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# FLORIN GEORGESCU: A NEW OUTLOOK ON ROMANIAN CAPITALISM

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## Abstract

In 2021, the Romanian Sociological Association awarded economist Florin Georgescu its Award for Excellence. This essay covers the author's magnum opus, titled *Capital in Post-communist Romania*, and focuses on the content most relevant to sociology. Unique in size and scope, the approximate 1,000 page three-volume book features three books in one: a 30-year economic history of Romania, a critical analysis of the way the Romanian capitalist economy developed in the second half of the 2010s, and a blueprint for structural reforms to foster development and reduce inequality. The essay includes a short author presentation and an overall review of the book's contents, an appraisal of the work's style and originality, and a review of the themes and subjects most salient for sociologists: capital – labour relationship and the distribution and redistribution system, income and wealth inequality, precarious work, the transition and privatisation processes, structural problems of capitalism, and development policies.

Keywords: Romania, capitalism, transition, market economy, labour, income inequality.

## Introduction

Over the past three decades, Romanian academia – economists, sociologists, political scientists – have written about subjects such as the transition from a Soviet-model economy to a market economy and development issues. Florin Georgescu, a leading economist, has published *Capital in Post-communist Romania* (2018), a book that, in the words of Andrei Marga (2019), is “an unprecedented work of Economics”. In late 2020, the book was awarded the prestigious “Petre S. Aurelian” prize of the Romanian Academy in economics sciences. In early

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2021, the Romanian Sociological Association recognized its outstanding scholarly contribution and awarded its Award for Excellence.

*Capital in Post-communist Romania* makes a first impression to the reader through its appearance: an elegant, full colour, three volume hardcover set. Usually, writing an essay or a review a book approximate 1,100 pages long is in itself a challenge. However, beyond its size, what makes it particularly daunting is the sheer volume and variety of themes and subjects, including original research data. In fact, we are dealing with three books in one: (1) a 30-year economic history of Romania, (2) a critical analysis of the way in which the Romanian capitalist economy developed in the second half of the 2010s, and (3) a blueprint for structural reforms to foster development and reduce inequality. By size and scope, this is a unique work. As there is so much to say, this essay will try and focus on the content most relevant to sociology and is structured as follows: (1) a short author presentation and overall review of the book's contents, (2) style and originality, and (3) review of the themes and subjects most salient for sociologists.

### **Author background and book structure**

Florin Georgescu has a deep understanding of the Romanian economy. As a bright young academic in the early 1990s, he won a prestigious position as a Fulbright Fellow and then became one of the youngest finance ministers in his country's history, aged 39. Since 2004, he has been the First Deputy Governor of the National Bank of Romania, the second highest position in the central bank. In 2012, he had a second stint at the Ministry of Finance, guiding the country through the exit from the 2009-2010 recession and yet another IMF loan. He has also pursued an academic career as professor of public finance at the Bucharest University of Economic Studies. Thus, as a former policy maker, central banker, and academic, Florin Georgescu is, in the words of Lawrence Summers, an insider (Warren, 2014; Varoufakis, 2018), but one with a critical outlook.

As befits a central banker and finance minister, the book is neatly organized. Each of the three volumes comprises three chapters, with the last volume also including a fourth, smaller chapter. Titled "Conclusion", this last chapter is a 100-page expanded summary of the three volumes. This final chapter targets the reader that does not have the time to read the entire book, but is interested in its overall content. In addition, each chapter features its own concluding section billed as "final remarks". The author seems to be aware of the fact that most readers no longer fully read books, especially academic books, but focus on their (sometimes narrow) areas of interest. In fact, the nine chapters could stand on their own, although they are larger in size than a journal article (only chapters one and ten are around 100 pages or lower) and are clearly interlocked as part of a larger design.

The book starts with an introductory chapter on capital, which deals with the basic concepts, but also the peculiarities of the (re)emergence of capitalism in

Central and Eastern Europe. The following three chapters (2-4) cover the main subject of the book, capital, under its different guises: equity capital, fixed capital, and financial capital. This part of the book is more microeconomics oriented, with a focus on the real economy and its vulnerabilities. The following chapters deal more with Romanian capitalism through the lens of economic history and policy. Chapter 5 looks into the relationship between labour and capital. Chapter 6 is the most historical and deals with the privatisation process during the transition period from a command, Soviet-type economy to capitalism. Special attention is paid to the relationship with the IMF and the World Bank, as institutional authors of the privatisation focused transition strategy. Chapter 7 covers Romania's EU accession and whether EU funds perform well as a source of capital and development. Chapter 8 is also more historical and deals with globalisation and deregulation as worldwide processes that influenced the transition period. Chapter 9 looks into the economic and social development of Romania through recent history, the current status of the country and its challenges, including the middle-income trap and entrenched inequality. Through its structure, themes and subjects, clearly this is a book for a diverse range of readers: students, academics, policy makers, but also the general readership with an interest in economics and policy.

### **Style and originality**

*Capital in Post-communist Romania* is written in a very accessible language. A person with a basic knowledge of economics would have no problems understanding both the microeconomics- and the macroeconomics-oriented chapters. The author guides the reader even on the more technical issues in the work from balance sheet and operating cash flow categories, to arcane labour regulations, and even the historical peculiarities, such as the crisis of the Soviet-style economy in the 1980s or privatisation laws.

That being said, people that have had the occasion to attend a lecture delivered by Mr. Florin Georgescu will discover differences between the public speaker and the writer. While Mr. Georgescu is arguably the best public speaker on macroeconomics – and was a pugnacious, witty debater in his career as a Member of Parliament –, his writing style comes across as more subdued. Especially in the concluding remarks sections, one could almost read through the lines and feel the central banker who wants to avoid controversy. While it has clarity, the writing style sometimes comes across as more impersonal, less dynamic, and with a somewhat diminished force of argument than the author's speaking style. In this clash of styles between the professor and the central banker, it seems that the latter got the upper hand.

