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Romania: Difficult Adjustment to the Financial Crisis



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An Intelligence Assessment

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July 1986

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Romania: Difficult Adjustment to the Financial Crisis



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An Intelligence Assessment

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**Romania: Difficult Adjustment
to the Financial Crisis** [redacted]

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Key Judgments*Information available
as of 15 June 1986
was used in this report.*

President Ceausescu's obsession with paying Romania's foreign debt has exacted a heavy toll from the economy and population, but his policies offer little hope for recovery in the foreseeable future. Misplaced priorities and excessive demands have drained the economy, leaving Bucharest still dependent on foreign creditors and more vulnerable to Soviet enticements. These problems do not appear to threaten Ceausescu's control, nor are they likely to force him to abandon his maverick stance vis-a-vis the USSR and Warsaw Pact, which has served US interests for the past two decades. But the departure of Ceausescu, who is 68 years old and rumored in ill health, and the transition to a successor regime struggling to establish itself and cope with a seriously weakened economy could open Romania to increased outside influence—from either the East or the West. Western policy toward a post-Ceausescu regime could be critical in shaping the new leadership's foreign policy course and the thrust of its economic policy.

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Romania's current economic dilemma has its roots in Ceausescu's reaction to the debt reschedulings of 1982-83. Humiliated by having to accept Western creditors' terms in return for debt relief, Ceausescu opted for rapid debt repayment to eliminate foreign interference with his policy prerogatives. But, as efforts to expand export earnings have failed, the regime has resorted to ever deeper cuts in imports and consumer welfare to generate the required trade surpluses and protect the country's industrialization drive through high levels of investment. Ceausescu's adjustment priorities have differed sharply from those of other East European countries, which, for fear of popular discontent, have given greater priority to protecting consumer welfare and less priority to investment and trade surpluses.


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The financial recovery that Ceausescu hoped to buy with this painful strategy has been short lived. Although Bucharest cut its debt by 35 percent during the period 1982-85, the economy probably will be unable to sustain trade surpluses sufficient to meet debt service obligations in 1986-88. After getting through 1984 without financial assistance, Bucharest had to borrow \$150 million in 1985 when a hard winter in the face of virtually no energy and raw material reserves disrupted economic and trade performance. The Romanians already have requested a rescheduling of \$260 million due this year to banks on the 1982 rescheduling agreement, and we think they will need more relief to help cover the expected financing gap of at least \$500 million.


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The terms and amounts of financial help obtained for 1986-88 will determine to a large extent whether Bucharest can make any progress toward financial recovery. A multiyear rescheduling of much of the \$2.8 billion in principal owed to banks in these years appears to offer the best prospect for a more balanced adjustment. But arranging a multiyear debt rescheduling would encounter several obstacles, not the least of which is Ceausescu's opposition to International Monetary Fund (IMF) supervision. Bucharest may well continue to push for large export gains and to request only small amounts of debt relief—an approach that would not ease the strain on the economy. Although the direct US role in commercial debt rescheduling is small, US views could be influential in setting the terms should Romania request a rescheduling of its debt to Western governments. 

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Romania is likely to hold to its present economic policies and priorities for the foreseeable future. Ceausescu maintains his intransigent opposition to any diminution in his personal control over decisionmaking or to any faltering in his drive to industrialize Romania and eliminate the country's debt. We believe the result is likely to be continued economic stagnation and grinding austerity. In our view, intimidation by the omnipresent security apparatus will probably keep popular protest in check. 

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Continued large financing gaps or a possible succession to Ceausescu, however, could produce major policy changes. A return to some type of IMF supervision or monitoring would seem the most likely departure from current policy in the near term if Bucharest concludes it has little alternative in the face of worsening financial problems. IMF guidance would probably have little impact on Romania's economic situation under a Ceausescu-led regime determined to minimize compliance. Fund measures to improve efficiency and balance Romania's economic resources with its needs could yield improvement under a successor regime committed to more rational economic policies. Alternatively, Bucharest might make political concessions to the USSR in return for economic assistance, but this seems more likely under a successor regime than under Ceausescu.



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Romania: Difficult Adjustment to the Financial Crisis

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Introduction

Since Romania slid into arrears in 1981, the foreign debt problem has shaped the country's economic policy and performance. Embarrassed by the need to request debt relief from creditors and take policy guidance from the International Monetary Fund (IMF), President Ceausescu resolved to pay Romania's hard currency debt by the end of the decade. To this end, Romania has moved its trade balance from large deficits to large surpluses through deep cuts in imports and a drive to expand exports. This has required domestic austerity that has deteriorated into draconian stringency and raised doubts about the economy's long-term prospects.

This paper will discuss the regime's adjustment strategy and its impact upon trade, economic performance, investment, and consumer welfare. It will examine the prospects for financial recovery, economic growth, popular welfare, and a closer economic relationship with the USSR. In considering Romania's economic outlook, the paper will assess alternative strategies that the current regime or a successor regime could adopt and their implications for the United States.

The Causes of the Debt Buildup

The roots of Romania's financial problems lie in Ceausescu's effort to transform the country into a modern, industrial power. His program of rapid industrialization launched in the early 1970s was built on costly imports of Western machinery and equipment. These required increased imports of raw materials and energy to cover the gap between the country's expanded industrial capacity and limited resource base (table 1). Romania's highly centralized and bureaucratic economic system compounded the problem by fostering inefficiency and poor competitiveness. The quality of many manufactured goods was

Table 1 *Thousand metric tons*
**Selected Imports of Raw Materials,
1970 and 1980**

	1970	1980
Apatite	317.0 ^a	896.0 ^a
Bauxite and aluminum oxides	190.2 ^b	23,327.0 ^c
Coking coal	685.3 ^a	2,557.0 ^a
Copper	15.2 ^b	43.8 ^d
Ginned cotton, fiber, and yarns	106.4 ^a	140.7 ^a
Iron ore	6,267.8 ^a	15,984.0 ^a
Lead	0.1 ^b	19.9 ^d
Magnesium	0.4 ^b	0.5 ^c
Manganese ores	0 ^b	216.0 ^c
Nickel	2.0 ^b	2.0 ^c
Tin	2.6 ^b	20.5 ^d
Zinc	1.4 ^b	20.5 ^d

^a *Anuarul Statistic al Republicii Socialiste Romania*, Bucharest, 1981.

^b *Comertul Exterior al Republicii Socialiste Romania*, Bucharest, 1973.

^c US Bureau of Mines, *Minerals Yearbook*, 1982.

^d *Economic Memorandum*, Bucharest, 1982.

inferior to Western products, a serious problem for a country that needed gains in exports to cover its rising need for imported energy and materials.

The most serious consequence of the industrialization program was the rapid increase in Romania's dependence on imported oil. Formerly self-sufficient in oil and natural gas and a net exporter of both, Romania in the 1960s began to develop an industrial base heavily weighted toward oil refining and petrochemicals production. Bucharest expanded its refining capacity even as mismanagement of oil and gas reserves

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Table 2 *Thousand barrels per day*
The Oil Trade, 1976-84

	Crude Oil Imports	Refined Products Exports	Net Imports
1976	170	159	10
1977	177	137	40
1978	259	153	106
1979	286	150	136
1980	320	178	142
1981	254	165	94
1982	218	133	86
1983	248	185	63
1984	269	212	57

Sources: Derived from data in *Anuarul Statistic al Republicii Socialiste Romania*, various years.

led to declining production. Oil production peaked at 308,000 barrels per day (b/d) in 1976 and fell to 242,000 b/d by 1980. To feed a refining industry with a capacity estimated at 600,000 to 700,000 b/d, Bucharest increased crude oil imports to 320,000 b/d in 1980, almost twice the 1976 level (table 2). The sharp rise in imports, coupled with reduced profits per barrel from refined products, turned Romania's small oil trade surplus of 1976 into a \$1.5 billion deficit by 1980 (tables 3 and 4). Romania was hard hit by the runup in world oil prices in the late 1970s because, unlike most other East European countries, Bucharest received little subsidized oil from the USSR. [redacted]

Bucharest's deliberate neglect of agriculture for the sake of industrialization also damaged Romania's hard currency trade. Meager investment in agriculture—which received less than 15 percent of total investment in the 1970s—limited gains in output. Increases in crop production did not keep up with expansion of livestock herds, and, as a result, Bucharest had to increase feed imports sixfold over the decade. Hard currency outlays for agricultural items rose from \$488 million in 1975 to over \$1.1 billion by

Table 3 *US \$ per ton*
Price Differential Between Crude Oil Imports and Oil Products Exports, 1971-84

Year	Price Differential ^a
1971	13.83
1972	10.37
1973	30.22
1974	-13.44
1975	8.51
1976	9.14
1977	3.08
1978	4.49
1979	NA
1980	29.00
1981	10.02
1982	25.78
1983	26.65
1984	26.67

^a Defined as revenues from oil products net of outlays for crude oil purchases.

Sources: Derived from data in *Economic Memorandum*, 1982, 1983, 1984, 1985, and partner country trade data.

1980. This increase together with a decline in earnings from agricultural exports turned Romania's balance on agricultural trade from a peak surplus of \$190 million in 1977 to a \$231 million deficit by 1980. [redacted]

Rising deficits in oil and agricultural trade coupled with weak growth of manufactured exports pushed Romania's hard currency trade balance into the red in the late 1970s. The trade balance shifted from a small surplus in 1976 to a \$1.6 billion deficit by 1980, and the current account deficit rose from \$61 million to \$2.4 billion over this period. Bucharest financed these deficits with readily available hard currency credits; by 1981 Romania's debt had mounted to \$10.2 billion, nearly three times the 1977 level (figure 1). The

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Table 4
Value of Petroleum and Petroleum
Products in Convertible Currency Trade

Billion US \$

	Exports		Imports	
	Petroleum Products	Total Exports	Crude Oil	Total Imports
1976	0.7	3.4	0.7	3.3
1977	0.7	3.7	0.9	3.8
1978	0.7	4.1	1.2	4.6
1979	1.7	5.5	2.1	6.6
1980	2.2	6.5	3.7	8.0
1981	1.9	7.2	3.4	7.0
1982	1.5	6.2	2.5	4.7
1983	2.0	6.2	2.5	4.6
1984	2.2	6.9	2.6	4.7

Source: *Economic Memorandum*, 1983, 1984, 1985.

