nordic countries. However, this observation requires further scrutiny, for two reasons. First, both variables may be correlated simply because they are correlated to a third variable, e.g. geographical proximity or historical and cultural ties. Second, the proportion of migrants coming from countries which are principal aid recipients is probably too high to result only from lobbying activities of immigrants: we observe this concentration even in donor countries which are not major destinations of immigrants, such as Italy, Japan or Spain. Actually, this correlation may be due to a reverse link, from aid to migration. Aid concentration in a given recipient country may stimulate migration into the donor country because it facilitates contacts and population movements with this donor country, through various channels such as technical assistance. Specifically, at least in some donor countries, a significant part of official development assistance is related to financing of scholarship for foreign students and support granted to refugees in donor countries. For instance in France these two components account for about 25 percent of total ODA in recent years. Such assistance may have a major impact on migration, insofar as it facilitates the mobility of foreigners to donor countries.

## Analytical framework

We propose in what follows an econometric analysis of the joint determination of migration and aid allocation. As just explained, there can be a two-way interaction between these two variables, and they may have also common explanatory factors. Hence we estimate a joint simultaneous model of two equations: migration and aid allocation. We also introduce the possibility that unobserved variables co-determine aid and migration, which in econometric terms implies a correlation between the error terms of the two equations be correlated. Hence the system can be written as follows:

$$\text{Migration}_{ij} = \alpha_1 + \beta_1 \text{Aid}_{ij} + \Gamma_1 X_{ij} + u_{ij}$$

$$\text{Aid}_{ij} = \alpha_2 + \beta_2 \text{Migration}_{ij} + \Gamma_2 Y_{ij} + v_{ij}$$

$$\text{Corr}(u, v) = \rho$$

where  $i$  stands for the country of origin of migration,  $j$  for the country of destination;  $X$  and  $Y$  are matrices of explanatory variables of, respectively, migrations and aid allocation (identification conditions require that  $X$  and  $Y$  be different);  $u$  and  $v$  stand for error terms;  $\alpha$ ,  $\beta$  and  $\Gamma$  are parameters. Parameters are estimated using the three-stage least square method, which permits both to correct possible simultaneity biases and to take account of the correlation between residuals of the two equations.

Observations are for the year 2000, with some exceptions. First, in order to smooth out fluctuations in aid flows, aid flows are averages over the years 1996 to 2000. Second, some explanatory variables in the  $X$  and  $Y$  vectors are lagged in order to avoid simultaneity issues.

Explanatory variables for migration (vector  $X$ ) that we have tested are the following:

- GDP per capita of the sending and the receiving country. In principle the latter has a positive parameter, while the former may have a positive or negative parameter, depending on whether the fixed cost effect or the relative income effect dominates.
- Population of the sending and the receiving country. In principle, both have positive parameters, but small size of the sending country may result in higher migration, since in a small country the only migration possibility is international migration, while in a large country it can be in some instances inter-regional migration.
- Bilateral distance between the sending and the receiving country.
- Dummy variables representing historical ties: a “former colony” dummy equal to 1 when countries  $i$  and  $j$  have had in the past a colonial relation and equal to zero otherwise; a dummy for common language. We also further test whether some post-colonial ties are more influential than others (e.g. within the Commonwealth, labour mobility is easier than between France and former French colonies).
- Dummy variables that take account of some stylised facts identified in the previous section: the fact that “western offshoots” have more immigrants than the “old” Europe; the strong link between United States and Latin America; and the cultural specificity of Japan, which has very restrictive attitudes vis-à-vis immigration.
- Trade intensity, measured by bilateral export from country of emigration to country of immigration, as a ratio of GDP of the country of emigration; a positive parameter would imply that labour flows and external trade are complements, while a negative parameter would imply that there are substitute.

Explanatory variables for aid allocation (vector Y) that we have tested correspond principally to previous findings by Berthelemy (2006), who has estimated aid allocation equations on bilateral time series. These variables are the following:

- Total aid budget by donor j (the parameter for this variable is expected to be reasonably close to 1).
- Trade intensity, measured by bilateral export from the donor to the recipient, as a ratio of GDP of the donor. Berthelemy (2006) already found that donors give more assistance to recipients that are major trade partners. In order to avoid simultaneity biases, this variable is lagged by 5 years.
- GDP per capita of the recipient, and its population.
- The same colonial dummies as before, to which we add a dummy variable equal to 1 for assistance provided by Japan to Asian countries, which takes into account the geopolitical specificity of the Japanese foreign policy in favour of Asia.
- Variables describing the quality of institutions. Here we depart from Berthelemy by using the World Bank's governance indicators developed by Kaufmann, Kraay and Mastruzzi (2005), namely: voice and accountability, political stability, government effectiveness, regulatory quality, rule of law and control of corruption.

For both the migration and aid allocation equation, there is a standard technical problem here, related to the censored nature of the dependent variable, which cannot be negative. Estimating such equations with all observations would result in potentially large biases. In the aid allocation literature, this problem is frequently treated by estimating equations on samples restricted to strictly positive variables. This permits also to specify equations in logarithmic form, which facilitates interpretation of parameters as elasticities. We adopt this logarithmic specification form here. This method may result however in a second bias – known as the selection bias –, which results from the fact that the selection of a country as a recipient of assistance (or as destination of migration) may depend on variables that also influence the amount of assistance (or the number of migrants). There is no perfect solution to this problem, in absence of variables that would explain the selection of a country, but not the amount of aid (or the number of migrants), that it receives. The most frequent approach is to assume that the selection bias is of second order, and we adopt this approach here. In his paper on aid allocation, Berthelemy (2006), which used on a much larger dataset because it had a time-series dimension, has found that there was no significant correlation between selection of aid recipients and aid allocation, suggesting that there is no significant selection bias.

### **3- Results for the whole “South/North” dataset**

Table 3 reports the main findings of estimation of our model of joint determination of migration and aid allocation. Each estimation is made of two equations: a migration equation [migr\_x] and an aid allocation equation [aid\_x].

Since we are principally interested in migration behaviours, the aid equation is reported here only for reference. Its properties are very similar to equations estimated by Berthelemy (2006), with the expected negative sign for the GDP per capita variable and positive signs for the trade intensity variable, the former colony dummy variable (with a significantly higher parameter for former Spanish colonies), and the Japan – Asia dummy variable. The sign of population is also positive.

With respect to the governance variables, we find that two of them are significant, and lead to very similar results: voice and accountability and quality regulation. We show results for both variables in Table 3 (resp. equations \_1 and \_2). Finally, we find that migrations influence aid allocation, but only to a limited extent. Our data are consistent with the hypothesis of existence of lobbying activities by immigrants in donor countries in favour of their countries of origin, but introducing this variable does not alter the significance of other cultural proximity variables, such as the post-colonial dummy variable. Moreover, it contributes only modestly to explain the overall correlation observed between migration and aid allocation, as suggested by the much larger parameter of aid in the migration equation that we comment hereafter.

Table 3: Preliminary results of estimation (three-stage least-squares)

	[Migr_1]	[Migr_2]	[Aid_1]	[Aid_2]
Aid	0.478 *** (13.050)	0.465 *** (12.730)		
GDP per capita_south	0.891 *** (17.680)	0.881 *** (17.580)	-1.326 *** (17.990)	-1.302 *** (17.830)
Population_north	0.399 *** (8.250)	0.408 *** (8.460)		
Population_south	0.551 *** (18.180)	0.557 *** (18.470)	0.178 *** (4.340)	0.156 *** (3.840)
Distance	-0.810 *** (13.360)	-0.802 *** (13.240)		
Common language	0.852 *** (7.090)	0.857 *** (7.120)		
Former colony	0.839 *** (3.830)	0.861 *** (3.940)	0.918 *** (3.800)	0.928 *** (3.840)
Former colony of Portugal	2.350 ** (3.380)	2.376 ** (3.400)		
Former colony of Spain			1.343 ** (2.950)	1.331 ** (2.900)
Former colony of UK	0.632 * (2.060)	0.627 * (2.040)		
USA-Latin America	0.725 * (2.420)	0.748 * (2.490)		
Japan-Asia			1.288 *** (3.710)	1.292 *** (3.690)
Western offshoots	1.640 *** (14.070)	1.630 *** (13.960)		
Japan	-3.640 *** (20.620)	-3.640 *** (20.630)		
Migrations			0.090 ** (2.640)	0.091 ** (2.650)
Total aid of donor			1.153 *** (25.210)	1.153 *** (25.180)
Trade intensity	0.085 *** (3.590)	0.088 *** (3.690)	0.351 *** (10.240)	0.342 *** (9.890)
Voice & accountability			0.259 *** (3.900)	
Regulation quality				0.235 ** (3.280)
Intercept	-8.463 *** (7.170)	-8.695 *** (7.380)	3.093 * (2.380)	3.128 * (2.390)
Number of observations	1560	1560	1560	1560
R2	0.6671	0.6712	0.5222	0.5222

Note: \*\*\*(resp. \*\*, \*, +) significant at 0.1 percent (resp. 1 percent, 5 percent, 10 percent). t-Student between brackets. \_south stands for the country of origin of migrants and \_north for their country of destination.

Source: Authors' computations

We find extremely significant parameters for most variables, with the right sign, in the migration equation estimations. However, the GDP per capita of countries of destination is not significant, or when it is significant it has the wrong sign. One possible explanation is that all our 22 countries of destination are rich countries, with relatively small differences of GDP per capita. In addition, many factors, beyond GDP per capita, may affect disparities of purchasing power actually obtained by migrants in the different immigration countries, and most of these factors are not observed here. For instance, depending on the functioning of the labour markets, immigrants, who are outsiders in the market, may face different obstacles in their search for a job. Such unobservable disparities, notably in terms of unemployment rates of immigrants, are potentially of much bigger magnitude than GDP per capita variations. Therefore, we have decided to drop the GDP per capita of the immigration country from our list of explanatory variables. This does not affect the rest of our results. Moreover, we have checked (results not shown) that when we consider worldwide migrations, and not only “North/South” migrations, the variable GDP per capita of the country of destination has the expected significant negative sign.

Foreign assistance exerts a significant and relatively large positive influence on migration. Certainly, the large parameter that we report should be interpreted with caution. It is possible that the influence of foreign assistance on migration be related to other factors than the impact of financial resources that are spent in favour of refugees and of students coming from recipient countries. It may be also related to the existence of some form of policy coherence between financial assistance and forms of foreign policy, including immigration policy. It is however impossible to fully disentangle this question. To do this, we would need detailed data on amounts of assistance that directly influence migrations, such as refugee and students support, to check whether the other assistance flows are also correlated with migrations.

In addition, a more detailed discussion of policy coherence would be necessary, going far beyond our present analysis. First of all, not all donor countries have the same degree of consistency in their foreign policies. This is amply suggested by information collected by the Centre for Global Development to produce its “Commitment to Development Index” (Roodman, 2005). For instance, the migration component of this index shows that France and Japan, which are among the biggest donors of foreign assistance, are also among the countries that implement the hardest immigration policies. Also, Nordic countries, which give a lot of financial assistance in proportion of their GDP, and are ranked very high by the Centre for Global Development for their aid policies, do not perform particularly well with respect to immigration policies. Second, some donors attract skilled migrants from developing countries, hence destroying capacities that they have contributed to build through their financial support. This issue cannot be explored with our data, but is documented with some examples by OECD (2006), notably regarding the emigration of skilled personnel in the health sector.

Population and distance variables have the right signs, respectively positive and negative. Our dummy variables have also the expected signs. Countries of origin of migrants which have a common language or a common colonial history with a developed country send more migrants to this country. The United States attracts similarly more people from Latin America. We find also that the United Kingdom and Portugal attract particularly more migrants from their former colonies than the other former colonial powers do. Finally, we find that the “western offshoots” attract more migrants than the “old” European countries, and Japan less.

Table 4: Results of estimation with a quadratic term for GDP per capita of country of origin

	[Migr_3]	[Migr_4]	[Aid_3]	[Aid_4]
Aid	0.503 *** (14.350)	0.485 *** (13.990)		
GDP per capita_south	3.844 *** (6.180)	3.777 *** (6.060)	-1.351 *** (18.510)	-1.329 *** (18.360)
GDP per capita_south2	-0.183 *** (4.660)	-0.180 *** (4.560)		
Population_north	0.369 *** (7.840)	0.382 *** (8.120)		
Population_south	0.521 *** (17.870)	0.530 *** (18.290)	0.149 *** (3.690)	0.126 ** (3.150)
Distance	-0.810 *** (13.540)	-0.801 *** (13.420)		
Common language	0.870 *** (7.360)	0.878 *** (7.400)		
Former colony	0.767 *** (3.550)	0.793 *** (3.690)	0.788 ** (3.300)	0.801 ** (3.350)
Former colony of Portugal	2.384 *** (3.500)	2.419 *** (3.540)		
Former colony of Spain			1.276 ** (2.880)	1.266 ** (2.830)
Former colony of UK	0.734 * (2.440)	0.727 * (2.410)		
USA-Latin America	0.595 * (2.030)	0.625 * (2.120)		
Japan-Asia			1.388 *** (4.120)	1.396 *** (4.100)
Western offshoots	1.612 *** (14.080)	1.604 *** (13.970)		
Japan	-3.558 *** (20.450)	-3.564 *** (20.500)		
Migrations			0.144 *** (4.330)	0.143 *** (4.290)
Total aid of donor			1.112 *** (24.660)	1.113 *** (24.680)
Trade intensity	0.088 *** (3.780)	0.091 *** (3.910)	0.341 *** (10.130)	0.332 *** (9.770)
Voice & accountability			0.278 *** (4.280)	
Regulation quality				0.260 *** (3.700)
Intercept	-19.204 *** (6.900)	-19.277 *** (6.920)	3.578 ** (2.790)	3.621 ** (2.800)
Number of observations	1560	1560	1560	1560
R2	0.6553	0.6615	0.5281	0.5283

Note: \*\*\*(resp. \*\*, \*, +) significant at 0.1 percent (resp. 1 percent, 5 percent, 10 percent). t-Student between brackets. \_south stands for the country of origin of migrants and \_north for their country of destination.

Source: Authors' computations

The parameter for GDP per capita of the country of origin of migrants has a positive parameter, suggesting that the effect of fixed costs of migration globally prevails on the effect of relative income comparison. However, consistently with stylised facts observed in previous section (Figure 2), it is likely that this effect of GDP per capita of the country of origin be negative after some threshold. This is tested in Table 4 (equations \_3 and \_4) by introducing a quadratic term. After taking account of the indirect effect of GDP per capita through aid allocation, we may conclude from estimations of equations \_3 that the total income effect is positive below a threshold about US\$5700, in PPP terms (and US\$6000 when we use

equations \_4 estimates). Hence, for most developing countries, the total income effect on migration would be positive, while for most emerging and transition economies it would be close to zero or negative.

The threshold should depend upon the costs of migrations, which are related, among other factors, to the distance to destination country. We interact GDP per capita and squared GDP per capita with the logarithm of distance (see Appendix 2), and find some significant results in equations\_6. We compute the thresholds obtained for the mean logarithm of distance (US\$5600 with equations \_6 estimates), mean minus one standard error (US\$3400) and mean plus one standard error (US\$22900). Our results are consistent with the intuition of migration costs being a decreasing function of distance.

#### **4- Differences between “South/North” equations and European “East/West” equations**

Can we interpret these results as describing all migration patterns from relatively poor countries to relatively rich countries? This is unlikely, given that from one region of the world to the other, and from one country to the other, there are vast differences of contexts that may affect migration behaviours, which cannot be taken into account in our econometric exercise. In this section, we check whether the European region has specific behaviours. Migrations within Europe may differ from migrations from developing to developed countries for several historical reasons. Until WWI, Europe had a geopolitical structure very different from what it became in the XXth century. The Austro-Hungarian Empire has been dismantled. Central and Eastern Europe has been separated from Western Europe during the cold war, and the end of the cold war has in turn created new waves of migrations from East to West. Migrations within Europe have been also revitalized in the past 15 years in the context of the enlargement process of the European Union. The civil war in former Yugoslavia and its dismantlement have pushed emigration from South-Eastern Europe.

We have tested the existence of specific behaviours of migration within Europe by introducing a dummy variable equal to 1 when the country of origin is in Central and Eastern Europe (including Cyprus and Malta, which have been included in the process of enlargement of the European Union), and the country of destination is in Western Europe (including non-EU members for which data are available, i.e. Norway and Switzerland). A Wald test performed on equations \_1 and \_2 shows that the vector of parameters of variables interacted with this European dummy variable is significantly different from zero, at the 0.1 percent level. Further scrutiny of results obtained for the different variables interacted with the European dummy suggests that three of them are very significant: the GDP per capita of the country of origin, the population of the country of origin, and the intercept. Results obtained after dropping the other variables, which are much less significant, are reported in Table 5. These results show that the GDP per capita of the country of origin influences negatively emigration from Central and Eastern European countries. Relatively rich countries such as Malta or Cyprus send, in proportion of their populations, large numbers of emigrants abroad. Moreover, the income of Central and Eastern European countries is in most cases above the threshold where its effect on migrations changes of sign, from positive to negative, in our previous regressions: close to three quarter of them have a GDP per capita above US\$5700.

Table 5: Results of estimation with specific parameters for European countries

	[Migr_5]	[Migr_6]	[Aid_5]	[Aid_6]
Aid	0.487 *** (13.340)	0.475 *** (13.070)		
GDP per capita_south	0.947 *** (18.200)	0.935 *** (18.070)	-1.330 *** (18.070)	-1.306 *** (17.920)
GDP per capita_south (Europe)	-1.015 *** (4.880)	-1.030 *** (4.930)		
Population_north	0.379 *** (7.880)	0.386 *** (8.040)		
Population_south	0.545 *** (17.750)	0.552 *** (18.050)	0.180 *** (4.380)	0.156 *** (3.840)
Population_south (Europe)	-0.423 (1.840)	-0.455 * (1.970)		
Distance	-0.871 *** (11.990)	-0.849 *** (11.750)		
Common language	0.842 *** (7.050)	0.850 *** (7.100)		
Former colony	0.846 *** (3.880)	0.867 *** (3.990)	0.928 *** (3.850)	0.936 *** (3.880)
Former colony of Portugal	2.341 ** (3.400)	2.367 ** (3.420)		
Former colony of Spain			1.313 ** (2.890)	1.296 ** (2.830)
Former colony of UK	0.645 * (2.110)	0.634 * (2.070)		
USA-Latin America	0.628 * (2.090)	0.662 * (2.200)		
Japan-Asia			1.276 *** (3.700)	1.282 *** (3.690)
Western offshoots	1.678 *** (14.470)	1.666 *** (14.360)		
Japan	-3.612 *** (20.620)	-3.612 *** (20.630)		
Migrations			0.088 ** (2.610)	0.090 ** (2.650)
Total aid of donor			1.154 *** (25.290)	1.152 *** (25.240)
Trade intensity	0.093 *** (3.930)	0.097 *** (4.070)	0.351 *** (10.290)	0.343 *** (9.930)
Voice & accountability			0.270 *** (4.070)	
Regulation quality				0.246 ** (3.460)
Intercept	-7.881 *** (6.430)	-8.201 *** (6.700)	3.121 * (2.400)	3.177 * (2.430)
Intercept (Europe)	14.841 ** (3.080)	15.496 ** (3.210)		
Number of observations	1560	1560	1560	1560
R2	0.6697	0.6734	0.5219	0.5222

Note: \*\*\*(resp. \*\*, \*, +) significant at 0.1 percent (resp. 1 percent, 5 percent, 10 percent). t-Student between brackets. \_south stands for the country of origin of migrants and \_north for their country of destination. Z\_[Europe] stands for Z multiplied by the dummy variable equal to 1 when both partners are European countries.

Source: Authors' computations



Such results suggest that, at the current stage of development of European transition economies, policies that are implemented by the European Union to facilitate the economic integration of non-members, and sustain a reduction of income disparities between East and West, will hardly stimulate migrations from East to West, and may prevent them in the most advanced new EU-members.

Of course, at the policy making level, a case-by-case discussion would be necessary. Emigration from relatively poor countries such as Albania, Armenia, Azerbaijan, Georgia or Moldova may be positively influenced by initial steps of development of their economies. Such migrations are however dampened by the distance of these countries from Western Europe. Conversely, emigration from already relatively rich countries may be slowed down by further development of their economies. This is in particular the case of all twelve new members of the European Union, whose GDP per capita is above US\$5900.

We find also that population size of the country of origin of migrants does not affect positively, neither negatively, migrations within Europe. This is due in particular to large migration flows out of the Balkans. Albania, Bosnia and Serbia, whose populations are 20 to 50 times smaller than Russian population, send each more emigrants to Western Europe than Russia. Among other European countries, only Poland has a number of emigrants to Western Europe equivalent to that of these countries. Emigration from these countries is partly specific, due to movements of refugees associated with the security crisis in the former Yugoslavia in recent years. But it is also associated with factors that are common with other countries in the South-Eastern European region. Other countries in the Balkans such as Romania and Bulgaria are also among the principal countries of origin of East/West migration within Europe. The small size of these countries, inherited from the historical events of the past century, is in itself a factor that may stimulate migration. In such small countries, internal migration is not an option, and therefore mobile labour can only move internationally. The same pattern is observed in other small European countries, such as Cyprus and Malta.

From a policy making point of view, these observations on the influence of size of emigration countries suggest that a better sub-regional integration within Europe might provide a partial solution to reduce migration from East to West. This is particularly true of course for the Balkans, which have sent large numbers of refugees to Western Europe.

## **5- Conclusion**

We have found in this paper that foreign assistance and migration are complements. They influence each other positively, suggesting that there is on average some consistency between immigration policies and foreign aid allocation policies, although there are well known examples of policy incoherence in some donor countries and in some sectors. Such policy coherence is all the more necessary that, for poor developing countries, increase in income per capita that would be promoted by efficient aid policies would also in a first step stimulate rather than dampen emigration forces.

Our exercise has also provided an assessment of the empirical pertinence of the lobbying model proposed by Lahiri and Raimondos Møller (2000). We have found actually a significant influence of migrants on aid allocation, as suggested by their model, but we have found also that this channel explains only a minor part of the observed correlation between aid and migration, the biggest part of which being potentially attributable to policy coherence between immigration and foreign aid policies.

With some alterations of our model, we have also derived lessons from our exercise for the analysis of East-West European migrations. The promotion of development of new members of the European Union should not accelerate emigration to Western Europe, given that these new members have already reached relatively high levels of income per capita. Sources of emigration within Europe are principally in the Balkans. Such migrants come from countries that are small, relatively poor, plagued by security issues, and geographically close to Western Europe. Probably the only policy that would help reducing such migration pressure would be to improve security and avoid political disintegration within this sub-region. Other relatively poor Eastern European countries, like Albania, Armenia, Azerbaijan, Georgia or Moldova, could also become significant sources of emigration to Western Europe, but there are more distant from Western Europe and are, maybe for this very reason, considered less strategic by the European Union in its foreign and regional integration policy.

