

DYNAMICS OF INSOLVENCIES/REGISTRATIONS OF ENTITIES IN CORRELATION WITH WAGE COSTS

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Abstract

The paper aims to investigate the nature of the relationship between insolvencies or registrations and the wage cost in Romania. The study uses monthly / annual data covering the period 2014 - October 2019. In order to investigate the short and medium term dynamics of insolvencies, enrolments and the influence of wage costs, the data collected for the mentioned period will be examined, highlighting the causal links between the three concepts at the level of the country as well as in the field of constructions. This study highlights the existence of a relationship between the three variables, but it does not provide certainty regarding the information about the direction and meaning of this causal link. The subject deserves to be investigated from the perspective of the existence of a “long term equilibrium” property, for the pair of registration and insolvency variables.

The question we can answer by means of looking for actual relationships is whether there is a connection between the registrations and insolvencies of the entities in a certain field. The result of the study reflects a very similar evolution of the insolvency pairs - insolvencies in the field of construction, registrations - registrations in the field of construction, registrations - insolvencies.

Keywords

Registration of economic entities, insolvent economic entities, wage cost.

JEL Classification

E32, C33

Introduction

The entities constitute a very diverse, heterogeneous reality, characterized by dynamism and adaptability. The equilibrium state of an economy depends on the number and dynamics of the entities, but also on the ability to develop efficient activities. The entities operate on certain coordinates, determined by their distinctive

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characteristics, which relate to their size, the rate of establishment, but also to the insolvencies caused by their "natural selection". The efforts made in the direction of increasing the economic efficiency require the commensuration of the ratio between the effort made and the effect obtained using the value levers, such as the wage cost. Knowledge of all aspects of costs has been and continues to remain a concern of specialists, theorists and practitioners.

In a transition economy, such as the one in Romania undergoing consolidation, there are many factors and constraints in action, most of them being of a legislative nature, materialized in regulations regarding the salary among other aspects. In various fields of activity, there is an increasing involvement of the entities in the productive and construction activities, an indicator of the fact that these sectors have reached a good level of development, a certain balance, the growth in the construction field being significant. This is why I chose to analyze the dynamics of registrations and insolvencies in relation to all entities as well as those in the field of construction. A significant difference is that the entities in the field of construction cannot support the business from commercial loans as they do from other areas where they receive the money very quickly and the debts are paid at 30, 60 or 90 days' intervals.

The cost is an important instrument for the entity's management activity, used not only to inform about the activity carried out, but also to establish the strategic directions of action for the future. In construction, the labour cost is much higher than in other areas, such as retail. Statistics say that in construction, 70% represents cost with materials and 30% represents cost with labour. It is difficult to support past debt payments to suppliers and wage payments without accurate calculations. In the field of construction, the labour cost is the most difficult to manage and at the same time, the most pressing. The cost analysis of the entity is particularly relevant for the management and control activity, as it highlights both the use and capitalization of all categories of material, financial, human resources, as well as the impact of their allocation on the performance parameters of the economic entity.

Under the effect of increasing competition pressure, rapid technological changes and globalization of the economy, the cost calculation is a management tool with which the management of any enterprise will arm itself, to meet its information needs, to guide its decisions, but also to face the new challenges (Capron, 1994, p.29).

Competition is a concept that is closely related to the elements of the present study and it represents the most important characteristic of business behaviour in the economy. The free entry on the market and the free exit from the market, the development of the entity, concurrently with the dynamics of the purchasing power of consumers, makes competition a sure foundation of relations between entities. Competition motivates the entry and the registration on the market of the entities and it eliminates from the market the non-performing entities that have non-recoverable costs.

The entity accumulates a whole series of malfunctions that give rise to hidden costs. The permanent interaction between economic structures and human behaviours affects the competitiveness, profitability, efficiency and quality of the functioning of the entity.

In order to control these malfunctions, a whole set of participatory and synchronized actions are needed, which must refer to the whole entity and must be aimed at avoiding insolvency.

The mechanism of operation of the enterprise has a complex content, in which the intervention of the human factor has varied valences at the level of production and managerial. According to the socio-economic approach, the company is considered a complex body, characterized by structures and behaviours, having as functions the achievement of economic performances, but also social performances, by ensuring appropriate conditions in the workplace (Savall & Zardet, 2014, p.85).