Romanians relied heavily on short-term borrowings that left them particularly vulnerable to liquidity problems when Western banks, alarmed over the Polish debt crisis, began to withdraw credit lines from Eastern Europe.

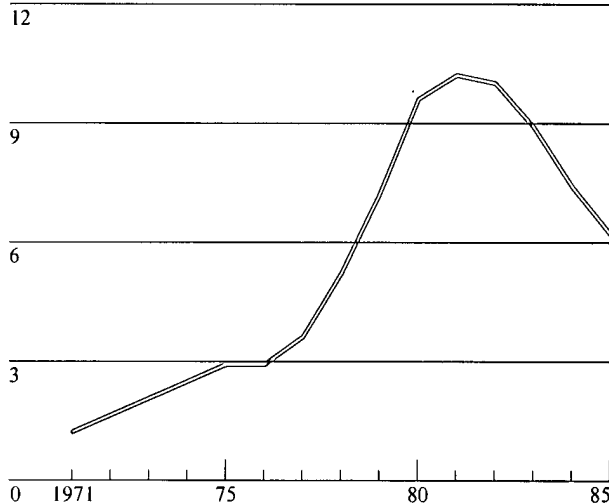
Financial Crisis

In early 1981 Romania negotiated a three-year standby credit and stabilization program with the IMF in hopes of reassuring bankers that Romania was bringing its balance-of-payments problems under control. But the bankers were not reassured and, by late 1981, the loss of credit lines had trapped Bucharest in a serious liquidity crisis with unpaid obligations mounting. With arrears a violation of the IMF charter, the Fund suspended drawings under the standby only a few months into the program.

Realizing that Bucharest's relations with foreign creditors had sunk so low that bankers were unlikely to resume normal lending soon, the IMF persuaded Bucharest to negotiate rescheduling agreements with its creditors. The negotiations proved long and contentious, but by late 1982 Bucharest had rescheduled the

Figure 1
Romania: Cumulative Hard Currency
Debt, 1971-85^a

Billion US \$

^a Yearend.

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1981 arrears and 1982 obligations with Western banks and governments. To reinstate the standby program, the IMF set new performance criteria that called for Bucharest to take additional actions on prices, exchange rates, and interest rates.

Although negotiations on 1983 debt reschedulings went more smoothly, the Ceausescu regime was embarrassed by the need to reschedule and was growing weary of foreign involvement in economic decision making. Highly sensitive to measures that would lessen his control over the economy, Ceausescu balked at IMF requests for additional information on the economy and for further policy changes. The regime embarked upon a "go-it-alone" course that would avoid new borrowings and further reschedulings and pay off Romania's debt by the end of the 1980s. The IMF, with Bucharest's agreement, canceled the last

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year of the standby arrangement in early 1984, and the regime reversed earlier policy actions recommended by the Fund. On numerous occasions since then, Ceausescu has denounced the IMF and called on the Fund to cease imposing economic conditions as the basis for its lending. [redacted]

Adjustment Strategy

Ceausescu's decision to rid Romania of foreign debt and creditor "meddling" required an adjustment strategy that placed top priority on running large trade surpluses. But Ceausescu also wanted to protect investment to preserve the industrialization program. Romanian authorities drafted a plan for moderately rapid growth that would provide the output needed for increased exports and growth in investment. The planners were less supportive of the consumer who was to receive a smaller share of output. [redacted]

The regime's plan to run large hard currency trade surpluses hinged on rapid growth of exports. The revised 1981-85 economic program released in 1981 called for 12-percent average annual growth in total trade and implied that this growth would originate mostly from increases in exports, apparently at levels well above 12 percent a year. Most of this growth was probably intended to be in exports to the West in order to generate cash needed for debt service. Much of the increase was to come from sales of machinery, which Ceausescu said should double over the period. [redacted]

Although the plan said little about imports, provisions for improved efficiency in use of raw materials and energy and more intensive development of domestic resources suggested that imports would be curbed, if not cut. Cutting the oil import bill was particularly important to reversing Romania's trade deficits. This required channeling imported crude into refining for export rather than domestic use, increasing domestic energy output to substitute for the imported crude used for nonexport purposes, and, finally, improving the efficiency of energy use. [redacted]

Previously planned increases in investment were protected in order to fuel economic growth. Growth in

industrial investment was to improve Romania's exports of manufactured goods and machinery and thereby lessen its dependence on refined oil exports. Sizable investments in energy production included plans to more than double coal output, construct a large nuclear power plant, and build more thermal and hydroelectric plants. Investment plans for agriculture emphasized increased machinery deliveries and land reclamation in order to expand crop production. Planned improvements in consumer welfare, however, were less than in the original guidelines, suggesting that the regime would sooner cut consumption than investment if resources were to grow scarce. [redacted]

Trade Results

Bucharest's foreign trade strategy, the linchpin of the 1981-85 plan, failed. Instead of increasing in 1982 and 1983, the value of hard currency exports declined 18 percent from 1981 (table 5). Romania's expectation of strong gains in sales of machinery and equipment proved unrealistic as exports of these items fell by more than 20 percent. Soft prices and reduced supplies of crude cut earnings from oil product sales from their 1981 peak. Hard currency exports rebounded by about 9 percent in 1984 as increases in exports of refined products, chemicals, and consumer goods—largely diverted from domestic uses—more than offset a further fall in sales of machinery and equipment. In 1985, however, hard currency exports fell back to the 1983 level. The declining quality of Romanian export goods and domestic production shortfalls largely explain last year's disappointing results. [redacted]

The decline in export earnings, loss of supplier financing, and the regime's determination to pay down its debt forced a sharp cutback in imports after 1980. Hard currency imports declined by 13 percent in 1981 when short-term credit dried up. Bucharest cut imports by an additional 40 percent in 1982-83 to swing its current account balance from a \$2.1 billion deficit in 1981 to more than \$900 million surplus in 1983. Imports grew only marginally in 1984-85 as the regime continued to run large surpluses to cover its obligations. [redacted]

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Table 5
Value and Composition of Hard Currency
Exports and Imports, 1980-84

Million US \$

	1980	1981	1982	1983	1984
Exports ^a					
Total	6,335	7,112	6,006	5,833	6,347
Machinery and equipment	1,039	1,821	1,705	1,413	1,207
Fuels, minerals, and metals	3,154	3,208	2,406	2,737	3,329
Chemicals and fertilizer	526	590	529	512	603
Consumer goods	1,026	1,095	919	836	902
Food and agricultural products	590	398	447	335	306
Imports ^a					
Total	7,967	6,902	4,604	4,321	4,283
Machinery and equipment	1,147	847	468	545	366
Fuels, minerals, and metals	5,330	4,472	3,404	3,123	3,251
Chemicals and fertilizer	605	490	331	327	380
Consumer goods	64	92	69	79	65
Food and agricultural products	821	1,001	332	238	221


^a Defined as trade with nonsocialist countries. Total figures for hard currency imports and exports as given in tables 4 and 21 are higher because they include some hard currency trade with socialist countries.

Source: *Economic Memorandum*, 1985.



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Bucharest has focused the import cuts primarily on items that are not essential for current production, such as capital and consumer goods, and has given priority to goods needed to produce exports, such as oil and raw materials. Imports of machinery and agricultural products have borne the brunt of the reduction, falling by more than two-thirds between 1980 and 1984. After making cutbacks in 1981-82, Bucharest resumed substantial imports of crude oil because refined petroleum products have remained the major hard currency earner and Romania has been unable to raise production of crude. Failure to increase mining output significantly has led the regime to continue large imports of iron ore, coking coal, and metallurgical coke; purchases of some minerals and metals were continued in order to maintain steel output, another significant hard currency earner. Likewise, the regime has continued large imports of

various ferroalloys needed to produce export items such as oil drilling equipment, automobiles, railway rolling stock, and ships. Finally, the regime last year resumed imports of spare parts for energy equipment in belated recognition that the lack of such parts was causing serious disruptions to the economy. 

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Direction of Trade

The trends in hard currency exports and imports measured in constant prices show that the adjustment effort has produced a substantial outflow of resources from the economy. Although the value of exports fell

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The Quality Problems in Export Goods

The failure to maintain production equipment, cuts in research and development, the meager supply of skilled workers, and shortages of specified inputs have contributed to the falling quality of output in several key export sectors, such as machine tools, construction materials, oil drilling equipment, refinery equipment, and railway cars. Deteriorating production in the machine-building industries has forced planners to divert chemicals, fuels, steel, and food products from the domestic economy in a faltering attempt to meet ambitious export targets:

- at the Arad railway car plant, which produces a large share of the 6,000 to 7,000 railway cars exported annually, Romanian-manufactured lathe machines required frequent repairs. Approximately 60 percent of the needed repairs were caused by negligent maintenance, such as poor cleaning and a shortage of spare parts and lubricating oil. In recent years, the factory has received numerous complaints from foreign customers about welding seams breaking apart, a problem attributed to the low quality of Romanian welding tools and poorly trained welders.
- *The Yemen Arab Republic in 1985 rejected a Romanian proposal for construction of an oil refinery and pipeline after concluding that Romanian technology lagged Western expertise.*
- *Expert analysis of the Romanian "state-of-the-art" numerically controlled machines and machining centers exhibited in early 1985 concluded that their*

quality was below not only Western but also other East European products.

- *According to an evaluation by a foreign company of a sample of Romanian televisions produced for export, the sets were technically outdated and the internal soldering and wires were unsafe.*
- *The low quality of Romanian steel used in the production of cars and machine tools has caused foreign customers to refuse delivery of several shipments. In order to compensate for the lack of high-quality steel, more poor-quality steel is used, causing the product to be heavier than specified.*
- *Brazilian officials told the US Embassy that recent Romanian efforts to increase imports of Brazilian iron ore have been hampered by Brazilian reluctance to accept Romanian manufactured goods in countertrade, primarily because of their poor quality. Brazil no longer imports Romanian offshore drilling equipment because it is obsolete.*

Complaints about Romanian goods are not limited to more discriminating nonsocialist trade partners. East German, Bulgarian, and Polish officials have indicated that the refusal of importing enterprises to accept Romanian exports limits the growth of bilateral trade. Chinese diplomats told US Embassy officials recently that China is reluctant to increase exports of crude oil to Romania in exchange for barter goods because it does not need the rudimentary machinery and shoddy goods the Romanians are trying to exchange.

