Dependent Development in EU's Extreme Periphery: Industrial Growth, Finance and the Great Recession in Romania

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Introduction

In the big picture of economic development during the past two decades, the European Union's new member states are often associated with fast and deep liberalizations (Gowan 1999; der Pijl 2001; Appel 2016). While neo-developmentalism shaped responses to globalization in Latin America, Asia or Russia as part of various leftist and conservative countermovements (Ban and Blyth 2012; Peck and Zhang 2013; Güven 2016; Doring et al 2017), many of the countries situated in the EU's Eastern part have played a more consistently liberal card instead (Sommers and Wolfson 2014; Bohle 2016; Drahoukopil and Myant 2016; Pavlinek 2016; Appel and Orenstein 2016).

Have the changes brought by the Great Recession hastened the pre-crisis (neo)liberalization steamroller in Eastern Europe's capitalisms, as some have hypothesized (Bohle and Greskovits 2012), or has stability been the norm? This is an important challenge for the VoC scholarship (Hall and Gingerich 2009; Hall and Thelen 2009; Thelen 2009; 2012; Jo Martin and Swank 2012), a tradition that has a penchant for predicting institutional stability and has had little to say about the effects that these crises have had on the institutional complementarities that they study. But this question begs for a follow-up: Has the result of the crisis years been the closing of the development gap, or its persistence? To date, the skeptical answer prevails in the scant literature on the topic. Yet given their date of publication the existing studies (Borocz 2012; Scepanovic 2013; Epstein 2014)[1] could not take the long view that the anniversary of the ten years since the crisis that this paper does.

By looking at the case of Romania, this paper shows that the pressures applied by the crisis such as international conditionality and capital flight have bolstered the neoliberal policy drive that predated the crisis. However, this did not led to the definitive entrenchment of a neoliberal variety of capitalism, as in the Baltics. Instead, the main result have been structural transformations that anchored the country's economy into the dependent market economy mode that scholarship had traditionally associated with the Visegrad countries (Nolke and Vliegenthart 2009; Drahokopil and Myant 2016).

The paper suggests that two transformations stand out. First, the paper highlights the "deep structures" of financial dependence. It finds that although the country's transnational banking model eventually proved to have a stabilizing effect, as others have

[1] Most of the recent literature on convergence deals with politics (Houghton 2014; Vachudova 2014) and state capacity (Bruszt and Vukov 2016).

argued (Epstein 2014; Spendzharova 2014; Önder and Özyıldırım 2016) this came at a high fiscal cost for the state and did not lead improvements in its capacity to deploy capital to help the economy narrow the country's developmental gap with the EU, a task left almost entirely to non-financial multinational corporations and the state. Second, as in Brazil, the classic case of "dependent development" (Evans 1979) Romania's multi-tiered forms of economic dependence have simultaneously closed the economic development gap with its comparable Western neighbors in terms of GDP and industrial sophistication while remaining an extremely fragile growth model saddled with a mediocre social performance.

To make these claims, the paper uses mostly primary evidence culled from Romanian financial media reports, public policy documents and statistics, analyses submitted by Romanian think-tanks and academics, and interviews with key state and corporate actors carried out between 2008 and 2016. The claims also draw on participant observation of roundtables bringing together corporate and state elites and organized by the Romanian branch of Aspen Institute in November 2012 and October 2016.

The study is organized as follows: after placing the paper in the literature on varieties of capitalism, a short historical background of the political economy of Romania is introduced in the first empirical section; then, in section two, the paper delves in the main body of the analysis by looking at the sources of investment dependence and the export profile of the Romanian economy; the comparative analysis of Romanian educational, innovation and corporate governance systems is addressed in sections three, four and five respectively.

Literature review

In a classic VoC perspective, soon after independence the Baltic countries have adapted the liberal market economy (LME): financialized corporate sectors, a service-oriented economy, minimal state intervention, deregulated and mostly firm-level industrial relations, thin safety nets, education and training focused on the acquisition of general skills. At the other end of the spectrum is Slovenia's coordinated market economy (CME), with the state playing a key role in coordinating capital and labor, neo-corporatist industrial relations, a social-democratic welfare state, patient domestic capital for firms and dual system vocational education that delivered the specialized skills needed by Slovenia's sophisticated industry (Feldmann 2006; Adam et al 2009; Crowley and Stanojevic 2011; Hubner 2011).

In between these two extremes stands East-Central Europe. Here, the prevailing variety of capitalism cannot be captured by the existing lexicon due to the transformation of these countries' economies into competitive assembly platforms for multinational (and mostly West European) corporations. Nolke and Vliegenhart call this dependent market economy (DME), an institutional hybrid seen as a variant of Ben Schneider's hierarchical market economy found in Latin America (Schneider 2009; Schneider and Soskice 2009). Its essence is a "specific type of comparative advantage that is not based on radical innovation (LMEs) or incremental innovation (CMEs), but rather on an assembly platform for semi-standardized industrial goods"(p. 679). Loaded with liberalizing tendencies, the DME model has a critical "nonliberal" nature as well. Its institutions provide not only for the efficiency of market actors, but also for their governance via a slew of institutional interventions orchestrated by the state which, despite some variation among the DME countries themselves (Duman and Kurekova 2012) end up privileging foreign capital over domestic capital and labor.

To demonstrate the distinctiveness of the DME variety, Nolke and Vliegenthart identify three institutional complementarities. First, MNCs don't get finance from domestic banks and run insider governance networks, as in the CME mode. Neither do they access finance on international markets and open themselves up to outside control by shareholders, as it is the case in the LME variety. Instead, "mother" companies control the subsidiaries in a hierarchical fashion and get finance from the same sources as the "mother" banks. In this way both finance and governance highlight the dependency relationship. Second, to keep costs down, MNCs prefer low taxes, a medium level of deregulation in the labor market and firm-level collective bargaining. Third, given that MNCs find it more efficient to transfer innovations to subsidiaries rather than invest in innovation-relevant skills or spend substantial amounts on vocational education schemes, as CME firms do.

This dynamic is compounded by the fact that CME-style vocational education schemes require wide coordination between state, capital and labor, an institutional characteristic that has been minimized by the dominant postcommunist transition paradigm. As MNCs have avoided the kind of joint ventures demanded by developmentalist regimes, for example, the corporate headquarters of the "mother" firm can have a tight hierarchical control on innovation flows. This traps DMEs in a situation in which they remain assembly platforms for technologies developed by MNCs. The main outcome of all these institutional complementarities is that they generate a comparative advantage in the assembly of manufactures of middle and high-levels of sophistication. In some countries (Poland, Hungary), the backlash came in the form of financial nationalism (Johnson and Barnes 2014).

In this variegated landscape, Nolke and Vliegenthart (2009) see Romania as a country "stuck" in an underperforming cocktail capitalism. Their motivation of their rejection of Romania from the DME group is based on the outdated Cernat (2006) study and a tangential piece of evidence (Bulgaria's poor performance in complex exports).[2] Similarly, Myant and Drahokoupil (2010; 2012) point to the export of simpler products as a reason for distinguishing Romania from DMEs (Myant and Drahokoupil 2010; 2012).

[2] According to Noke and Vliegenthart, "while the ECE states have outperformed former CIS states such as Russia and Ukraine in terms of GDP per capita development, their superior economic performance (particularly that of Slovakia) becomes most obvious when compared with Bulgaria or Romania. The DME model of Slovakia has been much more successful than the rather incoherent "cocktail capitalism" of Romania. This superior performance is also exemplified by the export share of complex, human-capital intensive industries; from 1996 to 2005 it rose in Solvakia from 41 percent to 51 percent while it decreased in Bulgaria from 31 percent to 23. Slovakia also reports rapid development in high-tech exports from 2003 on. In contrast, the Bulgarian export structure has been relatively stable for the last five years, with some increase in heavy basic exports."

In contrast to the literature on Romanian exceptionalism that draws on VOC, Bohle and Greskovits (2012) show that Romania (and Bulgaria) have in fact converged on the (neo)liberal pattern seen in the Baltics. These authors open a sophisticated discussion on postcommunist capitalist diversity that "grafts" select insights from VoC and classical political economy. Yet their analysis of Romania underestimates the extent to which its integration in European capitalism differs from the Baltic pattern in terms of the role of manufacturing is in need of updating. For example, their argument that FDI inflows in Romania went to low-skill "sweatshop" industries and avoided complex manufacturing sectors (Bohle and Greskovits 2012: 207) needs to be reexamined in the light of recent developments.

In addition to demonstrating that this neoliberal policy regime brought Romania into the DME camp, the paper also challenges the DME framework for its inattention to finance. This is an important gap given the centrality of financialization in the dynamics of contemporary capitalism in general and the economic transformations of the region in particular. A number of studies have looked into the dynamics of the financial crisis in the region and its effects on macroeconomic policy (Gabor 2010; Drahaokopil and Myant 2010; Blyth 2013; Ban 2016). Yet to date scholarship has not explored the implications of this event on the institutional complementarities of East European capitalisms. Furthermore, the paper further explores the implications of the argument made by Greskovits and Bohle (2012) that the Great Recession deepened the neoliberal drive in the region by inquiring about the effects of this drive on the local economic structure, as defined in the terms proposed by the varieties of capitalism scholarship.

Foreign direct investment and complex exports

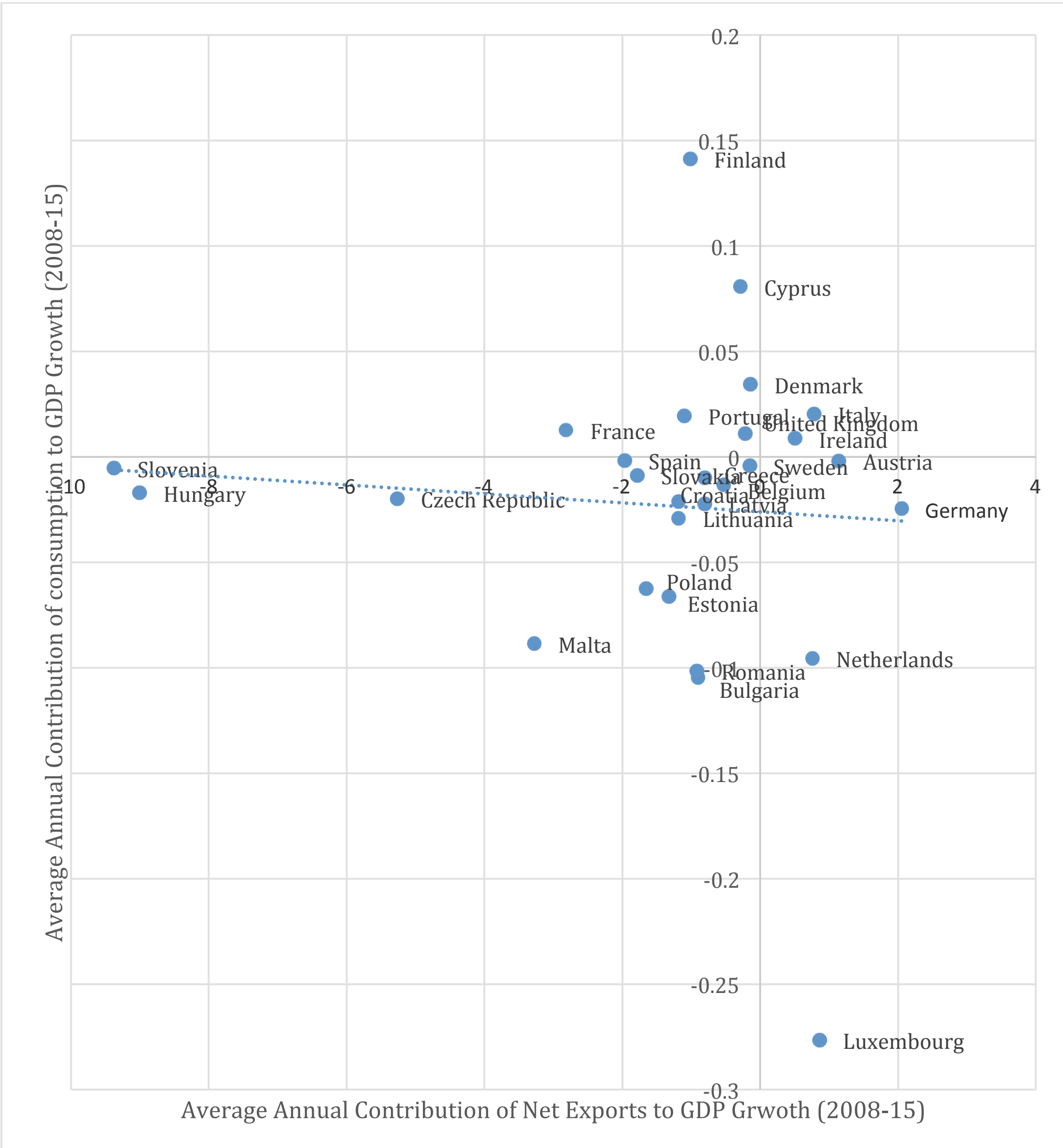
The trade off between the dominant position of foreign capital and the capacity to harness FDI to increase the complexity of exports appears to be the fundamental characteristic of the DMEs (Nolke and Vliegenthart 2009). While Romania did not fit this profile in the early 2000s it certainly did a decade later and, as such, it differs from the Baltic group. During the 2000s, multinationals churning out complex products gained a strong foothold in the economy and became the main engines of export-led growth. Like the average DME, Romania has a large share of industry in its GDP. Between 2004 and 2008 the growth of the turnover rate-or the total of all sales- in the manufacturing sector grew faster in Romania not only relative to the liberal Baltic models, but also relative to all the other DMEs (Eurostat 2012). Energy, automotive, steel and chemicals dominate the top 50 firms by size.[1]

