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The risks of Euro adoption in Romania – an analysis based on ten criteria

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Abstract. *In this study, I have proposed and examined ten criteria to analyze the challenges of joining at Monetary Union, explaining the need to include them in government and multinational companies' strategies. The criteria adopted in the case of Romania concern the potential impact of Euro adoption on economic activities, the common monetary policy effects on the Romanian economy, synchronization with the Euro area, labour market flexibility, as a tool of shocks adjustment etc. After stating each criterion, I have made a brief analysis of how that could affect the balance of costs and benefits of giving up own currency, using conclusions of the optimum currency areas theory.*

Keywords: real convergence; trade integragion; business cycle convergence; labour market flexibility; optimum currency area.

JEL Codes: F15, F43, F44.
REL Codes: 20E; 20H.

At first glance, the theme proposed in this study might seem inappropriate in a time characterized by increasing increasing uncertainty in the construction of the European Monetary Union and by the prospect of strict institutional arrangements that will increase the costs of participating at the Euro area. However, the analysis will certainly pass the test of time because they remain valid regardless of the fate of the Euro zone or the time of adoption of the Euro currency by Romania. In addition, I believe that the experience of the economic crisis was a test for adopting the Euro by Romania. Negative external shock was passed to the economy through trade and financial channels and monetary policy was not effective in neutralizing the impact of the shock. In other words, the economy has not benefited from an adjustment tool, that the economy will not have any when it will adopt the single currency. Romania recorded a slight economic recovery, but not by identifying other internal mechanisms for adjusting the negative shock, but benefiting from external channel adjustment (economic recovery of trade partners) or favorable natural conditions for agriculture, as in 2011.

However, these adjustment mechanisms will not work in all cases of Romanian economy slowdown. Therefore, the lack of internal solutions to neutralize the economic shocks will generate their persistence and rising costs of the single currency adoption. Therefore, the natural solution that should support government authorities would be to postpone the decision to adopt the single currency, in the context of a weak real convergence, a lower business cycles synchronization and lack the internal mechanisms of adjustment to shocks. However, the more trade and financial linkages between economic agents from Romania and those from the Euro area countries will increase the benefits of Euro adopting, helping to reduce the risk of asymmetric shocks and to increase the convergence of business cycles.

1. The degree of structural convergence of the Romanian economy with Euro area economies

In terms of an optimum currency area criteria, the costs of adopting single currency by Romania will be lower if there is a structural convergence between the economic and trade structures and if there is a close correlation between business cycles. Romanian economic expansion has not generated a lower structural divergence with the Euro area, and this situation will not improve significantly in the future. Romania has the most different structure compared to the Euro area economy, due to a relatively higher share of agriculture (more than four times higher in 2010), of industry (by about 10 percentage points over the average), of transport and trade (by about 4 percentage points higher) and of the constructions (9.6% of GDP compared with 5.9% in the Euro area). The share of the service sector was lower 24 percentage points in 2010 compared with European average.

If the divergence of incomes, productivity and economic structures is higher, then Romanian economy will be exposed to asymmetric shocks compared to monetary Union, and the capacity of neutralizing them will be much lower. However, the existence of a structural divergence with the Euro area is not always a negative aspect. Thus, the greater relative importance of certain sectors, such as manufacturing and agriculture, accounted for Romania an opportunity for economic growth in 2011. Moreover, the two sectors were the only drivers of growth of the Romanian economy in the context of rising external demand and favorable natural conditions. In general, the economies which recorded a process of structural convergence with developed economies will be able to increase the productive potential more easily, leading to sustainability of the economic growth and the reduction of macroeconomic volatility. Therefore, the private economic agents will know that lowers the risk of a "boom and bust" evolution.

