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December 23, 1983

To: Members of the Executive Board

From: The Acting Secretary

Subject: Romania - Staff Report for Review Under Stand-By Arrangement and Request for Waivers

Attached for consideration by Executive Directors is a paper on a review under the stand-by arrangement for Romania. A draft decision appears on page 14.

It is proposed that this subject be brought to the agenda for discussion on Monday, January 23, 1984.

If Executive Directors have technical or factual questions relating to this paper prior to the Board discussion, they should contact Mr. Brehmer (ext. 77062) or Mr. Prust (ext. 74872) or Mr. Reitmaier (ext. (5)7186).

Att: (1)

CONFIDENTIAL

INTERNATIONAL MONETARY FUND

ROMANIA

Staff Report for Review under Stand-by Arrangement and Request for Waivers

Prepared by the European Department and the Exchange and Trade Relations Department

(In consultation with Legal and Treasurer's Departments)

Approved by L.A. Whittome and S. Kanesa-Thasan

December 23, 1983

I. Introduction

A staff team consisting of Messrs. Brehmer and Prust, (both EUR), met with a Romanian delegation, headed by Mr. Marin of the Ministry of Finance, in London, December 6-8, 1983 to continue discussions related to a review under the stand-by arrangement. This review was continued in Washington from December 11-17, 1983, when the above Fund team was joined by Mr. Reitmaier (EUR) and Ms. Puckahtikom (ETR). Understandings were reached on all areas under the two reviews referred to in paragraph 3(b) of the March 1983 Executive Board Decision No. 7375-(83/56), namely the magnitude and timetable for policy actions designed to further rationalize the structure of relative prices on the basis of four joint studies--exchange rate policy, interest rates, the costing of capital, and energy prices (Appendix II).

The current three-year stand-by arrangement for Romania was approved by the Executive Board on June 15, 1981 (EBS/81/111, 6/1/81) in an amount of SDR 1,102.5 million, equivalent to 300 percent of (old) quota of SDR 367.5 million (Table 1). Romania has so far made five purchases under the arrangement for a total of SDR 633.9 million (172 percent of old quota, or 121 percent of new quota). During the December 1982 Executive Board review it was decided to limit total purchases by Romania in 1983 to SDR 367.5 million (100 percent of old quota). Of this total, approval was given for the purchase of SDR 92 million (25 percent of old quota) at the Board Review on March 30, 1983 (EBS/83/54, 3/8/83). The second purchase of SDR 91.9 million was approved on June 24, 1983 (EBS/83/128, 6/21/83) after the Board decided that satisfactory arrangements had been made for the 1983 debt rescheduling, Romania having met all the performance criteria in the first quarter of 1983 (Table 2).

The remaining two purchases under the 1983 program, totaling SDR 183.6 million, are inter alia conditional upon the completion of two reviews by the Fund. In the attached letter to the Managing Director, the Minister of Finance sets out the Romanian authorities' economic policy intentions in the fields covered by these reviews. Despite extensive discussions, agreement on the outstanding issues was not reached until December 17, 1983. This date made it impossible for the Executive Board to consider the Romanian request for a drawing of the remaining two purchases under the 1983 program in December 1983 without extreme compression of the normal timetable for the preparation of the Staff Report and for Board consideration of it to an extent which would have been unjustifiable. To allow the Romanian request to be considered on a normal timetable and also because no new agreed 1984 program can be put in place for several months, the Romanian authorities have requested a waiver of paragraph 3(c) of the March 1983 Executive Board Decision No. 7375-(83/56, 3/30/83), which precludes purchases in 1984 until a program is approved for the remainder of the stand-by period in that year. Specifically, they have requested that they be permitted to purchase the two remaining tranches originally phased for 1983 without an agreed program for 1984.

The release of the two remaining purchases under the 1983 program is also conditional upon the observance of the performance criteria under the 1983 program. Romania has met all quantitative performance criteria in the second and third quarters of 1983 (Table 2). For the remaining two purchases to be released, fulfillment of the performance criteria in the final quarter is also required. Since the last two purchases under the 1983 program cannot now take place in calendar 1983, the Romanian authorities expect that gross international reserves will rise by only US$55 million during 1983 rather than the targeted increase of US$250 million which was specified as a performance criterion. The Romanian authorities have also requested a waiver of this performance criterion.

The Romanian authorities do not believe that they will be able to introduce sufficient additional measures of structural price reform in the relatively short remaining period of the existing stand-by arrangement (ending June 14, 1984) to justify release of the undrawn amount of SDR 285 million. They therefore accepted the cancellation of the existing stand-by arrangement as of January 31, 1984 but expect to request a new stand-by at a later date. Since time is needed to study the effects of measures already taken, they do not expect a new stand-by arrangement to be in place before June 1, 1984.

If realized, the remaining two purchases under the 1983 program would bring total purchases under the current stand-by arrangement to 156 percent of new quota.

Romania has consented to an increase in its quota by 42.4 percent to SDR 523.4 million. As of December 19, 1983 the Fund's holdings of lei amounted to the equivalent of SDR 1,272 million or 346 percent of old quota, including holdings related to purchases under the compensatory financing facility (SDR 271 million or 74 percent of old quota) and under enlarged access (SDR 323 million or 88 percent of old quota).

Total gross disbursements by the World Bank to Romania in 1982 amounted to US$331 million and are projected by the Romanian authorities to be US$357 million in 1983. An IBRD economic mission that visited Romania in the spring of 1983 felt that overall the investment pattern was appropriate: the development of subsectors with relatively high value added per unit of output has been accelerated in the 1981-85 plan period, while the growth of subsectors with relatively low value added and energy-intensive production has been slowed. Recently the Government has requested a resumption of borrowing from the Bank. The Bank subsequently sent a senior level mission to Bucharest to explore a number of lending options. The mission indicated, however, that a resumption of lending would be contingent on agreement on debt reporting requirements and procurement procedures, and the provision of more information on the investment program and on other key areas of country and sector policy. Discussions on all these items are continuing.

II. Economic Developments and Prospects 1/

1. Developments in 1983 2/

a. The external sector

(1) Convertible currencies

The program target for the 1983 convertible current account surplus was US$800 million compared with a surplus of US$655 million in 1982 (Tables 4 and 5). The trade surplus was programmed to rise to US$1.6 billion. Developments in the first ten months of 1983 suggest that these targets are likely to be met: the authorities now expect the trade and current account surpluses to be above the program targets by US$50 million and US$70 million, respectively. However, the composition of the trade balance is likely to differ substantially from earlier expectations. The surplus on non-oil trade and the absolute levels of non-oil exports and imports will be significantly below program targets. Non-oil exports, originally expected to rise by 2 percent in U.S. dollar terms, are now expected by the authorities to decline by 9 percent. In the staff's view even the latter forecast may be somewhat optimistic as it assumes that average exports in the last two months of the year will be 38 percent above the monthly average in the first ten months. This is to be compared with an apparent decline in the monthly rate of non-oil exports in the course of 1983. The monthly average in the first half was US$355 million, but perhaps due to seasonal factors, fell to only US$309 million in the ensuing four months. The Romanian authorities said

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1/ Supplementary information on economic developments will be provided in January 1984.

