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Liviu Voinea

Protective Structures in Romania

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About

Shortly after the end of the Kosovo war, the last of the Yugoslav dissolution wars, the Balkan Reconstruction Observatory was set up jointly by the Hellenic Observatory, the Centre for the Study of Global Governance, both institutes at the London School of Economics (LSE), and the Vienna Institute for International Economic Studies (wiiw). A brainstorming meeting on Reconstruction and Regional Co-operation in the Balkans was held in Vouliagmeni on 8-10 July 1999, covering the issues of security, democratisation, economic reconstruction and the role of civil society. It was attended by academics and policy makers from all the countries in the region, from a number of EU countries, from the European Commission, the USA and Russia. Based on ideas and discussions generated at this meeting, a policy paper on Balkan Reconstruction and European Integration was the product of a collaborative effort by the two LSE institutes and the wiiw. The paper was presented at a follow-up meeting on Reconstruction and Integration in Southeast Europe in Vienna on 12-13 November 1999, which focused on the economic aspects of the process of reconstruction in the Balkans. It is this policy paper that became the very first Working Paper of the wiiw Balkan Observatory Working Papers series. The Working Papers are published online at www.balkan-observatory.net, the internet portal of the wiiw Balkan Observatory. It is a portal for research and communication in relation to economic developments in Southeast Europe maintained by the wiiw since 1999. Since 2000 it also serves as a forum for the Global Development Network Southeast Europe (GDN-SEE) project, which is based on an initiative by The World Bank with financial support from the Austrian Ministry of Finance and the Oesterreichische Nationalbank. The purpose of the GDN-SEE project is the creation of research networks throughout Southeast Europe in order to enhance the economic research capacity in Southeast Europe, to build new research capacities by mobilising young researchers, to promote knowledge transfer into the region, to facilitate networking between researchers within the region, and to assist in securing knowledge transfer from researchers to policy makers. The wiiw Balkan Observatory Working Papers series is one way to achieve these objectives.

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Measuring Costs of Protection

This study has been developed in the framework of the Jubiläumsfondsprojekt Nr. 9957: Measuring the Costs of Protection in the Southeast European Countries.

The objective of the project was to analyse quantitatively the costs of current protection in the Southeast European region or, to put it the other way around, to assess the potential benefits of liberalisation in the Balkans. In this way, the study was designed to be able to estimate the intra-regional gains and losses from breaking up fragmented structures and to show the policy implications that arise from this for each of the Balkan countries and the EU in the light of bilateral free trade agreements.

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Liviu Voinea

Protective Structures in Romania

I NON-TARIFF TRADE BARRIERS IN ROMANIA

Romania has a recent history of trade liberalization that went fast and very far. Romania signed the EU Association Agreement in 1993, became founding member of the WTO in 1995 and joined the CEFTA in 1997. With the fast erosion of its tariff protectionism, Romania had only a limited recourse to non-tariff barriers in the form of quantitative restrictions.

Quotas secure a certain degree of protection to local producers irrespective of market conditions. They are currently used only for agricultural products and produces. If we proxy the incidence of NTBs by the share of products subject to quotas to total imports, then this coverage ratio is below 3% for Romania's imports from the EU.

Import licensing is used for health, environment and safety reasons, while automatic licensing is used for petroleum, wheat and flour and used goods.

In the food, drink and tobacco sectors in Romania, the incidence of non-tariff measures is dominated by product characteristics requirements to protect health and by non-automatic licence. According to OECD (2001), in 2001 there were a total number of 1708 non-tariff measures in the above mentioned sectors (at 6 digit levels tariff lines), of which: 7 tariff quotas, 317 non-automatic licences, 22 authorizations for animal health protection, 19 authorization to prevent drug abuse, 801 product characteristics requirements to protect animal health, 523 product characteristics requirements to protect plant health, 19 product characteristics requirements to prevent drug abuse.

These products requirements are in line with the international standards, as Romania is member of the following international standards organizations: Codex Alimentarius, IPPC, OIE, ISO.

There are only two recent cases recorded by WTO in which Romania was accused on introducing specific NTBs: a case of minimum import prices, filed by the United States, and a case of import prohibition based on quality requirements.

- The US requested consultations in 2000, following the 'arbitrary' establishment by Romania of minimum and maximum import prices for meat, eggs, fruits and vegetables, clothing, footwear and certain distilled spirits. Romania was also accused of having introduced burdensome procedures for investigating import prices when the

CIF value falls below the minimum import price. Romania and US notified the WTO's Dispute Settlement Body that they had reached a mutually satisfactory solution in 2001.

- Hungary requested consultations in 2001, and later on that year even the establishment of a panel, accusing that a joint decree of the Ministry of Agriculture, Food Industry and Forestry, Ministry of Family and Health and the National Consumer Protection Authority prohibited the import of wheat and wheat flour which does not meet certain quality requirements, while the domestic products were not subject of the same quality requirements. Hungary withdrew its request for the establishment of a panel in January 2002.

1 Quantitative restrictions

1.1 Import licensing

Goods	Authorities in charge with the import licensing procedures
A. Goods subject to import control	
• wastes that could be recycled, subject to conditional import	Ministry of Water and Environment Protection, Ministry of Health and Family, Ministry of Industry and Resources
• goods that may endanger people's health and the environment: - vitamins, hormones, antibiotics, other organic products - pharmaceutical products - essential oils, cosmetic products - soap and washing products - insecticides, fungicides, herbicides	Ministry of Health and Family or Ministry of Agriculture, Food and Forestry
• essential chemical substances and their precursors, in order to prevent them from being deterred from their licit use	Ministry of Internal Affairs and Ministry of Health and Family or Ministry of Industry and Resources
• gases with irritating, suffocating or paralyzing effect, intended for self defence	Ministry of Internal Affairs
• hunting guns, guns with neutralizing gases, guns for decoration, compressed air guns, guns' components and similar devices	Ministry of Internal Affairs
• radioactive materials and nuclear installation	National Commission for the Control of Nuclear Activities
B. Goods subject to contingents, excepted or exempted from custom duties, in accordance with decisions of the Romanian Government (see below the list of contingents with various commercial partners)	
C. Goods subject to automatic licensing	
• petroleum and derivative products	Ministry of Industry and Resources
• used goods	
• wheat and flour	Ministry of Agriculture, Food and Forestry
• birds' eggs	