The real intellectual added value comes not from the book's 1,000+ page size, but from the quality and quantity of data on which the analysis is based. *Capital in Post-communist Romania* stands out due to its unique data sources and the

outstanding level of scholarship behind them. To say that the three-volume book is full of macroeconomic and microeconomic data compiled and calculated by the author does not do it full justice. The amount of data used in this book that comes from original research by the author stands out. Moreover, Mr. Georgescu operates with the ease of a virtuoso with the multitude of data sources that go beyond public data available from Eurostat or national statistics authorities. Data from administrative sources such as the consolidated database of legal persons' (companies) balance sheet statements, natural persons' tax returns, bank deposits' breakdown, privatisation revenues and use of privatisation funds, breakdown of labour contracts by type and duration, breakdown of restitution payments and compensation in kind for property seized by the former Communist regime, to name just a few, are all marshalled in the analysis. The book also features an insightful legal and policy analysis into some of the key controversial laws and regulations in the functioning of the economy and the redistribution of wealth and income, such as privatisation law, enterprise law, the labour code, and tax law, but also IMF and World Bank agreements, to name the most salient. Overall, even the seasoned, academic reader is overwhelmed by the sheer amount of data, facts, and arguments based on them.

Looking at the book and its empirical material through a different lens, one could trace back the resume of the author. It seems that throughout Mr. Georgescu's career in public life, including the central bank, he has also pursued academic goals, collecting unique data, out of the reach of ordinary researchers. It is as if all the academic chips collected through a lifetime in key institutions were placed on the table for one gamble at a defining work. Only an academic with a passion for knowledge and thirst for answers would use his position for such a unique endeavour.

### **Labour vs. capital: who has the upper hand?**

The share of employees' earnings in GDP is markedly lower in Romania than in Western, developed economies (437-440). Moreover, labour's share saw a further decline during the 2009-2010 recession and its immediate aftermath. In the mid-to late 2010s, labour's share recovered somewhat, due to more jobs and the policy to increase the minimum wage. Even so, Romania is third last in the EU, very close to Greece and above Ireland. Overall, this is caused by structural changes in the economy, especially the loss of skilled, better paid jobs in manufacturing and their replacement with predominantly low skill, low pay jobs in the service sector, especially trade, tourism, and restaurants (441).

Georgescu focuses on the path from economic output to wage and profit. The reader is introduced to the terminology and methodology behind this calculus. The first finding is that intermediate consumption, which depresses both profits and wages, is 5% higher than in developed economies (444). The causes include

lower economic complexity, but also practices ranging from transfer pricing to unjustified expenses for goods and services, in many instances with no connection to a company's core activity, but for the personal benefit of shareholders and company administrators. These practices, which are pushed to the limit of the law or even beyond, reduce the profitability of companies (444-445). Another point in this analysis is the increasing gap between the gross domestic product (GDP) and the gross national income (GNI). Romania features a lower GNI to GDP ratio than other former socialist countries. This is relevant because GNI is more strongly linked to the standard of living than GDP (448-449).

The share of labour compensation in various economic indicators – GDP, core GDP, gross and net added values, adjusted net added value, and net national income – is calculated by the author. The overall picture is the same: a significant reduction of labour compensation in favour of capital, and a much lower share of labour compensation in Romania than in Western and neighbouring countries, such as Poland and Bulgaria. The share of labour compensation ranges from the low 30s of GDP to 50% of the adjusted net added value. Moreover, the return on capital is 10% in Romania in 2016, compared with 5% in France and Britain, where the labour – capital relationship is more balanced (449-460).

To find out why the labour – capital relationship is so unbalanced in favour of the latter, the author looks into the distribution and redistribution mechanism of newly created value. The overview of the role of the state in both phases is a textbook example of clarity and a must read for all students and researchers in social policy (460-461). The detailed policy analysis that follows includes all categories - fiscal, social, company and labour law, etc. - and is second to none. An impressive array of irrefutable facts and figures supports the statement that “the state advantaged capital and weakened the bargaining power of labour” (460). Georgescu pays special attention to the policy response to the 2009-2010 recession. The outcome was the *precarisation* of labour and the consolidation of capital through various policies, such as more part-time and fixed-term work contracts and other labour market deregulation measures, reducing the ability of workers to form or maintain unions, stripping away bargaining rights through labour legislation, especially by cancelling the national collective agreement, freezing the minimum wage, etc. One of the end results: the unionisation decreased to 21.5% and just 10% in the private sector, down from 80% in 1991 and 35% in 2008 (461-471).

The author sums up the effect of all these policies through an original calculus of the economic cost of recession and policy adjustment, from 2009-2011: labour lost 12.2 billion euro, while capital lost 0.7 billion euros, a breakdown of 95 to 5 out of 100 or 17.4 times more for labour than capital. During 2012-2016, after the crisis subsided and the economy returned to growth, capital's share in the new added value continued to be lopsided due to policy: 16.3 billion euro for capital, 29% more than the 12.6 billion euro for labour (471-473).

The sustained wage growth of the mid to late 2010s brought about a public debate. Critics pointed out to an alleged loss of competitiveness and increase of wages above productivity. Once again, Georgescu brings forth irrefutable facts: hourly labour costs in Romania are just 21.6% of the EU average and 63.9% of Poland; the gap between labour productivity and hourly labour costs marginally increased from 2008-2016, despite wage growth during the latter part of the interval. Despite the increase in wages, the economy added some 700,000 jobs during 2012-2017. The author stresses the gap between price (higher) and wage (lower) convergence to the EU level: in 2016, prices were at 52% of EU average, while hourly labour costs lagged far behind at just 22%. Despite the increase in the purchasing power of wages, the gap compared to regional peers remains substantial (10% vs. Poland and Hungary) (475-479).