1. Review of the scientific literature

Together with a brief review of the specialized literature - I wanted to outline the main theoretical problems related to the correlation of the minimum wage, the impact of raising the minimum wage in Romania, liquidations, registration of economic entities. All three concepts have an extremely pronounced relationship, of different nature, with the management of the entity. According to some authors, managerial accounting is a broader concept involving professional knowledge and skill in the preparation and especially in the presentation of the information necessary for the management at different hierarchical levels. The source of such information is represented by financial accounting and management cost accounting (Caraiani & Dumitrana, 2004).

Permanent interaction between different structures and human behaviours sometimes also creates dysfunctions (Savall & Zardet, 2005). The economic incidence of these dysfunctions needs to be evaluated, because the organization must react to these dysfunctions, by identifying the causes and by means of establishing corrective actions and measures that will involve certain costs.

The correct identification of costs focuses on the work component and the production component. An important concept in the analyzed topic is that of hidden wage cost. A cost is called hidden if it does not explicitly appear in the entity's information systems; similarly, we will say that a cost is visible if it is detected. The visible costs, although they allow the quantification of the results and of the deviations, do not allow an analysis of all the causes at the origin of the phenomenon. The hidden costs are related to the quality of the functioning of an entity and by their non-detection, they are the first ones that trigger the malfunctions, while their intensity reduces the liquidity of the entity leading to insolvency.

The socio-economic theory of the entities emphasizes the quality of the functioning of the entity as well as their capacity to manage their material, physical, monetary and human resources. This approach allows highlighting the malfunctions that constantly disturb the situation of an entity, which will prevent the achievement of the goals and which, unless they are stopped, will result in insolvency. In this case, the economic incidence of these dysfunctions must be evaluated. The entity must react through certain corrective actions, which will entail certain costs. These costs may refer to additional

wage expenses, which go beyond the established strategy and remove the entity from the intrinsic economic balance.

At the level of business people, competition is seen as a battle between the entities for the market share. Access to a market, obtaining a market segment and development are the major objectives of competitive marketing.

Entities must find the best solutions, the best way forward to achieve their goals, first of all to ensure and protect their profits, within a competitive environment. The entity is vulnerable to offensives of other competitors. Economic analyses and predictions take into account the existence of certain barriers to accessing certain markets, especially in terms of costs, but also of permanent change in the intensity of competition, barriers that often cause the cessation of activity. The most complete analysis of these problems can be found in two papers, one written by Michael Porter in 1998, entitled “Competitive Advantage: Creating and Sustaining Superior Performance”, and the other written by Gerry Johnson and Kevan Scholes in 1984, with the title “Exploring company strategy”.

The entity is regarded as a form of organization of an economic activity, autonomous from a patrimonial perspective and also authorized, according to the legislation in force, while carrying out commercial activities in order to develop the activity and to obtain profit in competitive conditions. In an economy where microenterprises account for the most, long-term business is a real challenge. Insufficient capitalization is one of the reasons why most entities fail. One reason for the financial blockage is the excessive use of the commercial credits, not receiving invoices in an optimal term leading to the blocking of the activity. Many of the insolvent entities, beyond the financial blockade, do not have well-defined investment plans, with risk strategies, and if they have them, they do not take into account the realities of the economy.

Insolvency should be seen as a solution to remove some of the problems that are inherent in the business environment. Insolvency can ensure the elimination of debtors in a situation that is permanently compromised in order to prevent their insolvency status from contaminating the business environment and causing other bankruptcies, job losses etc. Another reason why entities fail to meet the economic challenges is represented by difficult access to bank financing and harsh credit conditions. The financial behaviour of investors is a factor that intervenes in the balance of registrations and insolvencies, given that there are many who direct their activity following their flair or impulse, while disregarding economic considerations.

The results of the economic researches that are done on the gross minimum wage in different countries are mixed, in the sense that some show the negative impact of the increase of the minimum wage on the employment, meaning that it generates unemployment, while others show that there is no effect or, on the contrary, a positive effect may even occur if the minimum wage is increased. Other research, more rigorously done, focuses on the correlation between the increase of the minimum wage and the profitability of companies. We can say that there are no identical situations in two different countries. Also, in the absence of any measurement, we do not know

exactly the correlation between the number of new jobs actually created in the economy and that of jobs which disappear due to insolvencies.