## APPENDIX 1

Table A1: Data Sources and Definitions

Variable name	Source	Definition
Migration	Development Research Centre on Migration, World Bank	Stock of migrants
Aid	DAC database, OECD	Aid flows averaged on a five-years period (1996-2000), constant prices 2000 US\$
Total aid donor	DAC database, OECD	Sum of total aid flows committed by a donor, constant prices 2000 US\$
GDP per capita_north	World Development Indicators, World Bank	GDP per capita of migrants home country, constant prices 2000 US\$
GDP per capita_south	World Development Indicators, World Bank	GDP per capita of migrants host country, constant prices 2000 US\$
Population_north	World Development Indicators, World Bank	Population of migrants home country, million inhabitants
Population_south	World Development Indicators, World Bank	Population of migrants host country, million inhabitants
Distance	CEPII database	Bilateral distance between home and host country
Common language	CEPII database	Dummy variable, equals 1 if the home and the host country share a common language
Former colony	CEPII database	Dummy variable, equals 1 if the home and the host country have a colonial link
Former colony of Portugal	Own calculations	Dummy variable, equals 1 if the home country is a former colony of Portugal
Former colony of Spain	Own calculations	Dummy variable, equals 1 if the home country is a former colony of Spain
Former colony of UK	Own calculations	Dummy variable, equals 1 if the home country is a former colony of United Kingdom
USA-Latin America	Own calculations	Dummy variable, equals 1 if the home country is a Latin American country and the host country is United States of America
Japan-Asia	Own calculations	Dummy variable, equals 1 if the recipient is an Asian country and the donor is Japan
Western offshoots	Own calculations	Dummy variable, equals 1 if the host country is Australia, New Zealand, Canada or United States of America
Japan	Own calculations	Dummy variable, equals 1 if the host country is Japan
Europe	Own calculations	Dummy variable, equals 1 if the home country is a Central and Eastern European country and the host country is a Western European country
Trade intensity	Feenstra et al. database (2005), NBER	Exports from the donor to the recipient country, % of donor's GDP, lagged by 5 years
Voice & Accountability Regulatory quality	Kaufmann et al. database (2005), World Bank	Measured in units ranging from -2.5 to 2.5, with higher values corresponding to better governance outcomes

## APPENDIX 2

Table A2: Results of estimation with GDP per capita and quadratic GDP per capita of country of origin interacted with distance

	[Migr 7]		[Migr 8]		[Aid 7]		[Aid 8]
Aid	0.512 *** (14.480)		0.493 *** (14.020)				
GDP per capita_south	16.331 (1.900)		13.368 (1.550)		-1.346 *** (18.380)		-1.319 *** (18.170)
GDP per capita_south (squared)	-1.079 * (2.100)		-0.902 + (1.750)				
GDP per capita_south*Distance	-1.506 (1.530)		-1.175 (1.190)				
GDP per capita_south	0.107 + (1.830)		0.088 (1.490)				
Population_north	0.359 *** (7.630)		0.374 *** (7.950)				
Population_south	0.518 *** (17.890)		0.528 *** (18.350)		0.158 *** (3.900)		0.135 ** (3.360)
Population_south (Europe)	4.140 (1.010)		2.780 (0.680)				
Distance	0.845 *** (7.150)		0.857 *** (7.230)				
Common language	0.808 *** (3.740)		0.832 *** (3.870)		0.819 ** (3.430)		0.836 *** (3.490)
Former colony	2.304 ** (3.390)		2.337 ** (3.420)				
Former colony of Portugal					1.255 ** (2.830)		1.252 ** (2.780)
Former colony of Spain	0.693 * (2.310)		0.689 * (2.290)				
Former colony of UK	0.505 (1.720)		0.540 (1.830)				
USA-Latin America					1.368 *** (4.060)		1.370 *** (4.010)
Japan-Asia	1.694 *** (14.480)		1.688 *** (14.400)				
Western offshoots	-3.512 *** (20.310)		-3.516 *** (20.320)				
Japan					0.137 *** (4.140)		0.134 *** (4.010)
Migrations					1.115 *** (24.770)		1.119 *** (24.820)
Total aid of donor					0.337 *** (9.970)		0.330 *** (9.640)
Trade intensity					0.290 *** (4.440)		
Voice & accountability							0.260 *** (3.690)
Regulation quality	-59.678 (1.660)		-47.857 (1.330)		3.375 ** (2.620)		3.401 ** (2.620)
Intercept	1560.000 (0.659)		1560.000 (0.666)		1560.000 (0.528)		1560.000 (0.528)
Intercept (Europe)	14.818 ** (3.070)		14.841 ** (3.080)		0.229 (1.130)		0.315 (1.560)
Number of observations	1560		1560		1560		1560
R2	0.6699		0.6738		0.5216		0.522

Note: \*\*\*(resp. \*\*, \*, +) significant at 0.1 percent (resp. 1 percent, 5 percent, 10 percent). t-Student between brackets. \_south stands for the country of origin of migrants and \_north for their country of destination.

Source: Authors' computations

## References

- Berthélemy, Jean-Claude (2006), Bilateral Donor's Interest vs. Recipients' Development Motives in Aid Allocation: Do All Donors Behave the Same?, *Review of Development Economics*, 10(2): 179-194.
- Clark, X., Hatton, T. and J. Williamson (2002), "Where Do US Immigrants Come From? Policy and Sending Country Fundamentals", NBER Working Paper 8998, National Bureau of Economic Research, Cambridge, Mass. (June).
- Cogneau, D. and F. Gubert (2005), "Migrations du Sud, Pauvreté et Développement", in E.M. Mouhoud (éd.), *Les nouvelles migrations*, Editions Universalis.
- Faini, Riccardo, and Alessandra Venturini (1994), Migration and Growth: The Experience of Southern Europe, CEPR Discussion Paper n° 964.
- Faini, R. and A. Venturini (1993), "Trade, Aid and Migrations: Some Basic Policy Issues", *European Economic Review*, vol. 37, pp. 435-442.
- Harris, John R., and Michael P. Todaro (1970) Harris J. and M. Todaro (1970), Migration, Unemployment & Development: A Two-Sector Analysis, *American Economic Review*, 60(1):126-42.
- Hatton, T. and J. Williamson(1998), "The Age of Mass Migration: Causes and Impact", Oxford University Press, New York.
- Hatton, T. and J. Williamson(2002), "What Fundamentals Drive World Migration?", paper presented at the Conference on Poverty, International Migration and Asylum, Helsinki, September 27-28.
- Kaufmann, Daniel, Aart Kraay and Massimo Mastruzzi (2005), Governance matters IV: governance indicators for 1996-2004, Volume 1 of 2, World Bank, Working Paper n° 3630.
- Lahiri, Sajal, and Pascalis Raimondos-Møller (2000), "Lobbying by Ethnic Groups and Aid Allocation," *Economic Journal*, 110 (2000): C62-79.
- Lucas, R.E.B. (2004), "International Migration to the High Income Countries: Some Consequences for Economic Development in the Sending Countries", Paper prepared for the Annual World Bank Conference on Development Economics – Europe, Brussels.
- Markusen, James R. (1983), Factor Movements and Commodity Trade as Complements, *Journal of International Economics*, 14(3-4): 341-356.
- Mundell, Robert A. (1957), International Trade and Factor Mobility, *American Economic Review*, 47(3): 321-335.
- OECD (2006), Migration, Aid and Trade: Policy Coherence for Development, OECD, Development Centre, Policy Brief n°28.
- Parsons, Christopher R., Ronald Skeldon, Terrie L. Walmsley, and L. Alan Winters (2007), Quantifying International Migration: A Database of Bilateral Migrant Stocks, World Bank, Working Paper n° 4165.
- Roodman, David (2005), An Index of Donor Performance-Revised August 2005, Center for Global Development, Working Paper n°67.
- Stalker, P. (2000), "Workers without Frontiers: The Impact of Globalisation on International Migration", Lynne Rienner Publishers, Boulder, CO.
- Schiff, Maurice (2006), Migration, Investment and Trade: Substitute or Complements? Paper presented at the AfD / EUDN Conference on "Migration and Development: Mutual Benefits?", Paris. <http://www.eudnet.net/download/Schiff.pdf>
- Vogler, M. and R. Rotte (2000), "The Effects of Development on Migration: Theoretical Issue and New Empirical Evidence", *Journal of Population Economics*, Vol.13, pp. 485- 508.
- Martin, Philip L (2006), "The Trade, Migration, and Development Nexus", mimeo, University of California at Davis. <http://www.dallasfed.org/news/research/2006/06migr/martin.pdf>

# THE BENEFICIARIES OF THE “REFORMED TREATY”

RAZVAN BUZATU<sup>1</sup>

As the world globalizes to the extent to which we become neighbors with our fellow human beings from America or China or India or anywhere else in this global village that we live in, we become globalized ourselves, acting at continental, regional or local levels. Some of us are active players in building new edifices, while some of us retain the place of witnesses to these actions. Both are influenced by these changes, some in a positive manner others in a negative manner.

As the world changes, we face a plethora of challenges that give us the opportunity to provide solutions to the problems of the 21<sup>st</sup> century. In this diverse global environment, we see global actors as integrators of the solutions found at continental, regional and local levels.

Europe is in a constant change. The European Union is in a constant change. We can see this by the last 50 years of struggle to build a European edifice that, supposedly, will unite Europe, politically, economically, socially and culturally. We see our Europe as becoming one of the global actors. But, in order for this to be achieved, we must come to an agreement of what this European edifice will look like and, consequently, how will it become more effective and visible on the global stage. By we, I mean the citizens of Europe, the social sector, the private sector, the local public administrations, mass-media, the national parliaments and governments, the European officials.

If we look at the recent informal meeting in Lisbon of the Heads of State and Government of the EU, i.e. the Autumn 2007 Intergovernmental Conference, one could argue the fact that we already have an agreement. True. But upon what do we have an agreement?! Is it on a European Union, is it on a European Confederation, is it on a European Community, is it on a European Federation of Nation-States, is it on a Federal Europe or is it on the United States of Europe. Of course, one could do a PhD thesis on any of these possible European architectures. Still, the question remains. How do we see the future of Europe? Before deciding if we need a Constitution for Europe, first we must agree amongst ourselves what kind of European edifice would need a Constitution of Europe. I am not talking about how will we name this European edifice, but, instead what would be its values and principles. A Constitution should establish the relations between the citizens of Europe and the institutions of the edifice to be built. When we will have decided all this, we can start building trust throughout Europe and its citizens.

---

<sup>1</sup> Expert in EU affairs, PhD. Candidate; Adviser at the Committee for European Affairs of the Parliament of Romania; former adviser at the Committee for Foreign Affairs and at the Committee for Civil Liberties, Justice and Home Affairs of the European Parliament; former member of the National Secretariat of the Romanian Delegation to the European Convention for the Future of Europe; former adviser to the President of the Sub-Committee for External Relations of the Council of Europe Parliamentary Assembly; former adviser of the President of the OSCE Parliamentary Assembly; e-mail: [rbuzatu@gmail.com](mailto:rbuzatu@gmail.com) , [rbuzatu@cdep.ro](mailto:rbuzatu@cdep.ro) .

The European Union lacks a lot of things. If we are over-pessimistic, then we will not be able to build anything. If we are over-enthusiastic, then we will not see our deficiencies when we lay down the bricks and layers for the future of Europe. Giving the impression of combining those two characteristics, the “Heads of State and Governments of Europe”, reached an accord on how better to cut and paste the Constitutional Treaty, leaving the European Union with merely a treaty.

But, let us see how was it done and if the other components of the debate were taken into consideration.

Even if the idea and ideal of creating a united Europe goes a long way back in time, we can see that as the European edifice evolved from the stage of European Communities to the European Union, *it was always sealed under the form of treaties*, and only some of these treaties provided the distinct historical momentum to celebrate the progress.

The European Convention for the Future of Europe that started in the year 2002 and ended formally in 2003 and informally with the signing of the Treaty establishing a Constitution for Europe in Rome of 2004, created such a momentum.

Europe, at that time, decided to meet and discuss the next steps of the evolution of the European Union, having in mind to put on paper the values and principles of a Constitution for Europe. The outcome of this unique diplomatic exercise was the fact that we started to speak about a Constitution for Europe, about integrating the European Union policies, about integrating the Charter of Fundamental Rights, and hoping that after the ratification of the Treaty establishing a Constitution for Europe, we could move to the next phase, acknowledging officially that the European Union has evolved to the stage of a European Federation of Nation-States.

Hence, after another period of time would have passed, we could have debated about the creation of a Constitution of Europe, thus entailing the presence on the European continent of a Federal Europe. But it was not meant to be. Not yet anyway. In our enthusiasm created by the success of the debates, the members of the European Convention left out three very important aspects.

Firstly, the fact that the citizens of Europe, even if, for the purposes of argument, say they were ready to become European citizens, could not understand the so technical, too wide and political thick book that spoke about how their future would be. They were more concerned with their day-to-day life and keeping or improving their standards of living. And who can blame them for not seeing the link between a possible “Treaty” or “Constitution” for Europe and their standards of living. The fathers of the future of Europe should have taken the time to explain it to them.

Secondly, even if some of the representatives of the national parliaments and governments of the EU member states were very much involved in drafting the Constitution for Europe, after the European Convention ended in 2003 they went back to their countries and found themselves amongst the few that realized the importance of the debates that took place at the European Convention. At the informal meeting in Rome, the Heads of State and Governments kept their influence over the institutions of the European Union, by changing much of the Constitutional Treaty (i.e. Constitution for Europe) into the Treaty establishing a Constitution for Europe. The importance of national politics again retained its place in front of European politics. The importance of the national interest retained its rightful place, at a rightful time, in front of the European interest. For those who believe that the national interest will fade in time as much as we give up our sovereignty, I will just say that the European interest is closely linked to the national interest to the extent that they become complementary. The European interest is the summing up

of all the national interests of the EU member states and finding the common denominator to act at community level, thus creating the premises and the basis for the next phase in the evolution of Europe: the Federal Europe.

Thirdly, the lack of disseminating the information and results of the European Convention, and afterwards, the lack of communicating and advertising the newly signed Treaty establishing a Constitution for Europe to the citizens of Europe, plus the ever so changing and influencing national political environment, gave us the negative votes of France and the Netherlands in 2005. So, the ratification process was stopped, sending the European Union back to the reflection phase.

Europe is evolving at its own pace. It has its own time. What I believe we should do is see at what stage it has arrived presently, what the reality of the European policies is and how are the widening and deepening going along so far. Coming down to earth from the ideals is as necessary for the European Union as air. Striking and keeping the balance between ideals, reality and the citizens is necessary.

The drafting phase for the new document which would show the next stage of the European Union started at the beginning of the year 2006, through inter-parliamentary meetings with the European Parliament and at the academic level. After a year and half of debating and after several presidencies of the EU sought to put on their agendas the topic of re-negotiation and adoption of a new version of the Treaty establishing a Constitution for Europe, we find ourselves in the position where we do not have anymore such a document. Instead, we have an intergovernmental treaty, with bits and pieces of the original constitutional document.

From this moment on, we cannot speak anymore of a Treaty establishing a Constitution for Europe, of a Constitutional Treaty or better yet, of a Constitution for Europe. What we have at our grasp is the two basic treaties of Nice, i.e. the Treaty on the functioning of the European Union and the Treaty establishing the European Community, flanked by the European Atomic Energy Treaty, that were amended. The procedure of amendment followed the same as with Amsterdam or Nice. So, it is improper to speak about a “Reformed Treaty” in the sense that it was thought about, because we did not reform anything, we amended what it existed and we provided the governments with the necessary tools to create the procedure of self-amendment for the next steps. The outcome was “The Lisbon Treaty”. The final result will be at the end of 2009, after ratification.

“The Lisbon Treaty” retained some aspects of the Treaty establishing a Constitution for Europe, but left out the whole preamble, the symbols of the Union and some nuances regarding legislation. The difference is that the Treaty establishing a Constitution for Europe was set to replace all the earlier treaties. Instead, the Lisbon Treaty only amends the Nice Treaty, even if some amendments are taken from the Treaty establishing a Constitution for Europe *per se*. These aspects can be observed quite easily.

A first aspect is that the European Union will have a legal personality, giving it legitimacy and one voice around the world, instead of confusion brought about by the different messages sent by various heads of European Union institutions.

A second aspect taken from the original document is that a chosen politician will be president of the European Council for a two-and-a-half year period, thus replacing the current six month rotating system of presidency of the European Union.



A third aspect is the creation of a new position of High Representative of the Union for Foreign Affairs and Security Policy instead of a Foreign Minister of the Union. This position will combine the posts of foreign affairs official, Javier Solana, and of external affairs commissioner, Benita Ferrero-Waldner.

A fourth aspect is that, as of 2014, we will have a smaller European Commission, with fewer commissioners than there are member states.

A fifth aspect is the redistribution of voting weights between the member states due to take place between the years 2014 and 2017.

A sixth aspect is the new powers given to the European Parliament, the European Commission and European Court of Justice and moving to majority voting in new areas, thus removing vetoes from the national level to the community level.

A seventh aspect is that it gives national parliaments a bigger say in European Union affairs.

So, where do we stand? Until 2009, we will still apply the Treaty of Nice, which has become unfitting for a Europe of 27 members. Better yet, as opposed to the Treaty establishing a Constitution for Europe, were in order to stop the entry into force of the document, we needed less than 1/5<sup>th</sup> <sup>2</sup> of the member states to vote against, with the Lisbon Treaty we only need one negative vote out of 27 members. Now isn't that quite nice?

The 10 new member states that entered the European Union in 2004, plus Romania and Bulgaria in 2007, have negotiated and signed their Accession Treaties based on the Nice Treaty and not on the Treaty establishing a Constitution for Europe. But, in case the latter would have been ratified, the Accession Treaties contained the necessary provisions that would have entered into force automatically and updated the new-comer states to the new document.

The reactions of the EU member states representatives that participated in the informal meeting in Luxembourg (at foreign minister level) and then in Lisbon (at heads of state and governments level) were as different as their own political and national interests. Yet an agreement emerged out of the darkness. What if the United Kingdom had their "red lines" to iron out with the EU and now that it is done, they will vote YES? What if Belgium will still vote over 90% in favor of the "Lisbon Treaty"? What if France reconsiders its position and gives a positive vote? But, yet again why shouldn't it change its views one more time? What if the Dutch reconsider the no vote in 2005 and should decide to vote even more overwhelmingly against the "Lisbon Treaty"? What if Ireland is in favor, but, as with Nice in 2001, the referendum called according to its constitution will go negative? And what if Poland, seeing the French and Dutch negative votes in 2005, will be even more fervently for approving the "Lisbon Treaty"? What if Bulgaria, needing to show the muscle of the new-comer negotiated and got the concession of the Cyrillic EVRO symbol and for this it will vote in favor? What if?

---

<sup>2</sup> The provisions regarding ratification of the Constitutional Treaty (Art. IV-447): in the case of an eventual impasse due to the fact that one or more States fail to ratify, the Declaration adopted by the Heads of State and Governments (annexed to the Constitutional Treaty and based on Art. IV-443, par. 4) suggests a political solution. Hence, it is envisaged that, "if two years after the signature of the treaty amending this Treaty", a small minority of Member States (less than 1/5<sup>th</sup>) "has encountered difficulties in proceeding to ratification, the matter is referred to the European Council".

As you can see, there are always envisaged the opinions and interests of the most influential states from within the EU, whilst the smaller states remain, at times, unsatisfied with the outcome of negotiations. This is the reason why the seats in the European Parliament were re-negotiated and the votes in the Council of the EU weighted so that one, two or more larger states would not be able to impose a decision on a group of smaller states. The balance will be self-evident when we will start applying this system, from 2014, that is if the “Lisbon Treaty” is being ratified by then.

We saw the ingredients of the negotiations of this new document. All of them resume to politics, interests – national and European alike -. So, the true beneficiaries are the governments of the EU member states. The main beneficiary, in the long term, is Europe. The rightful beneficiaries of the negotiations and their results – “the Lisbon Treaty” - should be the citizens of Europe and their interests. If one participates in the public debates of the civil society in the EU, take Debate Europe Forum for instance, scrolling down over the many topics, one can find out what the interests of a part of the citizens of Europe and of the EU are: interests such as social welfare and their family; its external borders and immigration; preserving the environment and finding new alternate energy sources and last, but not least, Europe's global role.

Europe should open up to its citizens constantly through their elected representatives, while the governments should put into practice the necessary mechanisms to give the people an increasing standard of living. The citizens of Europe should decide if they are satisfied with remaining consumers of EU legislation or they become more active in initiating it. With this new form of document, “the Lisbon Treaty”, the citizens of Europe will have the right and means to initiate EU legislation based on a million signatures. Is that too much for an EU of 500 million people? But, will this suffice in order to increase the awareness of the EU and the governments of the EU member states to involve citizens much more in building the architecture of the future of Europe or will we need more?

