

University of Missouri, St. Louis

IRL @ UMSL

UMSL Global

1-1-1997

Land Mines on the Road to Market Economies in Romania and Albania Pyramid Schemes and Individual Investment in the 1990s

Elez Biberaj

Peter R. Mueser

Robin Remington

Mircea T. Maniu

Follow this and additional works at: <https://irl.umsl.edu/cis>



Part of the [International and Area Studies Commons](#)

Recommended Citation

Biberaj, Elez; Mueser, Peter R.; Remington, Robin; and Maniu, Mircea T., "Land Mines on the Road to Market Economies in Romania and Albania Pyramid Schemes and Individual Investment in the 1990s" (1997). *UMSL Global*. 85.

Available at: <https://irl.umsl.edu/cis/85>

This Article is brought to you for free and open access by IRL @ UMSL. It has been accepted for inclusion in UMSL Global by an authorized administrator of IRL @ UMSL. For more information, please contact marvinh@umsl.edu.

Occasional Paper No. 9707
May, 1997

Occasional Papers

The Center for International Studies of the University of Missouri-St. Louis issues *Occasional Papers* at irregular intervals from ongoing research projects, thereby providing a viable means for communicating tentative results. Comments on these papers, therefore, are particularly welcome. *Occasional Papers* should not be reproduced or quoted at length without the consent of the author or of the Center for International Studies.

Land Mines on the Road to Market
Economies in Romania and Albania:
Pyramid Schemes and Individual
Investment in the 1990s

Elez Biberaj, Peter R. Mueser,
Robin Remington, and Mircea T. Maniu

Land Mines on the Road to
Market Economies in Romania and Albania:
Pyramid Schemes and Individual Investment in the 1990s

Elez Biberaj
Voice of America
Washington, DC, U.S.A.

Peter R. Mueser
Department of Economics
University of Missouri-Columbia, Missouri, U.S.A.

Robin Remington
Department of Political Science
University of Missouri-Columbia, Missouri, U.S.A.

Mircea T. Maniu
Department of Economics
Babes-Bolyai University, Cluj-Napoca, Romania

May 1997

The original version of this paper was presented at the Central Slavic Conference, University of Missouri-Columbia, October 3-5, 1996. Its publication as part of this occasional paper series is supported by the University of Missouri Research Board funded project "Beyond the Iron Curtain: Legitimacy, Identity, Security." Project Director: Dr. Robin Alison Remington, Professor of Political Science, University of Missouri-Columbia.

Introduction

In the wake of the fall of state economic control in Eastern Europe, free enterprise activities have grown dramatically, accompanied in most cases by moves toward multiparty politics. Against this backdrop, a variety of pyramid investment schemes took root in several of these countries. Among the largest and most important were those in Romania and Albania. This paper is a preliminary comparison of schemes arising in these countries, which are among the poorest and formerly most repressive in Eastern Europe.¹

Our analysis is designed to look at a range of economic, political and security issues flowing from the triple transition underway in all the formerly one-party hegemonic countries of communist Eastern Europe. First, we wish to consider what this detour on the road to the market has meant for these economies. How do such activities interact with the "shock therapy" prescribed by Western financial power brokers who hold the purse strings that control credits and foreign investments. Secondly, what do the rise of these schemes imply in terms of standard economic theory? We consider whether these represent the kind of irrational behavior that Kindleberger (1989) argues fuels speculative bubbles. Thirdly, and with regard to Albania most tentatively at this stage, what are the political-security consequences that result from government policy towards these get-rich-quick schemes that played on the dreams and greed of needy societies with little experience in evaluating emerging investment opportunities.

We first begin with Caritas, the largest and most successful of the Romanian schemes, because the 1992-1993 time line of the rise and fall of Caritas means that political and economic policy makers in Albania had an opportunity to observe this experience prior to the 1996 expansion of similar schemes in their country. Furthermore, interested outsiders--the International Monetary Fund, the World Bank, the European Union and the U.S.--could use the Romanian example in their attempts to impress upon the Tirana government the risks of such schemes.

Among the variety of pyramid schemes which developed in Romania after the 1989 revolution, most failed after a few months, providing returns to their organizers and a few early

¹The analysis here builds on Maniu and Mueser (1996).

investors. In contrast, Caritas survived for nearly 19 months in 1992 and 1993. The returns for successful "investors" in the scheme were extraordinary, providing payments of eight times the original investment in three to four months, equivalent to an annual interest rate of more than 100,000 percent. For those who invested during the first 15 months of the scheme, promised payments were made out of an ever-increasing pool of new investments. At its peak, the flow of investments may have amounted to more than 10 percent of the gross domestic product of Romania. In all, Caritas may have involved more than 4 million investors who made total payments of well over \$500 million and possibly several times that amount. When the scheme failed in late 1993, a substantial share of Romanians suffered losses. Caritas may have been the largest transparent pyramid scheme to ever exist.

As in Romania, in Albania the fall of communism and the demise of the centrally planned economy led to the rise in 1991 of a number of pyramid schemes. In contrast to the experience in Romania, a substantial number of Albanian get-rich-quick schemes remained in operation for extended periods, involving a large proportion of the country's inhabitants, many of whom appear to have invested their life savings in the schemes. More than in Romania, the schemes were tied to the central government and to political parties. Consequently, the collapse of pyramid schemes in early 1997 had a devastating impact on Albania, sparking widespread violent unrest in many cities and plunging the country into its worst political and economic crisis since the downfall of communism. The Albanian schemes were clearly unique in terms of their impacts on the social and political structure of a national unit.

The growth and extent of such pyramid schemes are of interest both to students of economic transition and to those interested in the application of modern economic theory. The dominant paradigm used by economists assumes that markets reflect rational behavior and mutually consistent expectations. As a result, pyramid schemes cannot exist. Since most of those who invest in such schemes must ultimately be disappointed, investors' expectations taken jointly are mutually inconsistent. - Just as economic markets will determine prices for land, stocks, or bonds based on underlying expected return, rational behavior will ensure that no one participates in pyramid schemes.

The survival of these schemes therefore provides a challenge to the applicability of the dominant economic theory. In large part, this analysis will attempt to understand how schemes of this kind could survive so long and grow so large, identifying why the simple implications of the economic theory are violated. Of course, the first question that might be asked is whether theory which applies in developed economies may not apply in these countries. Following years of direct government control of the economy, individuals may not have had sufficient experience to form consistent economic expectations. In this case, the growth of pyramid schemes may merely identify a learning phase for an economy's participants, expected to yield to a stable set of expectations and ultimately to economic stability. Alternatively, there may be something unique in the political or social climates that allowed the schemes to prosper. In this case, cultural or political changes may be necessary before economic stability within a free enterprise framework can obtain.