At 21 percent of GDP, the Romanian manufacturing sector's share of the economy puts Romania in the same league with Slovenia, Slovakia and Hungary, rather than with the less industrialized Baltic states or Bulgaria (World Bank 2012). With 1.2 million industrial workers, Romania has the sixth largest manufacturing labor force in the EU27[3]. Moreover, the contribution of exports to GDP growth over the 2008-2015 period is in the same league with Slovakia and the Baltics and far outstrips that of traditional export champions like the Czech Republic and Hungary (figure 1). These facts do not fit

[3] Eurostat, Manufacturing Statistics.

squarely with the conventional representation of Romania as a deindustrialized economy but figure 1 also shows that in both Romania and Bulgaria this came at the cost of the largest squeeze on the share of consumption to GDP growth over the same period.

Figure 1: The contribution of exports and consumption to economic growth (2008-2015).



Source: AMECO

An extensive study (Mereuta and Pandelica 2013) covering 99 percent of the rollover of non-financial firms found that in 2011 foreign firms accounted for 86 percent of gross corporate profits and 92 of the top 100 exporters. Half of all companies that play the role of nodes in each economic sector were foreign-owned. In manufacturing, a sector that accounted for 92 percent of exports in 2014, no less than 74 percent of rollover was controlled by MNCs. The same is true in oil and gas, utilities, IT, retail and telecom, legal services, accounting and marketing. Basically only agriculture, furniture, constructions and tourism are dominated by domestic capital. That said, according to 2016 data, domestic capital's contribution to gross capital formation is three times larger than that of foreign capital, it hires twice as many workers as MNCs, and is more likely to declare its profits to the taxman.[4]

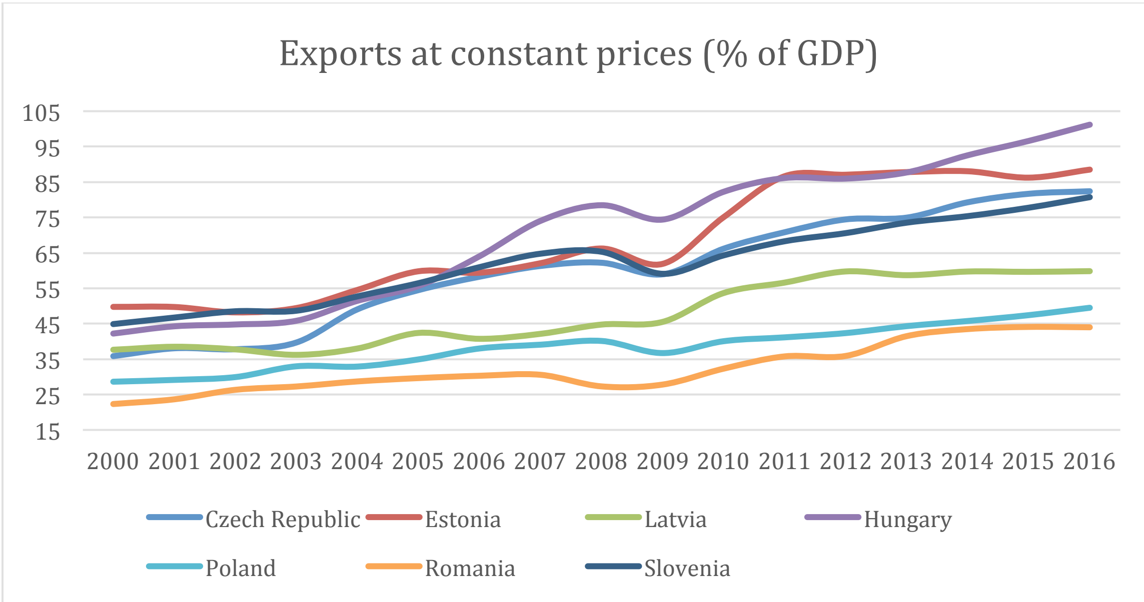
The transnationalization of the Romanian economy was the result of identifiable political decisions. Throughout the 2000s governments consciously attempted to convert the core of the economy into an assembly platform for MNCs.[5] This strategy was facilitated by the ascendancy of neoliberal economic ideas on both sides of the political spectrum and was strongly incentivized by chronic shortages of capital in the public sector and the weakness of domestic private capital (Ban 2011).

The incorporation of Romania's industrial economy into the assembly platforms of MNCs started a convergence process with the export-led DME economies. By the end of that decade, Austrian, German, French and Italian firms (in this order) accounted for about two thirds of Romania's exports. By 2011, of the top 100 exporters, 96 were subsidiaries of multinationals. Thanks to such firms, exports boomed: compared to the 1990s, exports in 2010s were 600 percent larger and their share in the GDP increased. When austerity depressed domestic demand after 2010, growth projections were tied strictly to export dynamics (Canagarajah et al 2012). Critically, once recovery began in 2013, Romania has had the greatest average annual growth rate in exports in the region.

Figure 2: Comparative exports in ECE

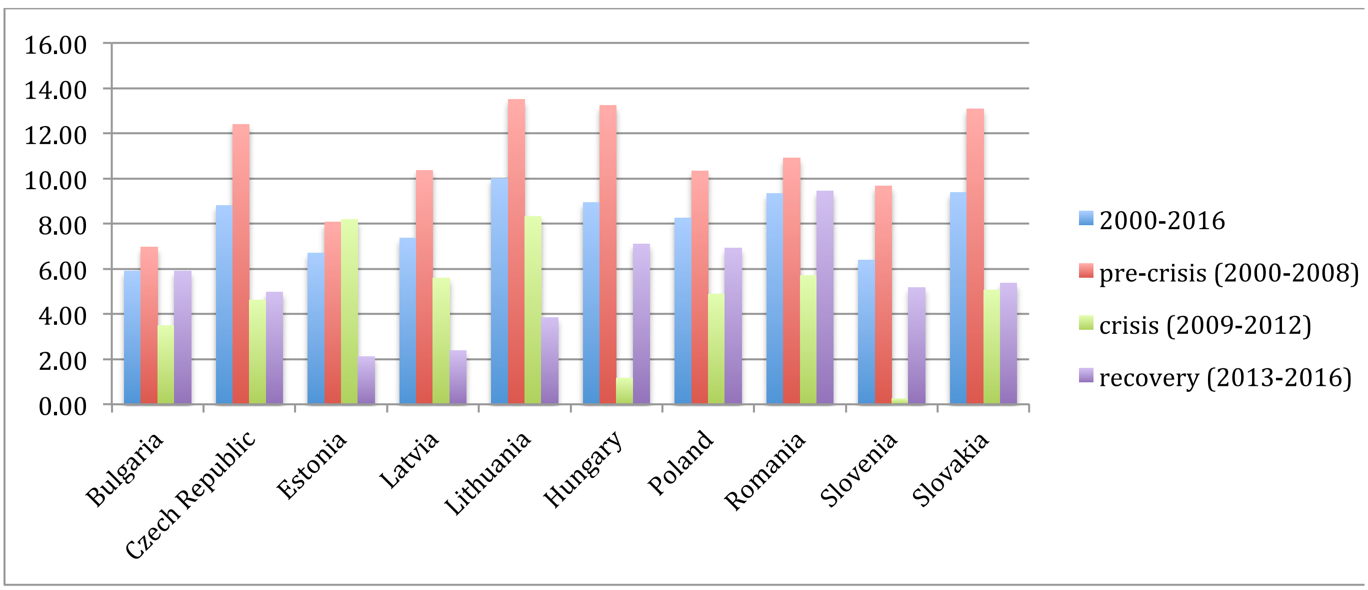
[4] Author's calculations based on data from the Romanian Central Bank and the National Institute of Statistics.

[5] Author interviews with Ion Iliescu, former President of Romania (1990-1996; 2000-2004), June 16, 2006; Nicolae Vacaroiu, ex-prime minister (1992-1996), January 9, 2009; Mircea Geoana, ex-chairman of the Social-Democratic Party (2004-2010), December 17, 2012.



Source: AMECO

Figure 3: Average annual growth rate in exports (select periods)



Source: AMECO

Most importantly, this analysis challenges the thesis that Romania's incorporation in the European economy is dominated by exports of low complexity (Vliegenhart and Nolke 2009; Bohle and Greskovits 2012). By 2012-2013 Romania was no longer the low-end textiles-and-steel territory of the 1990s. The bulk of FDI was invested in energy, chemicals, means of transportation, industrial equipment, mining and steels. Manufacturing attracted most FDI (44 percent), as the low wage army of labor with solid engineering skills made possible by the modernist educational philosophy of Romanian socialism made possible a boom of Western investment in manufacturing, from cars to aircraft parts.

