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NATIONAL DEFENSE PLANNING CHALLENGES DURING ECONOMIC AND FINANCIAL CRISIS

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Abstract:

Romanian economy is linked with worldwide economies, thus meaning that the international financial crisis affected also Romania. These reflected on GDP which by extent reflected also upon figures allocated to programs, which in turn had a major impact upon defence planning. We have to admit the transcendence of the good and bad things of the global economy to the individual economies, Romania not being an exception. At that time Romania was engaged in the process of the European integration, one dimension of it being the financial one, meaning that it cannot be secluded from the crisis impact.

With a fully current account liberalized, convertibility and high openness of the economy towards world economy, in terms of foreign trade, during a crisis with such a geographical extension, there is no doubt that some well-known vulnerabilities are perceived strongly by investors and analysts. A balanced approach of internal factors which can be under the pressure of the transmission channels bringing external shocks is more appropriate for the judgment of the possible domestic outcomes of the present crisis, either in financial field or economic one.

Key words: crisis, globalization, financial system, risk

1. Introduction

In Europe, some of the most dangerous effects of the most recent financial and economic crisis have not been fully understood yet. For almost three years, the focus has been on the financial sector, the job market, and on the stability of the common currency. These were the fields where the immediate effects of the crisis were most damaging and where systemic stability was at stake. Due to massive state intervention, the system did not collapse and where it crumbled, further state intervention prevented worse.

2. Overview on national defence planning

“A process of determining the volume, structure and allocation of resources (human, material, financial etc.) needed for the fulfillment of objectives related to national security and Romanian defense”.

2.1 What is Defence Planning?

Defence Planning is a process that has the objective to put in practice the defence policy objectives by transforming them into military capabilities. During financial crisis, defence planning can be very hard, due to the scares resources and competition for them.

Defense planning seeks to ensure that a nation has the necessary forces, assets, facilities and capabilities to fulfill its tasks throughout the full spectrum of its missions.

Like in every modern democratic state, defence integrated planning is a tool that provides democratic control over the armed forces. The desired level of control can be

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achieved through PPBE System, which offers a clear view for expenditures of armed forces and also on their profile.

2.2. Defence planning after 1990

After 1990, due to the obvious orientation to the west organizations, like North Atlantic Treaty Organization (NATO) and European Union (EU), it was obvious that some changes have to be made to the approach on defence policy.

That means that major changes in the basis of security and defence mechanism had to be made very quickly, to shift from an east oriented thinking to a more democratic western approach. These did not happened smoothly and softly due to different opinions and because it had to be made “on the run”. Also, due to the need of rearrange the national laws in the light of the new democracy, a large number of important laws and amendments for the defence strategy were postponed and pushed back, in order to solved more important economic and social issues.

To begin the presidential authority must issue National Defence Strategy which gives the lines for the White Paper of the Government (WPG), adopted by the government and approved by the Parliament. These will have inputs also from the Romanian National Security Strategy, issued also by the presidential authority. Based on the WPG the Ministry of National Defence (MoND) will issue the Romanian Military Strategy, who has to be approved by the government.

After the approval of the Romanian Military Strategy, the Romanian Ministry of Defence will issue the Defence Planning Guidance which will give the directions and basic lines for main defence programs, Annual plans, Defense plans and contingency plans.

3.Challenges to National Defence Planning during economic and financial crises

In almost all European states, including Romania, and also in U.S., the defence budget is being used as a convenient quarry for saving money, exactly because the adverse effects of cutting defence are long-term and quite abstract – and therefore, also, hidden. As a consequence, many European states are on the verge of losing even basic defences capabilities, despite painful reform efforts to make their military more efficient. Most unfortunately, this is happening at a time in global politics where the traditional guarantor of European security, the United States, is struggling with its own budget crisis and problems of military overstretch.

