

AN ANALYSIS OF UNDERGROUND ECONOMY IN ROMANIA

GABRIELA CORINA SLUSARIUC *

ABSTRACT: *Shadow economy is a negative phenomenon, which exists in all countries of the world, in varying proportions in GDP, being an unavoidable component of a country's economy. Estimating the underground economy is a difficult issue, the real size of the underground economy remains unknown and the controlling of it is almost impossible.*

KEY WORDS: *control, underground economy, clandestine work, economic development, tax avoidance, GDP.*

JEL CLASSIFICATION: *O17; O47; D78, H11, H26, K42, O57.*

1. INTRODUCTION

Shadow economy exists in all countries of the world, in varying proportions in GDP, being an unavoidable component of a country's economy. The emergence of the underground economy coincides with the emergence of the state and the taxation in any form, and therefore the development of the phenomenon is correlated with the historical stages of state development.

Clandestine trade in diamonds or other precious stones, spices and silks, poaching, clandestine distilleries are illegal activities since ancient times. Also, the complementary trade, the border trade with consumer goods missing from the organized socialist market and the big business, such as arms trafficking, human trafficking, drugs, tobacco, alcohol, has completed the underground economy throughout history. The underground economy appears in the literature under various names: unofficial, illegal, dissimulated, parallel, appendix, dangerous, ghost, invisible, dual, cash, informal, secondary, shadow, immeasurable, contra economic, occult, hidden.

* *Assoc. Prof., Ph.D., University of Petroșani, Romania*

2. THE CONCEPT OF SHADOW ECONOMY. LITERATURE REVIEW

Specialized literature has many concerns for defining the underground economy. However, the definitions differ as a result of the various methodologies used to assess its size, and there is also a disagreement on the definition of underground economy activities (Schneider and Enste, 2000).

Among the most recognized and accepted definitions: (Choi and Thum, 2005), the underground economy is made up of activities that are not recorded in government statistics. The underground economy is made up of all unregistered business activities that would otherwise contribute to gross domestic product calculated (or noticed) according to a commonly used definition (Schneider et al., 2010).

In another definition (Feige, 1994), the underground economy comprises activities that are the result of transactions in illegal goods and services or tax evasion offenses. Schneider, who uses the term "shadow economy" for the underground economy, estimated in several papers its annual size (as a percentage of gross domestic products) for many countries around the globe over different periods.

One of the most complex definitions of the underground economy is given by Pierre Pestieau, according to which the underground economy is "the whole economic activity that is done outside criminal, social or fiscal laws or that escapes the inventory of national accounts". The European Commission defines the shadow economy as being "those economic activities and the income derived from them that circumvent or avoid government regulations or taxation" (European Commission, 2014, p. 1).

So the underground economy can be defined as the totality of the organized economic activities, but in which the social norms and the economic laws are not complied, aiming at obtaining revenues that are uncontrolled and taxed by the state.

Within the scope of the underground economy were included many varied practices, namely tax fraud, clandestine work, drug trafficking, arms trafficking, corruption, prostitution, and a lot of domestic activities that bring unregistered income.

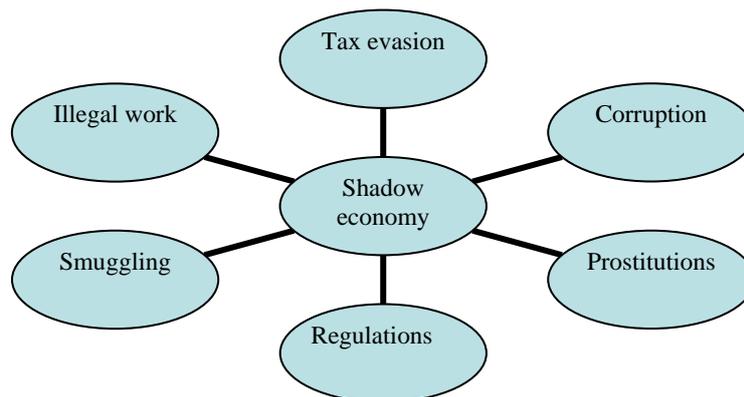


Figure 1. Main components of shadow economy

Participants in the underground economy are part of two categories of people; those who work and earn only in the underground economy, and the second category is the people who receive income from both legal sources and the underground economy. Specialized literature identifies as some of the main causes generating underground economy: pressure exerted by state regulations (Ivaggi, 2007); fiscal pressure exerted by taxation (Caballé, Panadés, 2007); the moral attitude of citizens towards the state (McGee, 2005, Torgler, Valev, 2007).