One of the major contributions of the work deals with income and wealth inequality. The author makes the analysis to showcase the results of the abovementioned policies on distribution and redistribution. Using data from the Ministry of Finance database of all individual (natural persons) tax returns from the early 2000s, when income tax law required universal tax returns, the author notes that income inequality was high even before progressive taxation was abandoned. In 2004, the top 20% highest income earners totalled 54% of all taxpayers' incomes, while the top 10% got 37.9%. The introduction of the flat tax regime starting in 2005 increased income inequality: 10% of taxpayers gained 40% of the total earnings from the tax cuts.

Wealth inequality is analyzed through the best available proxies. First, the bank deposits breakdown is revealed, through administrative data from the deposit guarantee scheme. In 2016, 76% of bank depositors owned just 3.6% of the 143 billion euro in deposits, while 1.63% owned 40%. The top 0.13% owned 14.4% of all household deposits. Another spectacular first is the data on wealth redistribution through the restitution and compensation for property seized by the former Communist regime, which once more comes from administrative data. The total cost of *restitutio in integrum*, as the process was called, totals 20 billion euro, out of which 5.5 billion in cash or shares, 5 billion in future compensation, and the rest restitution in kind in real estate, farming land and forests. All this wealth was distributed to a small number of Romanian citizens and foreigners that put forward claims for compensation for property nationalised by the Communist regime (479-490).

Georgescu takes a closer look at how fiscal policy could reduce income and wealth inequality. The former finance minister notes that, in the future, Romania will require more government spending for public services, especially healthcare and education, and infrastructure, but government revenue, especially fiscal revenue, is alarmingly low. Moreover, Romania is on a divergent path from the EU as a whole. In 2016, the average fiscal revenue in the eurozone was 41.3% of GDP, whereas in Romania it was just 26%, a 15.3 percentage point difference. Moreover, whereas the EU trend for fiscal revenue saw a marginal increase from

39% to 40% of GDP in the mid to late 2010s, in Romania the trend was opposite, a decrease from 29% to 25.9%. Closing the gap of 15-percentage points of GDP compared to the eurozone would require action on two fronts. First, improving the tax collection process by cracking down on tax evasion; Georgescu argues that this could yield a maximum of 6 percentage points of GDP and it will take some time. Still, there remain 9 percentage points to close the gap. Therefore, the second front is an overhaul of the tax system. Georgescu calls for income tax reform. Since the Ministry of Finance lacks data on income and wealth distribution to formulate policy, Georgescu advocates the (re)introduction of yearly tax returns on all income for all taxpayers, seconded by an asset return, especially for real estate. Once the data is collected, Georgescu recommends discarding the flat tax regime and a return to progressive brackets for the income tax, and progressive taxation of wealth.

### **Transition, privatisation, and their discontents**

One of the major themes in Romanian sociology in the 1990s and 2000s was the emergence of capitalism through the transition period. Based on original research data, Georgescu delivers a definitive account of the privatisation process as the key part of the wider transition process.

Chapter 6 starts with an analysis of the economic crisis of the command economy system during the 1980s. Once again, Georgescu's builds upon the contributions of leading economists from a previous generation (Dobrescu & Postolache, 1990; Ionete, 1993; Văcărel, 2001) by adding new, original insight into the structural problems of how the Soviet-type economic system functioned in Romania. Two points in particular are worth mentioning here. The author argues that the 1982 balance of payments crisis could have been handled within the limits of economic policy, without resorting to austerity. Second, the flaws or rather the faux in the planning processes are revealed in detail. Although official ideology claimed that the economy was run via a scientifically developed plan, major planning decisions were, in fact, arbitrary, in some instance at the whim of dictatorship. These decisions, which disregarded facts and real capabilities, degenerated into "lies" in the material balance sheet which underpinned planning. As a result, enterprises were trapped in a quasi-permanent default, unable to accomplish the planned output targets. The overall picture of an economy clogged and mired in structural crisis during the final years of the Communist regime is vivid and compelling. On top of this structural crisis was the decision by the dictatorship to pay the foreign debt in full and ahead of schedule, which added more harm to the economy (520-530).

The fall of Communism was followed by a freefall of the economy everywhere in the former Soviet bloc, including Romania. The 1990-1992 period saw a collapse of output, with domestic demand outpacing GDP, a collapse of exports,

and fiscal and foreign reserves crises. In these circumstances, Romania faced a quasi-permanent dependence on support from the leading international financial institutions (IFIs), the IMF and the World Bank, due to lack of confidence from private capital markets throughout the transition (535-540). Inside the former Soviet bloc, Romania was disadvantaged compared to Hungary, Poland, and the Czech Republic. Their starting position was more competitive and benefited from continuing capital markets financing. “A serial IMF borrower” (781), Romania had a poor bargaining position in the negotiations with the IMF and the World Bank. In exchange for its financial support, the IMF demanded neoliberal policies.

Georgescu makes a compelling case, based on Western sources from leading economists and IMF officials at the time, that there were two competing models or strategies for the transition to a market economy, i.e. capitalism: gradualism versus radical free market, “shock therapy” reforms. Here, the author makes a very important factual point. In the first part of the transition (up to 1997), Romania opted for the gradualist approach. Georgescu argues that it was the only sensible strategy after the austerity of the 1980s, since there was no support from the population for another “shock therapy” because the population had already endured another “shock therapy” in the 1980s in order to pay the foreign debt in full and ahead of schedule.

Georgescu delivers what is arguably the most in depth coverage, anywhere in the specialty literature, of Romania’s relationship with the IMF and the World Bank during the transition, based on a forensic analysis of loan agreements, economics indicators, policies and laws enforced at that time (542-570). Once more, the scholarship is outstanding and built upon previous contributions (Văcărel, 2001; Stănescu, 2014). Two points stand out. Privatisation was “the essential pylon of structural reforms” pushed by the IMF and World Bank, itself a follow-up of the policies from the Reagan-Thatcher era of the 1980s (580-582). Moreover, IFIs were very austere towards Romania throughout the transition. The net foreign financing provided by the IFIs was just 190 million USD on average per year during 1990-2004. The author stresses the asymmetries in the IFIs treatment of Romania: just enough “oxygen” to keep the economy alive during the 1990, especially from 1994-1996, in order to bring about the further contraction of state-owned enterprises versus a “full oxygen” treatment for the same economy, but now dominated by private enterprises, during the post-transition recession of 2009-2011, this time in order to prevent capital losses for private entrepreneurs and foreign private lenders (561-565).

