Daniel DĂIANU, July 5, 2026

The Growth Model: A Misconception Must Be Avoided

At the most recent meeting of the AAFB (Association of Financial-Banking Analysts), held in June this year, participants discussed the exhaustion of Romania's current growth model, putting forward a number of compelling arguments. The latest National Bank of Romania (NBR) Annual Report includes an insightful section on competitiveness, the technological gaps facing the Romanian economy, and implications of artificial intelligence (AI), which may further widen these gaps. Such debates are by no means unique to Romania; they are taking place across many countries.

However, the discussion on Romania's growth/development model should not lead to a misunderstanding regarding the primary source of the country's macroeconomic difficulties. Nor can it be reduced simply to the relationship between investment and savings. It must also take into account the broader international environment, characterized by geopolitical fragmentation, trade conflicts, risks to the stability of the international financial system arising from a new wave of financial deregulation, the growing role of non-bank private credit and crypto-assets, as well as the transformative impact of artificial intelligence.

Questions about future economic growth also concern advanced economies

Questions concerning how to overcome development gaps have a long history; they have accompanied both periods of success and episodes of stagnation or decline in the modern economy. Some emerging economies have achieved remarkable breakthroughs, escaping the middle-income trap through exceptionally high rates of investment and domestic savings. Asian countries, in particular, have excelled in this regard, with China and South Korea perhaps being the most notorious examples. Other emerging economies, however, have followed more uneven development paths, exhibiting significant structural vulnerabilities.

It is therefore no coincidence that concepts such as *path dependency*, structural dependency, and institutional constraints have long been the subject of debate in Latin American countries. Indeed, the global economy has always been characterized by a centre–periphery relationship, marked by varying degrees of asymmetries.

Several years ago, Davide Furceri of the International Monetary Fund (IMF) delivered a presentation in Bucharest on the difficulties faced by emerging economies in overcoming the middle-income trap, emphasizing the importance of capital accumulation, investment, the quality of institutions, and income distribution. It is worth recalling here that economic growth can be explained analytically through capital accumulation and productivity gains. However, what is commonly referred to as the Solow residual within the production function still contains an element that remains hard to explain, as Elhanan Helpman observed in *The Mystery of Economic Growth* (2004). Along these lines, institutional quality and innovation capacity have emerged as key explanatory factors, consistent with the endogenous growth theory developed by Paul Romer, Philippe Aghion, and Peter Howitt—all internationally renowned economists whose work has profoundly shaped modern growth theory.

The globalization promoted by international financial institutions in the aftermath of the Second World War has, over time, revealed its less favourable aspects, particularly insofar as it contributed to the emergence of financial crises. What has become an even greater concern for policymakers in advanced economies, however, has been the process of deindustrialization in the West, which occurred simultaneously with the extraordinary economic rise of China and other emerging economies, fundamentally altering the global balance of industrial and technological power. Asian economies have demonstrated that competitive advantages—distinct from comparative advantages, such as abundant low-cost labour or natural resources—can be created through active industrial policies. This development has fuelled calls for greater protectionist measures and renewed industrial strategies in both the United States and Europe, as reflected, for example, in the Draghi Report.

A centre–periphery relationship also exists within the European Union, although the countries of Central and Eastern Europe that joined the Union after 2004 have experienced significant economic convergence. Their progress has been supported by structural and cohesion funds, which acknowledge the need to address development disparities within a single market. In this respect, the European Union represents a distinct European version of globalization, characterized by common institutions and regulations, integrated financial markets, a common central bank and a common currency (the euro area), and other forms of economic integration.

Poland and the Czech Republic, in particular, can no longer be regarded as emerging economies. It is no coincidence that Poland is among the six-member core group seeking to advance the process of European integration. At the same time, the European Union remains highly diverse, encompassing both large economies with substantial populations and smaller Member States. Technological development also varies considerably across the Union. Among the smaller countries, Estonia stands out for its advanced level of digitalisation and its strong commitment to education. As a whole, however, the European Union faces a competitive disadvantage stemming from its high energy costs, which are several times higher than those in the United States and China. Moreover, increased reliance on liquefied natural gas (LNG) is not an economically attractive solution, as it is considerably more expensive than other energy sources.

AI: A Competitive Disadvantage for the EU

The issue of the growth and development model is being widely debated within the European Union, particularly in light of its lag behind the United States and China in frontier technologies and the adoption of artificial intelligence (AI)—a technological revolution that promises significant benefits while also entailing major risks. Beyond the systemic risks and profound uncertainties associated with AI, which were also discussed at the recent central bankers' meeting in Sintra, where both the Federal Reserve and the European Central Bank (ECB) signalled their intention to move away from forward guidance as a monetary policy communication tool, it is difficult to deny that the United States and China enjoy a considerable lead over the European Union in the deployment of new technologies. They also benefit from more dynamic innovation ecosystems, supported by vast, organically integrated markets and the presence of global technology giants capable of undertaking massive investments.