#### **References:**

##### **I. Official documents of the Intergovernmental Conference of the EU on the Reformed Treaty**

[IGC 2007 Opinion of the Committee of the Regions entitled "Relaunching the process of reforming the European Union in anticipation of the European Council of 21 and 22 June 2007"](#), CIG 7/07, 27/07/2007

[2007 IGC Indicative and forward timetable of the Working Party of Legal Experts](#), CIG 6/07, 24/07/2007

[IGC 2007 Statement by Ms Anna E. Fotyga, Polish Minister for Foreign Affairs, on the occasion of the opening of the Intergovernmental Conference](#), CIG 5/07, 25/07/2007

[IGC 2007 Draft Treaty amending the Treaty on European Union and the Treaty establishing the European Community – Draft Preamble](#), CIG 4/1/07 REV1, 5/10/2007

[IGC 2007 Draft Treaty amending the Treaty on European Union and the Treaty establishing the European Community – Draft Preamble](#), CIG 4/07, 24/07/2007

[IGC 2007 Draft Treaty amending the Treaty on European Union and the Treaty establishing the European Community – Protocols](#), CIG 2/1/07 REV1, 5/10/2007

[IGC 2007 Draft Treaty amending the Treaty on European Union and the Treaty establishing the European Community – Protocols](#), CIG 2/1/07 REV1|COR1, 12/10/2007

[IGC 2007 Draft Treaty amending the Treaty on European Union and the Treaty establishing the European Community – Protocols](#), CIG 2/07, 23/07/2007

[IGC 2007 Draft Treaty amending the Treaty on European Union and the Treaty establishing the European Community](#), CIG 1/1/07 REV1, 5/10/2007

[IGC 2007 Draft Treaty amending the Treaty on European Union and the Treaty establishing the European Community](#), CIG 1/07, 23/07/2007

[IGC 2007 Draft Treaty amending the Treaty on European Union and the Treaty establishing the European Community](#), CIG 1/07 COR1, 3/08/2007

Convening of an Intergovernmental Conference [en](#) [fr](#)

Reforming Europe for the 21st Century

Opinion of the European Commission, pursuant to Article 48 of the Treaty on European Union, on the Conference of representatives of the governments of the Member States convened to revise the Treaties [en](#) [fr](#)

European Parliament resolution of 11 July 2007 on the convening of the Intergovernmental Conference (IGC): the European Parliament's opinion (Article 48 of the EU Treaty) [en](#) [fr](#)

Council's opinion in favor of convening an Intergovernmental Conference under Article 48 of the TEU [en](#) [fr](#)

Opinion of the European Central Bank of 5 July 2007 at the request of the Council of the European Union on the opening of an Intergovernmental Conference to draw up a Treaty amending the existing Treaties [en](#)

Amendment of the Treaties on which the Union is founded [en](#) [fr](#)

IGC 2007 Mandate [en](#) [fr](#)

Treaty reform process (extract of the European Council Presidency conclusions of 23 June 2007) [en](#) [fr](#)

## **II. Octobre 2007 - documents approuvés lors de la réunion informelle des chefs d'État et de gouvernement des 18 et 19 octobre 2007 à Lisbonne**

Protocole (no 9 bis) sur la Décision du Conseil relative à la mise en œuvre des articles 9 C, paragraphe 4, du traité sur l'Union européenne et 205, paragraphe 2, du traité sur le fonctionnement de l'Union européenne entre le 1er novembre 2014 et le 31 mars 2017, d'une part, et à partir du 1er avril 2017, d'autre part

Déclaration ad articles 9 C, paragraphe 4, du traité sur l'Union européenne et 205, paragraphe 2, du traité sur le fonctionnement de l'Union européenne

Déclaration concernant la délimitation des compétences

Composition du Parlement européen

Déclaration concernant l'article 222 du traité sur le fonctionnement de l'Union européenne relative au nombre d'avocats généraux à la Cour de justice

Déclaration concernant l'article 9 E du traité sur l'Union européenne

Projet de traité modifiant le traité sur l'Union européenne et le traité instituant la Communauté européenne - Projet de préambule

Projet de traité modifiant le traité sur l'Union européenne et le traité instituant la Communauté européenne

### III. Internet sources

The Constitutional Process – The European Convention - <http://european-convention.eu.int>

### IV. Books

**Albu Cornel, Andreescu Eugen, Carata Viorel** - *Piata comuna si perspectiva anului 2000*, Bucuresti, 1993.

**Alexandrescu Gr., Popa V.** - *Posibile arhitecturi institutionale europene*, Editura Universitatii Nationale de Aparare, Bucuresti, 2004.

**Giuliano Amato** - *A Strong Heart for Europe*, Robert Schumann Centre for Advanced Studies at the European University Institute, Florence and Harvard Law School, 2000;

**Barbulescu Iordan Gheorghe** - *UE de la national la federal*, Editura Tritonic, Bucuresti, 2005.

**Barbulescu Iordan Gheorghe** - *UE de la economic la politic*, Editura Tritonic, Bucuresti, 2005.

**J.M.Beneyto** - *What is the European Constitution? The declaration on the future of the Union and setting up a common constitutional order*, European Commission, Public debate on the Future of the Europe, 2001;

**Bertrand Christoph** - *Europa in balanta*, Clavis, Bucuresti, 1996

**Bibere Octav** - *Uniunea Europeana între real si virtual*, Bucuresti, Editura All, 1999.

**Blidar Gheorghe, Florea Paul Tiberiu** - *Banca Europeana de Investitii. Promotorul dezvoltarii Uniunii Europene*, Editura Bibliotheca, Targoviste, 2006.

**Booker Christopher, North Richard** - *Uniunea Europeana sau Marea amagire. Istoria secreta a constructiei europene*, Editura Antet, Filipestii de Targ, 2004.

**Brague Rémi** - *Europa, calea romana*, Editura Idea Design & Print, Cluj, 2002.

**Brădescu Faust** - *Europa unită*, Editura Majadahonda, Bucuresti, 2000.

**Busek Erhard, Werner Mikulitsch** - *Uniunea Europeana si drumul catre rasarit*, Editura Institutul European, Iasi, 2005.

**Carp Radu** - *Proiectul politic european, de la valori la actiune comuna*, Editura Universitatii din Bucuresti, Bucuresti, 2006;

**Courty Guillaume, Devin Guillaume** - *Constructia europeana*, Editura C.N.I. "Coresi" SA, Bucuresti.

**Cowles Maria Green, Smith Michael** - *Starea Uniunii Europene, Vol. 5, „Risc, reforma, rezistenta, relansare”*, Editura Club Europa, Bucuresti, 2002.

**Daianu Daniel** - *Ce vom fi in Uniune. Pariul modernizarii Romaniei*, Editura Polirom, Iasi, 2006.

**Joschka Fisher** - *From Confederacy to Federation: thoughts on the Finality of European Integration* -, discours, 12 mai 2002;

**S.Hix** - *The Political System of the European Union*, 1999;

**Husar Al.** - *Ideea europeana sau noi si Europa. Istorie, cultura si civilizatie*, Institutul European, Iasi, 1993.

**Lionel Jospin** - *L'avenir de l'Europe*, discours, 28 mai 2001;

**Charles Leben** - *Fédération d'Etats-Nations ou Etat Fédéral?*, Harvard, Jean Monnet Working Papers, Harvard Law School, Cambridge, 2000;

**Lutzeler Paul Michael** - *Europa dupa Maastricht, perspective americane si europene*, Institutul European, Iasi, 2004.

**Magnette Paul** - *Europa politica. Cetatenie, constitutie, democratie*, Editura Institutul European, Iasi, 2003.

**Martens Wilfried** - *O Europa si cealalta*, Editura Metropol, Bucuresti, 1995.

**Morin Edgar** - *Gandind Europa*, Editura Trei, Bucuresti, 2002.

**Muraru Ioan, Tanasescu Simina Elena, Iancu Gheorghe, Deaconu Stefan, Cuc Mihai Horia** - *Cetatenia europeana*, Editura All Beck, Bucuresti, 2003.

**Nastase Adrian (coord)** - *România si viitorul Europei*, Regia Autonoma Monitorul Oficial, Bucuresti, 2001.

**Nastase Adrian** - *Europa Quo Vadis ?*, Regia Autonoma Monitorul Oficial, Bucuresti, 2003.

**Neumann Victor** - *Neam, popor sau natiune ? Despre identitatile politice europene*, Editura Curtea Veche, Bucuresti, 2003.

**Pond Elizabeth** - *Renasterea Europei*, Editura Pandora-M, 2003.

**Johannes Rau** - *Plea for a European Constitution*, discurs, 4 aprilie 2001;

**Schuman Robert** - *Pentru Europa*, Regia Monitorul Oficial, Bucuresti, 2003.

**Tartler Grete** - *Europa natiunilor, Europa ratiunilor*, Editura Cartea Romaneasca, Bucuresti, 2001.

**Tartler Grete** - *Identitate europeana*, Editura Cartea Romaneasca, Bucuresti, 2006.

**Tsoukalis Loukas** - *Ce fel de Europa ?*, Editura Bic All, Bucuresti, 2005

**Wallace Helen, Wallace William** - *Procesul politic in Uniunea Europeana*, Editura ARC, Chisinau, 2004.

**Zorgbibe Charles** - *Constructia europeana. Trecut, prezent, viitor*, Editura Trei, Bucuresti, 1998.

# **OIL, DEVELOPMENT AND SECURITY: A MARKET-BASED APPROACH**

*RADU MUSETESCU<sup>1</sup>*  
*CRISTIAN PAUN<sup>2</sup>*

*Motto:*  
“We can have an effective and comprehensive energy policy  
only if the Federal government takes responsibility for it”.  
(U.S. Federal Report)

## **Abstract**

The present paper will attempt to explore the argumentation frequently employed in the public discourse – but less in economic theory – by different categories of stakeholders that the exhaustion of world oil reserves will have a dramatic impact on global economic growth and development. Because of such an alleged impact, policy makers in different countries argue that a stable and cost-effective supply of oil is a matter of national security. Significant political events at a world scale are the result of such an approach. Starting by demystifying the concept of “economic security”, the present paper demonstrates that the best approach to such an alleged problem is to let the markets do their job. Any other solution won’t solve the problem but impose significant costs on society for the maintenance of a status quo which is not sustainable. The history of the myth of the “peak oil” is more a matter of political debate rather than of an economic one. It serves certain categories of stakeholders but not the consumers, the alleged targeted beneficiaries.

**Key words:** nonrenewable resources, petroleum industry, government policy

**JEL classification codes:** L71, Q31, Q38,

---

<sup>1</sup> Lecturer, PhD, Department of International Business and Economics, Academy of Economic Studies, [radu.musetescu@rei.ase.ro](mailto:radu.musetescu@rei.ase.ro);

<sup>2</sup> Lecturer, PhD, Department of International Business and Economics, Academy of Economic Studies, [cpaun@ase.ro](mailto:cpaun@ase.ro);

## **The first lesson of economics: any resource is scarce**

Economics has long ago agreed that there are two types of mineral resources in the natural environment: general conditions and economic resources (or goods). On the one hand, the first type of resources is not subject to the economizing action from the part of human individuals because it is perceived to be in an abundant supply. The air we breathe is the most used example. The general conditions of the environment are not subject to formulation of property rights because their use by human individuals does not generate conflict. On the other hand, an economic resource is subject to the economizing activity of human individuals as it is the input to the production of goods valued by final consumers. That means that economic agents use scarce production factors in order to bring that particular resource into the production process.

The issue of scarcity of resources is debatable because of different possible angles of analyzing it. From a broader perspective, all mineral resources of the environment are limited (as Earth itself has a limited volume in space and, at least for the moment, human beings still do not extract resources from other extraterrestrial sources). From a narrower perspective, the issue of scarcity (or of limited supply of certain resources) is raised only in the case of the minerals whose supply (both as a stock and as a flow) is considered to be insufficient in comparison to their consumption.

A mineral resource does not have *per se* an objective value but it has a value only if final consumers value certain consumer goods whose production process uses it as an input. Supply and demand – the market process – will always regulate the quantity and the value of all economic goods. From the perspective of exchange, the buyers of a resource will always argue (as they prefer) that the price is too high (and the quantity supplied too low) while the sellers of a resource will argue (because of their preference) that the price is too low (and the quantity too high). *Ceteris paribus*, any buyer of an economic good will prefer that its supply to be increased (both in quantity and as number of suppliers) or the competing demand be decreased (a smaller number of competitors) while any seller of a resource will prefer that its supply be decreased (both as quantity and as number of suppliers) or the demand be increased (a smaller number of competitors).

These competing interests in any exchange can be solved only through the institution of property rights and the freedom of exchange. Economics cannot objectively argue, in a theoretical proposition, that a mineral resource is too scarce or too abundant (or its price is too high or too low). Market prices will always reveal actual conditions of supply and demand, of the scarcity of and the interest for an economic good.

## **The concept of security and its economic dimension: the yardstick of property rights**

“Security” is one of the most abused and misinterpreted concepts in social sciences. Because of its wide and vague psychological connotations, it has a highly subjective meaning. For two different individuals, the same situation may seem both secure and insecure. “Security” is not a physical situation or action (like “aggression”) but just a personal perception. It can be compared to risk-aversion. There may be individuals who feel secure but become victims in few seconds or individuals who live all of their life in a perceived insecurity but they won’t be harmed in any way. Insecurity is not, and we must stress that, aggression.

Scholars and politicians have always been involved in a quest to objectively define the concept of “security” but they failed because they didn’t have a proper yardstick (or because, more exactly, they lacked an ethical approach). For example, interests of individuals involved cannot be an objective yardstick. As individual interests are subjective, they may be competitive. Imagine two persons who participate in an auction to buy the same piece of land from a seller. As their interests are opposed, each one of them may regard the other one as a threat to his personal security as the other one attempts to buy the land and prevent him from doing so.

Legal scholars have demonstrated that the institution of property rights naturally emerged in human society in order to reduce conflict in the use of scarce resources. In the case of the above mentioned two persons, the one who will pay the higher price will get the piece of land. He didn’t aggress against his competitor and manifested his higher preference for the resource by paying a higher price. The losing bidder must accept the idea that his preference was not higher enough (he didn’t pay a higher price) or his welfare didn’t allow him to do so (he didn’t have the money to pay a higher price). Because of his welfare, he must accept to give up that particular piece of land (but he remains free to bid for other pieces of land till he is successful). If he doesn’t accept the outcome, he has “only” the solution of aggression: he may eliminate his competitor (and be the only buyer who bids the resource) or force the seller to transact with him. In this latter case, he not only does aggress against the property of one of the other two parties but also negatively affect the welfare of the other<sup>3</sup>.

The same analysis is valid in the case not only of an event-transaction but of repeated transactions. If I daily buy bread from the neighboring baker, I may feel insecure (my welfare is threatened) in the case that, in one particular day, I cannot buy the product because the baker didn’t produce a sufficient quantity or other buyers offered a higher price than I was prepared to. I can claim that my security was threatened by the baker or by another buyer but, as long as anybody didn’t aggress against my property rights, I cannot have a substantiated claim. Imagine that, in a particular day, I decide not to buy bread because I prefer to consume another product (instead of bread). My decision will affect the welfare of the baker who will realize, at the end of the day, that he produced more than the quantity actually demanded (and actually bought by clients). From the perspective of property rights, nobody aggressed against him. From the perspective of his interests and welfare, he may claim that I threatened his security.

The concept of economic security refers usually to the stability of the welfare of an individual. Because of his highly subjective interpretation, it is just a metaphor (or a psychological consideration) and cannot justify violent action (like the baker forcing me to buy the bread every day). It is usually related to the past behavior of individuals on the market<sup>4</sup>. Such a mundane economic analysis proved that the only objective yardstick in defining security (and aggression) is the institution of property rights. Any other yardstick is not ethical and cannot make people agree.

---

<sup>3</sup> If he eliminates the competitor, he will potentially bid a lower price for the resource so the seller will be affected as in the case of free exchange. If he forces the seller, the competitor will not be able to bid and will be adversely affected in his subjective welfare.

<sup>4</sup> Suppose that another baker moves in town. If nobody buys from him, he can claim that every consumer of bread affects his prosperity by not buying from him. In such a situation, every buyer knows that he is in a lose-lose situation: if he buys from the new baker, the old baker will have his welfare negatively affected. If he keeps buying from the older one, the new one will be affected.



## **Exploring national economic security**

While the issue of national security is a legitimate question for a nation, making appeal to it is one of the most frequent battle-cries of interventionism and expansion of government scope and regulations. As one commentator noticed, “nearly all individuals would feel that an action should be taken or a sacrifice borne if it clearly would contribute substantially to national defense” [Thorp, 1960]<sup>5</sup>. It is the ultimate argument: “Every advocate of some public action tries to associate his proposal with the defense of the nation. No one can be against it ... [Fowke, 1952]”<sup>6</sup>.

For example, one of the real cases when the argument of national security was raised in United States was the imports of Swiss watches. Watches were considered “precision products requiring fine tolerances” and “this industrial ability was stated to be essential in the light of the rapidly developing field of bombs and missiles with its need for time fuses and other intricate and compact machinery” [Fowke 1952]<sup>7</sup>. A loose correlation with the production of defense equipment can be realized for any kind of industry (steel, auto, electronics, and so on)<sup>8</sup>.

One may wonder how does a state of perfect national security (economic or not) look like? It can be compared with perfect equilibrium models used by economics. Their fundamental traits are total absence of uncertainty as well as optimum allocation of resources. Unfortunately, the other characteristic is their virtual character: they will never look like a world fundamentally characterized by change.

## **The second lesson of economics: impossibility of socialist planning**

Different scholars have argued that the problem with government intervention in the allocation of resources in a society resides not only in opportunism of public agents (and other stakeholders looking for appropriable rents) but, maybe more importantly, in the impossibility of rational planning. Free markets are the only mechanism that maximizes societal welfare and efficiency in the allocation of resources. Only the prices that emerge in free exchange are relevant for the demand for resources in that particular society. Any government intervention in such a natural process will distort the pricing process and ultimately cause misallocation of resources between industries.

---

<sup>5</sup> Thorp, Willard – “*Trade Barriers and National Security*”, The American Economic Review, Vol. 50, No. 2, Papers and Proceedings of the Seventy-second Annual meeting of the American Economic Association, May 1960;

<sup>6</sup> Idem. As another scholar argued, “The Canadian system of protective tariffs has long been known as the National Policy. Professor Underhill describes this designation as a stroke of a genius”. See Fowke, V. C. – “*The National Policy – Old and New*”, The Canadian Journal of Economics and political Science, Vol. 18, No. 3, August 1952, page 271;

<sup>7</sup> Idem

<sup>8</sup> One of the most spectacular logical inconsistencies of such arguments was revealed by the brilliant French economist Frederic Bastiat in his 1850 metaphor “*La Pétition*”: “nous [fabricants de chandelles, bougies, lampes, chandeliers, réverbères, mouchettes, éteignoirs, et des producteurs de suif, huile, résine, alcool, et également de tout ce qui concerne l’éclairage] subissons l’intolérable concurrence d’un rival étranger placé, à ce qu’il paraît, dans des conditions tellement supérieures aux nôtres, pour la production de la lumière, qu’il inonde notre marche nationale à un prix fabuleusement réduit ; car, aussitôt qu’il se montre, notre vente cesse, tous les consommateurs s’adressent à lui et une branche d’industrie française, ont les ramifications sont innombrables, est tout à coup frappée de la stagnation la plus complète. Ce rival, qui n’est autre que le soleil, nous fait une guerre si acharnée, que nous soupçonnons qu’il nous est suscitée par la perfide Albion”.

Let's take two brief examples which, as we will see, were used in the debate related to the oil sector. Import quotas on foreign products usually cause a reduction of foreign supply on the local market and determine prices to rise (as no government will introduce a quota which is higher than the real imports). As a direct consequence of such a rise, that particular sector will become more attractive for domestic investors due to its higher profitability<sup>9</sup>. On the other hand, price controls (which are usually set at below-market levels) act in the direction of a reduction of the rate of return in a particular industry and the run of the factors of production from that particular sector.

As we can already notice, a government will always use different types of interventionist measures which sometimes have conflicting effects on a particular industry. The resulting complex mix of measures that affect an industry in different directions will be an increasingly difficult framework for the manifestation of entrepreneurship. As the logic of interventionism operates, "middle-of-the-road policy leads to socialism". The government intervention is in a continuous process of expansion as desirable effects from the point of view of the government are usually paired with undesirable effects. As an interventionist scholar argued, "a defense policy for crude oil makes no sense all by itself. The problem also involves oil demand; it involves oil transportation; it involves oil refineries; it involves all the factors bearing on supply of and demand for coal and steel and so on down and across the input-output table. More generally, it involves proper allocation of capital investment and protection of the tax base" [Nelson, 1958]<sup>10</sup>.

## **Oil and society**

Oil has been one of the most important mineral resources in the human society: "Oil is the largest internationally traded good, both in volume and value terms – creating what some analysts call a "hydrocarbon economy" [Considine, 2006]<sup>11</sup>. In short, it can be stated that world economy runs on oil and there is no substitute in sight" [Gawdat, 1999]<sup>12</sup>. Because of its historical critical role in providing energy to human society, several metaphors are used to describe its importance: "Oil is the lifeblood of America's [and world] economy".

Because of its importance, any factor that affects the conditions of supply and demand may be perceived by the already existing buyers and sellers as a threat to their economic security. *Ceteris paribus*, as Chinese producers start buying more oil on the international market, the existing buyers (America being the largest one) will feel threatened.

For almost half a century after the start of its industrial production (the discovery of petroleum by Edwin Drake in Titusville, Pennsylvania, in 1859), oil had not been a strategic resource.

---

<sup>9</sup> On a free market, the rate of return across all economic sectors will tend to be equalized (what Ludwig von Mises calls the natural rate of interest) by the migration of factors of production from the low return sectors to high return sectors. We exclude other preferences that may affect such a tendency. For example, if everybody wants to become a petro-preneur due to the success of TV serial "Dallas", the rate of return in the petroleum sector will be lower than in the other economic sectors as individuals look for other gains than the monetary profit, which is the successful societal model of J.R. Ewing (hard drinker, Texan accent and womanizing).

<sup>10</sup> Nelson, James – "Prices, Costs and Conservation in Petroleum", The American Economic Review, Vol. 48, No. 2, Papers and Proceedings of the Seventieth Annual Meeting of the American Economic Association, May 1958;

<sup>11</sup> Global sales of oil reached \$ 1.100 billion in 2004. Considine, Timothy – "Is the Strategic Petroleum Reserve our Ace in the Hole?", The Energy Journal, 2006, 27, 3, page 91;

<sup>12</sup> Gawdat, Bahgat – "Oil security at the dawn of the new millennium", The Journal of Social, Political and Economic Studies, Fall 1999, 24, 3;

One of the key decisions that affected this industry was taken by Winston Churchill before the First World War as he decided to switch the British Royal Navy from coal to oil. As the experience of both World Wars seemed to prove that the military success is also determined by availability and continuity of fuels supply (the defeat of Germany and Japan was also justified by the lack of petroleum resources), U.S. Interior Secretary Harold Ickes firstly proposed in 1944 the stockpiling of crude oil for emergencies<sup>13</sup>.

One of the most interesting relations between oil and security was the fact that, after the Second World War, U.S. policy makers considered that the imports of *cheap* oil were a threat to national security. As the classical protectionist argument goes, “the certified requirements of our national security [...] makes it necessary that we preserve to the greatest extent possible a vigorous, healthy petroleum industry in the United States. Excessive quantities of low priced oils from off-shore sources threaten to impair the national security” [Thorp, 1960].

Moreover, U.S. government subsidized the expansion of the domestic oil industry through fiscal incentive in the field of exploration and consequent over-expanded production: “these tax policies have probably been the most important items of government interference in the petroleum industry. In the absence of these artificial stimulants the market would have delayed production” [Mead, 1979]<sup>14</sup>. In fact, the U.S. government used all the available tools of protectionism found in economics manuals: subsidies, import quotas<sup>15</sup>, price controls<sup>16</sup> and so on. The resulting structure and performance of the American oil industry is the direct outcome of all these powerful interventionist measures. The historically low prices that end-consumers benefited from were maybe an involuntary outcome of an over-expanded domestic oil sector: “in 1950, the United States provided 52% of the world’s crude oil production; by 1997, that figure dropped to 10%” [Gawdat, 1999].

One of the critical events that shocked the U.S. and international oil industry was not the energy crisis *per se* but the powerful wave of nationalization in the producing countries in the 1970s. That trend ended the period of the Seven Sisters<sup>17</sup> and empowered the producing countries vis-à-vis international oil companies. Oil companies increasingly loose their political leverage and become “more of a mule than of a rider”. However, new actors emerge on the special-interest arena, at least in the capitals of the developed economies, environmentalists and consumerists: “One might assume that with the declining power of the oil industry in the last decade, future energy policy will be legislated in the national interest. However, the only change is that the power of one interest group has been displaced by others. The structure of public policy formation [...] is unchanged” [Mead, 1979].

---

<sup>13</sup> The American Congress did not vote for the plan. Both US Presidents Harry Truman and Dwight Eisenhower signed bills to set up a strategic oil reserve but they were not implemented but their attempts were failures.