2. Research methodology

The variables we used in this study are the following: entity registrations, construction registrations, insolvency professionals, insolvency professionals in the construction field. The main source of data is the National Institute of Statistics.

The main purpose of the study was to investigate the nature of the relationship, the number of registrations and the number of insolvencies, but also to identify any possible direction of causality between them.

I used quantitative methods in order to identify extensive knowledge of the case, using detailed data and theoretical principles. Data collection consisted in centralizing statistics. Using the inductive method, the particular situations were analyzed by individual study of the facts through which general conclusions were formulated, which helped to discover some generalized themes and aspects that are based on the systematic observation of reality. Over 61,000 entities have gone into insolvency over the past 6 years due to insufficient financial resources, wrong investments and lack of a risk strategy based on the realities of the economy. Business failure can occur in the case of entities that are in a risky situation, many of them immediately closing the activity.

The ratio between the insolvent entities and the newly registered entities decreased significantly during the period under analysis, 2014 - October 2019. The dynamics of insolvencies and entity registrations is influenced negatively by costs when they are too high, but in a positive way, motivating towards the start of new businesses when there is hope for reasonable costs. Beyond the evolution of the two variables analysed from the perspective of the number of entities, there are significant aspects related to the number of employees coming from the entities facing insolvency, which is not always absorbed by the hires within the new entities. Another limitation of the research is that there is no comparison of the turnover of the two categories of entities.

3. Results and discussion

The evolution of registrations and insolvencies differs significantly depending on the sector of activity. This is why we analyzed the evolution of variables for the construction field. In this study, we analyzed data regarding the insolvencies as well as the registrations at national level and in the field of construction.

The centralization by year of these data is in the table no. 1.

Table no. 1. Dynamics of registrations and insolvencies of economic entities between 2014 and 2019

The year	Registrations	Percentage	Dynamic	Insolvencies	Percentage	Dynamic
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2014	101627			20696		
2015	113167	11,36%	↑	10269	-50,38%	↓
2016	105982	-6,35%	↓	8371	-18,48%	↓
2017	136699	28,98%	↑	9102	8,73%	↑
2018	135532	-0,85%	↓	8304	-8,77%	↓
Oct 2019	116820	-13,81%	↓	5170	-37,74%	↓

Source: National Trade Register Office-Romania - own processing

There are 15,193 more entities registered in 2019 compared to 2014 and 15,526 fewer entities in insolvency. During the analysed period, 2014 - Oct 2019, according to the official data announced by the Trade Register, the analysis reveals a decrease in 2015 as compared to the previous year by 50.38% of the insolvencies. The years 2016 and 2019 come with the reduction of the number of registrations of entities but at the same time, we observe the reduction of the number of insolvencies, which attenuates the first aspect, a negative one if evaluated individually. A decrease in the number of registrations would be a signal of a decrease in the appetite for investments, as a result of the worsening conditions in the real economy, heavily exacerbated by the financial bottleneck and lack of funding especially if it were doubled by massive insolvencies.

Costs influence the process of economic-financial decision making through several relationships, the most significant being the cost-price relationship, the cost-profit relationship, the cost-economic efficiency relationship and others. In the economic-financial analysis, an important component is the wage cost, a component that can significantly change the fate of an entity. That is why we have highlighted aspects such as the importance, the necessity, the role of this cost. In general terms, the wage cost represents in a monetary expression the human resources consumption occasioned by the achievements of the entity, products and services. The wage cost represents the essence of the entity's economic-financial strategy, because, in concrete terms, it largely reflects the way in which the competitive capacity is sustained. The decisive role of the wage costs also derives from the fact that reducing the volume and optimizing their structure, together with the increase of prices through quality, remain a safe way for the entity to obtain the expected profit without risking insolvency. Direct competition between entities on the same market also generates indirect competition through costs, the balance being inclined on the part of those with lower costs.