2/ For a fuller description of developments and policy actions in the first half of 1983 see the staff report for the 1983 Article IV Consultation, SM/83/173 (August 5, 1983) and SM/83/173, Supplement 1 (September 12, 1983).

that the poor performance of non-oil exports was fairly generally spread across commodity groups and was, in their opinion, to a large extent attributable to weak foreign demand. A loss of competitiveness also played a role, as did, the staff would suspect, a shortage of imported inputs essential to export industries. Moreover, the appreciation of the U.S. dollar against other major currencies has served to depress the dollar value of exports.

The poor performance of non-oil exports in 1983 is likely to be partially offset by a smaller deficit on oil trade (US$300 million compared with a program target of US$500 million) largely on account of lower crude oil imports for domestic use. Nevertheless, achievement of the trade balance target will imply considerably slower growth in non-oil imports than earlier envisaged. The authorities now project that these will rise by only 4.5 percent as compared with the targeted increase of over 20 percent. They claimed that the low growth in non-oil imports had not had a significant adverse effect on the domestic economy because the good 1982 harvest had allowed imports of foodstuffs and agricultural items to be reduced and because of efficiency gains which had led to lower requirements for imported raw materials and other inputs. The revised target for imports implies an unrealistically sharp pick up in the monthly rate of imports in the final two months of the year. This will only be consistent with the trade balance objective, if a similar pickup for non-oil exports is also realized. The 1983 deficit on services account, estimated at US$780 million, will be in line with the program but about US$100 million lower than in 1982 because of lower interest payments abroad and higher receipts from tourism.

A net capital outflow of US$874 million is now officially forecast for 1983 compared with a net inflow of US$117 million in 1982. 1/ This is about US$70 million higher than originally expected. While net outflows on medium and long term account are now estimated to be lower than

1/ The major part of this turnaround, which was anticipated in the program, is attributable to developments on medium and long term account. Inflows on this account in 1982 included imputed receipts related to the rescheduling of arrears of the order of US$750 million, compared with a corresponding amount of about only US$100 million in 1983. There was also an increase in the net outflow of short term capital. This was mainly the result of a sharp drop of about US$400 million in new short term credits received, primarily related to oil trade. In addition, short term credit receipts in 1982 included imputed inflows of about US$400 million relating mainly to the postponement to early 1983 of downpayments due under the 1982 rescheduling agreements; the corresponding amount in 1983 is estimated to be some US$250 million less. The above factors are partially offset by an estimated reduction of some US$260 million in net short term credit extended by Romanian exporters between 1982 and 1983.

expected, the forecast for net short term outflows are over US$200 million larger. The latter partly reflects a shortfall of about US$80 million in receipts of new credits. In addition, net credit extension by Romanian exporters is now expected to be US$90 million compared with an originally foreseen net inflow for this item of about US$30 million.

The authorities anticipate an overall balance of close to zero as programmed. Purchases from the Fund will be some US$200 million less than previously anticipated with the result that there will be a corresponding shortfall from the targeted reserve increase of some US$250 million. The authorities now expect reserves to rise by only US$55 million to reach US$645 million equivalent to less than two months' imports from the convertible area.

(2) Nonconvertible currencies

The Romanian authorities had expected to record a deficit with the nonconvertible area in 1983 on both the trade and the current account. This objective is now out of reach but they expect to reduce significantly the surpluses on both merchandise trade account (from US$289 million to US$50 million) and the current account (from US$385 million to US$95 million) in 1983. Exports are expected to be virtually unchanged compared with a forecast increase of 11 percent. Imports are still expected to rise, but by only 4 percent compared with 20 percent originally anticipated. In the first three quarters of 1983 the merchandise trade balance with the nonconvertible area was in considerable surplus of almost US$150 million, largely on account of trade with CMEA countries.

b. The domestic economy

At the beginning of the year GNP was officially forecast to rise by 3.8 percent in real terms in 1983. Gross industrial and agricultural output were forecast to rise by 3.5 percent and about 5.5 percent, respectively. These forecasts have not been officially revised although the Romanian authorities now accept that some shortfall from the overall growth target is likely and that the real GNP growth rate may be closer to 3 percent, or about the same as in 1982. As a result of the very low levels of precipitation in 1983, agricultural output is now expected by the authorities to be approximately unchanged from the previous year with higher output of animal products, fruits, and vegetables compensating for significant declines in the spring cereal harvests. Industrial output, on the other hand, is expected to increase by about 5 percent in real terms which is in line with the results recorded for the first three quarters (Table 7).

The staff believes that official expectations concerning the growth in total domestic output in 1983 may still be over-optimistic. For the agricultural sector, in which exceptionally good results for many items were recorded in 1982, 1983 seems to have been an exceptionally bad year for certain major crops because of the drought. Thus, notwithstanding increases in the area under irrigation and other improvements in production techniques, it would not be surprising if agricultural output had in fact fallen in 1983. Regarding industrial performance, the staff finds the rapid rate of output growth somewhat surprising in view of the substantial shortfall from targets for overall imports (both from the convertible and nonconvertible areas). The authorities' revised trade forecasts imply a slight fall in total imports in dollar terms compared with an originally expected rise of about 13 percent. However, the authorities argue that changes in the mix of production and in production techniques have led to substantial economies in the use of imported inputs.

The staff considers that the picture presented by the authorities of macroeconomic developments in 1983 also raises some questions. If the official forecasts for the balance of payments both in convertible and nonconvertible currencies are realized, net exports will change little from 1982. Data for the first three quarters of 1983 (Table 7) show the main components of domestic demand as having either fallen somewhat (investment) or risen only slightly (household consumption). The combination of rising output and virtually unchanged final demand seems to imply an accumulation of stocks that could, in the staff's view, be implausibly large.

Financial policies have been tight in 1983. Revised estimates suggest a fall of 5.4 percent in budgetary expenditure. Some of the allocation to the reserve (contingency) fund has been spent, contrary to initial expectations, and the actual decline in total expenditure will as a result be somewhat less than the 9 percent originally planned. Revenues appear likely to be close to the original budget targets and are expected to decline by 7.5 percent. The overall budget surplus is now projected at about lei 13 billion compared with the earlier estimate of lei 20 billion and a surplus of lei 20 billion or 2.7 percent of GNP in 1982.