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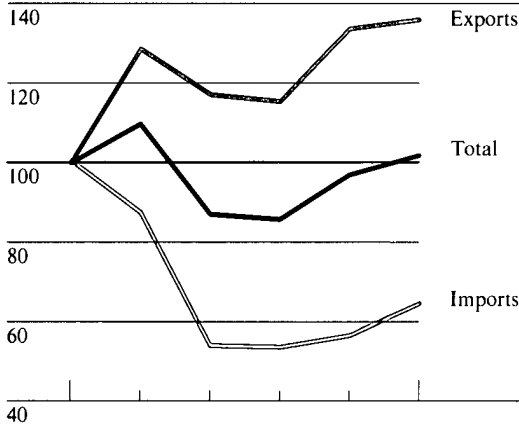
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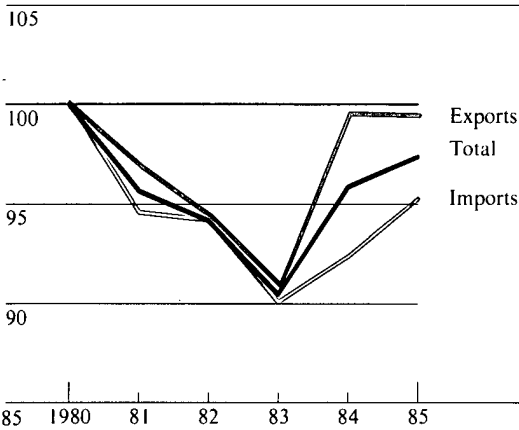
Figure 2
Romania: Volume of Trade by Region, 1980-85

Index: 1980 = 100

Volume of Trade With Market Economies



Volume of Trade With Socialist Countries



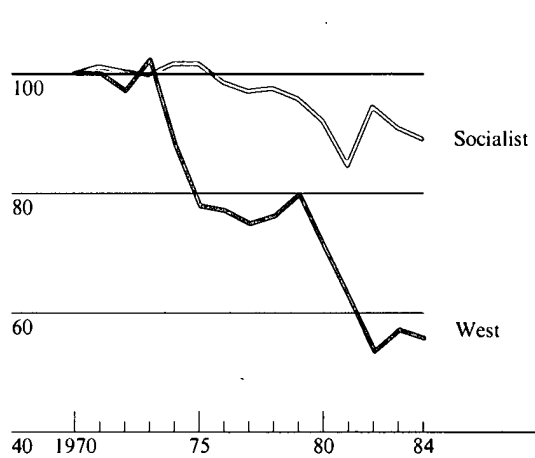
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in 1981-85, they increased by nearly 20 percent in volume over the 1980 level (figure 2). Imports, on the other hand, fell by nearly 35 percent in volume in 1982-83 from their peak in 1980 before recovering slightly over the past two years. The large shift in the net flow of resources (real exports less real imports) resulted not only from the need to move trade into

Figure 3
Romania: Terms of Trade With Socialist Countries and the West, 1970-84

Index: 1970 = 100

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surplus but also to offset unfavorable price movements that produced a nearly one-third decline in Romania's terms of trade with the West in 1980-84 (figure 3).

Trends in exports and imports with the socialist countries have not eased the burden placed on the economy by the massive adjustment of hard currency trade. A deterioration in Romania's terms of trade with the East—albeit more modest than that with the West—has required the economy to produce a greater net flow of resources to socialist countries. This has come about through a decrease in real imports over the 1981-85 period. The decline occurred in the first three years of adjustment when real imports fell 10 percent; gains over the past two years have offset only about half of the reduction. By contrast, real exports, which fell in tandem with imports in 1981-83, returned to their 1980 level by 1984.

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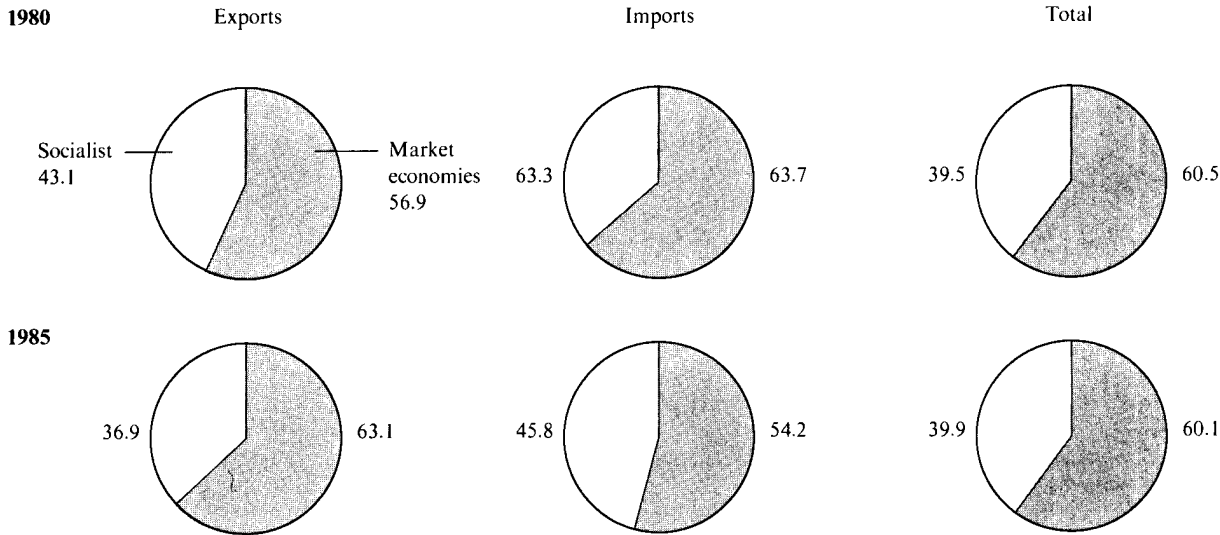
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Figure 4
Romania: Regional Breakdown of Exports, Imports,
and Total Trade in Real Terms

Percent



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Changes in the regional distribution of Romania's exports and imports show that the West benefited much more than the East from the shift in resource flows. Romania's overall trade in real terms moved only slightly toward the socialist countries in 1981-85; however, the regional shares of exports and imports changed dramatically (figure 4). Bucharest's drive to pay down its debt has increased the West's share of Romanian output at the East's expense while the East is supplying a much greater share of imports.

This trend, however, does not represent a reorientation of the Romanian economy to the socialist countries. The overall decline in real imports from all sources indicates that the Romanian economy has had to reduce its reliance on foreign resources in general (figure 5). The decline in Western imports has simply been greater than in Eastern imports.

The Limits of Growth

The failure of Romania's trade strategy doomed Bucharest's plans for moderately rapid growth and debt reduction. By calling for increases in output without growth in imports, the plans from the outset made highly unrealistic assumptions about gains in efficiency and import substitution, thus putting the economy under considerable strain. The economy was stretched even further when export shortfalls forced import cuts and the investment program failed to improve efficiency and produce import substitutes, particularly for energy.

Unrealistic expectations for trade performance and investment payoff led Romanian economic policy makers to overestimate by a wide margin the economy's growth potential during the initial adjustment period of 1981-82 (table 6). Growth fell far short of plans by comparison with previous periods because the planners counted on greater resource availability

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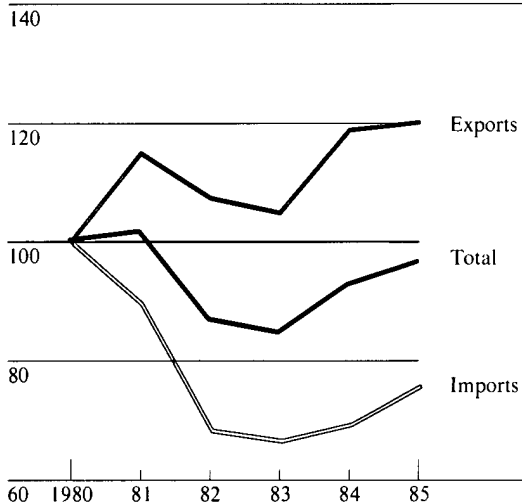
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Figure 5
Romania: Volume of Total Trade,
1980-85

Index: 1980 = 100



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through imports, domestic production, and efficiency gains. This slowdown led planners to adopt a more realistic target of 3.5-percent growth in national income in 1983—the lowest goal in the nearly two decades of Ceausescu's rule. [redacted]

A small revival in performance in 1983, however, rekindled the leadership's ambitions for rapid growth. Planners raised the target to 7 percent in 1984 and to 10 percent in 1985. Together with ambitious plans for 1986-90, released in 1984, these goals suggest that the leadership believed it had weathered the debt crisis and could resume its pursuit of rapid growth unfettered by foreign creditors and the IMF. Economic growth strengthened in 1984, and the overconfident regime accelerated sharply both investment and exports of refined oil products. These decisions prevented an easing of bottlenecks and drew down the economy's energy reserves, choking off the economic recovery in 1985. [redacted]

Protecting Investment

Despite the resource constraints resulting from the trade strategy failure and lower-than-planned economic growth, the regime opted to protect its investment goals as much as possible and to place the burden of adjustment on the population. Investment corrected for price inflation dropped only 0.1 percent in 1981-84 compared with 1977-80. Although this small decline was a major change in the trend of investment, which had shown average annual real growth of 10 percent in 1966-80, the reduction pales in comparison with the estimated decrease of at least 20 percent in the standard of living in 1981-85.¹ Moreover, the regime cut investment only in 1981-82 during the initial liquidity squeeze; the regime accelerated investment more rapidly than originally planned in 1983-84 when it perceived an easing of the pressures for adjustment. [redacted]

Ceausescu's adjustment priorities have differed sharply from those of other East European countries. The other financially strapped regimes, for fear of popular discontent, have given greater priority to protecting consumer welfare and less priority to investment and trade surpluses. Despite shortfalls in economic growth and exports, Bucharest has not abandoned its overriding objectives of elimination of foreign debt and preservation of the industrialization program through high levels of investment. [redacted]

