THE IMPACT OF GOVERNMENT INTEGRITY AND GOVERNMENT SPENDING ON ECONOMIC FREEDOM

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Abstract: As a basic feature of a market economy, a nation's economic freedom must often be viewed in terms of its relationship to prosperity. A low degree of economic freedom indicates barriers imposed by political governance to personal choice, freedom of exchange, investment decisions, property, and protection of the person. Taking into account the components of the economic freedom index, this article will capture how government integrity and government spending influence economic freedom in Romania. Without claiming to be an exhaustive approach, by identifying threats and opportunities, we believe that pertinent solutions can be found to improve the degree of freedom.

Keywords: economic freedom; government integrity; government spending; correlation; prosperity

Introduction

Now in its 30th edition, the Index of Economic Freedom (Heritage Foundation, 2024) once again demonstrates the relationship between progress and economic freedom, and the consideration of the 12 components, of equal importance, allows the establishment of the score of each state, in the basis of which opportunities and threats to economic growth and prosperity can be considered.

Considering the four aspects on the basis of which economic freedom is determined (Rule of law, Government size, Regulatory efficiency and Market openness), we consider it appropriate to subject Government Integrity and Government Spending to analysis, since the size and method of allocation of public financial resources, as well as lack of government integrity have a significant impact on economic dynamism.

Starting from the significance of Economic Freedom, Government Integrity and Government Spending, we will analyze the evolution of these indicators at the Romanian level, the position occupied at the global level and the influence on economic freedom. Based on the positive and negative aspects obtained as a result of the analysis, we will identify possible solutions for improving the indicators, taking into account both studies and research in the specialized literature, as well as good practices found in other states.

Studies and research on Economic Freedom, Government Integrity and Government Spending

Along with establishing the concept and methods of quantification, economic freedom is treated in many studies by considering the benefits to each person and each nation, both for the general framework and for each of its components.

From the perspective of the general framework of economic freedom, the relevant and most cited studies in the specialized literature highlight: the relationship between economic freedom and economic growth/prosperity (De Haan and Sturm, 2000); analyses and comparisons of the index of economic freedom at a global level (Gwartney, 2008); the impact of economic freedom on entrepreneurship (McMullen, Bagby and Palich, 2008); the relationship between economic freedom and quality of life (Stroup, 2007); the impact of

economic freedom on foreign direct investment (Azman-Saini, Baharumshah and Law, 2010); the relationship between economic freedom and sustainability (Thiele, 2024).

For the components of economic freedom which are the subject of this article, we consider the following to be relevant:

- Vizibilitatea The visibility of the positive impact of government spending on economic growth is usually in the short term and less in the medium term (Lin, 1994) and is higher in more democratic countries (Plümper and Martin, 2003). While there is a direct relationship between the increase in government spending and the increase in consumption (Galí, López-Salido and Vallés, 2007) and real wages (Ramey, 2011), the multiplier of government spending is related to the nominal interest rate (Christiano, Eichenbaum and Rebelo, 2011) and its increase is observed when fiscal policy is based on higher fiscal progressivity (Ferriere and Navarro, 2024). Thus, the rationalization of public spending is an essential factor of fiscal sustainability (Afonso and Alves, 2023) and the appropriate application of fiscal rules significantly reduces public spending (Vinturis, 2023).
- In the current context, governance can no longer be treated without taking integrity into account (Huberts, 2018) and regardless of the manifestation plan (national or local), government integrity must aim at: attention to integrity; clear definition of objectives, strategies, measures and responsibilities of those involved in integrity; for each manager, integrity must become a standard concern; the existence of a balance between rules/procedures/application and the degree of awareness of the implications of integrity; the existence of clear integrity monitoring policies; coherent establishment of measures, activities and functions to maintain and promote integrity; monitoring, evaluation and permanent adaptation of the integrity policy. (Hoekstra, Huberts and van Montfort, 2023).