<sup>14</sup> Mead, Walter – “*The Performance of Government in Energy Regulations*”, *The American Economic Review*, Vol. 69, No. 2, Papers and Proceedings of the Ninety-First Annual Meeting of the American Economic Association, May 1979;

<sup>15</sup> Introduced by President Dwight Eisenhower in 1959;

<sup>16</sup> Introduced in 1971: the fixed prices were artificially low which amounted to a subsidy of the refining sector;

<sup>17</sup> The period of the Seven Sisters lasted from the end of the First World War to the beginning of the 1970s. The sisters were the biggest oil companies, the real players on the international market for petroleum. There were 5 American companies (Exxon, Mobil, Chevron, Gulf Oil, Texaco), 1 British (British Petroleum) and 1 Anglo-Dutch (Royal Dutch Shell). The governments of the producing countries did not have any power in controlling the behavior of these companies and the exploitation of the national resources. While this is not wrong in itself, it is wrong in the case that the regime was imposed by the Big Powers. See Podolny, Joel and John Roberts – “*Global Oil Industry*”, Graduate School of Business, Standford University, November 30<sup>th</sup>, 1998 as well as Vietor, Richard and Rebecca Evans – “*World Oil Markets*”, Harvard Business School, November 11<sup>th</sup>, 2003;

## Strategic Petroleum Reserve of United States

After the first energy crisis of 1973, US President Gerald Ford signed the Energy Policy and Conservation Act that created the Strategic Petroleum Reserve [Considine, 2005]<sup>18</sup>. The Act called for a Strategic Petroleum Reserve (SPR) of 1 billion barrels, equivalent of 62 days of consumption at mid 1970s levels. The US President George Bush decided in 2004 to fill the reserve to its maximum present-day capacity of 700 million barrels. At a present day price (September 2007) of \$ 80 per barrel, SPR has a market value of \$ 56 billion dollars.

The investment of U.S. public resources was of \$ 22 billions (\$ 5 billion for facilities and \$ 17 billion for crude oil<sup>19</sup>). While SPR seems to be a good bet for the US government (but who can argue that the job of the government is to bet taxpayers' money?), it is a useless as well as debilitating public policy.

First of all, the new global security and military environment is increasingly far away from a classic war like the World War II. The today conflicts are asymmetric and resources are not the critical factor. For example, in the case of a war between superpowers, a mutual assured destruction (a nuclear holocaust between them) does not need significant energy resources. The crisis in Iraq is also a powerful example as guerilla warfare and mass crimes do not need energy resources.

Second of all, an embargo of the oil producing countries towards United States and Western World may deprive those countries from the revenues of oil in the short run but they are increasingly less dependent of oil<sup>20</sup>. Saudi Arabia, Kuwait as well as United Arab Emirates are diversifying their sources of income and a political decision can be enforced without jeopardizing their chances to implement it.

Third of all, any kind of strategic reserve cannot solve the most pessimistic scenario of total depletion of oil resources. Such reserves can only prolong for several month a reality that will affect the entire world. The confidence that U.S.A. will still have oil while the rest of the world depleted it is not a device for making friends or money for America.

But the use of SPR in United States is a proof of the same expansion of the scope of public bureaucracy. The Energy Policy and Conservation Act, which regulates the operation of SPR, define three types of draw-downs:

“1. Full drawdown: The President can order a full drawdown of the Reserve to counter a "severe energy supply interruption." EPCA defines this as "a national energy supply shortage which the President determines -

(A) is, or is likely to be, of significant scope and duration, and of an emergency nature

(B) may cause major adverse impact on national safety or the national economy; and

(C) results, or is likely to result, from (i) an interruption in the supply of imported petroleum products, (ii) an interruption in the supply of domestic petroleum products, or (iii) sabotage or an act of God.

EPCA also states that a severe energy supply interruption "shall be deemed to exist if the President determines that -

---

<sup>18</sup> Considine, Timothy and Kevin Dowd – “A Superfluous Petroleum Reserve?”, Regulation, Summer 2005, 28, 2;

<sup>19</sup> Website of US Department of Energy, <http://www.fe.doe.gov/programs/reserves/spr/index.html> (September 2007);

<sup>20</sup> Not to speak that, in such a case, China or India will in fact be ready customers for the Arab oil.

(A) an emergency situation exists and there is a significant reduction in supply which is of significant scope and duration;

(B) a severe increase in the price of petroleum products has resulted from such emergency situation; and

(C) such price increase is likely to cause a major adverse impact on the national economy.

2. Limited drawdown: If the President finds that -

(A) a circumstance, other than those described [above] exists that constitutes, or is likely to become, a domestic or international energy supply shortages of significant scope or duration; and

(B) action taken....would assist directly and significantly in preventing or reducing the adverse impact of such shortage" then the Secretary may draw down and distribute the Strategic Petroleum Reserve, although in no case:

(A) in excess of an aggregate of 30,000,000 barrels....

(B) for more than 60 days....

(C) if there are fewer than 500,000,000 barrels....stored in the Reserve".

A large number of analysts noticed the ambiguity of the concepts used in the Act. Such an ambiguity will always allow a free (re)interpretation from the part of public bureaucracy. While the operation of the SPR during First Gulf War was a matter of "*too-little-too-late*", it was timely employed in September 2000 when U.S. President Bill Clinton released 30 million barrels of crude oil at the request of ... the U.S. Vice-President Al Gore, in the middle of a presidential race [Considine, 2005]<sup>21</sup>. The perversion of the SPR came "in the spring of 1996, Congress authorized the selling of \$ 227.6 million worth of oil in order to reduce the federal deficit. This marked a dramatic shift in the purpose of the SPR: instead of a strategic asset, the reserve was used as a piggy bank that could be tapped during fiscal hard times" [Considine, 2005]<sup>22</sup>.

In fact, the idea of buffer stocks in order to prevent the rapid adjustment to market conditions is not very novel. Different international commodity agreements (cartels of producers) attempted such a policy but they failed miserably (PANCAFE - the international coffee cartel orchestrated by Brazil, international tin agreement, and so on). And the fundamental observation was that "once played, the SPR card had modest impacts on world prices and could be easily trumped by actions of other players, including output adjustments by world oil producers" [Considine, 2006]<sup>23</sup>. And one of the significant effects was on private companies. Due to the availability of oil drawbacks in cases of "emergency", such companies gave up their own buffer stock as these were immediately available from public authorities<sup>1</sup>.

According to mainstream economists, the maximum security a society can reach regarding oil supply is to give up foreign trade in that commodity and produce everything internally; that is, complete autarky. From this point of view, SPR can also be perceived as a central bank for petroleum companies which can use it in cases of emergencies. Such availability (on

---

<sup>21</sup> Because of a spike of heating oil prices in North-Eastern United States, the presidential candidate Al Gore made an appeal to the President to a limited drawback of oil from the strategic reserve. It seems that the real motive was the poor results in surveys of Al Gore as compared to the Republic candidate George Bush. See Considine, Timothy and Kevin Dowd – [2005]. Unfortunately for mankind, Al Gore noticed that the warming of the Planet Earth occur only under Republican presidents.

<sup>22</sup> Considine, Timothy and Kevin Dowd – [2005];

<sup>23</sup> Considine, Timothy – "*Is the Strategic Petroleum Reserve our Ace in the Hole?*", The Energy Journal, 2006, 27, 3, page 91;

taxpayers' money) creates wrong incentives for private operators as in the case of fractional-reserve banking.

## Conclusions

Unfortunately for the modern day society, policy makers (but also the majority of consumers) define security in terms of welfare and not property rights. Any factor that affects their welfare (and interestingly, not only the already existing welfare but also its projected growing one) may be perceived as a threat to security. Such a perspective on economic security is problematic as it sooner or later will generate conflicts which cannot be solved as there is no consideration of objective yardstick. "Interests" *per se* may always be mutually exclusive and they cannot offer a peaceful and sustainable solution.

The perceived problems of the security of oil supply are even more problematic as they are also the result of conflicting objectives of public policy. On the one hand, the alleged protection of environment determined a series of public policy decisions which have a deep impact on the role of oil in the energy policy of the majority of developed states. The bans on the expansion of nuclear industry as well as on the exploration and drill in certain "natural wildlife reservations" are some of the examples.

Another significant example is the taxation of oil (and oil derivatives). While taxation is considered, from this point of view, a measure to reduce oil consumption (see the European and Japanese examples), in case of emergency (like high oil prices), national governments should lower the taxation of these products (in order to maintain a supply of "cheap" oil). This is not however the case because the governments would reduce their own resources extracted from the taxation of oil products. According to certain estimates, European countries "earned [in 1992] about \$ 200 billion in taxes on the 11.8 million barrels per day of oil products they consumed. This is nearly three times the \$ 74 billion that the oil exporters earned selling a similar amount. The Italian treasury alone earns as much as its tax take on 2 million barrels a day of consumption as Saudi Arabia earns in producing more than 4 times as much oil"<sup>24</sup>. As a direct conclusion, taking into account the acclaimed inelasticity of oil consumption, national governments would, *ceteris paribus*, prefer higher oil prices than lower ones. And there is, for sure, a logical inconsistency between the declared goal of abundant and cheap oil and the goal of maximizing tax revenue.

The claim of an apocalyptic end of the oil availability is oversold because policy makers will have a strong argument for the expansion of interventionism and planning both in this industry as well as foreign policy. As International Energy Agency declares, "in the absence of new government policies, the world's energy needs will rise inexorably"<sup>25</sup>. Such a statement which raises the prospect of a negative phenomenon is a declaration of distrust in every type of markets. A better statement will be: "In the absence of free energy markets, the world's energy needs will surely not be satisfied (and will cause wars)". Such claims are the outcome of a wrong perspective on world politics were the situation is a zero-sum game.

The idea that there are particular goods or services which are more important than others (defined as "strategic") is based on an implicit consumption model advanced (or implied) by

---

<sup>24</sup> Stanislaw, Joseph and Yergin, Daniel – "Oil: Reopening the Door", Foreign Affairs, September / October 1993, 72, 4;

<sup>25</sup> \*\*\* - "World Energy Outlook 2005: Middle East - North African Insights", International Energy Agency, 2005;

the analyst. Is the bankruptcy of a bakery a problem of security in a small community? Or the bankruptcy of Coca-Cola in today globalized world?

What it is often forgotten in the debate about the future of oil availability is the fact that present-day technologies and production activities use oil in a large degree because it was the cheapest energy commodity. Production processes and technologies which are today qualified as “expensive” and “non-efficient” will become cheap and efficient when they will be adopted by a large number of entrepreneurs and businesses. They are not attractive today because using oil is more efficient.

The inclusion of oil on the political agenda is a wrong development. It is a brutal oversimplification of a complex economic reality. Oil is a “star” commodity (ab)used in the political discourse maybe also because it is easier for policy-makers to claim success (or for competing policy-makers to claim failure) or the demand further powers to intervene in the economic sphere from political constituencies. As one political actor commented, “Given our habits, change is very difficult. Conservation faces popular resistance, Given those circumstances, we need to have that supply of oil not only for national security, not only to keep the economy running, but to keep the transportation system running and the automobile owner happy. That automobile owner is the voter. For the average American, his car is his temple, not his castle. When politicians begin to muck around with that temple, they put their own reelection at risk”<sup>26</sup>.

However, any public policy that may attempt to block or oppose such a natural reality can be easily qualified as expensive and futile. The natural reality cannot be changed by a public policy. The fact that some mineral resources are perceived to be scarce is a fact of the natural environment. We may argue that absent the scarcity, they wouldn’t have been qualified as economic goods. In the case of any economic planning and forced allocation of resources by public authorities, any factor that may jeopardize this allocation can be defined as a threat to national economic security.

As an analyst of the oil industry concluded, “assertions about the future in general, and about energy developments in particular, may occasionally turn to be accurate, but mostly will not”<sup>27</sup>.

---

<sup>26</sup> Bartel, Richard – “*Will War Yield Oil Security?*”, *Challenge*, March/April 1991, 34, 2, page 25;

<sup>27</sup> Clarke, A. W. and T. F. Hart – “*Appraising World Energy Prospects*”, *Managerial and Decision Economics*, Vol. 1, No. 2, Oil and Energy, June 1980, page 49;

### **Selected bibliography:**

Bartel, Richard – “*Will War Yield Oil Security?*”, *Challenge*, March/April 1991, 34, 2

Bastiat, Frederic – “*La Pétition*”, 1850, online edition;

Clarke, A. W. and T. F. Hart – “*Appraising World Energy Prospects*”, *Managerial and Decision Economics*, Vol. 1, No. 2, Oil and Energy, June 1980, page 49;

Considine, Timothy – “*Is the Strategic Petroleum Reserve our Ace in the Hole?*”, *The Energy Journal*, 2006, 27, 3;

Considine, Timothy and Kevin Dowd – “*A Superfluous Petroleum Reserve?*”, *Regulation*, Summer 2005, 28, 2;

Fowke, V. C. – “*The National Policy – Old and New*”, *The Canadian Journal of Economics and political Science*, Vol. 18, No. 3, August 1952, page 271;

Gawdat, Bahgat – “*Oil security at the dawn of the new millennium*”, *The Journal of Social, Political and Economic Studies*, Fall 1999, 24, 3;

Mead, Walter – “*The Performance of Government in Energy Regulations*”, *The American Economic Review*, Vol. 69, No. 2, Papers and Proceedings of the Ninety-First Annual Meeting of the American Economic Association, May 1979;

Nelson, James – “*Prices, Costs and Conservation in Petroleum*”, *The American Economic Review*, Vol. 48, No. 2, Papers and Proceedings of the Seventieth Annual Meeting of the American Economic Association, May 1958;

Podolny, Joel and John Roberts – “*Global Oil Industry*”, Graduate School of Business, Stanford University, November 30<sup>th</sup>, 1998

Stanislaw, Joseph and Yergin, Daniel – “*Oil: Reopening the Door*”, *Foreign Affairs*, September / October 1993, 72, 4;

Thorp, Willard – “*Trade Barriers and National Security*”, *The American Economic Review*, Vol. 50, No. 2, Papers and Proceedings of the Seventy-second Annual meeting of the American Economic Association, May 1960;

Vietor, Richard and Rebecca Evans – “*World Oil Markets*”, Harvard Business School, November 11<sup>th</sup>, 2003;

Yucel, Mine – “*Reducing US vulnerability to oil supply shocks*”, *Southern Economic Journal*, 61, 2, October 1994;

\*\*\* - “*World Energy Outlook 2005: Middle East and North African Insights*”, International Energy Agency, 2005;

Website of US Department of Energy, <http://www.fe.doe.gov/programs/reserves/spr/index.html> (September 2007);

---



# **THE ALLIANCES OF EUROPEAN RETAILERS AND THEIR EFFECTS IN THE FIELD OF MARKETING AND SUPPLY CHAIN**

**Professor CARMEN BALAN Ph.D.<sup>1</sup>**

## **Abstract**

While in Romania retailing is in the growth stage, in the mature market economies of Europe, it is facing fewer development opportunities within the countries of origin. Fierce competition, more demanding customers, higher expectations, increasing pressure on prices are the common shades of the retailing landscape of these countries. Consequently, retailers have focused on the concentration and internationalization of their activities, supply chain efficiency and effectiveness, marketing strategies, prices and alliances. Among the strategies devised by the major retail players of Europe range the international alliances in the supply chain, under the form of buying groups. The paper aims to bring to light some of the major buying groups existing in Europe and to analyze their role and effects in the field of marketing and supply chain.

**Key words:** retailing, alliances, European Union

**JEL classification:** D 74, F18, F23, M20

---

<sup>1</sup> Professor, Ph.D., Academy of Economic Studies, Faculty of Marketing, Department of Marketing, E-mail: [cbalan@ase.ro](mailto:cbalan@ase.ro).

## **Buying groups**

Buying groups are a major type of international retail alliances. In essence, a buying group is an organization created by several retailers with the aim of improving their purchasing power in front of the manufacturers and distributors as well as enhancing their market competitiveness compared to other types of retail players. Some experts such as the IGD specialists challenge the frequently used terms “buying group” and consider that “negotiation group” or “roof organization” are more relevant terms.

The buying groups are in fact buying alliances that are a shield used especially by independent retailers to consolidate their position on the market in front of the aggressive marketing and distribution strategies of the large manufacturers, distributors and retailers.

From the perspective of marketing management experts, the integration of the efforts of retailers is an example of vertical marketing system (VMS) and more precisely an example of contractual system. In essence, a VMS consists of various types of marketing channel players that join their forces in order to achieve common objectives by acting as a unified system.

In general, a contractual VMS includes different independent firms from various levels of the marketing channels that collaborate on contractual basis in order to obtain more economies of scale or sales impact than they could achieve each one separately. (Kotler, Ph., Keller, K. L., 2007, p. 251). Thus, the buying alliances of retailers are relevant examples of contractual vertical marketing systems. In fact, such an alliance generates a higher value for members than what they are able to obtain negotiating with their suppliers and selling to their customers relying only on their own efforts and resources. The buying alliances are value adding partnerships.

The economic literature has approached since the 1990s the issue of strategic alliances. In essence, a strategic alliance refers to the functioning of two or more organizations in close connection based on a perception of a single interest shared by the parties. Some experts have called the strategic alliances “a fad of the 1990s” (Doorley, T.L., 1997, pp. 1, 9). While at present experts and practitioners use widely the term alliance, in the 1970s, business partnerships have been considered unnatural and inferior forms of governance in Western business.

Alliances are based on the genuine commitment of each party. Commitment means much more than having an ongoing cordial relationship. (Anderson, E., Weitz, B., 1992, pp. 18-34). It is related to the following key aspects: long time horizon, sense of loyalty to the other parties, willingness to grow and invest in the relationship.

## **Objectives, generating factors and impact**

Buying groups are created by their members in order to accomplish a set of clear objectives. Among the main **objectives** of a buying group range the following:

- to obtain better acquisition prices based on the enhanced negotiation power generated by the combined purchasing power of the members;
- to get trading benefits such as special rebates or promotional support;
- to distribute international private brands of the retail members;

- to exchange information and know-how among members, in order to promote best practices, as long as they are not competitors;
- to create partnerships for the expansion in new markets in Central and Eastern Europe.

The objectives are primarily defensive, respectively to enhance the price competitiveness in the retail environment through the consolidation of the purchasing power of the members. At the same time, the buying alliances may have proactive objectives, such as the promotion of own national or international brands, the expansion on new attractive markets.

The **factors** that led to the creation of the buying groups relate both to manufacturing and distribution/retailing. The major generating factors are the following:

- a. increased power of manufacturers.** One of the major trends in manufacturing and retailing is the ever greater concentration. For instance, in France, the first eight global industrial groups in the agro-food sector have a market capitalization higher than Carrefour that is the second global retailer and the first European retailer. The degree of concentration is very high in the key manufacturing fields. For example, in France, Kraft represents 44.7% of coffee sales; Procter & Gamble 32.2% of detergents; Nestlé 32.3% of chocolate drinks; Kellogg's 43.2% of cereals; Masterfoods 35.7% of pet food (Salto, L., 2007, II-102). On the French market, the total number of large groups is 260. They represent 3% of the number of suppliers, 56% of the product references and 60% of the turnover of the food retail stores. Most of them are multinationals (95%) and foreign (70%). From another perspective, the buying alliances are of benefit not only to retailers in order to face the manufacturing giants, but also to manufacturers with a view to increasing their turnover and improve the use of their processing capacities. The alliances provide manufacturers significant opportunities for the production of the retailers' private brands. The actual advantage consists in the pan-European reach of the alliances, in the significant market potential that may be tapped by manufacturers even under the brand names owned by the alliances.
- b. challenges issued by discounters and hard discounters.** Lately, discounters and hard discounters have expanded aggressively their presence in the European landscape. They represent a powerful threat for the other types of retail formats, even for hypermarkets and supermarkets. Significant examples are the discounters Aldi and Lidl that hold a combined share of 40% of the German market (Lucht, D., 2007). These retailers have implemented continent-wide internationalization plans. In Western Europe, they boldly compete with hypermarkets and supermarkets. The pillars of the rapid expansion of discounters and hard-discounters are the following: low retail prices; good to high quality food products, low operation costs; efficient management. The business model promoted by discounters is so successful that leaders of hypermarket and supermarket formats have to rethink their own models and identify ways to enhance their competitiveness such as: diversification of their own portfolios of retail formats, cost reduction programs, improved supply chain strategies, emphasis on the non-food sector, initiation and development of their online presence etc.

The main retail alliances in Europe and their situation are presented hereinafter. Their sales value is also listed.

According to the evaluations made public by EMD, the leading retail alliance in Europe, the top 15 retailers and retail alliances in Western and Central Europe have a combined share of 77% of the sales value. The list of players and their sales figures are presented below:

**Table 1 – Top 15 retail players of Europe in 2002 (based on EMD estimates)**

<b>Crt. no.</b>	<b>Retailer/Retail alliance</b>	<b>Sales value (million Euros)</b>	<b>Share of the retail sales in Europe (%)</b>
1	EMD	119,439	11.5
2	Coopernic	96,939	9.3
3	Carrefour Europe	78,785	7.6
4	Agenor / Alidis	76,310	7.3
5	AMS	69,511	6.7
6	Metro Group	66,651	6.4
7	Tesco Group	55,927	5.4
8	Schwarz Group	40,598	3.9
9	Aldi	40,448	3.9
10	Auchan Europe	36,903	3.6
11	Ahold Europe	27,385	2.6
12	Casino	26,030	2.5
13	Sainsbury	25,329	2.4
14	Asda (Wal-Mart UK)	23,961	2.3
15	Morrisons UK	19,402	1.9
<b>Total Top 15</b>		<b>803,618</b>	<b>77.4</b>
<b>Total Europe (Western &amp; Central)</b>		<b>1,038,527</b>	<b>100</b>

Source: *EMD at a glance*, <http://www.emd-ag.com/e/untern001.shtm>, download date: 4 September, 2007.

According to the IGD experts, in the fiscal year 2004/2005, in Europe, the top 10 retailers and buying alliances have been the following:

**Table 2 – Top 10 retail players of Europe in 2004/2005 (based on IGD estimates)**

<b>Crt. no.</b>	<b>Retailer/Retail alliance</b>	<b>Sales value (billion Euros)</b>
1	EMD	119.0
2	Coopernic	88.5
3	Carrefour	72.6
4	Alidis	70.4
5	AMS	69.6
6	IRTS	56.4
7	Metro	53.1
8	Tesco	49.2
9	Aldi	35.9
10	Lidl & Schwarz	32.5

Source: *Five major European retailers found Coopernic alliance*, 02/05/2006, <http://www.igd.com/CIR.asp?menuid=50&cirid=1930>, download date: 9 March 2007.

The list is dominated by two retail alliances: EMD and Coopernic that have reached together a sales value of 207.5 billion Euros in 2004/2005. Consequently, they are twice more powerful than Carrefour, the second global retailer ranked after Wal-Mart Stores Inc. - the leading retailer worldwide - that has achieved retail sales of 312.4 billion USD in 2005. Other top retail alliances are Alidis and IRTS.

