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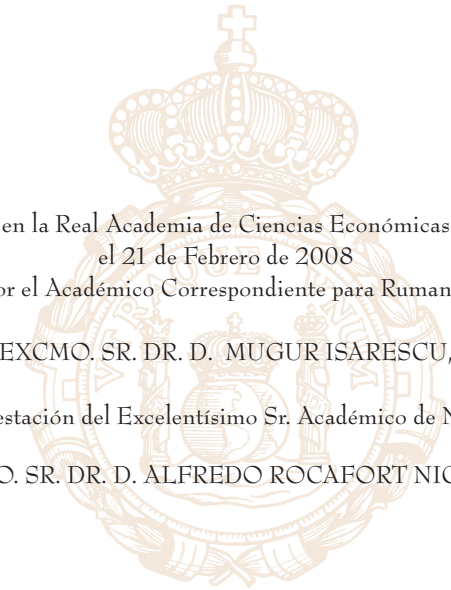
Monetary policy issues in an emerging economy. The case of Romania



Discurso de ingreso en la Real Academia de Ciencias Económicas y Financieras leído,
el 21 de Febrero de 2008
por el Académico Correspondiente para Rumania

EXCMO. SR. DR. D. MUGUR ISARESCU,

Y contestación del Excelentísimo Sr. Académico de Número

EXCMO. SR. DR. D. ALFREDO ROCAFORT NICOLAU

Barcelona 2008

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EXCMO. SR. DR. D. MUGUR ISARESCU

EXCELENTÍSIMO SEÑOR PRESIDENTE,
EXCELENTÍSIMOS SEÑORES ACADÉMICOS,
SEÑORAS Y SEÑORES,

Desearía, ante todo, expresar el gran honor que constituye poder compartir este venerable espacio con tan altas personalidades académicas en esta importante Sesión Internacional en la cual se hace pública mi elección como Académico de esta Real Corporación.

La ya larga historia de la venerada institución que me acoge y el alto prestigio internacional que ha alcanzado en los últimos años constituyen, para mi, un fuerte acicate para continuar trabajando desde la independencia y la libertad y a través de la ciencia y la cultura económico-financiera en la constitución de un futuro de progreso social y armonía entre las naciones.

Agradezco a los excelentísimos señores académicos su generosa acogida y espero ser merecedor de tan grande honor.

Muchas gracias!

Introduction

There is a consensus among central bankers, academics and even the public at large that price stability is beneficial and monetary policy should be tasked to achieve it. This general policy recommendation is valid for both industrialized and emerging economies, although in the latter case, as financial markets are less mature and operate with less diversified instruments, it might be a more challenging task for central banks to deal with real and nominal shocks. Such shocks could come from unanticipated movements in food and energy prices, administered prices and, last but not least, from massive capital flows. The above-mentioned limits to monetary policy efficiency make the case for a coherent policy mix even stronger in emerging economies. Without support from the other economic policies, monetary policy may find it difficult to achieve sustainable low inflation. In other words, delivering price stability may come at the expense of other macroeconomic equilibria and may ultimately be self-reversing.

Central and Eastern European transition economies in particular have been confronted with large FDI inflows, both independent of and associated with the privatization process, and also with portfolio investment, fostered by the presence of a significant interest rate differential against advanced economies. Large capital inflows raise a dilemma to policymakers. On the one hand, they foster economic development and thus support real convergence; they also help subdue inflationary pressures in the short run through their effects on exchange rate appreciation and through shifting consumption towards tradable goods. On the other hand, through the same effects on exchange rate appreciation, capital inflows may erode external competitiveness of the economy, widen external imbalances and thus result in depreciation and higher inflation. In addition, large external imbalances render an economy more vulnerable to a change in the market sentiment or to shocks associated with high volatility in external financial markets.

This paper examines the particularities of monetary policy and the constraints it faces in the small open emerging economies in Central and Eastern Europe (with a special focus on Romania) and evaluates its role in the policy mix.

Section 1 and 2 discuss the reasons for setting price stability as the main goal of monetary policy and explore the interlinks between price stability and financial stability, in order to identify particularities and limits of monetary policy in small open emerging economies. Section 3 focuses on reviewing literature and country experiences with capital flows, which point to both macroeconomic benefits and potential risks to macroeconomic and financial stability. Section 4 deals with challenges faced by the authorities of Central and Eastern European countries and argues in favor of a macroeconomic policy mix that supports real convergence with the EU while maintaining macroeconomic stability. Section 5 describes Romania's experience with liberalizing capital flows concomitantly with adopting inflation targeting. Section 6 concludes and identifies main challenges.

1. Monetary policy – particularities and limitations for a small open emerging economy

In the last decades, three standard monetary policy strategies proved successful in providing an effective nominal anchor: monetary targeting, exchange rate targeting and inflation targeting. A strategy that has been suggested by Frankel (1995) as best suited for semi-open economies is nominal income targeting; however, a major problem with this strategy is that it has never been tried in practice, either in industrial or emerging markets (Mishkin and Savastano, 2000).

Among the standard strategies, only exchange rate targeting and inflation targeting are currently in use in the new EU Member States in Central and Eastern Europe. Monetary targeting lost ground in these countries as it did before in most developed economies, following the breakdown of the previously stable relationship between monetary aggregates and inflation; this development is mainly linked with the fast remonetisation that occurred after inflation was brought down to moderate levels, banking systems were privatized and capital flows were liberalized. However, the ECB still takes into account explicitly money growth in its policy framework by following a two-pillar heterodox strategy: 1) the assessment of the short to medium-term determinants of price developments, with a focus on real activity and financial conditions in the economy (economic analysis); 2) the exploitation of the long-run link between money and prices (monetary analysis). It is worth mentioning in this context that inflation targeting does not preclude the central bank from paying attention to monetary aggregates to the extent they contain useful information for forecasting inflation.

Smaller economies tend to favor exchange rate anchors – currency board arrangements in Bulgaria, Estonia and Lithuania, hard peg in Latvia. The remaining countries chose more flexible exchange rate arrangements – ranging from a free float in Poland and managed floats in Czech Republic and Romania to an ERM II type target zone in Hungary, coupled with inflation targeting regimes.

While monetary policy is set on "automatic pilot" in currency board arrangements, central banks operating in an inflation targeting framework are supposed to make active use of their monetary policy instruments and have to adopt complex decisions on a regular basis in order to minimize their loss functions. A relatively comprehensive loss function is presented below, but usually discussions focus on the first two parentheses:

$$L = \alpha(\pi-\pi^*)^2 + \beta(y-y^*)^2 + \gamma(r-r^*)^2 + \delta(er-er^*)^2 \qquad \alpha, \beta, \gamma, \delta > 0$$

where:

π – inflation rate
π^* – inflation target compatible with price stability
y – GDP growth rate
y^* – potential output growth rate
r – real interest rate
r^* – equilibrium real interest rate
er – real exchange rate
er^* – equilibrium real exchange rate
$\alpha, \beta, \gamma, \delta$ – coefficients describing the relative importance of objectives considered in the loss function

Thus, the central bank needs to set its policy instrument such as to stabilize inflation around the inflation target without generating excessive fluctuations in economic activity. In practice, central banks also need to pay attention to objectives other than price stability. Quoting Mervyn King, "central bankers are not inflation nutters".

The gradualism induced by concerns related to the stabilization of the output gap around trend is usually supplemented by the need to avoid sharp movements in interest rates (interest rate smoothing and stabilization) and exchange rate that may jeopardize the stability of financial markets and external equilibria.

The particularities of emerging economies, such as the predominance of supply shocks, widespread currency substitution, weak fiscal institutions,

shallow financial markets, vulnerability to sudden stops of capital inflows and labor force migration add another layer of complexity to policy decisions aimed at achieving price stability[1]. The euro area entry requirements are seen as an additional strain on the monetary policy conduct in the new EU Member States, as it is essential that the Maastricht criteria be fulfilled without jeopardizing the achievement of real convergence. In this respect, the requirement to spend at least two years in ERM II is a challenge. As pointed out by many analysts, ERM II creates incentives for speculative attacks. Fischer (2001) argues that target zone type arrangements are regarded as risky, as evidenced by the dwindling number of countries that have in place such an exchange rate regime across the world.

In view of the risks involved, ERM II entry should be thoroughly prepared, as the participation in this mechanism is mandatory. I believe that spending some time after EU accession outside ERM II is advisable in light of volatile capital flows, large fiscal imbalances and/or risks of economic shocks. This period should be used as an opportunity to deal with macroeconomic imbalances.

1. Advanced countries are not immune to problems with their fiscal, financial and monetary institutions, but there is a major difference in the degree of the problem in emerging market countries (Mishkin, 2004).

2. Price stability and financial stability in the design of monetary policy

It is unanimously accepted that there is no long-run trade-off between inflation and unemployment. Both Friedman (1968) and Phelps (1968) argued that the standard Phillips curve was misspecified, as it failed to factor in inflation expectations, and in its updated version "any trade-off between inflation and unemployment would be short-lived at best" (Bernanke, 2006). In other words, one could not achieve systematically an unemployment rate lower than the natural rate by accepting higher inflation.

In view of this, one cannot but conclude that price stability is the appropriate overriding long-term monetary policy goal. Price stability is both an end and a means of monetary policy, since it contributes to sustainable economic growth and macroeconomic stability (Bernanke, 2006). Thus, not only is the pursuit of price stability the only thing that monetary policy can do effectively, it is also the best thing it can do in terms of overall social welfare. According to the Treaty establishing the European Community, "the primary objective of the European System of Central Banks shall be to maintain price stability".

The effectiveness of monetary policy is limited, however, in the absence of a viable and stable financial system, particularly in the case of single-digit inflation rates. Shallow financial markets hamper the functioning of the standard interest rate and credit channels, limiting the ability of the central bank to fine tune the economy and may cause it to rely excessively on the exchange rate channel to manage aggregate demand.

It is largely accepted as one of the core macroeconomic principles that financial frictions play a significant role in business cycle fluctuations. The sharper complementarity between price stability and financial stability is connected to economic globalization and, in particular, to the removal of barriers to the free movement of capital. Against the background of the opening-up of national economies, financial stability has become a basic component of macroeconomic stability, with capital flows taking advantage of the financial system vulnerabilities in order to promptly sanction errors or any inconsistency of economic policy.

In contrast to price stability, there is no universally accepted definition of financial stability. According to Jaime Caruana (2005), "although we have a well-developed framework for debating and conducting monetary policy, our thinking on financial stability is less advanced". Haugland and Vikøren (2006) point out that, although it is not clear-cut what weight should be attached to financial stability and price stability considerations, respectively, in the conduct of monetary policy, "both the communication and the monetary policy decisions of central banks indicate that financial stability is in the process of acquiring a more distinct role in monetary policy. This can be ascribed to the recognition that financial stability has consequences for future developments in inflation and output".