The development of AI requires enormous financial/energy resources, which could result in a relative shortage of capital at the global level—a form of global crowding-out effect—and could lead to an increase of the natural rate of interest worldwide. Such developments could further widen inequalities, creating new "haves" and "have-nots" among both firms and countries, while also increasing the likelihood of new sovereign debt crises. Whenever the growth rate of nominal GDP (g) falls below the cost of borrowing (i), debt crises become considerably more likely. Romania, inevitably, would also be affected by changes in the global natural rate of interest and by less favourable international financial conditions.

In my view, Philippe Aghion offers particularly convincing explanations for the widening gap between the European Union, on the one hand, and the United States and China, on the other, in the adoption and effective use of artificial intelligence (see also „Why is Europe's economy falling short?", Project Syndicate, 6 June 2026)—an interpretation that differs from those advanced by Olivier Blanchard and Paul Krugman. The key lesson is that the European Union needs deeper integration if it is to remain competitive with the United States and China. This is not merely an economic issue, but also a technological, geopolitical, geoeconomic, and security challenge. It is impossible to speak meaningfully about technological sovereignty or strategic autonomy while simultaneously falling behind in the global technological race. Nor is the issue simply one of financial resources. Equally important are the broader innovation *ecosystem*, the institutional framework, market organisation, industrial policies, and regulatory arrangements that foster sustained technological progress. It is somewhat ironic that a substantial share of European savings is invested in the United States—a point highlighted in the Draghi Report too.

Romania's Imbalances Stem Not From Its Growth Model, But From Macroeconomic Policy Mistakes And Weak Institutions

The questions raised by Romanian economists are part of a broader European debate concerning both relations within the European Union and the Union's position in relation to the rest of the world.

The sharp increase in energy prices following Russia's invasion of Ukraine has affected the entire European economy, while the EU's single energy market continues to function imperfectly. The positioning of European economies within global production and supply chains has also become a major concern across the continent. Yet no other EU Member State is currently confronted with budget and current account deficits as large as those of Romania.

Romania's macroeconomic imbalances are the result of poorly designed macroeconomic policies. In particular, imprudent fiscal policies have led to excessive fiscal deficits. This assessment does not overlook the remarkable economic convergence achieved over the past two decades, during which GDP per capita, measured in purchasing power parity (PPP), has more than tripled relative to the EU average.

Nevertheless, this convergence has been accompanied by an unbalanced pattern of development, characterized by substantial regional disparities—perhaps inevitable under the prevailing circumstances—and by a significant loss of human capital through emigration, itself largely driven by persistent income and development differentials. **Moreover, the concept of a growth model cannot be reduced merely to the relationship between investment and savings.**

It is not a flawed economic growth model that primarily explains Romania's large fiscal deficits over the past decade—including a deficit exceeding 9% of GDP in 2024, when economic growth was below 1%. Rather, these imbalances are the consequence of expansionary macroeconomic policies and the failure to address the pressing need to increase tax revenues through more effective measures against tax evasion and tax avoidance. Romania's tax revenues, including social contributions, amount to only 27–28% of GDP, compared with an EU average of around 40%.

An economy can achieve sustainable growth while maintaining reasonable fiscal deficits and a sustainable level of public debt. In Romania, however, there has been an attempt to accelerate the development process by bypassing necessary stages, accompanied by the implementation of populist policies. As a result, the country now faces the urgent need for a comprehensive fiscal consolidation, one that entails significant economic and social costs. At the same time, Romania continues to struggle with serious institutional weaknesses, widespread corruption, and a profound lack of public trust in state institutions.

It is commendable that attention is being devoted to Romania's future growth model and to the country's long-term development strategy. **However, the implementation of a new growth and development model should not become a precondition for continuing fiscal consolidation.** Such consolidation is an absolute necessity if Romania is to maintain control over its public debt. According to analyses conducted by the Fiscal Council, if fiscal adjustment were to be discontinued after 2026, public debt would remain on an unsustainable trajectory, exceeding 80% of GDP by 2034. The upward path of public debt is also reflected in the deterioration of the gross financing requirement—that is, the combined financing needs arising from debt rollover and budget deficit financing. Gross financing needs are projected to increase from around 15% of GDP in 2026 to approximately 20% of GDP by 2034, substantially increasing refinancing risks. Although the fiscal consolidation measures adopted so far have helped slow the growth of public debt, they are not sufficient to stabilize it.

There is a growing sense of fatigue and public discontent following two years during which public sector wages and pensions have remained frozen (although both had been increased substantially prior to 2025). For this reason, fiscal consolidation could include a prudent indexation of pensions in 2027, linked to the projected inflation rate for that year, so as not to deviate from the intended path of expenditure control. To protect vulnerable households, the extension in 2026 of the cap on mark-ups for essential food products is a welcome measure. At the same time, a much more effective collection of tax revenues would significantly help the fiscal adjustment required in the years ahead.