1.2 Licences for specific operations

Operations	Authorities in charge with the licensing procedure
• commercial activities in the framework of clearing, barter and cooperation agreements	Ministry of Public Finances
• debt recovery through imported goods	Ministry of Public Finances
• imports financed through foreign loans granted by foreign governments or by international financial organizations	Ministry of Public Finances

1.3 Contingents

A. List of contingents with EU

	Tariff position HS classification	Product/group of products	Contingent (tones) 01.01.-31.12.2004	Tariff rate applied %	Maximum limit of allocation %
1.	0201, 0202	Beef (bovines) meat	4000, of which: 3200-traditional importers 800-new comers	0	 0.65 2.5
2.	02061095, 02062991, 021020, 02109951	Beef (bovines) fillet	100, of which: 80-traditional importers 20-new comers	0	 25.0 100.0
3.	0207	Poultry	4050, of which: 2050 – between 1.01/30.06, of which: 1650-traditional importers 400-new comers 2000 – between 1.07/31.12, of which: 1600-traditional importers 400-new comers	0	1.22 5.0 1.25 5.0
4.	04021019, 04022111, 04022119, 04022191	Powder milk	1500	15 18.8 18.8	1.34
5.	040510, 040590	Butter	1900, of which: 1600-traditional importers 300-new comers	18.8	 1.25 6.7
6.	0406	Cheese, different sorts of	2700	0	0.75
7.	07019050, 07019090	Potatoes	20000	18.8	0.3
8.	10019091, 10019099	Wheat	125000	0	4.0
9.	10020000	Rye	30000	18.8	2.0

10.	10030010	Barley (seeds)	1118	18.8	3.0
11.	10030090	Barley (others)	55882	18.8	5.0
12.	100510	Maize (seeds)	1000	0	4.0
13.	10059000	Maize (other)	49000	0	1.64
14.	1006, 11023000, 11031950, 11032050	Rice, rice flour, and products thereof	10000	0	0.5
15.	1101, 110311, 11032060	Wheat flour	3000	0	1.1
16.	1107	Malt	10000	0	0.5
17.	151710	Margarine	1000	18.75	2.0
18.	16023111, 16023119, 16023130, 16023190, 16023211, 16023219, 16023230, 16023290, 16023921, 16023929, 16023940, 16023980	Prepared or canned chicken meat	675, of which: 350- between 01.01/30.06, of which: 270-traditional importers 80-new comers 325-between 01.07/31.12, of which: 260-traditional importers 65-new comers	0	7.45 25.00 7.70 30.78
19.	160250	Prepared beef (bovines) meat	500, of which: 400-traditional importers 100-new comers	0	5.0 20.0
20.	170111, 170112, 170199	Sugar	20000, of which: 18000-traditional importers 2000-new comers	18.8	1.12 10.0
21.	17019910	Sugar	15000, of which: 14000-traditional importers 1000-new comers	45	1.43 20.0
22.	18063210, 18069019, 18069031, 18069039, 18069050, 18069060, 18069070, 18069090	Chocolate and other food products containing cocoa	900	43.2	2.3
23.	20057010, 20057090	Olives	5000	0	1.0
24.	21050010	Ice cream	160	41.3	10
25.	22030001, 22030009, 22030010	Beer	70,000 hl	55	0.5
26.	24011010, 24011020, 24011060, 24011070, 240l2010, 24012020	Tobacco	2500	18.8	2.5

B. List of contingents with Bulgaria

	Tariff position HS classification	Product/group of products	Contingent (tones) 01.01.- 31.12.2004	Preferential tariff rate %	Maximum limit of allocation %
1.	070310	Onion	150	20% less than applied rate	14
2.	170199	Refined sugar	200, of which: 160 – traditional importers 40 – new comers	20% less than applied rate	13 50
3.	200190	Vegetables and fruits, fresh or caned	100	15	20
4.	200710 200799	Jams, sweets, jellies	50	15	20
5.	200980	Juices, from other fruits and vegetables	50	20% less than applied rate	20
6.	200990	Mixed juices	80	20% less than applied rate	25
7.	2203	Beer	50 hl	30% less than applied rate	20
8.	2401	Tobacco, not processed	250	25	20

C. List of contingents with Croatia

	Tariff position HS classification	Product/group of products	Contingent (tones) 01.01.- 31.12.2004	Preferential tariff rate %	Maximum limit of allocation %
1.	0202	Frozen beef (bovines) meat	100	25	20
2.	0406	Cheese, different sorts of	50	75% from the applied rate	20
3.	080520	Mandarines, tangerines	600	0	3.35
4.	160210 160220 160231 160232 160239 160242 160249 160250	Meat, other products and canned food, thereof	50	15	20
5.	21069098	*Cedevita*- Vitaminized food products	600	0	3.35
6.	2204	Wine from fresh grapes, unfermented wine	1000 hl	70% from the applied rate	10

C. List of contingents with Slovenia

	Tariff position HS classification	Product/group of products	Contingent (tones) 01.01.- 31.12.2004	Preferential tariff rate %	Maximum limit of allocation %
1.	040120	Milk and sour cream	33	30	30
2.	1601	Sausages and similar products	33	28	30
3.	160290	Other products from meat, or from animal blood	30	28	30
4.	200490	Vegetables, processed, others than those at position 20.06	10	25	50

D. List of contingents with Macedonia

	Tariff position HS classification	Product/group of products	Contingent (tones) 01.01.-31.12.2004	Preferential tariff rate %	Maximum limit of allocation %
1.	180631 180632 180690 190531	Chocolate Biscuits	50	0	30
2.	20019020	*Capsicum* sort of fruits	30	0	50
3.	20019050	Mushrooms	30	0	50
4.	20059080	Other prepared or canned vegetables (Ajvar)	20	0	50
5.	210111 210112	Extracts, essences and products thereof	5	0	50
6.	21039090 210410	Prepared sauces and products thereof	10	50% from the applied rate	50
7.	2401	Tobacco, not processed	200	0	2