2. The degree of trade and financial integration with the Euro zone economies. Macroeconomic developments of the main economic partners

The economic integration process between Romania and the Euro area has supposed rising trade and financial linkages, both having a decisive role in stimulating the economic convergence in the period 2003-2008. Therefore shocks affecting monetary union countries will pass faster in the Romanian economy, affecting the degree of business cycles synchronization. Before the economic crisis, financial flows to Romania, either through direct investment or bank financing, have generated a growing non-governmental credit which was reflected in the increase of the private consumption, investment and imports, current account deficit and foreign private debt. The economic crisis triggered in 2008 stressed the importance of the two transmission channels of shocks in the absence of internal solutions to stimulate the economy. From a trading point of view, Romania recorded a high integration with the EU-27, in particular with the economies of the Euro area core. Thus Romania was in 2010 the seventh economy in terms of trade with the EU-27 (73.3% of exports and 74.3% of imports), and the degree of convergence between the structure of exports and imports increased significantly compared to 2000. In terms of technological content of goods exported, Romania recorded one of the fastest structural adjustment, currently accounting for over 40% of medium technology goods exports compared to about 20% a ten years ago, being the fifth EU economy by this criterion.

Also, the monetary union countries hold 70% of the stock of foreign direct investment in Romania and the largest part of national banking assets, 85% of which being owned by foreign banks. FDI inflows have contributed both to stimulate economic growth in Romania and structural convergence with the European Union in the context of changes in sectoral and trade structures. Also, FDI have represented a stable source of financing the increasing current account deficits during the economic boom. Financial integration has been an opportunity to support the convergence of the countries of Central and Eastern Europe during their expansion, but may represent a threat because of problems arising from the successive crises in the Euro area. Financial flows received by Romania have increased dependence on foreign banks financing the economy, especially from the Euro area, which generated a vulnerability to financial shocks.

In terms of private economic agents, the financial sector can represent both a way to mitigate economic shocks by increasing funding for economic activities, as well as prolonging the recession, due to the effects of financial contagion and reducing confidence in the national economy. In terms of foreign capital invested in the banking system in Romania, there is a high exposure to Greece, Austria, the Netherlands and France. Compared to the 2000 year, the share of foreign capital owned by Austrian banks recorded the highest increase reaching a maximum of 30% in 2008, reducing then to 21% in 2010. The Greek capital remains the majority (30 percent) among banks with foreign-owned banks, but with a declining trend, the same trend being followed by the the Austrian and French banks, too.

In the context of trade and financial integration, it becomes extremely important the macroeconomic evolution of the main economic partners of Romania. Thus, the promotion of economic austerity policies by economic partners will generate a reduction in external demand, including for products obtained in Romania, which will led a drop in domestic economic activity. Therefore, the Romanian exporters must know the macroeconomic developments of trading partners, the impact of stimulus measures/economic austerity and to adjust theirs business plan in advance accordingly with these evolutions. Exporters may try to seek other faster growing markets, in the context of the projected declines recorded by traditional partners. Similarly, financial businesses from Romania must know and accurately anticipate the impact of financial developments recorded in the economies which ensure funding for domestic banks. For example, a financial shock in an integrated economy with Romania may rise expenses and reduce the financial resources attracted from that economy, which will adversely affect the ability of public and private debt financing.

3. The degree of business cycle/industrial production convergence with Euro area economies

The degree of business cycles synchronization with the Euro area constitutes one of the most important criteria to study costs and benefits of the single currency adoption. This criterion has a complex endogenous feature, being influenced decisively by the previous criteria set out above, namely the degree of structural convergence, respectively trade and financial integration. The analysis of this criterion can be made ex-ante, because it allows both evaluations of the cyclical gaps between Romania and the Euro area, as well as domestic business cycle dependence on those recorded by the main trading partners. Also, this criterion can be rated ex-post also, because it may be sensitive to the introduction of the single currency, which generates an increase of trade and financial exchanges. The case of the Monetary Union peripheral countries suggests the possibility that the degree of synchronization of the two economies to grow, even if structural differences between these are persistent. In these conditions, cyclical convergence process is not sustainable, and the difference between these economies may increase.

For example, two economies may register a similar macroeconomic evolution as a result of factors specific to aggregate demand, while supply factors are not correlated. Romania and the Euro area are extremely divergent in terms of share of agriculture, public services and certain industrial branches (which produce public utilities), but shocks affecting an economy will not be reflected automatically in the other economy. If there is no trade with products specific to a particular sector or financial links between economic agents concerned, then structural divergence shall not constitute an obstacle to business cycles synchronization with the Euro area. The current differences between the Euro area economies have existed in some form before the current crisis, but it was considered that they are not able to adversely affect the functioning of monetary union.