The increase of the minimum wage directly influences the salaries of at least 22% of the employees from the private sector in Romania. The indirect effects are the increase of the salaries of the employees with the wage remuneration above the minimum

threshold. The most vulnerable are small and medium-sized entities. The pressure is higher for the entities in the construction field, as more than 40% of the employees were at the minimum threshold of the economy, pressure further accentuated by the 2019 legislative change regarding the increase of the construction wages. Minimum wage increase exerts negative effects on the employees and even on the liquidity of the entity. The higher the threshold, the more difficult it is to cross the barrier towards the labour market from two points of view: the mismatches between supply and demand on the labour market and the insolvency of many entities. The increase in productivity over the last five years in Romania is four times lower than the increase in the wage cost per employee. According to the data compiled by the National Institute of Statistics, the cost of an employee's salary has increased by about 42% in the last four years. In the ratio of GDP growth over the same period of only 21%, the pace is double. A simple calculation shows that an investment will be discouraged because the high state taxes for an employee are not offset against the actual output or the efficiency with which the investment is rewarded. Basically the rate of return does not compensate the actual cost of an employee. The evolution of wages during the analyzed period was reflected in an increase in purchasing power in the short term, and for entities in increasing costs, which made many entities no longer able to meet obligations and go into insolvency. The evolution of wages from 2014-2019 can be found in the Figure 1.

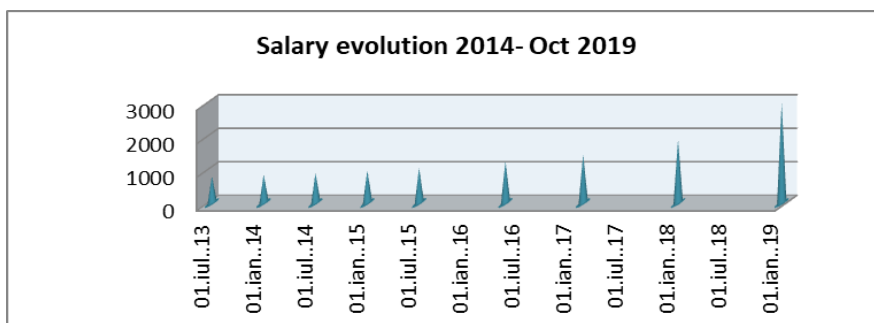


Figure no. 1: Salary evolution in the period 2014- Oct. 2019

Source: National Institute of Statistics –Romania- own processing

The labour force plays a major role in the functioning of an economy and represents a cost (the cost of labour) that includes not only actual remuneration, but also social contributions. The opportunity of salary increases becomes problematic, if the discussion focuses on equity, without taking into account the effect of the labour cost on the profitability of the entities.

So, what do we take into consideration when setting the gross minimum wage on the economy? Is it economic indicators, social indicators or a mix between these indicators? If we consider a mix of indicators, what would they be, so that we can measure the effects as accurately as possible?

Following the centralization of the data made available by the National Trade Register Office in Romania, we analyzed the annual dynamics of the respective registrations of the insolvencies of the entities during the period January 2014 - October 2019.

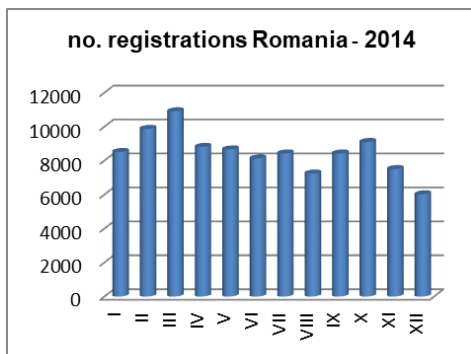


Figure no 2: Entities registrations
 Source: National Trade Register Office-Romania - own processing

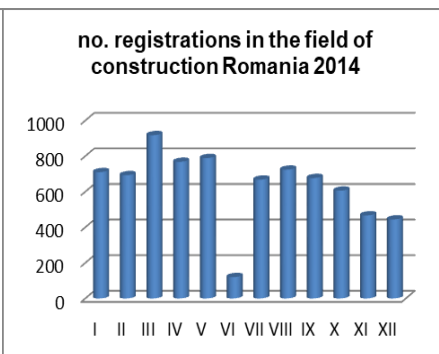
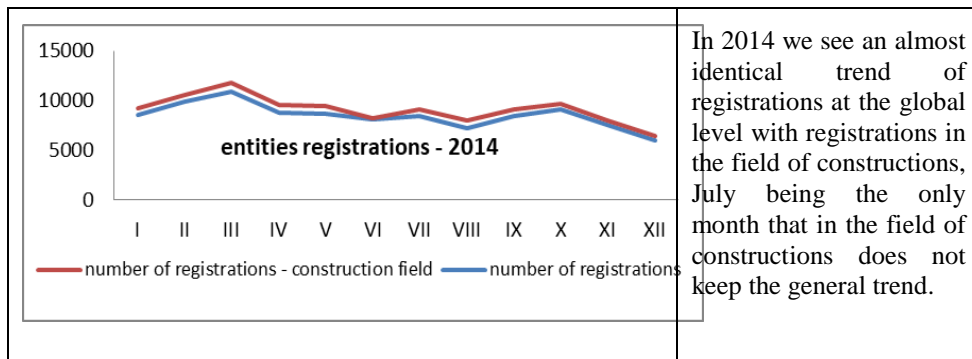


