



## **Governing Body**

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Working Party on the Social Dimension of Globalization

**WP/SDG**

**FOR INFORMATION**

SECOND ITEM ON THE AGENDA

## **Recovering from global crisis**

### **Social dialogue and adjustment in Romania: Progress report on ILO cooperation with constituents and the International Monetary Fund**

#### **Overview**

**Issue covered**

This paper reports on ILO work with constituents and the International Monetary Fund (IMF) on social dialogue and adjustment in Romania.

**Policy implications**

The report covers work in progress.

**Financial implications**

None.

**Action required**

None.

**References to other Governing Body documents and ILO instruments**

GB.309/WP/SDG/1.



1. Following the joint IMF–ILO conference on “The Challenges of Growth, Employment and Social Cohesion” hosted by Prime Minister Jens Stoltenberg of Norway, which was held on 13 September 2010 in Oslo, the ILO and the IMF agreed to work together on exploring the scope for: a social protection floor; employment-creating growth; and the central role that effective social dialogue can play in building the consensus needed to tackle the difficult adjustment challenges created by the current economic crisis.<sup>1</sup> This progress report focuses on social dialogue and adjustment in Romania.
2. Shortly after the Oslo conference, the IMF invited the ILO to participate in a seminar on 2 November 2010 for trade unions in Romania to discuss issues related to the current economic crisis. Since that time the ILO and the IMF have been collaborating closely in Romania and both institutions are strongly committed to helping the Government and the social partners reach consensus about a durable legislative framework and a set of labour market institutions and policies that can support strong, sustained and balanced economic and employment growth.

## **Background: The impact of the global economic crisis on Romania**

3. Romania, like many economies in Europe, was badly affected by the global economic crisis in late 2008. In the second half of that year the Romanian stock market went into rapid decline, losing two-thirds of its value over the next nine months. Previously strong capital inflows into Romania and other European economies were abruptly reversed. As a result, by October 2008 the commercial banks were experiencing liquidity problems and interest rates spiked. The resulting uncertainties for fiscal policy and concerns about the magnitude of the current account deficit led the international rating agencies to cut Romanian credit ratings more severely than for other emerging economies. Although Romanian sovereign foreign debt was very moderate, between November 2008 and April 2009 the interest on Romanian bonds rose sharply, peaking at close to 800 basis points (8 per cent) higher than those for German government bonds in February 2009. This was significantly higher than the bond spreads faced by many other emerging economies in the region.
4. The Romanian currency, the lei, depreciated by around 20 per cent against the euro between October 2008 and January 2009. Currency reserves also dipped but remained adequate. However, following rapid growth of foreign currency lending to Romanians in the years prior to the crisis, there were significant concerns about how the banking system would cope as the local currency lost value, pushing up loan repayments in lei and increasing the likelihood of increasing defaults.
5. These financial pressures were reflected in the real economy in the last quarter of 2008. Real GDP growth, which had been increasing at an average annual rate of 9 per cent in the first three quarters of the year, collapsed in the final quarter of 2008, falling by an annual rate of 13 per cent. This was one of the most dramatic turnarounds in all emerging markets. The impact of the global economic crisis was transmitted to most emerging economies through a combination of factors including: massive capital outflows as international investors fled more risky markets; declining domestic demand and access to credit as confidence deteriorated; and a major contraction in export markets. All three factors were at play in Romania but it is notable that the initial downturn was driven by a major contraction in domestic demand consequent on the major shift in capital flows, while the decline in exports was far more moderate in Romania than in other European countries.

<sup>1</sup> GB.309/WP/SDG/1.

## IMF Stand-By Arrangement

6. In May 2009, the Government of Romania reached an agreement with the IMF for a Stand-By Arrangement (SBA) over a two-year period for an amount of nearly 13 billion euros. This Arrangement was supplemented by 5 billion euros from the European Union and 2 billion euros from other multilateral sources. In 2009–10, the Government implemented in various stages expenditure cuts and tax increases amounting to 9 per cent of GDP. Many of the austerity measures implemented in conjunction with the SBA had far-reaching implications for public employment levels, pension and other transfer payments, public-sector wage levels, and other measures that impact on disposable incomes and living standards (see below for details). Issues of labour market flexibility were not included in the initial Letter of Intent from the Government to the IMF in April 2009.

7. The IMF undertook its regular Article 4 consultations with Romania in May 2010. The staff report on these consultations included a significant focus on structural reforms and concluded that “Romania’s labour market is rigid compared to others in the region”.<sup>2</sup> Shortly after the conclusion of these consultations, in June 2010, the next Letter of Intent under the SBA from the Government of Romania to the IMF included the following statement:

We will introduce by end-2010 a revised labour code and collective contract legislation, to increase flexibility of working time, and to reduce hiring and firing costs through more flexible contracts. We also aim to allow greater wage flexibility.<sup>3</sup>

8. Subsequent Letters of Intent between the Government and the IMF have mentioned labour market reforms. The latest, from 22 December 2010, states:

We are continuing work on labour market reforms to increase flexibility, increase representativity in the negotiations between social partners, and encourage greater labour force participation, particularly for young people ... Before end-December (after consultation with social partners and the IMF, the World Bank and the European Commission), we will send a revised social dialogue code and an improved labour code to parliament.<sup>4</sup>

9. Issues related to labour legislation and labour market flexibility have been prominent features of economic discussions with the international financial institutions in Romania for many years and were regularly discussed in IMF Article 4 reports and various IMF and World Bank research papers between 2003 and 2008.

