

ROMANIAN LOCAL GOVERNMENTS' INDEBTEDNESS – A MACROECONOMIC AND TERRITORIAL APPROACH

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Abstract

Financing local activities at an appropriate level by reference to local communities' development needs cannot be left, especially where these needs are major, solely to the account of ordinary resources, but loan resources must complete them. However, the existence of a legal framework allowing for local governments to borrow and the fulfillment of the legal requirements do not guarantee that local communities will make use of loans to raise additional resources and finance their development needs, as a number of factors interfere.

On this basis, we intend to analyze Romanian local governments' indebtedness as well as the particular forms that it takes, both at macroeconomic level, aiming to assess the overall debt of all Romanian local governments and from a territorial perspective, aiming to highlight the discrepancies in promoting local indebtedness for various types of local communities. Our approach combines the quantitative analysis, based on processed data from the Ministry of Public Finance, with the analysis of the involved qualitative issues.

Our main conclusion is that until now the local indebtedness potential has not been exploited enough to make its contribution to the financing of local investments and the development of local communities, the main driving factors being the low involvement of local governments, the limited local economic base and financial potential, the fluctuating and perfectible legal framework but also the national and international social and economic conditions.

Keywords: local governments, local indebtedness, debt sources, local development

JEL classification: H74, H81

1. INTRODUCTION

Financing local communities' needs is usually done, in normal times, through ordinary financial resources, mobilized from sources over which the right of decision mainly goes to

local authorities. However, the economic and social conditions or the effective development needs of different administrative-territorial units often engender imbalances between the expenditures to be made and the revenues normally possible to be raised, in which context indebtedness sometimes reveals itself as the sole applicable option. From this point of view, the legal recognition of local communities' access to loan resources reflects their vocation for financial autonomy, vocation which materializes to the extent that the legal indebtedness capacity is exploited by borrowing.

Practically, a higher indebtedness capacity (in terms of the legal requirements to be met) does not ever guarantee that that community will raise additional resources to finance its development needs, as a number of factors of influence always interfere. For the particular case of Romania, where inter and intraregional development disparities and correlatively, development needs, especially of infrastructure, are obvious, raising additional financial resources to local budgets proves to be vital, which raises the issue of local communities' real access to those resources. Although the basic problem appears to be, by itself, that of local borrowing, it is important to reveal, in this context, the specific links that can and should be established with other categories of available resources, mainly the structural funds. Thus, accessing EU funds financing often involves co-financing (possible to be obtained by borrowing) and further, resources from European funds will finally bring their contribution to the creation of local (additional) tax base and will generate favorable conditions for contracting and reimbursement of future loans. On this background, at least two conditions must be met: the access to loan resources must be conditional on the use of these resources to finance capital expenditures and not current ones and loans for co-financing European projects must be distinctively treated when assessing local indebtedness capacity.

From a wider perspective, the recognition of local governments' access to loan resources must be connected to the internal logic of the budget system, being well known its quality to operate on the principle of communicating vessels. To the extent that the autonomous or heteronomous debt limits apply to the central budget, we must note that financing local current needs through transfers may practically generate a repercussion of local public debt on the state budget deficit, which calls for both the correlation of central and local governments' debt limits and the establishment of an "alarm system" in steps (restricting access to borrowing at a certain debt limit and, subsequently, even banning it).

As we shall see, however, a careful analysis of local indebtedness and its sources in Romania, compared with the situation of other EU member states, shows that the theoretical possibility of raising additional resources for the benefit of local communities is not quite enough exploited, rather being "a privilege of the rich" (regions or administrative units), although the pressure of the need for development is obviously greater for communities "lagging behind".

2. THE SUBJECT OF THE RESEARCH, METHODOLOGY AND STATE OF KNOWLEDGE

The scope of this study is to analyze Romanian local governments' indebtedness as well as the particular forms that it takes. The analysis is further developed in two different directions, namely the macroeconomic approach that aims to assess the overall local indebtedness and its sources for all Romanian local communities and, respectively, the territorial approach (by development regions, urban/rural areas, type of administrative divisions) that aims to highlight the particularities/discrepancies in promoting local indebtedness, in direct

correlation with the disparities in development existing in our country between various types of local communities.

Our approach combines the quantitative analysis, primarily based on processed data from the Ministry of Public Finance's reports on public debt and budget execution (2000-2010) as well as data from the Ministry of Public Finance on the territorial breakdown of local government debt and its service (2009), with the analysis and monitoring of the involved qualitative issues. In interpreting results and formulating public policy recommendations, our analysis has permanently related to the legal framework in work over the considered period of time.

The issue proposed for debate did not represent the subject of a major and distinctive research in Romanian literature, partially being captured in the broader context of treating local public finances or public budgetary system issues. Thus, I Văcărel and others [Văcărel, 2006, 591-602], N. Hoanta [Hoanta, 2000, 264-271] and Gh. Voinea [Voinea, 2008, 102-103] approach the issue of local governments' loans (considered to be in close relationship with local autonomy) when analyzing the financing resources of local activities, without giving a quantitative picture of the actual use of loan resources by local governments in Romania and other countries. T. Mosteanu and others [Mosteanu, 2004, 248-259 and 286-287] provide a more consistent approach on this subject, treating in detail the issue of municipal bonds (legal framework regulating their issuing, Romanian practice etc.) and clarifying the basics on the concept of local public debt. Although theoretical (and sometimes even empirical) approaches are not missing from Romanian specialized literature, the main gap that the authors of this paper aim to fill stems from the lack of a consistent quantitative analysis to show the degree to which Romanian local governments actually take advantage of the opportunities created by the law, resorting to debt financing in order to complete their own resources, and the determinants of their behavior. Moreover, for the first time, the paper approaches local indebtedness from a territorial perspective, highlighting how the disparities in development between different types of Romanian local communities impact on their access to loan resources.