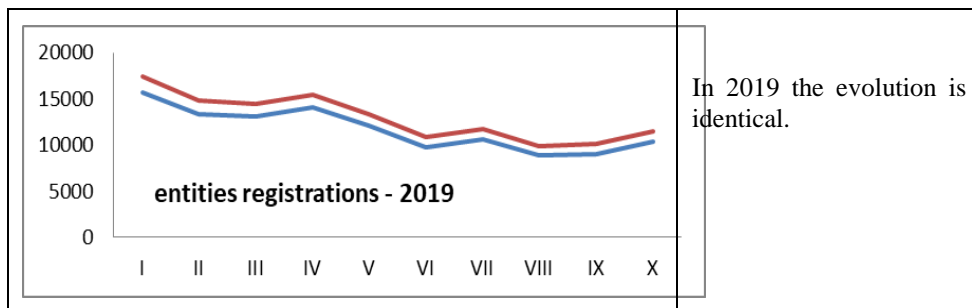
Figure no 3 Entities registrations in the field of construction Romania 2014
 Source: National Trade Register Office-Romania - own processing

Tabel no 2. Evolution of the registrations of entities at general level and in the field of construction (Monthly evolution)



In 2014 we see an almost identical trend of registrations at the global level with registrations in the field of constructions, July being the only month that in the field of constructions does not keep the general trend.

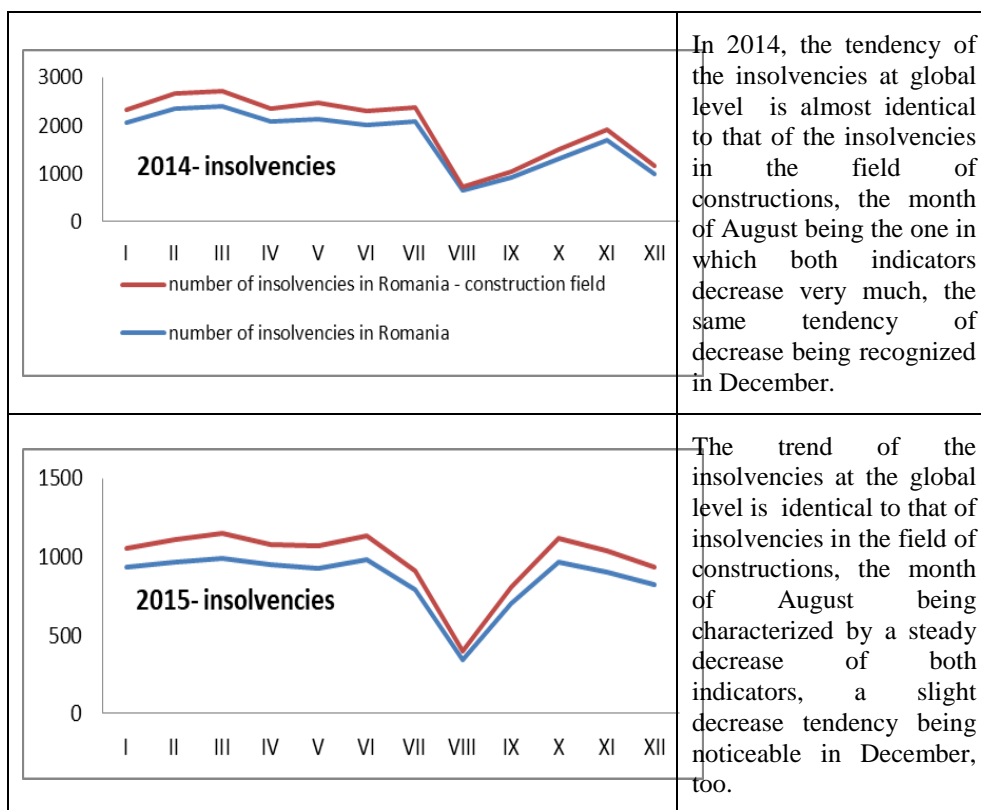
<p>entities registration - 2015</p>	<p>The year 2015 comes with an identical evolution of the global registrations respectively in the field of construction.</p>
<p>entities registrations - 2016</p>	<p>In 2016 we observe a trend of the registrations at the global level that is almost identical to that of the registrations in the field of constructions, August being the only month that in the field of constructions does not keep the general trend.</p>
<p>entities registrations - 2017</p>	<p>The year 2017, with the exception of January, comes with similar evolutions of global registrations as well as registrations in the field of construction</p>
<p>entities registrations - 2018</p>	<p>In 2018 the evolution is identical.</p>