The 1983 program targets were for growth in the net domestic assets and liquid liabilities of the banking system to be limited to 7 percent and 2 percent, respectively. These targets appear likely to be achieved. Net domestic assets declined in the first three quarters of 1983 and, at end-September 1983, were about 6 percent above their level of one year earlier. Liquid liabilities of the banking system were approximately unchanged in the first three quarters of 1983. Enterprise deposits fell by about 7 percent, in line with the policy of eliminating excess liquidity of the enterprise sector, and household savings deposits grew only marginally.

2. Prospects for 1984 and beyond 1/

The authorities expect an approximately unchanged surplus in the current account of the convertible balance of payments in 1984 of US$900

1/ For a fuller discussion of the medium term outlook see page 9 and Table 8 of SM/83/173, 8/5/83.

million. The decline in exports in evidence since 1981 is expected to be reversed with non-oil exports rising by about 9 percent. The oil balance is expected to show no change from 1983. The more buoyant performance expected from the export sector would thus permit substantial growth in non-oil imports of about 15 percent, thereby reversing the trend established since 1980.

The convertible capital account is expected to show a deficit of about US$950 million, only slightly larger than in 1983. The authorities do not intend to seek any debt rescheduling in 1984 and are assuming only a modest increase in new capital inflows. A sharp change in the composition of the overall capital balance is forecast as between the medium- and long-term account and the short-term account. Net outflows on the former are forecast to rise by about US$900 million, largely reflecting the absence of debt rescheduling. New medium and long term capital inflows are expected to fall somewhat with lower disbursements from the World Bank being only partially offset by higher borrowing from other sources. Almost all of the latter increase is expected to be related to the construction of a nuclear power plant. By contrast the short term account is forecast to move from a net deficit of US$750 million in 1983 to a small surplus in 1984. There are three main reasons for this sharp change. First, as already explained, a large part (about US$400 million) of the short term outflows in 1983 was accounted for by downpayments under the previous year's rescheduling agreement; the corresponding figure for 1984 will only be about US$100 million. Secondly, new short term borrowing (largely trade-related) is forecast to rise by US$130 million to US$300 million. Thirdly, a net repayment of credit extended by Romanian exporters of about US$70 million is forecast, compared with a net outflow for this item of US$90 million now foreseen for 1983.

In the staff's view, export competitiveness will be a key factor governing the attainability of the official balance of payments forecast for 1984. Similarly, sustained export growth will be necessary to ensure simultaneous achievement in the medium term of an orderly servicing of the external debt and a satisfactory rate of economic growth. It is essential to avoid a vicious circle in which declining exports lead to corresponding falls in imports thereby exacerbating supply constraints in the domestic economy. The forecast for non-oil export growth in 1984 is consistent with Romania's maintaining its share broadly unchanged in export markets. While in itself not overambitious, this target has to be seen in relation to the substantial decline in market shares that occurred in 1982 and 1983. The policy measures scheduled for January 1, 1984, particularly the devaluation, should facilitate achievement of the target. The authorities are also placing considerable emphasis on the role of efficiency improvements in restoring competitiveness, but in the staff's view it would be unrealistic to expect a major impact in the short run from such measures alone.

The current account of the nonconvertible balance of payments is officially projected to show a deficit in 1984 following a small surplus in 1983 (Table 3). Thus, the level of total net exports of goods and services, both to the convertible and nonconvertible area, is expected to be little changed for the second consecutive year.

The authorities are projecting a rapid rate of increase in real GNP of 7 percent largely on the basis of productivity improvements. In the staff's view, this is an extremely ambitious target.

III. Economic Policy Measures Under the 1983 Program

In the first half of 1983, the Romanian authorities introduced a number of policy actions, particularly in the field of exchange rate policy. The commercial exchange rate was depreciated by a total of 14 percent in two stages, on January 1 and July 1. On the latter date the remaining special rates for certain exports were abolished and a unified commercial exchange rate was established. By July 1983, the effective exchange rate of the leu (weighted by the non-oil trade pattern) had depreciated by 6.8 percent in nominal terms and by some 9 percent in real terms compared with the end-1982 position (Table 6). Also on July 1, 1983 the leu was pegged to a basket of the six currencies of Romania's main trading partners in the convertible area rather than to the U.S. dollar as previously; subsequently rates for the dollar and other currencies have been adjusted at least weekly to maintain the nominal value of the leu in terms of the basket. The authorities have also been adjusting the noncommercial rate so as to preserve an approximately constant spread of lei 4 per U.S. dollar between it and the commercial rate. Other measures introduced in 1983 include increases of 3 percentage points and 1 percentage point in lending and deposit rates of interest, respectively, on January 1; increases in the price of natural gas on July 1 and October 1 amounting cumulatively to 50 percent; and a doubling in the domestic producer price of crude oil at the beginning of 1983.

The authorities have also introduced certain largely administrative measures to improve labor productivity by linking earnings more closely to plan fulfillment and to encourage greater efficiency in the use of energy and other scarce inputs, particularly those that are imported. The latter will, inter alia, involve a revision of production "norms" governing the permitted level of input use for a given quantity of output and changes in the investment pattern, the production mix and production techniques. The authorities are also placing increased emphasis on quality control.

The staff and Romanian authorities have jointly carried out four studies in 1983 to determine what further actions were necessary in the fields of the exchange rate, interest rates, the costing of capital, and energy pricing. It was originally intended that the first three of these studies would be completed by mid-1983 with actions on interest rates and the exchange rate to be effected by July 1, 1983 and October 1, 1983, respectively. Completion of the study of energy pricing was expected by November 1983 with action on this and on further measures related to the costing of capital to take place in 1984. Since understandings on actions in the fields of the studies could not be obtained until December 17, 1983, it was not possible to adhere to this timetable and no policy measures in any of these areas are to be taken before January 1, 1984.

1. The exchange rate

On January 1, 1984, the commercial rate will be devalued by 15 percent against the basket. At the present rate of exchange, (lei 18.2 = US$1 on December 12, 1983) this would imply a move to lei 21.4 = US$1. Thereafter the authorities intend to continue the current practice of maintaining the value of the leu constant in terms of the official Romanian currency basket. The authorities consider that a corresponding adjustment of the more appreciated noncommercial rate would not be appropriate at the present time. They have an earlier commitment to unify the commercial and noncommercial rates by July 1, 1984.

The move proposed by the authorities for the commercial rate for January 1, 1984 will substantially offset the real effective appreciation that has occurred since the major exchange rate realignment at the beginning of 1981. However, the results of the real effective exchange rate calculations need to be interpreted with great caution because of limitations on the reliability of the data and some doubt about the relevance of the analytic techniques themselves. One complication is that the price indices (available only once a year) do not fully reflect market conditions. If the devaluation is to have its maximum effect it will be essential for the authorities to ensure, as they have agreed to do, a rapid and full pass-through of its effects to final prices for traded goods.