Kindleberger's (1989) view of the behavioral bases of speculative bubbles implies that a more radical revision of economic theory may be necessary to understand such schemes. Kindleberger argues that although stability prevails under most circumstances, occasionally irrational and mutually inconsistent expectations seize a market and grow to dominate. He suggests that financial crises are fueled by individual behaviors that are outside the predictions of rational models. The success of pyramid schemes may support Kindleberger's claim and also may provide some clue as to when such instability will prevail. While conventional economic theory underscores the need for the government to enforce property rights, if Kindleberger's interpretation is correct, it suggests a broader role for government.

In most of the former communist countries, standards of living and other indicators of economic health have suffered severe declines since the fall of communism. Schemes such as those in Romania and Albania draw resources from productive investments, ultimately enriching the few winners at the cost of the many. More important, long term economic growth requires the establishment of stable markets for investment. These schemes may reduce the confidence in general investment markets, possibly reducing the willingness of individuals to support productive enterprises.

*The Rise and Fall of Caritas*²

The Rise. Caritas began operations in the Romanian city of Cluj on April 14, 1992. It had previously operated in the city of Brasov, about 200 miles from Cluj, where it had been registered as a limited liability company. In the face of apparent difficulties, it was reestablished in Cluj where the nationalist leader and city mayor Gheorghe Funar welcomed it. Caritas was established by Ioan Stoica, who maintained sole control of operations throughout the life of the scheme.

The scheme's rules were simple. An individual invested a sum of money and received a receipt. The minimum initial investment was 20,000 lei (\$20), and the maximum was 120,000 lei, although the latter limit was not in force in the later stages of the game.³ Three to four months later, the investor's name would be listed in the *Mesagerul transilvan (Transylvania Messenger)*, a Cluj newspaper, at which point he would be eligible to retrieve an amount eight times the original investment. Payments were available in cash, but those claiming payments were also given the option of reinvesting any winnings for additional cycles.

After the fall of Romania's communist government in 1989, a large number of similar schemes had been established, but few of them had lasted more than a few months. In each case, the final wave of investors had lost their money. In contrast, Caritas continued to grow through 1992 and most of 1993. It was originally located in offices rented to it by the municipal government near the Cluj central city, but with growth, it moved to more spacious quarters. Near its peak in the summer of 1993, it was operating in a public sports complex. In addition to its

² We are aware of only a limited and dispersed literature dealing with Caritas. Of accounts in English, Verdery (1996) provides the most detailed, while Shafir (1993) provides a good summary with an emphasis on political matters. While coverage in the Romanian press has been extensive, we know of no single comprehensive source. A two part sociological analysis appeared in Mihiu (1993b).

³ Shafir (1993) and Verdery (1996) reported a maximum initial investment limit of 160,000 lei in late summer 1993. Many of the details involved in Caritas are not known with certainty, since published reports are often inconsistent. This may reflect inconsistencies in actual practices, changes in practices over the life of the game, or misinformation provided to journalists.

main office in Cluj, Caritas operated branches in Turda and Dej, towns within 40 miles of Cluj, but investments made in these locations were small compared to those made at the main office.

While the investment limit of 120,000 lei may appear modest, it exceeded the average monthly earnings in Romania in that period. In return for a payment equal to a single month's salary, an investor could obtain the equivalent to five years' salary in just two cycles--seven months--or a lifetime's earnings in just three cycles. Stories of investors purchasing expensive consumer goods, automobiles and housing were common by the summer of 1993. The newspaper in which winners' names were listed, grew dramatically from a circulation of several thousand to several hundred thousand.

Size and Extent. The peak month, in terms of numbers of players investing, was probably July of 1993. Simple calculations suggest that even with a very small start, the scheme would have needed to attract a large number of new investors to survive 15 months. However, the necessary size depends on the reinvestment rate. During the life of the game, the reinvestment rate was probably between 50 percent and 90 percent and probably closer to 90 percent.⁴ With the latter reinvestment rate, the scheme would need to attract new investors to pay only a tenth of the winnings owed.

During early July of 1993, we counted the number of winners listed in the newspaper as 20,000 to 30,000 per day. Since the scheme operated seven days a week at that point, this implied a minimum of 600,000 winners during July, but allowing for growth during the month, the number could easily be a million. Since all winners during this time received full payment, if the size of each account and reinvestment rate were known, we could calculate the total amount of money newly invested in the scheme during the month. A lower estimate can be obtained by assuming that the number of investors receiving payments was 600,000, that they had invested 20,000 lei, and that they chose to reinvest 90 percent of the 160,000 lei that they were owed. In

⁴ Inferences about Caritas investors are based on media reports and interviews we conducted with more than 100 Caritas investors. Our interview sample is not random, since it is largely based on personal contacts and is heavily weighted toward residents of Cluj. One advantage of using personal contacts is that the information may be more accurate than that obtained through survey methods, especially given the distrust that Romanians have of official bureaucracy.

this case, new money equal to 32,000 lei per person would need to be invested, or approximately 7.2 billion lei (\$7.2 million). On the other hand, if the total number of investors receiving payment was 1 million, with prior cycle investments of 120,000 lei, and they were reinvesting only 50 percent of their winnings, the total required to pay investors would have been 480 billion lei (\$480 million). Our best guess is the typical participant reinvested appreciably more than 50 percent of his winnings, and that the average prior investment was over 100,000 lei, so that the total money raised in July was probably in the range of 200-250 billion lei.

This estimate is a little higher than the figures provided by Caritas in a November 1993 press conference. Caritas reported that, at its peak in July, it had raised 138 billion lei, provided by the investments of 1.109 million new participants, suggesting an average investment of 124,000 lei per person. There are reasons to believe that such figures may underestimate actual investments. When the government ultimately seized Caritas records in 1994, accounting information was in disarray, with accounting tasks decentralized to the point of chaos. The structure of computer programs and accounting methods would have allowed easy alteration of records.⁵

The importance of the scheme in the Romanian economy can be gauged by noting that the 1993 gross domestic product for Romania was 19,737 billion lei (Economist Intelligence Unit, 1994). Using 200-250 billion lei as the scheme's draw in July corresponds to 12-15 percent of the monthly gross domestic product. If reinvestment rates remained the same, in the next cycle, the scheme would have had to attract eight times this amount of money, or a flow of between 96 percent and 120 percent of Romania's gross domestic product.

