Statement by Balmiki Prasad Singh  
Date of Meeting: June 19, 2001

**Romania (1) Country Assistance Strategy; and (2) Social Sector Development Project**

We thank the Management and Staff for the candid and comprehensive CAS for Romania. We think that the CAS has quite accurately pinpointed Romania's development needs and we particularly agree with the identified unfinished structural reform agenda (pages 9-11). The problem, as always, is in the implementation of the agenda. Romania emerged in 1989 from the Ceausescu dictatorship with the most distorted economic structure of any ex-Communist state. It lags far behind its Central European neighbors not only in reforms but also on almost every macroeconomic indicator. Domestic policy is being increasingly driven by the desire for EU accession. Under the circumstances, we welcome the CAS’s mention of “partnership and selectivity” with European agencies like the EU and the EBRD. We believe the Bank should let the EU take the lead in setting the development agenda for Romania from the donor’s perspective.

**Macro-economic overview**

2. Romania’s GDP per head, at $1,500, is the lowest of all EU accession states. Inflation remains at worrying levels. Consumer prices rose in the first quarter 2001, year on year, by over 40%. Some of this is due to higher excise duties and hikes in electricity prices, but the average inflation forecast is 35% for this year. Export growth, which was a robust 24% in 2000, will slow to 5.4% as EU demand for industrial inputs weakens. GDP growth is forecast to be 2.6% this year, driven by private consumption and fuelled by inflationary wage rises. The key determinants driving inflation in Romania are the high unit labor costs and, to a lesser extent, the exchange rate. The deeply rooted fiscal indiscipline of state enterprises has been the key factor in driving inflation to the highest level amongst all transition economies. The problem of reducing the consolidated government budget deficit to 3% of GDP has been complicated by expenditure commitments undertaken by the outgoing government under Mugur Isarescu in the run-up to the elections to increase pensions and salaries to low-paid workers in the public sector.

What is the Government of Romania’s strategy to control inflation? What are the Staff’s views on the feasibility of controlling inflation in the near term?

**Restructuring of public enterprises**
3. It is still not clear whether the government has the necessary political will to tackle the militant trade unions on the issue of labor sector reform. While some closures have been carried out, notably in the coal industry, much remains to be done. The authorities fear civil unrest, remembering the violent strikes of the early 1990s. Restructuring has also been delayed by powerful vested interests, including trade unions, plant managers and bureaucrats. Also, there is genuine concern about the impact of redundancies on some of Europe’s poorest people. Unemployment is already running at 15 per cent; a serious restructuring program could push it above 20 per cent. About 41 per cent of Romanians live below the official poverty line, according to World Bank data. Uniquely in post-Communist Europe, agricultural employment is rising as the jobless poor abandon the cities and return to the villages to till small plots. The World Bank says agriculture’s share of unemployment has risen from 28 per cent to 36 per cent.

We find it surprising that the CAS makes no mention of the promotion of employment as a development strategy. It is only through employment generation that the new initiatives will have popular support. What are the Bank’s view on this? What is the Bank’s strategy for the reform of agriculture? What ESW is planned for Romania’s agriculture sector which could lead to both employment for the poor and enhancement of productivity in agriculture?

Privatization:

4. An overhaul of privatization strategy is necessary. The main concern is to stamp out corruption, which has dogged the process of effecting improvement in Romania, and has come in the way of tightening contracts and needed supervision. The Government of Romania has a long list of companies it wishes to privatize, including Banca Agricola, the farmers’ bank, Sidex, the steelworks which is Romania’s largest industrial enterprise with 28,000 workers, and more than 60 other companies. Banca Commerciale Romana, the biggest bank, is also on the list for late this year or early 2002. However, public trust must be rebuilt in the process. A particularly notorious case is that of the state tobacco monopoly, which the government last year wanted to sell to a local company called InterAgro for $67 million, in preference to Leaf Tobacco A Michailides, an international consortium, which offered Dollars $167.5 million.

The CAS makes no mention of any proposed reform of the privatization process in Romania.

Pension reform:

5. We welcome the proposed loan’s efforts to reform the pension system, which is one of the greatest challenges facing Romania. An estimated 1m of Romania’s 4.5m workers are employed producing little or nothing. Others have left work prematurely: Romania’s average retirement ages of 50 for women and 54 for men are among Europe’s lowest. The number of pensioners has doubled in a decade. The number of people on disability pensions has trebled. All these people and their families are a burden on the productive sector. It is carried, in part, by some of the region’s highest payroll taxes, which run at 60 per cent of the employee’s pay and are a significant barrier to job creation.
Reform of this complex system contains inherent political risks and a strong possibility of popular backlash. A considerable amount of time and effort would be needed to communicate the benefits of the new system and the unsustainability of the existing system. The project, we feel, has not addressed these risks in a concrete fashion.

**Social sector:**

6. Romania has emerged as one of the world’s largest centers of trafficking in drugs, prostitutes and migrants. There have been widespread concern about the treatment of the ethnic minority Romas, the overwhelming majority of whom are poor. We are concerned at the lack of attention in the CAS to the sharp deterioration in the social sector, in general, and in the health-care system, in particular, in Romania. Romania's health-care system has deteriorated in recent years, as hospitals have lost funding and expert staff as a result of public-spending cuts, and is considerably below the standards of western Europe. Most households are unable to afford private alternatives. Although the infant mortality rate has declined, from 26.9 deaths per 1,000 live births in 1989 to 18.6 per 1,000 in 1999, it remains one of Europe's highest, and compares with an average in east-central Europe of 13.7 per 1,000. Among east European countries outside the CIS, only Albania and Macedonia have equivalent or higher infant mortality rates. The maternal mortality rate, at 60 per 1,000 births, is six times that of Poland or Hungary and three times that of Russia, according to UN figures. Romania's death rate is one of the highest in eastern Europe (excluding the Commonwealth of Independent States, CIS), after Bulgaria, Hungary and Estonia. Male life expectancy fell from 67 years in the early 1990s to 65 years in 1997, rising to 66.2 in 2000; female life expectancy stabilized in the 1990s at just over 73 years. Health expenditure accounted for only 2.8% of GDP in 1998, compared with an EU average of 8.1% and an east-central European average of 5.5%. The number of reported cases of AIDS rose from 1,683 in 1991 to 5,730 in 1998 (of which 5,040 were children, often infected in childcare institutions), although this partly reflects improvements in the system of diagnosis. Up to 10% of the population are reported to be carrying hepatitis B.

The Board had approved a health sector reform project for Romania in June last year. What has been the experience in implementation so far? What are the Bank’s strategy for improving health outcomes in Romania in the near to medium term?

7. Subject to the remarks made above, we endorse the CAS and support the proposed Loan.