The retail alliances have a strong impact in the field of marketing and supply chain. On one side, the marketing impact refers to the coordination of the product, price, distribution and promotion strategies of the members. On the other side, the supply chain impact relates primarily to the harmonization of the buying strategies of the members, in order to obtain better prices from suppliers.

At the same time, the alliances have a direct impact on the competitive balance within the market, at European level. They enhance the competitiveness and the negotiation power of the independent retailers in front of the powerful integrated groups. Simultaneously, they provide smaller manufacturers access to a larger market and opportunities for the production of private brands that will be distributed by the alliance members at European level.

## **EMD**

The acronym EMD stands for European Marketing and Distribution. EMD is a partner for the most prominent manufacturers. This fact is proven by the following data: 50 multinational manufacturers cover 60% of the procurement volume of EMD and the top 100 European manufacturers represent 75% of the purchasing volume.

The array of services provided to the members is relatively large. It includes: sales promotion drives, euro-promotions, product launches and brand repositioning, sales and quantity guarantees. At the same time, EMD aims at setting up strategic partnerships among members in order to support the joint development of their presence in the high-potential markets of Central and Eastern Europe.

**Table 3 – EMD members in 2002**

Country	EMD member	Market volume (Euro)	Turnover (Euro)	Market share (%)	Surface (sq.m.)
Austria	ZEV Markant	20,000	2,641	13.2	778,727
Belgium/ Luxemburg	Delhaize Le Lion	22,983	3,900	17.0	621,000
Greece	Delhaize / Alfa Beta	10,500	908	8.6	156,000
Romania	Delhaize / Mega Image	15,574	83	0.5	15,000
Czech Republic	Markant Cesko	16,397	1,407	9.1	300,000
Germany	Markant	213,942	39,500	18.5	13,342,000
Denmark	SuperGros	18,268	5,663	31.0	1,000,000
Spain	Euromadi	59,965	10,735	17.9	5,797,704
France	Système U	207,956	15,141	7.3	1,607,015
Finland	Tuko Logistics	11,404	1,631	14.3	500,000
Great Britain	Musgrave/Budgens/ Londis	193,967	3,196	1.6	526,000
Italy	ESD Italia	86,400	13,738	15.9	2,291,841
Ireland	Musgrave	14,923	2,600	17.4	350,000
Norway	Unil / NorgesGruppen	18,218	7,110	39.0	1,000,000
Netherlands	Superunie	26,665	8,060	31.0	1,500,000
Sweden	Axfood	21,285	3,006	14.1	400,000
Slovakia	Markant Slovensko	5,590	120	2.1	25,000
Total		964,037	119,439	12.4	30.8 Mio

Source: *European Trade, EMD Members*, <http://www.emd-ag.com/e/report002.shtm>, download date: 4 September, 2007.

On January 1, 2007, EMD had thirteen full members. The group is present in twenty two markets, more precisely in all the Western European markets and in countries of Central and Eastern Europe, including Romania. The countries covered by EMD are the following: Austria, France, Belgium, Netherlands, Czech Republic, Slovakia, Germany, Denmark, Spain, Finland, Greece, Great Britain, Italy, Ireland, Sweden, Norway, Portugal, Romania, Poland, Bulgaria, Croatia and Hungary. It is the number one purchasing and marketing organization in Europe.

In 2007, according to the EMD estimates, the buying alliance had a sales potential of Euro 123.4 billion and a market share of 12.9%. The profile of the EMD members is diversified. The buying alliances includes from international food retailing groups to national or regional supermarket chains. Delhaize and Markant range among the international groups that are EMD members.

Delhaize Group (a food retailer headquartered in Belgium and listed on Euronext Brussels) has become a member of EMD in 2001 (Delhaize Group, March 12, 2001). The membership referred only to the European activities of Delhaize Group: Delhaize Belgium, Alfa-Beta (Greece), Delvita (Czech Republic and Slovakia) and Mega-Image (Romania), without the operations of US and Asia. At the beginning of the decade, when it joined EMD, Delhaize Group has operated in 10 countries, achieved sales of Euro 18.2 billion in 2000 and its net

profit amounted to Euro 169.9 million in 1999, results generated by a sales network of 2,360 stores and 153,000 employed associates.

NorgesGruppen ASA is one of the most recent entries in the list of members. (EMD-AG Press Release, 8<sup>th</sup> January 2007). It holds a leading position in the market of origin, fact reflected by a market share of 36.7% of the Norwegian food retail sector.

## Coopernic

The denomination Coopernic is in fact the acronym corresponding to the following set of terms: Coopérative Européenne de Référence et de Négoce des Indépendants Commerçants. This buying group is the most recent on the European landscape. It has been created as a joint venture between Leclerc and Conad in December 2005. It was officially launched in Brussels in February 2006 with three additional members. At present, the members of Coopernic are the following: E. Leclerc (France), Conad (Italy), Co-op Schweiz (Switzerland), Colruyt (Belgium) and Rewe Group (Germany).

The founders of the alliances have stated that future admission of new members is possible. However, in their opinion, the optimal size is six members, in order to maintain control and reduce management complexity.

Four of the five members are co-operatives. In essence, a retail co-operative is a vertical marketing system created by small independent retailers that join their forces mainly to obtain better commercial terms from their suppliers.

**Table 4 – The EMD members and their market situation**

	<b>Colruyt</b>	<b>Conad</b>	<b>Coop Schweiz</b>	<b>E Leclerc</b>	<b>Rewe</b>
Ranking in home market	3rd	2nd	2nd	2nd	2nd
Value share in home market (%)	18.6	12.2	15.7	17.5	16.1
Total turnover in 2005 (bn Euro)	4.4	8.5	9.6	30.1	40.8

Source: *European Buying Groups – A Threat or An Opportunity?*, 25 August 2006, <http://www.igd.com/CIR.asp?menuid=50&cirid=2031>, download date: 9 March 2007.

Coopernic is the second major retail player after EMD. The alliance has reached an aggregated turnover of 95 billion Euros. According to its own estimates, the second largest European grocery buying group has a 10% share of the all European grocery trading. Compared to it, the leading three integrated retailers – Carrefour, Tesco, Metro – have a 20% share.

The members intend to bypass the intermediaries and reduce the logistic costs, with a view to providing customers with attractive products at a price advantage. The main objective of Coopernic has a defensive character. The buying group has been set up as a response to the growing power of the multinational grocery suppliers. This fact is confirmed by the press release that has announced the creation of Coopernic on 16 February 2006, according to

which, on large market segments, 3-4 international firms provide 80% of the products sold in hypermarkets (Coopernic, Communiqué de presse, 16 février 2006).

However, from a supplier perspective, most of the major members of the group have already had favorable buying terms in their individual contracts. Thus, Coopernic becomes a significant challenge for the supplier due to the aggregated negotiation power.

The organization is owned in equal shares by its members. However, the members differ in terms of size and geographical coverage. For instance, Rewe represents 40% of the aggregate turnover and has a wide presence in Europe. Specialists consider that the large branded suppliers of Rewe have little gain in coverage from the other members of Coopernic.

**Table 5 – The geographical presence of the EMD members**

Region	Country	Colruyt	Conad	Coop Schweiz	Leclerc	Rewe
Western Europe	Belgium	615 SE,SM				
	France	44 SM,WS			502 HM,SM	FS
	Germany					7,401 HD,HM,SM,WS
	Portugal				12 HM	
	Italy		2,944 HM,SE,SM		22 HM	345 HD,HM,SM
	Spain				7 HM	
	Switzerland			1,433 SE,SM		
Central Europe	Austria					1,853 SM
	Croatia					16 SM
	Czech Rep					224 HD
	Hungary					142 SM
	Slovakia					65 SM
	Slovenia				1 HM	
Eastern Europe	Bulgaria					1 SM
	Poland				16 HM	36 SM,WS
	Romania					26 SM,WS
	Ukraine					8 SM

Note: Shading indicates retailer presence. FS: Foodservice, HD: Hard Discount, SE: Superette, SM: Supermarket, WS: Wholesale

Source: Coopernic, Communiqué de presse, 16 février 2006.



Total membership of Coopernic is 7,495 independent businesses, with 17,208 retail outlets across 17 countries from Western, Central and Eastern Europe. The number of members fluctuates constantly as small retailers enter and leave each of the four co-operatives. The range of store formats is large and includes hypermarkets, supermarkets, wholesale depots, discount stores and superettes.

The members of Coopernic aim to fulfill the following main common objectives:

- a. to optimize the buying of the top brands;
- b. to organize market tests;
- c. to coordinate new product launches and retail procedures;
- d. to provide regional manufacturers the access to the retail displays of the members;
- e. to reduce logistic costs.

Compared to the buying centers of the integrated groups, each member of COOPERNIC maintains his full buying autonomy. The alliance allows members to increase their national offer with selections of best products from the portfolios of the other members.

Inside the alliances, the co-founders may delegate logistics operations to one of the members that is considered the best performer. For example, from France, E. Leclerc provides fuel to the first service stations of CONAD in the North of Italy.

In order to share costs and generate substantial expense reductions, the members have decided to: elaborate common procedures for the private brands and the first-price products; ensure the free access to a common data base of supplier audits (to control the social and ethical aspects of the manufacturing conditions on the international markets).

The creation of COOPERNIC has led to the dissolution of the Lucie alliance. In 1997, Leclerc and Système U have created Lucie alliance. When Coopernic was established, Système U has announced it would join EMD, the leading retail alliance in Europe. At the same time, a former potential project of three French cooperative retailers - Intermarché, E. Leclerc and Système U – will not materialize at least for the moment.

## **Alidis**

The Alidis alliance has been formed on 24 September 2002. It is a strategic alliances that has been created to fulfill not only the primary goal of negotiating price advantages but also other joint objectives relative to new product launch, first price product range, common brands, loyalty programs etc.

At present, the members are Les Mousquetaires (Intermarché), the second largest group in France, Eroski Group, one of the leading food distributors in Spain and Edeka Group, the first food distributor in Germany. Edeka Group has joined the alliance in 2005.

The three independent groups have an aggregated turnover of 75 billion Euros (Alidis Communiqué de presse, 28 avril 2005) and 17,000 stores. Their aim is to provide a better quality/price ratio to the consumers by joint purchasing strategies and an exchange of know-how.

The group has a significant presence in Europe. The members cover a market of 10 countries: Belgium, Bosnia-Herzegovina, Denmark, France, Germany, Poland, Portugal, Romania, Serbia and Spain (Alidis, Dossier de Presse, 24 octobre 2006).

The group Les Mousquetaires is a major distribution player in Europe. It holds the third rank in the distribution on the French market and the fifth rank in Europe. In 2004, the group has reached a turnover of 38 billion Euros. The group has 4,000 stores on the continent and 112,000 collaborators. The market presence includes Portugal, Spain, Belgium, Poland and other countries from Central and Eastern Europe. The main trade names are Intermarché, Ecomarché, Netto, Bricomarché, Logimarché, Vêtimarché, Rody, Restaumarché and Espace Temps. The group positioning is focused on the best quality/price ratio.

The Eroski Group has approximately four decades of existence. The group has witnessed an important development in the present decade. For example, in 2004, the profit has reached 129 million Euros, due to a 20% increase compared to 2003. A number of 122 new stores have been opened in 2003. In Spain, Eroski Group has 1,700 stores and 30,000 employees. The main trade names are Eroski hypermarkets, Eroski supermarkets, Eroski/city, ALIPROX self-service, Viajes Eroski, Parfumeries IF, Forum stores for sport products.

Edeka had a turnover of 31.57 billion Euros in 2004, 8,500 stores and 220,000 collaborators. The group holds the leading position on the German food retail market.

The buying policy of Alidis is implemented by the buying central Agenor set up in 1998. The alliance aims at diminishing the costs all along the supply chain. It provides suppliers many services such as: (i) access to European statistics consolidated by country and by product; (ii) design and implementation of euro-promotions; (iii) support provided to suppliers at pan-European scale for a specific product category; (iv) support for the launch of new products on a specific market.

Since 2005, after Edeka Group has become a member of Alidis, the alliance has focused on several priorities: (i) “massification” of purchases, in order to mitigate the over-dependence on the large and powerful suppliers; (ii) best practice sharing among the three members; (iii) design of a common range of European products; (iv) common purchases of fruits and vegetables; (v) quality auditing of the suppliers; (vi) joint IT practices; (vii) Web site for consumers and industrial partners.

### **A potential strategy for the future**

In Romania, retailing is one of the most dynamic sectors. Since 1990s, consumers have witnessed tremendous changes in the diversity and quality of product supply and in the store formats.

The arrival of major international players on the Romanian market has visibly increased competition. According to GFK, one of the most prominent market research companies that are present in Romania, the structure of the retail sales is market by the continuous increase in the share held by the modern retail formats.

**Table 6 – Retail sales structure in Romania, in 2004 and 2006**

<b>Retail format</b>	<b>Share in the retail sales (%)</b>	
	<b>Year 2004</b>	<b>Year 2006</b>
Hypermarkets	<b>1</b>	<b>8</b>
Supermarkets	<b>11</b>	<b>16</b>
Cash & carry	<b>6</b>	<b>6</b>
Discount stores	<b>1</b>	<b>4</b>

Small shops	<b>56</b>	<b>52</b>
Stalls and open market	<b>8</b>	<b>4</b>
Other formats	<b>17</b>	<b>10</b>
Total	<b>100</b>	<b>100</b>

Source: Vlad, A., 27 August 2007.

Between 2004 and 2006, the share of the modern retail formats has increased from 19% to 34%. At company level, significant increases have been achieved in 2006 compared to 2005 by Metro Group (21%), Rewe Group (34%) and Carrefour (39%). This trend has a major impact on trade practices and on the balance of power within the marketing channels.

On one side, the small independent retailers loose ground in front of the international retail groups. Their sales decrease as consumers favor the array of goods and brands of the hypermarkets, supermarkets and discount stores recently established on the Romanian market.

On the other side, the manufacturers see their negotiating power diminishing each day in front of the very powerful buyers of the modern formats. The financial effort required to be present in the portfolio of a hypermarket, supermarket and discount store act like a “natural selection” force among the manufacturers. Only those that are able to comply with the requests of the big players will have access to the market, to an increasing flow of customers.

At present, a producer of soft drinks that wants to be present on the shelves of a hypermarket network has to pay in the first year, for the introduction of two products, almost Euro 200,000 (Vlad, A., 27 August 2007).

The first entry of a manufacturer in a modern store costs Euro 10,000. Besides the entry fee, the manufacturer must pay Euro 2,000 for each type of product from its portfolio. Four to five times yearly, the manufacturer must participate in the promotion based on catalog, organized by the retailer. The corresponding fee is Euro 700 for each appearance.

These figures demonstrate the ever increasing power of the major retail players on the expense of both smaller retailers and manufacturers. Consequently, as the trend will become stronger, the small retailers and manufacturers will be interested to identify methods and strategies to enhance their competitiveness. The alliances will very likely be formed in order to meet the pricing challenge issued by the international retailers.

For the moment, in Romania, few alliances have been established. At the same time, those created do not have a very strong power.

In the future, face with the accession of the modern retail formats, the smaller players on the Romanian market will look for economies of scale and consolidated buying to be able to compete with the low price policies of the retail leaders. This trend will become more visible as Romanian market will enter the late growth and maturity stages.

Retail cooperatives, voluntary chains and other types of strategic alliances represent a future potential strategic choice of those companies that want to manage profitably their competitiveness.

## References

*Dossier de Presse*, Alidis, 24 octobre 2006.

Anderson, E., Weitz, B., "The Use of Pledges to Build and Sustain Commitment in Distribution Channels", *Journal of Marketing*, 24 (February 1992), pp. 18-34.

*Colruyt, CONAD, COOP, E. Leclerc et REWE Group annoncent la création de COOPERNIC, première alliance de distributeurs européens indépendants*, Communiqué de presse, Bruxelles, le 16 février 2006.

*Delhaize Group joins EMD, the largest European buying group*, Press release, March 12, 2001, [http://www.delhaizegroup.com/divclassdg\\_MenuText\\_YellowMEDIAdiv/PressReleases/2001/tabid/74/ctl/ViewPressRelease/mid/424/PressReleaseID/333/language/en-US/Default.aspx](http://www.delhaizegroup.com/divclassdg_MenuText_YellowMEDIAdiv/PressReleases/2001/tabid/74/ctl/ViewPressRelease/mid/424/PressReleaseID/333/language/en-US/Default.aspx), download date: 4 September 2007.

Doorley, T.L., "Corporate Strategies: Building Successful Alliances", *Crossborder Monitor*, 5, no. 10, (1997), pp. 1, 9.

*EMD at a glance*, <http://www.emd-ag.com/e/untern001.shtm>, 9 March 2007.

*European Buying Groups – A Threat or An Opportunity?*, 25 August 2006, <http://www.igd.com/CIR.asp?menuid=50&cirid=2031>, download date: 9 March 2007.

*European Trade, EMD Members*, <http://www.emd-ag.com/e/report002.shtm>, download date: 4 September 2007.

*Five major European retailers found Coopernic alliance*, 02/05/2006, <http://www.igd.com/CIR.asp?menuid=50&cirid=1930>, download date: 9 March 2007.

Kotler, Ph., Keller, K. L., *A Framework for Marketing Management*, Pearson Education Inc., Upper Saddle River, N.J., 2007, p. 251.

*Les Mousquetaire (Intermarché) et Eroski accueillent Edeka au sein de l'alliance Alidis*, Communiqué de presse, Paris, 28 avril 2005.

Lucht, D., *European Grocery Retailing 2007*, Verdict Research, Datamonitor Group, London, 2007.

*NORGESGRUPPEN FULL MEMBER OF EMD AS OF 01.01.2007*, EMD Press Release, 8<sup>th</sup> January 2007, <http://www.emd-ag.com/e/aktuell001.shtm>, download date: 4 September 2007.

Salto, L., *Consommation, commerce, et mutations de la société*, Rapport présenté au nom de la Section des Activités Productives, de la Recherche et de la Technologie par Léon Salto, Conseil Économique et Social, Paris, 15 février 2007, II-102.

Vlad, A. "Cat costa sa fii pe raft la supermarket", *Evenimentul Zilei*, no. 4915, 27 August 2007.

# DEVELOPMENT MANAGEMENT FOR THE COMPANIES THAT ACT IN THE ROMANIAN PROCESSING INDUSTRY

**Eng. BRICEAG CATALIN ALEXANDRU**

## **Abstract**

As the opportunities given to Romanian companies rose, due to the global market process, while growing competition, at both macro and micro-economical level, so grew the necessity for an analysis able to stress competitively and to substantiate the best developing means.

At C.A.E.N.\* division level it appeared the necessity to calculate the internal market quota and imports/exports ratio, in order to rank the processing national companies from the competitive abilities' point of view versus external competition. It was also evaluated the representation degree of various indexes as far as companies' competitively is concerned for seven industrial fields of the national processing industry, using the Excel Regression Module, by multiple regression.

The conclusions drawn afterwards can help company managers who aim to develop, to base their decisions on elements with a high positive effect and to efficiently use available resources.

---

\* Classification of National Economic Activities

The major changes, that took place in the world industry evolution, some domains' development and others' limitation, the opportunities given to the Romanian companies together with giving the market an international aspect, but also the dangers appeared because of the competition increasing, claims a deep analysis, at the macroeconomic level as well as at the industrial companies one, performed by each manager, so that the best action strategies can be chosen for active assistance at the world value circuit. To reduce the risks associated with the growth, the means of development, the native managers have to use ways of planning through which they can identify the best means of development, the efficient grant of the investment funds and achieving the balance between work and production process. A good manager also has to foreseen the most exactly as possible the effects the company's dimension development and increasing can perform in what concerns the competition.

For these reasons, the conclusion that the primary resources of the competition which are represented by the capital and work can be drawn up, and that the application of the scientific management upon the production issues presupposes these measures contribution improvement.

At the same time with the Romanian processing industry importance, as well as with the fact that this economic domain is situated under the increasing rhythm of national competition, it is necessary to identify the actual eminently domains, as well as the critical points of the incorporate sectors, respectively where shortages of internal performance are pointed out. Thus, the measure acknowledgement where the native companies respond to consumers' exigency is aimed in conditions which it confronts the external competition and the evolution of this ability in time.

The main domains of the processing industry, from the contribution's point of view in GDP are, in a decreasing order, the provisions industry (DA-15), iron (DJ-27), clothes industry (DB-18), means of road transport (DM-34), chemical industry (DG-24), furniture industry (DN-36), crude oil processing and coal coking (DJ-28), machines and equipments exclusively the electric and the optic ones (DK-29) etc. At the same time, through the domains of the processing industry with the least share in GDP, there are, in an increasing order, tobacco products (DA-16), means of estimation and office technique (DL-30), apparatus, medical and precision instruments, optical and clocks and watches (DL-33), equipments, radio, television and communication equipments (DL-32) etc.

To place the domains afferent the divisions C.A.E.N. from the medium level point of view in which the native companies that act in these economic sectors own competitive abilities to respond the consumers' demand in the conditions in which they confront an external competition, the internal market quota is calculated, with the formula<sup>[1]</sup>:

$$C_{pi} = \frac{P_{ind} - E_{xp}}{P_{ind} - E_{xp} + I_{mp}}$$

And the remittance level of the imports through exports

$$G_a = \frac{E_{xp}}{I_{mp}}$$

Interpreting the obtained data makes allowance for the fact that, the internal market as well as for the remittance level of the imports through exports show, at a sector level, the commercial exchange balance and the competition level of the companies that act in these domains.

It is important to know the market quota, at a macroeconomic level, for the analyzed industrial sectors, but at each industrial enterprise level as well.

Thus, the market quota for each company can be calculated after the formula:

$$Cp_{FirmaX} = \frac{P_{ind\ FirmaX} - E_{xpFirmaX}}{P_{int}}$$

This indicator helps the managers of the native enterprises to place in market and to identify the influence level of the products tender upon the consumers' preferences, as well as the company's performances effect that they lead upon the stakeholders. Pushing forward in time of the mentioned indicator may help at the strategic decisions fundament of the company, as well as the developing, consolidation or limitation and at the future evolution foreseeing, important element in performing the planning activities on medium and long term.

In what concerns  $G_a$ , the smaller than 1 this is, it indicates a commercial shortage that signals the low competition level of the native manufacturers as against the external ones.

Thus, relevant are the industry domains of the means of estimation and office technique (DL-30), publishing houses, polygraph and reproducing the registering on supports (DE-2) and the substances and chemical products industry (DG-24), where the low value of  $G_a$  indicates, at the industrial enterprises, the need of investment granting for re-technology and know-how import or strategic associations regarding the competition increasing. At the same time, the distinguishing is assigned to the imperatives of development, for the strategic sectors or basing on the import alternative, at the same time with the added value contribution for the downstream activities, on the technological chain to the final consumer.

As a matter of fact, for the industrial sectors placed on the inferior levels of the production cycle, generally catalogued as being with low added value, the companies that act in the developed countries aim a low  $G_a$ , and for the activities that belong to the superior processing sectors, a big  $G_a$ , that shows a positive specialization of the internal manufacturers.