According to the endogenous hypothesis, the economies with a common currency will have automatically more synchronized business cycles and the monetary policy decisions will be more symmetrical among Member States. Their cyclical correlation is influenced by three factors. The first refers to trade integration, which tends to occur at intra-industry level. The disappearance of currency risk will intensify trade integration, and this will be accompanied by a smaller asymmetry of shocks, ie more synchronized business cycles. The second factor takes into account financial integration, a phenomenon that arises in the context of a common currency. Financial shocks will be transmitted symmetrically and the economies of a monetary union will become more convergent. The third factor relates to structural gaps between members economies. In general, these economies tend to converge in terms of structure, as a result of competitive pressures and of deepened trade and financial integration. If the countries with a single currency are more structurally convergent, then the internal and external shocks will be more uniform transmitted, and the degree of business cycles synchronization will increase.

Generally, increasing trade and financial integration with the Euro area core countries will increase correlation with their business cycle, while promoting divergent macroeconomic and structural policies will generate a lower business cycles synchronization. Therefore as much, the synchronization of business cycles will be lower then the cost single currency adoption will be higher. In the conditions of asymmetric shocks, there must be effectives other adjustment mechanisms both at the level of markets (for example, labor mobility), and at the level of macroeconomic policy (for example, using fiscal stabilizers or fiscal transfers to the countries affected by the recession). If prices and wages are flexible, the financial and labor markets are not sufficiently integrated to ensure full mobility of factors and fiscal transfer system does not exist, then the only shock absorption mechanism is the similarity of demand and the supply side shocks and the business cycle synchronization with the Euro area. Countries that are exposed to the symmetric shocks tend to have more synchronized business cycles and, therefore, similar economic policies. Asymmetric shocks are not single cause of the monetary integration costs because these may result from the different ways in which member countries respond to some symmetric shocks.

4. Assessing the role of stabilizer of monetary policy before and after the adoption of the single currency

If the monetary policy promoted by the NBR is more effective in neutralizing shocks affecting the Romanian economy, then giving up the national currency will be more costly because it loses a useful tool for economic adjustment. However, the transmission channels of local monetary policy are adversely affected by a number of factors such as the high degree of euroisation in Romanian economy, reduced confidence of economic agents in the economic recovery, the budget deficit covered from internal sources etc. In addition, monetary policy is less effective in emerging economies characterized by low resistance to external and structural shocks, the latter affecting more the aggregate supply. Under these circumstances it can be said that the main cost associated with the decision to join the Euro area is to reduce the potential for absorption the temporary aggregate demand shocks. The supply side shocks become permanent, requiring higher flexibility of the economy for their neutralization. Implementation of policies to stimulate aggregate demand as countercyclical policies may have perverse effects in a monetary union, leading to increased inflation. This situation causes an increase of the relative price, which involves loss of external competitiveness, the final positive impact on real output being more reduced.

Following the adoption of the Euro currency, Romania can lose the independence of domestic monetary policy, and the economy will react to monetary policy decisions taken by the European Central Bank. I believe that the Romanian economic agents need to know, to anticipate the effects of the common monetary policy and to interpret the effects on economic activity at the national level. According to Lane (2006), EMU automatically contribute to the amplification and not to mitigate asymmetric shocks, the common monetary policy leading to a divergence between real interest rates between countries in the context of the inflation differential. As a general rule, decisions of the ECB are favorable for the most important economies of the Euro area, because these countries influence decisively the aggregate variables of the Monetary Union. Under the terms of a common monetary policy, countries will be able to maneuver only the instruments of fiscal policy and the structural policies. Thus, asymmetric shocks and lack of business cycles synchronization are the biggest threats for the currency area optimality.