Investment Priorities: Winners and Losers

Although real investment in 1981-84 equaled that of the previous four years, large shifts occurred in allocations among the various sectors of the economy and among the branches of industry. These shifts have been consistent with the priorities set out in Bucharest's original adjustment strategy and reflect an effort to deal with the imbalances that produced Romania's

¹ The per capita consumption of basic goods and services was estimated and weighted by household expenditures for each category of goods and services. [redacted]

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Economic Plans and Results, 1966-90^a*Percent*

	1966-70	1971-75	1976-80	1981-85	1980	1981	1982	1983	1984	1985	1986-90
Plans											
National income produced	8.4	11.0-12.0	10.3	7.1	8.8	7.0	5.5	3.5	7.3	10.0	7.6-8.3
Gross industrial output	11.6	11.0-12.0	10.7	7.6	11.4	7.0	4.7	3.5	6.7	7.5	6.0-6.5
Gross agricultural output	4.7-5.7 ^b	6.3-8.3 ^b	6.5-8.6 ^b	4.5-5.0 ^b	4.7-6.0	NA	6.0-7.9	5.1-5.6	5.4-6.0	6.0-6.8	5.4-5.8
Investment	11.1 ^b	11.3 ^b	10.3 ^b	5.2 ^b	4.9	4.4	5.0	1.5	4.0	8.3	1.8-2.5
Retail sales	9.2-9.7	7.0-8.0	8.1	4.8	9.3	6.0	4.6	3.0	3.0	1.0-1.5	1.7-2.0
Results											
National income produced	7.7	11.3	7.2	4.4	2.8	2.2	2.7	3.4	7.7	5.9	
Gross industrial output	11.9	12.9	9.5	4.0	6.5	2.6	1.1	4.7	6.7	4.9	
Gross agricultural output ^a	(1.9)	4.6 ^b	4.8 ^b	2.0 ^b	-4.3 ^b	-0.9	7.5	-2.0	13.3	0.1	
Investment	12.5 ^b	11.4 ^b	8.5 ^b	1.3 ^b	2.6	-7.1	-3.8	2.9	6.1	1.6	
Retail Sales	10.1	8.2	7.9	1.7	6.4	4.3	-2.5	0.5	4.8	1.8	

^a Average annual real growth.^b Annual average real growth, 5-year average over preceding 5-year average.

Source: Romanian official data.

Note: The 1981-85 plan results for industry are inconsistent with the annual plan results reported for each of those years.

debt problem. Romanian planners have focused investment on improvement of agriculture, domestic energy production, and industrial exports:

- Long-starved agriculture was the only sector to receive an increase in investment, amounting to nearly 25 percent in real terms over the four-year period (table 7). The biggest losses were felt by sectors serving the population's needs, such as municipal services, education and health, and housing, and by sectors supporting the economy's infrastructure, such as transport and communications.
- Planners largely protected industry as a whole from any significant loss of investment but shifted resources heavily toward energy production and away from those branches whose rapid expansion in the 1970s fostered the economy's appetite for energy and raw materials (figure 6). Investment in electricity and thermal power nearly doubled and increased by half in fuel production (table 8). Ferrous metallurgy, the chemical industry, and construction materials suffered major losses in resources. Although

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Table 7
Investment by Sectors, 1980 and 1984

	1980 (billion 1977 lei) ^a	1984 (billion 1977 lei) ^a	Percent Change
Total	210.45	205.31	-2.4
Industry	105.88	104.12	-1.7
Agriculture	27.70	34.37	24.1
Construction	9.55	8.01	-16.2
Research and development	1.33	1.16	-12.8
Transport and communications	25.01	22.08	-11.7
Education and health	3.77	1.53	-59.4
Housing	21.69	19.45	-10.3
Municipal services	6.39	8.78	-37.4
Retail trade	4.52	4.25	-6.0
Other	4.61	1.56	-66.2

^a Romanian official investment numbers in current lei were deflated by an implicit index derived from various Romanian data concerning total investment growth in real and nominal terms.

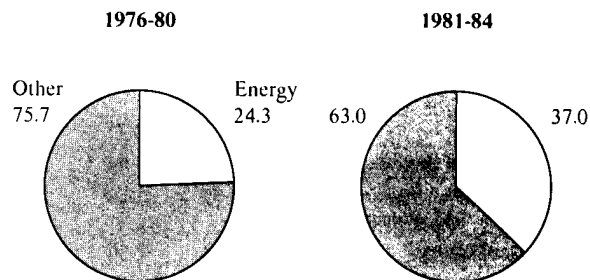
Sources: Derived from data in *Economic Memorandum*, 1985, and *Anuarul Statistic al Republicii Socialiste Romania*, various years.

investment in machine building contracted by nearly 30 percent, planners allocated more resources to expanding industrial exports—primarily autos and trucks—and to building an electronics industry virtually from the ground up. More investment was put into food processing, presumably to keep pace with the planned increase in agricultural output and to support an expansion of food exports. Investment in production of nonfood consumer goods, however, fell by nearly half.

Although targeted to the economy's priority needs, investment did not produce the increase in supplies and efficiency needed for strong growth and improved trade performance. Clearly, too many resources were spent on projects whose payoff will come only in the long term—if ever—but not in the period of greatest need. Comparatively small expenditures for the repair and maintenance of existing capital stock and infrastructure were slashed while substantial resources

Figure 6
Romania: Share of Energy in Investment Allocation to Industry

Percent



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flowed to still uncompleted projects. Excessive micro-management from central authorities, including Ceausescu himself, resulted in the irrational use of resources at the producer level. As a result, industry and agriculture suffered from tightening bottlenecks as the impact of inadequate supplies of domestically produced and imported inputs reverberated throughout the economy.

Energy Shortages

The energy program has been the weak link in Romania's domestic adjustment effort. Although Bucharest has reduced its oil trade deficit, increases in domestic production have been far below plan, and energy efficiency has not improved sufficiently to meet the regime's ambitious goals. Bucharest's effort to force rapid growth has depleted the economy's energy reserves and produced widespread shortages.

Romania substantially reduced its reliance on imported energy for domestic consumption between 1980 and 1984 (table 9). Net oil imports (oil not refined for reexport) decreased from about 142,000 b/d to 57,230 b/d over this period, and the oil trade deficit was

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Table 8
Investment in Industrial Branches, 1980 and 1984

	1980 (billion 1977 lei)	1984 (billion 1977 lei)	Percent Change
Total industry	105.88	104.12	-1.7
Electricity and thermal power	11.45	21.84	90.7
Fuel (coal, coke, crude oil, natural gas, and propane)	13.93	21.00	50.8
Ferrous metallurgy	12.34	7.59	-38.5
Nonferrous metallurgy	2.61	3.50	34.1
Machine building and metalworking	30.57	21.55	-29.5
Chemicals	14.80	10.79	-27.1
Construction materials	4.44	1.94	-56.3
Forestry and woodworking	1.92	2.50	30.2
Light industry	5.51	2.77	-49.7
Food industry	4.68	6.85	46.4
Other	3.63	3.79	4.4

Sources: Derived from data in *Economic Memorandum*, 1984, and *Anuarul Statistic al Republicii Socialiste Romania*, various years.

Table 9
**Share of Net Imports in Domestic Energy
Consumption^a**

	Net Imports	Consumption	Share
1973	22	1,031	2.2
1974	5	1,044	0.5
1975	29	1,125	2.6
1976	73	1,219	6.0
1977	111	1,242	8.9
1978	187	1,314	14.2
1979	234	1,318	17.7
1980	265	1,367	19.4
1981	212	1,355	15.6
1982	198	1,347	14.7
1983	196	1,375	14.3
1984 ^b	212	1,415	14.9

^a Thousand barrels per day oil equivalent; the heat value of crude oil equivalent for all energy sources is assumed to be 10,010 Kcal/kg.

^b Estimate from *Economic Memorandum*, August 1984.

Sources: Derived from data in *Economic Memorandum*, 1984, and *Anuarul Statistic al Republicii Socialiste Romania*, various years.

Table 10
Net Imports of Primary Energy, 1980, 1983, 1984^a

	Total ^b	Oil	Gas	Coal	Electricity
1980	265	142	24	96	2
1983	196	63	28	94	10
1984 ^c	212	57	30	109	15

^a Thousand barrels per day oil equivalent.

^b Because of rounding, components' totals may not add to the totals shown.

^c Estimate.

Sources: Derived from data in *Economic Memorandum*, 1984, and *Anuarul Statistic al Republicii Socialiste Romania*, various years.

Table 11
Romania: The Energy Balance, 1980-84^a

	Consumption ^b	Production	Net Imports
1980	1,367	1,102	265
1981	1,355	1,143	212
1982	1,347	1,149	198
1983	1,375	1,179	196
1984 ^c	1,415	1,203	212

^a Thousand barrels per day oil equivalent.

^b Consumption is assumed to equal production plus net imports.

^c Estimate.

Sources: Derived from data in *Economic Memorandum*, 1984, and *Anuarul Statistic al Republicii Socialiste Romania*, various years.