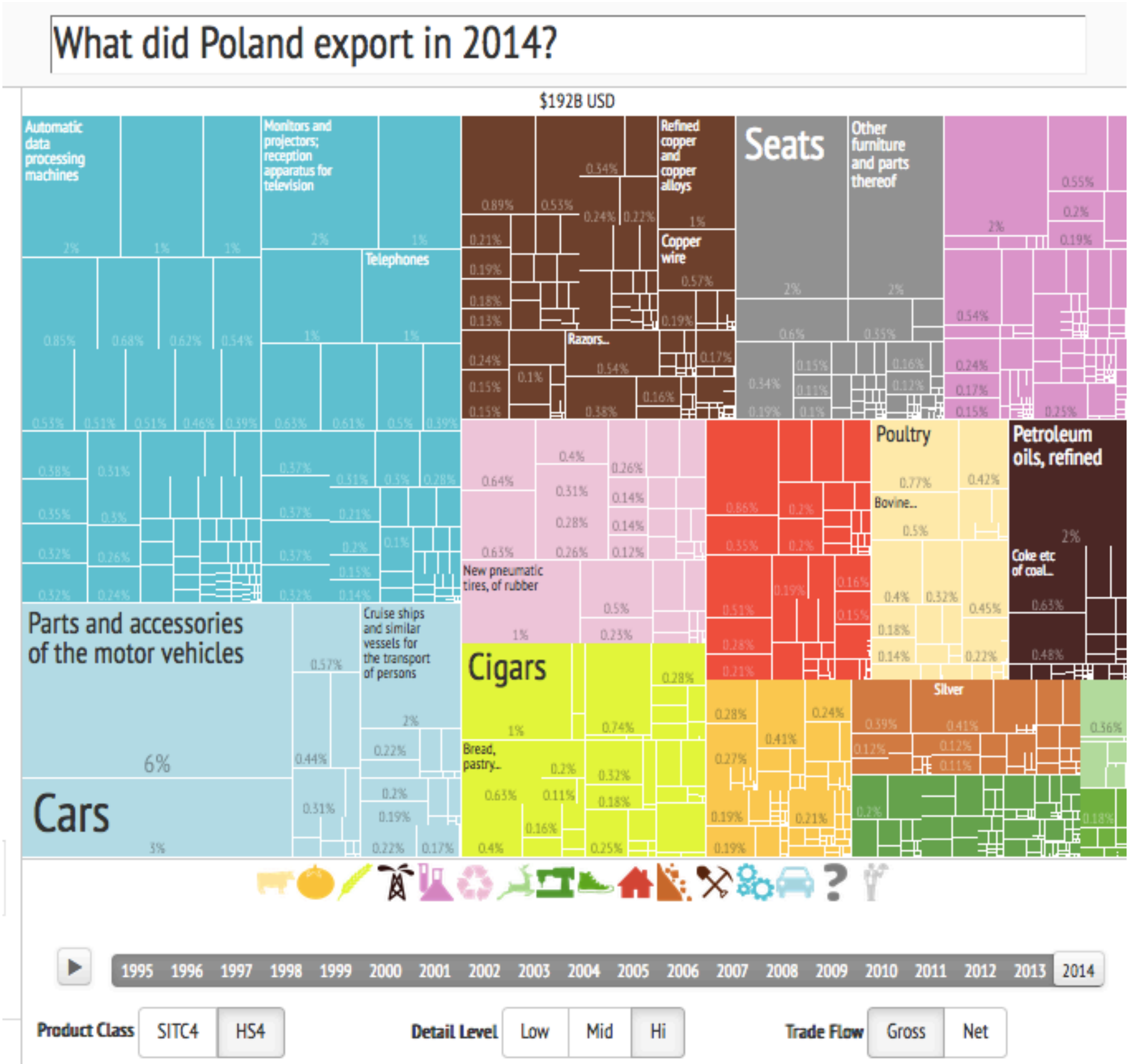
International brands like Renault or Ford established some of their largest plants in Romania by purchasing off-the-shelf factories built during socialism but others (Continental, Nokia) built new ones. Textiles and footwear, the erstwhile export niche of the Romanian economy, received only 1.4 percent of FDI, three times less than the IT sector.[6] Like in the DMEs and unlike in the Baltic countries, this outcome was as much the result of a decades-long experience with industrialization as of industrial policies targeted at multinationals that invested in activities of medium and high complexity.

In relative terms, this transformation makes Romanian exports quite similar to the DME model. In the ranking of export complexity done by MIT's Economic Observatory, the level of complexity of Romanian exports has gone from a low level in the early 2000s to ranking close to the Netherland's, lower that that of Hungary, the Czech Republic or Slovakia. Surprisingly, it is higher not only relative to medium-income Bulgaria and the Baltics, but also to Spain and Portugal, two high-income European economies.[7] Within the DME world, Romania's export profile is virtually indistinguishable from Poland in terms of their complexity. In contrast, the Baltic states and Bulgaria have export profiles that put them in the company of commodity exporters (Brazil, Canada), traditional low end manufacturing economies (Portugal) or war-ravaged economies (Lebanon, Serbia, Bosnia).

Figure 4: What did Poland Export in 2014?

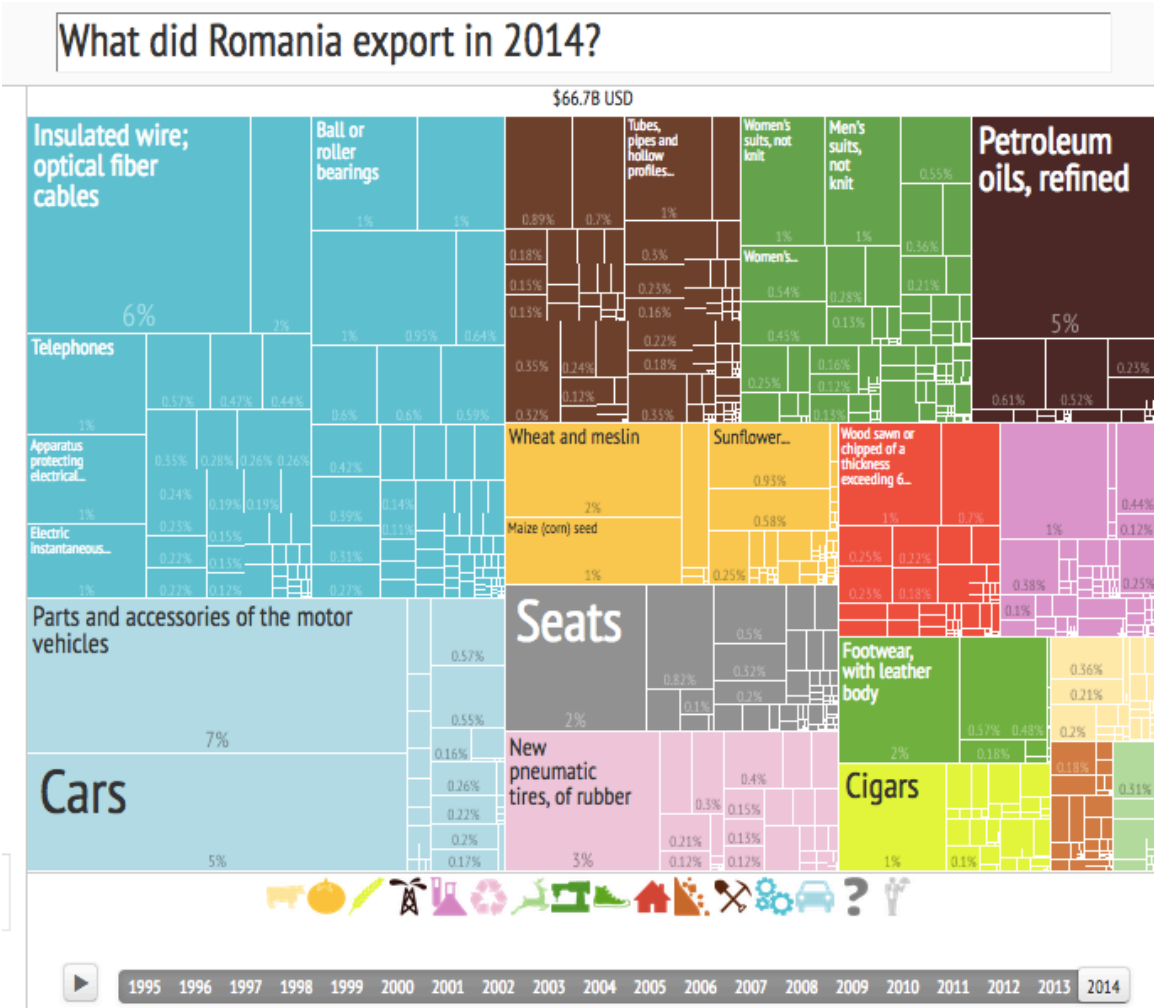
[6] Marin Pana, "A growth engine: FDI and their role in the economy from Roman to Boc/Un "motor" de creştere: Investiţiile străine şi aportul lor la economie, de la Guvernul Roman la Guvernul Boc, *Curs de Guvernare*, September 30, 2012

[7] MIT, The Observatory of Economic Complexity, http://atlas.media.mit.edu/rankings/



Source: MIT Atlas of Economic Complexity

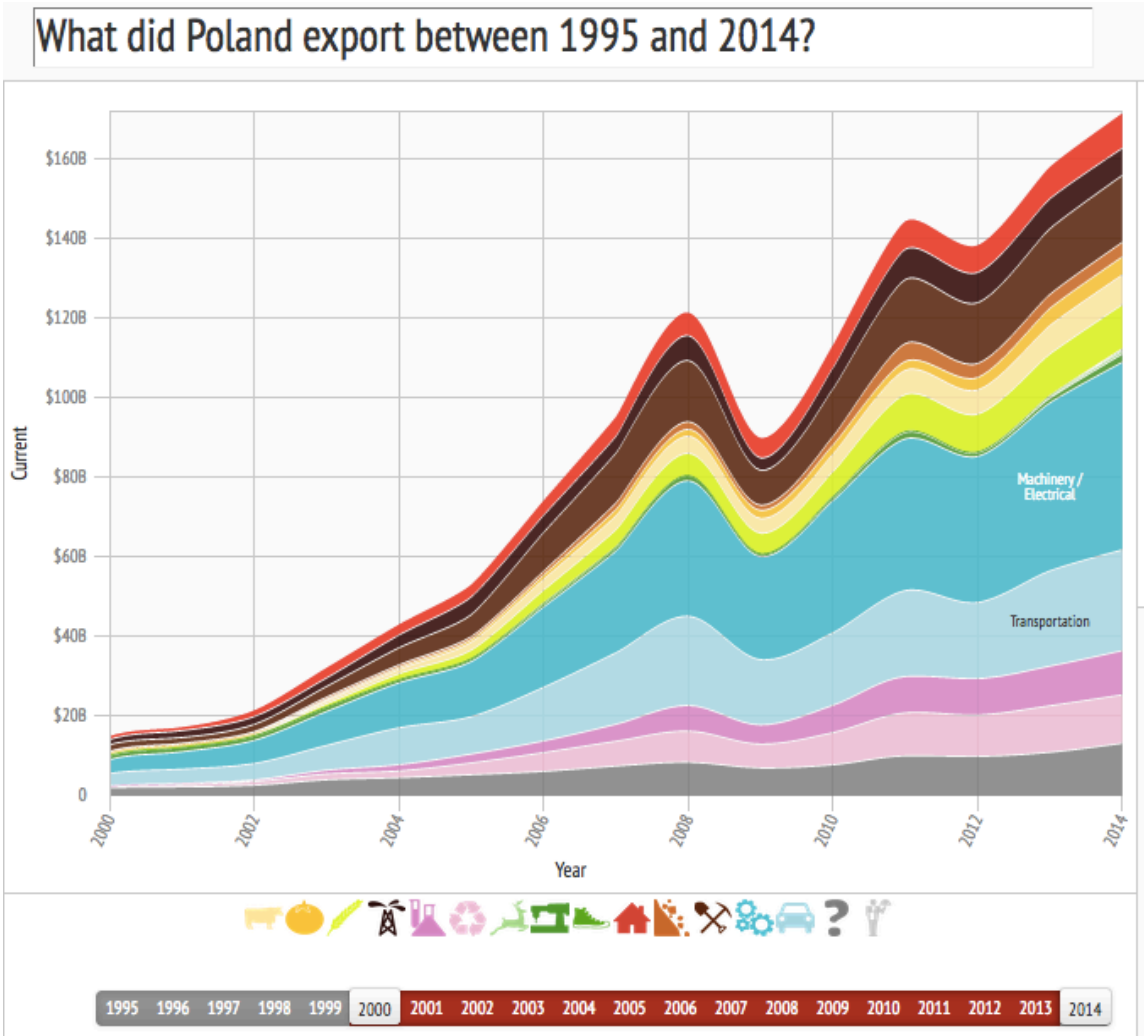
Figure 5: What did Romania export in 2014?