E. List of contingents with Albania

	Tariff position HS classification	Product/group of products	Contingent (tones) 01.01.-31.12.2004	Preferential tariff rate %	Maximum limit of allocation %
1.	04069029 04069031 04069033	Cheese	50	0	30
2.	07082000	Bean (between 01.11/30.04)	100	0	20
3.	07133100	*Vigna mungo* sort of bean	50	0	30
4.	08042090	Dry figs	100	0	20
5.	08071100	Water melons (between 01.11/30.06)	500	0	4
6.	08071900	Other sorts of melons (between 01.11/30.06)	100	0	20
7.	1509	Olives' oil	100	0	20
8.	1601	Meat products	50	0	30
9.	1602	Canned meat	50	0	30
10.	20019065	Olives	100	0	20
11.	200911 200919 200921 200929 200931 200939 200941 200949	Juices from citric plants	100	0	20
12.	2201 2202	Mineral water	1000	0	2

2 Transaction costs

There are various measures for estimating the transaction cost related to the procedure of importing goods in a country. Most of these estimates are based on surveys. One of the internationally recognized surveys also tackling this issue is *The Global Competitiveness Report* edited by the World Economic Forum[1]. The survey includes 102 countries; the partner institute for Romania is The Romanian Economic Society. As far as Romania is concerned, the survey was administered to a representative sample of 100 companies; the sampling procedure took into consideration geographical diversity (more areas within Romania), production structure proportionality (agriculture, manufacturing and services were represented according to their contribution to GDP) and ownership structure proportionality (local state capital, local private capital and foreign capital firms). Although the results must be treated with caution, this survey is, at the best of my knowledge, the most in-depth, reliable and updated one in various matters of competitiveness, trade aspects being included. We have selected for interpretation a very limited number of indicators as presented in the above mentioned report.

1. The cost of importing foreign technology (the combined effect of import tariffs, licence fees, bank fees and the time required for administrative red tape raises the cost of importing foreign technology by: 1-less than 10%, 2-between 11% and 20%, 3-between 21 and 30%..., 9-greater than 80%). Romania's score is 3.3 (ranking: 75 out of 102), the standard deviation of responses being quite large (1.8). The score recorded in the 2003-2004 Report is slightly better than the one recorded in the 2002-2003 Report (3.4), the deviation from the world's mean being 0.7 in 2003-2004, as compared to 1.0 in 2002-2003.

First, this suggests that the total costs of importing foreign technology (irrespective of the country of origin) is between 21% and 30%, closer to the 21% lower limit. Furthermore, this cost is diminishing in time (among explanations, one might consider learning by doing, and improved customs procedures) and it is becoming less harmful to business, as it approaches the world's mean. This cost nevertheless varies substantially from firm to firm (quite high standard deviation); one might interpret this by saying that the business environment in Romania is still in the making, and it provides different opportunities (chances) to different companies. There is also a matter of accumulating experience in dealing with specific custom procedures.

However, from this estimation of the transaction cost, import tariffs should be deducted. The weighted average tariff rate was 6.12% in 2003[2], which means that the non-tariff

[1] World Economic Forum , *The Global Competitiveness Report 2003-2004*, Oxford University Press.

[2] Author's calculation. First, the average tariff rates were computed for EU, CEFTA and the rest of the world, for agriculture products (1-24) and industrial products (25-99) separately. Then, this rates were weighted for each of the three main trade partners, based on the share of agriculture in total imports. Finally, the average tariff rate was compounded by weighting the three partners' average rates and their shares in total imports.

component of the cost of importing foreign technology is below 20% of the cost of the foreign technology itself. Of course, foreign technology is only a part of Romanian imports. In fact, an earlier study shows that about half of total Romanian imports are final goods for current consumption, and capital goods only represent 6% of total imports[3]. By excluding licence fees (royalties), the total non-tariff cost of imports should drop even further.

2. Hidden trade barriers (hidden import barriers, others than published tariffs and quotas, are: 1- an important problem, 7-not important). Romania's score is 3.3, ranking as the 96th country out of 102. The result in the 2003-2004 Report is similar with that recorded in the 2003-2004 Report, despite various measures taken by the Romanian government aiming towards higher transparency and efficiency at the customs[4]. This may indicate the existence of resilient problems, that are not to be solved by the process of trade liberalization. However, these hidden trade barriers have not deterred much trade, since total imports almost doubled in Romania over the last four-five years. Still, they have increased the cost of imports.

3. Irregular payments in exports and imports (in your industry, how commonly would you estimate that firms make undocumented extra payments or bribes in connection with export and imports: 1-common, 7-never occurs). Romania ranks 98th, with a score of 3.0 (far from the world' mean of 4.8). However, the standard deviation of responses is quite high (1.9), which suggest that experiences with irregular payments vary considerably from industry to industry and from firm to firm). These irregular payments might be a measure of the extent of the costs associated with hidden trade barriers.

4. The non-tariff transaction costs for imports are nevertheless counter-balanced by the exchange rate policy of national currency's appreciation. The national currency (ROL) has appreciated in real terms against a basket of USD and Euro both in 2001 and 2002, and against USD in 2003; the trend of real appreciation is set to continue in the coming years, following two objectives: an increase in real income, and a stable one-digit inflation rate. This policy of real appreciation helps imports, which are cheaper in foreign currency.

Other potential barriers rise from the distortions induced by government procurement, on the one hand, and state aids, on the other hand.

- Government purchasing. According to Law 212/2002, Government purchasing in Romania is governed by the principles of free competition, efficient use of public funds, transparent procedures, equal treatment and confidentiality. Foreign companies (be them suppliers, subcontractors, main contractors) are treated on the same foot with domestic enterprises provided that the reciprocity is provided. Nevertheless,

[3] Caetano et all, 2002

[4] Such measures were included in the 'Plan for improving the business environment', adopted in the autumn of 2002, with support from the World Bank.

contracting authorities have the right to request to the main contractor that 30% of the total contracts undertaken to be attributed to designated third parties. Given the potential for discrimination comprised by such a provision, thoughts are being given, at the level of the Government, to abrogate it.

- State aid. State aids mounted to 6% in 2001; most of them take the form of giving up to fiscal revenues, such as debt forgiveness or debt-equity swap. The attached Excel file summarizes state aids and state direct subsidies, latest available data.