3. ANALYSIS OF ROMANIAN LOCAL GOVERNMENTS' INDEBTEDNESS AND ITS SOURCES - A MACROECONOMIC PERSPECTIVE

The accumulation of local public debt in Romania mainly occurred since 2000, on the background of the developments in local governments' capacity to use public borrowing in order to finance local interest investment projects, in the context of the comprehensive program of reforms initiated in local public administration since 1998 and resulting in enhanced financial autonomy of local governments. From this perspective, trends in our country have apparently been in contradiction, in the sense that as the level of local governments' own revenues increased, as a result of the legislative reforms of local public finance, local public debt increased too, on the background of the recognition of the ability of local governments to contract and guarantee loans, since 1998. In these circumstances, the growing amount of own revenues, yet still well below local expenditures or the actual requirements of local development (especially infrastructure), have led to encouraging local governments to contract or guarantee local loans, synthetic data regarding the size and evolution of local public debt being presented in Table no. 1.

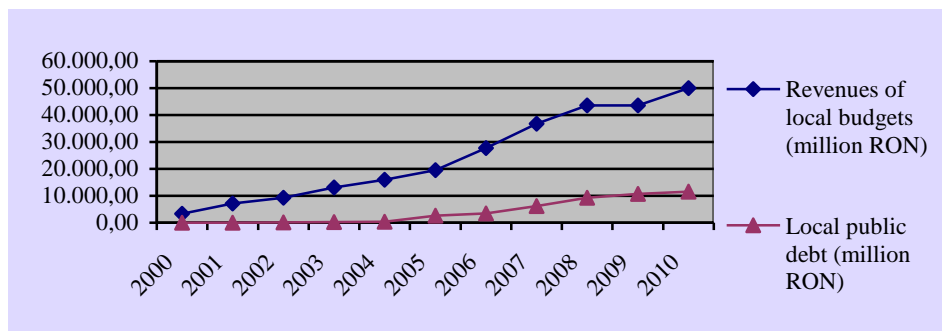
Table no. 1 The evolution of local public debt (2000-2010)

Local public debt	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
million RON	3,3	41,4	73,6	226,7	404,9	2629,0	3472,3	6174,7	9238,6	10828,7	11572,5
million EUR	1,4	14,9	21,1	55,1	102,1	715,0	1026,8	1710,4	2317,8	2536,2	2694,0
% of GDP	0,00	0,04	0,05	0,11	0,16	0,91	1,01	1,50	1,83	2,20	2,25
% of general government debt	0,01	0,12	0,17	0,44	0,73	4,46	5,48	7,50	8,41	7,35	5,98

Source: [Ministry of Public Finance, 2011a and authors' own calculations]

As can be noticed from the data presented in Table no. 1, local public debt was practically non-existent in Romania before 2000. Later on it began to rise from 0,01% of general government debt in 2000 to 8,41% in late 2008. Although the upward trend of local public debt continued in 2009 and 2010, as the international economic and financial crisis affected quite strongly our country, central government started to incur massive debt, which resulted in the reduction of the share of local public debt in general government debt to 5,98% at the end of 2010. A similar trend can be observed when analyzing local public debt as a share of GDP, which increased from 0,04% in 2001 to 2,2% in 2009 and 2,25% at the end of 2010. Thus, recourse to public indebtedness proved to be in Romania one of the viable solutions possible to be applied by local governments to finance investment projects, mainly in infrastructure, so necessary for the fulfillment of the European integration requirements.

From a comparative perspective, as shown in Figure no.1, the upward trend in nominal local public debt registered, however, a less pronounced dynamics when compared to that of the overall revenues of local budgets, trend which may be explained by the sometimes exaggerated prudence of local governments, but also by the lack of a global (legal, economic, financial) environment favorable to local indebtedness.

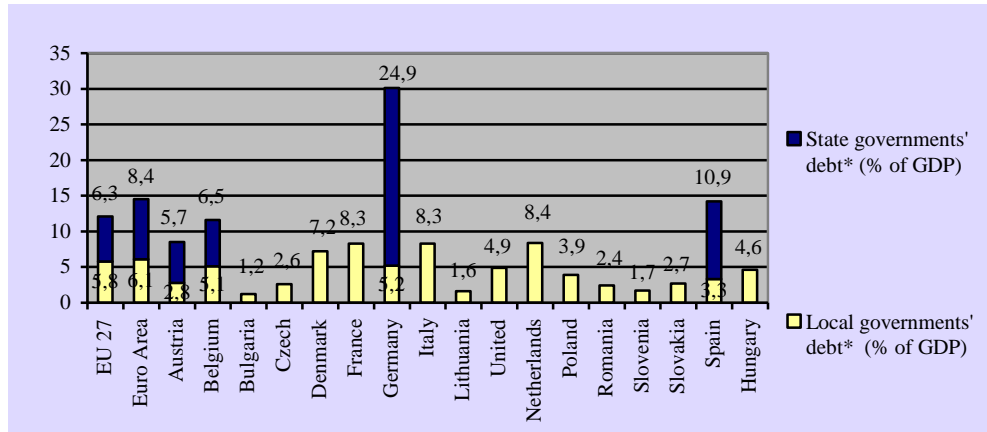


Source: [Ministry of Public Finance, 2011a and 2011b], [National Institute of Statistics, 2011] and author's own calculations

Figure no. 1 The comparative evolution of local public debt and local budgets' revenues (2000-2010)

However, local public debt is still relatively low in Romania, when compared to the EU average debt level of subnational governments. In Figure no. 2 one can see that the latter represented, at the end of 2010, approximately 12,1% of GDP, out of which 6,3% was state

governments' debt, compared to only 2,4% of GDP in Romania. At the same time, in euro area Member States the subnational governments' average debt represented 14,5% of GDP, out of which 8,4% was state governments' debt.