The Demise. Many observers recognized that the scheme could not survive much longer given its size in the summer of 1993,⁶ but predictions of its failure had been common since the beginning. In early October, Caritas suspended payments, claiming that computer problems were to blame. Although the press confidently proclaimed the scheme's collapse, after a few

⁵ Shafir (1993) estimated that the scheme was drawing 3 billion lei per day during July and 4.5 billion lei per day by August. He does not indicate the bases for these estimates.

⁶ See, for example, Mueser and Franz (1993a, 1993b).

days payments resumed. The episode may have reinvigorated the game, for a new surge of investments followed resumption of payments.

Payments to investors continued through November 5, 1993, when they were again suspended. Some payments appear to have been made to investors after that point, but the last investors to have received full returns equal to eight times their investment were those investing on July 4, 1993.

In the fall and winter of 1993, Stoica attempted to establish branches of the scheme outside the Cluj region, apparently hopeful of attracting still greater levels of investment. He set up a branch of the scheme in Petrosani, the mining capital of Transylvania, with the support of the miners' leader. Although it attracted substantial local investment, this was insufficient to maintain the scheme. When local authorities denied his request to establish a branch in Bucharest, he threatened a hunger strike. He did set up a branch in a suburb of Bucharest, but it drew only a small number of investors. Rumors also spread that Stoica had traveled outside of Romania to establish branches of scheme, but nothing appears to have come of such efforts.

The feared social upheaval following collapse did not occur. In part, this may have been partly due to Stoica's efforts over the next several months to resurrect the scheme. Given that payments continued for some three months after July, it seems very possible that as many as four million Romanians invested as much as 1 trillion lei (\$1 billion) in Caritas over its lifetime.⁷

In the wake of the Caritas failure, a variety of similar schemes, with names like Mondoprosper, Driada, and Novo Caritas, proliferated, but none lasted very long. Many collapsed before making a first payment, their organizers recognizing the first cycle of investments as the only return.

In 1995, the Romanian government brought criminal charges against Stoica for his activities as head of Caritas. On conviction, Stoica was sentenced to two years in prison, although he was released after 10 months. He faces a civil suit brought by 600,000 investors

⁷ Our estimate of the total investment is therefore close to that given by in a recent Reuters report (Eremia, 1996), but is smaller than the \$5 billion total that some sources suggested (e.g., Perlez, 1993).

seeking compensation for losses in the case. Currently, legal restrictions appear to effectively preclude the establishment of new schemes.

Growth of Pyramid Schemes in Albania

Albania's get-rich-quick schemes sprung up in 1991, less than a year after the last communist president Ramiz Alia, facing widespread popular unrest, agreed to permit the establishment of opposition political parties. Taking advantage of the political turmoil and power vacuum which characterized the first phase of transition from communism to pluralism, emerging businessmen set up several pyramid schemes, primarily in Tiranë. Initially these schemes made little headway because the economy had practically collapsed and the population lived in extreme poverty, having become totally dependent for its survival on foreign humanitarian assistance. But as Albania embarked on the road to recovery, following the Democratic Party's sweeping election victory in March 1992, companies promising impossibly high returns increasingly gained ground.

Between 1991 and 1996, there were at least nine companies that were suspected of operating as pyramid schemes, the most important being Vefa Holding, Gjalica, Xhaferri, Populli, Kamberi, and Sudja. Thousands of unwary investors put their savings into these companies, which promised interest rates of up to 50 percent a month. Earlier depositors made huge profits from the deposits of those who followed them. According to conservative estimates, Albanians invested close to \$1 billion in the funds, the equivalent of about 25 percent of the country's annual gross domestic product.

While pyramid companies had been active since the early 1990s, it was during the summer and fall 1996 that their operations expanded most dramatically. This coincided with a busy and troubling period as Albania held controversial parliamentary elections, in May 1996, which were severely criticized by international observers and whose results were not accepted by leading opposition parties. Berisha's government was preoccupied with the political fallout of these elections and in campaigning for local elections, held in October 1996, and the government was not willing to take the political risk of shutting down the schemes. The opposition, too,

maintained a conspicuous silence. Meanwhile, in fall 1996 the pyramid schemes engaged in an interest rate war, some of them, such as Sudja, hiking their monthly interest rates to 80 percent.

In November 1996, an IMF delegation urged Prime Minister Aleksandër Meksi to impose strict controls on the pyramid schemes and refused to sign a new agreement with Albania. Despite this and other warnings, and other signs of a looming crisis, the government failed to take action against the schemes at that time. Although Parliament appointed a transparency commission to investigate the operation of the questionable investment companies, by the time the government took action, the schemes were beginning to crumble, and large amounts of money had already been transferred abroad. In November 1996, Sudja company, which had operated mainly in Tiranë, stopped making payments, while Sandër Grunasi, the director of a small fund Grunasi, fled the country with \$13 million.⁸ In mid January, 1997, Sudja declared bankruptcy and its owner was arrested.⁹ This was followed by the collapse of Xhaferri and Populli foundations. The government seized \$255 million held in state banks by Xhaferri and Populli.¹⁰ On January 24 the authorities arrested the directors of the two funds, Rrapush Xhaferri and Bashkim Driza, as well as some 50 operators throughout the country.¹¹ Rrapush Xhaferri admitted that his company, which began operations in 1993, was a pyramid schemes.¹² In early February, Gjallica declared bankruptcy. Gjallica reportedly had attracted about \$300 million in deposits; but its assets amounted to only a fraction of that amount (Done and Hope, 1997).

⁸ Sandër Grunasi left Albania on 6 November 1996, reportedly using an official passport. See *Zëri i Popullit*, 23 January 1997, p. 9.

⁹ *Albania*, 24 January 1997, p. 3.

¹⁰ Tiranë TVSh Television Network in Albanian, 1900 GMT, 16 January 1997, in FBIS-EEU-97-012, 16 January 1997.

¹¹ ATA in English, 2158 GMT, 24 January 1997, in FBIS-EEU-97-017, 24 January 1997.

¹² See Rrapush Xhaferri's interview in *Albania*, 23 January 1997, p. 3. Bashkim Driza had worked for Xhaferri but in July 1996 set up his own company, Populli. Ironically, Driza is head of the People's Party, a left-wing party with close links to the Socialist Party.