2. Interest rates

The authorities intend to raise interest rates on "normal" bank lending (i.e., bank loans other than special and overdue credits) and on enterprise deposits by 2 percentage points on January 1, 1984. The average bank lending rate for normal purposes will then be about 8.5 percent; lending rates on normal credits to the important industrial sector other than investment credits would be 10 percent. After the increases take effect, interest rates on enterprise deposits will range from 3.5 percent to 5 percent depending on maturity. The objective of these adjustments is to achieve a structure of interest rates which is broadly positive in real terms. The new structure of interest rates is to be compared with an officially estimated average rate of price increase in 1983 of 5-7 percent. The staff believes that a similar figure is in prospect for 1984 if price reform measures are fully reflected in the prices of final goods. It will be important for the authorities to keep the level of interest rates under close review and to be prepared to make adjustments more flexibly than in the past.

3. Costing of capital

The authorities intend to complement the above interest rate adjustments by two other moves to ensure a more realistic pricing of capital. First, there is to be a general shortening of depreciation periods on fixed assets so as to bring Romanian practices more into line with those of other industrial countries and to induce a more rapid modernization of the capital stock. The authorities intend to start this process on January 1, 1984 when depreciation periods will be shortened for equipment used in the important machine building industry. It is estimated that the effect of the proposed changes will be to raise this sector's annual depreciation charges by about 15 percent, or about lei 4 billion. Schedules for other sectors will be revised in the course of 1984 and 1985. The authorities estimate that the total effect of the changes to be introduced over these two years will be to raise depreciation charges by about 10 percent or lei 7-8 billion at an annual rate.

Also on January 1, 1984 the authorities will introduce a capital charge on the unamortized amount of new investment financing provided from the budget. This charge will operate as a surrogate interest rate on such financing and will be a source of budget revenue. Hitherto budgetary investment financing has been interest free. The charge will be set at the beginning of each year at levels comparable with prevailing interest rates on "normal" bank loans to economic units for investment purposes. For 1984 the charge will be set at 7 percent. The purpose of this measure is to ensure that the cost of investment financing is broadly identical as between all sources of funds and all categories of borrower. The introduction of these charges and the changes in interest rates and depreciation schedules will necessarily affect industrial costs and will be fully reflected in the prices of final products.

4. Energy pricing

As described above, the authorities introduced various increases in energy prices in 1983. At the beginning of 1984 the domestic producer price of crude oil is to be increased from lei 1,100 per ton to lei 1,750 per ton; the authorities had previously planned an increase to lei 1,650 per ton on January 1, 1984. This price will be further increased to lei 2,000 per ton by July 1, 1984. These measures are intended to encourage domestic production and to reduce the gap which now exists between the world price for crude oil and the domestic producer price. The latter is currently equivalent to no more than 30 percent of the world price. This ratio would rise to some 50 percent by July 1, 1984 at prevailing exchange rates and constant world prices. The proposed increases in the crude oil producer price are also intended to forestall a reduction in the delivery price of crude oil to refineries that would otherwise have resulted from the declining relative importance of imported oil for domestic use: the delivery price is determined as a weighted average of the prices of domestically produced and imported oil.

The authorities do not at the present time intend to introduce any further increases in the price of natural gas pending further consideration of the substitutability of gas for other fuels and its implications for pricing. They note that the price of natural gas has been increased many-fold in recent years, including an increase of 50 percent in 1983 alone. Neither do the authorities intend to raise the final sales prices of refined petroleum products in the immediate future. These were last adjusted in mid-1982. On available information, the staff estimates that these prices are in the lower range of comparable prices abroad. Thus, for the time being, a major instrument for achieving further energy conservation will continue to be the administrative measures described earlier.

IV. Staff Appraisal and Proposed Decision

In the past few years Romania has followed policies that have contributed to a very major turn-around in the convertible current account. This process continued in 1983 with tight financial policies, continuing wage restraint, and the adoption of a series of important measures designed to improve the way the economy functions (two devaluations, full unification of the commercial rate of exchange, pegging of the leu to a basket of currencies, an increase in interest rates, and substantial increases in energy prices). However, at the time of the last Executive Board meeting on Romania in September 1983 the staff expressed the view that more needed to be done in view of the continued fall of non-oil exports in 1983 and the associated shift of the adjustment burden to undue import restraint with adverse implications for economic growth. This view has been reinforced by recent developments in the convertible current account which have not shown any shift to a more viable position, for the decline in exports may even have accelerated. In assessing the marked improvement recorded in the current account of the convertible balance of payments, the striking feature is the very sharp decline in imports. Certainly, some room, perhaps considerable, may have been available to save on the use of imported inputs by a more efficient allocation of resources. However, despite a rundown of stocks of imported inputs, it is difficult, in the staff's opinion, to avoid the conclusion that the compression of imports must have put severe strains on the economy. In consequence it is vital to increase exports so that these strains can be somewhat alleviated.

Against this background, the preponderant view expressed at the September 1983 Board meeting was that the staff should come to an understanding with the Romanian authorities, as soon as practicable, on the measures required to release the remaining two purchases under the 1983 program (SDR 183.6 million or 50 percent of old quota). This understanding was to include prompt implementation of further policy action, particularly regarding the exchange rate and interest rates. However, despite extensive discussions, understandings on the outstanding issues were not reached until December 17, 1983, a date that did not allow adequate time for the preparation of papers and their consideration by the Executive Board which would have permitted the release of the two purchases before the end of December 1983. The staff recommends a waiver of paragraph 3(c) of the March 1983 decision stipulating that no purchases could be made after December 31, 1983 without the establishment of performance criteria for 1984.

Since the remaining two purchases under the 1983 program cannot now take place in 1983, Romania will not be able to fulfill its commitment to increase gross international reserves in 1983 by US$250 million, which is a performance criterion. In the staff's opinion a waiver of this performance criterion would be appropriate.

The Romanian authorities believe that more time is needed to study the effects of the structural price reform measures, particularly those of the devaluation, before seeking to determine what further measures might be necessary. The present stand-by arrangement ends on June 14, 1984, which leaves insufficient time for these matters to be adequately considered. The staff notes the decision of the Romanian authorities to cancel the current stand-by arrangement as of January 31, 1984 and the Romanian authorities' intention to request a new one-year stand-by arrangement which is not expected to be in place before June 1, 1984.