* according to EU methodology ESA 95

Source: [European Commission, 2011]

Figure no. 2 Subnational governments' debt in European Union Member States (2010)

Among the most indebted subnational governments were those of the EU15 Member States, both federal states like Germany (30,1% of GDP), Spain (14,2% of GDP) and Belgium (11,6% of GDP), where state governments' debt had an important contribution (for example, in Germany, lands' debt represented 24,9% of GDP and that of the autonomous communities, in Spain, 10,9% of GDP) and unitary states like France (8,3% of GDP), Italy (8,3% of GDP), Netherlands (8,4% of GDP) and Denmark (7,2% of GDP).

Romania's situation proves to be similar to that of the new Member States which joined EU in 2004 and 2007, most of them from Central and Eastern Europe. At the end of 2010, local public debt represented 1,2% in Bulgaria, 3,9% in Poland, 2,7% in Slovakia, 2,6% in the Czech Republic and 4,6% in Hungary, a much lower level than the one registered in EU15 developed Member States.

This situation can have many explanations being the result of both the lack of experience and unwillingness of local authorities in these countries to use debt resources and the underdeveloped legal framework ([Dafflon, 2009] and [Freire, 2004]). From another perspective, one can admit that, given the smaller amount of financial resources collected to local budgets (main source for the repayment of loans and payment of interest outlays), including as a result of the lower economic development stage, the level of public debt that local governments in these countries can sustain is generally lower. One of the conclusions highlighted in the literature on government debt, which we consider to be perfectly applicable to subnational level, is that less developed countries record lower affordability thresholds and may encounter problems in honoring their financial obligations at much lower public debt levels compared to developed countries [Callen, 2003, 120].

When analyzing the size and evolution of local public debt by its main components, namely domestic and external debt, taking into account the source of loan resources, we find that the access of local governments to borrowing on the internal debt market and the accu-

mulation of domestic local debt are relatively new, as it results from the data presented in table no. 2.

Table no. 2 Domestic and external local public debt indicators (2000-2009)

Domestic and external local public debt		2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
<i>Domestic local public debt</i>	<i>million RON</i>	3,3	41,4	63,5	196,7	341,0	671,7	1542,7	3296,6	5673,5	6612,6
	<i>% of GDP</i>	0,00	0,04	0,04	0,10	0,14	0,23	0,45	0,80	1,13	1,35
	<i>% of overall local public debt</i>	100	100	86,25	86,76	84,22	25,55	44,43	53,39	61,41	61,66
<i>External local public debt</i>	<i>million RON</i>	0,0	0,0	10,1	30,0	63,9	1957,3	1929,6	2878,1	3565,1	4110,9
	<i>% of GDP</i>	0,00	0,00	0,01	0,02	0,03	0,68	0,56	0,70	0,71	0,84
	<i>% of overall local public debt</i>	0,00	0,00	13,75	13,24	15,78	74,55	55,57	46,61	38,59	38,34

Source: [Ministry of Public Finance, 2011a and authors' own calculations]

Domestic local public debt represented only 0,04% of GDP in 2001 and it increased to 1,35% of GDP until 2009. A similar situation can be noticed in the case of external local public debt, which increased from 0,01% of GDP in 2002 to 0,84% in 2009. As a share of the overall local public debt, if between 2000 and 2004 domestic local public debt represented more than 80%, it afterwards substantially reduced, hovering at around 60% in recent years.

We must however mention that the conclusions of the previous analysis of local public debt breakdown by the source of loan resources are consistently influenced by a single loan, that of the city of Bucuresti, placed on the foreign capital markets in 2005, worth 500 million Euro. In the absence of this loan, the situation would change fundamentally; we can estimate that the external local public debt would have been, in this case, at the end of 2009, of no more than 25% of the overall local public debt (compared to 38,34%, which it was in reality), evidence of a still limited access of Romanian local authorities to external borrowing, especially on international capital markets.

Although local public debt's breakdown by the source of loans can be in some ways relevant, we consider it to be more significant the breakdown by the currency of denomination, based on the finding that a large amount of debt denominated in foreign currency exposes local authorities (the revenues of which are collected in national currency) to a great currency risk, especially when important fluctuations of the exchange rate are registered. On the other hand, it is admitted that under the continuous depreciation of national currencies, financing in a foreign, more stable currency, can be appealing when considering the financing costs, allowing for local authorities to contract loans at lower interest rates and thus reduce annual interest expenditures. Relevant data on local public debt's breakdown by the currency of denomination are presented in Table no. 3.