The collapse of Gjallica caused immediate and widespread unrest in Vlorë. For days security forces battled with angry protesters, finally abandoning the city altogether. Unrest spread in other southern cities. Although many investors knew that the pyramid schemes had no sound economic basis and that eventually they would crumble, they now blamed the government. Opposition parties fueled the protest, in the hope of forcing the ruling Democratic Party to make political concessions. What began as essentially an economic protest soon took on political nature. Although the opposition had not criticized the schemes, it moved to capitalize on the anger of the depositors, which turned against the government. Forum for Democracy, a loose coalition bringing together former communists and a group of former political prisoners, demanded the resignation of the government and new elections.

The collapse of pyramid schemes wiped out the savings of more than half-a-million Albanians and led to widespread violent unrest throughout the country. It also brought Albania to the brink of civil war; resignation of Prime Minister Meksi, and the declaration of a state of emergency.

In early February 1997, the authorities began repaying investors in Xhaferri and Populli from the two firms' deposits that had been frozen in the state banks with payments amounting to 50 to 60 percent of their initial payments. They were given the choice of cash or savings deposits. Some investors, however, refused the partial compensation, hoping to get full compensation later. Those Albanians who had invested in Sudja and Grunjasi, which did not have any assets, were unlikely to get any of their deposits.

Lacking resources and unwilling to undertake unfunded spending that might trigger hyperinflation,¹³ the government has refused to provide cash handouts from state coffers. However, it has said it will try to find ways to compensate investors, and it has promised to help the most severely affected people by offering them public jobs and providing credits to start private businesses.

¹³After several years of low inflation, inflation jumped to close to 20 percent in 1996.

Comparison of Caritas and the Albanian case with Related Schemes

It is useful to briefly consider related schemes in other times and places. The scheme of Charles Ponzi in Boston, Massachusetts in 1920 was notable for the public attention it commanded. Ponzi offered 50 percent interest for 45 days in 1920, or the equivalent of approximately 2,500 percent per year. Ponzi claimed that he was able to take advantage of differing exchange rates across countries, buying and selling financial instruments in different currencies to obtain sure profits. When newspapers publicized the opinions of financial experts that such profits were impossible, Ponzi admitted that the exchange rate story was not true, claiming he had a method of investment that he wished to keep secret so Wall Street speculators would not catch on. Over a period of seven months, Ponzi collected \$9.6 million before the operation was closed down (Russell, 1973).

Minsky (1982) has labeled such arrangements, in which returns for investors come from payment by new investors, as "Ponzi" financing. Schemes of this kind are hundreds of years old. Kindleberger (1989) described several historical cases. One scheme established in 1872 promised Bavarian farmers interest of 20 percent per year; another nineteenth century scheme offered to pay 40 percent per year. In both cases, the perpetrators drew extended prison sentences.

Many stock frauds are also based on similar financing structures. The famous "South Sea bubble" in 1720 provided spectacular returns for investors in the South Sea Company who purchased stock that appreciated as speculation and fraudulent claims drove the stock price up. When it became clear that there was little return in the underlying assets of the company, the stock price collapsed, inducing a financial crisis. Sir Isaac Newton was one of the investors who purchased stock at the peak, and he lost £20,000 (Kindleberger, 1989, p. 38). In Russia, the MMM stock offering attracted investors by promising dividends of 3,000 percent. While early investors made fortunes, others lost everything when the company collapsed in early 1994.

Pyramid games and chain letters operate under the same basic financing structure. In such arrangements, individuals pay for the right to recruit new individuals, who, in turn, recruit others. A recent report described pyramid games played by residents of Palm Desert, California (Emshwiller, 1996). A typical pyramid had 15 positions, with one person at the top, two at the

second level, four at the next, and eight at the bottom. When all positions were occupied, each person at the bottom would pay \$2000, with the \$16,000 total going to the player at the top, who would then leave the pyramid. The pyramid would then split in two, with each player moving up a level, and eight new positions in each pyramid being filled by recruits paying again \$2000. As with all of these schemes, when the game exhausts the willing population--as it must, ultimately --the players who have not yet received their payoffs get nothing. At the time of the report, more than 1000 residents of Palm Desert had participated in the games, including local elites such as the president of a community college and senior officials in several local organizations.

A chain letter that operates on the same principle but with very different dollar values has been active on the Internet for at least the past two years. In this case, participants obtain instructions from a message posted on a news group. A participant mails \$1 to each of five names on a list, removes a name from the list and adds his own, and then sends the message, via electronic mail, to at least 200 additional news groups. The message carries testimonials claiming returns of \$20,000 to \$50,000.

A final kind of pyramid scheme is observed in what are called multi-level marketing arrangements. Although the goal of such structures is to sell a product, in such arrangements a sales representative's returns derive primarily not from selling a product but from enlisting new sales representatives. The Amway company in the U.S. uses a multi-level market structure to sell household products. One potential participant calculated that if sales commissions were to grow at the rate he had been promised, Amway sales would exceed the entire U.S. economy in five years (Kling, 1996). Where they are successful, multi-level marketing can provide substantial returns to early participants, but their gains are at the expense of later recruits who join after the market for both the product and new recruits are exhausted.

Some authors have drawn a distinction between schemes that fraudulently claim to have found some genuine investment opportunity allowing payment of extraordinary returns from more transparent pyramid schemes and chain letters. At least one writer has reserved the term Ponzi for schemes involving such fraudulent claims (Nehra, 1996). In the case of Caritas, Ioan Stoica did not have a detailed story to explain the high returns. When pressed by journalists, he did refer to a secret method of making money, even talking of training followers to take over at

his death, but these claims amounted to little more than general assurances. In its formal registration, Caritas described itself as a "mutual collective helping game," tantamount to a statement that the scheme was based on pyramid financing. In terms of claims made to investors, Caritas appears to have had more in common with transparent pyramids and chain letters than with fraudulent investment companies.

Explicit fraud appears to have played a larger role in the Albanian schemes. Some of the investments were offered by firms that strongly denied being pyramid schemes, maintaining that they obtained returns from corporate holdings. Founded in 1991 by Vehbi Alimuçaj, a former soldier, Vefa Holding became the country's largest company. It acquired numerous holdings all over the country, including supermarkets, food processing plants, tourist centers, a ferry line, and a mine. Gjallica, operating mainly in the south and in the northeastern city of Kukës, was involved in tourist development, hotels, and gas stations. Other companies such as Kamberi, Cenaj, and Silva also claimed to have legitimate businesses. Xhaferri and Populli, on the other hand, portrayed themselves as charitable organizations, suggesting a similarity with Caritas.