The package of measures proposed by the Romanian authorities, in the staff's view, represents a significant effort in the present circumstances. An important ingredient of this package is the 15 percent devaluation vis-à-vis the basket of currencies scheduled for January 1, 1984. This measure, originally to have been introduced on October 1, 1983, will complement the two devaluations in 1983, substantially offsetting the real effective appreciation of the leu that occurred in the last three years. It should help to reverse the decline in convertible non-oil exports and in Romania's share of export markets, and strengthen the confidence of foreign creditors. It will also support the recently adopted program for improving efficiency in industry and in product quality, the effects of which, in the staff's view, can only be modest in the short run. However, for the devaluation to be effective it is vital that its effect on prices of imports from the convertible area be fully and immediately passed on to domestic consumer and producer prices and its financial incentive be given in full and immediately to exporters to the convertible area. This is especially important in the centrally planned Romanian economy, where no market mechanism exists to assure that these effects are passed on automatically. It is also important that plan targets for exports (so far expressed in terms of local currency value rather than volume) are revised upward in line with the devaluation. With improved competitiveness, a revival of convertible non-oil exports and an associated increase in non-oil imports in 1984 should become feasible. The staff regrets that the devaluation of the commercial rate of the leu on January 1, 1984 will not be accompanied by a devaluation of the noncommercial rate (applied mainly to the relatively small services item of individual tourism), so that the present differential of lei 4 per

US$1 between the commercial and noncommercial rate of exchange will widen accordingly. It is important, in the staff's view, that the Romanian authorities fulfill their standing commitment to unify the commercial and noncommercial rate on July 1, 1984.

The package of economic policy measures also contains three steps designed to address the problem of underpricing of capital. The first is an increase in interest rates both for bank lending and enterprise deposits from January 1, 1984. According to staff estimates, at the new level the main lending rates would be at or just above the rate of price change implied by the full pass-through of the price reform measures. In judging whether interest rates are at real positive levels it should be borne in mind that the official price indices do not fully reflect the scarcity of supplies. The second step in the field of the costing of capital is the introduction on January 1, 1984 of a capital charge on the unamortized amount of new investment financed from the budget (which so far has been interest-free) at levels comparable with prevailing interest rates for investment credit. The third step is the shortening of depreciation periods for capital assets over a two year period starting from January 1, 1984 in order to bring Romanian practices in this regard more in line with those in other countries. For the above three measures to be effective, a full and immediate pass-through of their effects to consumer and producer prices is essential.

As regards energy pricing, it had been intended that the results of the study would be reviewed in November 1983 when a timetable for action would be established. As noted, however, by a number of Executive Directors at the September 1983 Board meeting, the technical issues in this field are very complex, which could warrant postponement of the final determination on some of these issues beyond the 1983 program. Following substantial increases in energy prices and the introduction of a range of non-price measures in recent years, Romania will make further increases in crude oil producer prices on January 1, 1984 (beyond the increase already agreed earlier) and again by July 1, 1984. These increases will reduce the gap between domestic and world market prices, which will however still remain considerable. While this will increase incentives for domestic oil production, there will be no consequent upward adjustment of final petroleum product prices, which are in the lower range of comparable prices abroad.

On balance, the staff considers that the package of measures, as described above, represents a significant adjustment effort toward achieving a viable balance of payments position. Accordingly, the staff recommends that Romania be permitted to purchase the amounts originally phased for purchase in 1983.

In view of the foregoing, the following draft decision is proposed for adoption by the Executive Board:

1. Romania has consulted with the Fund in accordance with paragraph 3 of Executive Board Decision No. 7375-(83/56), adopted March 30, 1983, (EBS/83/54 and paragraph 13 of the letter from the Minister of Finance of February 11, 1983 in order to review developments under its economic program and to reach understandings subject to which further purchases may be made under the stand-by arrangement approved by the Fund on June 15, 1981 (EBS/81/111, Sup. 1, June 17, 1981).

2. The attached letter from the Minister of Finance dated December 20, 1983, shall be annexed to the stand-by arrangement for Romania and the letter of February 11, 1983, shall be read as supplemented and modified by the letter of December 20, 1983.

3. The Fund decides, pursuant to paragraphs 3(b)(i) and 3(b)(ii) of Decision No. 7375-(83/56), that the respective reviews are completed.

4. The Fund decides, in view of the circumstances described in EBS/83/273 that Romania may proceed to make purchases under the stand-by arrangement, provided that cumulative purchases under the arrangement shall not exceed the equivalent of SDR 817.5 million through January 31, 1984.

5. In accordance with the request of the Romanian Government, the stand-by arrangement approved by the Fund on June 15, 1981 is to be cancelled s of January 31, 1984.

Table 1. Romania: Schedule of Purchases Under Stand-By Arrangement

	Amount Available				Purchases	
	Original plan 1/		Phasing in 1983			
	Millions of SDRs	Percent of old quota	Millions of SDRs	Percent of old quota	Millions of SDRs	Percent of old quota
June 15, 1981- June 14, 1982	367.5	(100.0)	...	...	140.0	(38.1)
June 15, 1982- June 14, 1983	367.5	(100.0)	...	...	402.0	(109.4)
June 15, 1983- June 14, 1984	367.5	(100.0)	...	...	275.5 2/	(75.0)
Calendar 1983	...	...	367.5 3/	(100.0)	183.9	(50.0)
During which:						
1st purchase	...	...	92.0 4/	(25.0)	92.0	(25.0)
2nd purchase	...	...	91.9 5/	(25.0)	91.9	(25.0)
3rd purchase	...	...	91.8 6/	(25.0)	...	...
4th purchase	...	...	91.8 6/	(25.0)	...	...
January 1984 (final purchase)	...	...	...	...	183.6 7/	(50.0)
Total	1,102.5	(300.0)	...	...	817.5 2/	(222.4)

Source: IMF, European Department.

1/ As set out in EBS/81/111 (6/1/81).
2/ Including purchase presently proposed.
3/ As set out in EBS/82/218 (11/24/82)
4/ As set out in EBS/83/54 (3/8/83); the purchase was made on April 15, 1983 following regularization of the remaining part of (nonguaranteed) arrears to suppliers owed until March 1, 1982.
5/ As set out in EBS/83/128 (6/21/83); the purchase was made on June 30, 1983 following satisfactory completion of debt rescheduling arrangements for 1983.
6/ As set out in EBS/83/128 (6/21/83); purchases were to be made in the second half of 1983 subject to the completion of two reviews relating to action under the four joint studies.
7/ Purchase presently proposed.