It is assigned the identification of those indicators that draw manager's attention, priory, to be subject to the necessary funds to improve them, contributing, thus, at choosing the best strategies to increase the competition, using the disposed resources efficiently.

The competition level estimation for the processing industry, during the period 2002-2005, is assimilated within this study of the industrial production evolution (Pind), with the reason that this must be sold, so there is outlet for it and it is not agglomerated on the supply, and the main indicators that influence the medium position of the companies that act in these industrial domains, in comparison with the competition, are considered the corporal immobilization value (Ic), investments (I), expenses with the research-development (CD) and the medium number of the employees. (Nr. sal.).

The choice of the industrial domains for which the estimations are performed takes consideration, at the same time, for their contribution at GDP organizing, their dependence of capital investment amount, of intern market quota, respectively the remittance level of imports through exports, as well as of the training effect estimated in the equipments and services supplying companies implication from the horizontal industry. Thus, there are chosen 7 industrial domains, considered important in the Romanian processing industry assembly, for which it is desired choosing the

action directions for increasing the competition level, the above mentioned indicators' value registered in these sectors, during the period 2002-2005, presented in table 1.

**Table 1 – The main economic indicators value for 7 domains of the processing industry.**

<i>Industrial Domain</i>	<i>Period</i>	<i>Industrial Production -millions RON-</i>	<i>Corporal Immobilizations -millions RON-</i>	<i>Investments -millions RON-</i>	<i>Research-Development Expenses -millions RON-</i>	<i>Medium Number Employees -thousands people-</i>
<i>Processing Industry D</i>	2002	100157,9	54201,3	6033,6	215,685	1594
	2003	123512,4	69271,6	8947,4	231,488	1581
	2004	148312,0	82616,7	11869,8	328,142	1491
	2005	170129,7	94085,5	11295,4	356,092	1425
<i>From which:</i>	2002	16570,2	8057,3	1176,9	1,804	163
	2003	20589,2	11022,6	1784,2	2,576	162
	2004	25575,1	12930,1	1930,1	5,033	161
	2005	29300,4	16276,3	2294,5	7,236	166
<i>Grocery and beverage DA-15</i>	2002	14251,7	2531,6	161,4	23,436	18
	2003	15946,4	3251,5	415,5	33,051	15
	2004	17405,7	3712,9	901,8	55,969	15
	2005	25342,4	3855,0	732,6	42,323	14
<i>Crude rock processing, coal classification and nuclear combustion treatment DF-23</i>	2002	7042,7	4117,0	329,7	19,759	64
	2003	8732,0	5732,8	375,5	18,332	58
	2004	10990,4	6400,3	639,6	27,959	51
	2005	9979,3	6857,0	701,3	45,099	49
<i>Chemical substances and products DG-24</i>	2002	3988,7	3362,1	377,7	4,191	77
	2003	4859,3	4320,0	554,4	6,207	72
	2004	6375,4	5309,6	1032,1	5,522	63
	2005	6660,6	5796,0	775,5	6,810	60
<i>Building materials and other products manufacturing from non-metallic minerals DI-26</i>	2002	15254,2	10042,4	482,2	19,168	85
	2003	17180,7	9097,8	369,3	23,498	76
	2004	18714,8	9804,5	817,2	27,719	63
	2005	19531,7	10859,8	774,9	22,765	57
<i>Metallurgy DJ-27</i>	2002	3371,2	1498,3	212,7	136,106	78
	2003	4679,6	2144,8	298,3	137,063	86
	2004	6098,8	2680,1	406,1	194,947	86
	2005	7050,2	3142,4	516,3	215,401	85
<i>Construcții metalice și produse din metal DJ-28</i>	2002	3405,1	1441,0	274,5	2,555	99
	2003	4116,2	2335,7	364,4	2,415	106
	2004	5193,1	2938,8	422,8	1,392	103
	2005	5298,3	3496,2	407,5	2,145	99
<i>Furniture and other industrial activities unclassified somewhere else DN-36</i>	2002					
	2003					
	2004					
	2005					

Source: Romanian Statistical Yearbook, National Institute of Statistics



The problem consists of importance amount valuation of each 4 indicators, and its solving implies using the multiple regression, having as estimation basis the time series 2002-2005 and appealing to the *Regression* module from the *Excel* application.

The dependant variable which gives the medium competition measure that act in the analyzed domains, is the industrial production , and the independent variables that influence the competition are the 4 indicators above established, as it results from the figure 1 , that represents the estimations for the processing industry assembly.

***SUMMARY OUTPUT***

**Regression Statistics**

<i>Multiple R</i>	0,994428
<i>R Square</i>	0,988887
<i>Adjusted R Square</i>	0,98724
<i>Standard Error</i>	4878,201
<i>Observations</i>	32

**ANOVA**

	df	SS	MS	F	Significance F			
<i>Regression</i>	4	5,72E+10	1,43E+10	600,6395	5,97E-26			
<i>Residual</i>	27	6,43E+08	23796844					
<i>Total</i>	31	5,78E+10						
	Coefficients	Standard Error	t Stat	P-value	Lower 95%	Upper 95%	Lower 95,0%	Upper 95,0%
<i>Intercept</i>	1448,092	1078,089	1,343203	0,190389	-763,964	3660,148	-763,964	3660,148
<i>X Variable 1</i>	1,583592	0,292502	5,413949	1E-05	0,983427	2,183757	0,983427	2,183757
<i>X Variable 2</i>	1,362305	2,046568	0,665653	0,51128	-2,83691	5,561515	-2,83691	5,561515
<i>X Variable 3</i>	10,4206	14,8052	0,703848	0,487554	-19,9571	40,79836	-19,9571	40,79836
<i>X Variable 4</i>	-0,71506	6,126262	-0,11672	0,907946	-13,2851	11,85499	-13,2851	11,85499

Fig. 1 – Multiple regression of the 4 economic indicators influence upon the production amount in the processing industry.

As it can be seen in fig. 1, the multiple determination coefficient (Multiple R), of correlation between the  $y_i$  and  $y_i^*$  values adjusted through the regression equation (R Square) and through determination adjusted (Adjusted R Square), that has to be as closer of 1, performing the conditions that the linear regression should be accepted.

At the same time, the values of **F (600,6395)** and Significance **F (5,97E-26)** determines the hypothesis that the chosen model adjusts well the data in the pattern.

The influence coefficients values for the 4 variables are:

**Ic – 1,58**

**I - 1,36**

**CD – 10,42**

**Nr.sal. - -0,71**

The sold production dependence, as competition element, on corporal immobilization value (Ic), investments (I), expenses with research-development (CD) and the medium number of the employees (Nr. sal.) can be estimated through the following equation:

$$P_{ind} = 1,58 * Ic + 1,36 * I + 10,42 * CD - 0,71 * Nr.sal + 1448$$

## **Conclusions**

A first conclusion that can be drawn from the equation coefficients analysis is the necessity of assigning funds for research-development, at the same time with improving the employees' training level and, on this background, the increasing of work productivity, including through decreasing of the odd staff.

At the same time, for a company's manager that wants to develop himself through the business increasing, the gross formation importance of fixed capital and the corporal immobilization amount are highlighted.

A company's high level of competition is equivalent with the economic efficiency, and in order to reach it is necessary to adopt those strategies that optimally combine the inputs at the lowest cost for society.

In what concerns the labour, the inputs improvement is performed through education and continuous training, and for the capital, through technological progress.

That is why the performed investment to improve these indicators must be assigned in a balanced way. An industrial enterprise cannot obtain performance if assigns only for the endowment with high technology if it does not present interest for the professional training of the employees.

---

<sup>[1]</sup> Mereuță Cezar, „România 2007 Industria prelucrătoare;piețe și potențial”, Editura Finmedia, 2003

**EU-RUSSIA RELATIONSHIP: SMOOTH AS OIL?**  
**AN ANALYSIS OF THE LINKAGES BETWEEN THE EUROPEAN**  
**UNION AND RUSSIA IN THE GLOBAL OIL MARKET**

**GABRIELA DRAGAN<sup>1</sup>,**  
**ROXANA VOICU-DOROBANTU<sup>2</sup>**

**Abstract**

The paper focuses on the evolution of the European Union relationship with Russia in the context of the 2004/2007 enlargements, after which, the former became the largest neighbour of the EU. Considered as strategic partners, the European Union and Russia are currently interacting on a huge agenda of common interests and concerns, among which oil and other petroleum related products represent a significant issue.

The analysis covers the peculiarities of previous and current economic and political developments of both sides influencing their relationship, mostly from the point of view of the oil industry. Of particular relevance to the issue is considered to be the percentage of the imports and exports of crude oil between the European Union and Russia. The paper analyzes the situation from a strategic perspective, with a focus on latest developments on the global oil market caused by the supplies of the US and OPEC.

**Key words:** European Union, Russia, oil

---

<sup>1</sup> Professor PhD., Department of International Business and Economics, Academy of Economic Studies, Bucharest, Romania.

<sup>2</sup> Assistant Professor, PhD Candidate, Department of International Business and Economics, Academy of Economic Studies, Bucharest, Romania.

## ***I. A short historical overview of the relation between Russia and the European Union***

After the 2004/2007 enlargements, Russia has become the largest neighbour of the EU and it is now bordering five EU member countries (Finland, Estonia, Latvia, Lithuania and Poland). Russia is now a “strategic” partner for the EU but also an independent player and sometimes an unpredictable one, both parts interacting on a huge agenda of common interests and concerns. Relationship between EU and Russia has been and is strongly influenced by the peculiarities of previous and current economic and political developments of both sides. Therefore, while the EU has been progressing from an economic cooperation towards a political union, Russia has been progressively moved from a centralised and authoritarian regime to a democratic system. However, at the moment, both partners, which are major players in the world economy and, especially on the European continent, must intensify the political dialogue in the interest of political stability, lasting security and economic prosperity in the whole region, since significant obstacles remain on the way to deeper cooperation.

Some authors<sup>3</sup>, considers that “the main factor that prevents Moscow and Brussels from overcoming the ambiguity and the crisis of confidence in their mutual relation is the lack of a long-term strategic vision”. This relation might remain uncertain despite a well-developed system of bilateral ties at different levels, from Partnership and Cooperation Agreement to European Neighbourhood Policy.

### ***1) The Partnership and Cooperation Agreement***

The first important legal instrument between Russia and EU is the **Partnership and Cooperation Agreement (PCA)**, which was signed by President Yeltsin in Corfu on 24 June 1994<sup>4</sup>. The PCA was concluded for a period of 10 years with the possibility of automatic extension beyond 2007 on an annual basis.

The Agreement is based upon the following principle and objectives: promotion of international peace and security, support for democratic norms as well as for political and economic freedoms and cover a wide range of policy areas including political dialogue, economic cooperation, cultural cooperation, energy cooperation in nuclear and space technology, prevention of illegal activities.

The PCA has established a complex **institutional structure** for regular consultations as follows:

- At the *top executive level*, summits of the Russia President, the President of the Council and of the Commission take place twice a year, at summits held in Russia and EU territory, in order to define the strategic direction for the development of the EU-Russia relations;
- At *Ministerial level*, members of the Council and Commission, representing the EU, meet with members of Russian Government in the Permanent Partnership Council (PPC). PPCs have so far been held with the participation of Foreign Ministers, Justice and Home Affairs, Energy, Transport and Environment Ministers. These meetings take place at last once a year;

---

<sup>3</sup> CEPS Working Documents, No.25, July 2005

<sup>4</sup> PCA entered into force only in 1997 because of the Union’s protest over Russia’s handling of the Chechen situation.

- *At senior officials and expert level.* The Cooperation Committee is made up of experts assisting the higher level group;
- *At parliamentary level.* The Parliamentary Cooperation Committee is made of parliamentarians of both sides.
- Since 2005, regular consultations on human rights are organised.

**Political dialogue** takes place at regular Foreign Ministers meetings, at meetings of senior EU officials with their counterparts, monthly meetings of Russian Ambassador to the EU with the troika of the Political and Security Committee and at expert level, on a wide range of international issues.

Since the entry into force of the PCA in 1997, the EU and Russia have concluded several limited **sectoral agreements** such as agreements on trade in textiles, steel and nuclear materials, as well as other agreements, for instance, the agreement between Russia and Europol or Science and Technology agreements. Moreover, the EU and Russia have agreed on a series of joint initiatives in recent years, covering a broad range of areas including organized crime, non-proliferation and nuclear disarmaments, higher education, civil protection, human rights and transport.

## 2) *The European Neighbourhood Policy*

The last European Union enlargement wave, called *the «big-bang» enlargement*, fundamentally changed the geopolitical context in Europe. Consequently, aware of and interested in increasing its role on the external level, the European Union initiated a more and more coherent process of regional cooperation and openness within its geographic proximity, defined by three interest areas: Central and Eastern Europe, the Western Balkans and the Mediterranean Sea. The common elements of the different regional approaches were the following: peace, stability, promotion of shared values (especially democracy and fundamental liberties), commercial development and integration.

The European Neighbourhood Policy presently includes 17 countries that can be grouped in **three geographic areas**: the Mediterranean Region (**10 countries**), Eastern Europe (**4 countries**) and Southern Caucasus (**3 countries**). **The Eastern Europe Area**, geographically linked by the EU, includes the so-called “**New Western Independent States**” – **Moldova, Ukraine and Belarus**. The regional programmes developed under the European Neighbourhood Policy (ENP) and covering the Eastern Europe, Southern Caucasus and Central Asia, intend to encourage regional cooperation by financing projects in many areas such as transport, energy, trade, environment, border management, migration, fight against organized crime, etc.

The relations are mainly bilateral, through **Partnership and Cooperation Agreements (PCA)**, which as we have already underlined, are based on respecting the democratic principles and the human rights and set the legal frame for the economic, political and commercial relations between the EU and the partner countries. There are also cooperation measures in the field of justice and internal affairs (especially illegal activity prevention, drug traffic and money laundering control), environment, science and culture.

Practically speaking, Russia takes part in the ENP only through association and not as a state directly affected by this new policy. The bilateral relations take place parallel to the neighbourhood policy, but separately and the joining elements are provided by the objective similarity and the common financing through the ENPI. The situation is mainly the result of the issues raised by the EU influence in the area, leading to a dynamics of the EU-Russia

relations based on certain procedures and mechanisms different from those adopted within the relations with other countries of the ENP.

The relationship with Russia, the Union's most important partner in its Eastern neighbourhood, develops within the strategic partnership concerning the creation of four "**common spaces**", a concept which was agreed by Russia and EU and adopted at St. Petersburg Summit, in May 2003. The four common spaces are the following:

- *an economic area* (including special provisions concerning environment and energy);
- *a common space of liberty, security and justice*;
- *a cooperation area in the security field* and
- *an area of research, education and culture*.

According to the EC Country Strategy Paper 2007-2013, Russia involvement in ENP has been disappointing because Russia did not appreciate to be treated in the same manner with smaller, neighbourhood countries. However, it is anticipated that the establishment of the Common Spaces might reduce Russian hesitations and determine Russia to assume a leadership role in regional cooperation programmes<sup>5</sup>.

## **II. Russia – an economic success story**

The President Putin's 2003 goal was that Russia continued its strong economic growth and to double the GDP in the following ten years, by attracting new technologies, diversifying the economic base and developing the production of high-value and knowledge intensive goods and services.

Therefore, it is not accidentally that in the last years, Russia has experienced a strong reversal of its traditional capital outflows since the foreign direct investment (FDI) has more than doubled between 2005 and 2006, from USD 14.6 billion to around 30 billion<sup>6</sup>.

Trade and economic cooperation are at the centre of the EU-Russia relationship, even if, this relationship is an **asymmetric** one. Thus, according to 2005 data, the EU's share in Russia's export was 56% and its share in the country's import was 44.8%. On the other hand, the Russia's share in EU's export and import was only 6.2% and respectively 10.1%.

At the same time, it is not less significant that the EU has received two-third of Russia's oil and gas exports. While in 1999, 21% of the oil and 41% of the gas used in the Union came from Russia, these figures have grown with the accession of the new member states (that rely on Russian energy to a great extent).

Russian exports are heavily dominated by energy and raw materials, due to both the internal structure of the Russian economy and the fact that manufactured products are often of a lower quality compared with EU goods and thus having difficulties in competing on the European market. Moreover, those areas where Russia might be able to compete, for example in agriculture, are still highly protected such as the Common Agricultural Policy. On the other hand, the Russian market is still perceived as being too bureaucratic and state interventions noticeable and falsifying the market economy's framework.

---

<sup>5</sup> Country Strategy Paper, 2007-2013, Russia Federation

<sup>6</sup> On the other hand, the FDI yearly inflows are now higher than 3% GDP. However, even the investment<sup>6</sup> share of GDP is now roughly at the OECD average, its level of 22% is rather low compared with other emerging economies like China.

There is a strong mutual interest in a closer **energy partnership** between EU and Russia. Consequently, the EU Energy Commissioner Andris Piebalgs, at the International Energy Week, Moscow, October 2006, said that “in the energy sector, Russia needs Europe as much as Europe needs Russia. The energy that Europe buys from Russia has been one of the key factors in Russia’s economic revival and stable flows of reasonably priced energy has been an important motor for Europe’s economic growth. In the energy sector, in other words, we are reinforcing each other”.

Given the substantial common interest in energy field, the **EU-Russia Energy dialogue** was launched in 2000, providing opportunities at both the political and expert level to foster cooperation and solve the key problems. Among the issues discussed there are aspects concerning barriers to investments in terms of transparency, reciprocity and protection of investors in the energy sector, as well as cooperation on new technologies and infrastructure projects. Special attention would be paid to energy efficiency and energy saving<sup>7</sup>.

### **III. Financial cooperation between the European Union and Russia**

Financial cooperation with Russia began in the **early 1990s**, under the **TACIS programme**, which aimed to help smooth Russia’s transition to democracy and market economy. Since 1991, well over €2.7 billion of assistance<sup>8</sup> were provided through the European Commission. Given the latest positive economic evolutions, the need for such broad assistance has considerably diminished and financial cooperation is now focused to meet objectives defined in the road maps to the Common Spaces.

Priorities for cooperation, as described above, are set out in the national, regional and cross-border indicative programmes for 2007-2010, approved by the EU member states and agreed with the Russian Government. These kind of programmes set out the amount of allocations for cooperation with Russian federal authorities and/or with the countries in the regions but also for the cooperation between local authorities on either side of Russia-EU border.

Thus, up to €60 million per year will be available to foster the EU-Russia relationship in the next three years, focusing mainly on the four Common Spaces and supporting some Russian regions (the Barents, Baltic and Black Seas Programmes, Karelia, South-East Finland/Russia, Estonia/Latvia/Russia and Lithuania/Poland/Russia). Moreover, funding for financial cooperation with Russia can also be supported through other instruments such as the Nuclear Safety Instrument, the Democracy and Human Rights Instrument and a number of thematic programmes. Furthermore, if a crisis were to occur, the financing might be assured from several instruments designed to respond to humanitarian or other crises. Therefore, the total amount could rise to €100 million depending on the level of Russian involvement in regional, cross-border and other kind of programmes set up by the European Commission.

### **IV. The game of resources between Russia and the EU**

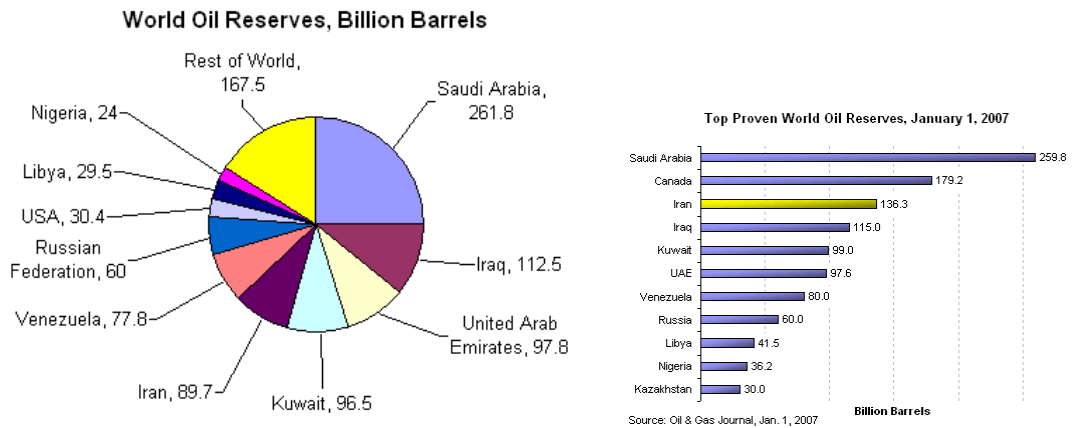
Considered to be in the Top Ten of the Proven Oil reserves of the world in 2007 (see figure below), Russia is not shy in making use of its power in this domain. However, in order to further grasp the extent of the issue, a few considerations have to be analyzed.

---

<sup>7</sup> According to International Energy Agency (IEA) data, energy efficiency per GDP in Russia is still 2.5 times lower than in the OCDE countries.

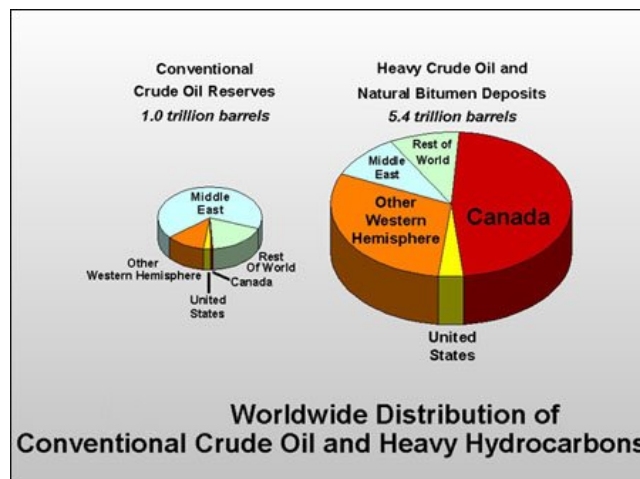
<sup>8</sup> EC Commission, Country Strategy Paper 2007-2013, Russian Federation, p.4





### Global Proven Oil Reserves as of 2006-2007

**Firstly**, regardless of the position held by Russia in the Top Ten of the global oil reserves, the proportion of the Russian heavy crude oil and bitumen deposits is rather unremarkable, as shown from the picture below. Even in terms of petroleum oil, the percentage held by Russia in the global outlook reaches a mere 4.6% in 2006. However, regardless of the proportion of resources, as compared to the Middle East, Russia is currently the second largest oil producer in the world, with a daily production of 9,668,000 bbl per day (equivalent of 1537000 m3 per day), which fails to reach the maximum of 11 million bbl per day on the 80s. The International Energy Agency (IEA), in its Medium term Oil Market Report published in 2007, forecasts that Russian oil production shall increase in the period from 2006 to 2011 by at least 1.1 million barrels per day, taking into consideration the increase of 400,000 bblpd from 2006 to 2007.