Public Opinion: How People Understood the Schemes

Given that simple deception does not fully explain these schemes, it is natural to consider the structure of expectations that undergirded their growth. How did investors view the schemes and what was their understanding of the processes producing returns? Were there special circumstances that permitted mutually inconsistent expectations to form? And, if so, can we predict when such circumstances will occur?

From its inception, opinions about Caritas were divided. A substantial portion of the press attacked the scheme, predicting first its imminent demise, and then, as it continued to prosper, economic and social disaster following its ultimate failure. While Caritas critics included many of the educated elites in Romania, such elites were not absent among its supporters. Cluj mayor Funar lauded the scheme. During the last months of the scheme, he appeared with Stoica on national television expressing his full confidence in Caritas, triggering the last large inflow of investments. Grigore Zanc, prefect of Cluj county, expressed only slightly more tempered enthusiasm for the scheme when he commented, "I think it is worth

taking advantage of this phenomenon and using it, and supporting it, as much as we can, without forgetting at any moment that each of us may be a loser" (Toader, 1993). Zanc noted that Caritas brought substantial benefits to the Cluj area. As many as 2000 employees worked directly for the scheme at its height. Funar claimed that voluntary donations by Caritas winners to the Cluj city coffers were substantial.¹⁴

Investors we talked to had a variety of explanations of how the scheme provided such extraordinary returns. Many investors suggested that Caritas operated as part of an illegal money laundering scheme.¹⁵ This is similar to a view that is common among individuals who invest in fraudulent investment companies. Investors often believe there is some hidden illegal activity which explains both the high returns and the fact that it is secret. However, explanations of this kind did not provide the basis on which most investors acted. For the most part, those who had confidence that the scheme could continue indefinitely had no consistent explanation for how the returns were produced, merely basing their confidence on past performance. One person told us that since it had lasted longer than previous schemes it would last indefinitely. Taken at face value, such views suggest that these investment choices were made without any understanding of or concern for the underlying processes producing returns. A second class of participants, generally those who were more educated, recognized that the scheme would eventually fail. They invested on the chance that it would not fail before their return became available, hoping that others would be losers.

Among those investing, a substantial share hailed Stoica as a national hero. Not only did crowds of investors cheer him, but the supportive press carried glowing accounts of his acumen as a businessman, economist and psychologist, declaring Caritas the salvation of Romania. One writer suggested that Caritas revealed "the miracle of money laundering," with no irony intended (Goga, 1993, p. 3). On what turned out to be the last day in which investors received full

¹⁴ For an unabashed defense of the scheme, in English, see Morris (1993).

¹⁵ Verdery (1996) gives detailed accounts of a variety of explanations given by participants for how the scheme worked. The extraordinary range of explanations supports our own interpretation that they served as little more than window dressing, not as serious bases driving the investments.

payments, Cluj sociology professor Achim Mihi wrote, "the ultimate strength on which Caritas rests lies with the human soul and its dreams; one cannot judge that negatively and simply abandon it" (Mihi, 1993a). Those newspapers that continued to display hostility toward the scheme suffered in the face of a supportive populace who appeared to view the attacks as an attempt to abrogate their newly gained economic freedom. Even after payments ceased, a substantial portion of investors remained loyal to the organizers.¹⁶ As late as February 1994, Cluj mayor Funar is reported to have said that he was confident that the game would be durable over the long run (Tudosiciuc, 1994).

Given that several major schemes operated in Albania, one might anticipate great heterogeneity in the attitudes toward them. In fact, government leaders, the press, and popular opinion were, without serious exception, strongly supportive of the schemes. There were no meaningful warnings from either government or the independent media. Party and non-party newspapers as well as the state controlled radio and television provided widespread, positive coverage to the pyramid schemes, ran their advertisements, and prominently featured scheme directors. Moreover, senior government officials continued to give tacit endorsement to the investment funds even as collapse became imminent.

In an interview in November 1996 with the pro-government paper *Albania*, Blerim Çela, chairman of the State Control Commission, said he did not believe that these firms faced bankruptcy. Indeed, he insisted that there was nothing illegal about these companies, adding "I think that these firms are involved in a good business, because they help people . . ." (Çela, 1997). Arben Kallamata, a Foreign Ministry official and a former Nieman scholar, denounced a correspondent of an Albanian-American newspaper who had written about the looming crisis, as "a hack journalist in the Bronx." He also dismissed growing alarm about the pyramid schemes as mere propaganda (Kallamata, 1996). As late as November 1996, Prime Minister Aleksandër Meksi attended an anniversary celebration for Vefa Holding, the largest investment company.

¹⁶ Mihi (1993b) reported that 62 percent of respondents surveyed agreed that "the media act in an evil manner against Caritas," 66 percent agreed that "Mr. Stoica means only well for everyone," and 68 percent agreed that "Caritas will survive in the end."

It may well be that many Albanians, poorly educated and with little experience of the free market, were simply taken in by the claims of investment opportunity. By late 1996, the suspected investment companies had launched a well coordinated publicity campaign to convince Albanians that they were not pyramid schemes. In an article in November 1996, a spokesman for Vefa Holdings claimed the company had invested "several hundred million dollars" in various projects, from "mines, supermarkets, tourism, processing industries, production lines in light industry and the food industry, stock raising complexes, catering, sea and land transportation, and other cultural and sports activities." The spokesman strongly denied that Vefa was a pyramid business (Iliazi, 1996). Like investors in Caritas, many Albanian investors justified the scheme's returns with reference to the possibility of money laundering, perhaps with greater justification than in Romania. According to some sources, organized crime groups may have pumped hundreds of millions of dollars into the unregulated schemes. It is therefore plausible that the Italian mafia and other foreign crime rings, working closely with domestic groups, may have used the pyramid schemes to launder profits from drug and arms trafficking, and refugee smuggling.¹⁷

The strong support of the schemes in both Romania and Albania is reminiscent of the support by investors in Charles Ponzi. Even after his purported methods of obtaining high returns had been revealed as deception, supportive crowds cheered Ponzi, confident that the scheme would in time be resurrected (Russell, 1973).

How can we explain continued faith in schemes with no meaningful economic basis? It should first be noted that participants who recognize that the scheme will ultimately fail and that the losers will predominate may nonetheless rationally choose to invest if they believe they will be paid before the scheme collapses. As a group, residents of Cluj obtained substantial net benefits from Caritas, since they were over-represented among early investors. It is difficult to

¹⁷ See OMRI Daily Digest, No. 32, Part II, 14 February 1997. There have also been allegations, fiercely denied by the ruling Democratic Party, that senior government officials, including former Minister of Internal Affairs Agron Musaraj and Minister of Defense Safet Zhulali, were involved in drug trafficking and illegal arms, and sale of oil to Serbia in violation of United Nations sanctions (*The Independent*, 14 February 1997).

argue that such insider investments in the scheme were irrational. Similarly, early investors in the Albanian schemes, perhaps including a disproportionate number of elites, benefited from those schemes. On the other hand, there are inevitably a much larger number of others who make investments that do not pay off, those that we may view as outsiders. The difficulty is in understanding their behavior within the rational structure.