The core of the chapter deals with the privatisation process. Georgescu makes the case that the opportunity to maintain important and viable companies and sectors for the real economy was lost. One example was the 1997 ASAL loan from the World Bank, which led to the liquidation of the meat production companies. As a result, the livestock and the meat industry never really recovered. Since then, Romania has remained a long-term net importer of meat, despite its potential. The detailed, forensic analysis of the privatisation legal framework reveals a

gradual relaxation in favour of investors. Arguably the most interesting part is the evaluation of the sale of state-owned enterprises (SOEs), the revenues, and their utilisation. Once more, the author uses original research data from administrative sources. Romania raised 7.1 billion euro from the sale of 8,200 SOEs over a 26-year interval. The average sale price was 866,000 euro, or 592,000 if the one-off sale of the largest bank is discarded from calculation. This is the price of a luxury apartment in Bucharest. Yet another first of the book is the breakdown of privatisation funds usage: 5.7 billion euro are still in the Treasury, 0.4 billion euro were the overhead costs of the privatisation authority, 0.4 billion euro were various pre-privatisation and privatisation expenses, 0.6 billion compensation for former owners and other budgetary expenses. Georgescu argues that the use of the privatisation receipts was inefficient.

The outcome of the privatisation-led transition strategy is reviewed *via* an evaluation of the post-privatisation economy. The scale of the deindustrialisation process is fully revealed via a comparison of physical output. After nearly three decades, industrial output was 70% of the 1989 level in 2016. For instance, 90% of the chemical industry was wiped out. The share of high-tech products in total imports doubled to 12%. Georgescu charges policy makers with ignoring industrial policy. The overall effect of deindustrialisation is that the main sectors of the economy are unable to create gross added value to meet the country's development needs and to increase living standards. The status of a deindustrialised, underproductive economy is stressed by the dynamic of firms specialized in civil engineering demolition. The scale of their activity and the deindustrialisation process is showcased by the export of 35 million tons of scrap metal, equivalent of a 42,000 km long train, 5% more than the equator. These massive scrap metal exports came from factories and plants built through heavy toil and sacrifices by Romanians during 40 plus years of Communist regime (615). On the ground, deindustrialisation is vividly showcased with tables of former plants and factories in and around the capital city, which were turned into malls, housing, and office buildings or could do so in the future (623-626).

In the post-privatisation economy, the real sector is dominated by large, multinational corporations. Much of the data from this section overlaps with the content from chapters 2-4, a point to which we will return. Out of the 1,700 active corporations in 2016, 772 foreign capital corporations totalled 30% of the turnover and 28% of the gross added value in the economy. The post-privatisation manufacturing sector is unable to meet internal demand, leading to a structural balance of payments deficit. The service sector is expanding in the new economy, but with a low level of complexity and gross added value. The author concludes that this trend will be unable to deliver sustainable growth and development (628-629). Another key trend is the persistent low rate of capital accumulation, even after privatisation (629-631). The review of stock exchange listings further reveals the underdevelopment of Romanian capitalism. Just 7 of the 71 real sector companies listed on the Bucharest stock exchange are private companies founded

after 1989. Their overall performance is modest: 4% share in the turnover of all listed companies, 7% of the market capitalisation. The vast majority of listed companies are state-owned (9) or formerly state-owned companies (62). Georgescu notes that the low interest of shareholders for listing their companies could only be justified through the option of entrepreneurs to avoid transparency, corporate governance, and financial discipline standards imposed by the status of being a stock exchange listed company. Conversely, financing day-to-day operations of private enterprises is done mainly by creditors, either transparently by banks or by “wild commercial credit” from suppliers or by withholding tax payments, due to the inefficiency of the revenue service (631-640). International comparisons with other countries in the region complete the picture of the scale of deindustrialisation. After privatisation, the share of industry in the gross added value is lower in Romania compared to the pre-privatisation era, unlike in Poland, Hungary, and Czechia. One final remark on privatisation is that “if it was not a failure, it was certainly unsuccessful” (665).

## **Development issues and the middle-income trap**

Chapter 9, which deals with development issues and challenges, is also highly relevant for sociologists. This chapter fits best with the sub-book focused on structural reforms and development.

Georgescu picks up from where he left off in chapter 6, which covered transition and privatisation. Starting with 1990, the author sees a deep political and economic paradox unfolding. The electorate voted for the reforms and policies in political parties’ manifestos, but at each election cycle it rejected the previous government, due to deteriorating living standards. The electorate’s discontent stemmed from the contradiction between the promises for a better life in the manifestos, which were in accordance with the electorate’s aspirations, and, on the other hand, the real policies once in government, which, in accordance with the IMF and World Bank agreements, became much more austere compared to the manifestos. Georgescu quotes Zbigniew Brzezinski, who argued the same idea independently put forward by Romanian sociologists such as Cătălin Zamfir (2004), namely that the high social costs of transition was caused by the unpreparedness of the West when Soviet-bloc Communism collapsed and it scrambled to react in terms of policy.

Georgescu is also in line with the idea of some Romanian sociologists that the transition ended somewhere in the mid to late 2000s (Pasti, 2006; Stănescu, 2014; Zamfir, 2015). He places this moment in 2007, “after 17 years of intense efforts and high social costs”. The author sees two trends in society afterwards: prolonging the transition in order to correct it versus the *status quo* approach, namely preserving the results of the transition. The former is desired by a majority of citizens dissatisfied with the results of the transition; the latter is the option of social groups, small in numbers that benefited the most from how the transition

unfolded. He concludes that one thing is certain: the transition is over, and the current state of society is the basis from which one could start to build a better future. In other words, the transition's legacy, i.e. the 1990s and part of the 2000s, and not Communism's legacy, i.e. the 1950s to 1980s, is the right frame of reference for the debate on development policies (821-825).