3. ANALYSIS OF THE SHADOW ECONOMY IN ROMANIA

Friedrich Schneider (2015), using the MIMIC model, has estimated the dynamics of the underground economy for the period 2003-2015, showing a decrease from an average of 22.6% to 18.2% of GDP (sample being made up of 28 EU Member States).

Table 1. Shadow economy evolutions in Romania in 1999- 2016 years

Years	Shadow economy % GDP
1999	34,3
2000	34,4
2001	33,7
2002	33,5
2003	32,8
2004	32,0
2005	31,7
2006	30,7
2007	30,2
2008	29,4
2009	29,4
2010	29,8
2011	29,6
2012	29,1
2013	28,4
2014	28,1
2015	28
2016	28

At beginning of the analysed period, Romania quantified the underground economy to a third of GDP. In the period 1999-2016, Romania recorded a continuous decrease of this phenomenon, except for the period 2010-2011, it has the best recovery (-5.6%). However, Romania recorded a high share of the shadow economy in present.

Analysing the evolution of Romania's underground economy from 1999 to present as a percentage of GDP, according to Schneider's estimates, based on the MIMIC model, it places the underground economy at about 34% of GDP in the first years of the studied period (maximum 34.4% reached in 2000) and around 30% of

GDP in the last years of the period (the minimum value of 29.4% achieved in 2008 and 2009), the overall trend being a decrease in its size.

Estimating the underground economy is a difficult issue, and several methods can be used for this purpose, which provide results that sometimes differ greatly between them. The assessment of Romania's underground economy has come to the attention of several Romanian researchers. According to a survey (Albu, 2008), between 2000 and 2006, informal incomes are decreasing in Romania from 22.3-22.8% of total household incomes to 16.3-17.5%.

In specialized literature (Andrei, 2011), it was determined the size of Romania's underground economy in the period 2000-2009, based on Cagan and Ahumada's monetary method, which is higher than 30% of GDP.

The Fiscal Council has made an analysis of the unnoticed economy in 2013, which it has not updated for lack of data. According to this, black labour and VAT evasion represented the bulk of the black economy. On the economic sectors, the most important contribution to "undeclared work" is the industry (548.4 thousand persons), followed by trade (358.9 thousand people), construction (335.6 thousand people) and transport and communications (163.3 thousand people).

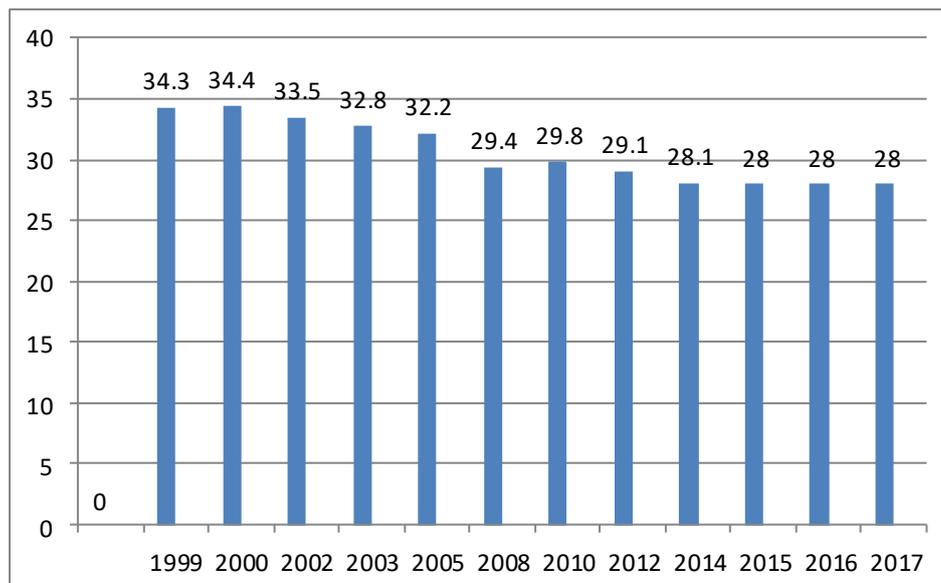


Figure 2. Dynamics of shadow economy in Romania in GDP

Experts estimate that in 2017, in Romania, the black economy will produce more than 228 billion lei of GDP estimated at 815 billion lei, which will lead to a loss of 81 billion lei for the state budget, about 18 billion Euro. The 334 billion lei as the Romanian state has borrowed, that loan could be paid in four years if we did not have a shadow economy. But this is an ideal situation, which does not exist in any country, yet a realistic variant, to reduce the tax evasion by 10 percentage points, would bring

to the budget 29 billion lei, in half of the amount that the state will have to borrow this year.

