

~~SECRET~~

Central Intelligence Agency

46 (b)(1) (b)(3) 1/R

Washington, D.C. 20505

APPROVED FOR RELEASE - CIA INFO DATE: 07-07-2011

7 July 1994

Romania: Economic Slide Ends, But Economic Reform Faces Uphill Battle

Prime Minister Vacaroiu is seeking external support for restructuring Romanian industry, but three years of gradual reform have prolonged Romania's painful transition, squandering resources and delaying recovery. A 1994-1995 IMF agreement commits Romania to accelerate privatization and restructuring, but growing poverty risks undermining support for a market economy.

Economy Bottoming Out

GDP grew slightly in 1993 on improved performance in the industrial and agricultural sectors,

- Industrial production grew 1.3 percent in 1993.
- Agricultural production grew 12 percent in 1993, the first increase since 1988.

Pro-Growth Policies Fueled Inflation

Romania's inflation rate--nearly 300 percent last year--led the region. Workers' real wages fell 15 percent as prices soared.

- Subsidies for nonviable industries increased inflation and diverted credit needed by the growing private sector.
- High inflation created negative real interest rates, eroding savings.

IMF Pushing Economic Reform

The Vacaroiu government signed a tough IMF program last December pledging to take measures to reduce inflation and accelerate reforms in return for over \$700 million in new loans.

- Bucharest has already raised interest rates and tightened the money supply, sharply reducing inflation.

This memorandum was prepared by the Office of European Analysis. Comments and queries are welcome.

~~SECRET~~

17

- The program demands progress on structural reform, including faster privatization and the restructuring of 300 enterprises. [redacted]

Reforms Face Growing Opposition

The Vacaroiu Government probably no longer has the political strength to implement the program, however. If the current government is unable to attract support from more reform-minded parties Bucharest is likely to fall short of at least some of the agreed targets.

- Support for labor protests is growing. Unions, protesting higher unemployment and falling wages, brought thousands of supporters to Bucharest last month, forcing the government to raise salaries. [redacted]

Outlook for Stability

Bucharest, which believes its national security lies with integration into Western economic institutions and security arrangements, will almost certainly continue market-oriented reforms in the near term, although its political weakness rules out full compliance with the IMF program.

- In the end, the population is likely to judge the new political and economic system by its success or failure in improving living standards. By putting off painful economic reforms in the state sector, Bucharest is postponing economic recovery, leaving the new institutions with less support to handle a future crisis. [redacted]