Table 2. Romania: Quantitative Criteria for the 1981, 1982, and 1983 Programs

	Dec. 1981	Dec. 1982 (a) 1/	Dec. 1982 (b) 2/	March 1983	June 1983	Sept. 1983	Dec. 1983
				(In billions of lei)			
Net domestic assets of the banking system							
Ceiling 3/	--	449	437	444	444	453	456
Actual 3/	413	...	435	435	432	437	...
Trade surplus in convertible currencies (cumulative)							
Floor	--	550	1,200	350	700	1,100	1,600
Actual	204	...	1,525	456	711	1,162	...
Gross international reserves in convertible currencies							
Floor	--	675	550	(587) 4/	(587) 4/	(687) 4/	837
Actual	550	...	587	622	675	708	...
Outstanding short-term debt in convertible currencies							
Ceiling	--	1,000	1,000	...	500	...	400 5/
Actual	643 6/	...	564 7/	...	442	...	...
New external debt in convertible currencies in a maturity range of 1-5 years (maximum)	...	...	...	...	...	...	500 5/

Sources: IMF, European Department; and data supplied by the Romanian authorities.

1/ According to the original 1982 program (see EBS/82/73, 4/29/82).
2/ According to the amended program (see EBS/82/218, 11/24/82).
3/ 1981 and 1982 data are based on the exchange rate of lei 15 = US$1; data for the ends of the first two quarters of 1983 are based on an exchange rate of lei 16.5 = US$1 and data for the last two quarters are based on an exchange rate of lei 17.5 = US$1.
4/ Indicative target.
5/ Excluding credits obtained to refinance any of US$370 million in nonguaranteed debts to large suppliers outstanding at end-1982.
6/ Excluding arrears of US$318 million on short-term credits.
7/ Excluding short-term credits arising from postponement to early 1983 of downpayments to banks (US$307 million).

Table 3. Romania: Balance of Payments Summary

(In millions of U.S. dollars)

	1980	1981	1982	Program forecast 1983	Official estimate 1983	Official forecast 1984
A. All currencies						
Exports, f.o.b.	11,024	12,367	11,559	12,500	11,400	12,400
Imports, f.o.b.	-12,685	-12,264	-9,745	-11,050	-9,700	-10,900
Trade balance	-1,661	103	1,814	1,450	1,700	1,500
Services balance	-759	-936	-774	-716	-735	-720
Current balance	-2,420	-833	1,040	734	965	780
Capital balance	2,222	-533	-226	-789	-914	-877
Overall balance	-198	-1,366	851	-55	51	-97
B. Convertible currencies						
Exports, f.o.b.	6,503	7,216	6,235	6,600	6,100	6,600
Imports, f.o.b.	-8,037	-7,012	-4,710	-5,000	-4,450	-4,900
Trade balance	-1,534	204	1,525	1,600	1,650	1,700
Services balance	-865	-1,022	-870	-800	-780	-800
Current balance	-2,399	-818	655	800	870	900
Capital balance	2,154	-570	117	-804	-874	-952
Overall balance	-245	-1,388	807	-4	-4	-52
C. Nonconvertible currencies						
Exports, f.o.b.	4,521	5,151	5,324	5,900	5,300	5,800
Imports, f.o.b.	-4,648	-5,252	-5,035	-6,050	-5,250	-6,000
Trade balance	-127	-101	289	-150	50	-200
Services balance	106	86	96	84	45	80
Current balance	-21	-15	385	-66	95	-120
Capital balance	68	37	-343	15	-40	75
Overall balance	47	22	44	-51	55	-45

Source: Data supplied by the Romanian authorities.

Table 4. Romania: Balance of Payments, Convertible Currency

(In millions of U.S. dollars)

	1980	1981	1982	Jan.-Sept. 1983	Program Forecast 1983	Official Estimate 1983	Official Forecast 1984
Current account, net (for details, see Table 5)	-2,399	-818	655	631	800	870	900
Capital account, net	2,154	-570	117	-591	-804	-874	-952
Medium- and long-term capital, net	1,810	896	602	-1	-265	-123	-1,024
Credits received	1,920	1,001	752	140	-72	68	-770
Receipts	2,747	2,107	2,833	1,178	1,247	1,298	420
Payments	-827	-1,106	-2,081	-1,038	-1,319	-1,230	-1,190
Credits extended	-110	-105	-150	-141	-193	-191	-254
Receipts	104	141	143	105	157	129	161
Payments	-214	-246	-293	-246	-350	-320	-415
Short-term capital, net	344	-1,466	-485	-590	-539	-751	72
Credits received	355	-1,482	-133	-498	-571	-661	--
Receipts	2,124	643	956	314	385	301	300
Payments	-1,769	-2,125	-1,089	-812	-956	-962	-300
Credits extended	-11	16	-352	-92	32	-90	72
Receipts	91	101	--	135	232	180	262
Payments	-102	-85	-352	-227	-200	-270	-190
Errors and omissions, net	--	--	35	--	--	--	--
Overall balance	-245	-1,388	807	40	-4	-4	-52
SDR allocations	33	32	--	--	--	--	--
Monetary movements, net 1/	212	1,356	-807	-40	4	4	...
Monetary gold	-3	4	--	--	--	--	...
SDR holdings	1	--	-12	12	--	12	...
Special escrow deposit 2/	--	--	-316	316	316	316	...
Foreign exchange	162	-81	-25	-133	-258	-67	...
Use of Fund credit	52	290	301	153	334	131	...
Purchases	(159)	(402)	(346)	(198)	(400)	(198)	(...)
Repurchases	(-107)	(-112)	(-45)	(-45)	(-66)	(-67)	(...)
Arrears	--	1,143	-755	-388	-388	-388	...

Source: Data supplied by the Romanian authorities.
1/ Increase in assets (-).
2/ Established in 1982 for the downpayment (made in 1983) under the 1982 rescheduling agreement with commercial banks.

Table 5. Romania: Current Account, Convertible Currency

(In millions of U.S. dollars)

	1980	1981	1982	Jan.-Sept. 1983	Jan.-Oct. 1983	Program Forecast 1983	Official Estimate 1983	Official Forecast 1984
Exports, f.o.b.	6,503	7,216	6,235	4,401	4,997	6,600	6,100	6,600
Oil	2,153	1,931	1,532	1,394	1,627	1,800	1,800	1,900
Non-oil	4,350	5,285	4,703	3,007	3,370	4,800	4,300	4,700
Imports, f.o.b.	-8,037	-7,012	-4,710	-3,239	-3,636	-5,000	-4,450	-4,900
Oil	-3,738	-3,359	-2,462	-1,729	-1,943	-2,300	-2,100	-2,200
Non-oil	-4,299	-3,653	-2,248	-1,510	-1,693	-2,700	-2,350	-2,700
Trade balance	-1,534	204	1,525	1,162	1,361	1,600	1,650	1,700
Oil	-1,585	-1,428	-930	-335	-316	-500	-300	-300
Non-oil	51	1,632	2,455	1,497	1,677	2,100	1,950	2,000
Tourism	208	190	116	72	...	155	91	128
Transportation and telecommunications	-458	-346	-139	-74	...	-220	-120	-210
Receipts	335	372	294	211	...	350	255	300
Payments	-793	-718	-433	-285	...	-570	-375	-510
Interest on debt	-788	-1,047	-917	-572	...	-805	-790	-730
Receipts	48	68	45	56	...	85	66	70
Payments	-836	-1,115	-962	-628	...	-890	-856	-800
Other services	173	181	70	43	...	70	39	12
Services balance	-865	-1,022	-870	-531	...	-800	-780	-800
Current balance	-2,399	-818	655	631	...	800	870	900

Source: Data supplied by the Romanian authorities.

