

THE PRIVATE PERCEPTIONS REGARDING THE NATIONAL BANK OF ROMANIA'S INDEPENDENCE

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Abstract

The independence represents an essential condition for the central banks that conduct an inflation targeting monetary policy. According to the international economic literature, the central banks' political and economical independence influence the formation of the private inflation expectations. Even if the aspect of central bank independence is new in our economic literature, we have some valuable papers about this subject. These papers study the role of NBR independence or analyze the evolution of the NBR independence. Our approach is different. The law 312/2004 stipulates that NBR is an independent public institution, but we want to see if the society has the same perception. In consequence, we decided to study the private perceptions regarding the National Bank of Romania's independence. To achieve this goal, we evaluated the civil society perceptions regarding the influence of presidency, government, parliament and political parties in the NBR's activity. Our research is based on the data gathered during the time span March 2007 – February 2008.

Introduction

The economic literature argues that the “independent central banks, compared to central banks subordinated to the government, deliver better outcomes for inflation, as well as outcomes for real variables such as output and employment that are no worse than those achieved by less independent central banks” (Bernanke *et al.*, 2001). Independence is more important for the inflation targeting central banks: in order to achieve credibility – one of the most important feature of the inflation targeting monetary policy – the central banks need to be perceived as being economically and politically independent.

In the last twenty years the independence of central banks increased considerably (Crowe and Meade, 2008). The factors that sustained this evolution can be grouped into global and regional factors (Cukierman, 2007). The great interest for price stability, the development of capital flows in the international capital markets and the general perception that governments are subject to inflation bias (due to their intentions to sustain employment and economic growth) represent the main global factors sustaining the increase of central bank independence. On the other side, the major regional factors are: the fall of other institutions designed to assure nominal stability, the good experience of highly independent Bundesbank, the implementation of Maastricht Treaty, the necessity to reduce the possibility to occur high inflation levels and to assure an appropriate functioning of market economies.

According to Bernanke and its collaborators (Bernanke *et al.*, 2001, p. 37), some of the economists consider that the central banks should be directly responsible to the society representatives (presidency, government and parliament), while other economists think that the central banks should be absolved of any political responsibility. If a central bank is accountable to an institution there are great chances to lose its independence. As a consequence, the central bank decisions will be influenced by that institution. From our point of view, such situations should be avoided because the central bank independence represents “the only solution which allows central bank to fight against inflation” (Cerna, 1999, p. 16).

The objectives of monetary authorities should be different by the political sector objectives. We can have situation when, for electoral reasons, the governments manipulate the society applying expansionist economic policies and, after elections, they implement restrictive policies in order to reduce the inflationary effects. According to Cerna, these practices create “political-inflationary cycles” (Cerna, 1999, p.11), cycles that have a negative impact on the economy. If a central bank wants to be credible it should be immune to such practices, which mean it should be independent.

On the other hand, left political parties have a more accentuated tendency to generate inflation through their policies in order to reduce unemployment (Cerna, 1999, p.12). In the time spans when a country is governed by left parties the chances are to have a lower unemployment, but a higher inflation. This is the reason why we sustain that the governments should harmonize their policies with the monetary policy objectives.

As a result of the great importance given to the central banks independence, economists developed methods to measure this aspect. A comprehensive synthesis of these methods

was made by Dumiter F.C., who accentuated the fact that the trend towards more independent central banks gains more support in the modern theory of monetary policy (Dumiter, 2008, p. 544). In the evaluation of NBR independence we do not use any of the indices mentioned by Dumiter, the measure of the peoples' perceptions regarding NBR independence being the distinctive element of our approach.

1. The evolution of NBR independence

At the beginning of 1990's, NBR was, technically, independent (Cerna *et al.*, 1998, p. 1). In spite of the declared independence, the Romanian government and the Parliament adopted some laws, under which NBR was forced to finance the activity of two unprofitable sectors: energy and agriculture. Even if these loans had preferential interest rates they did not solve the problems because the producers were not encouraged to be more competitive. More than that, these loans, being realized through monetary issue, had inflationary effects. In 1992, the amount of the preferential credits was 60% out of the total amount of the refinancing credits (Bîrsan and Ebbers, 1999, pp. 221 – 222). This is why we subscribe to the idea enounced by Bîrsan and Ebbers according to which, the NBR was rather a government branch than a central bank.