**Secondly**, Russia's position worldwide as a force to be reckon with in the oil market is sustained by its placement as the second largest oil exporters in the world, according to the EIA: *International Energy Annual* (2000-2004), *International Petroleum Monthly* (2005-2006), with a net export per day of 6,565,000 bbl. From this amount, the estimates are that close to 4 million bbl are crude oil, and the rest of more than 2 million are oil products.

The oil trade balance between Russia and the European Union is thus enhanced by the proximity of the two entities, as well as by the lack of resources of the European Union. Not comparable with the gas exports, yet as important, the oil exports from Russia to the EU sum

to 85% of the total Russian exports of crude oil and oil products, estimates being that by 2015 the mass of total exports of crude oil and oil products in this stream may reach as high as 200 million tons. The dependence of Europe on the Russian oil has been evermore noticeable, especially when the reliance on Russian crude exports has risen from 9% of total crude imports in 1995 to 29% of total crude imports in 2006, simultaneous with an increase from 7.5% to 25% of the total oil consumption over the same period of time.

A discussion regarding the outlet of Russian oil into the EU cannot be complete without an overview of the European Crude oil market, divided by infrastructure into North European, South European and East European Markets. Contrary to the popular opinion, the largest and most interesting outlet for the Russian oil is the Northwestern European area, even though it is directly connected to the North Sea Oil. The explanation is two-pronged. First, the decline in the production in the North Sea is a current issue, noticeable in the fall to less than 20 dated Brent cargoes a month. Second, the regional crude oil benchmark that is the Brent blend from the North Sea, also known as a marker crude, is light, sweet, low on sulfur, produced near key oil consuming and or refining capacities. The physical value of the Brent (recognized as an international benchmark) is used for determining the value of all sorts of crude oils worldwide, including the Russian oil. Compared to this benchmark, Russian oil, especially the exported amounts, are heavy and sour in quality, being used mostly as heating fluids, due to the high costs of refining and to the strict regulation in the EU regarding the content of sulfur in gasolines. An interesting issue in the oil market is that Russian oil supplies most of the spot market volume in Europe, whilst trying to increase the proportion from sour crude to sweet, and to develop its own benchmark, the relatively heavy sour Urals.

Infrastructure is an important issue to consider when discussing the relation between Russia and the EU in terms of oil. Close to half of the exports of crude into the EU have been exported through the Druzhba pipeline (linking Russia with Belarus, Ukraine, Germany, Poland, Hungary, Slovakia and the Czech Republic), although, due to the increase in the world prices of crude oil, most of the exports are transported via railroad, in order to circumvent the Transneft controlled pipelines, as may be seen in the table below.

Novorossiysk	768
Other Black Sea	217
Primorsk	1,255
<b>Druzhba Pipeline</b>	<b>1,261</b>
Germany	437
Poland	466
Hungary	136
Czech Republic	104
Slovakia	118
Lithuania	158
<b>Exports</b>	<b>3,660</b>
Non-Transneft Sea	170
China (Rail)	178
Murmansk (Rail)	47
Other Non-Transneft Rail	47
CPC	53
<b>Total Crude Oil Exports</b>	<b>4,155</b>

**Russian Oil Exports in 2006 by outlet**

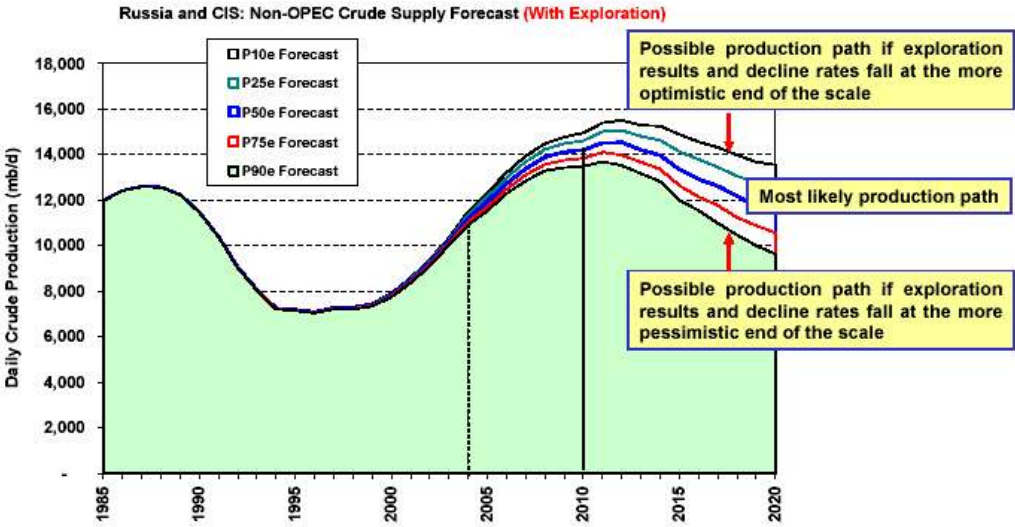
However, at the beginning of 2007, a dispute between Belarus and Russia has affected the European imports through the 2,500-mile Druzhba pipeline, that has been closed temporarily

due to accusation by Russia that Belarus is siphoning oil destined to German and Polish consumers from the pipeline. The problem has been aggravated by the Russian attempt to stop Belarus from reexporting oil products made from the refining of the cheaper Russian oil, thus it has imposed an export duty of 180\$ (at the beginning of 2007) a ton on oil sold into Belarus. The response has been the imposition of an import duty of 45\$ a ton by the Belarus party on Russian oil shipped to Europe across their territory.

Although not tragic at the moment, the problem between the two former USSR members has yet again underlined the reliance of Europe on Russian oil and on out-of control pipelines, most of them passing through countries not under any Neighbourhood policy treaties.

**Thirdly**, the global oil reserves, mentioned in the beginning of this section, are approaching, and in some countries, have already reached and passed, their peak. Russian Industry and Energy Minister Victor Khristenko was quoted in 2004 claiming that the moment of peak for the Russian oil production is around 2010 with a two year span, according to the figure below.

The irreversible decline in daily oil output is an issue in the mind of all worldwide, especially with an 100\$ a barrel crude in the international markets. The crisis may not be as bleak for the Russia as for the rest of the world, especially when 38 out of 44 oil producers have already reached their peak, and several authors list Russia as the only, apart from Venezuela and China, to still have not yet accessed reserves. However, taking into consideration the rate of depletion of the current reserves, which is about 3.5% per year, compared to the Saudi Arabia which is about 1% per year, and the rate of national consumption of the Russian oil, the picture seems to be indeed gloomy. Post-communist Russia has a growing market for oil, mostly from the point of the view of the increasing number of cars, and the situation is proven by the increase in the exploration and production figures, simultaneous with a stagnation in amounts exported.



In conclusion, EU cooperation with Russia may be considered in terms of strengthening the existing strategic partnership in order to maintain a stable supply of energy, cooperation in the field of justice and home affairs, environment and nuclear safety. The EU has recently set out a new European Neighbourhood Policy in order to create a security, prosperity, sustainable development and good neighbourhood area, respectively a «ring of friends» at its external frontiers, characterized by close and pacifist relations based on cooperation”<sup>9</sup>.

<sup>9</sup> COM(2004)373 final, Brussels, 12 May 2004.

However, since Russia has made clear that it should not be considered as falling under this policy, the EU has acknowledged this by establishing, in cooperation with the Federation, the four Common Spaces. Consequently, the significant objectives contained within the ENP remain highly relevant to the Common Spaces, from preventing the emergence of new dividing lines in Europe, progressive consolidation of a zone of stability, security and prosperity, all these objectives being achievable through a significant degree of economic integration and political cooperation.

Therefore, it is more than obvious that the next strategic agreement between Russia and the EU would reflect the new Russia's specificities, taking into account both its significant geopolitical position but also its unwillingness to accept an automatic alignment at EU norms and policies and its interest to be treated as an "equal partner" in the relation with the EU. Furthermore, the position of power of Russia is increasing due to the European dependency on Russian oil and gas, hence the need for cooperation at a political and economic level, mostly when looking at the picture of governmental and business structures involved in the oil markets connecting Russia and the EU.

**References:**

Barnahazi, Borbala, Korobchenko, Konstantin – EU-Russia relations with special emphasis on economic cooperation, Central European University, 2006

Common Strategy of the EU on Russia, adopted by the European Council, 4 June 1999, [http://ec.europa.eu/comm/external\\_relations/ceeca/com\\_strat/russia\\_99.pdf](http://ec.europa.eu/comm/external_relations/ceeca/com_strat/russia_99.pdf);

Kalland, Trygve, The EU-Russia Relationship: What is missing?, SIPRI, April 2004

European Commission, Country Strategy Paper 2007-2013, Russian Federation

Emerson, Michael, Tassinari Fabrizio, Vahl Marius, A new agreement between the EU and Russia: why, what and when ?, CEPS, no.103, May 2006

Energy Charter Protocol on Transit (draft) 31 October 2003;

Partnership and Cooperation Agreement (PCA) between the European union and the Russian Federation, 24 June 1994, [http://ec.europa.eu/comm/external\\_relations/ceeca/pca/pca\\_russia.pdf](http://ec.europa.eu/comm/external_relations/ceeca/pca/pca_russia.pdf);

The Road Maps (Road Map for the Common Economic Space; Road Map for the Common Space of Freedom, Security and Justice; Road Map for the Common Space of External Security; Road Map for the Common Space of Research and Education, Including Cultural Aspects) 10 May 2005, Moscow EU-Russia Summit, [http://ec.europa.eu/comm/external\\_relations/russia/summit\\_05\\_05/finalroadmap.pdf](http://ec.europa.eu/comm/external_relations/russia/summit_05_05/finalroadmap.pdf);

<http://www.platts.com/Oil/Resources/News%20Features/crudeanalysis/index.xml>

[http://www.eia.doe.gov/emeu/cabs/Russia/Oil\\_exports.html](http://www.eia.doe.gov/emeu/cabs/Russia/Oil_exports.html)

<http://rumining.info>

<http://www.petroleumequities.com/cgi-bin/site.cgi?p=investing1.html&t=4>

<http://www.russiaprofile.org/page.php?pageid=MainPage>

<http://omrpublic.iea.org/countryresults.asp?country=Russia>

# EUROPEAN UNION'S DEPENDENCY ON RUSSIAN ENERGY. GEOPOLITICAL CONSIDERATIONS

SILVIU NEGUȚ<sup>1</sup>,  
MARIUS CRISTIAN NEACȘU<sup>2</sup>,  
VIOREL MIONEL<sup>3</sup>

**Abstract:**

Russia is no longer a military or economic superpower, but it still is an energy one. What is its upperhand? It controls access to energy resources located in its own territory as well as nearby fields. From the geostrategic energy resources point of view, the Caspian Sea is a „Russian lake” or a „nostrum sea”. Given the fact that the Middle East is under „American rule” and in a state of conflict for the last 30 years, and China has become a „black hole” in this field, absorbing everything it can, the Caspian region appeared to the major European consumers as a „promised land” of energy, especially after the implosion of the communist regime. However, all the major players can be found here now: Russia, U.S.A., The European Union and China. Will the Caspian region become a new „Middle East”?

**Key Words:** geostrategic energy resources, The European Union, Russia, the geopolitics of energy resources.

---

<sup>1</sup> Professor, Ph.D., Academy of Economic Studies, Bucharest, Romania.

<sup>2</sup> Assistant Professor, Ph.D. candidate, Academy of Economic Studies, Bucharest, Romania.

<sup>3</sup> Academy of Economic Studies, Bucharest, Romania.

## **Introduction**

Energy security is probably the most frequently used term in current literature and discussions concerning world economy. Even the strongest regional bloc in the world, the European Union, has this problem on its agenda, strongly reaffirmed by Germany, which held/exercised the presidency of the Union through the first semester of 2007 – through the voice of its Foreign Affairs Minister, Frank-Walter Steinmeir, who declared “energy security as a priority of this mandate.” If we add the standpoint on this issue of the world’s greatest power, the United States (together with the European Union it makes for approximately two thirds of the world GDP), we will have an even better understanding of how great the importance of energy resources is, and particularly that of strategic ones (oil and natural gas).

The world’s hydrocarbon reserves (oil and natural gas) are unevenly spread all over the Globe, the majority of both developed, as well as developing countries being importers of oil (and oil products) and gas.

### **1. Oil and gas: World reserves, production and consumption**

The doubtless world oil reserves are estimated, today, at approximately 140 billion tons.

Apparently paradoxical, these are a lot larger than 25 years ago (approximately 87 billion tons), not to mention almost 70 years ago (4 billion tons in 1938). Because oil doesn’t form in historical times, we find the explanation in the fact that, these days, there are methods which allow a more correct evaluation of deposits.

Same as in the case of other resources, oil deposits are actually concentrated as spatial distribution. Thus:

- Approximately 70% of the planet’s proved reserves are found on the Asian continent, mainly under the sand of the deserts in the Middle East (between 62 and 66% out of the world total). This region is also the home of the richest countries in terms of oil: Saudi Arabia (approximately 35 billion tons – almost a quarter out of the world total), Iran (approximately 18 billion tons), Iraq (approximately 16 billion tons), Kuwait and The United Arab Emirates (each of the two countries with more than 13 billion tons);

The Middle East is the most fragile place in the world’s geopolitical system; it is the place where continents meet, it is the place where the cultures and great religions of mankind meet.

- Approximately 15% is located in America (especially the Gulf of Mexico area), out of which, the following stand out: Venezuela (approximately 11 billion tons), Mexico (depends on the source, between 2,5 and 5 billion tons) and U.S.A.. The last studies point Canada outrunning Mexico on the list of rich hydrocarbons areas;
- There are added a few other „oil areas” like the Caspian Sea Area, which, according to recent estimates, would be the second region on the planet in this field (this is the explanation of the project „The Road of Caspian Energy to Europe”), Saharan North Africa, Equatorial West Africa, The North Sea and others.

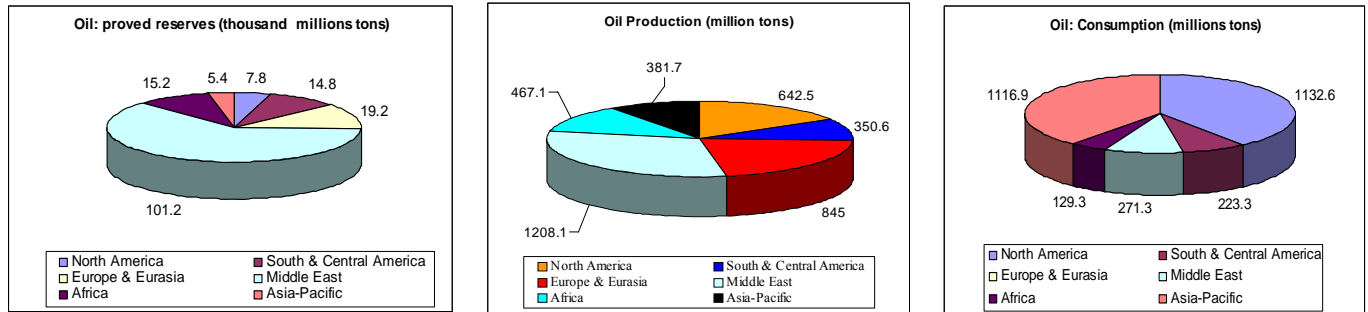
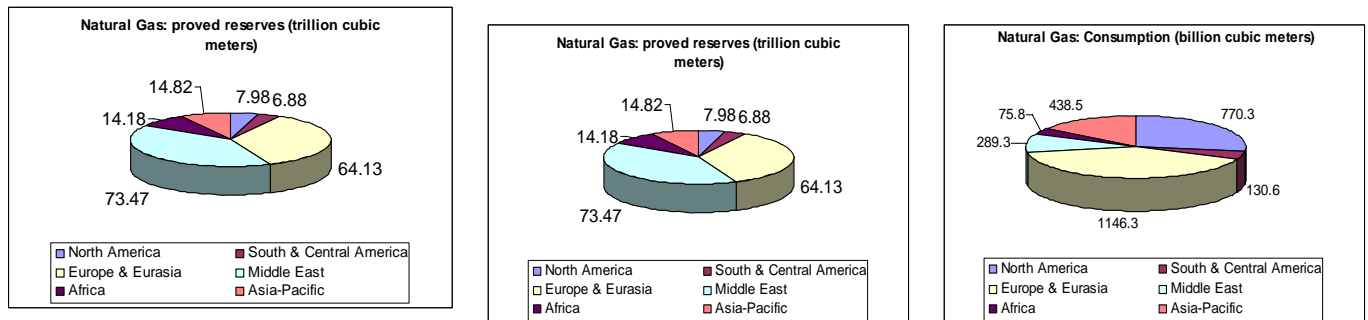


Fig. no. 1 – World oil reserves, production and consumption

The past several years have pointed out another energy resource, natural gas, which, left in the hands of only one actor, in the context of many beneficiaries depending on him, may become an instrument of force in influencing the foreign policy of those respective countries.

The world's certain natural gas reserves are currently appreciated at about 177 thousand billion m<sup>3</sup> and they are concentrated particularly in three countries: Russia (over one quarter of the world's total), Iran and Qatar (each with approximately 15% of world certain reserves).

In what concerns the production, we notice two important countries, which hold the top places: Russia and the United States (with over 500 billion m<sup>3</sup> each), followed, at long distance, by Canada, Great Britain and Iran. The same two countries (Russia and the United States) are also



present at the top of the consumption ranking.

Fig. no. 2 – World gas reserves, production and consumption

Russia, the world's largest producer (and its second consumer), holds dependent almost entire Europe (basically, with the exception only of the Netherlands, Norway and Great Britain, who provide their necessary by themselves, from their internal production). Being energy dependent on one source is, for obvious reasons, dangerous, the more dangerous the more the "supplier" has interests contrary to those of the "beneficiary" and the more it has the possibility to force its hand or to "punish" it.



## 2. The Caspian Basin – the “New Middle East”

**General Data.** The Caspian Sea, situated at the border between Europe and Asia, despite its vast surface (371 800 km<sup>2</sup>) and its name (*sea*), is, in fact, a lake. From here forth the main difficulty regarding the splitting of the continental plateau (and, implicitly, dividing the propriety of oil resources) between the five countries in the area (Russia, Kazakhstan, Turkmenistan, Azerbaijan and Iran). Russia relishes the approach of the Caspian Sea as an *international lake*, which allows it to exploit at its will, “in international waters”; in exchange, Azerbaijan, Kazakhstan and Turkmenistan appeal to the “law of the sea”.

Although appreciated as large, there isn’t a unity among opinions regarding the area’s oil reserves: 1.3 billion tons (“Oil and Gas Journal”), 2.6 billion tons (“Statistical Review of World Energy”, edited by British Petroleum), 4 to 4.5 billion tons (estimates of some large companies) all the way to 2.5 times greater than those of the Saudi oil field Ghawar (estimated at almost 12 billion tons<sup>4</sup>). The Tengiz resource alone, situated to the north of the Caspian, on the territory of Kazakhstan, appears to hold between 10 and 15 billion tons, which represents twice as much as all the oil in the North Sea. Likewise, many sources indicate the Caspian region as the second largest oil region in the world, following the Middle East. Given the fact that the Middle East has been for almost 30 years an area of ongoing conflicts, affecting deliveries (and, implicitly, prices) and, mainly those of oil, the Caspian Sea’s entering the spotlight has been almost natural.

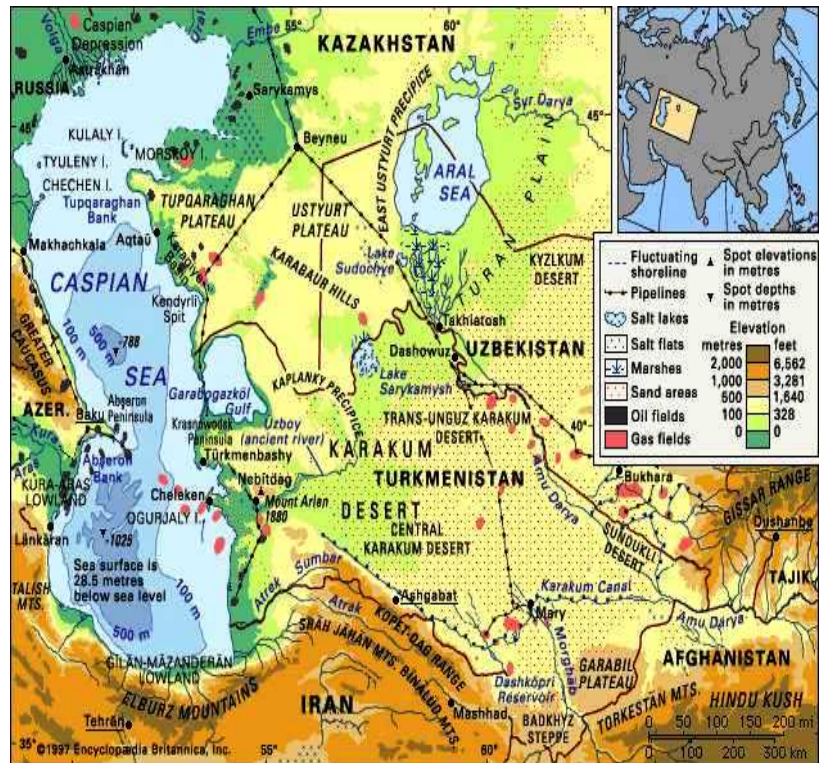


Fig. no. 3 – The Caspian Basin

The energy basin of the Caspian Sea presents at least two advantages to that of the Middle East:

- it is closer to the West (the beneficiary countries);
- it is more settled (there have been and there still are conflicts – those in the Caucasus, Chechnya and so on – but no wars).

Azerbaijan, Kazakhstan and Turkmenistan are the three republics separated from the former Soviet empire that have already started to have a powerful say in what regards energy resources at the beginning of the 21<sup>st</sup> century. The oil and gas reserves discovered here, but insufficiently explored, have caught the attention of the developed world, and, these hydrocarbons must reach

<sup>4</sup> According to *Energy choices in the Middle East*, The Centre for Strategic and International Studies, Washington DC, 2000.

Europe by routes that would not create dependencies, more so since there already are two other big producers in the area, namely the Russian Federation and the Gulf countries.

Therefore, the problem of the Caspian resources is no longer an economic problem, but also a political one, reason why, to date, neither the European Union, nor the United States possesses a clear strategy towards the Caspian and, particularly, towards neighboring Russia.

In 2005, for example, the cumulated production of these three countries was less than 100 million tons, more exactly 94.9 million tons (a lot under the potential), the partition among the countries being as follows: Kazakhstan – 63 million tons, Azerbaijan – 22.4 mil tons and Turkmenistan – 9.5 mil tons.

Given the facts, two problems remain unsolved. The first consists of the financial capabilities of the aforementioned countries to invest in prospecting and exploration facilities. The second relates to the means of transporting the respective resources towards the markets they will be distributed on. With the exception of the BTC pipeline (Baku – Tbilisi – Ceyhan), the existing oil pipelines only connect to the Russian Federation, and, anyhow, can not stand the quantities of oil that are to be pumped.