Not only underlying inflation differential matters to asymmetric impact of the common monetary policy. Differences in terms of inflation developments, real GDP, and the output gap lead to different optimal rates of interest in Euro area countries, applying the Taylor rule. In the economies where the optimal interest rate is much different from that set by the ECB, monetary policy generates asymmetries regarding developments in inflation and output gap, not providing their stabilization of them. Based on this criterion it results that it should be checked often developments in inflation and the business cycle in Romania with those recorded in the most important countries of the Monetary Union. If Romania has another phase of the business cycle compared with Germany, France and Italy, the common monetary policy will be pro-cyclical in Romania, which is not providing the economic stabilization. Also, in the context of higher rates of inflation in Romania compared with the Euro area, monetary policy becomes more expansionary for our economy that will generate not a reduction but an increase in the inflation rate.

5. The competitiveness differential between Romania and the Euro area. The risks of damage the competitiveness after the adoption of the euro

The adoption of the Euro currency supposes abandoning the national currency, in the context of which a flexible exchange rate is a tool for shock stabilizing and mitigation competitiveness gaps. Thus, in the case of a single currency, less competitive economies no longer have a tool to artificially increase the efficiency of exported goods. Removal of exchange rate risk will increase the competition between economies of the Monetary Union and the most development and sustainable economies will win. Naturally, economic agents coming from less developed economies, such as Romania, will be less competitive. However, not only the initial state of the external competitiveness degree level matters, but also promoted policies within the Euro area. Inside the Monetary Union the economies where inflation is higher than in the case of trading partners and in which there is an increase of the real wages higher than labor productivity will lose. Regarding the latter aspect, it will not matter just to observe the correlation between wages and productivity, but also to obtain a competitive gain toward trading partners. For example, if Germany records a declining of the real unit labour costs by 2% in the industrial sector, then the economies without a similar or better evolution will lose competitiveness relative to Germany. Consequently, Romanian companies need to know the evolution of prices for industrial products (tradable goods) in the rest of the Euro area countries, as well as the evolution of labor costs in those economies, in order to assess in real time their own competitiveness on the European market.

The inflation differential between the member countries of the Euro area generates divergences of external competitiveness and of real interest rates. Differences in the level of indirect taxes, the level of charges applied to labor or exposure to global shocks are explanations for the differential inflation within the Euro area. Thus, the economies characterized by an inflation rate above Euro area average will record, on the one hand, a reduction in demand due to the relative loss of competitiveness, and, on the other hand, an increase in demand due to lower real interest rate (Walter's critique). In the first decade of the Euro currency introduction the countries which currently have problems relating to debt financing (Spain, Ireland, Greece and Portugal) have recorded a loss of competitiveness by about 20% compared to Germany. In other words, the real unit costs of labor have increased by about 20% lower in Germany than in the peripheral countries of the EU. To gain competitiveness, the peripheral countries must promote internal adjustments in order to decrease the labour costs.

Spain and Ireland experienced the largest reduction in competitiveness after 2003 year, beginning with the real estate boom, while Germany registered the most significant improvement in competitiveness since 2000, by decreasing the real unit cost of labor. Differences in competitiveness are reflected in the divergent evolution of foreign trade. Thus, the economies that register a significant increase in the unit cost of labor relative to the Euro area will be characterized by a slower export growth rate compared to the Euro area. The consequence of this evolution will be the increasing trade deficit countries of the less competitive compared to the most efficient countries. Romania may face to the so-called boom-bust effect, explained by Blanchard (2006) – increasing inflation and labor costs during the economic expansion will weaken the economic competitiveness within monetary union, in the absence of any others adjustment tools. If productivity growth is not sufficient to counteract the influence of higher wages, then the economy will slow down the growth rate. The economic agents from that economy will have to make some adjustments to diminish competitiveness deficit, which may lead to short-term increase in unemployment.

6. The degree of labour market flexibility. Risks of a high rigidity

The flexibility of the labour market is one of the most important tools for adjusting the shock in a monetary Union. The degree of flexibility can be assessed on the basis of several criteria – labour mobility, the reaction of wages depending on the unemployment rate or relative to the output gap, demand flexibility, labour legislation and the forms of flexibility related to the labor supply (work schedule, the typology of the contracts, the ability of individuals to be flexible on the labour market, etc.). Romanian companies must know and interpret progress in increasing labor market flexibility, because according to them it can evaluate the persistence of shocks will affect the Romanian economy within the monetary union. If the progress is reduced, then economic shocks will acquire a permanent character and cyclical synchronization of Romania economy will be reduced.

