

# ROMANIA

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## Introduction

This paper is based on statistical information from the National Commission for Statistics of Romania, EBRD, Standard & Poor's Sovereign Ratings Service, World Bank, OECD, and data provided to standardized questionnaire by Ms Mihaela Cimpoesu from the Freemarkonsult International, Bucharest. Opinions and conclusions further provided are based on interview with Mr. David Boren from Montpellier Asset Management, as well as from the official country presentation during the EBRD Annual Meeting which was held 17-20 April 1999 at London.

## I. Statistical data

### 1. General information

Romania is located in SE Central Europe. With its area of 238,391 sq.km the country is 11<sup>th</sup> largest in Europe.

Borders:

- North-East and East on the Republic of Moldova (681.3 km), with 4 cross-border points<sup>1</sup>;
- North and East on the Ukraine (649.4 km), with 5 cross-border points;
- South-East on the Black Sea (193.5 km);
- South on Bulgaria (631.3 km), with 4 cross-border points;
- South-West on Yugoslavian Federation (546.4 km), with 4 cross-border points;
- West on Hungary (448.0 km), with 6 cross-border points;

### 2. Population

The total number of the Romania's population is 22,500,000 (July 1<sup>st</sup>, 1997), or 94.4 inhabitants at sq.km. According to the census returns of January 7, 1992 the population was 22,810,035. 89.4% of population are Romanians. The second largest ethnic groups are Hungarians-7.1%. The others ethnic groups include Germans-0.5%; Ukrainians-0.3%; Jews-0.04%.

55 % of country's population is urban. About 8 million Romanians live abroad.

*sex*

<i>As of:</i>	<i>Male</i>	<i>Female</i>
<i>Jan. 7, 1992 (census)</i>	49.2	50.8
<i>July 1, 1996</i>	49.0	51.0
<i>July 1, 1997</i>	49.0	51.0

*Age (as of July 1, 1996) %*

<i>Age</i>	<i>1996</i>	<i>1997</i>
0-14	19,91	19,56
15-59	62,39	62,67
60 and over	17,70	17,78

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<sup>1</sup> Incl.road and rail

### 3. Education

Average years of education of total population is 8.6 years.

In 1997/1998 school attendance was 4,643,000, or 20.6 % of the country's population. The number of public university students was 361,000 and of private universities 111,000.

### 4. Economic indicators:

#### 4.1 Economic agents

Number of companies registered (years 1992-1998)						
	1992	1993	1994	1995	1996	1997
Number of active enterprises in industry, construction, trade and other services*	130076	217857	286501	304359	312067	na
number of registered companies**	174787	317192	428619	487952	548873	593562

\* 1997 Statistical Yearbook

\*\* National Bank of Romania – Annual Report 1997

According to the statistic only 56.8 % of registered companies in Romania were active in 1996.

For 4-years period (1992-1996) the number of registered companies increased by some 240 % while number of active enterprises rose by 140 %.

The majority (72 %) of active companies in 1996 was working in trade sector, 10.3 % -in industry and only 0.15 % -in finances.

The total number of private enterprises in Romania increased by 664 % for the period 1990-1997 (from 76 277 in 1990 to 582 411 in 1997). There is a steady growth of private sector share of GDP - it was 26.4% in 1992, 34.8 % in 1993, 38.9 % in 1994, 45% in 1995, 52 % in 1996, up to 58 % in 1997. About 98 % of small trade and service business are privately owned. Private sector activity made up 75 % of GDP in trade sector, 24 % in industry, and 71 % in construction in 1996.

#### Number of active economic and social agents of national economy

Type of agents	total 1995	total 1996
	<b>597408</b>	<b>634353</b>
<b>enterprises, of which:</b>	<b>314332</b>	<b>323633</b>
<b>agricultural holdings</b>	<b>9497</b>	<b>11095</b>
<b>enterprises from industry, construction, trade and other services</b>	<b>304359</b>	<b>312067</b>
<b>financial and insurance companies</b>	<b>476</b>	<b>471</b>
<b>public administration</b>	<b>33436</b>	<b>32174</b>
<b>private administration</b>	<b>23233</b>	<b>23516</b>
<b>private entrepreneurs</b>	<b>226407</b>	<b>255030</b>

#### 4.2 Levels of fixed capital investments

	1992	1993	1994	1995	1996	1997
gross fixed capital formation (% of GDP)	19.2	17.9	20.3	21.4	23.1	19.2
investments (% of GDP)	14.74	14.08	16.08	18.02	19.32	..