3 Political barriers, macroeconomic stability

There are no political barriers to trade in the case of Romania. The trade embargo with Serbia and Montenegro has been given up three years ago. Romania is a member of CEFTA since 1997. Romania has a history of extensive cooperation with its regional partners, in a number of regional organisms, such as Stability Pact, South East European Cooperation Initiative (SECI), Central European Initiative (CEI), Black Sea Economic Cooperation.

Regarding macroeconomic stability, Romania has recorded positive developments over the last four years. The inflation rate, once a significant shortcoming for the business environment, has been dramatically reduced, from 54.8% in 1999 to 17.5% in 2002 and 15% in 2003. The economic growth has resumed since 2000, and has recorded an average rate of growth of 5% in the period 2001-2003, with similar prospects for the period 2004-2006 (according to IMF projections). Both exports and imports have boomed since 2000 onwards, from USD 8.5 billion exports and USD 10.3 billion in 1999, to USD 14.6 billion exports and USD 18.8 billion imports in 2002. The trade openness index increased from 55% in 1999 to 74% in 2002. However, while exports were still booming in volume, the trade deficit widened in 2003 (at about 8% of GDP), and prospects may appear for short-term quantitative restrictions to selected imports for balance of payment adjustment.

II Selected sector-based studies

The sector based studies comprised by this paper may not be very extended, and may not respond to all aspects linked to the level of protectionism in those specific sectors. Nevertheless, the sectors addressed hereby are the hottest subjects in Romanian economic policy ahead of EU integration.

The textiles and clothing industry is the main export-oriented sector of the economy: it covers 25% of Romania's total exports, respectively 34% of Romania's exports to the EU; imports are also impressive in this sector, as Romania is one of the largest three export markets for EU textiles. Decreased protectionism means higher competitive pressures, both on domestic and external markets, for Romania's main export industry.

Agriculture and energy are two of the EU negotiation chapters most difficult to finalize. Higher imports are expected in these two sectors; the liberalization of energy prices, which in the first stage means higher prices and more import opportunities.

Financial services are also briefly addressed, as they have an important potential for development; the same is valid for the telecommunication sector, following its liberalization. One technicality about Romanian foreign trade: specific taxes are rarely used, and only for products with low shares in total trade (e.g., some alcoholic beverages and unprocessed tobacco) and therefore we have chosen to ignore them.

1 The textiles and clothing industry

1.1 Industry characteristics

Romania's foreign trade in textiles and clothing, million euro

	2000	2001	2002	2003
Exports	2719	3330	3720	3962
Imports	2315	2799	3105	3152

Source: INSSE, 2004

The main features of the competitive position of the Romanian textiles and clothing industry (T/C) are:

- The main competitive advantage stems from the low cost of the workforce. Labour productivity is low, but the even lower wages (relative to the industry average) lead to decreasing unit labour costs.
- Romania has a strong competitive position on the main European markets, and it records a positive dynamics. The countries against which Romania makes these competitive gains are not the direct competitors (from the production costs perspective), but mostly the EU member states. However, Romania's main clothing

export markets (Italy and Germany) are also the main sources of Romanian textiles imports. A change in the current structure of textiles supply might create a sustainability risk for the Romanian exports on those markets.

- Romanian exports are highly vulnerable to changes in either the foreign demand or the production factors' prices, given the exports' dependency of intermediate companies, the geographical concentration of foreign markets, and the dominance of vertical intra-industrial trade (in the clothing sector).
- Romanian products compete on market segments with low unit values; the competition is on price, not on innovation (vertical trade, mostly under lohn arrangements, and low R&D and advertising expenses).
- The most dynamic Romanian export products (within T/C industry)are those that also record important dynamic gains on the international market. A trend toward diversification of the export structure can also be noticed.
- The share of Romanian exports to EU under the OPT regime (outward processing traffic), which involves the lowest level of domestic processing, has diminished substantially. Since the market share for Romanian exports to EU has nevertheless increased, one could submit that a change has occurred towards higher production stages, and a substitution effect has also occurred in exports' structure.
- Romania's commercial surplus with EU in trading products of the T/C industry comes exclusively from the clothing sector. Hence, Romania singles out from its main competitors in clothing by that it is not an important supplier of textiles as well.
- Two thirds of Romanian textiles and clothing exports are operated through intermediate companies. The spread between the producer's prices and the final retail prices is usually two-three times higher than the producer's prices themselves.
- The tariff protection in EU is lower than the current tariff protection secured for Romanian producers.
- The access to financing is very difficult for companies in the T/C industry. Own funds represent 80% of the total investment commitments. Domestic loans are suffocated by high real active interest rates, while foreign loans are mostly short-term, of a commercial nature.

1.2 Commercial protectionist measures

The finalization of the Uruguay Round marked the end of the Multi-Fibre Agreement and the creation of a new 10 years framework for the international trade with textiles and clothing (TCA). Romania, as an WTO member, adopted this multilateral agreement. TCA refers to a gradual elimination of the quantitative restrictions that were negotiated on a bilateral basis within the former MFA.

Romania's imports of textiles and clothing have not been subject of quantitative restrictions. As for the tariff protection, one can remark a differentiation in the tariff level, correlated with how many production stages the respective product incorporates. E.g., in 2003, clothing products were subject of a consolidated and applied tariff rate of 30%, while textiles fires and fibres were subject of rates between 10 and 25% – the most notable exceptions being cotton, flax, hemp (38.5%) and carpets (40%). It may seem strange that the tariff rates are higher for imported inputs than for the final products, a situation that can only lead to a diminished level of effective protection for the domestic clothing producers using inputs such as cotton, flax and hemp. The reason for this comes from the authorities' intention to protect the local producers of technical plants.

The persistence of a rather high tariff protectionism for imports of raw materials in the T/C industry failed to support the domestic clothing production for the local market. One additional factor was the functioning of the 'active improvement' regime, that suspended tariffs for those raw material that were imported to be used as inputs for export-oriented clothing products. Therefore, prior to the liberalization of the textiles imports from most states with which Romania has preferential agreements, the tariff system acted towards supporting the export orientation of the clothing products.

Romania's record in a number of protectionist measures is briefly reviewed below.