The countries that are unable to find means of adjusting internal shocks will register a lower dynamic structural transformation and competitiveness losses within the monetary union. Therefore, the phases of economic recession will be prolonged and will be accompanied by increasing structural unemployment. In the case of small countries, even in conditions of functional rigidity of the labor market, its flexibility is favored by higher mobility of workers. However, for larger countries, this is a very important condition to faster economic adjustment. In Romania, there is a lower dispersion of regional unemployment rates compared to some CEE countries and the degree of workers' mobility is higher at intra-regional level, but the rigidities of the labour market cancel the potential positive previous features.

Generally, the labor market adjustment to certain shocks can be done by changing labor demand, through labor mobility and flexibility of real wages or unit labor costs. Mann-Quirici (2005) have tested the importance of real wage adjustment shocks in the absence of national monetary policy and argued that it is a better mechanism at European level compared to workers' mobility or fiscal transfers possible because it has a faster action compared the other two solutions. Differences between labor market institutions within EMU are one of the asymmetric shocks causes. Studies carried out in the case of the EU confirm a very low speed of adjustment of real wages to certain economic shocks. The lower wage flexibility is reflected by higher price rigidity at the economy level. Even if in the recession phases there is a higher pressure unemployment, the economic decline influences the employment degree rather than the wage level. Therefore, companies will decrease the wage costs only in a lesser extent, and their recovery will be more difficult. Some of the cases refer to certain specific labor market institutions, such as the degree of legislation rigidity on employment, trade union power, establishing a minimum wage or the existence of insider-outsider model type on the labor market. As the differences between the functioning of the labour market are more significant, both wages and prices will evolve divergent within the Euro area, even in the presence of symmetrical shocks. Therefore, the countries whose labour market institutions are different (either they are too flexible than average or much too rigid compared to this one), will find that the decision to adopt a single currency is too costly.

7. The risks of establishment an inappropriate EUR/RON conversion rate

One of nominal convergence criteria relate to exchange rate stability within a fluctuation band for at least two years of participation in ERM II. The exchange rate fluctuations are judged according to the central parity rate set at the beginning of the entry in the exchange rate mechanism. Consequently, the final rate of Eur/Ron conversion will be influenced both by the level of the exchange rate parity, but also by the fluctuations in the ERM II. Completion of the participation in the ERM II requires the establishment of the conversion exchange rate between the national currency and the euro, which will have a significant impact on domestic businesses.

If joining to the Euro area would be at too high conversion rate, ie a too appreciated national currency against the euro, then it would be adversely affected export competitiveness and thus economic growth process. Otherwise, a depreciated exchange rate will lead to boost exports, but will also generate additional inflationary pressures, which can not be easily mitigated by domestic macroeconomic policies. In this situation, ERM II can be considered a phase to test of the central rate, given that this will be influenced by performance of the Romanian economy, respectively by Romanian competitiveness relative to the Euro area. Setting the central parity exchange rate is very important because the accurate assessment of factors influencing equilibrium value of the national currency may cause an exchange rate central parity more similarly with final conversion rate of the national currency.

According to the experience of Euro area member countries, it can be said that there are two options for the entry in the ERM II, the appreciation of the national currency, in the case of Ireland, and the depreciation of the currency, as in the case of Greece. Before entering the Euro area, Ireland's currency has been fixed at a rate 8% under bilateral rate at that time, which result in a devaluation by that percentage. To reduce pressure on wages and prices, it was decided that bilateral exchange rate revaluation by 3%, which has dampened the expected depreciation. Greece joined to the ERM II with a depreciated exchange rate by 7.5% compared to the rate at the end of 1998, which led to a depreciated final conversion rate. Whether or not the conversion rate is over or under valued relative to the equilibrium exchange rate, the impact on competitiveness will be the same. On the one hand, a depreciated currency will generate inflationary pressures, which will increase the relative prices of goods produced in Romania and will decrease the efficiency of goods exported. On the other hand, an overvalued currency will automatically generate a reduction in exports and an increase in the current account deficit, a situation which can be countered only through the promotion of austerity measures and by increasing the unemployment rate. Therefore, the benefits of joining the Euro area will be higher if it will adopt a conversion rate as close to equilibrium exchange rate, i.e. the rate level that maintains internal and external imbalances in the sustainable limits.