In 1996 (the latest available data) investments of public sector was 51 % of total investments, and private sector invested 39,7 %.

#### 4.3 GDP

	1992	1993	1994	1995	1996	1997	1998 <sup>e)</sup>
Nominal GDP (in mill. USD*)	19575.3	26362.76	30074.44	35482.29	35157.61	34842.38	38200

e) Estimate; \* computed based on data in lei and the official yearly average exchange rate

During the period 1994-1996 Romania's GDP rose respectively by 3.5 %, 7.1 %, and 3.9 %.

In 1998 for second successive year Romania recorded decline by 7.3 % in real GDP after 6.6 % decline in 1997. The reduction of industrial activity led to a reduction of the sector to GDP from 35.5 % in 1997 to 31.7% in 1998. The share of agriculture to GDP declined by 2.1 % to 16 % while the share of services increased from 33.2 % to 37.8 %.

GDP per capita is estimated to be US \$1,697 in 1998.

Retail sales as share in GDP (years 1992 -1998)					
	1992	1993	1994	1995	1996
Retail sales as share in GDP* (%)	27.82	26.78	26.85	30.83	32.58

\* computed based on values in current prices (retail sales / GDP)

#### 4.4 Household incomes and expenditures structure

Household expenditures structure (% of total) (years 1992 -1998)	food	rent and household items	clothing	transport and telecommunications	health	education and culture	other (what)
1995	57.4	18.1	9.9	6.1	1.6	3.3	3.6
1996	57.6	19.5	9.1	5.2	1.8	3.0	3.8

About 42 % of household incomes in Romania come from salaries (bonuses and benefits are included), about 30 % - from equivalent value of consumption of agricultural products from own resources, 15.6 % - from social payments, 5 % - from sales of goods, land, buildings, 3.7 % - from own-account activity, and 0.4 % - from other activities.

#### 4.5 Foreign trade

##### Trade flows between Romania and other Balkan countries

(million USD)

	1992	1993	1994	1995	1996
<b>Greece</b>					
<b>export</b>	116	84	141	205	177
<b>import</b>	75	69	89	158	186
<b>Albania</b>					
<b>export</b>	2	3	5	7	23
<b>import</b>	*	*	*	*	13
<b>Bulgaria</b>					
<b>export</b>	116	103	103	71	71

<b>import</b>	89	71	65	77	73
<b>Bosnia-Herzegovina</b>					
<b>export</b>	49	7	*	1	3
<b>import</b>	22	15	*	*	1
<b>Croatia</b>					
<b>export</b>	4	4	9	10	14
<b>import</b>	2	4	1	3	4
<b>FYR Macedonia</b>					
<b>export</b>	20	19	27	38	10
<b>import</b>	11	19	20	20	4
<b>Yugoslavia</b>					
<b>export</b>	131	8	20	31	137
<b>import</b>	124	*	*	*	31
<b>Turkey</b>					
<b>export</b>	219	277	251	348	390
<b>import</b>	176	147	151	251	219

\* magnitude less than 0.5

In 1996 the total Romania`s exports amounted US \$8,060 million, of which US \$825 million (10,23 %) was directed to Balkan countries.

About 2/3 of Romania`s export in 1998 was directed to OECD countries. 65 % of the export was directed to European Union, 4.4 % - to CEFTA, and about 3 % - to Russia. For the same period 57.6 % of total import came from European Union. Among Romania`s principal trading partners are Italy, Germany, France, Turkey, etc.