Table 6. Romania: Nominal and Real Exchange Rates, 1981-83

(Commercial rate; January 1981 = 100.0)

End Period	Lei/US$ (Commercial rate)	Non-Oil Trade-Weighted Effective Exchange Rate 1/ Nominal	Real 2/	Real 3/
1981 Jan.	15.0	100.0	100.0	100.0
1982 Jan.	15.0	113.1	126.3	134.5
Dec.	15.0	122.2	127.7	139.0
1983 Jan.	16.5	113.4	118.9	129.3
Feb.	16.5	112.9	117.9	128.3
Mar.	16.5	115.0	119.5	130.3
Apr.	16.5	115.6	119.3	130.2
May	16.5	117.4	120.5	131.8
June	16.5	118.7	121.5	132.3
July 4/	17.6	113.9	115.9	125.6
3rd qtr. 4/ 5/	17.8	114.0	115.4	125.9
4th qtr. 4/ 5/	18.0	113.2	113.7	124.0

Sources: Data supplied by the Romanian authorities; and Fund staff estimates.

1/ Weights reflect 1980 non-oil trade pattern with 17 industrial countries; an increase in the index indicates an appreciation of the leu.
2/ Nominal effective exchange rate deflated by relative consumer prices.
3/ Nominal effective exchange rate deflated by relative wholesale (producer, for Romania) prices.
4/ Incorporating staff estimates.
5/ Quarterly data are averages of end-of-month estimates.

Table 7. Romania: Selected Quarterly Indicators of Domestic Supply and Demand

(In prices as of January 1 of current year)

	Industrial Production 1/		Investment in the National Economy from State Funds		Retail Sales of the Socialist Sector	
	In billions of lei	Percentage change from one year earlier at comparable prices	In billions of lei	Percentage change from one year earlier at comparable prices	In billions of lei	Percentage change from one year earlier at comparable prices
1980 1st qtr.	226.6	8.0	40.1	9.0	46.1	9.8
2nd qtr.	235.3	7.5	53.0	0.4	51.5	5.8
3rd qtr.	235.3	5.6	51.4	1.4	56.9	8.6
4th qtr.	239.3	4.9	53.1	3.9	58.6	6.6
1981 1st qtr.	224.0	3.7	37.1	-12.9	47.7	3.5
2nd qtr.	229.4	5.6	55.3	-1.8	54.1	5.0
3rd qtr.	228.9	2.9	51.6	-5.5	59.8	5.0
4th qtr.	226.7	-1.8	48.3	-5.8	61.6	5.1
1982 1st qtr.	233.5	0.5	36.6	-3.2	51.7	-0.1
2nd qtr.	241.3	1.1	55.5	-1.6	63.1	-0.1
3rd qtr.	262.7	0.8	54.0	-0.2	67.3	-4.5
4th qtr.	271.0	2.7	53.6	-0.6	68.9	-4.6
1983 1st qtr.	265.8	4.2	38.4	-4.7	56.9	0.0
2nd qtr.	277.2	5.2	58.9	-3.8	64.6	1.3
3rd qtr.	277.5	5.4	58.1	0.7	69.1	1.6
4th qtr.						

Source: Data supplied by the Romanian authorities.

1/ Data for 1980 refer to gross industrial production, and for 1981-83 to marketable production.

Table 8. Romania: Selected Economic Indicators, 1980-83

	1980	1981	1982	Program Forecast 1983	Official Estimate 1983	Official Forecast 1984
	(Percent changes, unless otherwise specified)					
National income and prices						
GNP at constant prices	3.3	2.7	3.2	3.8	3.0	7.0
Consumer prices (annual average)	2.3	2.2	16.9	5.0-7.0	5.0-7.0	...
Foreign trade (on the basis of U.S. dollars)						
Exports, f.o.b.	21.0	12.2	-6.5	8.1	-1.4	8.8
Imports, f.o.b.	26.6	-3.3	-20.5	13.4	-0.5	12.4
Non-oil imports, f.o.b.	1.5	-0.2	-18.2	20.1	4.4	14.5
Government budget						
Total revenue	-12.2	-5.9	-1.0	-8.2	-7.5	20.4
Total expenditures	-12.2	-8.5	-5.2	-10.3	-5.4	5.2
Money and credit						
Domestic credit	24.7	13.5	5.5	4.7	...	...
Money and quasi-money (M2) 1/	21.2	18.1	8.4	1.1	...	...
Velocity (GNP relative to M2)	-17.3	-9.6	6.8	10.0	...	...
	(In percent of GNP, unless otherwise specified)					
Central Government budget surplus	0.2	1.3	2.7	2.9	1.6	3.2
Gross domestic investment	38.1	31.4	31.4	30.4	...	...
Gross domestic savings	36.8	38.7	36.3	37.9	...	...
Current account balance	-7.0	-1.9	2.1	1.5	2.1	...
Convertible external debt 2/	16.5	23.8	19.8	19.3	19.1	19.9
Debt service ratio 3/	18.4	22.2	25.7	...	29.5 4/	25.4
Interest payments (in percent of exports of goods and services; convertible)	11.4	13.9	14.1	12.1	12.8	11.1
	(In millions of U.S. dollars, unless otherwise specified)					
Overall balance of payments	-198	-1,366	851	-55	51	-97
Of which:						
In convertible currencies	-245	-1,388	807	-4	-4	-52
Current account	-2,420	-833	1,040	734	965	780
Of which:						
In convertible currencies	-2,399	-818	655	800	870	900
Gross official reserves (months of convertible imports)	0.7	0.9	1.5	2.0	1.7	...
Convertible external debt 2/	9,557	10,198	9,854	9,157	9,004	8,282
Of which: short-term	2,124	643	956	385	295	295
External payments arrears	--	1,143	388	--	--	--

Sources: IMF, European and Exchange and Trade Relations Departments.
1/ Excludes blocked enterprise deposits.
2/ Including use of Fund credit.
3/ Net of rescheduled amounts, in percent of exports of goods and services.
4/ Staff estimate.