Bîrsan and Ebbers computed an independence index to measure the NBR independence between 1991 and 1998. Their results showed a low level of independence (Bîrsan and Ebbers, 1999, pp. 218 – 219):

- political independence: NBR obtained 5.25 out of 9 points in 1991, while in 1998, NBR obtained 8 out of 9 points. It is obvious that until 1998, when the Romanian Senate modified the NBR statute, our central bank was mostly dependent of the political institutions;
- economic independence (how central bank financed its budgetary deficit and what instruments had NBR to implement its decisions): NBR obtained 2.5 out of 6.5 points in 1991, while in 1998, NBR obtained 4.5 out of 6.5 points. We can see that the changes from the NBR statute enhanced its independence.

Often, on the short term, the price stability objectives come in conflict with the employment rise objective (Isărescu, 2006, p. 152). The governments, in order to be popular, try to assure a higher level of employment. The Romanian governments did the same thing: before 2000, in order to keep the unemployment as low as possible, they postponed the economic restructuration of the unprofitable enterprises. In spite of this tendency, we cannot affirm that the actions taken by the governments to reduce the unemployment are the only cause of the inflation evolution from our country. But, the materialization of the tendency illustrates a low level of independence for NBR.

Before 2004, the situation of NBR independence was approximately the same. Crowe and Meade (2008) evaluated the NBR independence using a scale from 0 to 1 (1 representing total independence) and the value obtained for 2003 was 0.59. But, at this moment, the situation of NBR independence is different. According to Law no. 312/2004 on the Statute of the NBR, "The National Bank of Romania is an *independent public institution* with its headquarters in Bucharest". Also, „the National Bank of Romania is solely accountable to Parliament and *is on no account subordinated to Government*; its relationship with the latter is co-operation on a regular basis”.

Analyzing the differences between the Law no. 312/2004 on the Statute of NBR and the Law no. 101/1998 on the Statute of NBR, we identify essential differences:

- the Law no. 312/2004 clearly stipulates that **NBR is an independent public institution**, while the Law no. 101/1998 specified only that *NBR is the central bank of Romania, having juridical personality*;
- according to Law no. 312/2004, in order to achieve its goals, **NBR will not demand or will not receive instructions from other public authorities**, while the Law no. 101/1998 sustain that, in order to fulfill its goals, *NBR will be consulted by public authorities in case of laws that regard the monetary policy*.

In our opinion, Law no. 312/2004 on the Statute of NBR assures a high level of independence to our central bank, aspect reflected in implementation of the monetary policy.

2. Private perceptions regarding NBR independence

After 2000, NBR gradually prepared the adoption of the inflation targeting monetary policy. Previously, we enhanced the importance of the central banks' independence for the inflation targeting monetary policies. In consequence, one of the measures taken by our central bank was to assure its independence, aspect achieved in 2004. As we mention earlier, according to law 312/2004, NBR is an independent public institution.

The success of the inflation targeting monetary policy depends not only on the actions taken by NBR, but depends, essentially, on the society reactions to its decisions. That means *is not sufficient NBR to declare its independence, it is necessary the society to believe that NBR is independent* otherwise its credibility will decrease. This is the reason why, in this paper, the authors study the private perceptions regarding the independence of NBR.

2.1. Method and results

The society's perceptions regarding NBR independence were studied conducting a survey. The method we implemented is common for this type of studies which have private perceptions and expectations (regarding inflation and monetary policy) as main objective (Monthly European Commission Consumer Surveys; Millet (2006), Lyziak (2003), Forsells and Kenny (2002) surveys). During the time span March 2007 - February 2008 we applied each month between 250 and 500 questionnaires to individuals from Transylvania. The number of valid questionnaires is variable due to the fact that in the data collection process we used an electronic questionnaire. The advantage of the electronic questionnaire is that it allowed us to collect information from a large number of individuals with reduced cost. Also, using electronic questionnaires the information is easily processed. The method we used had a disadvantage. We tried to apply the questionnaire to the same persons, but we could not control the respondents' willingness to answer each month to our questionnaire (only a part of them answered monthly). In spite of this inconvenience, we consider the results obtained as being relevant. We did not remove the answers obtained sporadically because we did not want our result

to be influenced by the fact that respondents were getting used with the questions. On the other hand, we wanted to have as much as possible perspectives regarding NBR independence.