Georgescu sees ideology as the base for the vision on development – a very sociological remark. The author makes a conceptual distinction between two approaches to development. The first is the economic or economics-based approach, which is focused on a country's performance, measured by GDP per capita; this approach sees development as a function of economy's capacity to generate a high level of GDP. According to this line of thought, social sustainability is implicit, based on the assumption of trickle-down. This is the conventional approach. The second is the "sociological approach", which highlights wellbeing and quality of life. This non-conventional approach sees development as the upward movement of the entire social system, through improving living conditions and the socio-economic structure of a country. Georgescu presents to the reader an overview of Romania's development through both the conventional and the non-conventional approach. The latter features indicators such as the World Bank's GNP per capita at purchasing power parity, the UNDP's human development indicators, and the EU Commission's sustainability indicators. In addition, special focus is given to the primary distribution between labour and capital and the redistribution system (840-853).

In Georgescu's analysis of the growth – development correlation in Romania, development is significantly slower than economic growth. In turn, this is caused by a relatively poor quality of growth and major deficiency in GDP distribution due to clogging of primary and secondary distribution channels, as an effect of the asymmetry of lax legal framework, payment indiscipline, and illegalities in society. The author sees the causes of the current status of Romania as a peripheral country in the EU not in the country's brand and institutional problems, but in the deep characteristics of the economy and society that place Romania closer to the states with a lower-than-average development level, and not at the side of the developed countries (854).

This is because the authorities fail to translate economic growth into better living standards and conditions. This is why Romania is next to last in the EU in terms of social progress. In turn, the population's dissatisfaction with living standards is fully justified: the relationship between economic growth and development, including poverty reduction, is fractured by an economy with performance below the aspirations of the citizens regarding the standard of living; indiscipline of payments, massive capital deficit of companies, tax evasion, corruption, massive income and wealth inequality (872-873). These considerations are based on and overlap with the findings from chapters 2-4, the more microeconomics oriented, with a focus on how the real economy and the private sector perform.

Based on ongoing trends, the author argues that there are worrying indications that Romania is in the risk zone for the middle-income trap. The economy registers unfavourable situations for six out of eight criteria in the scientific literature. A parallel is drawn with Portugal, a prime example for an EU member state in the middle-income trap, based on various economic and social indicators (864-871).

On the relationship between capital and development, Georgescu points to the increase of the deteriorating debt to equity ratio (see nature in Romanian capitalism section) in the private sector. This shows, in his view, that the Romanian market economy was developed and continues to be based mainly on debts and not on capital, as is natural in a capitalist society. (860)

Georgescu concludes that development is not the automatic result of EU integration, access to EU cohesion funds or foreign direct investment (FDI) (a critical review of EU structural and cohesion funds is found in chapter 7 and of FDI in chapter 3, section 4). Therefore, it would be necessary to raise the awareness and responsibility of decision makers that economic development is not a gift from abroad, but a product of Romanian society. The author believes that, in order to ensure a sustainable development process, it is necessary to change the paradigm, to move on from the currently dominant approach, focused on demand control policies, to the development of effective sectoral policies to stimulate supply (output). As a central banker in a globalized world, Georgescu is careful to add that such an attitude shows rationality and economic responsibility, and not nationalism (873-878). The chapter ends with a preview of the blueprint for structural reforms that is put forward in the book's last chapter.

### **The nature of Romanian capitalism**

In the manner of Romanian academia, the first chapter of the book deals with "the theory" - capital as a concept and its formation in post-communist Romania. While it is the least original chapter of the whole book, it sets the stage for the bulk of the analysis and findings that follow. Georgescu sees the emergence of Romanian capitalism in the overall trend of the transition in Central and Eastern Europe. Citing international and Romanian sociological and economic literature, Georgescu identifies three key traits of post-communist capitalism: (1) its top-to-bottom emergence, instead of the natural, organic bottom-up emergence in the West; (2) that it was built by relatively few social groups; (3) it was not based on individual capital accumulation over a long period of time, but rather redistribution of state property, owned by all citizens, in favour of a reduced number of individuals, based on arbitrary criteria lacking transparency and over a relatively short period of time. Georgescu concludes that the peculiarities of the Romanian society that emerged from the transition points to an atypical, hybrid kind of capitalism (29-30).

Chapters 2-4 deal with the main subject of the book, capital, under its different guises: equity capital, fixed capital, and financial capital. While this is the more microeconomic part of the book and might be less appealing to the sociological or casual reader, it reveals key features of the Romanian economy and post-transition capitalism.

First, Georgescu stresses the crucial distinction between capital and money (as in wealth): the entrepreneur transforms part of his wealth into capital, which implies a long-term commitment and a risk. The overall capital stock reveals the “power” ranking of an economy. In Romania, the capital stock was 120 billion euro in 2016, up from 22 billion euro in 1997. Non-financial companies had a share of 72% in the capital stock, while financial companies 21% (74-75).

The breakdown of the capital stock in the real economy (non-financial companies) by type and place of origin is revealing. Structural change has occurred during the transition from a command economy to a market economy. This is obvious from the share of state-owned enterprises in the capital stock. Over a 20-year period (1997-2006), it decreased from 55% to just 12%; in terms of number of companies, from 4,700 to 1,500. However, the key fact is that private domestic capital was not the big winner: its share increased by less than 5 percentage points (p.p.) over the almost 20-year interval, from 36% to 40%. The major winner was private foreign capital. Its share jumped a whopping 39 p.p. from 9% to 48%.