- *Anti-dumping*. Romania has never initiated an anti-dumping investigation in T/C industry, despite informal complaints from local producers against very cheap exports from Turkey and China. The lack of action may have two explanations. First, the national legislation on this issue is incomplete. Second, the local producers are not aware of the role they have to play in an anti-dumping investigation (they must start the process, by notifying the governmental authority in charge) and they do not know the steps to be taken until the anti-dumping decision is reached. As from the other perspective, Romania is not currently involved in any commercial dispute on dumping in textiles and clothing. In the last decade, however, Turkey and the UE had maintained for 5 years anti-dumping taxes on polyester fibres.
- *Salvgardation*. Romania has never used salvgardation measures in textiles and clothing, probably because of the same factors valid for anti-dumping measures; plus, such measures might have really not been necessary. Nevertheless, Romania was the subject of transitory salvgardation measures. A recent example: in July 2001, Poland introduced salvgardation measures against Romania for acrylic fibres, tariff positions 550931, 550932 and 550961. These measures took the form of quantitative restrictions administered through licences. According to these restrictions, one Romanian producer was allowed a maximum export of 50 tonnes. These measures were removed in March 2002, following the recommendation of the supervisory mechanism of TCA. The reason for imposing that measures was the higher rise in imports from Romania (35.8%) than the average rise in Polish imports (10,5%) in the preceding years and the consequent market share gains for Romanian imports (from 15 to 20%). Ironically, the rise in Romanian imports was a substitution effect, after Poland imposed, in mid 90s,

similar salvgardation measures against the then main source of Polish imports of acrylic fibres, Lithuania.

- *Custom evaluation*. In 1997, Romania introduced a new legislation that stated the so-called reference prices. For all imported products below their respective reference prices, the legislation demanded importers to make a interest-free deposit payment for 30 days (equivalent to the difference between the import price and the reference price), and in those 30 days the importers had the obligation to bring in documents justifying the low import price. That legislation also affected some clothing articles. US claimed that the legislation broke a number of WTO agreements signed by Romania, and by the end of 1998, Romania announced the reference price practice had been aborted.

1.3 The European Association Agreement

The textiles and clothing trade between Romania and the EEC was first addressed in a bilateral agreement signed in 1986 and entered into force in 1987. The current basis for trade between Romania and EU is the European Association Agreement, signed in 1993; it provided for a gradual implementation of a free trade area between the signatory parties. It was created on the principle of asymmetric concessions, in the sense that EU was the first to eliminate all tariff trade barriers (1998), followed by Romania (2002). Currently, there are now tariff rate and quantitative restrictions in the bilateral trade with textiles and clothing.

Some remarks on the liberalization of Romanian exports and the new rules of origin:

- the reciprocal trade liberalization between Romania and EU eliminated the need for quotas for Romanian exporters within the OPT regime. The active improvement-OPT link lacked its relevance, but the production under lohn agreements remained dominant. The OPT regime still influences Romanian exports, but indirectly, by being directed towards other states: Belarus, China, Serbia and Montenegro, India, Indonesia, Macao, Malaysia, Pakistan, Philippines, Singapore, Thailand, Vietnam (Report of the WTO – EU Secretariat, 2002). This means, for Romanian producers, an increase of the competitive pressure coming precisely from those states that are also gaining comparative advantage in clothing (due to the low wage costs).
- the Pan-European Cumulative System regarding the rules of origin is helpful for the Romanian clothing producers, as it represents an extension of their supply opportunities.
- a gain for domestic clothing producers means an increased competitive
- pressure for domestic textiles producers.
- Currently, Romania’s trade in textiles and clothing with EFTA countries, as well as with Turkey, is liberalized. Moreover, EFTA countries, CEFTA and Turkey are integrated in the Pan-European Cumulative System.

1.4 The impact of Romania’s accession to the EU on the domestic textiles and clothing industry

The main document that constitutes the basis for the European policy in this area is ‘The Action Plan for the Competitiveness of the European Textiles and Clothing Industry’. According to it, four main directions for action have been identified:

- facilitation of structural adjustments. The structural adjustment of European firms from the T/C industry refers to increasing producers’ capacity to adapt to the new information technologies and the e-commerce. This direction of action also aims at increasing the R&D expenses (as a percentage of turnover) and solving the market entry barriers for SMEs.
- improving the functioning of the common internal market, which refers to the adequate consumers’ protection and information.
- improving the hiring and training conditions.
- benefiting from external relations. In this context, the creation of a Euro-Mediterranean free trade area by 2010 represents a priority.

As of 2002, EU maintained quantitative restrictions on textiles and clothing imports against 15 states (e.g. Argentina, Brazil, China, Indonesia, Korea, Pakistan, Philippines) under a multilateral framework, against 3 states (Belarus, Uzbekistan, Vietnam) under a bilateral framework, and unilaterally against 2 states (Serbia and Montenegro and Korea). A significant moment for EU’s foreign trade relations was represented by China’s accession to WTO at the end of 2001. EU applies on Chinese imports of textiles and clothing, apart from the MFA quantitative restrictions, other quantitative restrictions on products that are not covered by MFA, such as flax or silk. For these products, EU is willing to abolish the quantitative restrictions, provided that China eliminates state’s monopoly on foreign trade (for silk).

Having these remarks in mind, one could submit a number of implications for the T/C industry deriving from Romania’s accession to the EU, under a commercial perspective:

- *tariffs*. Romania’s accession to EU will mean a substantial cut in the level of protectionism. Examples include: for textiles, the maximum level of the conventional rate is 8.7% (the average tariff is around 5%), while in Romania it goes, under MFN, to as much as 40%. For some of the most protected products in Romania, such as cotton, flax and hemp, EU does not imposes tariffs, which means higher foreign competition for Romanian textiles producers. The Common Agricultural Policy may compensate for this, but only on condition that specific requirements are met. Carpet producers will also witness a reduction of their tariff protection (from 30% in Romania to 8% under the Common External Tariff). Clothing producers will also be affected, since the current level of protection, 30%, is way below the EU level, 12%.

- It should be further mentioned that the EU level of protectionism may diminish in the coming years, following the implementation of international agreements; however, the Cancun failure casts doubts on this process.