In discussing speculative bubbles, Kindleberger (1989) claims that an initial period in which investors obtain very large returns induces patterns of behavior that violate rationality.

As firms or households see others making profits from speculative purchases and resales, they tend to follow . . . When the number of firms and households indulging in these practices grows large, bringing in segments of the population that are normally aloof from such ventures, speculation for profit leads away from normal, rational behavior . . . A larger and larger group of people seeks to become rich without a real understanding of the processes involved."

Kindleberger captures the emotional response that draws initially reluctant players into such a scheme with the observation, "There is nothing so disturbing to one's well-being and judgment as to see a friend get rich" (p. 19-20).

While the experiences in both Romania and Albania support Kindleberger's characterization, it is very difficult to reject an alternative explanation which does not rely on an assumption of irrationality. Friedman (1969) has argued that destabilizing speculation may reflect a positive demand for risk. The same logic may apply to investment in a pyramid scheme, even when its structure is transparent. In this view, investors were merely participating in a gamble in which the expected negative return was compensated for by the possibility of large rewards. This interpretation argues that gamblers need not be irrational to bet, even in the face of negative expected monetary benefits.

The possibility that the schemes filled an entertainment role appears more plausible in the case of Romania than Albania. Relatively few investors in Caritas appear to have suffered debilitating financial losses in the game. Even in the game's final stages, the average investment was only a little over 120,000 lei, or less than two months salary for an average Romanian. There appears to have been relatively little long term impact on most of the winners. Although we heard talk of winners quitting their jobs, our impression is that this was not widespread.

Caritas clearly served as a focal point for social interaction, with participants sharing of information in what many may have interpreted as a "mock capitalism."¹⁸

In contrast, the impact of the schemes on Albanians appears to have been much greater. Many impoverished Albanians sold everything they had, including homes, farms, livestock, and belongings, in the expectation of doubling their cash in a matter of weeks. By fall 1996, an estimated 700,000 Albanians out of 3.2 million had become dependent on interest from deposits in pyramid schemes for their livelihood and to supplement their meager wages.¹⁹ The total amount of money invested by Albanians, relative to the size of the national economy, was certainly several times that for Caritas or other schemes in Romania.

The Role of Government

As noted above, Cluj government officials aided Caritas in a variety of ways, facilitating use of government-owned office space and providing public statements supportive of the scheme. The central Romanian government undertook little direct action during the lifetime of the scheme, although it did license and tax it. According to Stoica, Caritas paid over 20 billion lei (\$20 million) in various taxes while it was in operation. We heard government officials say that the scheme violated no laws, so that there was no basis for acting against it. When pressed, officials frequently noted that the scheme involved just the kinds of voluntary trade on which the free economy is based. As opposition newspapers pointed out, the scheme's popular support, in conjunction with that of local government, would have made any action by the central government against the scheme politically costly.

As in Romania, the Albanian central government claimed that it had no role to play in regulating the investment schemes, insisting that it was a matter of citizens lending and borrowing among themselves. Not only did the government fail to warn citizens of the dangers

¹⁸ Among the large number of Caritas participants, some clearly did suffer economic hardship. Verdery (1996) reports that during the fall of 1993, Cluj banks repossessed more than 50 apartments that had been mortgaged so owners could invest in Caritas.

¹⁹ As a foreign journalist put it, "... it is difficult to find anyone in Albania who did not entrust his meager savings to one of the pyramid schemes" (Hockstader, 1997).

of investing in unregulated pyramid companies, but it provided the stamp of approval by maintaining close links with some of the companies, particularly Vefa and Gjalica. Moreover, there were reports that some of the companies had contributed to the Democratic Party's 1996 election campaign. In the eyes of most Albanians there was no doubt whatsoever of government endorsement of the pyramid investment schemes. Opposition political parties did not publicly condemn the existence of the pyramid schemes nor did they call for government intervention.

The government stance in Romania and Albania while the schemes were in operation contrasts markedly with that in the U.S. and other developed countries. Specific laws and general regulatory practice in almost all developed economies effectively prohibit schemes based on pyramid financing. Commentators appear to take for granted that if there is no long run method of actually obtaining the return promised to investors, that is, if the success of a scheme depends on bringing in ever more investors, the scheme is fraudulent. Charles Ponzi's scheme collapsed when Massachusetts state officials, under pressure from local financial leaders convinced that there was no underlying investment, prevented him from accepting further funds. Both federal and state securities laws prohibit the kind of misrepresentation in which Ponzi engaged.

In the U.S., not only are deceptive practices prohibited but so also are transparent pyramid schemes. The pyramid games in Palm Desert, described above, collapsed when participants were indicted for violating a state law prohibiting such schemes. Legal authorities are active in prosecuting the organizers of the substantial number of pyramid schemes that have been established recently on the Internet. In 1996, the Federal Trade Commission obtained a federal court order halting a pyramid scheme advertised by Fortuna Alliance on the Internet. Minnesota used state consumer protection laws to prosecute a pyramid scheme advertised to America Online customers by an organization identified as International Network.

While chain letters promising large returns are common in the U.S., especially now on the Internet, they are prohibited by both federal and state law. In 1994, the New Jersey Bureau of Securities filed a cease-and-desist action against participants in the same chain letter that is currently operating on Internet news groups (Consumers' Research, 1994). In addition, since chain letters involving money are classified as gambling, use of U.S. mails to send money, as

required by such schemes, is illegal. Chain letters are also a violation of "appropriate use" policy as set by the government agencies that administer the Internet backbone. Supported by these legal prohibitions, individuals using the Internet frequently respond to chain letter postings on news groups with marked hostility. Recent responses included statements indicating that legal authorities or the U.S. Internal Revenue Service had been informed of the sender's notice, and requests to the administrator of the sender's server that the account be canceled. One user provided instructions on how to cancel a chain letter notice, essentially preventing the sender from distributing it.

In contrast to other pyramid schemes, some multi-level marketing arrangements are legal in the U.S. To be legal, returns must accrue from sale of a product, not from payments made by new recruits for the right to recruit others. Although legal multi-level marketing may have some elements of pyramid returns, the laws do restrict them in ways that limit their extent.