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Table 12
Primary Energy Plans and Production, 1980-85

	1980		1981		1982		1983		1984		1985	
	Plan	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Plan	Actual
Oil (<i>million metric tons</i>)	15.0	11.51	12.57	11.64	12.50	11.74	13.50	11.59	13.0	11.45	12.6	10.70
Methane (<i>billion cubic meters</i>)	27.13	28.16	29.55	29.26	32.98	28.62	NA	27.70	33.50	28.10	32.85	27.20
Coal (<i>million metric tons</i>)	54.09	35.16	50.84	36.93	44.00	37.86	52.21	44.52	61.71	44.28	64.3	46.60

squeezed down to about \$500 million by 1984. Increased purchases of natural gas, coal, and electricity—mostly from the Soviet Union—offset about 30 percent of the energy value of the decreased oil imports (table 10). [redacted]

By 1984, Romania was able to increase domestic energy production sufficiently to offset the decrease in total imports and boost domestic supplies. Domestic energy production was 9 percent higher than in 1980, and total energy availability was 3.5 percent greater (table 11). Nonetheless, production and availability of energy were substantially below planned levels. The growth in energy production came from coal, particularly lignite; output of methane and oil declined slightly over the period 1980-85 (table 12). This trend combined with the reduction in net oil imports shifted the composition of domestic energy supplies toward lower grade sources. [redacted]

Compounding the shortfall in production, the Romanian economy did not achieve any improvement in energy efficiency. The ratio of GNP to energy use stayed at roughly the same level after 1980 (table 13). Moreover, [redacted] energy was reallocated away from “nonproductive” uses, particularly the household sector, to industry. This suggests that the efficiency of energy use actually declined in industry and possibly in transport. The decline in industrial efficiency probably resulted from reduced imports of energy-saving Western equipment; increased output of energy-intensive products, such as steel and heavy machinery; the changed composition of energy supplies; and bottlenecks in distribution. [redacted]

These developments, along with the effort to push economic growth, resulted in continually worsening energy shortages. Such shortages became acute when severe winter weather struck the country in early 1985, disrupting energy production and increasing demand when energy reserves were seriously depleted. Energy shortages continued throughout the year as energy output fell below 1984 levels. In October, Ceausescu declared a state of emergency in the electric power system and placed it under military cosupervision. Energy shortages in the winter of 1985-86 were less severe than during the previous winter, probably because of the relatively milder weather. [redacted]

Romania's failure to get much return from the substantial investments made in energy over the past few years reflects inappropriate priorities and bad luck. Half of energy investment has been spent on developing oil, gas, and coal production even though Romania's reserves of hydrocarbon energy sources are declining. Moreover, the plan to increase the use of coal has limited potential because coal reserves are largely lignite with very low energy value. Finally, the Romanians cut back imports of spare parts and neglected maintenance needed to keep existing gas and oilfield equipment functioning. In 1985, the Romanian press complained that the operating life of drilling equipment for these reasons had decreased by 40 percent. [redacted] the inability to service imported gas turbines impeded the flow of natural gas to Bucharest during the severe 1985 winter. [redacted]

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Table 13
Energy Efficiency of GNP, ^a 1973-84

1973	100.0
1974	107.4
1975	105.5
1976	103.1
1977	105.6
1978	104.6
1979	108.4
1980	106.7
1981	107.9
1982	109.5
1983	107.8
1984	106.7

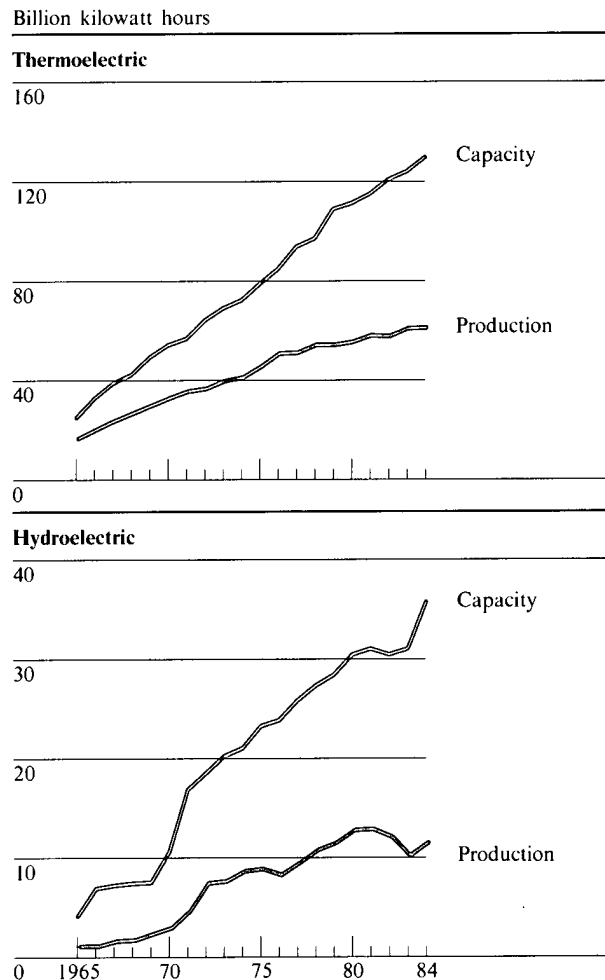
^a Calculated as thousand lei of GNP per consumption of energy in barrel per day oil equivalent. GNP in 1977 lei used in this calculation excludes agricultural output to remove the sizable fluctuations introduced by weather.

Sources: Derived from GNP in 1977 factor cost and table 11.

Complementing the effort to boost output of hydrocarbon energy sources, Romanian planners have allocated an additional 15 to 20 percent of energy investment to building coal, oil, and gas-fired electric generating plants. The 17-percent expansion in thermal power capacity between 1980 and yearend 1984, however, has outstripped increases in fuel supplies, resulting in continuing declines in utilization rates (figure 7). Poor maintenance of equipment, restrictions on imported parts, and the burning of coal of lower quality than specified for the equipment have further depressed capacity utilization and energy efficiency.

The overexpenditures on hydrocarbon energy resources and thermal plants have taken away resources from the development of alternative sources that offer the best prospects for significant increases in energy supplies. Nonetheless, existing investments in hydroelectric capacity and nuclear power have not helped ease Romania's energy constraints over the past few years. Hydroelectric capacity has increased by 18 percent since 1980, but bad luck in the form of drought has reduced power output to less than a third

Figure 7
Romania: Thermoelectric and Hydroelectric Powerplant Capacity and Production, 1965-84



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of capacity and below 1980 production. The first unit of the massive 3,500-megawatt, 5-unit nuclear power complex at Cernavoda is not likely to come on line until 1990 at the earliest. Meanwhile this much-delayed project is tying up resources that produce no return at a time of great stringency.

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Deteriorating Infrastructure

Misplaced priorities and bottlenecks have degraded other elements of Romania's economic infrastructure, particularly transportation. Romania has carried out some investments that could improve efficiency and productivity in transportation—for example, electrifying railroad trunk lines and upgrading facilities at the Port of Constanta. In general, however, Bucharest's approach has been penny-wise and pound-foolish. Substantial resources have been poured into ill-conceived projects such as the Danube-Black Sea canal while comparatively small outlays to maintain existing facilities have been neglected:

- According to numerous emigre reports, the lack of materials and fuel to operate repair equipment has led to a serious deterioration in highways that in turn has caused expensive damage to cars and trucks.
- Some 25 to 30 percent of state-owned trucks are down at any given time awaiting repairs and spare parts, and vehicles are often cannibalized for parts.

This deterioration in transport capacity coupled with the regime's excessive demands have snarled freight movement. Total tonnage of freight stagnated in 1983 and fell 4 percent in 1984. Despite Ceausescu's harsh public criticism of the transport sector, performance did not improve last year. Truck transport has suffered because of the lack of fuel and the large number of vehicles out of service. Efforts to shift freight to the railroads have been hindered by shortages of railcars and engines and by manpower shortages that have delayed the loading and unloading of railcars.

The erosion of transport facilities is symptomatic of the general deterioration in Romania's capital stock. The cutbacks in imports of Western machinery and equipment have increased the share of less productive, less efficient Romanian machinery in new investment. According to emigre reports, the quality of Romanian machinery has declined even further because shortages of standard materials and parts have forced

machine builders to use less desirable substitutes. Finally, the lack of parts and appropriate lubricants has resulted in increased wear and breakdowns of engines and machinery.

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Impact on Industry

Import cutbacks, diversion of goods to export (table 14), energy shortfalls, deterioration of capital stock, and transport snarls have combined to take a heavy toll on industrial production. Industry initially faltered badly as a result of the sharp import cuts of 1981-82 (table 15). Some recovery appeared in 1984 when supplies of energy and raw materials improved. But the fuel shortages in 1985 produced the most serious disruption in industrial production. Basic industries operated on reduced schedules, steel and aluminium output dropped, and manufacturers dependent on steel, aluminium, and other metals experienced slowdowns and shutdowns. Output in machine building, shipbuilding, and auto industries dropped while shortages of oil reduced operations in the chemical and petrochemical branches. With output down in most branches of industry, the plan fulfillment report for 1985 omitted direct comparison with branch results in 1984. The officially reported growth of 4.9 percent in industry as a whole for 1985 hardly seems plausible given the performance of the subcomponent branches.

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Impact on Agriculture

Despite the sizable increase in investment, agriculture has suffered even more from Romania's adjustment problems than industry. Agricultural output and productivity have been poor during the period of adjustment to the financial crisis. Average grain production for the 1981-85 period was less than for the 1976-80 period (table 16), and the returns to capital stock increments fell sharply from those of the previous five-year period (table 17). Agriculture has experienced the shortages of fuel, parts, and machinery that have disrupted other sectors of the economy.

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Table 14
Net Exports as Share of Domestic
Production

Percent

	1980	1983	1984
Fertilizer	55	60	62
Cargo railcars	54	68	84
Aluminum and aluminum alloys	36	50	50
Processed fruit	43	37	41
Processed vegetables	21	27	28
Edible oils	18	25	30
Refined petroleum products	26	37	41

Sources: *Anuarul Statistic*, 1981 and 1984, and *Economic Memorandum*, 1985

But agriculture has also had to contend with severe drought and—perhaps most important—Ceausescu's bizarre guidance. No other sector has suffered from Ceausescu's petty tutelage as has agriculture. He has brought the many details of farm management, ranging from size of the feed rations for hogs through production goals for honey under his purview. For example, in a two-hour diatribe to the National Council of Agriculture in early 1985, he mandated:

- That no soybeans or seed corn be imported.
- That fruit trees be planted closer together.
- That sheep and cattle not be stabled during the winter.
- That each cooperative farm produce five kilograms of silkworm cocoons per year.
- That only certain varieties of wheat be planted.
- That farms decrease fuel consumption and avoid "the excessive use" of fertilizers and pesticides.