In 2019 the evolution is identical.

Source: National Trade Register Office-Romania - own processing

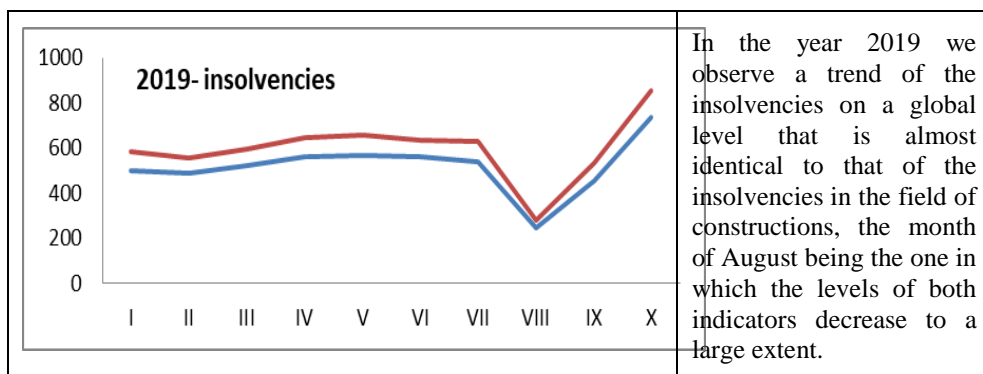
Tabel no 3. The evolution of insolvencies of entities at general level and in the field of construction (Monthly evolution)



In 2014, the tendency of the insolvencies at global level is almost identical to that of the insolvencies in the field of constructions, the month of August being the one in which both indicators decrease very much, the same tendency of decrease being recognized in December.

The trend of the insolvencies at the global level is identical to that of insolvencies in the field of constructions, the month of August being characterized by a steady decrease of both indicators, a slight decrease tendency being noticeable in December, too.

<p>2016- insolvencies</p> <table border="1"> <caption>Estimated data for 2016- insolvencies</caption> <thead> <tr> <th>Month</th> <th>Red Line</th> <th>Blue Line</th> </tr> </thead> <tbody> <tr><td>I</td><td>750</td><td>650</td></tr> <tr><td>II</td><td>900</td><td>800</td></tr> <tr><td>III</td><td>950</td><td>850</td></tr> <tr><td>IV</td><td>800</td><td>700</td></tr> <tr><td>V</td><td>820</td><td>720</td></tr> <tr><td>VI</td><td>850</td><td>750</td></tr> <tr><td>VII</td><td>700</td><td>600</td></tr> <tr><td>VIII</td><td>450</td><td>400</td></tr> <tr><td>IX</td><td>600</td><td>500</td></tr> <tr><td>X</td><td>900</td><td>800</td></tr> <tr><td>XI</td><td>1050</td><td>900</td></tr> <tr><td>XII</td><td>800</td><td>700</td></tr> </tbody> </table>	Month	Red Line	Blue Line	I	750	650	II	900	800	III	950	850	IV	800	700	V	820	720	VI	850	750	VII	700	600	VIII	450	400	IX	600	500	X	900	800	XI	1050	900	XII	800	700	<p>This month is the one in which the level of both indicators decreases very much, the same tendency of decreasing existing in December.</p>
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Source: National Trade Register Office-Romania - own processing

The evolution of the pairs entities registration,- entities construction, insolvency entities - insolvency entities construction can be seen in the figures no 4, 5 reflecting a statistical relationship between the two series of two random variables.