Explaining Pyramid Schemes in Romania and Albania

It is easy to dismiss most of the pyramid schemes springing up in Eastern Europe as the products of shady organizers preying on a small number of gullible initial investors. In contrast, the survival of Caritas in Romania and the nine large schemes in Albania are more difficult to explain. The single most important factor that distinguished Caritas from its short-lived competitors in Romania was the existence of strong initial support from government officials of a major city. With nearly half a million population, Cluj is a regional capital, competing with a small number of other Romanian cities with populations of less than a million for "second city" status after Bucharest. Space in government-owned offices gave the scheme a semi-official status. Support from Cluj mayor Funar, leader of a strongly nationalist Romanian political party, may have given a patriotic flavor to participation in the game for those sympathetic to nationalist politics. In the case of Albania, support for the schemes from the central government was much more explicit than in Romania, and this support appears to have been echoed by opposition politicians. In contrast to Romania, where elites were divided in their stance toward the pyramid schemes, few Albanian elites appear to have publicly criticized the schemes.

While the support of elites probably played an important role in both countries, there is no evidence that state resources were ever used to subsidize the schemes or that the police powers of the state abrogated property rights to foster the schemes' continuation. In neither country did the government ever pledge explicitly to make good the schemes' obligations. Rather, the local government in Romania and the national government in Albania were important primarily because they served to bolster general confidence in the schemes, where this confidence did not rest on any single guarantee or statement of purported fact. For many investors, it found form in the belief that new investors would continue to be drawn into the scheme--at least for a while. We suspect that although access to the media placed government officials in a position where they could aid the scheme in this way, since their actions did not rely on the powers of the state, highly visible support by other opinion leaders would have worked similarly.

A rather different analysis is necessary to explain why such a scheme succeeded in Romania and Albania and not in other countries. Observers frequently attribute the growth of such games to the low standards of living in these countries and the particularly severe economic hardship in the 1980s wrought by their repressive communist regimes. In terms of economic theory, it is tempting to assume that the absence of a free market experience left citizens of these countries with little basis to form rational expectations. If this were correct, such a scheme could not exist in developed economies.

Comparison with the U.S., where pyramid schemes are quite common, forces us to reject these explanations. Consistent with the observation in Romania and Albania, such schemes in the U.S. tend to survive longest when elites support them, for example, in the pyramid games observed in Palm Desert, California. However, chain letters, both those using the U.S. mail and computer links, exist as well, along with schemes advertised by various companies. Of course, none of the American schemes has had any major social or economic impact, and one reason is clearly the presence of legal sanctions. Continued active prosecution under innumerable local and federal laws means that no scheme in the U.S. can draw sufficient public attention--a necessity for a pyramid scheme--to grow as large as those in Romania and Albania.

The question then becomes one of political process. In the U.S., as in other free market economies, there is a substantial class of owners of capital who wish to channel investments into stable projects and to protect general confidence in existing investment structures. They have an interest in passing and enforcing laws that prohibit pyramid or Ponzi financing. It is interesting that the formal legal structures are fairly complex, and that direct pressure by financial leaders on state authorities to limit such schemes appears to often play a role. Pressure on local authorities by financial elites brought down Charles Ponzi. We suspect that the influence of the financial community plays a role in maintaining enforcement activities against current schemes.

Of course, neither Romania or Albania has a class of wealthy bankers and financiers, and so there was no group with a natural interest in closing down these schemes. If elites were overrepresented among the early investors, they might well benefit by the schemes even if most people ultimately lost money.²⁰

Pyramid Schemes, Speculative Bubbles, and Economic Theory

The analysis above suggests that, under some circumstances, large numbers of economic actors may behave in ways that violate assumptions of mutually consistent expectations. The qualitative description of investors' behaviors and beliefs corresponds closely with the dynamic which Kindleberger attributes to speculative manias. Yet, in the cases he considers, the existence of a base asset with a potential to yield returns makes it difficult to determine whether investors are irrational or merely mistaken. The fact that such a process can operate when the financing

²⁰ Verdery (1996) argues that Caritas and other pyramid schemes in Romania were created by coalitions "consisting of officials of the Communist Party, one or another fraction of the old/new Secret Police, members of the local police and judiciary, newly elected political officials, and the henchmen of all these--people like Stoica" (p. 197). The involvement of government officials in Albania is, of course, even clearer. Our view is that the organizers and beneficiaries of such schemes were merely entrepreneurs, taking advantage of an opportunity. Such individuals appear to exist in all economies, developed or not, and it is not surprising that they would include elites who would be able to attract participants to the schemes. What makes the Romanian and Albanian experiences different from that of developed economies is the absence of stakeholders with an interest in limiting such activities.

mechanism is an almost-transparent pyramid supports Kindleberger's claim that there need be little rational basis for investors' actions.

It is important to stress that Kindleberger does not view such episodes of irrational behavior as dominating economies. He suggests that when a variety of factors are coincident, such behaviors can grow to dominate certain markets. However, in the aftermath of the collapse of a bubble, fewer people are willing to make speculative investments, so such patterns cannot reoccur immediately. Only after some period of time, when memories have faded, do speculative bubbles again become possible.

Whereas Kindleberger's conclusions focus on actions by the monetary authority, the logic of his model would appear to suggest an important role for the state in overseeing investment arrangements. Actions to limit pyramid activities like those taken by governments in developed economies may be entirely appropriate if market pressures fail to do so. Of course, such an argument rests on at least a mild rejection of consumer sovereignty, since the justification for limitations on pyramid schemes assumes that individuals are unable to determine what is in their own best interests.

Conclusion: State Action in Pyramid Schemes and the Economy

The lesson for developing economies is that the structures necessary to provide for stable investment in the economy are complex, and they may require government intervention in a direct way. It does not appear that simple guarantees of well defined property rights, with the right to engage in mutually beneficial exchanges, are sufficient to ensure the existence of stable market behaviors. Of course, the argument for government involvement may be countered. It may be argued that if the government were to maintain a consistent *laissez faire* policy, institutional structures would develop to ensure the mutual consistency of expectations and the stability of markets. However, even if this is true, it still does not appear that such structures arise costlessly. Government involvement is ubiquitous in the developed economies, so we do not observe any environment where such free market structures assure market stability without support from the powers of the state. A more radical argument would oppose government intervention on the grounds that pyramid schemes are merely a form of gambling, which

participants value, and is therefore welfare enhancing. Of course, no developed economy allows unrestricted production and consumption of such "services"; even conventional gambling is severely restricted.