A reduction in taxes in 2027, as advocated by some political leaders, would constitute a serious policy mistake. It would send a highly negative signal to investors and creditors financing Romania's public debt. Likewise, the belief that a reversal of fiscal measures could be offset through privatization proceeds is fundamentally flawed. Not only would the adverse signalling effect remain, but privatization is also a lengthy process that cannot be carried out overnight. Moreover, permanent losses in permanent revenues cannot be compensated by temporary receipts. State-owned enterprises of strategic importance should not be privatized. This does not preclude restructuring, improvements in corporate governance, or partial stock market listings. Indeed, both the United States and Europe are witnessing a revival of industrial policy, driven not by ideology but by industrial competitiveness, security, and geopolitical considerations.

Fiscal consolidation could be significantly supported by a higher absorption of EU funds under the National Recovery and Resilience Plan (NRRP), as well as the Structural and Cohesion Funds. The SAFE programme may partially substitute the NRRP, but it relies on borrowings, albeit on favourable terms. The programme could provide a substantial boost to the Romanian economy if a significant share of its financing is channelled towards domestic industries.

Romania's accession to the OECD is undoubtedly a positive development. However, it should not be expected to produce economic miracles.

The problem of the dual economy

One aspect that appears to be underestimated in the debate on Romania's growth model is the relationship between domestic and foreign capital. Romania has **a dual economy**. This duality is not primarily about the multiple disparities between rural and urban areas—which have undoubtedly contributed to emigration—but rather about the country's capacity to pursue an effective industrial policy. If we accept that Romania needs an industrial policy, at least two issues must be taken into account. First, many of the large companies that dominate key sectors of the Romanian economy operate according to international business strategies. In other words, their strategic decisions are difficult to influence. If, for example, they decide to cease operations in Romania, there is little that public authorities can do unless they possess adequate policy instruments—as illustrated by the cases of the Mangalia shipyard and the Galați steel plant. Second, any industrial policy requires substantial financial resources, and Romania currently faces severe constraints in this regard because of its large fiscal deficits. The fiscal deficit cannot remain at around 6% of GDP; it must be gradually reduced towards 3% of GDP, while achieving a primary fiscal surplus, given that interest payments on public debt are expected to exceed 3% of GDP in the near future. Romania should therefore make full use of the European Union's Multiannual Financial Framework (2028–2034) to support its industrial policy objectives. At the same time, growing defence spending requirements further complicates the process of fiscal adjustment.

Domestic capital needs to become stronger and more dynamic, working alongside foreign capital in industries and sectors that generate higher value added. Romanian companies should also expand beyond the country's borders, following the example of firms from Poland, Hungary, and the Czech Republic. This, however, is not an immediate prospect.

There remains a very large number of enterprises—particularly small and medium-sized businesses—that are not bankable and therefore do not make use of bank financing.

Greater attention must be paid to the efficiency of public investment. Investment projects should be carefully prioritized, and the government should avoid launching numerous large-scale projects that it ultimately lacks the resources to finance, as occurred under the National Recovery and Resilience Plan (NRRP). The Romanian Development and Investment Bank should play a more active role in promoting public-private partnerships. Labour force participation also needs to increase. Romania requires a more effective agricultural policy and more diversified external economic relations, including with countries outside the European Union.

Given the absolute necessity of fiscal consolidation, it would be quite difficult for the public budget to sustain annual defence expenditure amounting to 3.5% of GDP (compared with approximately 2.4% of GDP in 2026), let alone 5% of GDP, even over a longer time horizon.

Achieving such spending levels would require reductions in other categories of public expenditure, together with higher tax and non-tax revenues.

Romania's public budget allocates insufficient resources to education, while expenditure on research and development (R&D) remains almost negligible. Under these circumstances, it is difficult to envisage Romania overcoming its structural dependence on the more advanced European economies.

Concluding remarks

We should avoid creating the misconception that Romania's macroeconomic imbalances are the result of a flawed growth model. These imbalances stem primarily from macroeconomic policy mistakes, although some would argue that a wage-led growth model explains the country's unsustainable economic expansion. Weak institutions are also an important contributing factor.

Some structural weaknesses can be mitigated over time, while others are likely to persist because they are rooted in broader challenges facing the European economy and in the balance of power within the European Union.

It is difficult to believe that Romania could become the "Norway of the Black Sea" by exploiting natural gas resources and generating substantial resource rents capable of significantly strengthening the public budget. Nevertheless, these resources can play an important role during the transition period, as Romania continues its gradual shift away from fossil fuels.

Demographic trends and population ageing constitute major constraints, not only for Romania but for all Member States of the European Union.

Romania's economic future is closely linked to that of the European Union. A different growth model will depend on sound public policies, both at the national and the European levels, as well as on sustained public and private investment.

Romania cannot join the euro area as long as it continues to run large fiscal deficits. Declaring the intention to adopt the euro is not enough; the necessary economic conditions must also be met.

The trap of persistently large fiscal deficits is more dangerous than the middle-income trap.

P.S. The views expressed in this article do not necessarily reflect the position of the Fiscal Council.