In order for the Caspian oil to reach Europe, and, considering the fact the oil pipelines in the Caspian have the eastern shore of the Black Sea as their destination, and the transit through the Bosphorus and the Dardanelle is limited from an ecological point of view but also in what regards transportation capacity, there are talks about building a new route from the western shore of the Black Sea towards the West, inside the European continent. Among the projects from the Caspian Sea towards Europe, we note:

- Burgas – Alexandropolis;
- Constanta – Omisalj – Trieste;
- Odessa – Brody – Gdansk;
- Turkmenistan towards Central and Western Europe, via Azerbaijan and Georgia;
- Turkey – Bulgaria – Romania.

**The “Caspian” actors.** There are a few categories of actors involved in the “Caspian energy route”:

- a) **Countries that border the Caspian Sea** (Russia, Azerbaijan, Kazakhstan, Turkmenistan; Iran is yet to draw any attention for projects regarding hydrocarbons);
- b) **Hydrocarbon beneficiary countries** (mainly the European Union and the United States, but also China and Japan);
- c) **Neighboring countries, that are transited** by the oil and natural gas (mainly Georgia, Turkey, Bulgaria and Romania);
- d) **Big oil companies** (Exxon, Mobile and others – US, ENI and Agip – Italy, British Gas – UK, Royal Dutch/Shell – the Netherlands).

Following the Soviet Union's implosion (1991), the power from Kremlin found itself forced to promote collaborative relations with the great Western Powers, mainly with the US. This was not due to its sympathy for the western democratic system but to the desire to overcome, with Western help, the economic and political crisis. In turn, to counteract the conservative potential of ex-communist origin, seeking restoration, the Western powers caved in and made many concessions: they tolerated exaggerate claims on the part of the Russian Federation to be recognized as "the only descendant and continuer" of the former Soviet Union (this included permanent membership in the UN Security Council, even though Ukraine had a similar request), established the Common NATO-Russia Council (practically giving Russia the ability to legally express its veto regarding the Alliance's actions) and they included it in the group of the most developed countries, the famous G7 becoming the G8.

Russia has recently stepped out of the shadow, being more and more active on the world stage: it hosted the first G8 summit on Russian land (July 2006, Sank Petersburg), it is on the edge of being received in the WTO, it is part of the SCO (Shanghai Cooperation Organization), but, most of all, it deals the cards in the energy games it plays with the West (the energy theme hasn't missed from the agenda discussed at any single one of the important summits within the last years where Russia was present).

Since the American power was surely to be the main *security supplier* for the former communist countries as well as for others, Russia chose to be their *energy supplier*. It uses its energy resources, and not seldom, for playing "political tap": "the gas war" with Ukraine and Georgia (2006), "the electric energy war" with Georgia (2005), the psychological pressure put on the European Union (especially concerning natural gas) and on Japan (oil) after having signed the contracts with China in 2006, whom is going to receive large quantities of both hydrocarbons that might affect deliveries to the other commercial partners.

In the same spirit of "political tap" we find the attitude, might we even say the boycotting by Russia of the energy projects initiated by Romania (the Constanta-Trieste oil pipeline) or to which Romania is a member (the NABUCCO gas pipeline).

### **3. Romania and The Caspian Energy's Road to Europe**

Romania, who was one of the world's biggest producers and, at the same time, exporters of oil between the two World Wars, and respectively, of gas, after World War II (in both cases, ranking 4<sup>th</sup>), is, at present, an importer of both. Its oil production (5.2 – 5.4 million tons annually), as well as its natural gas production (10 -13 billion m<sup>3</sup>) are insufficient to cover the country's consumption need, Romania becoming a net importer. As a consequence, Romania has become very interested in the grand energy projects, particularly in those generically classified under the expression "the Caspian energy's road to Europe".

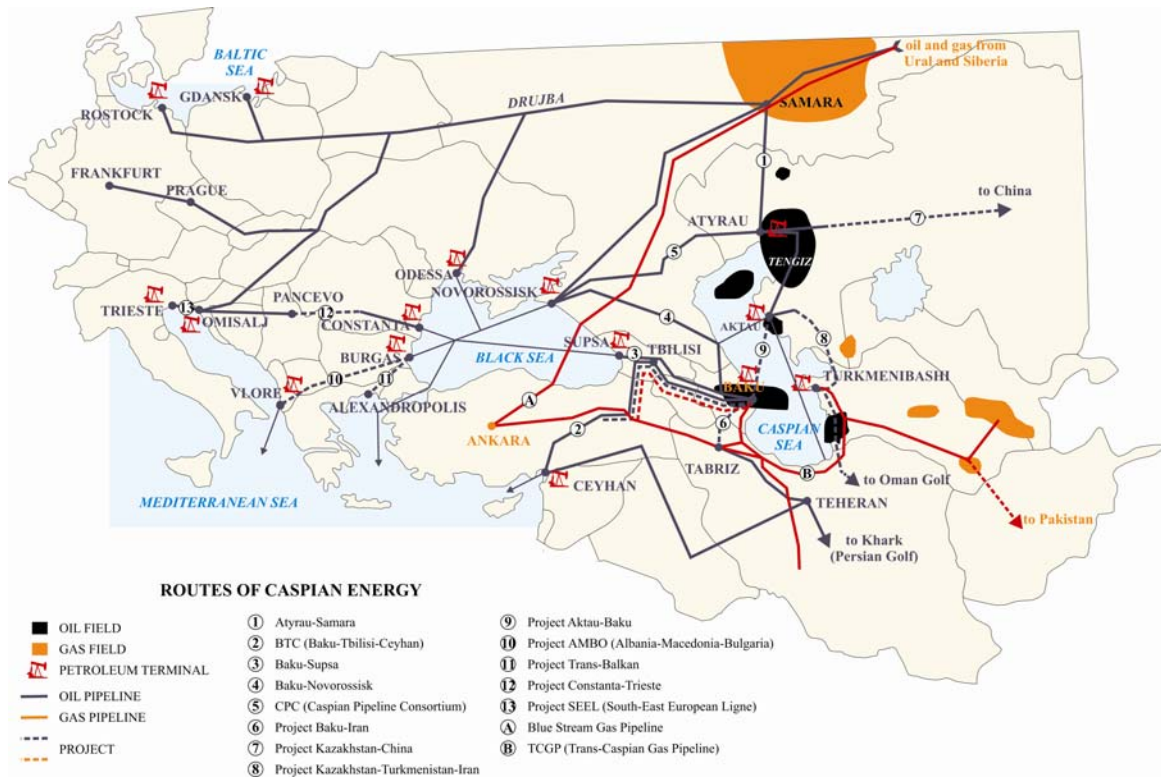


Fig. no. 4 – Routes of Caspian Energy

#### 4.1. The Pan European Oil Pipeline Constanta – Trieste or the Pan European Oil Pipeline (PEOP)

On April 3rd, 2007 the agreement (“Ministerial Declaration”) concerning the building of the oil pipeline Constanta (Romania) – Trieste (Italy) was signed in Zagreb, the capital of Croatia. Besides the three countries, Serbia and Slovenia were signatories as well. The document was also signed by Andris Piebalgs, the European Commissioner for Energy, thus confirming the European Commission’s interest and full support for the PEOP.

*The initiative:* It belongs to Romania, but has the support of the European Commission. The project isn’t actually new, as it participated in the 1998 competition, when the winner was announced (with the occasion of the OSCE Conference in Istanbul, in November 1999) to be the Turkish project BTC (Baku – Tbilisi - Ceyhan), given also the support and the interests of the United States and Great Britain, although the Romanian one presented a great deal more advantages, among which:

- Shorter land route (1,400 km as opposed to the BTC’s 2,000 km);
- Two thirds of the pipes already existed, lacking only to be connected;
- The absence of areas of conflict (within Turkey, the BTC crossed through the Kurdish territory);
- It traverses only low regions, the BTC requiring many pumping facilities (about 20), etc.;

- Constanta harbor has large facilities for the storage of oil and its subsequent distribution through pipeline;
- Romania has greater oil refining capacity (of over 30 million tons per year), surpassing by a lot internal production and consumption needs.

*The Main Features of the Constanta – Trieste Oil pipeline:*

*Length:* 1 360 km. *Capacity:* according to the feasibility study, performed by a consortium coordinated by Hill International UK, three alternative transporting capacities were being contemplated – 40, 60 or 90 million tons / year. *Costs:* \$2.27 billion, \$2.81 billion or \$4.26 billion, depending on the chosen alternative. *Completion Deadline:* 2009, 2011 or 2012. *Purpose:* the transporting of oil from the Caspian Sea region (especially from Kazakhstan and Azerbaijan), through the Black Sea (from the Caucasian oil ports, particularly, Supsa, Georgia to Constanta, Romania, the biggest port in the Black Sea region) towards Western Europe.

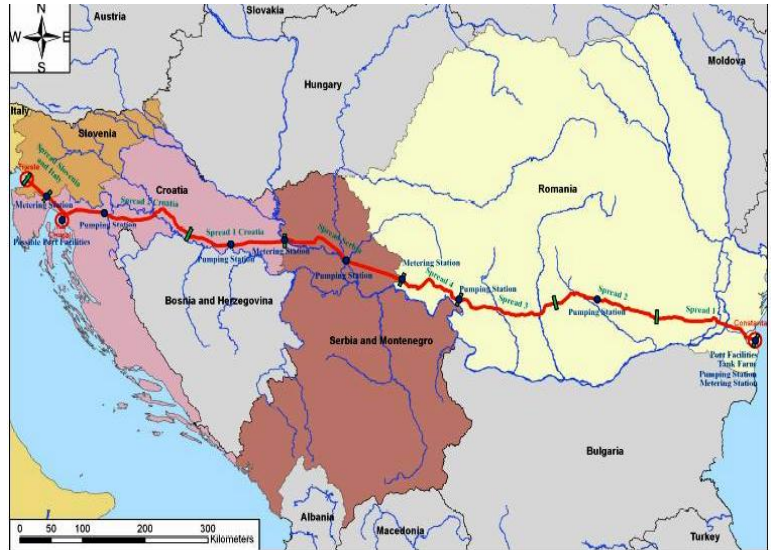


Fig. no. 5 – The Pan European Oil Pipeline (PEOP)

This pipeline contributes to reducing the European Union’s dependency on Russian and Middle Eastern oil.

The targeted market for the PEOP project Constanta – Trieste is, obviously, the European Union; its terminal point is Trieste because from there on the connection with the Trans Alpine Pipeline Network becomes possible, through which Austria, Germany and other West European states could be supplied.

*Advantages:*

- The shortest route to Central and Western Europe. *Note:* Another agreement signed in April 2007 was initiated this time by Russia, for a similar pipeline, with the route Burgas (Bulgaria) – Alexandropolis (Greece, north of the Aegean Sea); Only that in order for the oil to be forwarded farther, to Western Europe, the distance and, implicitly, the costs are very high.
- It could provide for other countries on route (Romania, Serbia, Croatia and Slovenia) or nearby (Bulgaria, Hungary, Austria), all dependant, either totally or partially, on imported oil; this means the oil pipeline could be “doubled” or even “tripled”.
- The oil pipeline could be doubled by a gas pipeline that could benefit from the arrangements made to accommodate the pipeline.

## 4.2. NABUCCO – gas pipeline

After the “gas war” between Russia and Ukraine (2005 - 2006), the European Commission regained its interest in the older NABUCCO project, as an “alternate source of energy”, meaning natural gas for Central Europe (its main beneficiary going to be Austria). “It’s not just a technical project, it is also a political one”, said the European Commissioner for Energy, Andris Piebalgs.

*Purpose:* the transporting of natural gas from the Caspian Sea region (especially from Azerbaijan, although the “Iranian branch” is also under consideration) towards Central Europe, with the route Turkey – Bulgaria – Romania – Hungary – Austria. Just like in the case of the Constanta – Trieste pipeline, the NABUCCO gas pipeline aims at narrowing the dependency on Russia, who is the European Union’s main supplier (40% of its consumption is provided for by Russia).

*The main features of the gas pipeline are:*

*Length:* 3,300 km. *Capacity:* 26 – 32 billion m<sup>3</sup>/year, to begin with. *Costs:* approximately \$5 billion (of which Romania is going to contribute \$1 billion). *The Companies* that voiced their intention to partake in the building of the gas pipeline: OMV (Austria) – around 50%, TransGaz (Romania), MOL (Hungary), BulgarGaz (Bulgaria) and Botas (Turkey). *Completion Deadline:* beginning of works in 2008, partially operational in 2011 and fully operational in 2020.



Fig. no. 6 – *The Nabucco Gas Pipeline*

Russia (concerning both types of hydrocarbons) in 2006, might render Russia’s satisfying EU’s need for gas impossible.

Unfortunately, the agreement regarding the project has not yet been finalized because Turkey, who initially enjoyed the idea of NABUCCO, is now delaying its signing procedures. There are rumors that, after the completion of the aquatic gas pipeline Blue Stream (Russia - Turkey) traveling the bottom of the Black Sea (in November 2005), Russia is influencing Turkey to consider building gas pipelines solely on its territory.

## 5. The “Political Tap “or “Russian Roulette”?

When there is only one energy supplier to a number of countries, it can dispose at its whim the stoppage of exports or any reductions of afore established export quantities. Although, in many cases, technical reasons are thrown to the front, in reality they are by all means political (to “punish” a certain country), thus the use of the “political tap”. Some analysts use the term of “Russian roulette”<sup>5</sup>, which I consider improper: in the case of a “Russian roulette” the victim is aleatory (the person having the misfortune to pull the trigger when the bullet is in the front chamber), while in the case of the “political tap” the victim is “chosen” and certain.

For instance, in the night of 21 to 22 January, 2006, two explosions affected the main stream and a secondary branch of the gas pipeline Mozdok – Tbilisi, the main pipeline alimenting two former Soviet republics (Georgia and Ukraine). The deflagrations occurred on the Russian part, not far from the border with Georgia. Shortly after, another deflagration also cut down the supply of electric energy to Georgia.

The Russians accused the Georgians and the Armenians of “sabotage”! In reality, they had no interest, since it all took place in the midst of winter (January!) and their reserves would only last for 24 hours. Therefore, the Georgian president, Saakashvili, denounced Moscow’s “blackmail”: “For a long time, I had been hearing the threats of Russian politicians that we might be left without natural gas and power, and now it has happened.”

Some analysts go further and notice many similar scenarios:

- After Russia substantially increased the price of its natural gas set for Ukraine and Georgia, the analysts regarding this as a form of reprisals following the “Georgian Revolution” in December 2003, the “Orange Revolution” in Ukraine in December 2004, the “Tulip Revolution” in Kazakhstan in June 2005, *GAZPROM* also announced the increase in prices for the gas delivered to Belarus (starting 2007, the price tripled). It was believed that, actually, the Russian company wanted to take over 50% of the stocks of Belarusian contender Beltrangaz, the owner of the pipe nexus feeding Europe, in order to stop paying taxes to Belarus in stead of them themselves cashing in directly; after Belarus’ tough reaction (on the part of Russia’s most loyal political partner), the Kremlin caved in.
- Russia cancelled Algeria’s debt (\$5 billion) on two conditions:
  - First: the buying of \$4 billion worth of weapons (40 MIG 29s, 20s, SU-30 planes and 40 T-90 tanks);
  - Second: *GAZPROM*’s access to its oil and gas fields, Algeria being Europe’s third energy supplier, after Russia and Norway; in addition, Algeria is also a member of OPEC.
- In March 2006, Russian president Vladimir Putin, signed together with Chinese resident Hu Jintao, an agreement by which they pledge to build two natural gas pipelines to China, thus becoming the country’s number 1 supplier. The agreement spawned concern within the European Union, because the gas that was going to be delivered to

---

<sup>5</sup> Russian roulette is a game in which you risk killing yourself by shooting at your head with a gun that has a bullet in only one of the six chambers.

China was to be extracted from Western Siberia, the same region that gives the gas Russia exports to Europeans. The deliveries were set to start in 2011, between 60 and 80 billion m<sup>3</sup> annually. Kremlin announced that Russia might also build an oil pipeline, thus upsetting Japan as well, since it could not meet both Asian demands.

All these elements – and others may be added (boycotting the NABUCCO project – which also includes Romania –, the recent reopening of the Burgas-Alexandropolis oil pipeline and so on) – suggest, according to some analyses, that Russia is currently transforming itself from a “defunct military superpower – although still nuclear – into a new energy superpower”<sup>6</sup>.

*Blue Stream – A Small Pipeline, Great Significance.* This gas pipeline was inaugurated with huge display on 17 November, 2005, in the presence of Russian president Vladimir Putin and Turkish prime-minister Recep Erdogan, Italy’s then prime-minister, Silvio Berlusconi, also taking part. The explanation for this was apparently simple: Russia “offered” natural gas, Turkey “benefited”, and Italy was participating as co-constructors of the project, through ENI trust (together with Russian colossus GAZPROM).

Several facts concerning the project: the underwater pipe (the deepest one on the Globe, at 2,150 m under sea level) is 309 km in length and links the ports of Drujba (Russia) and Samsun (Turkey). It is complemented by 373 more kilometers on Russian land (from the gas fields of Izobilnoj) plus 501 km on Turkish territory (from Samsun to Ankara, the country’s capital). Starting with 3.7 billion m<sup>3</sup> of natural gas, it is going to transport 15 billion m<sup>3</sup>, and finally reach a double capacity.

Other pipelines have been inaugurated, both before and after, but none arose so much interest. Analysts didn’t need much to notice that, in the middle of it, there was a long term, long range game that “opens new horizons for Russia”<sup>7</sup>. Not by chance nor by coincidence did the Kremlin propose the building of other new pipelines to Turkey, transporting not just gas, but also oil. These projects signal that “Moscow wishes to be thus capable of counterbalancing US-UK influence in the region (who were the promoters of the BTC oil pipeline, namely Baku – Tbilisi – Ceyhan) other than from the military security point of view”<sup>8</sup>. To put it differently, if the US has become the “security supplier” for many of the former communist countries, Russia seeks to balance this by becoming their “energy supplier”, not just the supplier of South-Eastern Europe, but also of the European Union, precarious in terms of energy resources and a great deal dependent on Russia. One may therefore appreciate that, in doing so, Russia wishes to win back its influence and protect its interests in Eastern Europe, at the same time augmenting its financial power and, why not, its political one as well<sup>9</sup>.

*Caspian Pipeline Consortium.* This represents another example of a project through which Russia looks after its own interests, while affecting those of transit countries (mainly Romania). The project aims to transport oil from Kazakhstan (from the great field of Tengiz), through Russia, to

---

<sup>6</sup> \*\*\*, *Russia’s Newly Found “Soft Power”*, The Globalist, August 26, 2004.

<sup>7</sup> See, for example, Federico Bordonro, *Blue Stream Opens New Horizons for Russia*, “Power an Interest News Report”, November 21<sup>st</sup>, 2005.

<sup>8</sup> Idem.

<sup>9</sup> To grasp the entire broad array of problems, see also part 4 (*Les points chauds du Globe*) of Yves Lacoste, p. 206 – 328.



the Black Sea, in the region of Novorosijsk port (a huge storage and loading/forwarding facility is going to be built nearby).

Main facts<sup>10</sup>:

*Length*: 1,100 km, of which 752 km already existed (Tengiz – Komsomolik - Kropotkin), and 258 km are going to be build afresh. *Facilities*: 15 new pumping facilities, 13 storage tanks (each with a holding capacity of 100,000 m<sup>3</sup>), 5 of which will be situated around Novorosijsk. *Main stakeholders*: the Russian government (represented by Lukoil, Rosneft and Transneft) – 24%, Kazahoil – 19%, the government of Oman – 7%, LukArco (JV Lukoil and Atlantic Richfield - US) – 12.5%, Rosneft Shell – 7.5%, Mobil (US) – 7.5%, Kaz Pipeline Ventures (JV Kazahoil, Amoco, the former Holding Munai Gaz) – 7%, and others. *Duration of project*: approximately 40 years; will operate at minimum capacity starting 2014. *Revenues*: Russia's profits alone are estimated around \$23 – 24 billion.

## 6. An “OPEC” for Natural Gas?

We are all familiar with OPEC's role on the world scene following the “oil shock” of 1973, who knew how to exploit at its fullest the most used and sought after strategic energy resource; there have been, of course, gaps along the way, but they do not concern the subject of this paper. Lately, there is talk about a similar gas cartel. Although some are still inclined to ascribe the paternity to Iranian ayatollah Ali Khamenei, who in January 2007 made a similar proposal, “Financial Times” used the term two months before (November 2006) when, quoting a NATO Report, it mentioned Russia's desire to create such an organization. The configuration of the anticipated cartel is extremely interesting, as it would contain Russia, some countries from the Gulf Region (Iran and Qatar), from North Africa (Libya and Algeria) and from Central Asia (Kazakhstan, Turkmenistan, Uzbekistan, and others). This would certainly wage a huge amount of power, since Russia and Iran alone concentrate 43% of the world's natural gas reserves!

### References:

Bordonaro, Federico, *Blue Sream opens new horizons for Russia*, in „Power and Interest News Report, November, 2005”.

Neguț, Silviu, *Introducere în geopolitică*, Editura Meteor Press, București, 2007.

\*\*\*, *Russia's Newly Found “Soft Power”*, in „The Globalist”, August, 2004.

\*\*\*, rev. „Lumea”, București, 2006-2007.

\*\*\*, British Petroleum Statistical Review of World Energy 2006.

www.caspenergy.com.

---

<sup>10</sup> Also refer to Terry Adams, *Caspian Hydrocarbours, the Politicisation of Regional Pipelines and the Destabilization of the Caucasus*, Center for European Policy Studies (CEPS), Brussels, 2000.

## **Acknowledgement**

The Conference proceedings were supported by the financial support under the CEEEX III research grant (2006-2008) of the Ministry of Research and Education of Romania.

The event was possible thanks to the dedicated efforts of the Conference chairs, Professor Mihai Korca, former Dean of the Faculty of International Business & Economics, Academy of Economic Studies of Bucharest, and Dr. Liviu Muresan, President, EURISC Foundation. Our appreciation also to the following people for their generous assistance:

### *Scientific Committee*

Ioan Popa, ASE Bucuresti  
Dumitru Miron, ASE Bucuresti  
P.M.E. Volten, University of Groningen  
Franz-Lothar Altmann, SWP Berlin  
Ovidiu Rujan, ASE Bucuresti  
Gabriela Dragan, ASE Bucuresti  
Mihaela Lutas, UBB Cluj  
Alexandra Horobet, ASE Bucuresti  
Radu Lupu, ASE Bucuresti  
Cristian Paun, ASE Bucuresti

### *Organizing Committee*

Alina Popescu  
Alina Chiciudean  
Iacob Adina Maria  
Roxana Voicu-Dorobantu  
Dan Dumitrescu  
Alina Draghici  
Ştefan Ungureanu  
Cristina Dragoi  
Sebastian Ceptureanu  
Eduard Ceptureanu

Valentin Cojanu  
Conference Organiser  
Faculty of International Business & Economics

February 2008