3.1 The economic and financial crisis of 2007 and its affect upon Romania

The progress of the emerging countries, characterized by the increase of their capacity of production and export of goods and services and of capital, but also their ability to become new markets for the most evolved western economies, resulted in a specialization of the strongly industrialized countries, which reached the limits of “danger” in terms of the external macroeconomic misbalances.

The financial crisis of 2007-2008 is considered to have been the worst financial crisis since the Great Depression of the 1930s. It began in 2007 with a crisis in the mortgage market in the US, and developed into a full international banking crisis with the collapse of the investment bank Lehman Brothers on September 15, 2008. Excessive risk-taking by banks such as Lehman Brothers helped to magnify the financial impact globally. The crisis was nonetheless followed by a global economic downturn, the Great Recession. The European debt crisis, a crisis in the banking system of the European countries using the euro, followed later.

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Of course we have to keep in mind the opinion which state that if a cycle of world economic growth ends, which was based on low interest rates and low inflation, which may open a new, tougher, competition for the cost of goods and services.

The initial intensity of the financial turbulences overlapped the crisis of the agro-food products, which has both structural causes such as reduction of cultivated agricultural land, conversion to bio fuels, and climacteric reasons displaying a long-term trend (global warming, el Nino, greenhouse effect).

The shock of basic agro-food offer highlighted even stronger the “energy shock” manifested by the continuous increase of oil price, which peaked at 147 USD a barrel, in July 2008.

Romania, as EU member state, as actor of the global economy, is exposed to the mentioned evolutions, some of them inherent to the option of market economy, other deriving from the contractual relations, primarily focused on the values of the political and economic democracy. In technical terms, the connections to the world economy, regarded by preferential regional groups, such as the affiliation to the European Union, refer to the types of liberalization: foreign trade, prices of goods and services, capital investments, capital account, national currency convertibility.

Starting from the premises of the causes of the current financial crisis, its acutization towards late 2007 and early 2008, displayed by the bankruptcy of systemic financial institutions and selective interventions to save them both in the USA and in European countries, puts us in front of accepting the evidence of realities in relation to which the feeling of immunity or invulnerability gets fluctuating connotations. At such a moment of perceptions, dominated by incertitude and lack of trust, any level of defiance or comfort in front of a possible adverse impact should better remain within the boundaries of rationality. This has several qualities:

- (i) acknowledgement of the intrinsic existence of the channels for crisis propagation;
- (ii) correct evaluation of the reception capacity of the propagation effects of the crisis through normal transmission mechanisms;
- (iii) existence of filters which deflect the frontal blow, consisting in regulation, conduit of the macroeconomic policies;
- (iv) financial reserves for intervention;
- (v) capacity to coordinate the specific measures on the horizontal of the institutions with similar responsibilities of the foreign partners.

As far as Romania is concerned, the analyses of the central bank or of independent banks show the existence of a certain resistance of the internal financial stability to the international financial turbulences, both through the indirect channel (impact on the real economy), and through the direct channels (impact on the banking sector and on the financial markets), although some adverse evolutions might affect much stronger Romania, such as interbanking interest rates volatility or speculative attacks on the exchange rate.

Having these into consideration, we must state that the impact of the world crisis on Romania was to some extent under control, mainly because of a sum of multiple factors that protect the financial Romanian system, to some extent, such as:

- the monitoring by the National Bank of the banks operating in Romania
- regulations imposed by National Bank have been in many times more restrictive than standards.
- National Bank representatives are involved, at the level of the competent community structures, in the process of analysis and improvement of the community regulations concerning the architecture of the financial system;
- The sustained deflation process, despite the inflexion during the second half of 2007 due to the shock of the offer, outside the central bank control

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- The level of the compulsory minimal reserves remained high for a long period, much higher than the standards of the European central banks
- The credit institutions in Romania are not exposed to subprime products.
- The measures intended to moderate the rate of credit increase, adopted by the National Bank, permanently aimed a sustainable long-term growth of credits,;
- Although the liquidity within the system of the credit institutions in Romania decreased compared to the previous years, it still is at an adequate level for a proper functioning of the markets. The relative decrease of the liquidity is also due to the repositioning towards normality of the Central Bank's role within the financial system, from net debtor, to net creditor;