Fund Relations with Romania

(December 19, 1983)

Date of membership:	December 15, 1972
Quota:	Old quota - SDR 367.5 million; new quota - SDR 523.4 million
Status:	Article XIV
Fund holdings of currency:	SDR 1,272.2 million (346.2 percent of old quota or 243.1 percent of new quota), which includes SDR 270.8 million (73.7 percent of old quota or 51.7 percent of new quota) under compensatory financing and SDR 322.6 million (87.8 percent of old quota or 61.6 percent of new quota) under enlarged access.
SDR position:	Romania's current holdings are SDR 168,000 or 0.2 percent of net cumulative allocation of SDR 76.0 million.
Direct distribution of profits from gold sales (July 1, 1976-July 31, 1980):	US$30.16 million
Purchases in 1983:	Romania's total purchases in 1983 are limited to SDR 367.5 million, of which SDR 92 million was made available in April 1983 (following the March 30, 1983 Board review) and SDR 91.9 in June 1983 following the successful conclusion of the 1983 debt rescheduling agreements. The two outstanding purchases under the 1983 program, both amounting to SDR 91.8 million, were originally scheduled for after July 31, 1983 and November 30, 1983, respectively.

CONFIDENTIAL

Dear Mr. de Larosière:

1. In accordance with paragraphs 11 and 13 of my letter to you of February 11, 1983, I am writing to you to describe the measures in the fields of exchange rate policy, interest rates, the costing of capital, and energy pricing under the 1983 program with the Fund. These actions were determined on the basis of the studies which were undertaken together with the Fund staff. They constitute part of the reform of the economic mechanism and should be looked upon as part of an ongoing process to help establish a viable balance of payments position. In order to achieve this objective, we have decided to take the various policy actions described below.

a. Exchange rate: After pegging the leu to a basket of currencies (instead of to the U.S. dollar as previously) on July 1, 1983 and thereafter keeping the peg to the basket unchanged, we will devalue the commercial rate of the leu against the basket by 15 percent on January 1, 1984. This devaluation will be applied to the U.S. dollar rate prevailing on December 31, 1983. In the meantime, the leu/U.S. dollar rate will continue to be adjusted so as to maintain the value of the leu vis-à-vis the basket at the July 1, 1983 level. Similarly, after the January 1, 1984 devaluation we will continue to adjust the value of the leu/U.S. dollar rate--and rates for all other currencies--at least once weekly in order to maintain the value of the leu vis-à-vis the basket at its new base level established on January 1, 1984. In addition, we will ensure that the devaluation of January 1, 1984 is fully reflected in the prices of imports from the convertible area and that these effects are passed on accordingly to final product prices, inter alia to ensure that no need for subsidies from the budget will arise. Finally, on the export side we will ensure that the financial incentives created by the devaluation are given in full to all exporters to the convertible area, and that plan targets for exports (so far expressed in terms of local currency value rather than volume) are revised upward in line with the devaluation.

b. Interest rates: We will increase both rates for "normal" bank lending (i.e., bank loans other than special credit and overdue credits), ranging now from 5-8 percent, and enterprise deposit rates, ranging now from 1.5-3 percent, each by 2 percentage points on January 1, 1984. Our interest rate structure will be kept under review in the light of conditions in international financial markets and in the domestic economy.

c. Costing of capital: In addition to raising interest rates, we will be addressing the underpricing of capital in two other ways. First, from January 1, 1984 we will introduce a capital charge on the unamortized amount of new investment financed from the state budget. The charge will be set at the beginning of each year at levels comparable with prevailing interest rates on "normal" bank loans to economic units for investment purposes. On January 1, 1984, the charge will be set at a level of 7 percent. The charge will be paid by enterprises and all other affected economic units and will be a source of budgetary revenue. Second, starting at the beginning of 1984, we will shorten depreciation periods where this is appropriate in light of our own recent experience with the length of the useful life of plant and equipment and in light of experience in other countries. As a first step, on January 1, 1984 we will shorten the depreciation periods for machinery and equipment in the machine building industry. We estimate that these changes will lead to an increase in annual depreciation charges for this industry of about 15 percent or lei 4 billion. We will complete this process for the remaining part of the economy by the end of 1985. We estimate that the additional depreciation charges will amount to about lei 7-8 billion at an annual rate, once these measures are taken.

The aforementioned changes in the costing of capital and in interest rates will be fully passed through to production costs and final prices.

d. Energy prices: We accept the need for a continued strategy to maximize domestic energy production and reduce energy consumption. This strategy is being implemented by a reorientation of investment and changes in technology and the structure of production in order to favor more energy-efficient products and production processes. We also have in mind further price adjustments to narrow the gap vis-à-vis world prices. To this end, we will increase the domestic producer prices of crude oil by an additional lei 100 per ton to lei 1,750 per ton on January 1, 1984, beyond the increase from lei 1,100 per ton to lei 1,650 per ton already agreed for the same date. We will increase this price by another lei 250 to lei 2,000 per ton by July 1, 1984.

2. In addition to the above measures, the Grand National Assembly has recently adopted a program regarding the further increase in labor productivity and the use of labor resources in the period up to 1990 and a program regarding the improvement of the technical quality of products, the reduction of the consumption of raw material, fuel and other energy per unit of output in the period up to 1990. As a result of the implementation of these programs, production costs will be reduced by about lei 50 billion in 1984.

3. The 1983 outcome of the convertible balance of payments is likely to be consistent with the achievement of the program targets for the trade account and the current account. However, as the last two purchases from the Fund under the 1983 program cannot now take place in calendar 1983, we shall be unable to achieve the increase during 1983 of US$250 million in gross international reserves specified as a performance criterion. We now estimate that reserves will rise by US$55 million in 1983. Accordingly, we request a waiver of the performance criterion in the stand-by arrangement relating to the level of reserves at end-1983.

4. We are anxious to continue our cooperation with the Fund. Our preference would have been to extend the present arrangement through the end of 1984. However, in light of existing Fund practices, we accept that the present stand-by arrangement is to be cancelled on January 31, 1984. Thereafter, we intend to request a new one-year stand-by arrangement. However, since we need more time to study the effects of the measures already taken, we do not think that a new stand-by arrangement can be in place before June 1, 1984.

5. Given our policy intentions as described above and our intentions for future relations with the Fund, we believe that the Fund can complete the two reviews referred to in paragraph 13 of my letter to you of February 11, 1983. However, we understand that it will not be possible for the Fund to complete these reviews until the latter part of January 1984. At that time the new arrangement which we intend to request will not be in place and the performance criterion contained in paragraph 3(c) of the March 1983 decision would operate to prevent further purchases under the arrangement, unless the Fund decides otherwise. We therefore request that the Fund permit purchases totaling the equivalent of SDR 183.6 million to be made, notwithstanding paragraph 3(c) of the March decision.

Sincerely,

Petre Gigea
Minister of Finance

December 20, 1983