Our research was conducted in two steps. Firstly, during the time span March – September 2007, we analyzed the society’s perceptions regarding NBR independence in relation to public institutions. To gather the necessary data we used the following question: *which is, in your opinion, the NBR level of independence in relation to Government, Parliament, political parties: very high / high / medium / low / very low.*

Secondly, during the time span October 2007 – February 2008, we conducted a more detailed analysis. We tested the NBR independence, separately, in relation to each of the following: presidency, government, parliament and political parties. To gather the data we demanded the respondents to evaluate the NBR level of independence individually for each institution.

In both cases, we quantified the answers using a scale from 1 to 5: 1 represented a very low level of independence, while 5 represented a very high level of independence. We estimated the independence level using the average of the results obtained. Also, we evaluated the NBR independence level reported to age, income, level of studies and knowledge about the inflation process.

2.2. Discussions

The results obtained during our study confirm that society’s view on NBR’s independence level is only a little over the average - the Pearson coefficient (4.46%) shows that the average value (3,247 on a scale from 1 to 5) is representative. The variance has a very low value (0.021) which means that the society’s perceptions regarding NBR independence were consequent. In Figure 1, we represent the evolution of society’s perceptions regarding the NBR independence:

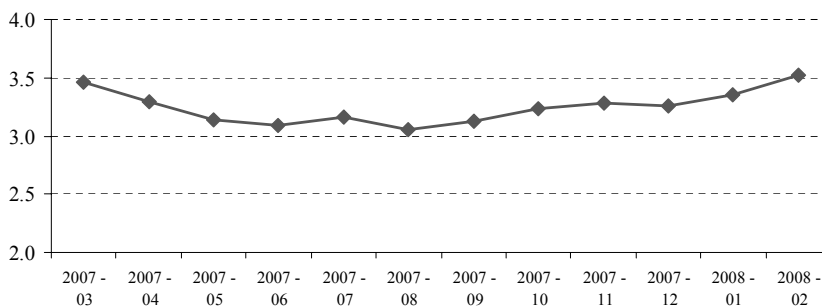


Figure 1: The evolution of perceptions regarding NBR independence. Source: Authors’ own calculations

Analyzing the data gathered in the second part of the study, we observed that NBR has the highest level of independence relative to presidency, while the lowest level of independence is in relation to the political parties. Also, NBR has an independence level little over the average in relation to government and parliament.

Analyzing the evolution of perceptions we observed that these are approximately similar each month. We believe that a higher level of independency related to Presidency is normal: according to the law, the presidency does not have the authority to influence the decisions taken by the central bank. On the other side, we consider unusual the level of perceptions regarding NBR independence in relation to the government. The NBR activity can be influenced by the Government in two ways: directly (establishing together the inflation target) and indirectly (through the lack of coherence in its fiscal policy and lack of correlation with the monetary policy). As a result, the NBR may be less independent in relation to the government.

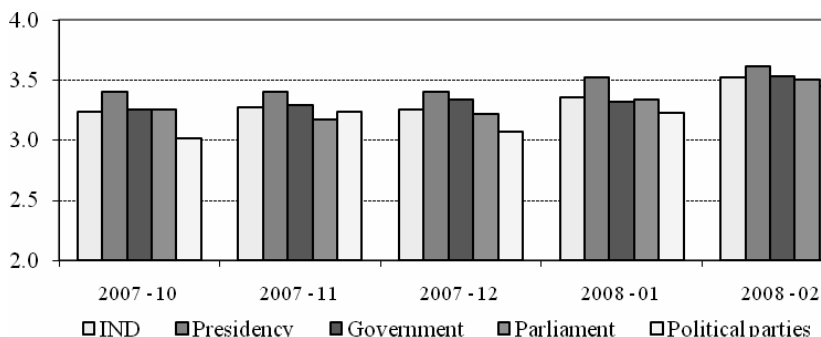


Figure 2: Perceptions regarding NBR independence. Source: Authors' own calculations

The respondents consider that NBR has the lowest level of independence in relation to the Parliament and political parties. In our view, this is the result of the Romanian political class demagogy. The society believes that the parliamentarians and the political parties, through their activity, protect rather private interest and not the society's interest. So, in this situation, in order to protect their own interest, they could influence the decisions taken by the central bank.