Financial stability should be thought of, in a broad perspective, as the situation in which the financial system is able to ensure an efficient allocation of savings to investment opportunities and to withstand shocks without major disruptions. A narrower yet more useful perspective, from a central bank's standpoint, is to define financial stability as the situation in which no banking crises occur and a certain stability of asset prices, including that of interest rate, is manifest. There is broad agreement that central banks have an essential role in restoring financial stability, although there are no rules or models to guide how this has to be performed and judgment should always be used in conjunction with hard science[2].

Both definitions imply an active role from monetary policy, but its relative importance is different. The first definition mentioned above, which focuses on the overall functioning of the financial system, suggests that prudential supervision should play the first violin in the pursuit of financial stability; monetary policy matters for allocative efficiency to the extent it can deliver price stability. By contrast, if financial stability is defined mostly as interest rate smoothness, as in the latter definition, monetary policy plays a more significant part and its freedom to make use of its policy instrument (i.e. the policy rate) may

2. Quoting Alan Blinder (1997), "I can testify that central banking in practice is as much art as science. Nonetheless, while practicing this dark art, I have always found the science quite useful".

become constrained – this way, a conflict between price stability and financial stability could emerge.

The conventional view of the relationship between price stability and financial stability treats inflation as the main cause triggering financial instability. Historical experience appears to confirm this view as most of the episodes of severe financial instability and banking crises occurred either during periods of high inflation or hyperinflation, or during recessions following the implementation, by the authorities, of inappropriate measures to dampen inflation.

Recent economic literature points out that, in contemporary economies, the achievement of stable and low inflation has created a new economic environment, which calls for carefully reconsidering the relationship between price stability and financial stability (Borio and Lowe, 2002). However, low inflation has proved it is not a sufficient condition for ensuring lasting financial stability. As Andrew Crockett (2003) put it, the successful war against inflation has not yielded as big a "peace dividend" as economists had hoped for. Therefore, a new battlefield opened up, to fight against financial instability. In this respect, the experience of some Asian countries in 1997-1998 is particularly relevant to the complexity of this relationship: before the outbreak of the financial crisis, substantial imbalances had built up in the respective economies even against the background of a relatively high degree of price stability. More recently, increased rates of default in the subprime segment of the housing sector in the US spread the crisis to the credit market in both the US and Europe. In the new environment, it is of great importance to assess whether the central bank is able to simultaneously ensure price stability and financial stability by using the instruments in its toolkit and in what way the two types of stability can be reconciled if their achievement requires conflicting measures. There might be situations when the need to safeguard financial stability takes precedence over the objective of price stability; radical interest rate movements aimed at restoring price stability in the short run will ultimately be self-defeating in the longer run if they contribute to the buildup of disequilibria in other sectors of the economy. I have to stress it again: there are no one-size-fits-all rules to be followed in such an event – one must always consider the particularities of the situation at hand.

I believe that Romania's experience, as described later on, shows that financial stability is of utmost importance to price stability. This experience indicates that, if forced to choose between rapid disinflation and the safeguarding of financial stability, the latter should take precedence, in order to ensure the long term fulfillment of the price stability objective. It is worth mentioning that the countries which embark on a disinflation path should choose an adequate disinflation pace so as to avoid a conflict with financial stability. I believe Romania has a good experience in this respect. The country has achieved an average disinflation rate of 5.8 percentage points per year during 2000-2007, while the financial system remained stable. In the long run, failure to maintain financial stability can only entail a renewed flare-up in inflation. This reminds me of standard airplane safety instructions, according to which, in case of cabin depressurization, the parent should put the oxygen mask on his own face first and only afterwards tend to the infant (which, in most cases, is the parent's reason to live).

Thus, if the endeavor of curbing inflation relies overwhelmingly on the appreciation of the exchange rate, which veers off significantly from its equilibrium level, thereby leading to a persistently high current account deficit, price stability over the long term will be undermined. The correlation between financial stability and the long run price stability holds true. Therefore, considering price stability in the long run to be the primary objective, the central bank should pay particular attention to financial stability and, I would add, to the overall developments in macroeconomic indicators. Otherwise, the disinflation gains, however spectacular they might appear at a given point in time, may prove completely unsustainable.

3. Capital flows and their consequences for the macroeconomic and financial stability

Capital account liberalization is one of the most hotly debated macroeconomic policy decisions, due to the fact that the various theoretical approaches had different effects on the desirability of taking such a measure.

3.1. A perspective from theory

In keeping with perfect market models, free capital flows cause financial systems functioning to improve, thereby increasing the volume of available funds along with their lower costs and allowing risk diversification (Frenkel and Razin, 1996). Obstfeld (1998) emphasizes that such a measure would render resource allocation more efficient; according to Stultz (1999) and Mishkin (2001), liberalization of capital movements fosters transparency and accountability, thus reducing the magnitude of adverse selection and moral hazard issues simultaneously with decreasing liquidity constraints on financial markets. According to the cited authors, international financial markets tend to impose stricter discipline on policymakers which otherwise could be tempted to take advantage of a captive domestic financial market. Bekaert, Harvey and Lundblad (2001) find that liberalization of capital flows fosters economic expansion, leading to growth rates higher than those seen prior to the time of liberalization.

There is a rich and influential literature holding that the paradigm of efficient markets is deceiving when it is applied to international capital flows. Thus, removing the distortions associated with the constraints on free capital movement may not be beneficial against the backdrop of other distortions (according to second-best equilibrium theory); such a situation is relevant especially for developing countries, where a great number of distortions is all the more likely. In line with Brecher and Diaz-Alejandro (1977), if there are industries insulated against external competition, capital account liberalization may direct capital towards sectors in which that particular country holds a comparative disadvantage. Brecher (1983) shows that capital account liberalization in economies with real wage stickiness causes the channeling of far too many resources towards capital-intensive industries, substituting capital for labor in the production function, thus worsening the resource allocation issue and

impacting negatively residents' incomes and wealth, effectively resulting in immiserizing economic growth. According to Stiglitz (2000), with informational asymmetries being endemic for financial markets and transactions, there is no reason for asserting that liberalization of capital movements would generate wealth and there are no guarantees for capital flows being channeled towards destinations where their marginal product would exceed the opportunity cost; this is all the more valid for the emerging economies, where the capability of collecting and processing relevant information for financial transactions is weak.

The developments in the late 1990s, especially the Asian crisis, led many economists to reckon that globalization went too far, creating excessively volatile capital markets and triggering costly crises. Moreover, they advocated the return to the former order of controlled flows. Stiglitz (1999) recommends developing countries to impose restrictions on capital inflows with a view to moderating the excessive magnitude of economic cycles on financial markets. Krugman (1998) supports the restrictions on capital outflows, long considered by literature as being totally inefficient, as such restrictions could help, even temporarily, to manage an otherwise disorderly capital flight. Rodrick (1998 and 2000) sees the restrictions on capital movements as desirable given that their free circulation leads to financial crises owing to their excessively volatile nature.

Empirical findings did little to reconcile the different opinions cited above. The literature dedicated to crises identifies empirically that excessive fluctuations on financial markets lie at the root of currency crises and financial deregulation is the source of such fluctuations. Other authors continued however to emphasize that financial market deregulation is beneficial, thus contributing to a decline in capital cost. According to Kaminsky and Schmukler (2003), there are two "weaknesses" of research that render reconciliation impossible. The first is that empirical research is focused on either short-term or long-term consequences of liberalization, failing to consider its possible time-variable effects. The second is the lack of a comprehensive treatment of liberalization, as approaches to date focused alternatively on the liberalization of the domestic financial sector, the capital account, or the stock market, even when liberalization reforms have entailed the progressive opening of the three sectors.

Despite the divergences in the literature, there is a broad consensus that financial markets are most likely to deliver on the promise of growth and stability if they are transparent and well regulated (Rato, 2007a). Also, financial globalization is least likely to produce instability for countries with more developed financial sectors, stronger institutions, sound macroeconomic policies, and more open trade systems (Rato, 2007b).

3.2. Developments in Central and Eastern European countries

Over the past few years, Central and Eastern European countries have been facing large capital inflows as restrictions on the free movement of capital had been gradually lifted during the process of full capital account liberalization, which was a prerequisite for EU membership. On one hand, investors' appetite was stimulated by persistently favorable interest rate differentials. On the other hand, the prospects for these countries looked more favorable in view of the EU accession. Lipschitz et al. (2002) point out that the transition countries which open up to global capital markets are like honest citizens in a dangerous world – they are vulnerable to large and potentially erratic flows. These flows should not be seen as one-off destabilizing events: they are intrinsic to the transition process and therefore need to be factored into the policy mix. In other words, despite their obvious advantages (higher economic efficiency, technology transfers), capital inflows may pose major threats to macroeconomic stability and external competitiveness, inducing an overheating of the economy if their volume exceeds its capacity to absorb them.

One of the main channels that lead to overheating of emerging economies is the lending channel, given the dominant position of banks in the financial system[3] and the increased volume of capital made available after removal of the restrictions on capital account.

Professional literature warns that a credit boom may have serious macroeconomic and macroprudential consequences. It may be frequently associated with macroeconomic and financial crises as a result of

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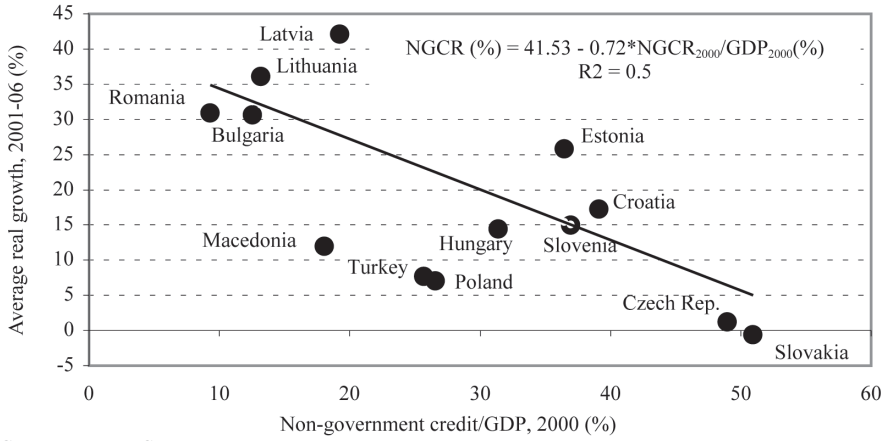
3. According to Backé, Égert and Zumer (2006), banks hold 85% of all financial assets, while capital markets play a much less important role.

macroeconomic imbalances and the worsening of banks' financial standing. Therefore, the authorities need to strike a good balance between the safeguarding of macroeconomic and financial stability and the credit expansion that helps boost the economy and improve the efficiency of resource allocation.