The aspects analyzed in this article are often also found in the fundamental or specific laws of a country, given their direct or indirect impact on economic growth. Thus, at the level of Romania, the Constitution contains aspects regarding: the essential characteristics of the market economy, based on free initiative and competition, as well as the framework that the state must ensure; fundamental rights and freedoms; the guarantee for economic freedom, with reference to the free access of any person to economic activity and free initiative; the relationship between budgetary expenditures and sources of financing; (The Constitution of Romania, 2003).

The situation of the Economic Freedom, Government Integrity and Government Spending in Romania

Since 1995, Romania has been present in the world ranking of economic freedom, taking into account in whole or in part the 12 components of the Index of Economic Freedom (information is missing for judicial effectiveness and fiscal health in the period 1995-2016; information is missing for labor freedom in the period 1995-2004).

Three sub-factors are taken into account in determining the Government Integrity score (perception of corruption, risk of bribery, control of corruption), and for the Government Spending score, the burden imposed by government spending (average total public spending at all levels as a percentage of GDP for the most recent three years) is taken into account.

Romania's overall score for economic freedom, as well as the scores for Government Integrity and Government Spending, indicate a sinusoidal evolution, as can be seen in the following figure.

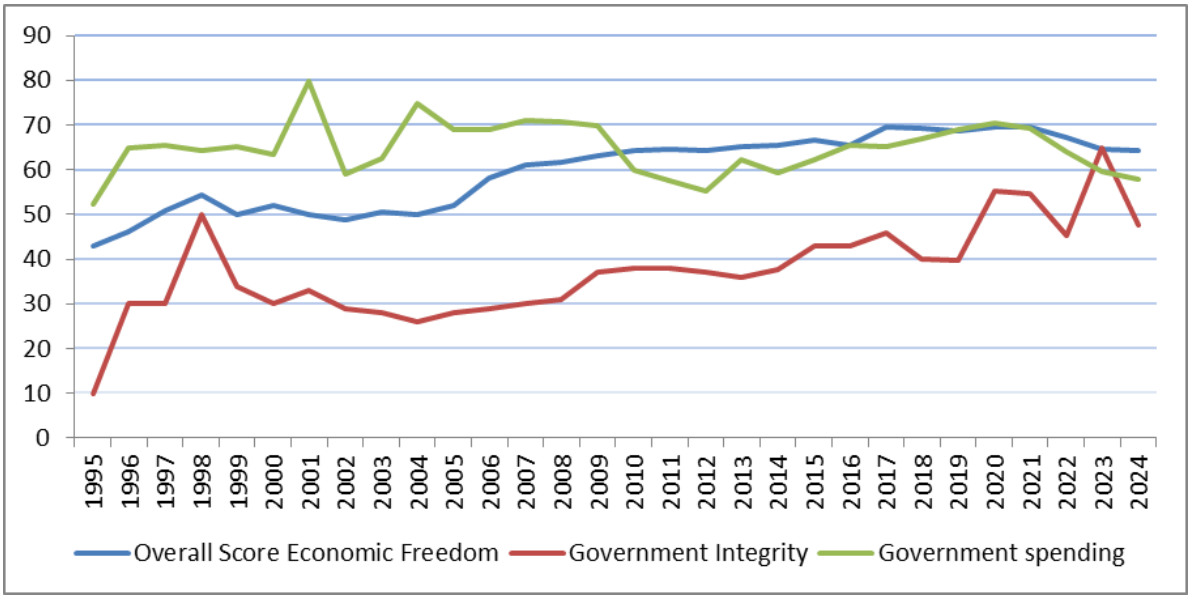

Fig. no. 1 Evolution of the Economic Freedom, Government Integrity and Government Spending in Romania, during the period 1995-2024

(Source: author processing after Heritage Foundation, 2024)

During the period 1995-2024, the overall score assigned for Economic Freedom in Romania indicates a significant increase from 42.9 in 1995 (considered repressed) to 64.4 in 2024 (considered moderately free), with the highest values in 2017 and 2020. For the same period, the score for Government Spending recorded the largest increases, being predominantly in the moderately free area, while the score for Government Integrity positions Romania predominantly in the repressed area.