In order to characterize the society's perceptions regarding the NBR independence we computed three statistical significance tests. We studied if age, income and knowledge regarding inflation influence the respondents' perceptions on the NBR independence.

Studying the relationship between the respondents' age and the respondent's perceptions regarding NBR independence, we conclude that, statistically, there is no relevant correlation between these two variables. Applying χ^2 tests, we can reject the null hypothesis, with a confidence level of 90%, in two out of the seven studied months. More than that, the values obtained are very low (maximum 0.06). So, we consider that the respondents' age does not influence their perceptions regarding NBR independence.

We reached the same conclusion when we studied the link between the respondents' income and their perceptions regarding NBR independence. During the time span studied, the descriptive analysis did not reflect any specific trend for any of the income categories. The results obtained with the χ^2 tests are also contradictory. Firstly, we rejected

the null hypothesis, with a 95% confidence degree, for three out of the seven studied months. Secondly, the values obtained for the *Kendal tau* correlation coefficient are very low (maximum 0.0493) and do not have the same sign: two of them show a positive relationship between these variables, while the third shows a negative correlation. In consequence, we consider that the respondents' income does not influence their perception regarding NBR independence.

Analyzing the correlation between the respondents' knowledge on inflation and their perception regarding the NBR independence we obtained more convincing results. The descriptive analysis showed that the respondents who are more informed on the inflation phenomenon consider that NBR has a higher level of independence, while the persons who do not know much about inflation believe that NBR is not so independent. We identified a direct relationship with a medium to high intensity, the correlation coefficient having the value $R = 0.7195$. Since the P value from the Anova table is lower than 0.01 ($P = 0.0083$), we sustain that between the respondents' knowledge on inflation and their perceptions regarding NBR independence exist a relevant relationship with a confidence degree of 99%. The R-squared statistic indicates that 51.77% of the perceptions' evolution regarding NBR independence variability is explained by the evolution of the respondents' knowledge about inflation. The most appropriate model that represents the relation between these two variables is linear, can be described through the following equation:

$$IND = 1.143 + 0.824 * INFO \quad (1)$$

where: IND – the respondents' perception regarding NBR independence;
INFO – the respondents' knowledge about inflation in Romania.

According to our previous studies, the population's information degree regarding the inflation phenomenon in Romania is low (Toader, 2008). In our view, this aspect justifies the fact that the society believes that NBR has only a medium level of independence. According to equation 1, individuals who are more informed on inflation tend to associate a higher level of independence to NBR. In conclusion, in our case, respondents' knowledge about inflation is low, so we consider the result we obtained are correct.

Due to the fact that the society, regardless of age or income, perceive the NBR's level of independence in relation to the political pressures as being a little over average, we consider that NBR should search and find different methods to assure the society that it is an independent institution, which make the best to achieve its target (price stability).

3. Conclusions

In conclusion, in spite of the fact that the NBR Statute stipulates that our central bank is an independent institution, the society perceives the NBR independence as being a little over the average. We consider this value as being lower than in reality. In our view, there are two main causes for this situation. Firstly, the society lack of confidence in the intentions of the political parties and parliamentarians. We observed that the

respondents consider that NBR has the lowest independence level in relation with to political parties and the Parliament.

Secondly, the respondents' knowledge on inflation is, in general, very low. Our analysis showed that the individuals who know more about Romanian inflation tend to associate a higher level of independence to NBR, while the other persons associate a lower level of independence.

NBR cannot control the respondents' perceptions regarding the negative influence of the political parties or the parliament on the NBR activity, but it can influence the society knowledge about the Romanian inflation phenomenon. NBR could adjust its speech in order to be understood by different categories of population. The inflation reports are too technical for the majority of people, so, we think that NBR should take in consideration the possibility to publish a "simplified inflation report".

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