Source: MIT Atlas of Economic Complexity

Moreover, the export profile of the two countries looks remarkably similar over time as well, with both of them increasing the value and the share of complex exports dramatically and not necessarily at the expense of traditional exports of raw materials, foodstuffs and textiles.

Figure 6: Poland's and Romania's exports (1995-2014)


What did Poland export between 1995 and 2014?
$160B
$140B
$120B
$100B
$80B
$60B
$40B
$20B
0
Current
2000
2002
2004
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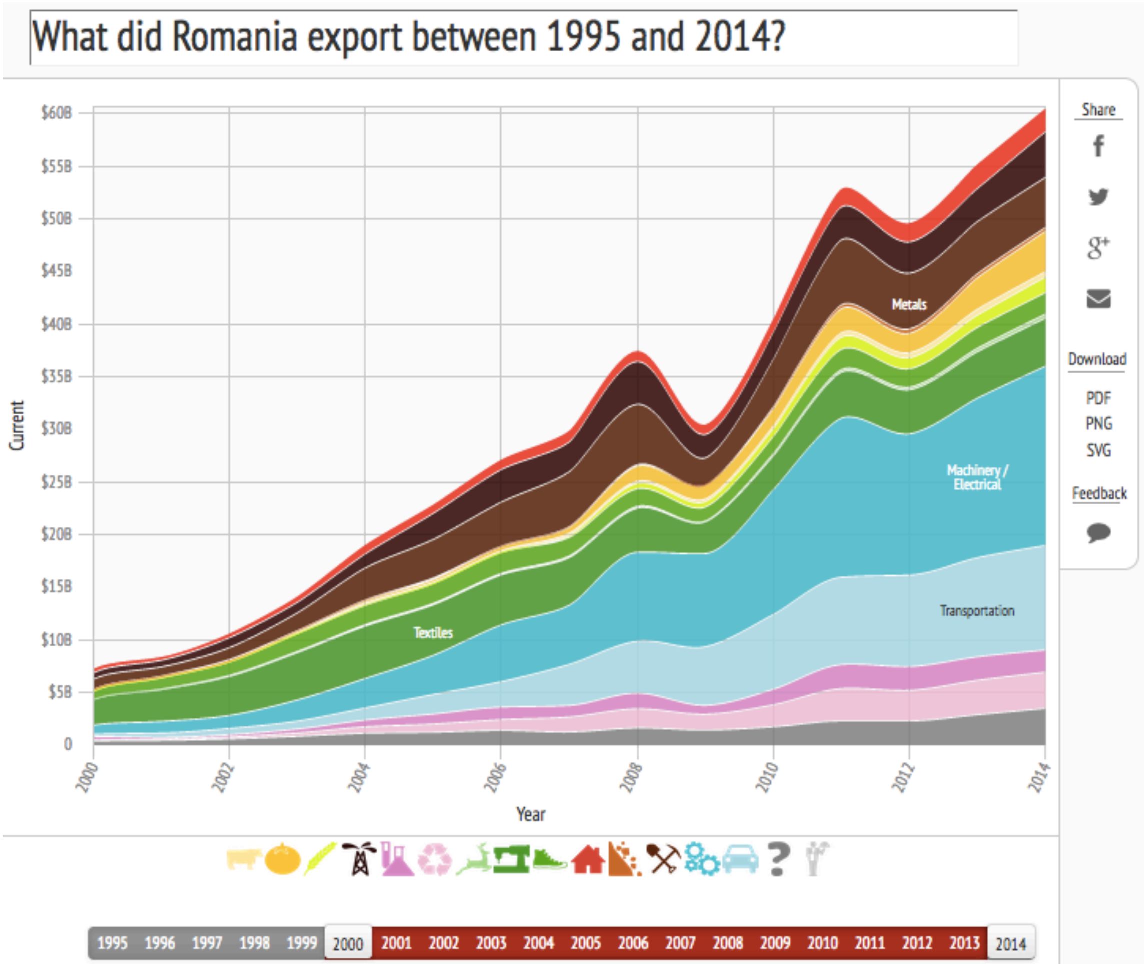
1995 1996 1997 1998 1999 2000 2001 2002 2003 2004 2005 2006 2007 2008 2009 2010 2011 2012 2013 2014



Source: MIT Atlas of Economic Complexity

Like in the other DMEs, a wide array of Western firms that are pivotal suppliers for the global car industry opened up large operations in Romania. When Renault announced that it would open a large research and development facility close to Bucharest and began hiring hundreds of engineers, many felt that the developmental shift from assembling Western products to designing and manufacturing them locally was within reach. Moreover, even in the midst of the crisis, a wide survey of hundreds of investors found that IT, telecom, energy and pharmaceuticals were expected to be the substantial contributors to future growth and that Romania was perceived in investor circles as a country whose emerging competitiveness clusters signaled a high likelihood of more high-tech development.[8]

The role of foreign capital should be further qualified by the fact that the state companies remain major contenders in some industrial sectors. Thirteen SOEs account for 20 percent of the turnover rate in the top 100 industrial firms and in terms of assets, six firms

[8] Ernst & Young, European Attractiveness Survey, 2012, http://www.ey.com/Publication/vwLUAssets/Attractiveness_2012_europe/$FILE/Attractiveness_2012_europe.pdf

from the top ten are state-owned, with one state company (Hidroelectrica) boasting assets worth 7 times more than the biggest multinational (Automobile Dacia Renault). In terms of net corporate profits, the Austrian-owned national oil company (Petrom) is followed by two state-owned energy companies, whose combined profits are almost as high as of the rest of companies in the top ten of Romanian corporations.[9] Finally, the most important two employers in the corporate sector are state-owned (mail and rail), with the national oil corporation owned by Austrian OMV and the internationally successful Dacia plant owned by Renault coming next. This situation is not unlike that of Poland (not to mention Slovenia).

Very much like Hungary or Slovakia a decade before, during the 2000s Romania offered manufacturing FDI a genuine "competition state" whose weak capacity in providing modern infrastructure on a par with its regional competitors was matched by its willingness to subsidize the internationalization of Romania's productive base through uncompetitive privatizations carried out at large discounts, tax breaks, subsidized energy or credit guarantees. State aid was coherently and competently managed and its terms were designed to target at multimillion dollar multinational investments with high multiplier effects and know-how trickle down. The biggest investments in the automotive sector (Renault, Ford, Delphi, Bosch, Draxlmaier, Honeywell, Pirelli), aircraft (Premium Aerotec), white goods (deLonghi), oil equipment (Lifkin), electronics (Nokia) and IT (IBM) were completed only following the granting of significant state subsidies.[10] State aid schemes were further institutionalized after during the crisis through several emergency decrees. [11]

Subsidies were important but the bulk of FDI-friendly interventions took place elsewhere. Rather than be carried out in the spirit of EU-advised competition, the privatization of utilities with West European capital offered instead opportunities for horizontal and vertical concentration (Haar and Marinescu 2011). Privatizations at discount prices were common. For example, the publicly-owned oil giant Petrom, the only east European oil company that sourced 75 percent of crude from domestic oil production, was sold in 2004 to Austrian-owned OMV at a woefully undervalued price.[12] The Romanian boom in renewable energy was fueled by government-issued "green certificates" [13] and many greenfield investments were carried out only following land grants and the public provision of utilities and transportation infrastructure. Energy sold cheaply by state-

[9] There is not a single firm owned by a private Romanian entity in top 10.
[10] Ministry of Finance, Lista agenţilor economici care au primit acorduri de finanţare emise de MFP în anul 2012 în temeiul H.G. nr.753/2008, până la data de 21 noiembrie 2012, http://www.mfinante.ro/listafinantare.html?pagina=domenii
[11] See H.G. 753, 1680 (in 2008) and 797 in 2012. Available at http://www.mfinante.ro/listafinantare.html?pagina=domenii
[12] The Romanian Intelligence Service informed the Parliament that the Romanian state lost nearly I billion dollars from the sale. SRI, Raport nr. 1255, December 8, 2007.
[13] Romania continues to be the world's 10th most attractive destination for investments in wind power according to global financial consultancy Ernst & Young (Ernst & Young Country Attractiveness Index 2013). See also "Winds of fortune blow through Romania" *Financial Times*, March 16, 2011.

owned hydropower and subsidized coal power stations benefited extensively foreign investments in energy-intensive industries like steel and aluminum.[14]

The post-Lehman crisis highlighted the limits of dependent industrial investment. Once removed, the vast net of perks with which FDI was attracted, multinationals confronted the Romanian government and society with a rude awakening to the reality of disloyal capital. A few high employment multinationals cut down their operations as a result of falling demand in Western Europe. Others (Finnish Nokia and Russian Mechel) simply used up the FDI incentives and then swiftly moved out to economies with even lower wages. In late 2012 foreign firms for whom subsidized power produced by state-owned hydro plants was a major reason for moving to Romania were considering moving out as well.[15] Moreover, the fiscal crisis of the state forced out revelations that the oligopoly of five Western European energy companies saved 250 million euro by not investing in the modernization of the power grid infrastructure they purchased with a discount in 2005-08,[16] often causing interruptions in the power supply.[17]

In short, during the past fifteen years Romania has acquired some of the defining feature of the industrial sectors of DMEs and has done so largely through FDI-focused industrial policy measures and failure to act on the dependent status of its innovation systems. As the next section shows, Romania follows the DME pattern in finance as well.

Dependent finance

If during the 2000s banks from the EU "core" banks made fortunes in Southern Europe largely through wholesale markets that boomed under the impetus of euro convergence (Gabor and Ban 2012), in Romania and Eastern Europe more generally they simply bought existing state-owned institutions. The results of the ensuing shopping spree were spectacular: the share of foreign-owned assets in total banking assets grew to 85 percent foreign ownership. While in 1998 five state-owned banks had 71 percent of banking assets, by 2008 the public banking sector had shrunk to 5.3 percent. Among the ten largest banks, only two (state-owned CEC and privately-owned Banca Transilvania) were domestic on the eve of the Lehman crisis. In contrast, in 2008 the subsidiaries of foreign banks had 89 percent of the market share. In the DME category, only the Czech Republic reported higher numbers.[18] As a result, over 80 percent of credit originates from the Eurozone.

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[14] "Romania May Have Given ArcelorMittal Unlawful State Aid" *Bloomberg News*, July 6, 2012, http://www.businessweek.com/news/2012-07-06/romania-may-have-given-arcelormittal-unlawful-state-aid-eu-says

[15] Interview with Doru Lionăchescu, consultant, Managing Partners, EvZ, http://www.evz.ro/detalii/stiri/2012-apogeul-crizei-Stlpii-economiei-prsesc-Romnia-1008417.html

[16] *Ziarul Financiar*, February 7, 2012. Available at http://www.zf.ro/companii/cel-mai-important-proces-pentru-stat-electrica-cere-la-paris-penalitati-de-250-mil-euro-de-la-cez-enel-si-e-on-10550057

[17] Investigation report undertaken by the Commission for the Privatization and Management of State Assets, no 816, May 31, 2010. On file with the author.