Ceausescu's directives were totally ill suited to the problems of Romanian agriculture. Romania could not forgo soybean imports given the serious protein deficiencies in animal nutrition and the poor prospects for increasing domestic production of soybeans. Seed corn imports were also necessary because of shortfalls

in production of high quality seeds. Hampered by the severe shortages of fuel, fertilizer, and pesticides, farmers could hardly be chastised for overexpending these items. [redacted]

Although increased investment in agriculture has provided more field machinery and irrigation equipment for Romanian farmers, the sector has suffered serious shortages of inputs during the adjustment period. Decreased allocations of medications, feed, pesticide, fertilizer, electricity, and fuels have depressed agricultural productivity. These shortages have resulted from cuts in the imports of some inputs and from increased exports of domestically produced items. This approach to improving trade earnings has been counterproductive. By reducing production below levels that would have been possible with adequate supplies, this strategy has lessened the availability of agricultural products for exports—items which the Romanians could have bartered with the USSR, in particular, for more oil. Energy shortages have prevented sufficient use of the expensive additions to the irrigation system to offset the dry conditions of the last three years. [redacted]

To add to the woes of the farm sector, President Ceausescu has tried to coerce private agriculture into boosting deliveries to the state marketing system. These measures have backfired because the private sector, which accounts for about half of the output of livestock products and of some crops, has reduced production and market supplies. The initial regulations—price ceilings on private sales—caused farmers to reduce their sales in village and urban farm markets. Because the excessively low state prices did not allow farmers to recover their production costs on sales of surplus meat and produce, they stopped raising more animals than needed for their own use. In response to this development, Ceausescu in early 1984 mandated compulsory deliveries to the state, which in turn apparently caused a further drop in private agricultural output. The authorities responded by curbing sales of livestock products in state retail

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Table 15 Percent
Growth in Industrial Output, 1978-85

	1978	1979	1980	1981	1982	1983	1984	1985
Total industry	9.0	8.1	6.5	2.6	1.1	4.0	6.7	4.9
Electric and thermal power	6.2	1.8	1.7	4.1	-1.2	2.8	6.3	0.3 ^a
Fuels	4.9	0.6	1.8	-1.3	-2.6	7.8	4.1	-1.0 ^a
Nonferrous metallurgy	5.8	3.7	6.5	0.6	-3.3	-1.6	3.6	NA
Ferrous metallurgy	8.7	8.0	1.0	4.3	-0.2	3.2	12.3	-4.2 ^a
Machine building and metalworking	14.3	11.4	10.1	2.2	3.5	5.3	9.0	9.6 ^a
Chemicals	10.1	1.9	6.7	3.9	1.3	5.4	8.1	0.7 ^a
Building materials	16.2	12.7	4.5	-0.2	2.0	2.4	5.0	-0.2 ^a
Forestry and wood-working	7.2	4.8	4.9	3.2	2.9	3.8	2.4	2.7 ^a
Textiles	8.3	8.2	9.6	6.3	2.4	2.1	-1.0	NA
Clothing	7.0	8.5	8.4	6.2	2.0	6.0	9.8	NA
Leather goods, furs, and footwear	7.2	8.3	8.6	4.5	3.2	10.2	7.1	NA
Food processing	0.4	7.9	1.3	-1.0	-2.2	5.2	5.3	NA

^a Estimated.

Sources: *Economic Memorandum*, various years, and *Agerpres*, 21 Feb 1986. Output by branch for 1985 is extrapolated from the 1981, 1982, 1983, and 1984 plan fulfillment reports and the 1985 plan fulfillment report, which gave only 1981-85 total growth for some branches of industry, apparently to disguise poor performance in 1985.

[Redacted]

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stores in rural areas to force the populace to increase private farming and become self-sufficient in these foods. In addition, supplies of animal feed and other agricultural inputs to private plot holders have been made contingent upon whether private farmers deliver animals to the state. More recently, [Redacted] rations of basic staples in many villages are not provided to rural residents unless they deliver a certain quota of animals to the state for slaughter. Nonetheless, inventories of privately owned animals appear to be decreasing, and private-sector output of livestock products is likely to continue to decline. [Redacted]

The Five-Year Slide in Consumer Welfare

The problems in production, the shift of resources to the external sector, and the priority given to sustaining investment have drastically reduced domestic consumption—which already was lower than in all other East European countries except Albania. Two critical components of consumer welfare—household energy use and food availability—have been affected most severely. During the harsh winter of 1984-85,

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Table 16
Grain Production, 1976-85*Million metric tons*

Year	Output
1976-80 average	19.4
1981	17.6
1982	19.8
1983	18.4
1984	19.0
1985	16.6
1981-85 average	18.3

Source: CIA Estimates.

Table 17
Returns to Capital Stock Increases in Agriculture

	Marginal Rate of Return ^a
1976-80 average	0.50
1981-85 average	0.38

^aDefined as the ratio of percent change in gross agricultural output to the percent change in capital stock. Calculations for each year were averaged by periods.

Sources: Derived from data in *Anuaral Statistic al Republicii Socialiste Romania*, various years.

the populace experienced hardships probably unprecedented since the immediate postwar period. This decline in consumer welfare apparently has contributed to a sharp rise in mortality rates. [redacted]

Energy

To shield industry from energy shortfalls, the authorities cut supplies to the household sector and increased consumer prices for energy by 80 percent in 1980-83. Between 1983 and 1985, the government mandated cuts of up to 75 percent in household energy consumption and shut off gas and electricity to residential neighborhoods for several days at a time during the exceptionally cold weather of 1984-85. Households were limited to one 15-watt lightbulb and one appliance with the militia inspecting residences, fining violators, and sometimes plastering over electrical outlets. During the winter of 1985-86, energy supplies to households were not cut as severely; nevertheless, even in Bucharest many residential areas received power for only a few hours each day. [redacted]

Food

The regime reacted to food shortages in late 1981 and early 1982 by imposing formal rationing on sugar, flour, and cooking oil. As agricultural production continued to falter, the regime decreased food supplies to local distributors, causing a reduction of about 25 percent in rations. Livestock products—especially

meat and milk—have become so scarce that they are not even formally rationed. Although Bucharest claims per capita consumption of meat supplies is about 60 kilograms per year, our analysis indicates it is less than half this amount. Moreover, food prices at state retail stores have surged by over 50 percent since 1980, with only bread prices remaining relatively stable (table 18). Embassy reporting indicates that food supplies in the winter of 1985-86 were even worse than during the previous winter. [redacted]

Falling Real Incomes

Despite official data to the contrary, we believe real incomes have fallen sharply—at least 20 percent—during the 1980-84 period. In addition to increases in prices for energy and food, many emigres have reported that rents have doubled, the prices of clothing and durable goods have jumped steeply, and the quality and variety of consumer goods have deteriorated. Meanwhile, some 2 to 5 percent of worker wages are being withheld under a mandatory “investment” program. [redacted]

Increased Mortality

Poor nutrition, inadequate heat, and the unavailability of medications have increased mortality rates in the past few years. Infant mortality, already significantly

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Table 18
State Retail Food Price Increases, 1981-84

Food Item	Percent Increases
Beef	100
Pork	83
Sausage	28
Chicken	77
Milk	39
Cheese	76
Rice	69
Sugar	72
Flour	37
Bread	8
Eggs	24
Coffee	106
Butter	35
Margarine	83
Oranges	38
Lemons	52
Apples	78
Vegetable oil	55
Vodka	37

Source: Calculated from a sampling of emigre reporting.

higher than elsewhere in Europe (table 19), climbed by 35 percent in November 1984-January 1985 compared with January-September 1984. [redacted] Official Romanian statistics reported infant mortality at 26.5 per 1,000 live births in 1984. However, according to official statistics, the infant mortality rate in eight *judets* that year exceeded 30 per 1,000 live births, and in two *judets* the rates were between 35 and 40 per 1,000. In some areas, baby formula is not available and young children can obtain milk only with a doctor's prescription. [redacted] a jump in the death rate among the elderly. The crude death rate (the rate unadjusted for shifts in the age and sex composition) for the entire population since 1980 has increased far more rapidly than in any other East European country (table 20). [redacted]

Table 19
Romania and Selected Countries:
Infant Mortality Rates, 1983^a

Romania	26.8
Bulgaria	16.5
Hungary	19.0
GDR	10.7
Poland	23.2
Czechoslovakia	15.6
US	10.9
Spain	10.0
Italy	12.0
Sweden	8.0

^a Per 1,000 children under one year old.

Sources: *Anuarul Statistic al Republicii Socialiste Romania*, 1984; *Statisticheskoy yezhegodnik stran-chlenov Soveta ekonomicheskoy vzaimopomoshhi*, 1984; World Bank, *World Development Indicators*, 1985.

Unrest, Apathy, and Regime Responses

Since a spate of quickly suppressed popular unrest in 1981-82, the populace has been demoralized by the seeming futility of challenging the regime. Although popular disaffection continues to surface in occasional strikes and industrial sabotage, the regime's main worry now seems to be absenteeism, which appears to have worsened even as many factories have required employees to work double shifts and holidays. Bucharest's concern about the effect of deteriorating popular morale on worker productivity has resulted in a steady increase in coercion, a heightening of the campaign to foster Romanian nationalism, and exhortations to work harder. The security apparatus has increased its surveillance of workers in industrial installations where unrest has occurred in past years and also among the Hungarian minority. Except for special food supplies for coal miners and workers in some large plants, the regime has not relied upon positive incentives. [redacted]

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Table 20 *Per 1,000 population*
Romania and Other East
European Countries: Crude Death
Rates, 1980 and 1983

	Year		Percent Change
	1980	1983	
Romania	10.4	12.3	18
Bulgaria	11.1	11.4	3
Hungary	13.6	13.9	2
GDR	14.2	13.3	-6
Poland	9.9	9.5	-4
Czechoslovakia	12.2	12.0	-2

Sources: *Anuarul Statistic al Republicii Socialiste Romania*, 1984; *Statisticheskii yezhegodnik stran-chlenov Soveta ekonomicheskoy vzaimopomoshchi*, 1984.

Economic coercion has taken several forms:

- The regime in 1983 raised production goals and installed a new wage system closely linking salaries to production targets. Workers in factories where targets are not met may lose 25 to 30 percent of their monthly base wages. In addition, workers receive only a small portion of their base wages when a factory shuts down for lack of energy or other raw materials. In late 1985, an even more punitive system of wage reductions was imposed on economic managers who failed to meet production goals.
- Retirement ages have been raised, pensions cut, and workers in some factories and mines forced to work double shifts.
- The regime has cracked down on black-market activity to limit shortage-caused disruptions in retail markets.
- The regime has announced programs to redistribute the rural population to centralize distribution of services and to resettle urban elderly to rural areas to free up housing in cities for the working-age population. Little has been done to implement these programs, however.