Table no. 3 Local public debt's breakdown by the currency of the contract (2000-2010)

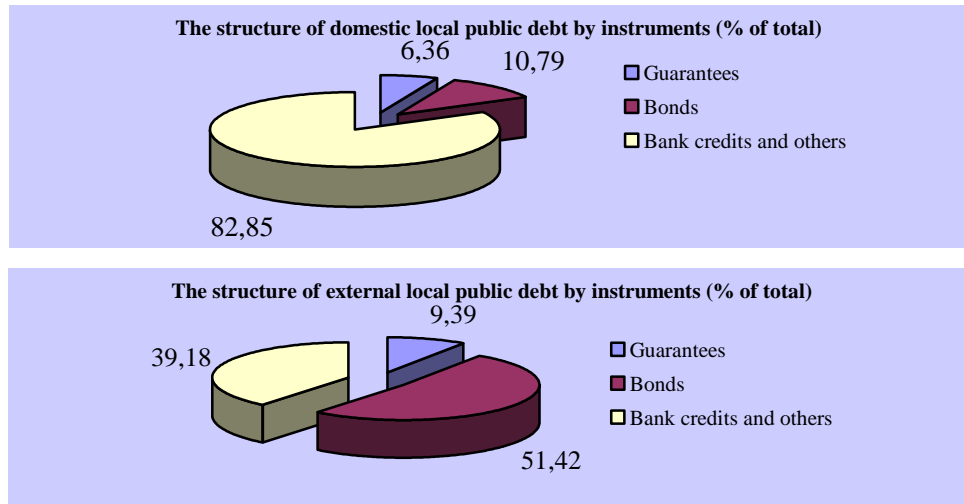
Local public debt by currency of denomination		2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
RON	million RON	3,3	41,4	63,5	196,7	608,6	671,7	1393,2	3296,6	5422,5	6494,9	6966,9
	% of the overall local public debt	100,0	100,0	86,3	86,8	90,5	25,6	40,1	53,3	58,7	59,9	60,2
EURO	million RON	0,0	0,0	10,1	29,9	63,8	1957,4	2072,8	2843,9	3783,1	4321,1	4594,0
	% of the overall local public debt	0,0	0,0	13,7	13,2	9,5	74,5	59,7	46,1	40,9	39,9	39,7
USD	million RON	0,0	0,0	0,0	0,0	0,0	0,0	6,3	34,2	33,0	19,2	11,6
	% of the overall local public debt	0,0	0,0	0,0	0,0	0,0	0,0	0,2	0,6	0,4	0,2	0,1

Source: [Ministry of Public Finance, 2011a and authors' own calculations]

Given that external borrowing was done mainly in foreign currency and the domestic one in national currency, the findings on the structure of local government debt by currency of denomination largely coincide with those on its structure by the source of loan resources. Before 2004 as well as since 2007, we can note the prevalence of domestic debt, a situation that can be ascribed to the limited real access of Romanian local governments to external capital markets as well as to their quite low rating. From another perspective, we can notice that foreign local public debt was denominated, almost exclusively, in euro, which was to be expected considering the membership of our country to European Union as well as public authorities' concerns for deepening integration through the adoption of euro as national currency. By reference to recent developments in the euro foreign exchange rate, we can admit that it has made its mark on the development of local public debt, contributing to enhance the burden of foreign currency indebted local governments¹.

Regarding the breakdown of local internal and external debt by type of instruments, before 2000, local governments' financing through loans from commercial banks and municipal bond issue on the domestic capital market was almost nonexistent, both due to the lack of a credit culture and a legislative framework to safeguard it. A study conducted by the National Bank of Romania in 2003 [National Bank of Romania, 2003, 49], on the basis of data from four commercial banks, indicates the existence of bank loans granted to municipalities in their portfolio starting with the second half of 2000, the value of such loans being practically insignificant before. Since 2001, the practice of domestic bond financing started to shape as a real alternative for local governments to find resources for financing local investment projects. Pioneers in this direction were two cities, Predeal and Mangalia, the value of their municipal bonds reaching 15 billion lei. So far this solution has been adopted by several local authorities, some of them having already issued bonds for two or three times.

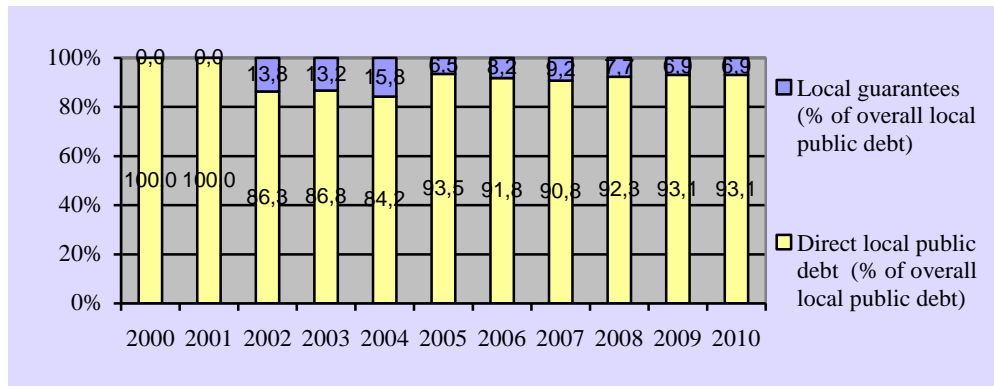
With regard to local governments' external borrowing, it mainly comes from international financial and banking institutions such as the European Bank for Reconstruction and Development, the International Bank for Reconstruction and Development, the World Bank and the European Investment Bank. The only issue of municipal bonds on international capital markets was conducted by the city of Bucuresti, in 2005.