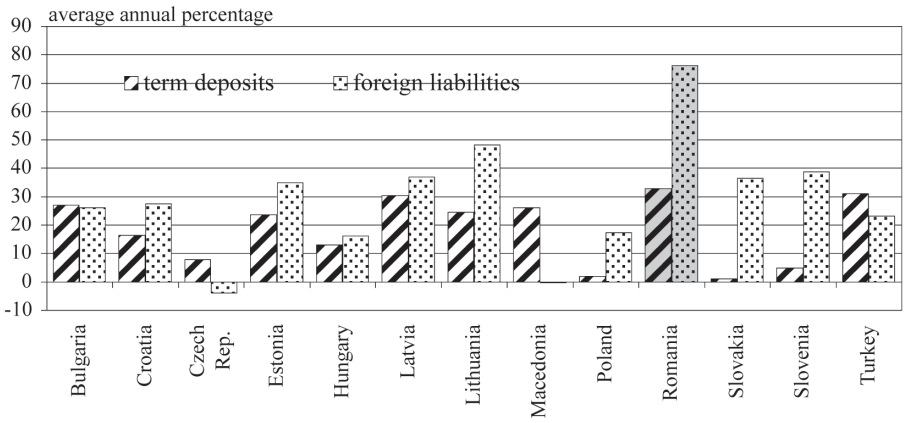
Figure 1. The Lower the Starting Point, the Bigger the Financial Intermediation Gains



Source: IMF- IFS, NBR

The fast credit growth in Central and East-European countries can be substantiated by the initially extremely low levels of financial intermediation and its natural convergence process towards the levels observed in advanced economies of the European Union.

Figure 2. Average Annual Growth Rate of Bank Liabilities, 2001-2006



Source: IMF - IFS, NBR

The rapid credit growth was financed by massive foreign capital inflows, occurring mostly through banks. These inflows were prompted by low capital-to-labor ratios compared to those in Western Europe, expectations of a long-term real appreciation of the currencies in the region and the presence of favorable significant interest rate differentials. Credit expansion followed also the successful implementation of macrostabilization policies; the latter helped reduce the aggregate risk level, and, together with the smaller size of the public sector, have made available additional resources for the private sector. One should not forget the significant wage increases and the narrowing spreads between lending and deposit interest rates – resulting from increased competition in the banking sector –, which, together with the prevailing nominal appreciation trends of domestic currencies, have increased the creditworthiness of households and their ability to take on debt in domestic and, even more, in foreign currency.

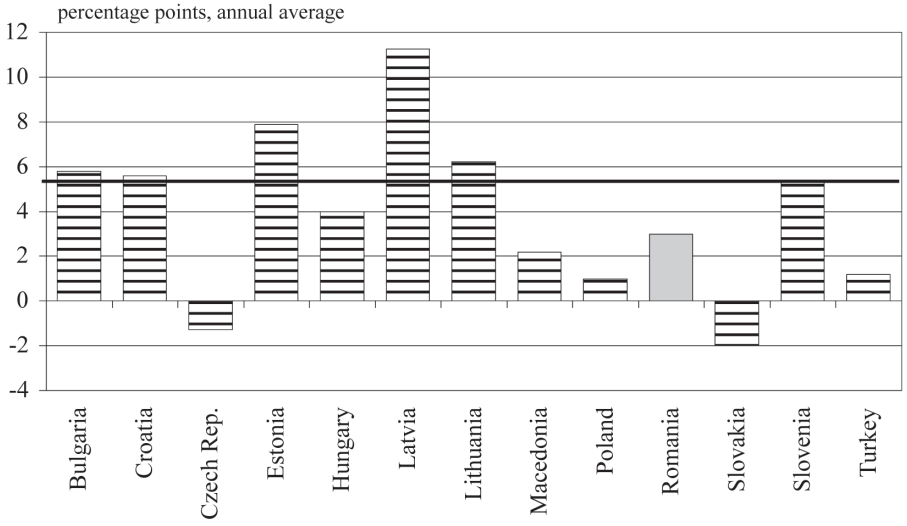
Certainly there are great benefits for the banking industry from capital inflows. Foreign players operating in the banking market lead to a more stable financial environment, enhanced corporate governance, and improved risk management capabilities. At the same time, it is reasonable to think that a rapid credit growth can possibly outpace banks' capacity to assess risks, thus leading to increased information asymmetry which could result in increased rate of

default. However, in the Central and Eastern-European countries the bank's model of doing business has not changed from the basic "originate and hold" on the balance sheet to the more sophisticated "originate and distribute" out of balance sheet and the region was not facing the problem of "frenetic securitization". This is a good base to say that the sophistication needed to assess the risk profile of the banking business in these countries is not that high as that needed in Western Europe in the context of the current credit crunch.

From a macroeconomic perspective, rapid credit growth fosters aggregate demand, thus generating inflationary pressures and contributing to wider external imbalances. While inflationary pressures have generally been fended off successfully thanks to the monetary policy implemented by all countries in the region, external imbalances have widened significantly in the Baltic States, Bulgaria and Romania, namely the same countries witnessing the fastest credit expansion over the past five years. However, central banks have difficulties containing credit expansion, both because restricting domestic currency denominated credit growth through tight monetary policy can lead to it being substituted by foreign exchange denominated loans, and because administrative measures aimed at limiting the ability of banks to take on exposure may very well end in their externalizing that exposure to their "mother" banks. Wide current account deficits are a threat because they are associated with a higher risk of an abrupt exchange rate adjustment, and increased volatility of the exchange rate has a major impact on monetary and macroeconomic stability in general. It is quite difficult to assess the sustainability of current account deficits posted by Central and East-European countries; external imbalances are perfectly normal in countries undergoing a real convergence process. However, excessive external deficits recorded in some countries are likely to pose further risks to macroeconomic stability.

As regards risks to financial stability, economic literature confirms that fast credit expansion is among the warning signs of a financial turmoil, without necessarily leading to such crises. Standard warning thresholds in the literature, such as the annual growth in financial intermediation by more than 5 percentage points of GDP over 5 years (Demirgüç-Kunt and Detragiache, 1997), beyond which the likelihood of a crisis becomes significant, have been surpassed by developments in Bulgaria, Croatia, the Baltic States and Slovenia.

Figure 3. Average Annual Gains in Financial Intermediation*, 2001-2006



Source: IMF - IFS, NBR

*) non-government credit/GDP

At first sight, bank prudential indicators for Central and East-European countries – such as capital adequacy ratios and the share of non-performing loans in the loan stock – have remained at comfortable levels and, in the latter case, have even improved in recent years. However, due consideration should be given to the high volume of new business, which could artificially diminish the share of bad loans and thus conceal any quality-related issues of the credit portfolio.

Table 1. Prudential Indicators

	Non-performing loans/ total loans		Capital adequacy ratio		ROE		ROA	
	2002	**2006**	**2002**	**2006**	**2002**	**2006**	**2002**	**2006**
Bulgaria	2.6	2.2	25.2	14.5	14.9	24.4	2.1	2.2
Croatia	10.2	5.2	17.4	13.6	13.7	13.0	1.6	1.5
Czech Rep.	8.1	4.1	14.2	11.4	27.4	19.4	1.2	1.2
Hungary	2.9	2.5	13.0	11.3	19.8	29.0	1.4	1.9
Poland	21.1	9.4	13.8	14.0	5.5	22.2	0.5	2.1
Romania	1.1	2.8	25.0	18.1	18.3	10.2	2.6	1.3
Slovakia	7.9	3.7	21.3	13.0	11.5	16.6	1.2	1.3
Slovenia	3.9	2.5	11.9	11.1	12.6	15.1	1.1	1.3

Source: websites of central banks, IMF Global Financial Stability Report, October 2007

The structure of credit growth poses further risks to financial stability in addition to those that stem from the speed of credit growth itself. Thus, consumer credit expansion has outpaced that of investment loans in most countries in the region. This means that much of the risk rests with households, which usually lack proper experience in managing risk associated with high level of indebtedness. Moreover, the share of foreign currency-denominated loans is still high in some countries in the region, fostered by both real and nominal appreciation trends and the availability of foreign currency funds from capital inflows. This could increase vulnerability associated with higher currency-based balance sheet mismatches, especially given the risk of disorderly external imbalances correction.

Decisions to be made in the face of a threat of overheating as a result of capital inflows are difficult. These decisions should be based on the economic objectives of the respective country and it is highly imperative that the exchange rate regime, institutional constraints, as well as the determinants and the composition of capital inflows be taken into account. Decisions often rely on incomplete information, particularly in the early stages of an episode of capital

inflows, when it is difficult to assess their nature, whether they are transitory or permanent.

Figure 4 describes a possible vicious circle of monetary policy induced by massive capital inflows. Attempts by monetary policy to alleviate the pressure for sharp currency appreciation are doomed to fail by the impossible trinity of autonomous monetary policy, free capital movement and fixed exchange rate. This circle is further integrated into a general scheme that shows how vulnerabilities and macroeconomic imbalances generated by massive capital inflows (see Figure 5) may trigger a crisis with adverse effects on both price stability and financial stability.

As previously stated, one of the characteristics of Central and Eastern European economies is the predominant role of the exchange rate channel in monetary policy transmission, a consequence of their high degree of trade openness and their still underdeveloped financial systems. Capital inflows boost the effectiveness of this monetary policy transmission channel in delivering rapidly low inflation, both directly through lower import prices and indirectly through its effect on net exports and thus on aggregate demand. However, excessive reliance on this transmission mechanism, while rewarding in the short run, may very well be punishing as it may deepen external imbalances, increasing the vulnerability to capital flows reversals, which sometime may be brought about by a mere shift in the mood of investors. Thus, there could be instances in which lowering interest rates may prevent the exchange rate from sharply appreciating, but such a policy action would be in conflict with the achievement of the inflation target. Again, this is always a delicate issue.