Assessing the trend of the underground economy in Romania in recent years, it can be seen that it is registering a slight decrease, the trend decreasing.

Table 2. The share of GDP in the underground economy and black labour

No	Country	Shadow economy %GDP	Illegal work %GDP
1.	Romania	28	15-20
2.	Bulgaria	30	22
3.	Poland	23,6	14
4.	Hungary	21,9	17
5.	Italy	20,6	5
6.	France	12,3	5
7.	Denmark	12	3
8.	Germany	12,2	7

We can see that undeclared work represents more than 50% in many states, but in particular in less developed countries like Romania, Bulgaria, Hungary.

Non-legal work is between 15-20% of GDP in Romania, according to the European Union Country Report published in 2017. If we take into account the minimum percentage of 15% of GDP, it is clear that Romanians are earning from undeclared activities 123 billion of lei, or about 27 billion euros. This means that the state will lose 54% of this amount (CAS, CASS, unemployment), 66 billion lei.

Table 3. Dynamics of shadow economy UE-4 (%GDP)

Years	Romania	Bulgaria	Hungary	Croatia
2003	32,8	35,9	25,0	32,3
2004	32,0	35,3	24,7	32,3
2005	31,7	34,4	24,5	31,5
2006	30,7	34,0	24,4	31,2
2007	30,2	32,7	23,7	30,4
2008	29,4	32,1	23,0	29,6
2009	29,4	32,5	23,5	30,1
2010	29,8	32,6	23,3	29,8
2011	29,6	32,3	22,8	29,5
2012	29,1	31,9	22,5	29,0
2013	28,4	31,2	22,1	28,4
2014	28,1	31,0	21,6	28,0
2015	28,0	30,6	21,9	27,7

Source: Based on Friedrich Schneider (2015)

Overall, it is a development of the formal economy corresponding to a contraction of the shadow economy. The countries of Central and Eastern Europe

(Romania, Bulgaria, Croatia) have a higher share of the shadow economy than the old countries from European Union (Germany, Austria, Belgium, Italy) research as Schneider show. His studies reveal an increase in the size of the underground economy from west to east and from north to south.

The underground economy has many facets in Romania. The most well-known are tax evasion and undeclared work, but there are many other activities that escape taxing the state. For example, drug trafficking, illicit arms trade, corruption, prostitution, tutoring, domestic activities, etc.

The key factors that have allowed for the underdeveloped development of the underground economy can be mainly the following:

- legislative uncertainties that accompanied economic changes;
- uncontrolled economic division, the emergence of small enterprises with temporary, speculative activity;
- decentralization, division of power through the distribution of responsibilities, thus increasing the number of corruptible individuals;
- the tolerant attitude of both the authorities and the population towards the violation of regulations, some reticence towards discipline;
- the immediate junction made by representatives of the parallel market in the socialist period with circles with similar concerns in the neighbouring states and, in this way, the connection to the international structures of the underground economy.

Some researchers say the "underground" economy can be beneficial as long as it serves the good development of the economic environment by meeting the demand for urban services and small craftsmen. From this point of view, the informal sector assures the entrepreneurial spirit of the economy, can lead to increased competition, increased efficiency and strong barriers to government activities that facilitate or even inhibit the manifestation of market instruments.

4. CONCLUSIONS

The phenomenon of circumvention is not just an economic phenomenon, but rather a social phenomenon with strong psychological implications. Economic literature has found its way out with the following argument: "it is in the nature of man to agonize and to avoid as much as possible the shedding of parts of wealth" or "man always has the adverse reaction to the authority he is trying to deceive" "Individualism is a more powerful human behavioural trait than collectivism" (Le Bars, 1979). The existence of the "underground" economy lies both in the incapacity of market agents and in the incapacity of state representatives (Voicu C., 2012).

The underground sector can contribute to creating markets, increasing financial resources, enhancing entrepreneurship, and ensuring the accumulation of economic and social institutions. Natural selection between the formal and informal sector can provide increased potential for economic growth, which leads to a positive relationship between the growth of the underground economy and economic growth. The beneficial effects of these expenditures on economic growth and income tax are obvious.

So, although the underground economy is a negative phenomenon, in a minimal proportion is acceptable, the right of the "underground" economy to existence as a branch among economic sciences is gained, and the main argument lies within the existing evidence that the "underground" economy is a source of development, subsistence and even escape from the periphery for underdeveloped economies.

The shadow economy has been and remains an important issue for scientific debates and an important problem for all governments of the states of the world.