Source: [Ministry of Public Finance, 2010 and authors' own calculations]
Figure no. 3 The breakdown of domestic and external local public debt by type of instruments (2009)

For 2009, the aggregate data presented in Figure no. 3 show that domestic local debt mainly comes from bank credits which, together with supplier credits and financial leasing provided 82,85% of the overall debt resources, while municipal bonds represent only 10,79% of the overall domestic local debt and the guarantees 6,39%. As for the external local debt, the situation is reversed, once again due to the essential mark of the loan of Bucuresti, the bonds issued on international capital markets counting for 52,41% of the overall external local debt, while the remainder is represented by bank credits and guarantees (39,18% and 9,39% respectively).

When considering local public debt's breakdown by the type of commitment, we can see, from data presented in Figure no. 4, that the directly contracted debt holds the largest share, currently over 90% of the overall local government debt. This situation can be explained by the fact that, in the absence of real possibilities for predicting local revenues, local authorities are reluctant to engage in guaranteeing loans for other local entities [Oprea, 2011, 237].



Source: [Ministry of Public Finance, 2011a and authors' own calculations]

Figure no. 4 The breakdown of local public debt by type of commitment (2000-2010)

We can also note from the above data that, although loans guaranteeing for other local entities by the authorities at this level was legally made possible in 2000, the first guarantees were granted in 2002 and had relatively small weights. The maximum level of debt coming from granted guarantees, in relative terms, was reached in 2004, being of only 15,77% of the total amount of local debt. Although in the following years the nominal value of guarantees increased, their share in overall local debt reduced to 6,5% in 2005 and 6,93% in 2010, including as a result of the loan of Bucuresti.

4. ANALYSIS OF ROMANIAN LOCAL GOVERNMENTS' INDEBTEDNESS AND ITS SOURCES - A TERRITORIAL PERSPECTIVE

As we have already seen, local governments' indebtedness is a relatively recent phenomenon in Romania, still far from knowing the magnitude observed in some developed European Union Member States. As a result of the lack of experience, reduced financial capacity, perfectible legal framework as well as of the national and international economic background, local indebtedness potential is not exploited enough to conclusively contribute to the financing of local investments and the development of communities at this level. However, these conclusions, drawn from the macroeconomic level analysis, can hide different territorial realities, mainly due to the disparities in the economic development of different types local communities.

From a regional perspective, synthetic data on local public debt are presented in Table no. 4. We can see that Bucuresti Ilfov region records the highest share of the overall local government debt (41,1%), followed at a considerable distance, by the North-East region (13,36%), Central region (9,85%), South-Muntenia (9,37%) and North-West (8,82%). The situation can be explained from a double perspective: on the one hand, Bucuresti Ilfov region is the most developed one, recording the highest GDP per capita (12 800 euro per inhabitant in 2007 compared to the national average of 5800 euro per inhabitant) and, on the other hand, Bucuresti's issuing of bonds worth 500 million euro on international capital markets, in 2005, has fundamentally changed this region's positions in the rankings. Basically, Bucuresti Ilfov region's local debt is almost equivalent to the aggregate level of all other regions' debt, with the exception of the Western and Central regions. Remarkable is the situation recorded by South-West Oltenia region, where the share of local debt in overall

local government debt is the lowest, of only 3,88%, situation which is explained by the low GDP per capita of this region (4500 euro per capita in 2007, well below the national average). From another perspective, regions that differ in population size, such as Central and South-Muntenia regions (with 2525,3 and, respectively, 3285,2 thousands inhabitants), are comparable in the level of local public debt (between 9 and 10% of overall debt), while regions similar in population size but different in the levels of development, as South-West Oltenia and Bucuresti Ilfov (with 2264,3 and, respectively, 2247,5 thousands inhabitants) stand at the opposite pole from the perspective of local government debt level.

Table no. 4 Local public debt and local economic development indicators by development regions (2009)

Indicators	North-West	North-East	South-West Oltenia	South-East	South-Muntenia	West	Center	București Ilfov	Total value
<i>Local public debt (millions RON)</i>	945,0	1432,7	415,9	701,4	1004,7	758,4	1055,9	4409,5	10723,5
<i>Local public debt (% of the overall local public debt)</i>	8,82	13,36	3,88	6,54	9,37	7,07	9,85	41,10	100,00
<i>GDP per capita* (EUR/capita)</i>	5600	3700	4500	4700	4800	6700	5900	12800	5800
<i>Population** (thousand inhabitants)</i>	2722,8	3720,1	2264,3	2822,1	3285,2	1925,6	2525,3	2247,5	21512,9

* data for 2007

** data for 2008

Source: [Ministry of Public Finance, 2010], [European Commission, 2011] and [authors' own calculations]

As far as local public debt's breakdown by urban and rural areas is concerned, the aggregate data presented in Table no. 5 show that urban areas record the overwhelming share of the overall local government debt, of 96,32%, compared to 3,68% of rural areas. This situation reflects the economic and social reality of Romania, which is particularized by the existence of large disparities in development between urban and rural communities (as well as, partially, between the urban ones). On this basis it should be noted that, practically, rural communities do not register high levels of own revenues, which could enable them to contract or guarantee more consistent loans.