Figure 4. The Vicious Circle of Monetary Policy

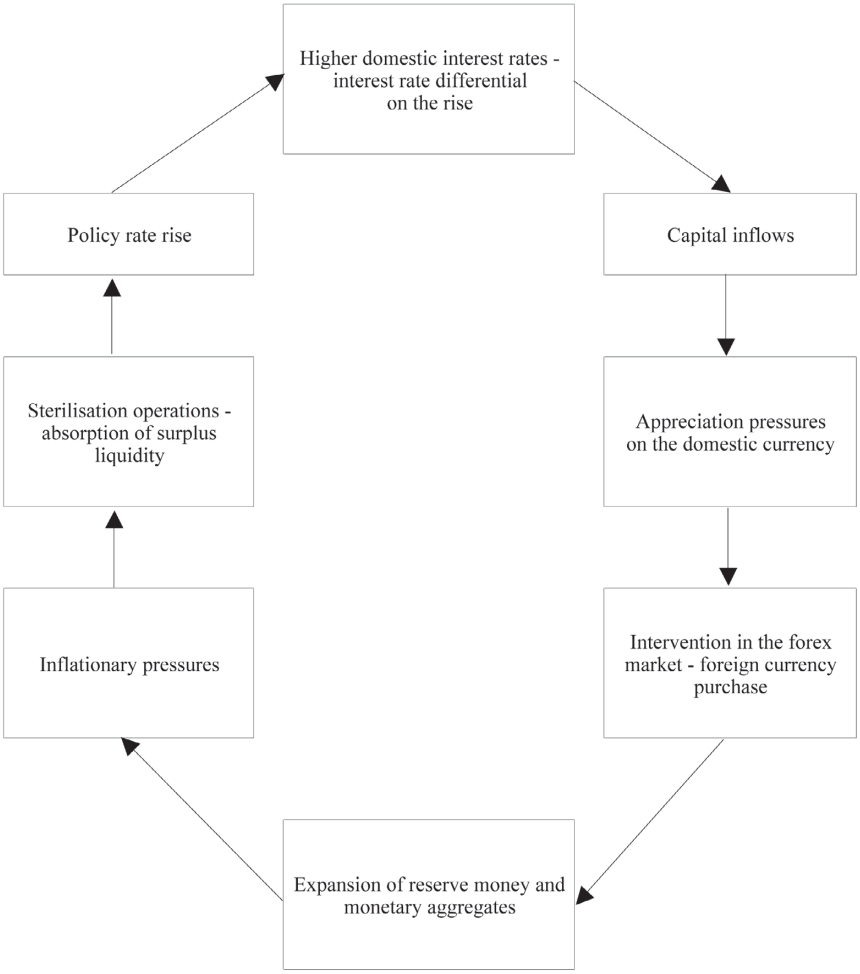
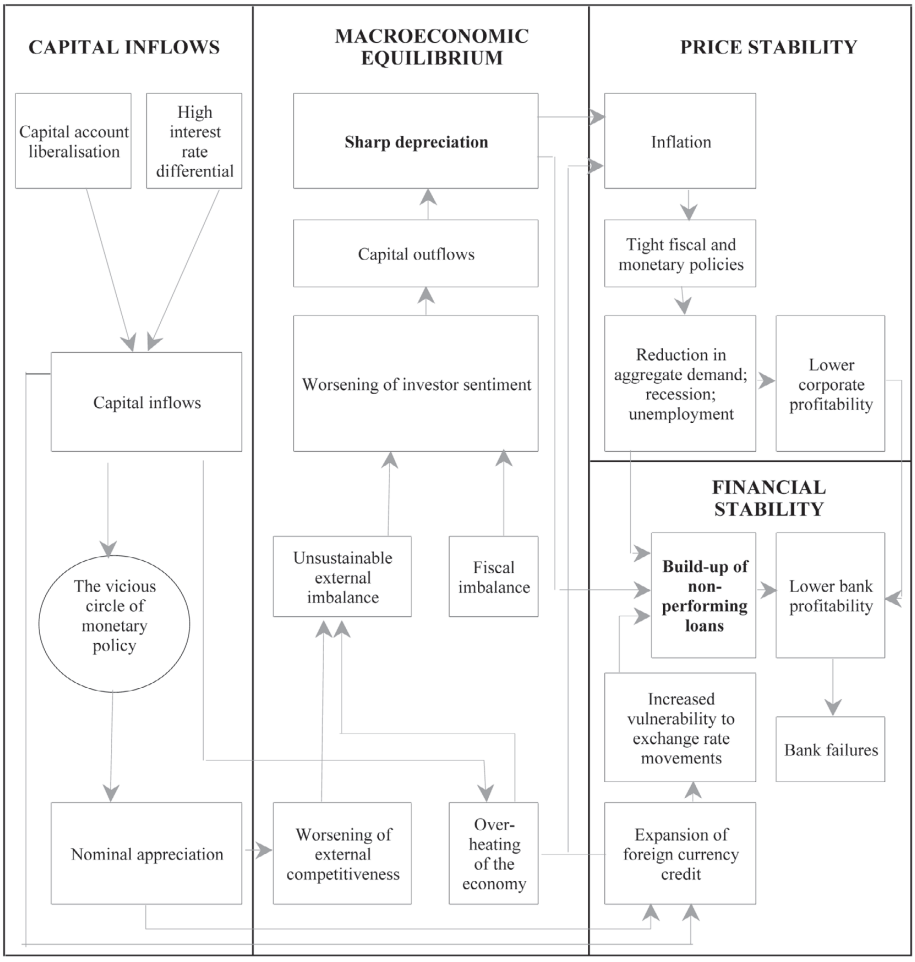


Figure 5. Vulnerabilities to Price Stability
and Financial Stability Generated by Capital Inflows



Given strong capital inflows, currency appreciation will continue and the external competitiveness of the economy will deteriorate. Imports will increase faster than exports, thus boosting the expansion of aggregate demand. Reflecting a growing aggregate demand, the current account deficit may reach unsustainable levels. If corrective measures such as contractionary fiscal policy action and tight income policy are not implemented in due time, investors'

sentiment may change, causing foreign capital flight. Experience shows that the magnitude of these capital outflows may exceed the authorities' capacity to safeguard the value of the domestic currency and may translate into a sharp corrective depreciation, i.e. a currency crisis.

The way in which the abrupt depreciation influences price stability is obvious – the effect is both direct, through import prices, and indirect, by fuelling inflation expectations. The response of monetary policy, whose primary objective is price stability, is obvious as well. A tighter monetary policy stance will compress aggregate demand, pushing the economy into recession and generating unemployment.

Financial stability may also be affected by the currency crisis, and the restrictive policies aimed at restoring price stability might make things worse. If the public perceives domestic currency appreciation as being persistent, a bias towards foreign exchange-denominated loans is unavoidable, thus rendering monetary policy less effective. However, as stressed above, an abrupt corrective depreciation might cause the deterioration of the balance sheet of households and companies, whose net wealth will decline.

With the real sector constrained, the health of the financial sector will suffer too. A large part of bank loans would become non-performing as economic agents would default on their payments. Problems related to maturity mismatches in the banks' balance sheets could add up to the existing large balance sheet currency mismatches and potentially turn into an across-the-board financial crisis.

4. The need for an adequate macroeconomic policy mix

The process of real convergence of emerging economies in Central and Eastern Europe with the European Union is underway and is going to continue for many years ahead given the existing gaps in many of these countries. In my view, the process will continue more or less smoothly, although episodes of acceleration, as those that have emerged in Romania over the last five years or so, could not be ruled out.

As it has happened since the beginning, real convergence is characterized by the concomitant occurrence of:

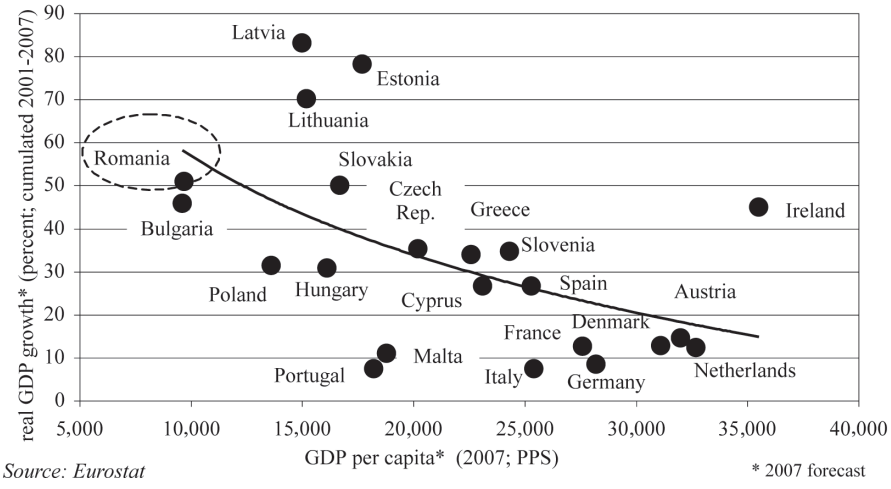
– above-trend economic growth rates, especially in the initial stages of the catching-up process;

– significant increase in per capita incomes;

– massive inflows of foreign capital;

– strong trend of real appreciation of the domestic currency.

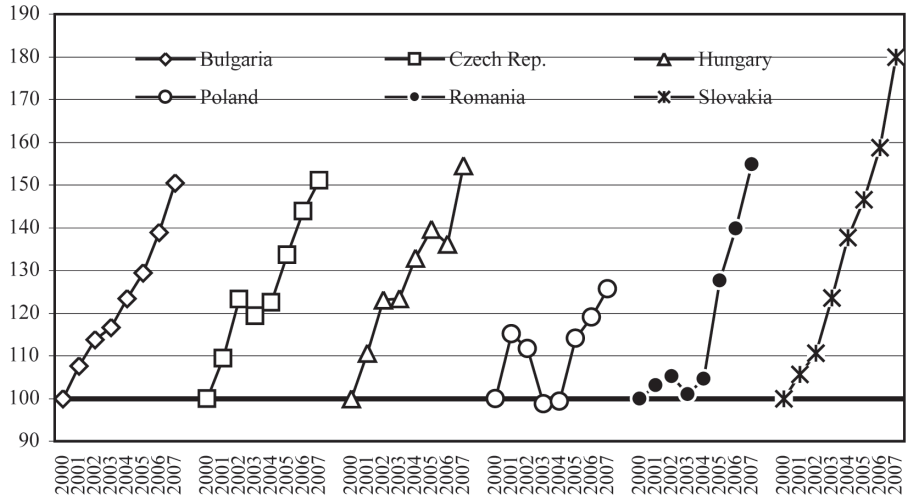
Figure 6. Real Growth and Convergence



Source: Eurostat

* 2007 forecast

Figure 7. Average Annual Real Exchange Rates
against the EUR in selected CEE Countries

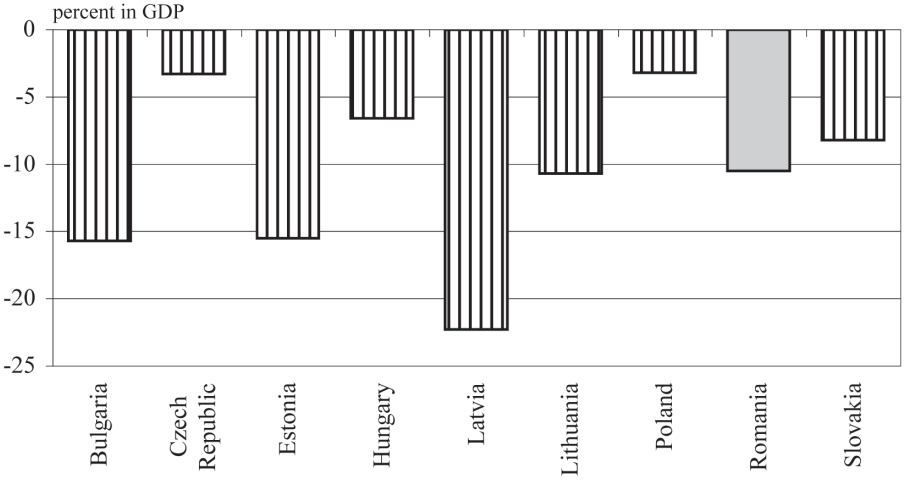


Source: Eurostat, NIS, NBR

Note: An increase in the index means appreciation

The main challenge for the authorities of these countries is to promote nominal and real convergence while maintaining macroeconomic stability.