REFERENCES:

- [1]. **Albu, L.** (2008), *A Model to Estimate Spatial Distribution of Informal Economy*, Romanian Journal of Economic Forecasting, Nr. 4.
- [2]. **Andrei, T.** (2011), *Relations de causalité entre l'économie souterraine et les variables macroéconomiques: application sur la Roumanie*, Revista Română de Statistică, Nr. 3.
- [3]. **Andrei, T., Roșca, I.Gh., Matei, A.** (2008), *Corupția. O analiză economică și socială*, Editura Economică, București Brașoveanu, I.V.
- [4]. **Brașoveanu, I.V.** (2010), *Economia subterană și corupția: probleme majore ale economiei românești*, Economie teoretică și aplicată, Vol. XVII, Nr. 11(552)
- [5]. **Brașoveanu, I.V.** (2009), *Analize ale politicii fiscale în România și în statele membre ale Uniunii Europene*, Editura ASE, București
- [6]. **Brașoveanu, I.V., Obreja Brașoveanu, L.** (2009), *Correlation between Corruption and Tax Revenues in EU 27*, Economic Computation and Economic Cybernetics Studies and Research, no. 4
- [7]. **Choi, J. P. and Thum, M.** (2005), *Corruption and The Shadow Economy*, International Economic Review, Vol. 46, No. 3, pp. 817-836
- [8]. **Dinga, E.** (2009), *Studii de economie. Contribuții de analiză logică, epistemologică și metodologică*, Editura Economică, București
- [9]. **Dinu, M.** (2008), *Economie teoretică și aplicată, Modelul explicativ al globalizării*, nr. 3
- [10]. **Friedman, M.** (1995), *Capitalism și libertate*, Editura Enciclopedică, București
- [11]. **Ghițescu, F., Banciu, M.** (2000), *Economic Crime in Romania*, The Journal of Social, Political and Economic Studies, Vol. 26, No. 4, 2001
- [12]. **Giddens, A.**, *Sociologie*, Editura Bic All, București
- [13]. **Manole S.**, *Impactul economiei subterane asupra economiei României*, disponibil la http://www.strategiimanageriale.ro/images/images_site/articole/article_8ed203a27d1505d5e5dd2d9719118eda.pdf
- [14]. **Perkins, J.** (2007), *Confesiunile unui asasin economic*, Editura Litera Internațional, București
- [15]. **Rădulescu T.** (2007), *Evaziunea fiscală în România în perioada de tranziție*, ASE, București
- [16]. **Schneider, F., Dominik, E.** (2002), *Shadow Economy*, Cambridge University Press
- [17]. **Slusariuc G.** (2012) *Control financiar*, Editura Universității din Petroșani,
- [18]. **Soroș, G.** (2002), *Despre globalizare*, Editura Polirom, Iași
- [19]. **Stiglitz, J.**, (2010), *În cădere liberă. America, piața liberă și prăbușirea economiei mondiale*, Editura Publica, București
- [20]. **Tudose B, Clipa R.**, *An Analysis of the Shadow Economy in EU Countries*, CES Working Papers – Volume VIII, Issue 2
- [21]. **Voicu Dobrescu, E.** (2002), *Tranziția în România. Abordări econometrice*, Editura Economică, București

-
- [22]. <http://studiaeconomia.uvvg.ro/images/2001/v2/34.%20economia%20subterana.%20abordari%20conceptuale%20si%20forme%20de%20manifestare.pdf>
- [23]. http://store.ectap.ro/articole/529_ro.pdf
- [24]. http://store.ectap.ro/articole/752_ro.pdf
- [25]. http://www.strategiimanageriale.ro/images/images_site/articole/article_8ed203a27d1505d5e5dd2d9719118eda.pdf
- [26]. http://www.ipe.ro/RePEc/vls/vls_pdf/vol12i4p20-50.pdf
- [27]. http://www.fin.ase.ro/ABC/fisiere/ABC1_2013/Lucrari/2.4.pdf
- [28]. <http://jurnalul.ro/bani-afaceri/economia/cu-banii-pierduti-s-ar-putea-face-sase-autostrazi-739646.html>
- [29]. <http://www.preferatele.com/docs/economie/9/economia-subterana-i15.php>
- [30]. <https://www.forbes.com/sites/niallmccarthy/2017/02/09/where-the-worlds-shadow-economies-are-firmly-established-infographic/#ecdd52a742cc>
- [31]. <http://www.econ.jku.at/members/Schneider/files/publications/2015/ShadEcEurope31.pdf>
- [32]. http://ec.europa.eu/public_opinion/archives/ebs/ebs_402_en.pdf
- [33]. http://www.atkearney.com/financial-institutions/featured-article/-/asset_publisher/j8IucAqMqEhB/content/the-shadow-economy-in-europe-2013/10192