Table no. 5 Local public debt's breakdown by urban and rural areas (2009)

Local public debt	Urban areas	Rural areas	Total value
<i>million RON</i>	10328,5	395,0	10723,5
<i>% of overall local public debt</i>	96,32	3,68	100,00

Source: [Ministry of Public Finance, 2010] and [authors' own calculations]

The correlation found for regions between the degree of economic and social development reflected by GDP per inhabitant and the amount of local public debt is partially respected for the urban and rural areas, more important local public debt of rural communities being registered, as shown in Table no. 6, in some "richer" regions such as Bucuresti Ilfov (56,8 million lei) and West (52,7 million lei) or in regions with an average level of GDP per capita as South-Muntenia (113 million lei). In "poorer" regions, such as South-East or South-West, local indebtedness of rural communities is generally low, an exception to

this finding making the North-East region. There where urban communities have more often resorted to contracting or guaranteeing of local loans, even if local public debt of rural areas expressed in absolute figures is more important, as a share in the total amount of local public debt its value is smaller (for example, in Bucuresti Ilfov this ratio is 1,29% of the total, lower than the one in the South-East region, of 1,51% of total).

Table no. 6 Local public debt's breakdown by development regions and local and urban areas(2009)

Local public debt		North-West	North-East	South-West Oltenia	South-East	South-Muntenia	West	Center	Bucuresti Ilfov
Urban areas	millions RON	920,6	1366,1	387,64	690,8	891,8	705,7	1013,1	4352,7
	% of the overall local public debt	97,42	95,36	93,21	98,49	88,76	93,05	95,95	98,71
Rural areas	millions RON	24,4	66,5	28,2	10,6	113,0	52,7	42,8	56,8
	% of the overall local public debt	2,58	4,64	6,79	1,51	11,24	6,59	4,05	1,29

Source: [Ministry of Public Finance, 2010] and [authors' own calculations]

Considering the degree and heterogeneity of local development in Romania by urban and rural areas - there still are some rural communities where not all basic services can be provided - we believe that central authorities' support, by guaranteeing these communities' loans, should be more widely accepted. However, as borrowed resources must be repaid from the local community's own revenues, it appears to be more reasonable for the state to supply/guarantee the amount of resources necessary for co-financing projects benefiting from structural instruments financing, which presently are a highly valuable source of financial resources for Romania (e.g. Cohesion Fund).

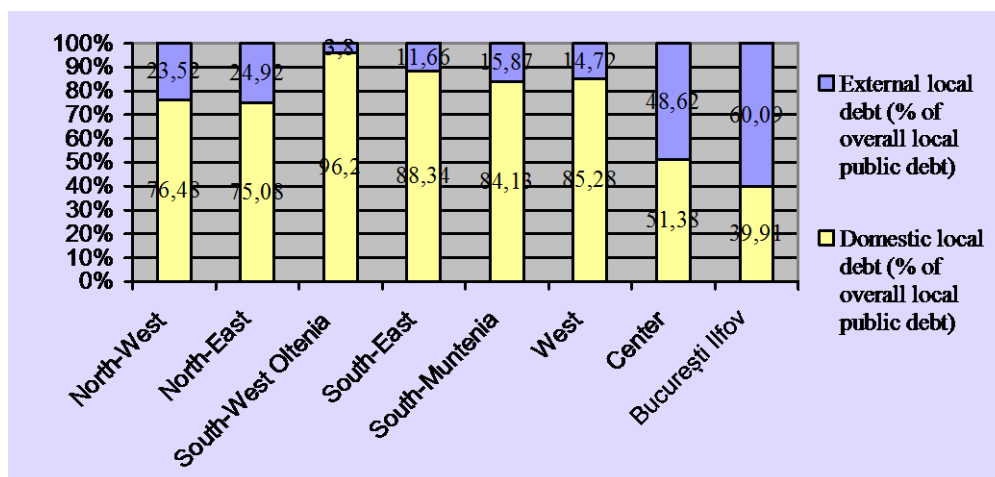
Table no. 7 Local public debt's breakdown by types of administrative divisions (2009)

Local public debt	Communes	Cities, other towns and sectors of Bucuresti	Counties, Bucuresti	Total value
million RON	395,0	6301,0	4027,5	10723,5
% of overall local public debt	3,68	58,76	37,56	100,00
% of overall local public debt – excluding Bucuresti	4,59	73,19	22,22	100,00

Source: [Ministry of Public Finance, 2010] and [authors' own calculations]

For different types of administrative divisions, the summarized data presented in Table no. 7 confirm the trend resulting from the analysis of urban and rural communities, communes' local debt representing only 3,68% of the total amount of local public debt. A more balanced situation is found among counties (by counties' councils and the General Council of Bucuresti) and towns and sectors of Bucuresti, the share being of 37,56% of the overall local public debt in in the first case and of 58,76%, respectively, in the second case. If we exclude the particular situation (by being situated in the richest region of the country) of Bucuresti, which contracted a 500 million euro loan on the international capital markets, the situation changes fundamentally, the spread between cities, other towns and sectors of Bucuresti' s debt and that of counties becoming considerably in size, of over 50% of the overall local public debt.

An analysis of the domestic and external local public debt by development regions (Figure no. 5) shows that, in 2009, external debt was more important in the case of more developed regions such as Bucuresti Ilfov or Center (60,09% of the overall local debt and respectively, 48,62%) and was less significant in regions with a lower level of development such as South-West Oltenia or South-East (3,80% of the overall local debt and respectively, 11,66%).