8. The impact of the Euro on transaction costs and on the inflation rate

The volatility of the national currency exchange rate is one of the factors that increase the uncertainty of certain business decisions of private economic agents, causing increased transaction costs incurred by them. Therefore adopting the single currency will generate lower transaction costs (financial and administrative) for the economic agents, and increase their profitability by eliminating the uncertainty about exchange rate changes. Another effect of the

Euro introduction relates to the impact on inflation in the context in which over 90% of Euro area citizens have argued that the adoption of the Euro currency has led to a price increase. In this context, 84% of European people perceived the relationship between the Euro and domestic prices as being in the disadvantage of consumers, because it generates a reduction in their purchasing power. The main reasons of this perception refers to the fact that there is a transfer of the conversion costs to the consumer, a rounding of the prices to the psychological levels, a nominal price rigidity demonstrated by menu costs hypothesis and the fact that firms take advantage due to lack of transparency of prices changes. However, the link between the introduction of the single currency and inflation becomes more insignificant after the first year, being other factors that explain the inflation differences between the member countries of the monetary Union, such as:

- the existence of different levels of economic development – less developed economies will register higher rates of productivity growth, which will generate accelerating inflation through Balassa-Samuelson effect, the process of price convergence and the anticipation of higher rates of profit.
- the event of asymmetric shocks due to differences concerning the shocks on the demand side and the supply side ones. Their causes concern, among other things, to the different structures of the consume, the structural divergences between the member states, the differences between macroeconomic policies promoted at the level of each economy.
- the differences in institutional, legal and financial framework. In the context of differences concerning taxation, business environment, market goods, labour market and the financial sector, there are different mechanisms of reaction to economic shocks which will generate a different influence on the inflationary process.
- the persistence of inflation. It describes the strong dependence of the current inflation rate by its previous levels, given that adjustment mechanisms of the inflationary shocks are ineffective. In the context of the lack of structural reforms to increase potential economy affected by a negative shock to aggregate supply side, these shocks will acquire a permanent feature and will increase the divergences compared to the more flexible economies.
- the existence of different trading structures. Heterogeneity of inflation inside the Monetary Union is determined both by the different opening to the commercial partners outside the Euro area, as well as divergent reaction to shocks resulting from the change in the course of the Euro

at internationally level. The depreciation or appreciation of the single currency is raising the price of goods imported from outside the Monetary Union.

Because Romanian economy is very divergent from the point of view of the economy's structure, degree of development and the functioning of markets, then the risk of divergence inflation rates with Euro area will be significant. It will increase due to the asymmetric impact of the common monetary policy and sue to the competitiveness gaps. Once have joined the monetary union, most less developed economies (Spain, Greece, Portugal and Slovenia) showed a significant increase of the domestic prices. Even though before the adoption of the single currency the inflation criteria represented an important criterion of nominal convergence, after accession, it will be more difficult to control it by the Member States. Economies where inflation has been reduced as a result of macroeconomic policies and certain predisposing factors, but not structural ones, will face to the higher prices. In addition, the lack of flexibility of the economy has emphasized the post-Euro inflation. Also Balassa-Samuelson effect can be an important source of price increase. If before admission to the Euro area there was a tradeoff between inflation and currency appreciation, after accession, that effect has a single consequence namely to inflation.

9. Fiscal policy constraints in Romania before and after joining to the Euro area

The adoption of the Euro currency by Romania involves loss of some tools for adjusting economic shocks, but keeping national fiscal policy. From a theoretical perspective, fiscal policy is highly effective in the case of a fixed exchange rate, representing a useful tool for the economic recovery within monetary union. However, there are some constraints on the stabilizing role of fiscal policy in Romania, which refers to the reduced margin of maneuver of the government and to the restrictive features of EU Fiscal Pact. To the extent that the economy will not be able to cope with these restrictions, the single currency will be more expensive for Romanian companies. The Government no longer can support them during periods of reduced sales by reducing the fiscal burden or increasing public demand.