A second main finding is even more disturbing: the low profitability of the private sector enterprises, especially private domestic capital. Contrary to economic textbooks and prevailing thought, losses increased at a higher rate in the private sector than in the state sector. The average loss per employee was up by 3.5 times in the private sector and just 2.5 in the state sector during 2000-2016. During the same period, profits increased at a lower pace in the private sector: the average profit per employee was up just 6 times, compared to 7.4 times in the public sector.

The real sector is underdeveloped compared to the size of the Romanian economy and other European countries. 98% of registered companies are limited liability companies, most of them with a short lifespan and low technology basis. Young enterprises are dominant: over 39% of the 634,500 active companies that filed balance sheets in 2016 were less than 5 years old. At the other end, less than 10% of companies were older than 16 years and reported a profit. The business model of private domestic capital companies features a low technology and knowledge capability, low productivity, and low added value. Private domestic capital enterprises comprise 91.5% of the total number of enterprises, employ 65% of the labour force, and yet deliver only 48% of the total added value in the economy. 98.4% of these enterprises are LLCs. At the other end, private foreign capital enterprises comprise just 7.2% of the total number of enterprises, 27% of the labour force, and deliver 44% of the total added value. Foreign capital also plays a leading role in the knowledge intensive services: despite being just 6% of

the total number of the enterprises in the sector, they secured 46% of the turnover and 48% of the total added value in 2016.

Structural changes in the economy during the transition led to a high degree of concentration of financial resources and economic activity. In the late 2010s, the economy was dominated by a small number of firms, while many companies play an insignificant role in GDP formation. In 2016, the top 1% of companies (6,345 companies, of which 2,635 with foreign capital) had a 67% share in the gross added value and employed 50% of employees. Based on a wealth of data from the real economy, Georgescu stresses the lack of vigour of domestic capital and the concentration of economic activity in general, and the most technologically advanced portions of it, in particular, in companies with foreign capital. However, many foreign capital companies do not have a sustainable economic behaviour: 37% had no income (turnover), 52% no employees, 48% negative shareholders' equity. The breakdown for domestic capital companies is: 25% no income (turnover), 41% no employees, 42% negative shareholders' equity. Economic data points to practices such as "fiscal optimization", transfer pricing, and losses registered in Romania by the same multinationals that are in the black in other states in the region (84-97).

The debt-to-equity ratio in the economy is deteriorating. From 0.3 in 1994, the indicator reached 2.1 in 2016. During 1994-2016, companies increased their income six times and their equity only 30%, whereas total debt increased 10 times. Analyzing the financing model of current operations, the author finds that Romania-based companies do not have enough equity to ensure a viable business model, favourable to an activity with a high degree of complexity, likely to generate high gross added value, which, in turn, could support higher salaries and profits. For instance, the debt-to-equity ratio was 1.0 for corporations in 2016, but reached an all-time high of 42 for microenterprises (99-107).

An analysis of the equity breakdown from 2000-2016 reveals that, in Romania, a majority of investors are looking for short-term gains, without a vision for the sustainable development of their companies, which is seen in the minimum level of capital injections and chronic divestment *via* losses and massive distribution of dividends (110-117).

Special attention is given to financial results and payment discipline. The author finds that one in three active companies (that filed a balance sheet) registered a loss in 2016. Low profitability compounds the low level of capital stock in the economy: 48% of firms had less than 1% profitability in 2016; the return on assets (ROA) was 1.7% compared to 7.5% in Poland and 6.7% in Germany. A detailed picture of losses in economy by company type is revealed. Surprisingly, the share of the private sector in total losses actually increased from 56% in 2000 to 90% in 2016. The author concludes that the transfer of ownership from the state to the private sector has, in reality, led to a worsening of the efficiency of resource allocation and to the quasi-generalization of payment indiscipline. The

improvement of the company debt to GDP ratio after the 2009-2010 recession was based on higher GDP and not in the reduction of outstanding debt. Out of the 7.3 billion euro in losses of non-financial companies in 2016, private sector companies' share was 6.6 billion, equally divided between domestic and foreign capital. However, the latter are fewer, so the average loss per foreign capital company is nine times higher (117-129).

Payment discipline is deeply flawed in the Romanian economy. Payment term for suppliers was, on average, 116 days in 2016; it increased to 150 days in early 2018. In comparison, it is 41 days in Poland and 19 days in Germany. Only 26% of companies pay their suppliers in time. A forensic analysis points to weak or unenforced legislations that need to be improved. Overall, the dysfunctions in the money circuit in the economy highlight the lack of a solid culture of Romanian companies regarding the observance of payment discipline and economic contracts. The author finds that the transfer of capital from the state to the private sector not only did not lead to superior performance of the business sector in terms of profitability and resource efficiency, but also failed to strengthen the discipline of payment in the economy. Private companies represent the most undisciplined category of companies with arrears of 17.9 billion euro, 80% of total arrears, equivalent to 11% of GDP in 2016 (129-139).

Georgescu concludes that Romania features totally atypical situations for a functioning market economy: persistent losses, inadequate capitalization, companies that carry on without income and without employees. In other words, the fundamentals of the market economy are severely distorted. The quasi-generalized inclination to conduct business with "other people's money", the frequent practice of "scheduled insolvencies" (bankruptcies) demonstrates the existence of a totally inadequate legal framework. "Profoundly abnormal situations, contrary to market economy principles" showcase the premeditated behaviour of shareholders to keep their own companies on the verge of survival, without the will to increase the competitiveness, value and financial capacity of the company (199). The Romanian market economy does not work according to the principle of private gain, public profit, but rather private gain, public loss. (862).

The newly formed private sector after the fall of Communism, which comprises over 88% of the business sector in 2016, reproduces to a greater extent the losses compared to the profits of the former state sector. The author notes that the change in the form of ownership was not reflected, as economic theory predicts, in increasing employment and the profitability of firms based on a more efficient allocation and use of resources in the economy.