After joining the EU, Romania will grant a preferential treatment to a larger number of states that benefit from it now. In fact, EU applies the conventional tariff regime to only 9 states (Australia, Canada, Hong Kong, China, Japan, Korea, New Zeeland, Singapore, Taiwan, US). Some of the states that will gain preferential, or even free, access on the Romanian market after Romania's accession to the EU are among the Romania's main competitors – a situation that, obviously, would not be in favour of the domestic producers. Romania will also have to apply the OPT rules. Romanian will practically become a donor of preferential treatment in international trade with textiles and clothing, from its present position of beneficiary of such treatment. This transformation will severely diminish the current tariff protection against foreign competitors, particularly against the Asian ones.

- *new free trade agreements*. As part of the EU, Romania will adhere to the EU efforts towards a Euro-Mediterranean Free Trade Area (comprising EFTA, Turkey, Algeria, Egypt, Israel, Jordan, Lebanon, Morocco, Palestine, Syria and Tunisia). EU has already signed association agreements with Macedonia and Croatia, as well as with Mexico and South Africa, and there are plans for free trade agreements with Mercosur sand with some Arab states from the Gulf.
- *quantitative restrictions*. Romania will join EU only after TCA expires, which means that Romania will be able to impose and/or maintain quantitative restrictions only against states that are not members of the WTO.
- *protectionist measures*. After joining the EU, Romanian will be able to recourse to a functional mechanism for protection, but two things are very important in this direction. First, Romanian producers must be aware of the required procedure. Second, Romanian producers will be better off within the European producers' professional networks and associations.

Note: As of 2003, Romania's unweighted average tariff rates for textiles and clothing were: 0% with EU and CEFTA-6 countries; 23.7% with the MFN countries.

2 Agricultural industry

Romania's foreign trade with agricultural produces and products (SITC Rev.3 groups 0,1,4), million euro

	2000	2001	2002
Exports	314	423	404
Imports	969	1188	1158

Source: INSSE, 2004

Romania's imports of agricultural products represent about 30% of its total imports from CEFTA members, but only less than 7% of its total imports from EU. CEFTA membership led to worsening trade deficits for Romania, especially on agricultural products. In fact, Romania is the only CEFTA member that performs better in trade with EU than in trade within CEFTA, in terms of the coverage ratio. A possible explanation is linked to the higher level of subsidies applied in other CEFTA members, mainly Hungary (due to a conservative budgetary policy and to the yet unresolved problem of property rights on former state owned agricultural enterprises, the level of subsidies for the Romanian agriculture was really low, and the main forms of subsidies were not linked to the volume or efficiency of production). At certain time intervals, the Romanian authorities intervened and imposed temporary surcharges on imports from Hungary (chicken meat was the most targeted import), but with no effect: in the context of insufficient domestic supply, the demand for imports of basic agricultural products proved quite inelastic to price.

The level of protectionism with EU, has been decreasing in recent years due to completion of the EU Association Agreement (plus an additional document, signed in 2000 and fully implemented by the end of 2003).

The share of products subject to contingents represents 9% in total Romanian import of agricultural products from the EU. In 2001 and 2002, EU used 100% of its contingent for chicken meat, 75% of its contingent for cheese varieties, 65% of its contingent for wheat in 2001 and 0% in 2002, and left contingents for products like maize and barley unused. For other processed agricultural products, EU used 100% of its contingent for margarine, and almost nothing of its contingents for chocolate and non-alcoholic beverages.

The adoption of the Common External Tariff will imply significant changes in the level of protectionism for Romania. The tariff protection for some products will diminish drastically; among these products, there are: poultry, margarine, butter, milk and diary products, some vegetables, sugar, oils, olives, coffee, whisky. For those products that are not domestically produced (olives, coffee, whisky), the only impact will be upon custom revenues. But for the others, domestic producers will face an increased competition. Other products, however, will witness their tariff protection increasing: by 117-141% for rice, 134% for animal food products, 128% for beef, 99-105% for tomatoes, 97-104% for apples, 55% for barley, 32% for flour, 10% for chicken eggs.

Note: As of 2003, Romania's unweighted average tariff rates for agricultural products were: 14.45% with EU; 10.18% with CEFTA-6; 21.76% with the MFN countries.

3 Electrical energy industry

Romania's foreign trade with mineral fuels, lubricants and related materials (SITC Rev.3, group 3), million euro

	2000		2001		2002	
	Export	Import	Export	Import	Export	Import
Coal, coke	-	184	-	265	-	241
Petroleum and related	725	1146	693	1506	1019	1402
Gas	33	363	32	398	35	447
Electric energy	51	27	69	26	106	13

Source: INSSE, 2004

Electric energy sector in SEE countries, 2002

	Production billion Kwh	Consumption billion Kwh	Exports billion Kwh	Imports billion Kwh
Romania	49.787	45.677	1.400	0.775
Albania	4.378	5.378	0.100	1.072
Bosnia-Herzegovina	2.615	2.577	0.205	0.350
Bulgaria	38.840	34.420	3.200	1.500
Croatia	10.578	12.638	0.900	3.700
Macedonia	6.395	5.992	0.030	0.075
Serbia Montenegro	32.984	31.546	0.430	0.914

Source: Oeconomica, 2003

Industry characteristics:

- Romania is not a large importer of energy as such, but a large importer (35% of its consumption needs) of energy resources, which are inputs for this industry.
- Romania has inherited an energy intensive economy, with subsidized prices (Angheluta et al., 2003). The liberalization process has begun; as this process will advance, price increases will likely be reflected in higher inflation rates in the short run.
- Regarding the domestic markets, there is a significant potential for improved consumption efficiency, by reducing subsidies and price controls. Subsidies will, in the end, be granted only to households with low incomes, as the unavoidable price increases lead to more severe welfare losses for those with below average income (Oprescu et al., 2002).
- The energy sector is the largest loss maker left in the Romanian economy: it has recorded a negative productivity dynamics combined with high wage increases. The energy sector is yet to be restructured: no privatization occurred in the last 15 years. Moreover, most arrears in the Romanian economy (which sum up 40% of GDP) are linked to the energy sector. Hence, this sector, in its current state, creates inflationary pressures and slows down the economic growth.