The first constraint of the fiscal policy refers to a limited fiscal space given that budget deficits (which automatically increase during recessions) have extended even during expansion, increasing the stock of public debt to GDP. Stabilizing role of fiscal policy is that it should not be pro-cyclical, structural budget balance should not worsen in periods of economic expansion or improve in the economic downturns. In the context of a pro-cyclical fiscal policies, the economy will overheat during periods of economic expansion, thus affecting the management of the monetary policy. Based on the structural budget balance can be estimated the fiscal adjustment to be achieved by Romania until 2015. Thus, Romania must achieve a fiscal consolidation by around 5% of GDP in just two years, which is one of the largest budgetary adjustments in an economy affected by the economic crisis. These adjustments should be made in the context of enormous pressure on the general government such as the increase of the social security budget deficits, the doubling of the public debt share in GDP in just three years, due to pro-cyclical fiscal policies pursued in previous years the economic crisis, but also rapidly rising interest expenditure, given that the Government is compeled to refinance debt accumulated. If public debt is still rolling short-term (or medium), then the Government will not win any time and will experience a very fast increase of the interest expenditures. The effects of an unsustainable public debt were analyzed by Hrebenciuc (2010).

The second constraint on fiscal policy relates to compliance with the conditions laid down by a New European Fiscal Pact, both before and after the adoption of the single currency. Its main rule relates to the requirement that the national budgets should be balanced or in surplus, i.e. the budget deficit not to exceed 0.5% of GDP. By setting this target, Romania undertakes an averaged budget deficit over a long time horizon, by a maximum of 0.5% of GDP. In the context of increasing share in the GDP of the interest expenditure it results that Romania have to register a surplus of primary balance, which will lead to lower public debt to GDP ratio. The constraints of the fiscal policy in the context of a new fiscal rule were analyzed by Socol and Soviani (2010), respectively Socol and Măntescu (2011).

10. The impact of the Euro on the attractiveness of the business environment in Romania

From a theoretical perspective, the Euro adoption lead to a reduction in transaction costs, an intensification of trade and an increase in investment, which contribute to increasing the productive potential of the Romanian economy. The business environment becomes more attractive which can boost economic affairs. However, a domestic effort is needed to facilitate the initiation, development, running a business, or to simplify the tax system and to make it more credible. All these structural reforms should be carried out before the adoption of the single currency, to increase flexibility of the Romanian economy. Joining the Euro area will intensify the competition for Romanian economic agents, but also will generate a loss of tools to shocks adjustment. Therefore, the economic policies of the Government must provision the adoption and promotion of structural reforms.

Structural reforms are those which determine the direction to be followed in order to reduce distortions in the functioning of an economy. It follows that the finality of the structural changes established at the macroeconomic level will be seen in the behavior of economic agents at the microeconomic level. To assess progress of structural reform measures a series of structural indicators have to be used. The most famous set of such reforms was proposed by the Lisbon strategy and continued by Europe 2020 Strategy, with the purpose to increase the competitiveness of the economies from the European Union. According to an analysis realized by the IMF (2004) it results that at the global level significant structural reforms gave been realized in the field of financial intermediation, goods markets, international trade, while the necessary changes on the labour market and the tax system were more reduced in intensity. For example, the reform of the labour market can generate higher costs in the short term on employment and production, which can reduce incentives to achieve them.

Conclusions

The objective of this study was to analyze the challenges of the single currency adoption based on ten criteria, inspired by the theory of optimum currency areas and features of weakly structured economy, such as Romania. In general most of the criteria analyzed suggest that adopting the Euro would be a bad news for the entire national economy due to lack of adjustment mechanisms of the economic shocks. The only good news is given by the trends of trade and financial integration, which can lead, under certain conditions, to increasing the probability of the event more symmetrical shocks and ultimately increasing business cycle synchronization with the Euro area.

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