Some evaluations made within the context of the mentioned circumstances, lead to noteworthy assertions in terms of the principal approaches to the effects of the crisis. If we refer to the direct transmission channel, represented by the international trade, foreign investments, exchange rate, interest rates to the lines of credit in foreign currencies taken by the financial and non-financial societies, the following are to be mentioned:

All these considerations are far from being an idyllic plead and, so much more, they must keep us far from any temptation of euphoria in front of a reality of an unprecedented financial crisis in the post war history. Do not forget that it compelled and still compels the governments and central banks from the United States and the other developed countries worldwide to take, also unprecedented, measures. A full analysis must also include the short and long-term risks. These have to be identified, understood and included in action plans to be corrected, knowing that for the time being the timetable for shifting to euro didn't change.

The limited effect of contamination of the Romanian financial system from the international financial crisis doesn't exclude effects on the real economy due to its opening towards world economy. Any delay in starting structural reforms will make the shocks of the recession from other parts of the world to be more painfully felt by the Romanian economy and shatter the few consumption exuberances of millions of citizens after decades of privations, of bad allotment of the resources.

3.2. The implication of financial crisis on the Defence Planning

Based on the Defence planning guidance each major program will develop programs with elements, sub elements and so on, for modernizing and training forces. Also, each year, every director of major program will design annual plans to maintain, operate, modernize and train the forces at his disposal, based on the funds allocated through the state budget.

They will keep track of those programs using the tool of Planning, Programing, Budgeting and Evaluation System. The cycle of PPBES is depicted in the below figure:

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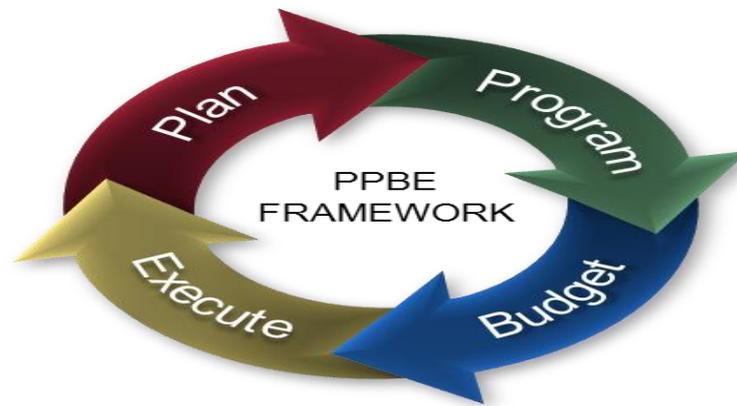


Fig.1 PPBE Cycle

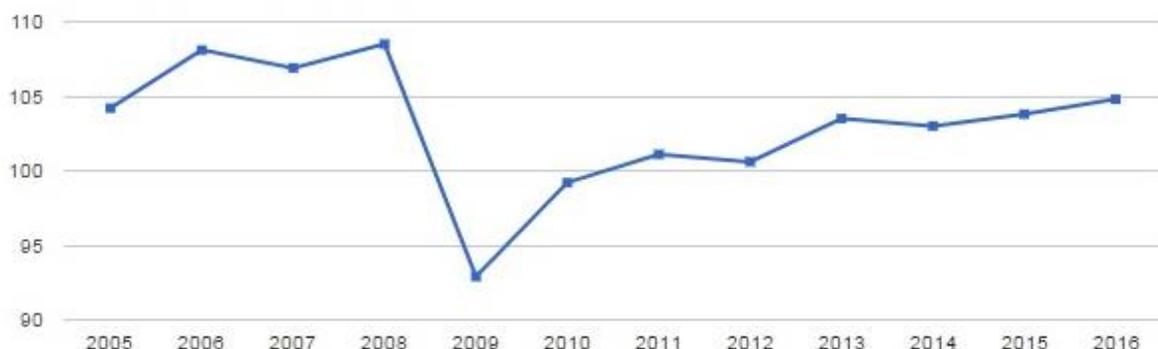
When crisis occurred it seemed only logical to cut the defence expenditures, this program being somehow less quantifiable than other more sensitive to the public, like domains like health, education and so on.