## 5. Employment

### 5.1. Distribution by age, qualification, branches, ethnic groups

Employment by branch in 1996 (thou persons)

<b>Total</b>	Of which:	Industry	Construction	Trade	Transport	Education	Health and social assistance	Other
<i>private sector</i>	<i>private sector</i>	<i>private sector</i>	<i>private sector</i>	<i>private sector</i>	<i>private sector</i>	<i>private sector</i>	<i>private sector</i>	
9379	3249	2741	475	772	448	441	337	373
- 4828	- 3000	- 604	- 282	- 582	-98	-10	- 4	-170

\* incl. electric and thermal energy, gas and water

In 1997 employees in the public sector was 41.2 % of total number while private sector employed 53 % of all employees in the country. For comparison in 1993 this proportion was 51.6 % employees in public sector and 43.7 % - in private sector.

#### *Structure of employment by age groups and level of education, in 1996*

Education	Total	Age group				
		15-24	25-34	35-49	50-64	65 and over
Total	100.0	100.0	100.0	100.0	100.0	100.0
Higher education	8.1	1.2	9.4	11.7	8.1	1.0

Specialty post-high school or foremen education	4.7	2.3	2.9	7.5	5.1	0.4
High school	29.8	46.0	51.9	26.8	8.4	2.0
Vocational or apprenticeship	21.0	22.5	26.0	27.6	9.7	1.9
Secondary school	20.9	23.5	8.4	21.0	30.6	29.4
Primary or without graduated school	15.5	4.5	1.4	5.4	38.1	65.3

## 6. Infrastructure

The roads, production and transmission of electricity, and gas transmission are public monopolies.

The country has well developed infrastructure. With area of 238,391 sq.km Romania has total public roads length 72859 km which means density per 100 sq. km =30.6. The country has 2 port on the Black Sea, 11 ports on the Danube, and 18 airports.

There is 13.04 telephone posts per 100 people

Romania recorded surplus in electricity which is due mainly to decline in economic activity in the country.

The gas volumes transmitted in Romania come from own production and from Russia

### 6.3. Plans for privatization

In November 1998 35 % stake in telephone company Romtelecom was privatized.

The government plans to prepare Romania's utilities (production and transmission of electricity and gas transmission) for privatization over the course of 1999.

### 6.4. Priority transit corridors

Corridor IV, Corridor VII (Danube), Corridor IX

## 7. Investments

### 7.1. Domestic investment

Government's investment program intentions (planned public investments for coming 1-3 years) include road infrastructure(rehabilitation of the roads, modernization of railways), development of energy system, dwellings, water network etc.

### 7.2. Foreign investment (incl. - from Balkan countries) in USD (years 1992-1998)

As of July 1998: Total foreign investment was **3,360,849.5** thousand USD (\$3.36 bill.)

of which Balkan countries:

Turkey: \$161,583.6 thou (4.8%)

Croatia: \$142.8 thou

Greece: \$80,692.4 thou (2.4%)

Bosnia-Herzegovina: \$91.6 thou

Yugoslavia: \$17,004.0 thou (0.5%)

Albania: \$73.2 thou

Bulgaria: \$7,992.3 thou (0.2%)

Slovenia: \$60.9 thou

Serbia & Montenegro: 211.3 thou \$

Macedonia: \$45.8 thou

## 8. Institutional

In Romania property registers are centralized and based on property.

Bankruptcy procedures last over 18 months average and is rarely used. Bankruptcy procedures for banks last even longer - over 24 months and that's why is rarely used, too.

Estimated time necessary to collect claims via court is over 18 months and application is bad.

In the field of public procurement there is wide use of open tenders, but application is estimated as unfair. In Romania is observed political influence in deciding winners concerning tender procedure. There also is political protection in privatization and in access to subsidies.

## **9. Banking System**

The two-tier banking system was formally established in March 1991. The major feature of the banking system is predominance of state-owned banks with high debt burdens. The banking system currently includes over 40 fully operational banks, including the representative offices of several major foreign banks. In Romania operates branches of the following international banks: Societe Generale, ING Bank, ABN AMRO, Raiffeisen Bank, BNP Dresdner Bank, Daewoo Bank, Frankfurt Bukarest, Bank, Banque Franco-Roumaine, GE, Citibank (Chase Manhattan Bank is leaving). Concerning banks from Balkan countries there is presence of Greeks and Turkish banks only.