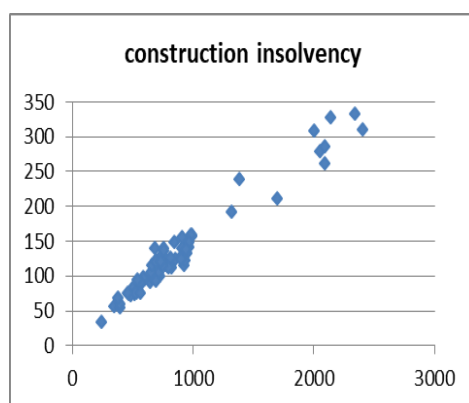


Figure no 4 Insolvency correlation

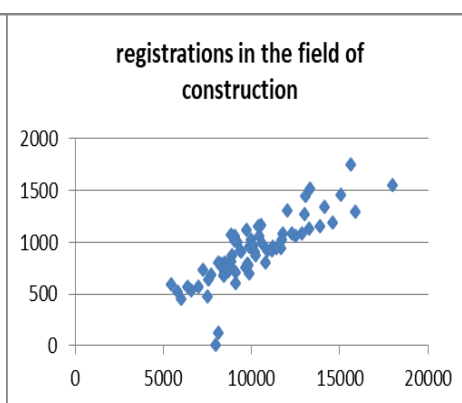


Figure no 5 Correlation of company registrations

Source: National Trade Register Office-Romania - own processing

Analyzing the correlation on each pair, we observe a wide class of relationships that involve the dependence between the indicators of each pair. The study of the dependence between each two variables in figures no. 4, 5 assumes that each of them is likely to be affected by a random scattering, applying the correlation analysis method. This correlation analysis takes into account the average behaviour of each variable according to the values of the other variable. The two variables appear as sets of points, each variable being located on one axis, observed within a common phenomenon.

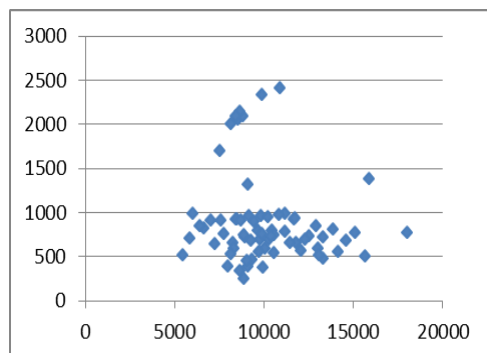


Figure no 6 Correlation between insolvency and registration

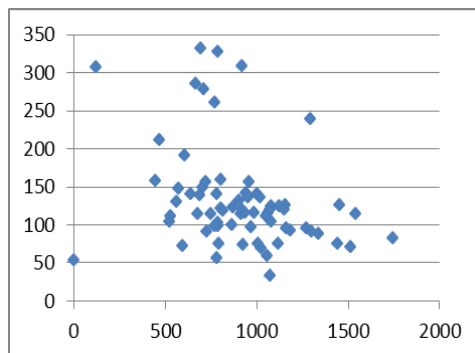


Figure no 7 The correlation between insolvency and registration in the field of construction

Source: National Trade Register Office-Romania - own processing

Thus the close connection between variables is observed. Depending on the dispersion of the points with the coordinates on the diagram, I appreciate that the type of correlation existing between the categories is a positive one because the modification of one of the variables is associated with the same type of modification of the other variables. We distinguish an increasing trend of registrations at the global level, the insolvencies having approximately constant values (figure 6). In the field of constructions, we observe that the slightly increasing evolution of registrations is complemented by the approximately constant number of insolvencies.

Conclusions

The competitive economy creates an intrinsic balance, eliminating the entities that generate loss. The workforce plays a major role in the functioning of an entity, from its perspective representing a cost. Thus, the cost determined by the labour force is a determining factor for the competitiveness of the entities.

The results of the analysis reflect a negative and statistically significant effect of the wage cost on the insolvencies.

We presented the evolution of registrations and insolvencies during the period 2014 - October 2019 and noticed that the phenomenon of insolvency decreased steadily and significantly during the period analyzed by 70%. The reasons identified are of legislative nature (the amendments no longer allow insolvency to avoid paying debts) and they are related to a healthy business environment. Thus, entities with problems, but which are also viable, are trying to recover and reintegrate into the economic circuit.

