

## BNR's Cristian Popa: Censure motion would impede on Gov't capacity to avoid massive rise in public spending

**By blocking the Government's right to issue emergency ordinances, through a censure motion, the political decision-makers knock out all possibilities of adjusting the increase of the pension point by less than 40 percent, putting the Romanian economy on a very dangerous trajectory, considers Cristian I. Popa, member of the National Bank of Romania's Board of Directors.**

"We are going through a public health crisis, an economic crisis, and we risk igniting yet another one: a public debt crisis. Putting in context the latest news is like playing with matches in the dark in a gas station. By context I mean the censure motion that would significantly reduce the government's ability to avoid a massive increase in public spending. So, once adopted, the censure motion would cancel the government's right to issue Emergency Ordinances, and without them, spending with pensions will increase by 40 percent as of September 1, which translates into a budget impact of 6 billion euros in 2021. Once granted, these pension rights can no longer be rolled back, and no, I don't think that governing and legislating through emergency ordinances is a healthy thing to do, that's why we have a Parliament; but in the midst of a pandemic, I can accept their legal nimbleness, given that this is the only way to avoid much more difficult situations," Popa writes on the BNR blog.

Cristian I. Popa sits on the BNR Board of Directors and is a member of the Board of the Romanian Chartered Financial Analysts Association.

The opinion published on Monday evening reflects the author's personal view and does not represent the position of BNR or CFA.

According to the cited source, if the current legislation remains unchanged, a few days after September 1 rating agencies will downgrade Romania to junk/not investment grade, and the country's financing costs would increase significantly.

"This is not a prediction, it is a certainty, it's a common sense observation. Romania's financing cost would increase significantly, and financing would be increasingly difficult to obtain, because we would become a risky debtor, with rising risks as regards the repayment capacity. It would also mean pressure on the exchange rate, because while certain lenders will only increase the interest rates at which they agree to loan Romania, others will 'shun' us, they will try to quickly sell their current local assets (including government securities) and to exchange their amounts in 'RON' for foreign currency to invest in other countries with better outlooks. And this not because they are bad people, but because Romania would become a risky country, a sub-investment grade state, not recommended for investment. Some may even be forced to sell their assets and exit Romania, as the applicable prudential regulations may require them to invest only in assets with a minimum 'investment grade' rating, therefore not in demoted Romania (think of a pension fund in Western Europe, for example)," Popa underlines.

He notes that before the pandemic, Romania's public debt was about 35% of GDP and with the increase of health and job-supporting expenditures, as well as with the shrinkage of the economy and budget revenues, the deficit exploded. At the latest correction this year the deficit was 8.6%.

"In this line, what was 35% will grow to over 50% in 2-3 years and with the current legislation on increasing pensions it would be just a matter of time until it exceeds 60%. The markets will not allow us to get indefinitely indebted. The investors have a simple approach: if we have the capacity to repay their loans without 'causing them headaches' they finance us, if not, they don't. And if we seem to be in the middle, so if we could repay but with some emotions (our repayment capacity is small or decreasing) then they will demand matching, high interest rates, because they take risks. And the truth is that without being sure of their repayment capacity, we would not

loan our acquaintances either," explains Cristian Popa.

According to him, investors also look at the health of the public budget and at how fast the deficits can be corrected, and the fact that fixed public expenditures accounted last year for 84 percent of the total state revenues means that 84 percent of expenditures are not under the state's control because they are either public sector wages or pensions, both of which cannot be cut.

Moreover, he mentions the lack of a serious discussion on sustainable pension growth while stressing that the pension system is not sustainable.

"(...) The public pension system is not an accumulation system, it does not have money set aside for the disbursement of future pensions (as private pension schemes do) but it transfers every month the contributions of the current employees to the current pensioners. So, in this (hypothetical but necessary) discussion, we should also mention demographics, emigration and the ageing of the population, but also the higher efficiency - in my opinion - of a private system of pensions with accumulation, which could give us a better chance of collecting 'pensions like abroad'. In the last 1-2 years, the question has been persistently put forward if money exists to increase pensions: running a deficit means that you are in the red, that you have to borrow, and Romania's deficit not only exists, but is unsustainably large and the Pension Office is also on deficit. So, is there money? The public pension system is not sustainable, it wasn't before the pandemic, and is even less sustainable now: with increases in benefits and lower contributions (yes, the private economy suffers, the unemployment rate is expected to grow, resulting in fewer employees and lesser contributions) its imbalance is gapping even more," Cristian Popa writes.

In the end, he explains that through the censure motion, the policy makers eliminate all possibilities of increasing the pension point by less than 40 percent, which will generate major imbalances that will have to be corrected in the coming years.

"By blocking the government's right to issue OUGs, through censure motion, the political decision-makers knock out any possibility of adjusting the increase of the pension point by less than 40%, putting the Romanian economy on a very dangerous, costly and risky trajectory, generating major imbalances that would be difficult, painful and mandatory to correct in the coming years, and also putting financial stability at risk. The political forces should cooperate to avoid such a scenario but the electoral reality is that it's exactly them that have brought us in this situation. There is, of course, one last possibility, sprinting between the motion and the OUG; we will see on August 31 whether a potential OUG issued before the motion still 'stands' and is not invalidated by Parliament.

To me, this is very clear: we are playing with fire! Even dangerously. The only question is whether we will return to reason or will drop the burning match on the ground, the future of this country depends on this," concludes Cristian Popa.