[18] UniCredit Group, CEE Banking-still the right bet, July 2008, www.bankaustria.at/en/index.html

The basic idea behind this transformation was that by selling their banks to brand names in Western banking the Eastern Europeans would shoot several rabbits with one shot: (a) break the links between government incumbents, state banks and state-owned enterprises responsible for cycles of non-performing loans, bank recapitalizations, and inflation (b) avoid the Russian and Ukrainian scenario in which local insiders would snap state banks for a song and build oligarchic business empires filled with bad politics (c) reduce the uncertainty of the EU membership negotiations by privileging buyers from the EU member state, (d) get a brand new off-the-shelf banking sector decked out with modern Western technologies and, most importantly, (d) address a decades old economic frustration of electorates-squeezed private consumption-by making consumer credit abundant and easy. Sensible people thought at the time that all this signaled international credibility, helped ease the Easterners from the EU waiting room into the boardroom and riveted the region's financial systems with powerful banks that were too big to fail at home.

Most importantly, however, this transformation supplied governments with a strong economic source of domestic legitimacy. Consumption levels depressed by restrictive macroeconomic policies of dubious benefit for the economy as a whole (Gabor 2012) recovered. From a paltry 5 billion euro in 1999, private debt went up to 200 billion euro in 2009. As a result, overall debt increased five times, from 10 billion in 2000 to nearly 50 billion in 2008. Since Lehman, the figure doubled, to nearly 100 billion in 2012.[19]

Dependent banking was a quick fix for the socio-political crisis of Romanian postcommunism, yet it failed to serve the Romanian economy well in the medium term. Foreign ownership in the financial industry blew a huge consumer and real estate credit bubble while making only a marginal contribution to industrial investment or the small and medium enterprise sector. As Gabor (2012: 101-105) shows, lending to the firms in 2008 was as high as in the 1994-1996 period, when the banking sector was domestic and predominately state-owned. Far from supporting the local small and medium entrepreneurs, the transnationalized Romanian banking sector had only 15 percent of this sector of the economy on its books. Moreover, while in 2000 industry received 56 percent of credit, by 2008 this share fell to 20 percent, outpaced by credit to households and the service sector. In contrast, in 2008 12 percent of credit was financing the construction sector.

As for MNCs, rather than get their finance from "local" banks, they brought their credit lines with them.[20] By 2008, cross-border intra-company loans reached almost 14 percent of overall credit to corporations (Gabor 2012: 101). Also, since easy credit benefited mostly an emerging middle class (about 20 percent of the population by most estimates) whose consumption patterns stressed imports, the local subsidiaries of foreign banks assembled together the main engine of the East European crisis: gaping current account deficits. Moreover, foreign banks funded a massive increase in construction expenditures by becoming the originators of a mortgage lending in euros and other "hard" currencies,

[19] Data supplied by the national Institute of Statistics (INS).
[20] Author interview with Sorin Mandrutescu, AmCham Romania, Bucharest, November 2012; interview with Andrei Radulescu, stock broker, December 2012.

owing to the importance that the favorable interest rate differential played in the profit strategies of the foreign-owned banking sector.[21]

The banking crisis of 2008-2009 and the collapsing confidence of international direct investment after 2008 sheared Romania's development model of its strengths. Indeed, while dependent development made Romania prone to FDI and portfolio investment booms on the upswing, it reversed them just as dramatically during the post-Lehman downswing. The result was a structural economic crisis that began as a banking crisis magnified by current account imbalances and followed by a dramatic cut of FDI inflows (Gabor 2010). Foreign banks that owned the financial sectors started to deleverage at home and considered pulling out to supply funds to mother banks hit by the Lehman crisis; the West European crisis depressed the optimism of foreign direct investors, leading them to abruptly cut investment flows to Romania; to boot, the countries where most Romanian remittances originated (Italy, Spain, Ireland) faced a dramatic surge in unemployment. With its coffers emptied by pro-cyclical tax cuts adopted before the crisis, the conservative government did not have ready resources to act countercyclically even in the unlikely ideological event that it wished to.

At this point the subsidiaries of foreign banks activated previously unexplored mechanisms of economic dependence that were bolstered by the EU and the IMF. First, in the fall of 2008 their treasury and currency desks actively orchestrated speculative attacks against the Romanian *Leu* (Gabor 2009; 2013). Second, in early 2009 that international banks reduced their cross-border loans to East European banks, with the greatest reductions affecting the most liquid of them (Slovakia and the Czech Republic), in a move that a BIS report termed as suggestive of the fact that "some parent banks may have temporarily used these markets to maintain liquidity at home" (Dubravko Mihalijek 2009, p. 4).

In relative terms, the reduction in cross-border banking flows as a percentage of GDP was about as big for ECE in 2008-2009 as it was for Asian countries in 1998-1999 (p.7). To alleviate the liquidity crunch, in 2009 central banks in Hungary, Poland and Romania tried to convince the ECB to broaden the list of eligible collateral for its monetary operations by including government bonds issued in local currency in exchange for haircuts to these non-euro government bonds. The ECB rejected the suggestions.[22] The panic of foreign banks who bought up local banks and now faced massive losses and the possibility of unbundling currency pegs was so great that 2008-9 many of them threatened to use the exist option, triggering fears that the ensuing capital outflow would shut down the economies of the region. The panic in early 2009 was so big that foreign banks were ready to overlook the fact that the Romanian lending market had a great potential: it was only worth around 40 per cent of GDP, whereas it's 150 per cent elsewhere in the region.[23]

[21] Author interview with Andrei Radulescu, Bucharest stock broker, December 2012
[22] "And justice for all: in emerging Europe," *Financial Times*, November 7, 2011.
[23] Interview with Vlad Muscalu, economist at ING Romania, *Financial Times*, February 13, 2012.

Third, in the specific conditions of the crisis of early 2009 the transnational banks constrained policy autonomy through joint international policy conditionality. This happened as the E.U. and the IMF intervened and orchestrated a massive bailout of the financial systems of Romania, Latvia, Hungary, Bosnia and Serbia. Ironically, it was in Vienna, the trigger of the Great Depression, where an agreement was signed in 2009 with banks, the European Central Bank, the European Commission, the EBRD, the IMF and the states in question sitting around the table. The core of the agreement was that West European banks committed to stay if ECE governments reiterated commitments to austerity and stabilizing the banks' balance sheets while the IMF and the E.U. put the corresponding bill (fiscal austerity, high interest rates, constraints on moRTRagees' rights, recapitalization I.M.F./E.U. loans deposited with the central bank) on the balance sheet of the states. It was no surprise then that as the West European sovereign debt crisis hit, another major vulnerability emerged: that foreign banks in Eastern Europe could become the transmission belts for the troubles of Western sovereigns. Following Greece's tailspin and Austria's downgrading in the spring of 2012, S&P turned Romanian bonds into junk status because the Romanian banking sector had too much Greek and Austrian financial capital.

The Vienna Agreement established a public-private international financial regime in which the IMF, the EU and the banks exercised a form of shared conditionality over the policy decisions of Romania, thus reinforcing the dependent status of its variety of capitalism. For the government, this meant reliable buyers of its bonds and a brake on the disorderly withdrawal of foreign banks. For the banks, it meant protection against the collapse in domestic demand made even more dramatic by the austerity included in the bailout package. It also meant protection against constraining regulatory interventions (Kudrna and Gabor 2012) and the attempts made by consumer organizations in 2010 to lend *erga omnis* value to court rulings finding abusive clauses in bank contracts. Claiming that hundreds of millions of euros a year would represent the value of their loses,[24] banks demanded and obtained IMF and central bank protection against Romanian courts.[25]

Fourth, the dependent status of Romanian capitalism has been further magnified by the workings of the sovereign-bank nexus afflicting the economies of Greece and Austria. Romania is exposed to Greek banks, who control of sixth of assets in the banking sector, with each crisis in Athens having the largest Europe-wide repercussions on the Bucharest stock of exchange.[26] Closer to home, in the summer of 2011 Greek subsidiaries in Romania used Emerging Europe interbank and swap markets to fund parent banks in

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[24] In 2013 the Romanian Banking Association (RBA), the financial sector lobby, estimated loses at 600 million euro a year in case new legislation allowed court rulings to have erga omnes power in cases where at issue were abusive contract clauses. *Ziarul Financiar*, November 21, 2012; http://www.zf.ro/banci-si-asigurari/ingrijorare-printre-bancheri-privind-intrarea-in-vigoare-a-codului-de-procedura-civila-arb-roaga-bnr-sa-intervina-pentru-ca-bancile-sa-nu-piarda-sute-de-milioane-de-euro-pe-an-10340113. The scale of these losses is most likely a huge exaggeration, precisely to stave off any action.

[25] The in-house report of the RBA explicitly acknowledged the role of the IMF and the central bank in limiting court jurisdiction and regulatory moves deriving from court jurisprudence. *Ziarul Financiar*, November 21, 2012.

[26] "CEE: Bearing the brunt of the storm," *Financial Times*, May 14, 2012.

Greece at the Romanian rate (6 percent), with rates in Greece being in the double digits. [27]

Under pressure from a downgrade and without adequately consulting with the Romanian government, in 2011 the Austrian government recommended-or exerted "moral suasion" as Vienna put it- that Austrian banks limit their exposure in emerging Europe by calling them to issue loans not in excess of 110 percent of the financing they raise locally. This sent shockwaves in Bucharest,[28] as according to Fitch Austrian banks own 31.5 percent of Romania's bank assets. Faced with such problems the Commission and the IMF were less successful at extracting Vienna 2.0, a commitment for Western banks to maintain their commitments in Romania and the rest of the region.[29] In response to Austrian and Greek troubles and despite the upbeat outlook on the economy, in November 2011 S&P downgraded Romania, a decision bolstered by the fact that foreign denominated debt exceeded 60 percent and foreign institutions owned 85 per cent of total banking sector assets. As Standard and Poors put it 'these subsidiaries are autonomous from their parents, which we believe will likely limit spillover effects if confidence in the Greek banking sector weakens further. In our view, however, there is a risk that if foreign parent banks run into difficulties they may significantly reduce cross-border exposure to their subsidiaries, thereby reducing credit activity." [30] The situation was potentially catastrophic. At the time Nomura estimated that foreign banks would suck 1.2 percent out of the Romanian GDP in the event of massive deleveraging, which was more than the total level of FDI in 2012.

So far the paper showed how dependent industrial investment made Romanian exports more complex, placing the economy squarely in the DME camp. Yet the crisis brought to the fore the limits of reliance on FDI while the other DME characteristic (dependent finance) armed the mechanisms of the Great Recession in Romania and acted as a transmission belt for the sovereign debt crisis of the European periphery. What is more, the DMEs reliance on foreign capital for establishing strong domestic innovation systems able to generate domestic high value added activities had modest results and eventually deepened the country's dependent development.

Innovation systems

Nolke and Vliegenhard argue that significant research and development (R and D) investments are not necessary in DME economies whose competitive advantage lies in the assembly of semistandardized goods. What matters is whether the economy has institutional complementarities that ensure profitability within MNCs with operations on

[27] "Honey, I shrunk Emerging Europe" *Financial Times*, November 4, 2011.
[28] Romanian President Traian Basescu told foreign banks "You have made huge profits and if you are now getting ready to leave Romania unfinanced during the crisis we will think it is an act lacking fair play towards Romania (…) I don't want to believe we will be left to pay the bills of banks' greed. There are European mechanisms. I urge you to use these mechanisms instead of choking the Romanian economy by reducing capital inflows." Cited by *Reuters*, November 24, 2011, http://uk.reuters.com/article/2011/11/24/idUKL5E7MO18J20111124
[29] Stefan Wagstyl, "Austria clarifies plan to curb eastward lending," *Financial Times*, January 17, 2012
[30] "Romania: Junked by S&P." Cited in *Financial Times*, November 29, 2011

the ground. In this perspective, the dynamics of domestic innovation capabilities is peripheral to the strategies of multinational capital. As such, dependent innovation systems represent an important development trap. Aside from a few industrial niches of excellence, Romania remains an assembly platform for innovations developed abroad and only Cyprus spends less on R and D. Indeed, to the extent that Romanian exports have become more complex and diversified, this had little to do with domestic R and D.