## **10. Political aspects**

Romania is a constitutional republic with a multiparty parliamentary system.

During the last 10 years Romania was ruled by 5 governments. Current government is center right coalition comprising Democratic Convention, Social Democratic Union, and Hungarian Democratic Union. The latest is an ethnic party of Hungarian. There also exists ethnic party of Roma ethnicity.

Average duration of political crisis experienced during past several years was 1 month.

## **II. Comments and conclusions**

### 1. General

Romania is a country with 5 ethnic groups- 89.4% of population are Romanians, 7.1 % - Hungarians. The others ethnic groups include Germans-0.5%; Ukrainians-0.3%; Jews-0.04%. There is no signs that Romania would face ethnic problems and related civil disturbances in near future.

Romania has territorial claims against Ukraine but significant problems is not likely to occur in near future.

The age structure of Romania's population shows availability of comparatively large labor force. The labor force is well skilled, 8.1 % of employees are with higher education, and 29.8 % are graduated high school. The cost of labor is low.

Romania has a favorable geographic position at the crossroads of Europe and Asia. The country is becoming one of the most significant business transportation areas in Central and Southern Europe. At the same time only 4,500 km of total 72,859 km public roads are classified as European-class roads and only 113 km are motorways. Considering the increased transport traffic flows the improvement of the conditions of the road network and restructuring railways is very important.

Romania has comparatively sufficient cross-boarding system but it has to be upgraded to ensure adequate flow of international road traffic. It is especially important for cross-border points between Romania and Bulgaria (1 bridge and 3 ferries).

### 2. Economic outlook

Romania is a country with one of the longest and most painful transition process among Balkan countries. Although most of the necessary legal framework (abolishment of most subsidies, adoption of contemporary tax legislation and tariff-based trade regime, prudential banking regulations, liberalization of most of the prices, etc.) and reform programs have been already adopted, Romania has to go long way of restructuring of the economy and establishment of real market economy.

After a period of visible progress (1994-1996) when **GDP** rose respectively by 3.5 %, 7.1 %, and 3.9 %, there was a reverse movement and in 1998 for second successive year Romania recorded decline

in real GDP which is estimated to be 7.3 % after 6.6 % contraction in 1997. Currently the economy is moving towards third year of contraction with 2 % forecast decrease of GDP. The reduction of industrial activity led to a reduction of the sector to GDP from 35.5 % in 1997 to 31.7% in 1998. The share of agriculture to GDP declined by 2.1 % to 16 % while the share of services increased from 33.2 % to 37.8 %.

Sectors which have prospects for future growth are:

- agriculture- the potential of the sector steams from Romania`s 10 million hectares arable land and excellent conditions for animal husbandry, as well as from government policy to support farmers through tax relief, attractive producer prices, etc.;
- food processing - the potential steams first from good potential of agriculture, and second, from the foreign investments and the large number of joint-ventures in this sector;
- services - although the standard of the sector are far below the European standards, there is a good potential for development in hotel and restaurant services and tourism.

The main problem of Romania`s economy is its **structural weakness**. Obstacles for achieving macrostability may be seen in existence of loss-making state-owned enterprises and a fragile, state-dominated banking system. **The state sector** still is predominant in Romania`s economy and accounts about 80 % of industrial production. At the same time most state-owned enterprises have antiquated, inefficient and energy-intensive assets and new investments are not been made from decades. Most of already privatized enterprises were sold to its management and employees which means that most of these enterprises might suffer lack of sufficient financing over next few years.