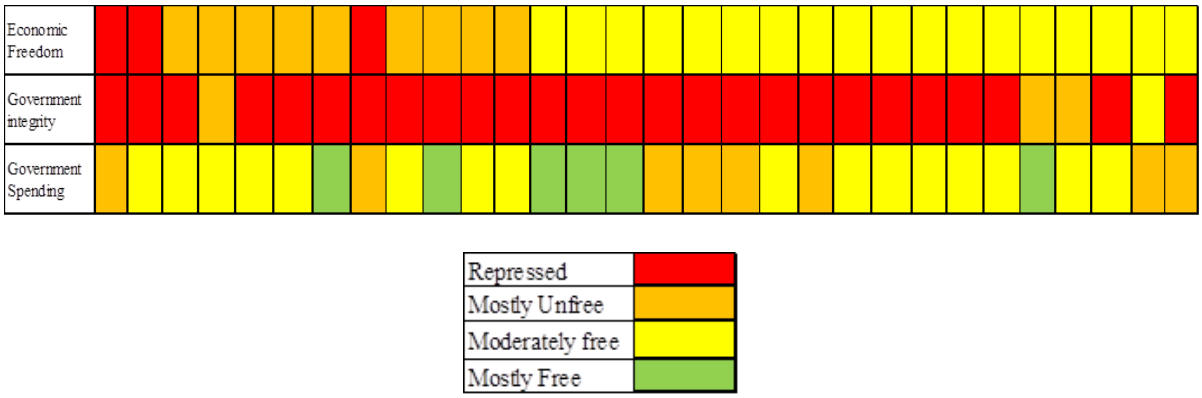

Fig. no. 2 Degree of freedom for Economic Freedom, Government Integrity and Government Spending in Romania, during 1995-2024

(Source: author processing after Heritage Foundation, 2024)

The positive impact of economic freedom is also visible in the correlation with Gross Domestic Product per capita in current prices (Statista, 2024), which for Romania indicates a moderate to good correlation, 72.04% of the variation in economic freedom being explained by the variation in GDP/capita.

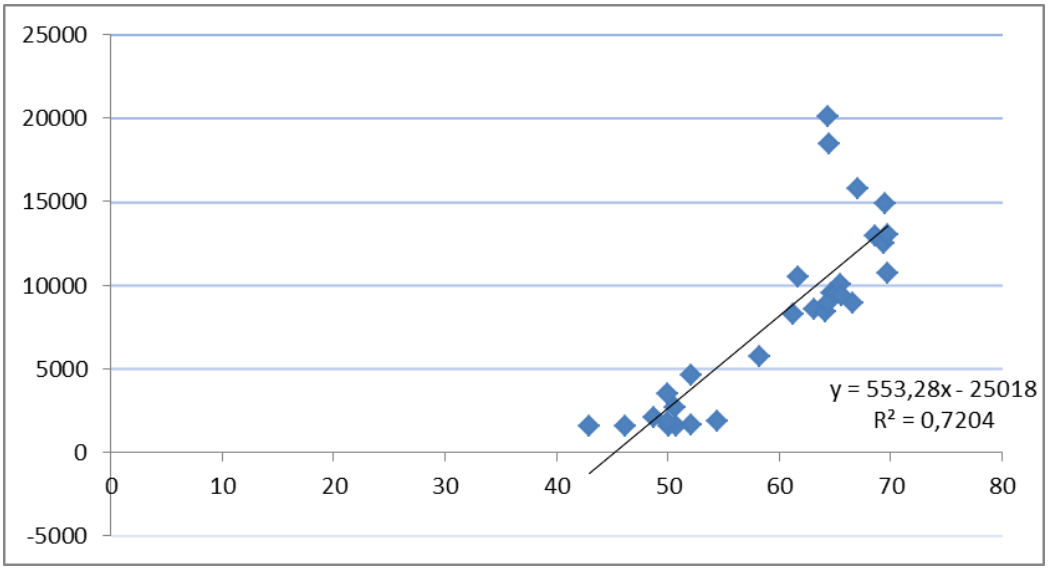

Fig. no. 3. Correlation between Economic Freedom and Gross domestic product per capita in current prices, for Romania, in the period 1995-2024
(Source: author's processing after: Heritage Foundation, 2024 and Statista, 2024)