There has also been very little technological trickle down from FDI flows. As in the case of the DME countries, FDI was focused on the use of local labor and government incentives, leaving R&D operations elsewhere. What is worse, domestic capital is even less likely to invest in innovation. The result is that in Romania private sector's share of R and D spending is up to ten times smaller than in West European countries where manufacturing has a similar share of GDP (e.g. Austria or Sweden).

MNCs strategies did not foster much local innovation but what about the state? While state involvement in this regard has been key in economic success stories from the US to Korea, in Romania the state has actively dismantled the extensive research infrastructure inherited from the years of socialist developmentalism and dramatically cut R and D spending. This is hardly a Romanian characteristic. While average R & D spending per GDP reaches 2 percent in the EU (with highs of 4 percent in Sweden an Finland), in Romania it is around 0.5 %, a level similar to that of Poland and Slovakia, but half the level of Hungary and the Czech Republic.

Joining the EU altered this passive R and D policy and encouraged an increase in R and D spending. While the share of EU funds for R and D remained minuscule and the share of the private sector in the total R and D investment even declined between 2005 and 2009, the share of the government budget spent on FDI nearly doubled between 2005 and 2009, from 0.5 to 1 percent of the government budget.[31] Yet it was as a result of the EU-assisted austerity package adopted in 2010 that Romania became one of the three EU states that cut public R and D spending. The state worsened this outcome by refraining from using even those innovation policies that have been allowed by Brussels,[32] such as public acquisitions of innovation-rich products. The state also failed to foster institutional complementarities between academic research and industry that foster industrial applications and in the spring of 2013 it went as far as halving state funding for ongoing research projects selected based on international peer review and signaled that it would weaken meritocratic grant section mechanisms in place since 2010.[33]

Overall, Romania's potential to improve its innovation dossier remains limited. But this owes as much to the state's institutional and fiscal weakness as to the strategies of the private sector. While more than half of R&D in the EU is made by private firms, in

[31] *http://epp.eurostat.ec.europa.eu/portal/page/portal/science_technology_innovation/introduction*

[32] Steliana Sandu, Michael Dinges (2007): Monitoring and analysis of policies and publicfinancing instruments conducive to higher level of R&D investments. The "Policy Mix" Project: Country Review Romania, United Nations University, UNU-MERIT, March.

[33] Interview with Mihai Dima, chairman of the National Research Council, http://www.ziare.com/scoala/universitati/motivul-cheie-pentru-care-au-demisionat-in-bloc-cercetatorii-din-cncs-interviu-1229865

Romania this percentage is barely 23 percent, with most R&D still originating in the public sector. Alternative market-based sources of funding R and D are late in arriving. The Bucharest Stock of Exchange does not have the strength to promote equity finance or project finance on an adequate level.[34] Venture capital for start-ups is virtually non-existent[35] and, while improved government access to EU funds could address some of the shortfalls in public funding, progress has been elusive.

There are some important wrinkles in this story. During the past few years there emerged a few niches of excellence. This is the case of innovation clusters in the auto and the IT sector, both of which benefited from extensive state aid and income tax cuts and exemptions. In IT, industrial policy has been critical via income tax exceptions for the country's software programmers. In 2012 a new government began to budget for adequate finance for start-ups and the coordination of private sector and university research capabilities.[36] It took extreme duress exercised by the European Commission to convince the government to start considering phasing them out gradually in 2013. This has been a particularly sensitive matter as this sector ensures full employment and high wages.[37]

Although it accounts for an important part of exports and high-skill employment, it was only from 2004 onwards that the IT sector emerged as a homegrown industry and benefited from significant foreign capital inflows. Benefiting from a supply of large classes of computer engineers ensured by the country's public universities, this innovation-heavy sector has recently attracted the likes of Oracle, Google and Microsoft. In 2016, the IT sector accounted for 2.6 billion euro in exports (a threefold increase since 2012) and 98.000 employees in 2016.[38]

The other example is automotive research, a sector of strategic importance for the comparative advantage of all DMEs (Haiss et al 2009). Renault set of one of its biggest design centers in Bucharest and a testing and engineering platform in Titu and received extensive state financial support to this end.[39] Built with local firms, managed largely by Romanian managers and hiring thousands of engineers, Renault Technologie Roumanie (RTR) has design, testing and engineering platforms in three cities. This 450 million euro research center is the biggest of a major European carmaker outside the "old" EU and some of Renault's 2012 new models were designed to a great extent in Romania.[40] RTR hires engineering students after training and testing them in internships, with no less than

[34] Author interview with Vincenzo Calla, BNP Paribas, November 8, 2012.
[35] Author interview with Irina Anghel-Ionescu, European Venture Capital Association, December 16, 2012.
[36] Author interview with Sorin Mandrutescu, chairman of the American Chamber of Commerce, November 8, 2012
[37] *Ziarul Financiar*, November 19, 2012.
[38] ANIS, *Software & IT Services in Romania – 2016 Edition.*
[39] Renault Technologie Roumanie has design, testing and engineering platforms in three cities and received from the government 30 million in subsidies as well as government guarantees for a 100 million loan during the 2008-2011 period. *Capital*, Seotember 27, 2011, http://www.capital.ro/detalii-articole/stiri/renault-urmeaza-sa-primeasca-ultima-transa-de-ajutor-de-stat-pentru-centrul-de-la-titu-153620.html
[40] Renault Technologie Roumanie, www.renault-technologie-roumanie.com

700 young engineering students taking up this opportunity. The center received from the government 70 million in subsidies as well as government guarantees for a 100 million loan during the 2008-2011 period. In short, Romania assembles around 400,000 cars a year and is developing the capacity to design them.

Surely, Renault is not alone in this regard. Continental (tires and auto parts), Siemens (railway), Alcatel-Lucent (telecom and software), Intel (software), GlaxoSmithKline (pharma), Oracle (software), Continental (tires) and Ina Schaeffer (ball bearings) have also spent tens of millions of euros on new R and D centers and hired thousands of engineers there. Overall, however, these are the exceptions that confirm the rule and are part of an integrated innovation system that could enable the country to move faster up the value added ladder.

Vocational education

At the heart of the CME model lies the dual education system. In Germany, for example, for each high school graduate there is a vocational school graduate (Thelen and Busemeyer 2012). In Romania, the ratio is one vocational graduate per year to 4 high school graduates. While recent institutional reforms point in the direction of an aspiration towards the CME model in Romania, the reality of education and training points towards a clear DME pattern, with its looming crisis of skill reproduction. In order to reach the German ratio, Romania would have to double the number of vocational school graduates every year. The main cause of this situation is that the institutions that provide vocational education are not supported by adequate funding by either the government or the private sector. The results of a recent reform creating CME-style vocational education are yet to produce results.

During the 2000s the Romanian government established institutions that mandated and created incentives for continuous vocational education within the framework of collective bargaining. As a result, vocational training by firms became tax-exempt and firms were expected by the law to provide regular training to their staff. This regulatory environment was hardly evidence of an arms' length take of the government on workers' skills. Instead, it showed determination to constrain firms to invest in training. What is more, amendments to the labor code adopted in the mid 2000s demanded that employers and unions establish vocational education training boards and centers meant to address the actual needs of companies and workers and license the vocational training staff. As a result, the number of training programs increased fourfold in a single year. The all-encompassing national collective contract for 2007-2010 stipulated that vocational training was mandatory and enforceable.

Before the Great Recession it seemed that the government and social partners were moving towards more coordination, although good intentions were not matched with adequate funding for covering the retraining of the unemployed. The moves towards more coordination were terminated by the structural reforms adopted in the aftermath of the crisis. At the request of an alliance of organized SMEs and multinational capital, supported by the IMF, national collective bargaining and the panoply of continuous vocational education institutions that came with it were terminated. Like its neo corporatism, Romania's continuous vocational education was largely a story of fleeting gains.

Vocational education for new workers has an more marked DME face. The skill revolution carried out by socialism proved to be a major asset for East European economies under capitalism and Romania was no exception. One of the legacies of socialist developmentalism in this country was a dual education system attached to specific industries (Ban 2012). But after 1989 budget cutbacks, poor reform designs and, most importantly, the halving of industrial labor was tantamount to vocational schools with obsolete equipment, a decimated staff and the transformation of these educational institutions into sites of social stigma.

Faced with this situation, governments embraced the then conventional wisdom about the obsolescence of vocational education. A 2003 reform extended the vocational school time to five years (a year longer than in regular high schools) and stressed the study of theoretical disciplines required by the high school graduation exam (*bacalaureat*). To boot, practical skill cultivation was squeezed from 2 days a week to a few hours. Despite complaining about the shrinking pool of skilled blue-collar workers as a result of mass migration (Ban 2012),[41] the private sector was late to mobilize to demand changes. Moreover, no longer did vocational school students face restrictions to take the *bacalaureat* and university entrance exams. As a result, vocational school ended up providing de facto general education within a time frame judged necessary for the academically challenged to take the *bacalaureat.* The denouement was inevitable: enrollment dropped dramatically and only a third of the students managed to graduate. In acknowledgement of system failure, the government dismantled vocational schools altogether in 2009. The result of these transformations was skill mismatch and the massive de-skilling of precisely the range of workers where Romania's comparative advantage was at its highest: mid-level manufacturing. [42]

The Great Recession seems to have triggered a reevaluation of vocational education, however. Nolke and Vliegenthart argue that foreign investors do not have incentives to demand training investments from the state, as the labor they use needs a very modest level of skills. This is not my finding in the case if Romania. Faced with skilled labor shortages, main organizations of foreign capital (AmCham and the Foreign Investors' Council) made the reintroduction of vocational education their main priority. [43] Their

[41] Elvira Şeptelean "Romanian Vocational System: A New Beginning/Invatamantul professional din Romania: Un nou inceput" The Romanian Teachers' Association, August 8, 2012, http://www.asociatia-profesorilor.ro/invatamantul-profesional-din-romania-un-nou-inceput.html; author interview with Florin Pogonaru, president of AOAR, one of the most dynamic employer associations, July 9 2006.

[42] Mary Canning, Martin Godfrey, Dorota Holzer-Zelazewska, "Vocational Education in the New EU Member States," World Bank paper no 116; J.Mitra, "Entrepreneurial and vocational education and training: Lessons from Eastern and Central Europe," *Industry and Higher Education, Volume* 18, Number 1, 1 February 2004 , pp. 53-61(9)

[43] Author interview with Sorin Mandrutescu, Chairman of AmCham Romania, November 8, 2012; American Chamber of Commerce, *Priorities for Romania*, Bucharest, 2012. www.amcham.ro/UserFiles/.../Priorities_EN_FINAL_10251300.pdf; press release by Continental Timisoara, tp://www.conti-online.com/generator/www/ro/ro/continental/pressportal/themes/press_releases/1_topics/others/pr_2012_09

move was successful and in 2012 vocational education was reintroduced, with the German model inspiring the new law and German multinationals spearheading the transformation. By law, employers now play a key role in deciding the number of seats, student training and then employment for this two-year educational system. Indeed, the number of seats is to be determined based on employers' needs and students sign contracts with specific firms. Most of the curriculum is practical and does not allow sitting for the *bacalaureat.* Vocational students can take the *bacalaureat* only if they decide to transfer to a high school. To incentivize attendance, a special chapter in the budget was earmarked for scholarships to all vocational school students. That said, funding for vocational education remains minimal and employers are not keen to chip in with their own financial resources. [44]

The 2012 reform looks promising. 13,000 students enrolled in 473 vocational schools and, reflecting the overall structure of labor demand, in the fall of 2012 most seats were in manufacturing-relevant skills. [45] In the same year engineering departments in universities enrolled 130,000 students, with 10,000 in IT alone. Foreign firms in some economic clusters such as Brasov and Timisoara, both dominated by German manufacturing capital, established their own vocational schools, with students also receiving a scholarship from the firms involved on top of the one received from the government.[46] Today, the multinational sector began to emphasize vocational education and continues to push towards an even deeper involvement of corporations in training. In 2012, the influential AmCham suggested amendments to existing legislation by suggesting that employer organizations send visiting teachers in schools, the introduction of IT education beginning with the kindergarten level, universal access to computers in all schools, mandatory training sessions in firms on a yearly basis, different rules for research and teaching colleges.[47]

Industrial relations

Once a heartland of postcommunist labor militancy and then budding neo-corporatism, during the Great Recession industrial relations in Romania have reinforced the institutional complementarity specific to both DMEs and LMEs: mid-level regulation and predominantly firm-level collective bargaining (Guga and Adascalitei 2015). Indeed, it took the extreme economic and political circumstances provided by the Great Recession for an emerging alliance between state and organized multinational capital to bring Romanian industrial relations in line with the least common denominator of its regional competitors.