Source: [Ministry of Public Finance, 2010] and [authors' own calculations]

Figure no. 5 The breakdown of local public debt by source and development regions (2009)

The above reflected situation is explainable by local communities' financial situation and by the rating assigned to them (see the case of the city of Oradea), which allow for a greater access to external borrowing resources. Basically, the trends previously outlined when analyzing the overall local public debt are respected in the case of external debt, in the sense that the South-West Oltenia region has the lowest share of external debt in overall local public debt, while the highest share is that of Bucuresti Ilfov region.

Summary data concerning domestic and external local public debt by urban and rural areas are presented in Table no. 8.

Table no. 8 The breakdown of domestic and external local public debt by urban and rural areas (2009)

Local public debt		Urban areas	Rural areas
Domestic	million RON	6225,7	386,9
	% of overall local debt	60,28	97,95
External	million RON	4102,8	8,1
	% of overall local debt	39,72	2,05

Source: [Ministry of Public Finance, 2010] and [authors' own calculations]

The data summarized and represented in the table above show that, for both rural and urban communities, domestic financing is predominant. However, for urban areas the share of external financing is much more consistent than in rural areas (39,72% of the overall local public debt compared to 2,05%).

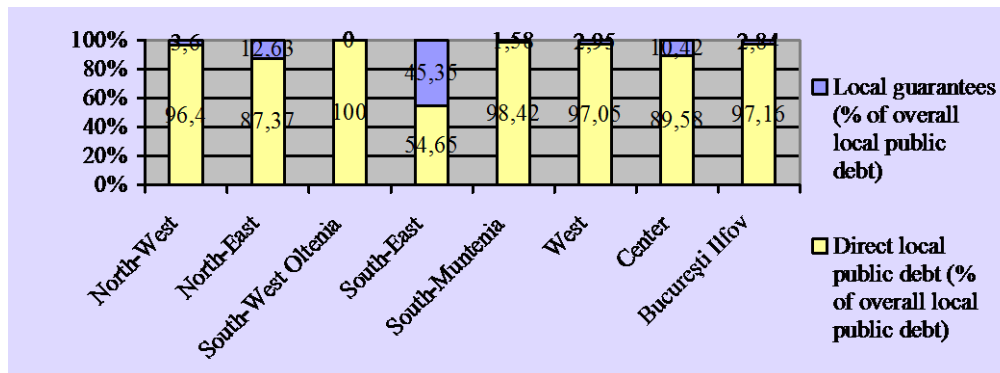
These correlations are also respected when considering the breakdown of domestic and external local public debt by type of administrative divisions, as shown in Table no. 9.

Table no. 9 The breakdown of domestic and external local public debt by types of administrative divisions (2009)

Local public debt		Communes	Cities, other towns and sectors of Bucuresti	Counties, Bucuresti
Domestic	million RON	386,9	4953,8	127,9
	% of overall local debt	97,95	78,62	31,58
External	million RON	8,1	1347,2	2755,6
	% of overall local debt	2,05	21,38	68,42

Source: [Ministry of Public Finance, 2010] and [authors' own calculations]

Although the global analysis for urban and rural areas revealed that external local public debt is less important than the domestic one (39,72% of the total compared to 60, 28%, for urban areas), in this case external debt is prevalent in counties and Bucuresti (68,42% of the overall local public debt).



Source: [Ministry of Public Finance, 2010] and [authors' own calculations]

Figure no. 6 The breakdown of local public debt by type of commitment and development regions (2009)

The analysis of local public debt by development regions and type of commitment shows, as it results from the data synthetically represented in Figure no. 6, that the highest amount of guarantees (as % of the overall local government debt) is found for the South-East region, although this region occupies the penultimate place in terms of the overall size of local public debt. In other words, the less significant local debt of this region when compared to other regions has mostly formed on the basis of the guarantees granted to other local entities. We also see that the region ranking last in terms of the overall size of local public debt, South-West Oltenia, did not grant any guarantees. The top of guarantees granted also includes, in that order, the North-East and Central regions, for the other regions the share being of only about 2 or 3%.

For urban and rural areas, we found that the guarantees are granted almost exclusively in urban communities, as can be seen from Table no. 10. This situation is explained by the fact that in Romanian rural communities, less developed, still really aren't public entities that provide public utility services, which means that the preponderant potential

beneficiary of guarantees is missing. Although these guarantees could be granted to private agents as well, it is our believe that the reluctance of Romanian authorities to direct borrowing is felt multiplied when guaranteeing private agents' loans, which could be explained by the unfavorable recent years' conditions for raising local revenues in Romania.

Table no. 10 Local public debt's breakdown by type of commitment and urban and rural areas (2009)

Local public debt		Urban areas	Rural areas
<i>Direct debt</i>	<i>million RON</i>	9522,2	394,7
	<i>% of overall local debt</i>	92,19	99,92
<i>Guarantees</i>	<i>million RON</i>	806,3	0,3
	<i>% overall local debt</i>	7,81	0,08

Source: [Ministry of Public Finance, 2010] and [authors' own calculations]

These correlations are also observed when analyzing direct and guaranteed debt by type of administrative division, as may be found in Table no. 11.