Romania's economic structure is one with a weak orientation towards productive sectors. Sectors that generate low gross added value are predominant, i.e. less complex, a low level of knowledge businesses in trade, transport, real estate, etc. For the economic and social development of Romania, it is necessary for companies to advance towards the upper phases of the value-added creative

chain. Labour market developments follow the economic structure and support the conclusion that the private sector in Romania lacks the ability to achieve a high level of employment and acceptable incomes, which caused labour migration for many Romanians (more than 3.4 million people), especially after EU accession.

Georgescu stresses the weak entrepreneurial culture: low appetite for risk and for assuming specific business responsibilities, long-term preservation of monopolistic positions enjoyed by many “rent hunters” (rent seekers), manifestation of large-scale payment indiscipline, and tolerance by authorities of hundreds of thousands of companies with equity capital below legal thresholds. Unlike their Western counterparts, Romanian capitalists seem less inclined towards capital accumulation, but rather wealth, even at the expense of their own firms’ profitability and sustainability.

This state of the Romanian economy is all the more worrying, the author argues, because no economic and social system can function indefinitely if it is not based on truths. Georgescu thinks that the manifestation in the market economy of weak budgetary constraints, in the context in which the freedom enjoyed by entrepreneurs is at very high levels is a contradiction and a fundamental ideological inconsistency, which leads to a totally atypical market economy, namely a hybrid capitalism. The overall result is a political and economic system that operates with an abnormal combination of political liberalism and a type of economic communism partially adapted to the requirements of the market economy (socialization of responsibilities). Georgescu concludes that in Romania there is no aversion to loss, but, abnormally, to profit. This behaviour is possible because in Romania there was “privatization of freedom” and “socialization of responsibility” (197-210).

## **What is to be done? Policies for the future**

Returning to the opening assertion that *Capital in post-communist Romania* is three-books-in-one, let us turn to the third book, namely a blueprint for structural reforms to foster development and reduce inequality. Unlike the other two “sub-books”, this one does not stand alone in one or more chapters. Policy recommendations are to be found in almost every chapter, especially in the concluding remarks section, but arguably more so in chapter 9, which focuses on development. However, it is the last chapter, entitled Conclusion, which also functions as an expanded summary of the entire three-volume book that features the policy recommendations most clearly.

Georgescu starts by noting that the emergence of capitalism and the market economy in Romania could only lead to a society with many imperfections and imbalances. This is because of the decisions taken in the transition period – the transition strategy and its execution. An adjustment is required. However, this adjustment cannot be made, on a rational basis, by annulling or amending the

millions of decisions, taken years of even decades ago, that have led to the current distorted market economy, although many of those decisions were immoral and some even illegal. Under the aegis of the goal to ensure the durability of Romanian capitalism and social cohesion, Georgescu calls for more transparent redistribution *via* fiscal policy.

The author places the real fault line in the policy debate for the future between transformative change – some sort of transition 2.0 – and *status-quo*. The millions of citizens that lost out during the transition and/or are discontent with its outcome would be in support of the change option. On the other hand, the numerically small groups of transition winners, that took advantage of the weak state and benefited from subjective, non-meritocratic methods in state asset distribution, would be in favour of *status-quo*.

Georgescu puts forward a “national project” – a misnomer of a national development goal or narrative in the parlance of Romanian talking heads – in the form of eurozone accession. The author lists all the major failures of the Romanian market economy and provides policy solutions. Noting that euro accession could only take place through “a solid partnership” with the EU Commission and European Central Bank, Georgescu calls for two major policy changes.

First, firmly carrying out structural reforms to boost potential GDP growth and especially production factors (capital, labour, productivity); this entails two key adjustments to deal with undercapitalisation and weak payment discipline in the real economy. The capital stock deficit is 35 billion euro or 21% of GDP (2016), 16.4 billion euro (46%) from private domestic capital enterprises, 14.5 billion euro (42%) from private foreign capital enterprises, and 3.5 billion (10%) from state owned enterprises. Improved payment discipline and hard budget constraints would deal with the outstanding 22.9 billion euro or 13% of GDP (2016) in arrears of non-financial companies. The author calculates that a 1 pp reduction per year in arrears would boost GDP growth by 0.5 pp, cut inflation by 0.5 pp, and increase potential GDP growth by 0.2 pp. After the reform of state-owned enterprises during the transition, the author notes that it is high time for private owned enterprise reform. Chapter 2 features forensic policy recommendation to this extent. The overriding goal would be to facilitate the market exit of decapitalised, loss-making companies in which owners and shareholders are unable or unwilling to invest by raising capital. Some of these companies are zombies (they aren't earning enough to cover their interest expenses), have no activity (file no balance sheet) or are used for fiscal optimisation and tax evasion purposes. The weak state regime of tolerance to payment and business indiscipline and to disinvestment should be ended.

The second major policy recommendation is a fiscal consolidation based not on austerity, i.e. cutting expenses, but on revenue enhancement, particularly fiscal revenue. Georgescu notes that an improvement of tax collection to the performance level of neighbouring Bulgaria would boost fiscal revenue from 26% to 30% of

GDP, while an even higher, Western European level of tax collection efficiency gain would bring 5% of GDP. In essence, this entails revenue service modernisation and no more tolerance for fiscal evasion. The author stresses that this policy course is required, but not sufficient for the task. An overhaul of the tax system is also required, especially of income and wealth taxation. Georgescu calls for the (re) introduction of yearly tax returns on all income for all taxpayers, seconded by an asset return, especially for real estate. Once the data is collected, tax reform has a base to be formulated upon. As a general principle, Georgescu recommends discarding the flat tax regime and a return to progressive brackets for the income tax, and progressive taxation of wealth.