_17_scoala_profesionala_ro.html; Foreign Investors' Council, *Investing in Romania-White Book*, October 2012.

[44] http://taraluiandrei.ro/files/2016/Raport%20IPT_11nov.pdf

[45] Interview with Gabriela Liliana Ciobanu, director of the National Center for the Development of Vocational and Technical Education, http://www.scoalaedu.ro/news/684/60/Un-nou-tip-de-invatamant-profesional-fara-someri

[46] "German vocational school prepares students for foreign firms" *Income Magazine,* September 17, 2012,

[47] AmCham Romania, "AmCham Comments on the National Strategy for Education and Research in the Knowledge Society" www.amcham.ro

Since the adoption in 2003 of pro-worker labor legislation (Trif 2008), neoliberal politicians and domestic small businesses organizations have reinforced the liberalizing demands of the IMF, the World Bank and multinational capital's organizations (Federation of Foreign Investors and American Chamber of Commerce). Opposing this position were all labor union confederations, some employer associations and the more left-leaning wing of the Social-Democratic Party, under whose government the pro-worker legislation had been adopted.

Before 2011, labor market deregulation had become part of IMF conditionality. In 2004 the Fund demanded that a World Bank-approved international expert draft the new code and asked the government to adopt the new code as part of the Fund's stand-by agreement with Romania. The advent of a neoliberal government in 2005 strengthened this pro-deregulation coalition. Consequently, during its first month in office the new government announced that it would adopt the World Bank-drafted legislation.

Yet the coordinated action of labor unions, their capacity to mobilize external support from West European unions and particularly the credibility of union threats ensured by the memory of extensive labor militancy during the 1990s (Munteanu 2003) made the government adopt a much more moderate labor reform in 2006, with union consent (Pilat 2008). The mass migration of the labor force in EU member states in the late 2000s and the subsequent drying up of excess labor further weakened the case for the kind of "big bang" deregulation that the liberal coalition of domestic and external interests wanted.[48]

In their brief analysis of Romania and Bulgaria during the crisis, Bohle and Greskovits (2012: 252) argue that in contrast to the Baltic countries, during the post-Lehman crisis the governments of these two states were "drifting and inconsequential in their policy responses and have been frequently challenged by massive protests waves."

At least when it comes to industrial relations in Romania this claim needs updating. For despite labor protests and, at least initially, the protestations of the biggest domestic employer organizations, in 2011 the conservative government of Emil Boc used an emergency procedure in the Parliament to undertake a radical deregulation of Romanian industrial relations.[49] Collective bargaining legislation was drastically changed: national level bargaining was eliminated, labor-capital relations are now limited largely to the firm level, union representatives lost their protections, firing became easy and temporary contracts and work conditions were freed from union intervention procedures. A new left-of-center government elected in November 2012 on a wave of popular resentment against austerity and structural reforms has offered no evidence that the 2011 labor reforms stand to be reversed, thus locking Romania in the DME model on this front as well.

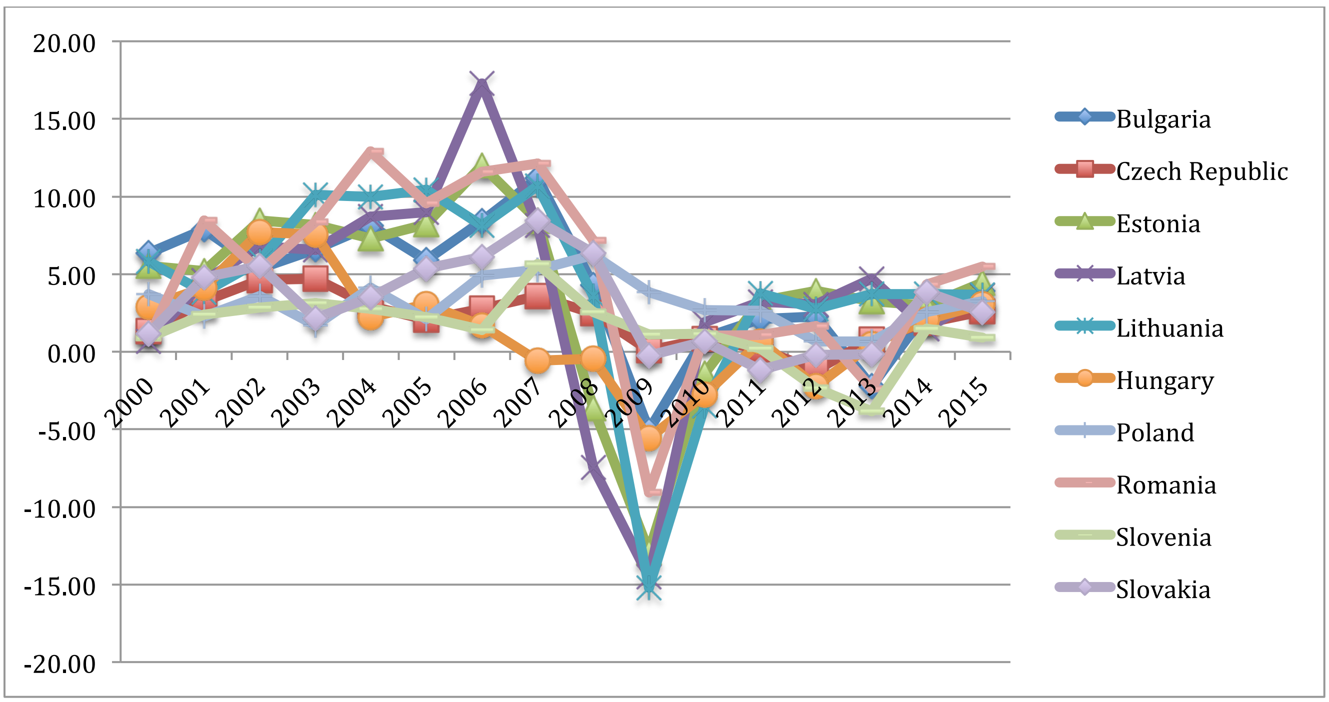
Dependent development and convergence

[48] Author interview with Florin Pogonaru, chairman of employer organization AOAR, June 12, 2006
[49] Author interview with Bogdan Hossu, chairman of "Cartel Alfa" Labor Union Confederation, December 16, 2012.

It is beyond the scope of this paper to do a comparative analysis of the drivers of growth in this country once dependent capitalism became embedded. However, several descriptive and broad evaluations are in order regarding aggregate performance on output and labor. F

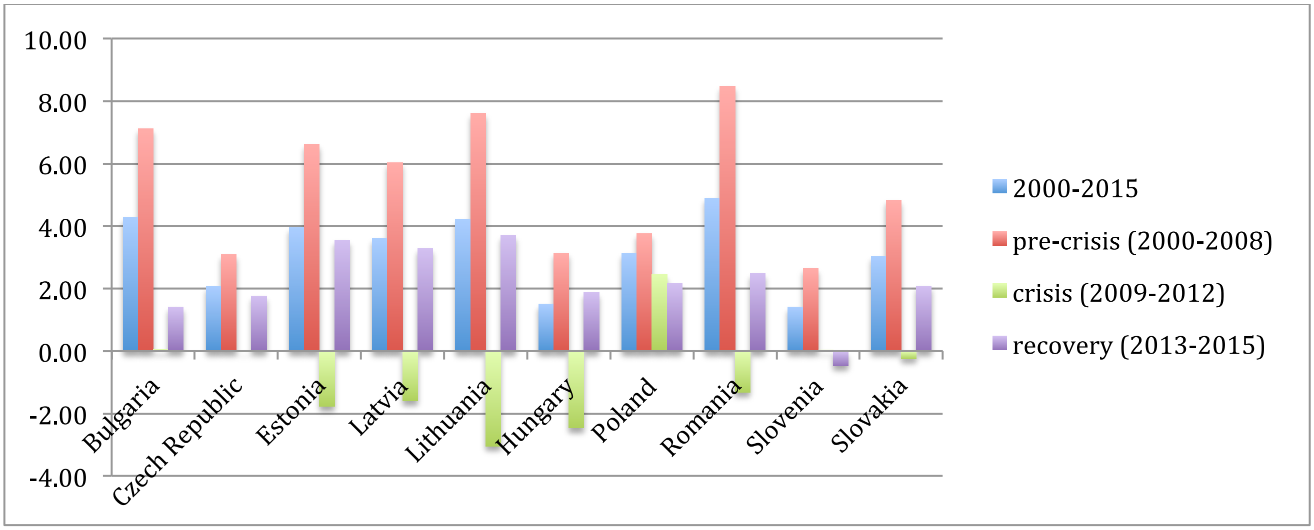
Regarding output, as the figures below show, outside of the exceptional circumstances of the crisis, Romania had the highest growth rate in the region for the entire 2000-2008 period and before the crisis and has had the strongest recovery after the Baltics since recovery began in Europe in 2013. From this standpoint, its characterization as a laggard is outdated. According to the IMF, the strong recovery since 2013 can be linked to Keynesian-style demand side policies such as the reversal of austerity and several rounds of minimum wage increases in an economy where a third of the employed population lives in minimum wage.

Figure 7: Annual GDP growth rates in ECE



Source: Eurostat

Figure 7: Average growth rate per cycle



Source: Eurostat and author's calculations

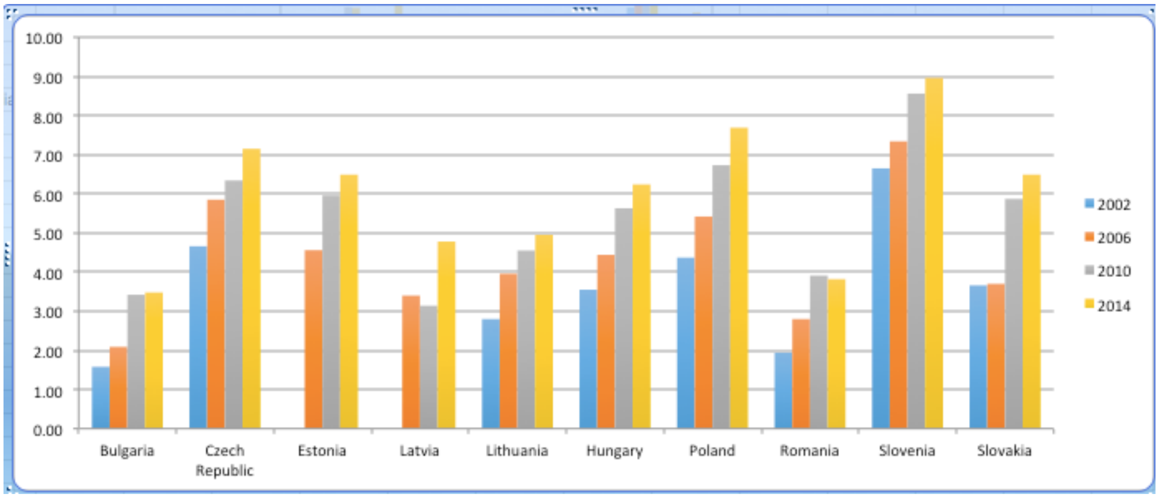
Indeed, as the table shows that even with the harsh austerity of 2010, Romania has had the largest increase in household consumption between 2000 and 2015. That said, wages in industry began to lag since 2010, in marked contrast to other ECE countries. Had it not been for governments trying to close the gap between the median and the minimum gap in what can be termed a wage-led recovery strategy, the situation would have been even more dire. This suggests that consumption increases cannot be traced directly to better remuneration by the most internationally competitive part of thee economy and that the cost of performance is paid by waged labor.