Figure 8. Current Account Balance, 2006



Source: Eurostat, NIS, NBR

Achieving both sustained economic growth and macroeconomic stability requires enhancing investment and preventing macroeconomic policies from being pro-cyclical. With respect to the former, governments need to improve the absorption capacity of EU funds; measures are also warranted to improve the business climate, rendering it more conducive to increased private investment. Since Central and Eastern European economies tend to overheat while converging in real terms, it is obvious that fiscal imbalances should not add to the economic cycle. Economic policies should take advantage of periods of high growth in order to promote necessary reforms, thus ensuring more room for policy maneuver during future downturns (Krueger, 2004). More specifically, regarding fiscal policy, it is advisable that it uses economic booms as an opportunity to realize fiscal surpluses in order to create a buffer in case of adverse conditions than it can be drawn on to counter economic divergences or asymmetric shocks during downturns (Trichet, 2001). However, in both old and new EU Member States this policy recommendation is not always applied, as the temptation to reap the fruits of good times is often difficult to resist and, in some cases, the need for modernizing infrastructure may be urgent.

In the context of massive capital inflows, monetary policy may face a dilemma. On the one hand, inflation developments could require successive increases in the monetary policy interest rate. Higher interest rates also boost domestic savings and thus ensure a balance between their level and the magnitude of investment, which is essential for avoiding an excessive current account deficit. On the other hand, higher interest rates may lead to a positive interest rate differential, thus attracting even more capital inflows that will press for further appreciation of the currency. Episodes of sharp appreciation may then be reversed, potentially resulting in increased inflation and tensions in the financial sector.

The market may resolve this dilemma by setting higher risk premia on investment in the transition economy. But, insofar as risk premia are sometimes erratic and, in any event, sensitive to factors beyond the reach of the authorities, capital flows can overwhelm efforts to stabilize the economy (Lipschitz et al., 2002).

Another highly sensitive matter is the desired monetary policy stance in the case inflation is kept under control during the target horizon, but financial and

macroeconomic imbalances deepen. If the authorities do not formulate and implement an economic policy response at an early stage, they contribute in a passive way to the sharpening of these imbalances, which sooner or later may either trigger a crisis or incur much higher economic costs due to a subsequent intervention when financial or macroeconomic strains have grown more severe. Although the necessity of intervention is clear from a theoretical point of view, the timing of an early intervention by the central bank, along with the likely support from other authorities, may raise problems difficult to solve such as:

1. Is it possible to clearly identify imbalances at an early stage?

2. If imbalances that occur at an early stage vanish by themselves/ spontaneously and the authorities take prompt restrictive measures, the combined effect of the two factors could push the economy into an excessive recession.

3. How could a tighter monetary policy be explained in the absence of inflationary pressures? (Crockett, 2003).

Given the complexity of these problems, adequate calibration of the monetary policy response is extremely difficult. Besides, considering the limitations induced by the opening-up of the capital account, the monetary policy cannot be tasked to maintain the macroeconomic equilibria by itself; instead, fiscal and income policies should act supportively and thus share the burden of the stabilization effort with monetary policy.

More specifically, fiscal policy should play the crucial role in correcting the current account imbalances. This means that countries must calibrate budgets to allow ample room to accommodate the rise in private sector demand, and build buffers to serve as a bulwark against possible crises, as the magnitude of the fiscal deficit contributes directly to the size of the current account deficit. Additionally, through its incentive-creating component, fiscal policy may foster exports and productive economic activities in general. Apart from the restrictiveness of fiscal policy, the government also needs to follow a cautious income policy by containing the public wage bill, an action that will also limit

the mirroring effects high public wage growth could have on the private sector. Thus, the undesirable event of having productivity growth outstripped by wage dynamics could be avoided.

However, in emerging economies, even these two policies can operate under serious constraints. The need to switch away from the inherited pay-as-you-go pension systems (where the present generation bears the burden of pensions for prior generations and future generations will bear the burden of pensions for the present generation) to funded pension schemes, together with the need for significant public investments in infrastructure, a highly significant component of real convergence, limit the potential for higher revenues and lower expenditures respectively. The effectiveness of income policy is undermined by a tight labor market, as the freedom of movement inside the EU has more often than not led to labor force migration towards old EU members; in this case, wage increase pressures may originate from the private sector and may be difficult to counteract by public wage policy. Moreover, efficient public governance and the need to avoid corruption require public workers be properly motivated and wage inequities in the public sector be removed.

History shows that vulnerabilities in financial systems and the accumulation of imbalances in other sectors of the economy can create sources of risk for macroeconomic and financial stability. The need for concerted action from all macroeconomic policies is even greater in a world of globalized capital markets, since, following pro-cyclical financial behavior or the accumulation of "excesses" during a boom, financial systems may amplify rather than mitigate the effect of shocks (González-Páramo, 2007).

5. Case study – capital account liberalization and inflation targeting adoption in Romania

In Romania, capital account liberalization and the adoption of inflation targeting were achieved relatively later (see Figure 9) than in other Central and Eastern European countries. There were several reasons for late capital account liberalization. First, the gradual approach to structural reforms and macrostabilization in the 1990s was reflected in higher inflation and interest rates as compared to other countries in the region and to EU countries. Second, the capital account liberalization had to be delayed until bank restructuring rendered the financial sector strong enough to deal with capital flows having a high reversibility potential. Third, the central bank needed to reach a comfortable international reserve coverage of prospective imports – this objective was attained in the first half of the current decade.

It is noteworthy that, despite this delay, the capital account liberalization was conducted in line with the following principles:

– inflows before outflows;

– medium- and long-term flows before short-term flows;

– direct investment before portfolio investment;

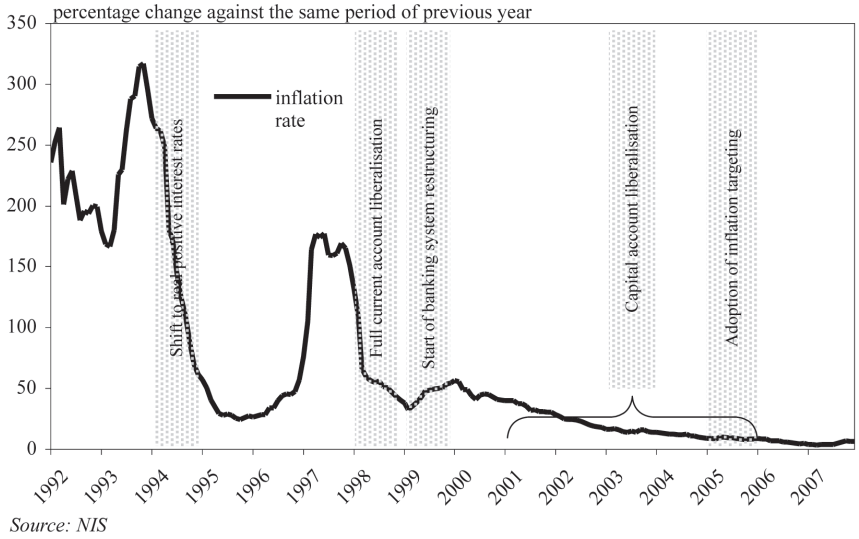
– observance of the banks – companies – households sequence.

Abiding by the above principles, full liberalization was completed in 2006, prior to Romania's accession to the EU, and overlapped with the shift to an inflation targeting strategy. This strategy was implemented in 2005, after being first considered in 2001, when it was mentioned in the Preaccession Economic Programme as the first option that the central bank took into account. The main rationales behind this choice were: i) the need for sustainable disinflation, including from the EU convergence perspective; ii) the instability of the relationship between monetary aggregates and inflation; iii) the fact that a

pegged exchange rate regime is extremely risky amid a convergence-induced appreciation trend and a progressive opening of the capital account.

An earlier adoption of inflation targeting was not possible as not all the preconditions were fulfilled, i.e. (i) the inflation rate was in the double-digit range; (ii) fiscal dominance, albeit declining, persisted in the form of the Public Finance Ministry's influence on not yet fully-fledged developed financial markets; (iii) the monetary policy transmission mechanism and the net debtor position of the NBR towards the banking system diminished the effectiveness of monetary policy actions; (iv) the central bank forecasting capacity was not sufficiently developed.

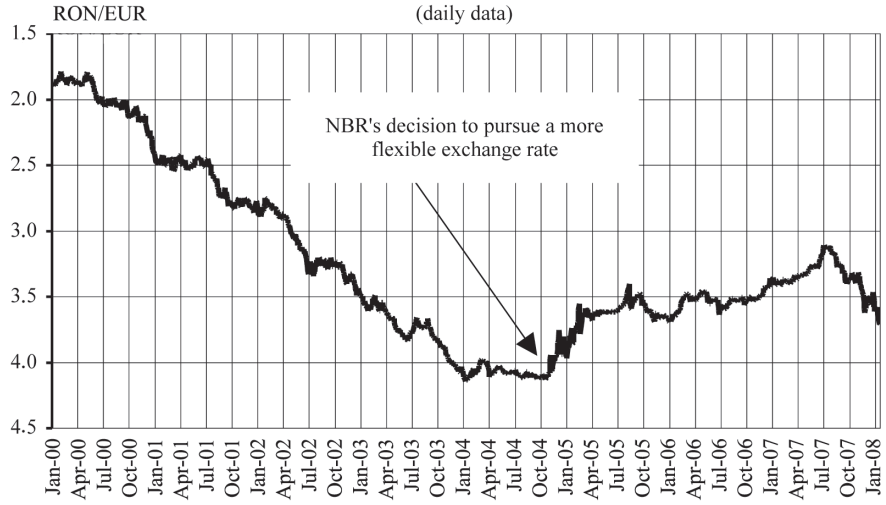
Figure 9. Calendar of the Measures Taken by the NBR
to Promote Price Stability and Financial Stability



Source: NIS

As Romania moved to inflation targeting in August 2005 and, in view of the EU accession, some short-term capital inflows previously postponed had to be liberalized by April 2005, large capital inflows ensued, and the decline in the interest rate differential was not enough to tame them.