Romania's situation in 2024 among the European states taken into account for determining the Fiscal Freedom Index (44 states, excluding Liechtenstein and Ukraine), indicates position 29 in Europe, with an overall economic freedom score of 64.4 (considered moderately free), very close to the European average, which was 67.2, surpassing EU member states such as Spain, France, Hungary, Italy and Greece.

The values recorded in Romania for the components of economic freedom indicate a perfectly positive, moderate to good correlation between Economic Freedom and Government Integrity and a random association (without correlation) between Economic Freedom and Government Spending, as can be seen from the following figures.

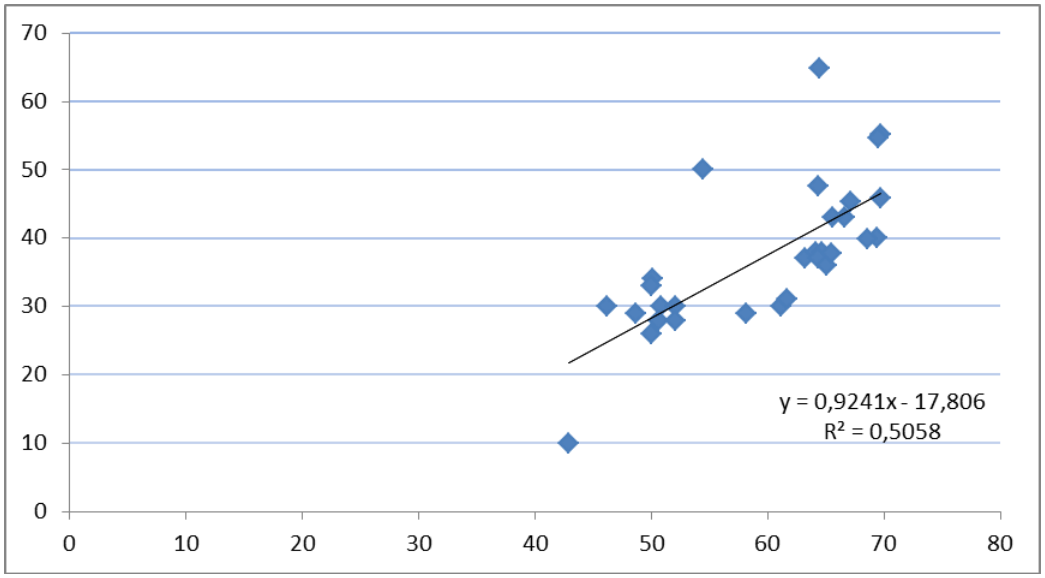

Fig. no. 4 Correlation between Economic Freedom and Government Integrity, for Romania, during 1995-2024
(Source: author processing after Heritage Foundation, 2024)