Within this article, a personal contribution of the author was materialized in the elaboration of a case study regarding the dynamic evolution of the registrations and insolvencies of entities at the level of the National Trade Register Office in Romania. Following the research conducted, the predetermined research hypothesis according to which "the entities in the field of construction follow the general trend regarding the insolvencies and registrations of entities in Romania, in the period 2014-2019" was confirmed.

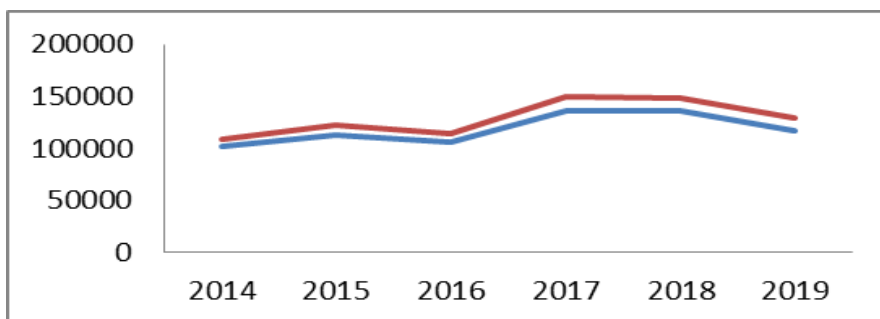


Figure no 8 Annual evolution of registrations of entities at general level and in the field of construction (2014 – 2019)

Source: National Trade Register Office-Romania - own processing

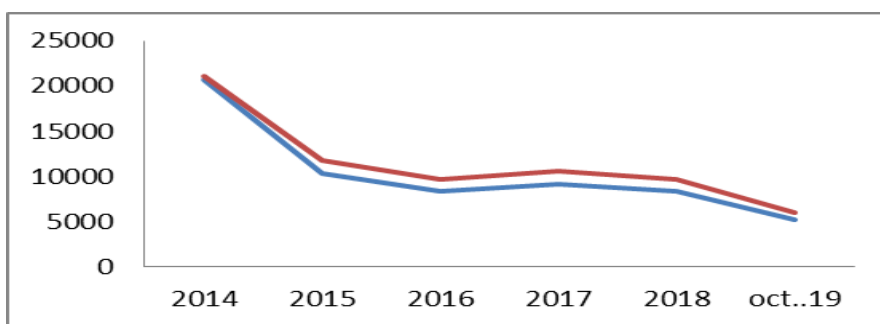


Figure no 9 Annual evolution of insolvencies of entities at general level and in the field of construction (2014 – 2019)

Source: National Trade Register Office-Romania - own processing

According to figure 8, the evolution of the registrations of entities at general level and of those in the field of construction, between 2014 and October 2019, are both identical, having a downward trend, the same thing being observed for the evolution of insolvencies. Following the comparison between insolvency and registration there is a two-way relationship since each situation may be the result of the other, all within a free self-regulation on the market. The inversely proportional relationship between the two

variables demonstrates a greater stability given by the perspective of the decrease in the number of insolvencies and that of the slight increase of the registration of new entities.

Even if the diagrams show a connection, one does not have to conclude that one of the variables is caused by the other. It may be the case that both variables and both pairs of variables presented in the figures 8, 9 are influenced by other variables.

Against the background of an uncertain economic situation and, unfortunately, with a visible negative trend, the Romanian business environment has tried to adjust the usual mechanisms necessary to preserve the business and, why not, to protect those involved in its development, including employees. The dynamics reflected in this study demonstrate the advantages of price stability in terms of total costs, in which the largest share is in wage costs. This contributes to raising the standard of living, reducing the uncertainty about the general evolution of prices and, consequently, improving the transparency of the pricing mechanism.

Beyond this study, it would be important to evaluate the calibre of insolvent companies, from the perspective of the financial loss caused to the creditors and the social dimension through the lost jobs (Guda I., 2018, p.6).

We have noticed that the real dynamics of labour productivity is repeatedly lower compared to the real dynamics of labour costs, the gap being quite large, which contributes to the elimination of many entities that cannot support this difference on the market.

From the study, it is observed that in the short and medium term, any increase in the gross minimum wage has a negative effect on the entities and it is reflected in an intensification of the insolvencies. All the ideas extracted lead to the conclusion that, given the way the minimum gross wage is fixed in the economy, the insolvency risk created in the case of wage increases should also be taken into account.

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