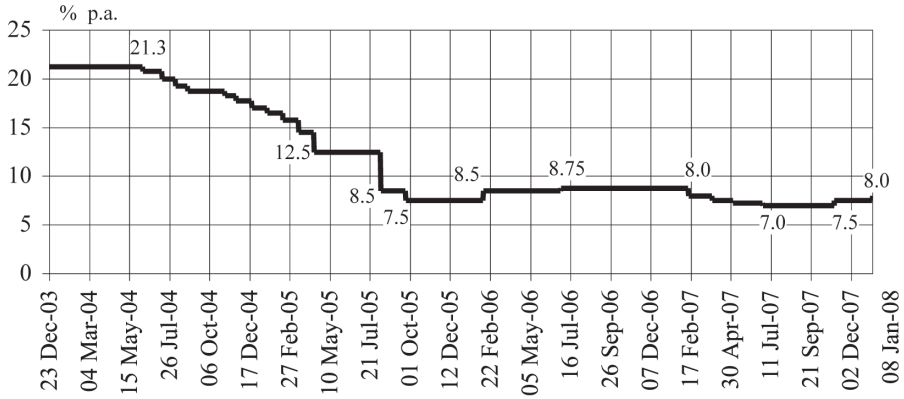
Figure 10. Forex Market Exchange Rate



Source: NBR

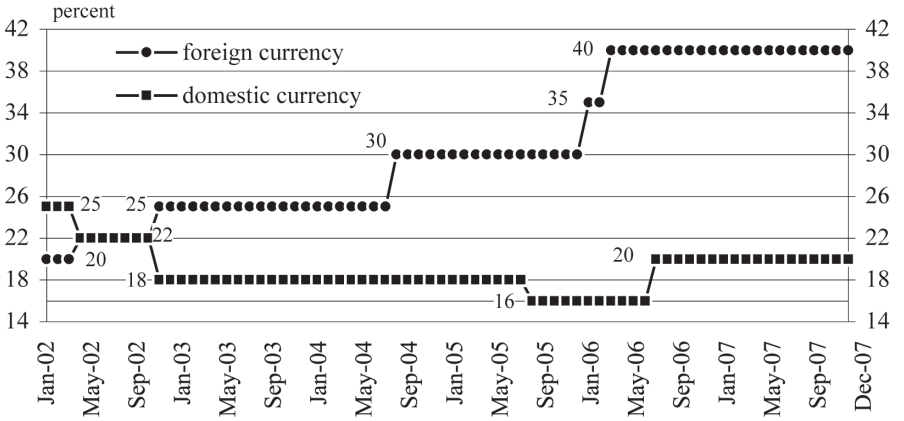
In these circumstances, a strategy to avoid getting caught in the impossible trinity needed to be formulated. Thus, the NBR embarked, starting with November 2004, on a policy of increased exchange rate flexibility (see Figure 10), intervening less frequently and less predictably, in order to try to avoid the vicious circle of money policy described in Figure 4. Concomitantly, with an aim to making the Romanian money market less attractive for speculative capitals, the National Bank of Romania steadily lowered its policy rate (see Figure 11) and mopped up only part of the liquidity surplus. With limited discretion and efficiency in adjusting its policy instrument in the absence of capital movement restrictions (e.g. an interest rate hike, while limiting domestic currency denominated credit growth, would have entailed a currency appreciation, ceteris paribus further raising the attractiveness of foreign exchange denominated credit), the central bank had to find other ways to ensure policy restrictiveness in face of buoyant aggregate demand. Overall, the monetary policy stance was tightened despite some significant reductions in the interest rate.

Figure 11. Policy Rate



In this respect, the minimum required reserves was actively used (see Figure 12), thus avoiding an excessive increase, from the perspective of financial stability, in the policy rate. Administrative and prudential measures were also adopted, combined with moral suasion of the banking sector and attempts to raise public awareness on exchange rate risk, with the aim of both supplementing traditional monetary policy instruments in curbing aggregate demand, and limiting the problem of a banking system asset-liability mismatch in what concerns the currency denomination (thus adding to the policy of higher minimum reserve requirements for foreign exchange denominated liabilities already in place).

Figure 12. Minimum Reserve Ratios



Source: NBR

The administrative and prudential measures package, updated several times, targeted both borrowers and lenders, aiming, on the one hand, at tightening the eligibility criteria for individuals and, on the other hand, at limiting the ability of banks to take on foreign exchange denominated exposure. Furthermore, legislation adopted in early 2006 enabled the NBR to exercise supervision over non-bank financial intermediaries, in order to contain spillovers from restrictions imposed by the NBR, such as increases in leasing activity as a substitute for bank intermediation. As a consequence, non-bank financial intermediaries became subject to the same regulations as commercial banks, such as capital adequacy constraints, eligibility criteria for customers, statistical reporting requirements, etc.

Romania's joining the European Union at the beginning of 2007, with the subsequent full freedom of provision of cross-border financial services via the single European passport, has made certain of these measures ineffective, since they would only affect domestically incorporated credit institutions. Therefore, the NBR has abolished the exposure limits to unhedged borrowers as of 1 January 2007. Also, changes were made in March 2007 to the above-mentioned loan-to-income limits on household indebtedness. Since then, credit institutions have been allowed to carry on lending activity based on internal risk assessment regulations, subject to their prior approval by the National Bank of Romania. Banks whose internal regulations have not been approved yet by the central bank continue to observe the 40 percent overall ceiling, as do non-bank financial institutions regulated and supervised by the NBR.

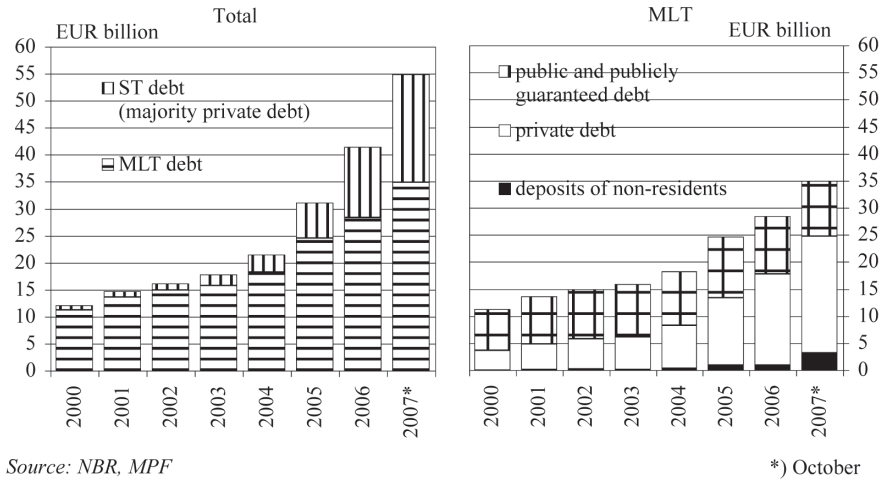
Romania's experience with prudential and administrative measures designed to limit the speed of credit growth shows that they are useful, but their effectiveness tends to erode over the medium run, as they become more porous and domestic credit institutions reconfigure their activity in order to avoid them. The collateral effect of these measures in Romania that accompanied a slowdown of foreign-exchange denominated credit growth has been that of a rebooking of credit with parent banking institutions (with some improvement in terms of domestic financial stability, but no decrease in the solvency of aggregate demand), as well as of direct borrowing abroad by corporate and higher net worth individuals, both resulting in a sharp pick-up in private foreign debt,

especially in short-term maturities (see Figure 13); this also suggests that prudential and administrative measures work together with more traditional policy tools, and that there are levels above which their side effects begin to render their further tightening counter-productive, additionally inducing the idea that a careful balance between assertiveness and caution must be employed when configuring their parameters within the toolkit of monetary policy.

By implementing these measures, the central bank was successful in bringing annual average inflation rate down from 11.9 percent in 2004 to 4.8 percent in 2007. Nevertheless, monetary policy could not avoid the steady widening of the current account deficit from 8.4 percent of GDP in 2004 to around 14 percent of GDP in 2007. This development could be regarded as normal in the context of the ongoing catching-up process of the Romanian economy and the ensuing investment growth.

However, the less desirable contribution of consumption growth should not be underemphasized. Recent developments are a cause for concern, as the weight of FDI in current account financing has declined in favor of its short-term, majority private, debt component, that climbed to an estimated EUR 20 billion in 2007 from EUR 2 billion in 2003 (see Figure 13). The increased reliance on short-term inflows renders the economy more vulnerable, especially in the wake of the recent international financial market turmoil generated by the subprime housing market crisis in the USA; if during periods of market optimism, investors seem less concerned with fundamentals, often contributing to creating the very imbalances they afterwards flee from, they become much more apprehensive in the aftermath of economic and financial shocks.

Figure 13. External Debt



Source: NBR, MPF

*) October

Looking to the future, the pace at which Romania's economy will advance in the area of real and nominal convergence will be largely dependent upon the overall consistency of the economic policies pursued by the authorities. In my opinion, it is essential that the major guidelines of economic programs should be observed relentlessly beyond the short horizon of an electoral cycle.

The path to euro adoption must be managed in a realistic and visionary manner, given that Romania's economy needs an adjustment period ahead of entering ERM II. This period should be treated as an opportunity of completing structural reforms and strengthening macroeconomic stability, not as a "break" that may result in early loosening of the macroeconomic policies.

The central bank has to ensure, by staying committed to its inflation targeting strategy, that inflation rate should gradually near the levels compatible with meeting the Maastricht criterion on price stability. Once low inflation has been consolidated, favorable conditions for sustainable fulfillment of nominal convergence criteria on long-term interest rate and exchange rate stability will be created. Concurrently, the pursuit of a cautious fiscal policy stance will bolster the sustainability of public finance. Under these conditions, Romania may enter the euro area at the horizon of the year 2014.

6. Conclusions

In an atmosphere of global financial interdependence and greater uncertainty, the ideal monetary policy should be characterized by commitment, time consistency, transparency, accountability, judgment, smoothness and flexibility, a set of attributes which, unavoidably, implies complexity (Solans, 2000). In addition, the central banks have to pay close attention to financial market developments, since a stable financial system is an important precondition for ensuring the smooth and efficient transmission of monetary policy, ultimately contributing to the achievement of the long-run price stability goal. In this respect, the systematic monitoring and assessment of financial stability conditions must be ensured, in order to enable the detection of key sources of risk and vulnerabilities for financial systems. However, these risks and vulnerabilities are not related only to developments within the sector itself, but also to changes in the macroeconomic environment.