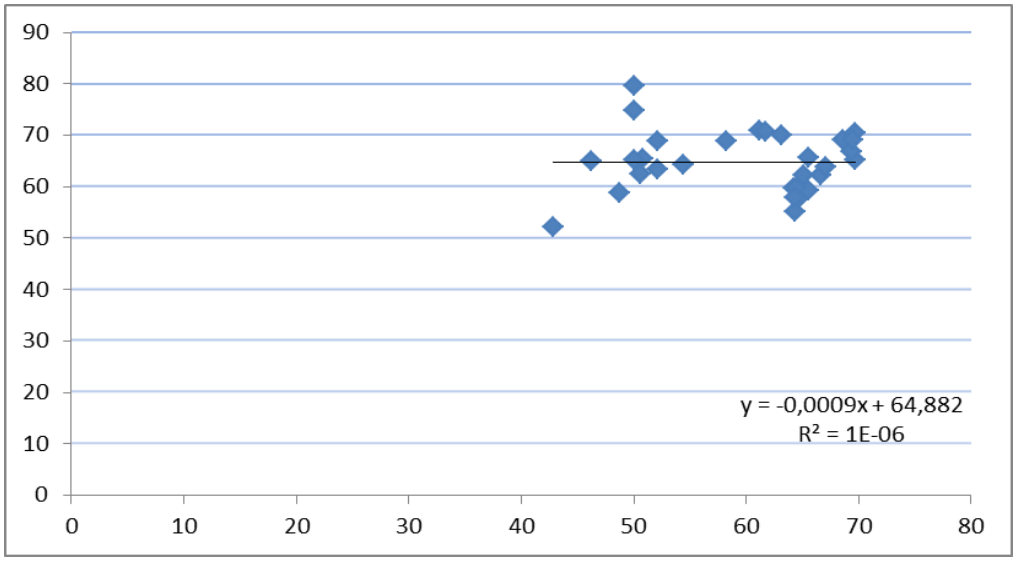

Fig. no. 5 Correlation between Economic Freedom and Government Spending, for Romania, during 1995-2024

(Source: author processing after Heritage Foundation, 2024)

At the level of the year 2024, from the Government Integrity perspective, the European average is in the moderately free zone (with an average score of 61.6), but Romania with a score of 47.6 - considered repressed, occupies the last positions among EU member states, along with Hungary and Bulgaria, at a very great distance from the top ranked states (Denmark, Norway, Finland and Sweden).

Regarding Government spending, in 2024, Romania, with a score of 58.0 (considered mostly unfree), exceeds the European average, which is in the repressed zone (with an average score of 41.4).

If the score for government integrity has a strong negative impact on the Rule of Law component, the score recorded for government spending, from the government size component, is much higher than the score recorded for fiscal health, as can be seen in the following figure.

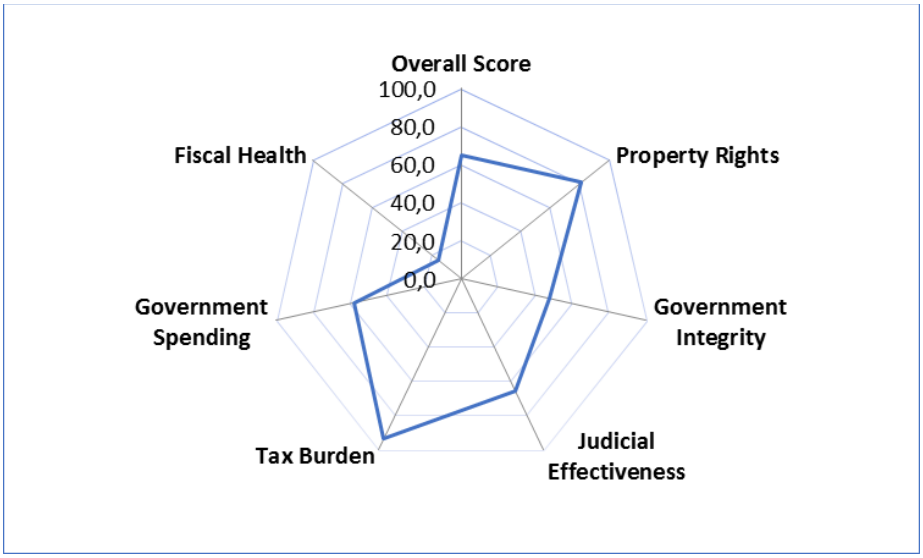

Fig. no. 6 Score for Rule of Law and Government Size, in Romania, in 2024

(Source: author processing after Heritage Foundation, 2024)

Even though, according to the scores recorded by Romania for government integrity and government spending in the period 1995-2024, there is no correlation, but only a random association (Pearson correlation coefficient, r = 0.024), we believe that by analyzing the subcomponents of these indicators, factors with direct or indirect influence can be identified, with a significant impact on economic freedom.