## Recent ILO engagement in Romania

10. Following the IMF trade union meeting in November 2010, the ILO consulted the Romanian social partners on a range of employment and social policy issues. In light of these consultations, the ILO suggested that a tripartite meeting be held on the occasion of a forthcoming IMF mission in late January/early February to review the contribution that labour market reform could make to adjustment and sustainable growth. The Director-

<sup>2</sup> IMF: *Staff Report for the 2010 Article 4 Consultation, Fourth Review under the Stand-By Arrangement*, Country report No. 10/227 (Washington, July 2010), p. 26.

<sup>3</sup> Letter of Intent from the Government of Romania to the IMF, 16 June 2010, para. 19, in IMF, *op. cit.*

<sup>4</sup> Letter of Intent from the Government of Romania to the IMF, 22 December 2010, para. 18.

General of the ILO subsequently wrote to the Prime Minister of Romania proposing, in the context of the next IMF mission to Romania, a meeting to be jointly hosted by the ILO and the Government and involving the social partners, the IMF and other relevant international organizations (World Bank and European Commission) to begin consultations on a range of labour market issues. The Prime Minister responded positively to this proposal.

- 11.** Also in November, the five national trade union centres in Romania wrote to the Director-General of the ILO referring to the IMF activities in the country. They requested that experts from the Office be assigned to analyse the need for modifications to the labour legislation and subsequently contribute to discussion on this issue if it was considered that reforms were required.<sup>5</sup> The Minister for Labour, Family and Social Protection also wrote to the ILO in December 2010 confirming that the Government was intending to amend and supplement the Labour Code and welcomed technical assistance from the Office during this process. Consultations were also held with representatives of several employers' associations that have national recognition status in Romania, and they also welcomed ILO participation and technical assistance in discussions concerning possible reforms to the labour legislation.
- 12.** On 15 December 2010, the Government of Romania released drafts of proposed changes to the Labour Code and the chapter on collective bargaining of a new social dialogue law that consolidates and modifies various other aspects of national laws. The draft reforms included provisions regulating: the system of collective bargaining; the recognition of trade unions and employers' associations; dismissal procedures; working time; temporary work; probation periods; and a wide variety of other issues. Both the recognized trade unions and employers' associations criticized the proposals. The social partners claimed that the Government had not followed the procedures concerning consultations established in the existing social dialogue law and, consequently, they initially refused to consider the draft laws in the Economic and Social Council.
- 13.** In early January 2011, informal consultations did commence between the Government and some of the social partners over at least some aspects of the proposed reforms. During this process, the Minister for Labour, Family and Social Protection set a deadline of 21 January 2011 for the completion of these consultations and indicated that, if negotiations were not finalized by then, the Government would submit the draft laws to Parliament. During the course of these negotiations the five national trade union centres wrote to the Director-General of the ILO requesting written comments on the two draft laws and ILO technical expertise in the tripartite discussions. The ILO responded to this request on 18 January with written comments on the draft legislation to the trade unions, also making copies available to the Government and the recognized employers' associations.
- 14.** A tripartite meeting on labour market institutions and policies for strong, sustained and balanced economic growth in Romania was held on 26 January 2011, at which the IMF, the European Commission and the ILO all made presentations. The Minister for Labour, Family and Social Protection and senior representatives of all the social partners actively and constructively participated in the subsequent discussions, which were broad-ranging. The objective of the ILO in suggesting this meeting was to set in train a process of tripartite discussions on a package of labour market reforms. The type of issues envisaged included: training and active labour market policies; possible improvements to labour administration and labour inspection; measures that might foster increased productivity in public and private enterprises and the formalization of informal activities; and arrangements for future wage policy. This package of reforms could assist Romania to improve both efficiency and equity in the labour market and eventually provide the country

<sup>5</sup> Letter to the Director-General of the ILO from the five national trade union centres in Romania, November 2010.

with coherent labour legislation, as well as labour market institutions and labour policies that are conducive to strong, sustained and balanced economic growth and decent work.

15. Regarding the specific question of the Government's labour law proposals, detailed negotiations informed by the ILO technical memorandum have continued with the social partners past the 21 January deadline. At the time of writing, these negotiations were ongoing.
16. The ILO in conjunction with the IMF, and in cooperation with the Government and the social partners, are planning follow-up activities in Romania in four broad areas: the promotion of active labour market policies; economic restructuring and productivity enhancement in public enterprises; labour law design and enforcement including strengthening the labour inspectorate; and the promotion of sound collective bargaining and social dialogue. The latest national accounts confirm that the economy remains in recession. Over 100,000 jobs were lost in the public sector in the last year and job opportunities in the private sector are not picking up. Underemployment and undeclared work, prominent features of the Romanian labour market since the 1990s, have expanded further in the last two years.

Geneva, 23 February 2011

*Submitted for information*