There is a tendency toward rapid growth in **private sector** activity. The total number of private enterprises in Romania increased by 664 % for the period 1990-1997 (from 76 277 in 1990 to 582 411 in 1997). A steady growth of private sector share of GDP is observed - from 26.4% in 1992 up to 58 % in 1997. About 98 % of small trade and service business are privately owned. Private sector activity is increasing also in construction and agribusiness. In 1997 employees in private sector was 53 % of all employees in the country. The main problem concerning the future development of the private sector is its small potential for generation of sufficient investment capital. The state still owns the main stake of productive resources in the country and provides more than half of the total public investments (in 1996 investments of public sector was 51 % versus 39.7 % of the private sector). The worsening economy affect SMEs sector and especially the ability of the companies to service their debt. As a result the amount of non-performing loans in the banks has increased substantially and thus threaten the stability of the banking system.

Another problem for Romania`s economy is an expanding **trade deficit**. There is a strong tendency toward reduction of the export. In 1998 import rose by 4,8 % while export fell by 1.6 % . The current account deficit in 1998 is estimated to be 7.7 % of GDP.

Romania has sought association with the EU and the European Free Trade Association (EFTA). 65 % of the country`s export in 1998 was directed to EU. Among Balkan countries main Romania`s trading partners are Turkey, Greece, Bulgaria and Yugoslavia (although there was temporary contraction of trade flows in 1993-1995 due to the embargo).

The foreign trade is expected to be the most affected sector by Kosovo`s crisis. As a whole direct trade links with the Balkan countries are small but the interruption of navigation on the Danube, which is one of the main routes for trade with EU and Central European countries will has a negative impact on the external trade. The alternative routes are longer which will rise the transportation cost.

On other hand Romania might benefit indirectly from intensified transit flows through the country.

Another reason for the Romania`s **vulnerable external position** is the large debt service payments. Official foreign currency reserves ( US \$ 1.24 bn by end-March 1999 versus US \$2.3 bn at the end of 1998) are able to cover only 30 % of the projected current account deficit. It is anticipated that even if Romania manage to receive financial support from international financial institutions and private-sector creditors, the reserves will cover up to 50 % of the external financing gap in the years ahead<sup>2</sup>.

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<sup>2</sup> According to Standard & Poor`s analysis

Given the downgrading country's credit rating there is obvious that Romania is going to have difficult access to the international capital market. That's why the privatization revenues is going to become very important. After the visible progress in privatization in 1998, in 1999 planned revenues from privatization (including committed investments) are US \$1.8 bn. **The privatization program** envisage 3,626 companies to be sold , 535 of them are large, and the rest are SMEs. The sale of the oil company Petrom could be implemented via public offer by the end of 1999. The rest of the telecom company Romtelecom (35 % was sold to the Greek telecoms company OTE) will be sold in annual tranches over the next three years. The government declared its intend to prepare for Romania's utilities in 1999.

Total **foreign investment** by July 1998 was US \$3.36 bn. 4.8 % of them came from Turkey, and 2.4 % - from Greece. Main part of these Greek and Turkish investments were directed to the banking system. It is expected that one of the results from eventual long-lasting crisis in Kosovo would have negative impact on foreign direct investment inflows.

Although there are more than 40 **banks** operating in Romania, four major state-owned banks still are dominating. These banks are heavy burdened by non-performing loans which resulted from the pre-1997 policy requiring banks to extend low-interest loans to agricultural and energy sector, as well as from general economic collapse which have negative effect on firm's capacity to service their loans. Currently the banking sector is fragile, credit activity is seriously contracted, banks demand high collateral and charge wide margins. There is no serious experience in risk management and assessment. After years of delay bank privatization started finally in March 1999 with the sale of a controlling stake in the Romanian Development bank to Societe Generale.

The government still plays active role in the economy. In Romania is observed political influence in deciding winners concerning procurement procedure. There also is political protection in privatization and in access to subsidies. There are complains of corruption of all level of government. **Corruption** might constitute actual business risk.

Given the long track record of political instability and political infighting it is not reliable whether governing coalition will keep up the pace of reforms. Restructuring of the economy and liquidation of loss-making state-owned enterprises is connected with painful mass lay-offs which makes them politically difficult. There are parliamentary and presidential elections scheduled by November 2000 and this causes an uncertainty whether the government will implement unpopular economic measures which would probably diminish their chances to win elections next year.