There are three main barriers to higher imports of electric energy:

- the fact that the energy price for consumers is still below costs: it covers only 80% of the production costs plus development costs for the electric energy (and less than 1/3 for the gas industry). Therefore, the domestic electric energy price is generally lower than the imported one. E.g., electric energy prices in Romania, for households, are half of those in EU, and 20% lower than those in other regional economies. Price liberalization is ongoing, a gradual programme being implemented.
- the degree of opening of the domestic market for electric energy is still limited: only 33% of consumers are now considered eligible, in the sense that they can buy the energy directly from the local or foreign producers. When the competition will increase, it may lead both to reduced domestic prices and to increased imports.
- an important technical barrier persists, as the Romania electric energy system has not yet been interconnected to the European network (Union for Electric Energy Transport Coordination). Romania managed to complete recently two 400kV lines, with Hungary and Slovak Republic. The interconnection with Bulgaria is still a problem, which also prevents Romanian exports to Turkey. The interconnection with Serbia has been delayed by post-war repairs in the former Yugoslav republic. Shall this problem be solved Romania will be connected to the European network. This would facilitate both exports and imports of electric energy.

4 Telecommunications

The Romanian telecommunication market became fully liberalized on January 1st, 2003 with the end of the monopoly of RomTelecom, previously maintained through the RomTelecom Privatization Act for fixed-telephony services (local, national and international) and leased telephony lines. The process of adapting and implementing the provisions of the EU New Regulatory Framework for Electronic Communication Services (Directives 2002/19/EC-2002/22/EC and Directive 2002/58/EC) is ongoing. The National Regulatory Authority in Communications (NRAC) was created for this purpose and is in charge for identifying the relevant markets in the electronic communication sector in Romania.

For the market of *unbundled access*, full or shared, to the local loop, NRAC has issued several decisions. RomTelecom was designated as an operator holding significant power and the obligations to be imposed on RomTelecom in relation to granting unconditional access to the local loop were established. The tariffs established by NRAC (1.15 €cents for peak hours and 0.90 €cents otherwise) are below the average of the similar tariffs from other EU countries that have liberalized the electronic communication market. (According to the third IBM Report, published in June 2003, the average local inter-connection tariff in EU is 0.77 €cents. In candidate countries, this average is of 1.4 €cents). The interconnection tariffs for ending calls from fixed to mobile telephony are now below the average of member and candidate countries.

The liberalization of the fixed telephony market is expected to impact more on the mobile telephony prices and penetration rates than directly on the fixed telephony prices and penetration rate. At a low penetration rate of the fixed telephony, the potential clients are more likely to choose the developing mobile communication means than to switch to an alternative operator of fixed telephony.

Nevertheless, up to 29th of March 2004, the National Regulatory Authority for Communications (NRAC) authorized 185 companies to enter the market as providers of telephony services.

The break down of companies authorized to provide telephony services according to their targeted market segments is as follows: 137 – local call segment, 143 – long distance call segment, and 162 – international call segment. A number of 82 companies intend to install a public phone and 63 companies will provide ISDN services.

In December 2003, the first alternative fixed telephony service was launched by Astral Telecom Cluj-Napoca, beginning with four cities (including Bucharest). The services provided are in average 30% cheaper. More projects are expected to be implemented in 2004. Government is taking the lead in catalysing the competition, by creating joint companies that will enter the fixed telephony market: Teletrans, Telecommunicatii CFR and POSTelecom.

There is also potential for decreasing the prices as at the moment of liberalization RomTelecom had in PPP terms, tariffs for local, interurban and international calls significantly above the EU average, and in the boundaries of EU member countries for subscriptions.

On overall, the liberalization of the telecomm market is expected to have a positive impact especially on the tariffs of international calls, as well as indirectly on the tariffs and penetration rates for the mobile telephony users. However, as the EC Regular Report for Romania shows, the attempt of implementing EU legislation in telecommunication, legislation that was conceived for more competitive markets, directly to a market still dominated by a monopolist incumbent might raise some risks. It is worth noticing that the newly created authority dealt in a successful manner the recent attempts of the incumbent operator resistance to increase its opening in terms of interconnectivity and to further rise prices. Although the threats of RomTelecom might have delayed the entering on the market of some of the operators it finally results in nothing else than a short-term disturbance.

5 Financial services

The Romanian financial system is based on the banking sector (which holds more than 95% of total assets in the system). The banking sector witnessed a series of major failures during the last decade, which diminished its credibility. The banking system has been cleaned up in recent years, but its strength has to be tested over a longer period of time, and the capital account opening will be a major challenge to its stability.

Romania – prudential regulations in the banking system

Type of regulation	Prudential regulations	Comparison with EU standards
Minimum capital	ROL 250 billion (approximately EUR 8.8 million)	EUR 5 million
Capital adequacy ratio (for credit risk)	12% (risk-weighted assets)	8% (risk-weighted assets)
Liquidity indicator	Effective liquidity/Required liquidity > 1	No European standards in place
Limits on credit exposure	20%	25%
Credit concentration per client or connected lending		
Loans to persons in special relationship with the bank	20% (aggregated amount)	20%
Limits on FX risk	20% (total FX position) 10% (individual FX position)	Any amount exceeding 2% is multiplied by 8 to reach capital requirement
Loan classification and provisioning	0% for standard loans 5% for loans under observation 20% for substandard loans 50% for doubtful loans 100% for bad loans	No EU standards in place
Reserve funds	Banks must allocate 20% of gross profit for the reserve fund until the latter is equal to share capital, afterwards up to 10% until the fund is twice as large the share capital. From that moment, allocations are made from net profit.	No EU standards in place
Deposit insurance	Every bank accepting household deposits must participate in the insurance fund. Minimum coverage: ROL 100.4 million (EUR 3,670)	Every credit institution must participate in insurance fund/s. Minimum coverage: EUR 20,000
Rules on shareholders	Any person intending to acquire an equity stake of at least 5% or wishing to increase its stake above levels representing multiples of 5% must win NBR approval.	Any person wishing to acquire, directly or indirectly, an equity stake of at least 10% or to increase its stake above thresholds of 20%, 33% or 50% must inform the supervisory authority that may oppose the acquisition.
Limits on banks' equity interest	20% of share capital of any commercial company not engaging in financial activities specified under The Banking Act; 10% of bank's own funds; 50% of bank's own funds (aggregate limit).	15% of bank's own funds; 60% of bank's own funds (aggregate limit).
Audited Annual Reports	External audit	External audit

Compared to other transition economies, the Romanian financial sector is still underperforming, primarily in terms of financial intermediation (low monetization, low domestic credit as share of GDP, low stock market capitalization) and insufficient development of non-banking financial markets.