It sounds plausible that shrinking budgets increase the pressure on member states, including Romania to cooperate and thus overcome the EU's problems related to capability development and restructuring of the defence industries and markets. On the other hand, national prerogatives still dominate despite a decade of rhetoric and initiatives for more cooperation and less state in EU defence. If this national focus continues to dominate under current financial circumstances, EU member states run the risk to implement cuts in their Armed Forces in an uncoordinated way. As a result, member states might end up with potentially even bigger capability gaps than they have today and hence even less opportunities to implement the Common Security and Defence Policy.

This is also what happened with the Romanian expenditures related to defence. Because of the decrease of the Gross Domestic Product (GDP) the battle for resources between ministries become more visible and more acute. The public pressure forced the authorities to make cuts from domains less visible to the public and with a low impact on him.

The ministry that lost the battle on resources was the Ministry of National defence, who experienced a big reduction of the budget which led to problems that are visible even today, although the crisis is over, and even though since this year, for a period of 10 years, there is a political consensus to allocate 2% of Gross Domestic Product to Defence.

In the figure below we can see the evolution of real GDP starting December 2007 all the way to the crisis period.



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Fig.2 Evolution of GDP

In a study of the Committee on Foreign Affairs Notes regarding the implications of the crisis upon defence expenditures we can sense the real concern regarding this topic. It underline that following the financial and economic crisis, unprecedented cuts in defense budgets have been made in almost every EU Member States, including Romania. This cuts led to negative effects on military capabilities and. The solution to overcome these aspects is a greater coordination and cooperation at European level.

The cuts in the military expenditure could also result in a complete loss of some of military capabilities, while the programs directors are put in a very difficult position of choosing between operating and maintain the existing capabilities, including personnel, invest in research and development or in acquisitions.

In these respect, it is worth mentioning that some of the important documents that stood at the bottom of Defence Planning are no longer viable, due to the significant changes in the economic and financial domain, but also in other domains.

If we take into account the process that is necessary to adapt and change the documents, that will result in major delays to the programs, delays that can have devastating effects upon the developing a coherent approach to the crisis.

The process of reviewing for example the White Paper should be continuous and should take into account the available means and resources, taking Consideration also of the non-traditional aspects of security. These should be done taking into consideration the link between national defense planning, a common security perspective and a common threat assessment.

In the figure below we can see the evolution of military expenditures from 2007 through 2014.