The Financial Gain—Worth the Pain?

The turnaround in Romania's trade balances after 1980, produced by import suppression and painful austerity, enabled the regime to reduce its dependence on foreign lenders for only a short time. Annual hard currency trade surpluses of over \$1.5 billion in 1982-84—compared with a \$1.5 billion deficit in 1980—helped Bucharest cut its hard currency debt by 30 percent to \$7.2 billion by yearend 1984. Thanks to the large trade surplus and a nearly 50-percent fall in scheduled repayment of debt from the 1983 level, Bucharest met its 1984 obligations without further debt rescheduling or new medium- and long-term borrowing.

Bucharest's strategy for financial recovery began to falter, however, in early 1985. The disruptions in production caused by the harsh winter and energy shortages cut hard currency exports by 25 percent in the first quarter compared to 1984. This loss of earnings coincided with an increase in debt service as the first payments on the 1982 bank rescheduling agreement fell due. Romanian financial authorities had to request an \$80 million short-term bridge loan from Western banks to cover these payments.

Financial pressures eased only slightly after the first quarter of 1985. The Romanian economy was able to squeeze out more hard currency exports in the second and third quarters, but the widening effects of energy and steel shortages caused exports to plunge late in the year. The hard currency trade surplus slipped to \$1.4 billion from \$2.2 billion in 1984, but this was still large enough to cut Romania's debt to \$6.6 billion by yearend. Nonetheless, Ceausescu had to ease his dictum against new medium- and long-term borrowing in order to meet all obligations. After prolonged negotiations, a syndicated credit of \$150 million was obtained in December from Western banks.

Romania's financial position has deteriorated further in 1986. Export performance has continued to falter, and expected repayments of about \$500 million from

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Romania's Middle Eastern debtors failed to materialize as the price of crude oil declined. As a result, Romania has again been running arrears. We estimate that, by the end of April, Bucharest had either rolled over on a short-term basis or missed approximately \$300 million of the \$650 million in payments due in January through April. [redacted]

[redacted] Bucharest would be unable to meet its May payments to commercial banks. They requested a rescheduling of the \$260 million due this year on the 1982 rescheduling agreement and later asked the banks to consider rescheduling similar amounts in 1987 and 1988. The need for new financing is becoming increasingly acute. With some \$800 million due in May through July to banks, governments, and multilateral institutions, Bucharest appears to have entered a period in which arrears will mount up rapidly. A financing gap of at least \$500 million this year seems likely; even with rescheduling of the \$260 million, Bucharest will need more financial assistance.

The financial outlook for 1987-88 is no more encouraging. Romania is unlikely to earn the hard currency trade surpluses necessary to cover debt service payments averaging about \$2 billion (table 21). Bucharest's ability to sustain the hard currency trade surplus of even \$1.4 billion earned in 1985 will be increasingly difficult as declining product quality, decreased price spreads between imported crude oil and exported petroleum products, and disruptions in industrial production depress export earnings. [redacted]

The terms and amounts of financial help obtained for 1986-88 will determine to a large extent whether Bucharest can make progress toward financial recovery. A multiyear rescheduling of much of the \$2.8 billion in principal owed to banks in these years appears to offer the best prospect for a more balanced adjustment. Short-term extensions on obligations would not provide any breathing room for Romania and would foster a climate of worry among banks that might hamper Bucharest's ability to obtain trade financing. Medium-term financing of about \$250 million would probably enable Romania to get through 1986 but would not relieve the substantial

financial pressure coming in 1987-88. In any event, voluntary lending of that amount by banks seems out of the question; in recent months, two efforts to raise considerably smaller amounts have failed. [redacted]

Arranging a multiyear debt rescheduling would encounter several obstacles. First, the banks might not agree to reschedule debt in amounts sufficient to allow Romanian planners to increase imports and set more realistic targets for growth and exports. Secondly, banks probably would insist that Western government creditors provide a comparable rescheduling of obligations due them. The Romanians, however, would probably not want to reschedule debts owed to governments. Finally, even if all parties agree to multiyear rescheduling, creditors probably would insist on some type of IMF oversight during the rescheduling period, as banks did when Romania requested multiyear rescheduling of rescheduled 1982 debts coming due in 1987 and 1988. The Romanians almost certainly would reject this condition again and indeed possibly the whole idea of a multiyear rescheduling because it would end Ceausescu's hopes for ridding Romania of debt and IMF "interference" in the near future. [redacted]

Outlook

The need for change in economic management is acute. Yet Ceausescu has vehemently ruled out both systemic reform and changes in economic policy. As long as he maintains his dominance, we see little chance for the emergence of political support for economic change. His control over policy extends from setting overall goals down to interference in minor operational procedures in enterprises and farms. [redacted]

Ceausescu's refusal to delegate significant authority in economic planning, his refusal to accept alternative views, and his sensitivity to any lessening of personal control have largely squelched discussion of new policies in the press or, apparently, among top officials. Because of Ceausescu's insistence upon absolute

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Financing Requirements and Sources, 1982-90*Million US \$*

	1982	1983	1984	1985	1986	1987	1988	1989	1990
Financing requirements	4,160	2,094	452	968	406	501	717	603	654
Current account balance	655	922	1,536	915	1,574	1,619	1,500	1,345	1,240
Trade account balance	1,525	1,688	2,186	1,445	2,090	2,060	1,870	1,650	1,500
Exports	6,235	6,246	6,892	6,280	7,380	8,270	8,650	8,900	9,200
Imports	4,710	4,558	4,706	4,835	5,290	6,210	6,780	7,250	7,700
Net interest	917	737	706	649	565	478	385	300	245
Other services	47	-29	56	119	49	37	15	-5	-15
Debt repayments	3,170	2,152	1,578	1,659	1,761	1,818	1,912	1,483	1,344
Medium- and long-term	2,081	1,211	1,045	1,269	1,258	1,361	1,402	978	794
Short-term	1,089	941	533	390	503	457	510	505	550
Net credits extended	-502	-476	-410	-224	-219	-302	-305	-465	-550
Arrears from previous year	1,143	388	0	0	0	0	0	0	0
Financing sources	4,065	1,791	418	988	406	373	580	853	848
Credits	1,372	903	602	478	776	662	838	853	848
Medium- and long-term	657	503	274	292	390	400	500	450	450
Short-term	414	268	272	361	462	510	505	550	505
IMF, net	301	132	56	-175	-76	-248	-167	-147	-107
Debt relief	2,718	976	0	0	260	0	0	0	0
Change in reserves	-25	-88	-184	510	-630	-289	-258	NA	NA
Errors and omissions	95	303	34	20	00	128	137	250	194
Financing gap/arrears	388	0	0	0	0	0	0	0	0

Sources: Romanian reported data for 1982-85 and Romanian projections for 1986-90.

agreement with his ideas and the pervasiveness of the internal security apparatus, Romanian officials apparently view themselves largely as executors rather than shapers of policy. Only a few signs of dissent at the top have appeared in recent years, and the attitudes of current top government and party officials on economic policies are not known to us. [redacted]

The recently intensified discussion of economic reform in the Soviet Union and reform measures adopted in some East European countries are unlikely to influence Ceausescu. He deeply mistrusts any measures that would move Romania's economy toward free market mechanisms. His lengthy diatribe at the

November 1984 Party Congress against systemic change was probably a message to other countries in the region that Romania will go its own way, as well as a warning to Romanian officials and economists not to question his management of the economy. [redacted]

The financial crisis appears to have stiffened Ceausescu's aversion to change. The regime has relied on the traditional central planning apparatus to reverse its payments deficits. And, as the economy faltered, it

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has increased the use of administrative fiat along with high-level supervision of enterprise operations. Although Romania's highly centralized economic planning has produced current account surpluses, it has not done well in allocating resources to promote efficiency over the longer term. [redacted]

Romania's Deputy Finance Minister recently told a Western government official that liquidating the foreign debt remained an obsession of the Romanian Government and that, in pursuit of this goal, the government would impose further sacrifices on the population. Indeed, Romania's need for borrowings last year spurred Ceausescu to impose even harsher regulations to push exports at the expense of the domestic economy. Furthermore, Romania's request for only \$260 million in debt relief for 1986 when its needs seem twice as great indicates that Ceausescu will continue to press for the maximum possible export earnings and debt reduction. [redacted]

Financial pressures and inflexible policies will prevent improvement in economic performance. The regime will keep pressing for rapid growth, but we expect inadequate imports of fuels, raw materials, and machinery to tighten bottlenecks and retard, if not prevent, gains in productivity. The deterioration in Romania's capital stock and infrastructure over the past five years will also brake economic growth. Without better allocation of resources and necessary inputs, Romania's investments in energy, industry, and agriculture will continue to yield limited returns. GNP growth is unlikely to exceed 1 to 2 percent annually on average over the next few years, and the Romanian economy will fall far short of 1986-90 plan goals. [redacted]

The outlook for living standards is not promising, in our view, because Ceausescu's drive to eliminate the debt and sustain investment will claim the bulk of available resources. Economic plans for 1986-90 allocate nearly all growth to investments and exports. Life for the long-suffering Romanians will continue to be a struggle. Since goods and services needed to maintain health and welfare are likely to remain curtailed, we expect mortality rates to continue their upward trend. [redacted]

Nonetheless, we do not foresee serious popular protest in the near future. The population is preoccupied with day-to-day existence, and the security apparatus maintains tight control. However, if rumors of Ceausescu's ill health prove true and he were to die in office or be incapacitated for long, the situation could deteriorate quickly. Unsure of the leadership's stability and resolve, the population could start to vent its frustrations. Despite the population's current passivity, discontent appears high and is certain to grow with worsening living conditions. [redacted]