Key prudential indicators have improved markedly in the last couple of years. The solvency ratio grew and non-performing loans went down dramatically over the last five years. Moreover, the foreign presence is dominant in the banking sector: as foreign capital ownership in total banking capital rose to 58.7% in 2002 versus 35.8% at year-end 1998; in 2003, the largest remaining state bank, Romanian Commercial Bank, with about 30% of system's capital and loans, was also privatized in favour of two foreign institutional investors.

The array of financial instruments available is small and, accordingly, they are not very effective: interbank deposits (including deposits taken by the central bank) hold the largest share of the interbank market; the small share of outright operations, which are more efficient in the case of sterilized operations (the daily average volume of reverse repo operations ranged from 8% to 16% of total deposit-taking operations in 2002); government securities experienced obvious weaknesses in the last two years, and it still lacks a developed secondary market.

There are (only) few types of operations in the forex market: mostly spot transactions, occasionally forward transactions, short-term transactions and seldom swap forex transactions. Dealing in derivatives has not started yet. Finally, the market is split due mostly to foreign banks' excessive cautiousness, which makes (often) surpluses coexist with deficits (at the end of the business day) on various segments of the market.

In the process of financial services liberalization, an important role is played by the opening of the capital account.

This KAL timetable came under criticism for a number of reasons:

- it looks imprudently compressed in time (in the end, some operations have been delayed; e.g., the possibility for residents to open accounts abroad was delayed to 2005) and it favours undifferentiated and complete liberalization of capital inflows.
- the KAL timetable makes no effective preference for long term flows against short term flows; maturity-type of restrictions are short-lived (1 year), and, in some cases, liberalization of short term flows is not accompanied by adequate prudential measures
- the KAL timetable makes no effective preference for capital inflows against capital outflows (one effect was that in 2003, for the first time after 1990, the 'errors and omissions' item of the balance of payments was negative).

Timetable for capital account opening

Type of capital flows	Type of operations	Status of liberalization
By capital nature (maturity)		
Long term flows	Direct investments, inward and outward*	Free
	Real estate investments, inward and outward*	Free
	Purchase of land by non-residents	Subject of derogation after EU accession
	Financial loans and credits, granted by residents to non-residents and by non-residents to residents, with maturity over 1 year	Free
	Sales and issue of bonds, shares and other securities dealt on the capital market, by residents, irrespective of maturity	Free
	Purchase of bonds, shares and other securities by non-residents, irrespective of maturity	Free
	Purchase of bonds, shares and other securities dealt on the capital market, by residents, irrespective of maturity	Free from 1.01.2003
	Sales and issue locally of bonds, shares and other securities dealt on the capital market, by non-residents, irrespective of maturity	Free from 1.01.2004
Short term flows	Financial loans and credits, granted by residents to non-residents and by non-residents to residents, with maturity less than 1 year	Subject of NBR authorization, except for banks, free from 1.01.2003
	Commercial credits related to international commercial transactions, by residents to non-residents and by non-residents to residents	Free
	Guarantees by non-residents to residents	Free
	Guarantees by residents to non-residents	Free from 1.01.2003
	Sales and issue of bonds, shares and other securities dealt on the capital market, by residents, irrespective of maturity	Free
	Purchase of bonds, shares and other securities by non-residents, irrespective of maturity	Free
	Purchase of bonds, shares and other securities dealt on the capital market, by residents, irrespective of maturity	Free from 1.01.2003
	Sales and issue locally of bonds, shares and other securities dealt on the capital market, by non-residents, irrespective of maturity	Free from 1.01.2004
	Personal capital transfers**	Free
	Personal loans and credits granted by residents to non-residents	Free from 1.01.2003
	Transfers in performance of insurance contracts	Free
	Operations in Lei deposit accounts opened by non-residents	Free from 1.01.2004
	Operations in deposits abroad by residents	No later than accession
	Physical import and export of financial assets	Free, except for cash; cash payments free from 1.01.2004
	Sales, issue, purchase of securities and other instruments dealt on the money market, by residents and non-residents	No later than accession
By capital destination		
Capital inflows	Inward direct and real investment*	Free
	Purchase of land by non-residents	Subject of derogation after EU accession

	Financial loans and credits granted by non-residents to residents, maturity more than 1 year	Free
	Financial loans and credits granted by non-residents to residents, maturity less than 1 year	Subject of NBR authorization, except for banks, free from 1.01.2003
	Commercial credits granted by non-residents to residents	Free
	Guarantees by non-residents to residents	Free
	Sales and issue of bonds, shares and other securities dealt on the capital market, by residents, irrespective of maturity	Free
	Purchase of bonds, shares and other securities dealt on the capital market, by non-residents, irrespective of maturity	Free
	Personal capital transfers	Free
	Transfers in performance of insurance contracts	Free
	Physical import of financial assets	Free, except for cash; cash payments free from 1.01.2004
	Purchase of securities and other instruments dealt on the money market, by non-residents	No later than accession
	Sales and issue of securities and other instruments dealt on the money market, by residents	No later than accession
Capital outflows	Outward direct and real estate investment	Free
	Financial loans and credits granted by residents to non-residents, maturity more than 1 year	Free
	Financial loans and credits granted by residents to non-residents, maturity less than 1 year	Subject of NBR authorization, except for banks, free from 1.01.2003
	Commercial credits granted by residents to non-residents	Free
	Guarantees by residents to non-residents	Free from 1.01.2003
	Purchase of bonds, shares and other securities dealt on the capital market, by residents, irrespective of maturity	Free from 1.01.2003
	Sales and issue locally of bonds, shares and other securities dealt on the capital market, by non-residents, irrespective of maturity	Free from 1.01.2004
	Personal capital transfers	Free
	Personal loans and credit granted by residents to non-residents	Free from 1.01.2003
	Transfers in performance of insurance contracts	Free
	Physical exports of financial assets	Free, except for cash; cash payments free from 1.01.2004
	Operations in deposits abroad by residents	No later than accession
	Sale and issue of securities and other instruments dealt on the money market, by non-residents	No later than accession
	Purchase of securities and other instruments dealt on the money market, by residents	No later than accession

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