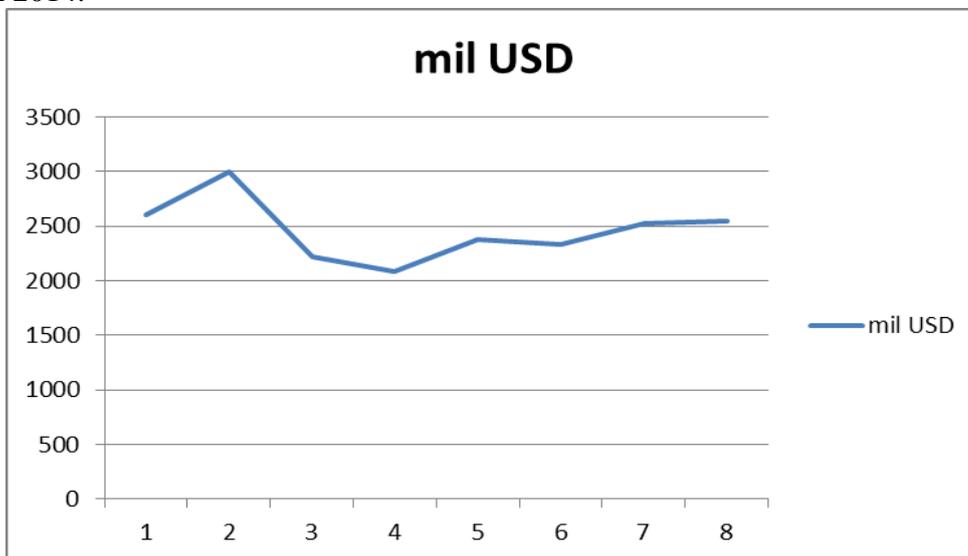


Fig.3 The military expenditures during 2007-2014

If we are to refer to Romania engagements to the organizations that she is part of, we cannot forget about our country commitment to participate to global security under NATO command. Due to the unprecedented cuts United States of America was forced to cover up to 75% of the defense spending of the North Atlantic Alliance.

The answer for this problem is a closer cooperation with between all stakeholders and coordinates their actions against the common threats identified. This can be a short to medium term answer to the increasingly complex and unpredictable security environment.

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Another factor of utmost importance is to recognize that not all threats are of a military nature and that the Romania, as part of European Union, can call upon a variety of tools for crisis prevention and management such as civilian capabilities and technical assistance instruments. Very important in that respect is the relationships with the neighboring countries but also the ability to stand up and respect is commitments, assumed by strategic partnerships or treaties. These will result in an increase of defense capacity by assuring a peace climate on his borders.

During crisis period a special attention is needed to the way in which most of these funds are spent on the basis of uncoordinated national defense planning decisions which resulted in persistent capability gaps. These also led to overcapacity and unnecessary duplication as well as industry and fragmented markets.

Thinking a little bit further, we must not forget that in times of economic and financial crisis, the reductions in the defense budget can lead to significant reductions or significant delays of the programs. These can also lead to disorders in the R&D and also can lead to job losses in the medium and long term.

During period of economic and financial crisis, defense policy should take into account cooperation between Member States in fields like research, technological and industrial know how in order to strengthen the competitiveness and resilience of the defense industry.

In this respect a very important role is played by the technological transfer between civil and defense industries, by analogy with what is being done successfully in the areas of communication and space, through the passage of traditional military operations to peace operations in recent years, terrorism, humanitarian assistance and support for civil authorities.

Very important to mention is the fact that in a report of EU is clearly stated that no defense industry in the EU can be viable at national level and that a strengthening of the EU defense industry will lead to a reduction in defense budgets. That leads us to the fact that, in the light of globalization, defense industry policy should promote multidimensional cooperation for the benefit of the country, highlighting the main industrial objectives, comparative advantages and strategic industrial sectors. In this respect is very important to stress the role of the European Defense Agency (EDA) in supporting cooperation between Member States.

In the same report is stressed the fact that, especially in sectors such as strategic and tactical transport, logistical support, maintenance, space capabilities, cyber defense, health care, education and training, as well as some niche capabilities, Member States would greatly benefit from putting together and sharing functions and facilities without creating significant dependencies that would limit their sovereignty in decision-making.

During the financial and economic crisis, the pool of resources becomes very limited. In order to mitigate that it is very important that pooling of resources to be accompanied by a deepening specialization so that it can be renounced to certain capabilities that can be offered by partners.

4. Conclusions

Although that the economic and financial crisis are not something to desire, they can be used as an opportunity to integrate the country defense policies, as this can provide the impetus for the creation and, ultimately, the implementation of ambitious reforms.

These defence policies should take into account also the involvement of the country to NATO and EU initiatives. From these result the need of a cross-border and transatlantic industrial cooperation can facilitate access to new technologies, promote the development

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of advanced products and provide incentives to seek effective cost-cutting and production-cycle measures.

The effect of the economic and financial crisis on the military expenditures was so big because of a series of factors, apparently independent one from each other. Due to the cuts made, programs had to be changed, defence industry were lacking orders, resulting in cuts of personnel who in turn reflected on GDP.

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