Emerging economies in Central and Eastern Europe have embarked upon a bumpy ride towards achieving nominal and real convergence with the European Union, a process that poses significant challenges for the conduct of monetary policy. Prominent among them is to strike a good balance in the design of the interest rate policy in order to reach inflation targets without giving even more incentive for increased capital inflows, which could erode an economy's external competitiveness and long-term growth prospects. Striking a good balance requires the central bank be guided by the fundamental idea that there is no long-term trade-off between inflation and growth, and that commitment to long-run price stability is the only way to set the stage for long term growth via improved efficiency associated with low inflation levels. If forced to choose between rapid disinflation and the safeguarding of financial stability, the latter should take precedence, in order to ensure the long term fulfillment of the price stability objective. It is worth mentioning that the countries which embark on a disinflation path should choose an adequate disinflation pace so as to avoid a conflict with financial stability. In the long run, failure to maintain financial stability can only entail a renewed flare-up in inflation.

A smooth convergence process requires that all risks to its sustainability be regularly monitored and reappraised, since their magnitude and nature change over time. It is only in this way that policymakers can properly devise the role and stance of monetary policy – and of the other economic policies – in ensuring macroeconomic stability. I must emphasize the fact that monetary policy needs help from other policies, especially from prudent, not pro-cyclical, fiscal and income policies. I personally support the view that adopting a monetary policy rule (in a sense inflation targeting is a form of a rule) should be accompanied by a fiscal rule, as proposed by Woodford (2001).

The case of Romania shows that, when performed prior to completing preconditions in their entirety, capital account liberalization involves significant risks and renders the monetary policy conduct increasingly difficult. Romania's experience shows that using administrative decisions such as debt-to-income ratios for households might be effective in the short-run in buying the time needed for other policies to intervene and address imbalances. However, in the long-run, markets and private agents learn how to avoid the administrative restrictions and the problem remerges.

Over the medium and long term, the only viable solution is to design and implement a coherent macroeconomic policy mix, capable of supporting economic growth and, at the same time, limiting the vulnerabilities of the economy. Achieving such a policy mix is much more important than each policy taken separately. As far as monetary policy is concerned, its increased restrictiveness can but partly and temporarily offset the lack of support from structural reforms, fiscal and budgetary policies, and income policy, with the outcome being suboptimal in terms of real convergence in the medium and long term. Against this background, budgetary policy has a key role in keeping the external balance at sustainable levels. Thus, since the deterioration of the current accounts reflects real convergence, fiscal policy should make more room for the imbalance between saving and investment in the private sector and avoid being pro-cyclical. At the same time, income policy must not exert excessive pressure on the demand side and preclude the risk of wage growth outstripping productivity dynamics from materializing.

The absence of an adequate mix of macroeconomic policies, especially in view of the international environment tending to become less favorable than in previous years, along with unorthodox measures losing their impact or being abandoned following EU entry, could cause the risk of widening macroeconomic imbalances to gather strength. If the economic policies pursued by the authorities fail to cool down an overheated economy and to smoothly adjust the macroeconomic imbalances, the risk of a hard landing increases.

The liberalization of capital flows has supported the convergence process in Central and Eastern European countries in accordance with theory, yet it also deepened their vulnerability towards external financial shocks and the ensuing investors' mood swing, especially in the present context, characterized by an awakening of global financial markets from an episode of prolonged exuberance. However, the renewed interest in fundamentals on behalf of the investors has long-term benefits, as it should provide the necessary stimulus towards more discipline in macroeconomic policies, enabling them to address successfully the existing imbalances.

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Es un honor para la Real Academia de Ciencias Económicas y Financieras de España poder dar la bienvenida y recibir en su seno al Profesor Mugur Isarescu y una honra muy especial para mí responder al Académico Correspondiente para Rumanía, país con el que desde hace ya 17 años me unen unos lazos muy especiales y que he visitado en diversas ocasiones.

El Profesor Mugur Isarescu es antiguo amigo de esta Academia. Recuérdese al respecto la Sesión Científica Común de la Academia Rumana y de nuestra Real Institución sobre el tema "Las dos Fronteras de Europa", celebrada en Bucarest el 20 de junio de 2005, en la que el Profesor Isarescu disertó sobre "Los nuevos y futuros Estados miembros. El papel de Rumania en una Unión Europea con 24 países". En su persona encontramos las tres características que deseamos para nuestra Academia y que el Pofesor Isarescu viene a reforzar: el aspecto mediterráneo, por su nacimiento y su dedicación profesional, y el europeo y el internacional, por los diversos cargos que desempeña en estos ámbitos.

Presidente de la Asociación Rumana del Club de Roma, Miembro de la Comisión Trilateral, Miembro del Comité Consultivo de la Oficina Regional para Europa y la Comunidad de Estados Independientes dentro del Programa de Naciones Unidas para el Desarrollo, Presidente del Club de Gobernadores de los Bancos Centrales en la Región del Mar Negro, los Balcanes y Asia Central, Vicegobernador por Rumanía en el Banco Europeo para la Reconstrucción y el Desarrollo, Vicegobernador por Rumanía del Consejo de Gobernadores del Banco Mundial y Titular por Rumanía del Consejo de Gobernadores del Fondo Monetario Internacional.

A estos cargos hay que añadir el de Gobernador del Banco de Rumanía, nombrado por el Gobierno en 1990 y ratificado por el Parlamento en 1991, cargo en el que fue confirmado por el Parlamento en Diciembre de 1998 y Noviembre

de 2004, y el cargo de Primer Ministro de Rumanía, que ejerció durante 12 meses (diciembre de 1999 a Diciembre del 2000).

Como Gobernador del Banco Nacional de Rumanía, recibió el mandato preciso de aplicar la reforma del sistema bancario conforme a los estándares internacionales.

Como Gobernador del Banco Nacional, titular por Rumanía del Consejo de Gobernadores del Fondo Monetario Internacional y Vicegobernador del Banco Mundial entre 1997 y 1998, Isarescu elaboró y sometió al Parlamento por cuenta del Gobierno un paquete legal para armonizar el sistema bancario rumano con las normativas de la Unión Europea, a la que el país solicitó el ingreso en junio de 1995.

En este sentido, Isarescu insistió ante los poderes políticos para que pisasen el acelerador de las reformas económicas y, fundamentalmente en los años en que gobernó el Frente de Salvación Nacional y sus partidos herederos de Ion Iliescu, advirtió contra la tentación de combinar las políticas de mercado con fórmulas intervencionistas, ya que un modelo de economía mixta, en su opinión, provocaría una hiperinflación de manera automática. Isarescu fue el responsable de negociar con el Fondo Monetario Internacional y el Banco Mundial la concesión de préstamos para financiar las reformas estructurales que la economía rumana precisaba y la amortización de la deuda exterior, y gozó de una amplia autonomía a la hora de definir las políticas monetarias para controlar la inflación y fortalecer la moneda nacional.

El nombramiento de Isarescu como primer ministro fue consecuencia de la dimisión forzada, el 13 de diciembre de 1999, del primer ministro Radu Vasile. Se planteó entonces la necesidad de encontrar un sustituto con un perfil tecnocrático, capaz de dirigir el Gobierno hasta las elecciones generales del año siguiente y, entre tanto, de tratar con la Unión Europea y los agentes financieros internacionales. El 16 de diciembre el presidente Emil Constantinescu nombró a Isarescu por considerarle el "buen negociador" y el "experto económico" que el país necesitaba en esos meses de transición.

El 21 de diciembre de ese mismo año el Parlamento aprobó la candidatura de Isarescu por 305 votos a favor y 35 en contra. Isarescu, que acababa de ser reelegido al frente del Banco Nacional por otros cinco años, no tuvo que cesar en el cargo al concederle el Parlamento una simple excedencia por el tiempo que durase su mandato gubernamental.

En el campo científico y de la investigación, el Profesor Isarescu es también una personalidad. Además de su tesis doctoral sobre políticas de tipos de cambio y de sus más de 300 publicaciones, como autor, coautor o coordinador, conviene recordar sus 19 años de investigación en la Academia de Estudios Económicos de Bucarest, la mayoría de ellos al frente de un equipo de investigadores. Desde 1975 desempeñó también labores lectivas como conferenciante y profesor en su antigua Academia, cimentando su prestigio como experto en cuestiones financieras y monetarias y en relaciones económicas internacionales. Isarescu impartió la asignatura de Políticas Monetarias en la Universidad Occidental de Timisoara entre 1994 y 1996, y en la Academia de Estudios Económicos de Bucarest durante 1995. Isarescu es también miembro fundador de la Sociedad Rumana de estudios económicos (SOREC) y Vicepresidente de la Asociación por el Derecho Internacional y las Relaciones Internacionales (ADIRI).

Como honor a toda esta labor profesional, docente y de investigación, ahí está el reconocimiento internacional de numerosos organismos y universidades: Doctor Honoris Causa por la Universidad de Cracovia, en Polonia, de las Universidades de Pitesti y de Maia Mare, en Rumanía, y las condecoraciones de la Gran Cruz "La Estrella de Rumanía, la orden del "Mérito Industrial y Comercial", la Orden de "Gran Cruz del Sur", la condecoración brasileña más importante concedida a un extranjero, la Cruz de Moldavia, la Cruz de San Andrés, la Cruz de Transilvania y un largo etcétera.

Tenemos ante nosotros a una personalidad multivalente, multicultural, multilingüe, una persona comprometida con la sociedad, una persona, que sin pertenecer a ningún partido político, está comprometida con la Política en mayúscula.

El profesor Isarescu nos ha expuesto en su brillante discurso los problemas de la política monetaria de una economía emergente, centrándose, sobre todo, en la política monetaria de su país, Rumanía, problemas que de alguna forma en un día no muy lejano afectaron también a España, y algunos de los cuales, además, dada la pertenencia de Rumania a la Unión Europea, nos son comunes.

Gran parte de su discurso está dedicado al papel que juegan en la economía de un país la estabilidad financiera y la estabilidad de los precios.

Según el profesor Isarescu,"la política monetaria debe proponerse como objetivo la estabilidad de los precios", "la estabilidad de los precios es beneficiosa para todos". Al hablar de la relación entre la inflación y el desempleo, nos recuerda que "la estabilidad de los precios es el fin primordial de una política monetaria a largo plazo. La estabilidad de los precios, nos dice, no es solamente algo que la política monetaria puede lograr, es lo mejor que puede lograr desde el punto de vista del bienestar social global".

Podríamos decir que esto vale tanto para las economías industrializadas como para las economías emergentes, pero como estas últimas están expuestas a ciertos factores que pueden poner en peligro su estabilidad, como son los movimientos imprevistos en los precios de los alimentos y de la energía, los precios administrados y las corrientes masivas de capital a través de las inversiones extranjeras directas, su tarea es mucho más ardua.