### **A critical look at the policy recommendations and other book features**

The policy recommendations put forward by Florin Georgescu could be separated into two distinct categories: the (stated) goal, namely eurozone membership, and the means. The latter primarily include structural reforms in the real economy, especially of private owned enterprises. In addition, Georgescu also calls for a strong sectoral policy. In effect, these supply-side policies would increase productivity, efficiency, and profitability by replacing the current preponderance of non-tradables goods, low gross added value, less knowledge intensive activities with tradables, and advance towards the upper phases of the value-added creative chain. This would also allow for more high-skilled and better paid jobs, and, implicitly, discarding the low skill, low pay model. On the fiscal side, Georgescu calls for the same kind of reforms that are in the mainstream of Western debate on income inequality: more progressive taxation and a quasi-roll back of some of the Reagan-Thatcher, neoliberal revolution, at least in terms of income and wealth taxation. However, his policy ideas were perceived as radical socialist in Romania, where the intellectual landscape is much more right-wing and neoliberal than in the West. In terms of social policy, especially labour and redistribution issues, the chapter on labour – capital relationship provides the best available policy reform blueprint.

In my view, it is not the means that are problematic, but the goal. This is to say not the policies, but the objective they are attached to. Eurozone membership looks and sounds as a repeat of the 1990-2000s reform strategy. A political goal – accession to EU and NATO membership – was used to mobilize the support of the population for the painful economic policies of the transition, for which the author provides a masterful analysis. The big question is whether the population is up for yet another such effort? Romanian society features high levels of social pessimism, lack of cohesion, and low trust in the political leadership. Moreover, even euro-enthusiasm is declining. In other words, after waiting so much for the Promised Land, the people are too tired for yet another effort. While the author

acknowledges the policy limitations of eurozone membership, there is no room in his project for a debate on the structural weakness of the eurozone institutional framework, highlighted, among others, by leading voices with a similar progressive outlook as Georgescu, such as Stiglitz (2016), Krugman, and James Galbraith and others (2015). What if Romania succeeds in eurozone membership, but without the structural reforms advocated by the author? Georgescu himself warns against boosting GDP by fiscal and monetary schemes as a deceptive, short-lived solution. In effect, this would, in his words, perpetuate the redistribution of the flow of newly created value in society in favour of rent seekers and monopolists (990). The eurozone membership goal seems more as a device to pre-empt the critiques of his policy recommendations from policy makers and other critics, who, in the context of Romanian public life, would not dare to position themselves against eurozone membership.

Throughout the book and starting with the title, Georgescu refrains from calling capitalism by its name. Instead, he uses the misnomer post-communist, borrowed from political science, but which has more to do with political institutions than the economy, or uses the more neutral term market economy. The title itself is a quasi-reference to Piketty's (2014) *Capital in the Twenty-First Century*. The clearest indication comes from the section about income and wealth inequality data and methodology that features the author's correspondence with Piketty's team. Another possible answer is that, unlike Piketty's book, this is a more analytical than theoretical book. In other words, the author's main goal is not a (mainly) theoretical contribution on capitalism in a country at the EU periphery, such as Romania, but an analytical and descriptive approach to how capital emerged and its key features. That being said, the author concludes that Romania features a certain type of capitalism, which he labels "hybrid capitalism".

The book features repetitions of data and even content from chapter to chapter, within the chapters, and even between chapters and the last chapters. While these repetitions might be disquieting for the reader of the entire book, this is very much tolerable and understandable due to the size of the individual chapters and the book itself. As stated before, there is also the reality that in our times most readers no longer read the whole book, but focus on their areas of interest. One could find this feature in other leading international economists, such as Stiglitz.

### *Final remarks*

Although the work of an economist, *Capital in Post-communist Romania* deals with fundamental subjects for Romanian sociology. Moreover, these are subjects that Romanian sociology dwells upon rarely or not at all, such as the capital – labour relationship and the distribution and redistribution system, income and wealth inequality, precarious work, the transition and privatisation processes, structural problems of capitalism, and development policies (Zamfir, & Filipescu,

2015). In part, this is because the dearth of objective data, which is so brilliantly researched by the author; in part, it also is due to the methodological crisis stemming from sociology's overreliance on what C. Wright Mills (1959/2000) called "abstract empiricism", i.e. subjective data collected via surveys. The book also pursues questions specific to classical sociology, as formulated by Mills (1959/2000, 6): "What is the structure of this particular society as a whole? What are its essential components, and how are they related to one another? (...) Where does this society stand in human history? What are the mechanics by which it is changing?" The book, especially through its focus on the transition period and the economy and society that resulted from it, answers such "big questions".

Regarding the style of thought, the sociological components from *Capital in Post-communist Romania* would fit both into explanatory sociology and constructive, or applied, sociology, to use the terms of Cătălin Zamfir (2005). In particular, the book provides a structural analysis for the causes of poverty, underdevelopment, and the perceived unsatisfactory quality of life, which stimulates emigration. Applied sociology permeates the policy recommendations, especially the ones about labour – capital relationship, the distribution and redistribution system, income and social inequality, and development. Due to the quality, quantity and originality of its data, and the analysis based on this data, as well as the excellence of its scholarship, this is the most valuable scientific contribution by an economist to Romanian sociology since Virgil Madgearu in the interwar years. On balance, Romanian sociology is enriched by this book. As such, the Romanian Sociological Association's Award for Excellence to Florin Georgescu is fully deserved.

Undoubtedly, it is one of the leading books about the transition period from Soviet-style socialism to capitalism in Romania. The analysis of the real economy and the nature of Romanian capitalism are groundbreaking. The book functions as a comprehensive 30-year economic and social history. As such, *Capital in Post-communist Romania* will be a starting reference for any sociological work from now on grand subjects such as transition and Romanian capitalism. In addition, the author makes an outstanding contribution to the debate about development policies. Due to its scope and size, this is Florin Georgescu's magnum opus and a lasting contribution to Romanian scholarship. This is why, although the book is freely available on the internet on the author's blog, an English version should be considered. Furthermore, a campaign to promote the English version book in Romania and abroad through all possible channels of distribution and popularization should be undertaken.

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