Catalysts for Change

We expect Romania to hold to its present economic policies and priorities for the foreseeable future, but further economic deterioration or a possible succession to Ceausescu could eventually produce major changes. A return to some type of IMF supervision or monitoring would seem the most likely departure from current policy in the near term if Bucharest concludes it has little alternative in the face of worsening financial problems. The impact on Romania's economic situation would probably prove minimal under a Ceausescu-led regime but could be more significant under a successor regime committed to more rational economic policies. Alternatively, Bucharest might make political concessions to the USSR in return for economic assistance, but again this would seem more likely under a successor regime than under Ceausescu. [redacted]

Return to the IMF

If Western creditors demand and Bucharest acquiesces in renewed IMF supervision in conjunction with a debt rescheduling, the Fund would have to adopt a more innovative approach to make any progress against Romania's economic problems. The conventional IMF prescription of domestic austerity to correct external imbalance is ill suited given the already deep cuts made in domestic demand. Moreover, the Fund's market-oriented policy recommendations in the 1981 program seemed to have had little influence

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on resource allocation in the highly centralized Romanian economy. In its 1985 report on Romania, the IMF argued that the severe cuts in demand and imports risked serious damage to the economy and that more gradual adjustment was needed. To deal more effectively in Romania, the Fund concluded that it needed better statistical data and that it had to play a more direct role in the formulation of plan targets and implementation measures. Such an effort—if the Fund is capable of mounting it—would push creditor “interference” deeper than ever into Ceausescu’s management of the economy. For this reason, we believe that the IMF probably could not bring about the structural changes needed for improved economic performance under the current regime. [redacted]

A Succession

A successor regime, in order to ease Ceausescu’s austerity and gain popular support, might be more willing to request extended debt relief and accept IMF conditions for a standby arrangement. A new leadership could point to the large reduction already made in Romania’s debt and argue that, under a regime committed to more balanced economic policies, Romania would be a more attractive candidate for Western financial support. On the other hand, a successor regime might well be dominated by individuals who would attempt to carry on Ceausescu’s tradition of resistance to outside “interference” or who would look to Moscow for support. [redacted]

In our view, a multiple stage succession characterized by significant instability and confusion, particularly initially, is not unlikely. The policy goals of the various officials who might come to power are unclear, although a regime headed by Mrs. Ceausescu, who is likely to take power if only briefly, would probably not find new solutions to Romania’s serious economic problems. Over the longer term, we think a regime at least somewhat more pragmatic and moderate than the current regime is likely to emerge. [redacted]

The Soviet Factor

Although rumors of Romanian political concessions to Moscow in return for economic aid have been frequent in recent years, Romanian-Soviet trade actually slumped over most of the 1981-85 period. Bucharest sought greater deliveries of Soviet energy and raw

materials on concessionary terms, but Moscow did not abandon its demands for balanced trade, world market prices, and high-quality goods. Production problems and Bucharest’s need to earn hard currency in trade with the West limited Romania’s ability to supply the goods required by the Soviets in return for oil. But after declining in 1981-84, trade grew strongly last year. Bucharest bartered more food products and other hard goods in return for desperately needed oil. Nonetheless, Romania apparently did not receive concessionary terms, and its dependence on Soviet oil and gas remained very small in comparison with the rest of Eastern Europe. [redacted]

The new Soviet regime has made it clear that economic relations will be transacted on a strict “quid pro quo” basis. Although economic cooperation will increase somewhat because of Romanian participation in joint energy deals and Soviet efforts to develop intra-Bloc cooperation, growth seems likely to remain slow. We believe Romania’s dependence on Soviet oil and gas will increase over the next several years but will still be below the level of the other East European countries. Furthermore, given the recent declines in the price of oil in world markets, the Romanians might well increase purchases from the spot market if they perceive Soviet terms to be too onerous. [redacted]

Substantial Soviet aid would probably materialize only in the unlikely event that the Romanians agreed to major concessions on participation in Warsaw Pact activities and support of Soviet foreign policy. Moscow’s insistence on quid pro quo trade arrangements suggests that the USSR sees little purpose at present in trying to buy greater foreign policy compliance from Romania. The Soviets do not appear to regard Ceausescu’s behavior as a sufficient threat to their interests to warrant expending substantial sums to try to rein him in. They probably realize it would be a feat nearly impossible to carry off. [redacted]

But the USSR will want to influence the choice of a successor who would be more cooperative and compliant than Ceausescu. Should a succession occur or appear imminent, the Soviets might well attempt to

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woo the new regime or potential successors with promises of economic concessions. The confluence of a more energetic Soviet leadership, deteriorating conditions in Romania, and a new regime struggling to establish itself could set the stage for a more active Soviet policy in which Moscow would use any influence it has to push a post-Ceausescu leadership to publicly endorse Soviet foreign and military policies. We do not know whether Moscow has a favorite candidate. [] the Soviets have few, if any, assets within the Romanian establishment—Ceausescu having repeatedly purged suspected pro-Soviet officials. In the unsettled political climate likely to follow Ceausescu's sudden departure, however, the regime's current bulwarks against Soviet influence might be so weakened as to afford Moscow a more significant role in the successor sweepstakes than current evidence suggests it will have. Soviet willingness to extend economic assistance to Romania in the next few years, however, may be limited by the USSR's own economic problems and the new Soviet leadership's determination to pursue its industrial modernization program. []

Should Romania go into default and be unwilling to conclude rescheduling arrangements, the country might become more vulnerable to Soviet pressures. The resulting disruptions in economic activity, as international banks refuse to extend trade financing, would make it harder for the leadership to maintain stability and control. Foreign policy and Warsaw Pact concessions in return for economic assistance might then seem more attractive to the Romanians. []

Implications for the United States

US policy distinguishes Eastern Europe from the Soviet Union and recognizes and encourages differences among individual East European countries to the degree that they distance themselves from Soviet policies. This distancing can take several forms: adoption of distinct and more individualistic foreign policies, greater political and economic exchange with the non-Communist world, greater tolerance of emigration and other human rights, encouragement of a more flexible climate for political expression and economic change, and experimentation with economic liberalization. []

US interests have been served largely by Romania's maverick foreign policy over the past two decades, which the United States has tried to encourage by granting most-favored-nation trade status for over a decade. While carefully avoiding direct challenges to Moscow, Ceausescu has expanded the scope of policy differences permitted for a Warsaw Pact member, disallowed joint Warsaw Pact troop maneuvers on Romanian soil, acted as a thorn in Moscow's side during Warsaw Pact and Council for Mutual Economic Assistance (CEMA) meetings, maintained extensive trade ties to non-Communist countries, and provided the United States with an East European country in addition to Hungary as a focus for its policy of differentiation. Domestic repression, however, has seriously tarnished Romania's reputation in the West and diminished the value of its foreign policy assertiveness. Except for making some improvements in the area of emigration, the Ceausescu regime has generally resisted Western urgings to moderate its harsh human rights practices, branding them as interference in Romania's internal affairs, and has rejected economic liberalization. []

As long as Ceausescu stays relatively healthy and in control, we believe Romania is unlikely to get in step with the other Warsaw Pact members. Neither is Ceausescu likely to ease his repressive internal policies significantly. Even if the Romanian economy continues to perform poorly and the regime faces an increasing need for financial assistance, we think the West will have only limited opportunities to exert pressure on Ceausescu on foreign policy and human rights. In the absence of nondiscriminatory trade treatment by the United States, however, we believe Bucharest would experience more difficulty in sustaining its policy of diversified trade and might increase the share of trade with socialist countries. This would also leave Hungary in the uncomfortable position of being the only East European Warsaw Pact country that receives favored US trade treatment. []

Once Ceausescu passes from the scene, however, US opportunities to influence Romanian policy may change significantly. The successor regime or the

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Comparing Official and Reconstructed Growth

Two frequently used measures of economic activity are the official national income produced (NIP) used in Marxist national income accounts and GNP as conventionally measured in the West. NIP and GNP differ in three ways: services, prices, and depreciation. Marxist national income accounts exclude as nonproductive most services, including housing, education, government administration, and consumer services. Prices also distort Marxist national income accounts. Goods are valued in purchasers' prices that include turnover taxes—taxes on sales to consumers that vary from item to item. Western-style GNP accounts, on the other hand, value goods and services used in their production. A change in turnover taxes will, therefore, affect Marxist national income, but not Western-style GNP. NIP measures also suffer an upward bias resulting from underestimation of price increases in official indexes. This upward bias is due to two factors: (1) the declining quality of goods while their prices remain the same and (2) the introduction of new products whose prices are set excessively high, although the new product may be in reality an older product with some insignificant alteration. The third difference is that GNP measures do not deduct depreciation from gross fixed capital formation while Marxist national income measures do. []

As a result of these accounting differences, growth rates measured in Western-style GNP terms differ

markedly from growth rates expressed in Marxist national income terms. Movement in Western-style GNP growth measures tends to be less extreme than their Marxist counterparts because services, excluded from Marxist accounting practices, usually are more stable on a year-to-year basis than the other components of production. []

Romanian national accounting methodologies are more upwardly biased and historically have produced NIP growth rates higher than those of other East European countries. In addition, the new-product-pricing problem is particularly acute in Romanian value of production subindices and, with the increasing substitution of domestic goods for imports, has caused greater distortion in recent years of industrial output measures. Finally, the Romanian leadership's highly punitive wage policies appear to have motivated economic managers to engage in more statistical falsification in recent years than formerly. []

The following tabulation compares percentage growth for Romania in NIP and GNP terms for 1971-85:

	1971-75 ^a	1976-80 ^a	1981	1982	1983	1984	1985
GNP	6.7	3.9	0.2	2.6	0	4.6	1.8
NIP	11.3	7.2	2.2	2.7	3.4	7.7	5.9

^a Average annual rate of growth. []

contenders for power may be more willing to listen to economic reason. In our view, the new leaders will be wary of each other, less confident of their ability to control the country and keep the Soviets at bay, and more anxious for rapid, large infusions of aid in order to satisfy popular demands for a better life. Under such circumstances, the opportunities for both East and West to influence Romania's policy would improve markedly. []

Western policy toward a post-Ceausescu regime could be critical in shaping the new leadership's foreign policy course and the thrust of its economic policies. Western banks, taking note of the lower debt burden

left by Ceausescu and impressed that the successors are more rational and flexible, might judge that Romania is a somewhat better credit risk. But the banks are unlikely to respond in that manner early in a succession, when support is most needed, without a lead from the United States and other Western governments. []

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