A todas estas dificultades con que se encuentra la política monetaria de Rumanía y que pueden ser un grave obstáculo a la estabilidad de los precios, hay que añadir el proceso de privatización de las empresas del país y la necesidad de adaptarse a los criterios de convergencia de Maastricht, es decir: estabilidad de precios, situación de las finanzas públicas, tipo de cambio y tipos de interés a largo plazo, ya que Rumania se encuentra dentro de la Unión Europea y pretende pasar a la tercera fase de la Unión Económica y Monetaria, es decir ingresar en la Zona del Euro.

Para superar todas estas dificultades, la política monetaria debe ir acompañada de las demás políticas económicas, como la política fiscal, la política cam-

biaria, la política de ingresos, es decir toda una combinación de las políticas económicas (una politic mix).

Voy a centrarme en la afirmación del profesor Isarescu de que la estabilidad de los precios es el fin primordial de toda política financiera y de que lo es precisamente desde un punto de vista del bienestar social global. Y lo hago porque creo que tiene en sí relevancia suficiente como para que le dedique una especial atención. Esta afirmación coincide casi literalmente, en cuanto a su primera parte, con el inicio del artículo 105 del Tratado Constitutivo de la Comunidad Europea, que establece: "El objetivo principal del Sistema Europeo de Bancos Centrales (es decir del Banco Central Europeo más los Bancos Centrales de los Estados Miembros) será mantener la estabilidad de precios". Ni siquiera se fija el doble objetivo de la Reserva Federal, el Banco Central de los Estados Unidos, que es no sólo la de garantizar la estabilidad de los precios, sino también fomentar el crecimiento y el pleno empleo.

Al parecer, la estabilidad de los precios es para el Banco Central Europeo el fundamento de toda política económica de la Unión Europea. Pero, como en el Tratado de la Comunidad Europea no encontramos un desarrollo de este principio, nos vemos obligados a buscar la razón del mismo, siguiendo la exposición del Profesor Isarescu.

¿Qué relación tiene la estabilidad de los precios con el bienestar social?.

Voy a dejar de lado el argumento de la relación entre estabilidad de los precios y desarrollo económico o el argumento contrario: la relación entre aumento de precios y desaceleración económica. De por sí, esta relación ya sería suficiente para justificar la estabilidad de los precios, pues dicha estabilidad fomenta la producción y sin producción no hay riqueza y sin riqueza no hay bienestar social. Por estabilidad de los precios se entiende lógicamente no una estabilidad absoluta, sino un tipo relativamente bajo de inflación.

Además de este efecto indirecto de la estabilidad de los precios sobre el bienestar social, es decir a través de la mayor producción, existe una relación directa, no siempre fácil de distinguir de la indirecta, entre estabilidad de precios

y bienestar social. William Easterly y Stanley Fisher, profesor y antiguo director general del Fondo Monetario Internacional respectivamente, hablando de la inflación, dicen que sus efectos se manifiestan en forma directa sobre la calidad de vida de sus habitantes, especialmente los más pobres. La inflación es un impuesto injusto, es regresivo, pues en términos relativos afecta más a los individuos más pobres. La gente de mayores ingresos puede protegerse mejor, ya que tienen acceso a instrumentos financieros que les permiten cubrirse, mientras que los más pobres suelen mantener solamente dinero en efectivo, dinero que, como sabemos, pierde valor en períodos inflacionarios. Los ingresos de los más pobres se reajustan con retraso y si la inflación es alta van perdiendo poder adquisitivo, es decir, la inflación actúa como un recorte en el presupuesto familiar. Los pobres también dependen más de los ingresos que el Estado les provee, y, como las pensiones, las transferencias y otros subsidios no están completamente indexados, pierden valor en términos reales. Según ellos, los individuos más pobres muestran estadísticamente una mayor preocupación por la inflación que los individuos más ricos.

En otro estudio Stanley Fischer (1991) analiza el período 1970-1985 de 73 países y encuentra una reducción de 0,7 puntos porcentuales en el crecimiento económico ante un incremento del 10% en la inflación. La caída del producto ocurre por el efecto nocivo de la inestabilidad de precios sobre la inversión. De hecho, el estudio desagrega el impacto: 0,5 puntos porcentuales por menor eficiencia de la inversión y 0,2 puntos porcentuales por un menor aumento de la inversión.

Easterly y Fischer examinan posteriormente (1999) la relación entre inflación y pobreza. Su estudio analiza la información de 31.869 hogares en 38 países y confirman una relación negativa entre la inflación y el porcentaje de la riqueza nacional de los más pobres, y entre los niveles de pobreza y el salario mínimo real. Así, un incremento en la inflación de 0 a 20% reduce el salario mínimo real en 8 puntos porcentuales por cada año de inflación elevada; además, las altas tasas de inflación disminuyen en 1,7% la participación de la riqueza de la población más pobre. Los autores confirman que la inflación es el impuesto más cruel, pues perjudica en mayor medida a los más pobres.

Los estudios empíricos y los teóricos, constatan de forma contundente una relación inversa entre el producto y la variación en los precios. Los resultados muestran cómo una inflación baja y estable incrementa la certidumbre, el ahorro, la inversión y el bienestar social y además, reduce la pobreza y mejora la distribución de la riqueza.

De estos estudios podríamos extraer a modo de corolario las siguientes conclusiones respecto a la estabilidad de los precios:

A) Conduce a una mejora del nivel de vida porque contribuye a reducir el grado de incertidumbre respecto a la evolución general de los precios y, en consecuencia, aumenta la transparencia de los precios relativos. La estabilidad de precios permite a los consumidores identificar con más facilidad las variaciones de los precios de los bienes en relación con los precios de otros bienes (es decir, los «precios relativos»), puesto que tales variaciones no están enmascaradas por las fluctuaciones del nivel general de precios. La incertidumbre acerca de la tasa de inflación podría también inducir a las empresas a adoptar decisiones erróneas en relación con el empleo.

B) Reduce las primas de riesgo de inflación de los tipos de interés. Si los acreedores tienen la seguridad de que los precios se mantendrán estables en el futuro, no exigirán un beneficio adicional (una «prima de riesgo de inflación») a fin de compensar los riesgos de inflación relacionados con la tenencia de activos nominales a largo plazo. Debido a esta reducción de las primas de riesgo y, por tanto, de los tipos de interés nominales, la estabilidad de precios contribuye a mejorar la eficiencia de los mercados de capital a la hora de asignar recursos y, de esta forma, incentiva la inversión. Esto fomenta la creación de puestos de trabajo y, en términos más generales, el bienestar económico.

C) Elimina actividades de cobertura del riesgo innecesarias. En un entorno de inflación elevada hay un incentivo para almacenar productos, debido a que en estas circunstancias conservan su valor en mayor medida que el dinero o algunos activos financieros. Sin embargo, el almacenamiento de una cantidad excesiva de bienes no es, evidentemente, una decisión de inversión eficiente y obstaculiza el crecimiento de la economía y de la renta real.

D) Los sistemas fiscales y de prestaciones sociales pueden crear incentivos que distorsionan el comportamiento de la economía. En muchos casos, la inflación o la deflación agravan estas distorsiones, por cuanto que los sistemas impositivos no suelen permitir la indiciación de los tipos impositivos y de las contribuciones a la seguridad social a la tasa de inflación. Por ejemplo, los incrementos salariales que tienen como objetivo compensar a los trabajadores por el aumento de la inflación podrían tener como consecuencia que al trabajador se le aplique un tipo impositivo más elevado; a este fenómeno se le denomina «progresión fría».

E) El mantenimiento de la estabilidad de precios evita los agudos problemas económicos, sociales y políticos relacionados con la redistribución arbitraria de la riqueza y de la renta que se observan en épocas de inflación y deflación. Esto resulta particularmente cierto cuando las variaciones del nivel de precios son difíciles de predecir, y para los grupos sociales que tienen dificultades para proteger el valor nominal de sus activos frente a la inflación. Por ejemplo, si se produce un incremento inesperado de la inflación, todo el que tenga activos nominales como contratos de trabajo a largo plazo, depósitos bancarios o bonos del tesoro a largo plazo, experimenta pérdidas en el valor real de los mismos. La riqueza se transfiere de forma arbitraria de prestamistas (o ahorradores) a prestatarios porque con el dinero con el que, efectivamente, se devuelve un préstamo pueden comprarse menos bienes de lo que se esperaba en el momento en que se otorgó el mismo. Si se produce una situación imprevista de deflación, aquéllos que tengan activos nominales podrían tener ganancias, porque el valor de estos activos (p. ej. salarios o depósitos) aumenta. No obstante, en tiempos de deflación, ocurre a menudo que los prestatarios o los deudores no pueden pagar sus deudas y podrían incluso declarase insolventes.

Tal como se demostró en diversos momentos del siglo XX, un nivel elevado de las tasas de inflación genera frecuentemente inestabilidad social y política, puesto que los grupos a los que perjudica se sienten burlados si las cargas (inesperadas) de la inflación se llevan una parte importante de sus ahorros.

Todos estos argumentos sugieren que un Banco Central que mantiene la estabilidad de precios contribuye sustancialmente al logro de objetivos económicos más amplios, como niveles de vida y de actividad económica y de empleo más altos y estables. Esta conclusión encuentra respaldo en los datos de la investigación económica que, en relación con muy diversos países, metodologías y períodos, demuestra que, a largo plazo, las economías con menos inflación crecen en promedio más rápidamente en términos reales.

En este sentido, estamos convencidos de que Rumanía sigue por el buen camino. En junio de 2004 adoptó una nueva ley modificando los estatutos del Banco Nacional de Rumanía, con el fin de reforzar su independencia y mantener la estabilidad de precios, poniendo fin al acceso privilegiado del sector público a las instituciones financieras y prohibiendo al Banco Nacional de Rumanía comprar obligaciones del Estado en el mercado primario. Esta ley prevé también la ampliación de la gama de activos que pueden servir de garantía para préstamos concedidos por el Banco Nacional de Rumanía, así como la supresión de la obligación de facilitar títulos garantizados por el Estado. Por otra parte, una segunda ley, adoptada también en junio de 2004, prevé la creación y funcionamiento del Fondo de Garantía de Depósitos en el sistema bancario y deroga las disposiciones que prevén la posibilidad de pedir prestado al Banco Nacional de Rumanía para consolidar los recursos del Fondo y responder a demandas importantes.

Antes de finalizar quiero felicitar nuevamente al Profesor Isarescu por su magnífico discurso de recepción como Académico Correspondiente para Rumanía. No dudo de que su ingreso significará un gran enriquecimiento para nuestra Real Corporación. Su prestigio internacional y su colaboración contribuirán a la mejora de la ciencia y de la comunidad de nuestros dos países.

Muchas gracias por su atención.

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