Table no. 11 The breakdown of local public debt by type of commitment and type of administrative division (2009)

Local public debt		Communes	Cities, other towns and sectors of Bucuresti	Counties, Bucuresti
<i>Direct debt</i>	<i>million RON</i>	394,7	5759,9	3762,4
	<i>% of overall local debt</i>	99,92	91,41	93,42
<i>Guarantees</i>	<i>million RON</i>	0,3	541,1	265,2
	<i>% of overall local debt</i>	0,08	8,59	6,58

Source: [Ministry of Public Finance, 2010] and [authors' own calculations]

The data above show that in communes local debt resulting from the guarantees granted is insignificant, with a share of 0,08% of the overall local public debt, while in cities, other towns and sectors of Bucuresti it represents 8,59% of the total amount of debt and in counties and Bucuresti 6,58%.

5. CONCLUSIONS AND POLICY RECOMMENDATIONS

A first important issue that the analysis conducted within this study, on Romanian local governments' indebtedness and its sources in European context, revealed is that although raising additional (loan) resources to local budgets was clearly needed, especially during the extensive administrative reforms period (1990-2000), local public finance successive regulations proved not to favor it until after 1998. Although it can be just as true that at that time qualitative factors such as the reluctance of local governments, their excessive caution and lack of experience have acted with enough force against local indebtedness, our study confirms that the main reason for the fragile exploitation of the opportunities to raise additional resources is the low affordability threshold of local governments which manage a insufficiently large tax base, face still (too) low local revenue collection rates, rely too much on central budget support and too easily invoke the objective impossibility to access European funds. In this respect, it is our opinion that a more direct link should be set between local borrowing and accessing European funding, a link that should engender a direct incentive compared to the current regulations, which stipulate that loans for co-financing European projects are excluded when assessing the indebtedness capacity, thus creating more a favorable setting, but which express only a possibility, not an incentive.

Secondly, we emphasized the prevalence Romanian local governments' indebtedness in national currency, which shows that their access to external capital markets is quite poor, in direct correlation with the pretty low rating assigned to them. As for the external local debt, euros denominated loans are undoubtedly the main imprint, with direct impact on debt repayments reflected in local budgets.

Thirdly, we noticed that in absence of an actual capacity to predict the amount of financial resources to be raised, both due to fluctuating legislation and economy, Romanian local governments show pretty little interest in guaranteeing the loans of other local entities, which is in fact a braking factor for local development, through the lack of a more serious support for their potential agents. Correspondingly, the "preference" for the direct local debt, mainly resulting from bank credits, is the main feature. In this context, we find it necessary for the local public finance legislation to more directly settle the issue of local budgets' sources of revenue, by clearly differentiating them from the central budget's sources of revenue, taking into account the proposals formulated in the literature, and to concomitantly diminish the importance of the system of transfers for balancing local budgets, thus helping to stabilize local public financial relations and creating an appropriate framework for local agents' initiatives and accountability.

Particularly important and with direct implications for public policy making, especially on the background of the controversies regarding the reorganization of Romania's administrative divisions, appear to be the conclusions of this study on local debt's territorial breakdown, which can be considered the expression of our country's local development disparities. While the most developed region has a local debt almost equal to all other regions' aggregate debt (excluding West and Central regions), South-West Oltenia records the smallest share of local debt in overall local public debt, in accordance with the small GDP per capita of this region. From another perspective, regions with different population size (Center and South-Muntenia) have similar local public debt levels, while regions with similar population size but different levels of development (South-West Oltenia and Bucuresti Ilfov) are diametrically opposed when considering their local government debt levels. In the same respect we noticed, when analyzing local debt's breakdown by urban and rural areas, that urban areas' public debt (without excluding, of course, some disparities) has an overwhelming share of the overall local public debt compared to rural areas, although for the latter the need for development is evidently more acute. This reality, resulting from Romania's economic and social background, marked by wide disparities in development between regions and urban and rural communities, must be countered by appropriate government regulations and policies, first requiring the reconsideration of the "procustian" approach on assessing local indebtedness capacity. Under the current legislative framework, the undifferentiated treatment of the local debt limits sometimes leads to the reality that while local communities with weak fiscal potential are given large room for maneuver, theoretically but not practically useful, more developed local communities, not lacking initiative and potential, are broken. As a result, it would be necessary that discussions on future regulations take into account the possibility of setting annual debt limits customized on the basis of the local specific for different administrative-territorial units (at least for classes/levels of development and potential, if not even individually).

Last but not least, the results of the analysis of local guarantees emphasized as a noteworthy aspect the fragility of the relationship between local governments and public or private agents providing local public services, agents that must be treated as local development drivers. For public policy-makers, the findings should be translated into creating a

more stimulating framework for public-private partnerships, similar to that of EU funding, by offering financial co-support or distinctively treating the guarantees granted for loans for projects in public-private partnership. Not only there aren't arguments to prove that stimulating initiatives or supporting healthy local development projects initiated by public or private agents, other than local governments, cannot have more consistent beneficial effects than those of public authorities' actions, but the practice of some EU member states even supports this approach.

The overall conclusion of this study indicates that until now, in Romania, the local indebtedness potential has not been exploited enough to make its contribution to the financing of local investments and the development of this level communities, the main driving factors being the low, partially motivated by the lack of experience, involvement of local governments, the limited local economic base and financial potential, the fluctuating and perfectible legal framework but also the national and international social and economic conditions.

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Note

1. According to art. 62 para. 11 of Law no. 273/2006 on local public finance, "In order to assess local public debt, any liability, expressed in other currency than the national one, is evaluated in national currency by using the official exchange rate announced by the National Bank of Romania on the last day of the reporting period". Thus, if the official exchange rate was 3,6771 RON/EUR on December 30, 2005, it rose to 4,2848 RON/EUR on December 31, 2010.