The deterioration of public finances in Romania in the recent period was mainly due to: strong procyclical fiscal incentives that increased the annual fiscal deficit; guarantees granted for loans and subsidies; the decrease in tax revenues; the increase in public spending as a result of the crisis triggered by the border war (Gröschl, 2024).

Increasing government spending above 30% of GDP (according to the Heritage Foundation methodology) negatively influences the economic freedom score, and a large budget deficit raises concerns about economic stability. The evolution of government gross debt as a percentage of GDP for the period 2007-2023 indicates significant increases for Romania, especially starting in 2020, reaching 58.14% in 2023 (OECD, 2023a).Financing public spending through debt or inefficiency can undermine fiscal stability and economic growth. A budget deficit estimated for 2024 at 8% of GDP (Szakacs and Ilie, 2024) far exceeds the European Union's recommended deficit of 3%, and even if part of the spending was aimed at improving living standards (energy subsidies, food subsidies, increases in public sector wages and pensions), allocative inefficiencies and dependence on loans raise major concerns.

Considering the enforcement of laws, the fight against corruption and the promotion of transparent governance, government integrity is an essential determinant of economic freedom. Romania has made significant steps in addressing corruption, through the efforts of institutions such as the National Anticorruption Directorate and through the directions of action included in the National Anticorruption Strategy 2021-2025. The OECD, through its 2023 analysis (OECD, 2023b), highlighted Romania's efforts to improve its integrity and anti-corruption measures (setting targets to improve transparency in public administration and reduce bribery and fraud; adopting integrity plans in public institutions; digitalizing public services), but also noted ongoing challenges, including the need for stronger political commitment and more effective integrity plans.

Despite its efforts, Romania still ranks low in terms of perceived government integrity. According to Transparency International's 2023 Corruption Perceptions Index, Romania obtained a score of 46 out of 100, ranking last in the EU, alongside Bulgaria and Hungary (Transparency International, 2023), highlighting aspects such as the influence of political interests on judicial independence, lack of accountability in public spending, and cases of nepotism in public sector employment.

The deficiencies found in terms of government integrity and government spending in Romania have direct implications for economic freedom, with reference to: (i) reduction/hesitation of foreign direct investment – the existence of a high level of corruption creates an uncertain business environment, discouraging long-term investments; (ii) administrative inefficiency – corrupt practices increase the cost and complexity of doing business, reducing competitiveness; (iii) the risk of increasing the tax burden – covering the budget deficit can be addressed by increasing taxes, which will lead to a possible reduction in the net profit and profitability of a business.

Conclusions

Since Romania, according to the Heritage Foundation's 2024 Index of Economic Freedom, reflects strong performance in areas such as property rights, tax burden, trade freedom, and investment freedom, it is necessary to consider the weaknesses/challenges for

government integrity and government spending that continue to affect overall economic freedom.

Because corruption remains a challenge at the national and regional levels, which limits Romania's development prospects and image in international environments, anti-corruption aspects must aim to prevent corruption, promote integrity at the level of each organization, increase the level of anti-corruption education, and fully recover the damages created by the commission of crimes (Government Decision, 2021).

A sound public finance sector guarantees appropriate management of public expenditure, which supports economic growth and promotes equity. In this regard, must be taken into account, elements such as: fiscal responsibilities; strengthening and improving public expenditure evaluation practices; performance-based public budgeting; improving budget execution practices; increasing the quality of national accounts; assessing and managing fiscal and budgetary risks; strengthening debt management operations (European Commission, 2024).

Without claiming to be an exhaustive approach, through this article we wish to emphasize that identifying opportunities for improvement in government integrity and government spending is essential for promoting a more solid and free economic environment.

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