Table 1: Actual individual final consumption of households at 2010 prices

Actual individual final consumption of households at 2010 prices (OCTH)										
	Bulgaria	Czech Repu	Estonia	Latvia	Lithuania	Hungary	Poland	Romania	Slovenia	Slovakia
	Billion BGN	Billion CZK	Billion EUR	Billion EUR	Billion EUR	Billion HUF	Billion PLN	Billion RON	Billion EUR	Billion EUR
1999	30.28	1775.78	6.16	8.95	13.38	14195.93	697.87	203.02	19.11	29.52
2000	32.21	1799.37	6.50	9.01	14.16	14608.58	723.67	204.83	19.28	29.87
2001	34.75	1858.19	6.84	9.42	14.71	15214.48	740.17	222.14	19.74	31.30
2002	36.61	1943.79	7.42	10.06	15.57	16389.87	766.90	233.71	20.30	33.03
2003	39.02	2035.51	8.02	10.72	17.14	17625.46	779.82	253.28	20.94	33.74
2004	42.20	2094.98	8.61	11.66	18.86	18019.51	812.17	285.95	21.52	34.92
2005	44.69	2138.10	9.31	12.71	20.83	18568.95	829.24	313.35	21.99	36.80
2006	48.45	2197.53	10.43	14.91	22.52	18886.90	869.90	349.66	22.30	39.05
2007	53.87	2276.79	11.32	16.12	24.93	18780.02	915.79	392.10	23.57	42.36
2008	56.19	2333.74	10.91	14.92	25.83	18699.58	972.83	420.24	24.17	45.06
2009	53.35	2335.44	9.50	12.75	21.90	17660.73	1010.19	382.16	24.44	44.94
2010	53.83	2355.05	9.37	12.99	21.14	17172.20	1037.44	386.13	24.72	45.24
2011	54.98	2359.32	9.67	13.41	21.93	17289.18	1064.88	390.33	24.77	44.71
2012	56.22	2331.63	10.05	13.82	22.54	16906.97	1071.89	396.83	24.19	44.62
2013	54.97	2350.49	10.38	14.47	23.38	16993.75	1078.93	387.31	23.27	44.56
2014	56.37	2394.73	10.69	14.69	24.25	17343.43	1106.77	404.17	23.62	46.27
2015	58.58	2457.31	11.16	15.22	25.14	17877.26	1142.73	426.36	23.83	47.46

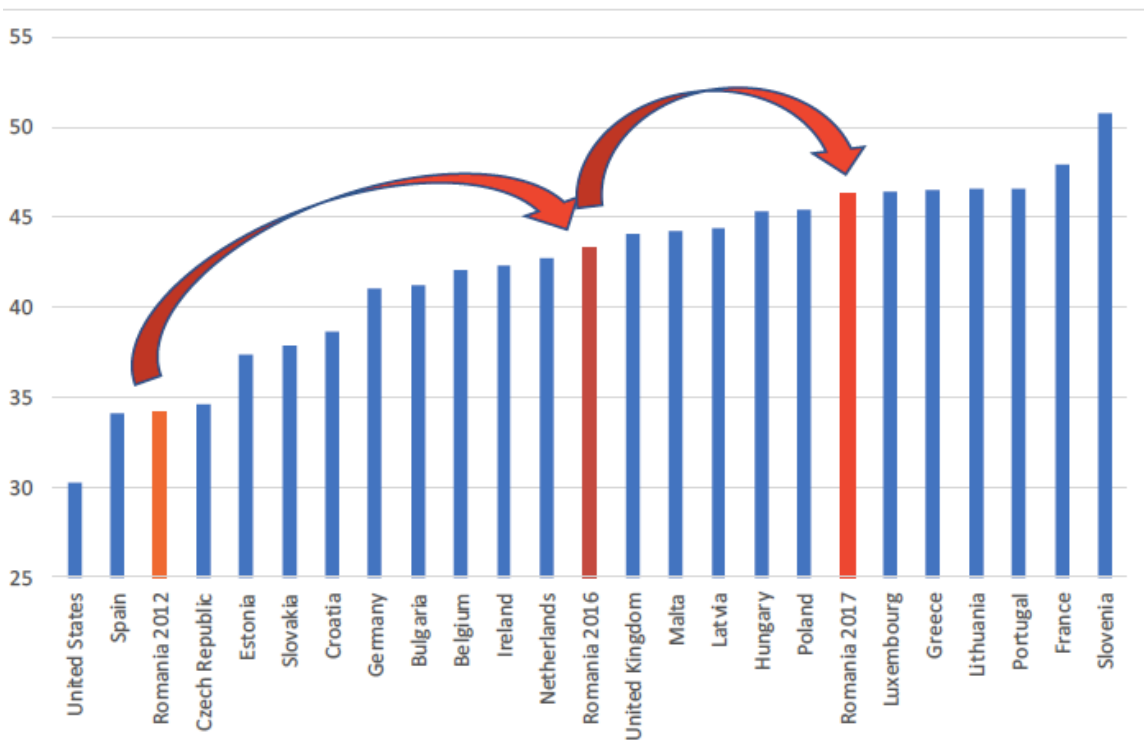
Source: AMECO

Figure 8: Mean earnings in PPP (industry, construction and services)



Source: Eurostat

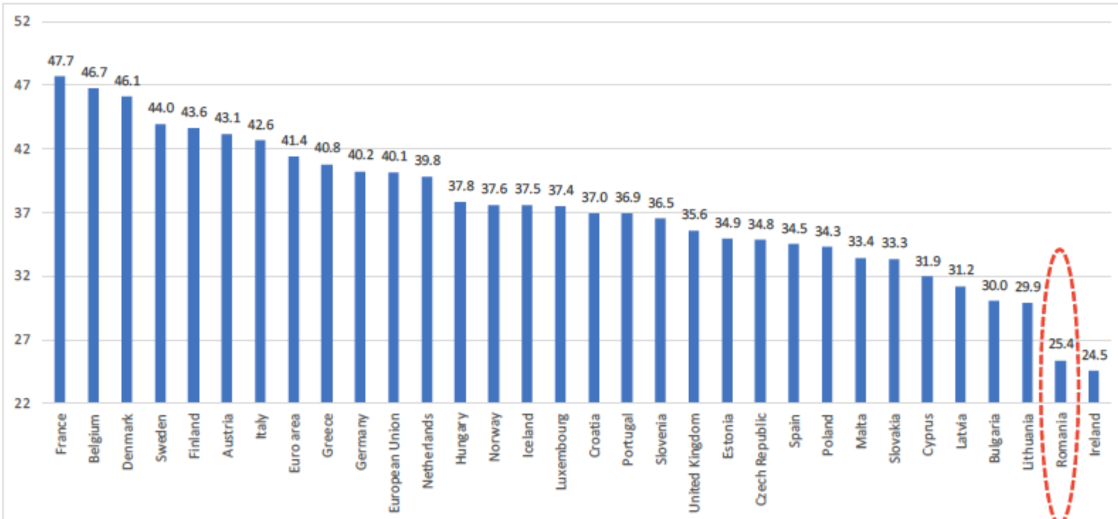
Figure 9: Minimum–median wage gap



Source: Romanian Fiscal Council

Much of the analysis presented in the paper suggests that considerable fiscal resources are needed to boost research and development, skills and infrastructure. However, as the figure below shows, Romania's fiscal state is one of Europe's most emaciated ones, with no prospects of improvement lying ahead, a situation that stands to reinforce the country's dependent development dynamics.

Figure 10: Government revenue as share of GDP (2017 estimate)



Source: Romanian Fiscal Council

Conclusions

This paper suggests that there is overwhelming evidence to argue that Romanian capitalism has converged with the dependent market economy model detected by scholars in East-Central Europe. Like Poland, Czech Republic, Poland and Slovakia, Romania has an economy dependent on FDI and financial flows that demands a higher degree of state-business coordination while excluding labor. These movements of capital made possible its economic boom during the 2000s, caused sharp increases in productivity and export complexity, slowed down the pace of deindustrialization and carved out niches of industrial excellence. At the cost of modest wage increases in relative terms, this dependent development nevertheless delivered high, albeit volatile output performance, export growth and increasing export complexity.

Like DME economies and in contrast to the Baltics' radical skepticism about industrial policy, Romanian governments adopted FDI-oriented industrial policies targeted at higher value added industrial niches. But Romania also replicated the other face of the DME model: a financial system largely divorced from the export industries, poor domestic innovation capabilities and has only of late began to reconsider its approach to vocational training. Similarly, alliances between state and foreign capital removed peak level collective bargaining and a pro-worker labor code, two institutional pillars that had made Romania less rather than more DME-like.

Yet the paper's findings reach beyond the case of Romania by tracking down mechanisms of dependence that do not appear in existing research and by qualifying some of its insights. Underexplored forms of dependence can be found in the banking sector, where Daniela Gabor's remark that Romania is a "dependent financialized economy" is both apt and potentially applicable to other DMEs (Gabor 2012). When the crisis struck, the subsidiaries of foreign banks that controlled the financial sector had both the incentives and the capacity to execute a run on the Romanian currency. Moreover, they threatened to help their "mother banks," draining a large part of the country's money supply. In exchange for these banks' maintaining their exposure, the Romanian government accepted an international public-private crisis resolution regime managed by the IMF and the EU that co-opted the banks in the mechanisms of policy surveillance. In this way, foreign banks added a new layer of dependence than the ones identified in the literature. At the same time, the same public-private international regime successfully protected the subsidiaries of foreign banks against domestic regulatory interventions and consumer group campaigns. Constrained by an internationally monitored fiscal consolidation package, with its money supply sold to transnational banks periodically shattered by sovereign debt downgrades in their states of origin and faced with a massive collapse of FDI, Romanian governments had dwindling resources to make domestic capitalism less dependent even if they had the capacity and the ideological proclivity to do so.

The argument that MNCs have no incentives to invest in local innovation systems is supported by evidence overall but it needs to be qualified by an analysis of the automotive and IT sector. Similarly, the lack of interest of MNCs in vocational education posited in the literature appears challenged by the case of Romania. The paper's findings suggest that labor shortages in a low-wage but increasingly complex export-oriented industry spurred MNCs to invest resources in vocational education reform. Given the emergence of such shortages in the other aging societies from the region, this development may become a new DME feature.

In a broader sense, the paper's findings may contribute to ongoing debates on the divide between neo-developmental and liberal economic models. Unlike in the case of open economy neo-developmental states like Brazil (Ban 2012), in Romania's dependent capitalism the state has an uneven capacity to create synergies between FDI, national development goals and the competitiveness of domestic capital. This finding bolsters Greskovits and Bohle's emphasis on the critical importance of state weakness in Romania's capitalist system. This is particularly challenging considering that that pure cost competitiveness is not enough when countries approach the technological frontier, a critical juncture when endogenous sources of innovation should replace imported productivity gains.

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