The growth of games like those observed in Romania and Albania should be of concern to the newly free economies. They demonstrate the potentially irrational structure of investor behaviors and they draw resources from productive activities that are necessary for development. Kindleberger's analysis suggests that the dynamic is similar in fraudulent schemes based on Ponzi financing.

One danger is that these schemes and related fraudulent investments will dampen the willingness of participants in the newly free economies to invest in productive activities. In his discussion of the South Sea bubble, Carswell (1960) argued that its effects on England were so profound that economic innovation ceased for nearly 50 years, government restraints and private fear of uncertainty overwhelming interest in any investment that might be viewed as speculative. In that period, he described England as "cautious, cynical, and artificial, clinging to all that was vested and established: a world we can study in slow motion" (p. 270). We hope that the governments of Romania, Albania, and the other transition economies do not follow a policy of retrenchment in the wake of Caritas and other speculative collapses that will restrain the inventiveness that is necessary for long term economic growth.

Conclusion: Security Implications in the Aftermath of the Collapse of the Pyramids

With regard to Romania and Albania alike, the pyramid schemes and speculative bubbles analyzed here damaged and, in many cases, destroyed the economic security of literally millions of individual investors. At best these schemes supplanted economic productivity; thereby weakening the long-term economic security of the state by tarring the public perception of the market economy. This undermined popular confidence in the ability of existing governments and politicians to guide needed economic restructuring. To the extent that government officials and opposition leaders supported and were associated with these economic earthquakes, their legitimacy declined and the process of building a stable multiparty system (political institutionalization) itself suffered.

The political consequences for Romania appear to have been much less severe than those in Albania. In Romania, the political and social turmoil that had been predicted following the collapse of Caritas failed to materialize, and none of the schemes that followed it attracted similar levels of investment. While many Romanians believed that government complicity played an important role in the rise of Caritas and that government officials benefited from the scheme in various ways, the losses experienced by most investors appear to have done little more than contribute to the already-high level of distrust in the government. On the other hand, the number and extent of fraudulent schemes using Ponzi financing appear to have grown in Romania. A private company Sabina Product SRL collected \$24 million from investors in Bucharest in 1995, promising 20 percent interest per month, before its organizers fled (Reuter, 1995). Two medium sized private banks, Dacia Felix and Credit Bank, both located in Cluj, are currently in the midst of financial crises following revelations of major losses due to poor lending practices, and, in the case of Credit Bank, fraud (Eremia, 1996).

Romanian free market reforms have been halting and slow, but it is difficult to determine whether Caritas or the various fraudulent investment schemes which followed it played a role. Certainly, these added legitimacy to the widespread perception that uncontrolled financial markets would not necessarily operate to the benefit of the populace and in that way contributed to the support for continued direct government control in the market. However, since popular and elite support for the free market reforms have been unsubstantial since the 1989 revolution, there is little evidence that the trajectory of reform shifted significantly after the decline of the schemes, and there is no indication that the stability of the Romanian state was adversely affected.

In contrast, in Albania the internal security system, already weakened by the Berisha government's purge of the Albanian armed forces, crumbled. Thousands of Albanians fled to Italy or Greece; those who remained faced the prospect of civil war. In the more traditional sense of military security, the economic collapse pushed Albania off the road from Communism to Democracy into armed anarchy. By March 28 this led to a U.N. Security Council Resolution calling for a multilateral force of some 2,500 troops, with another 2,500 in reserve, to "protect humanitarian relief assistance." This move came on the heels of an Italian threat to act

unilaterally if something was not done to stem the refugee flood of more than 13,000 Albanians that had already arrived in Italy. The U.N. and the Organization for European Security and Cooperation in Europe (OESCE) moved to restore order and to stop the human hemorrhaging by establishing conditions for internationally monitored June elections. The justification of this U.N. resolution hinged on issues of regional security defined in fears that the unrest could “spill over into ethnic Albanian minorities in neighboring states, encouraging them to seek a ‘greater Albania’ ” (Lewis, 1997).

The appeal of a ‘greater Albania’ is exaggerated. Albanians in Kosovo and Macedonia are not naive. They know that linking up with an Albanian government that by May 1997 is still not in total control of the country with U.N. troops mandated to leave in June would not improve their living conditions or political situation. Whether the Berisha government or an opposition coalition led by Albanian socialists is in control, Albania has no help or resources to give in the foreseeable future.

Yet essential abandonment of Kosovo in December 1991 by the EC and the international community combines with the current crisis to form a different kind of dangerous mix. At that time, the Kosovo appeal for recognition was rejected while those of Slovenia and Croatia were accepted. Subsequently the 1995 Dayton Accords, implementing plans in Eastern Slavonia in Croatia as well as Bosnia and Herzegovina, were put in place. In an attempt to prevent the spread of unrest into Kosovo, the leader of the nonviolent resistance movement in Kosovo, Imbrahim Rugova has been pressured into postponing until December 1997 the election that he had called for September. The U.S. and other foreign diplomats have told Kosovo Albanians to forget about independence and to take part in the democratization of Serbian politics instead (RFE/RL Newswire, vol. 1, part II, 7 May 1997).

On the spectrum of Kosovo political options, this message can only weaken Rugova’s Democratic League of Kosovo in favor of more militant alternatives. In an interview with New York Times correspondent Chris Hedges in Geneva, the anonymous leader of the Kosovo Liberation Army insisted that “we are not a terrorist organization . . . we have support of nearly all Albanians . . . we target the secret police, Albanians who collaborate with the regime, and Serbian leaders” (Hedges, 1997). Reports that in recent months the frequency and

professionalism of his organization's killings has increased (RFE/RL Newline, vol. 1, no. 28, part II, May 12, 1997) do not encourage optimism for internal security within Kosovo, Serbia, or the Federal Republic of Yugoslavia.

The choreography of such political violence, escalating state violence in response, widening support for militants at home and economic support from abroad is an old dance of death that only expands the killing fields. And if war comes to Kosovo, it remains to be seen what would happen to the ultimatums of Presidents Bush and Clinton, to Serbian President Slobodan Milosevic, that the U.S. would intervene unilaterally if necessary to prevent such bloodshed.

With regard to Macedonia, it appears that the Macedonian government has not been able to learn from economic disaster next door. On May 9, 5,000 people demonstrated in Bitola, demanding that the government foot the bill for money lost in the collapse of the local TAT pyramid scheme. There are promises of partial reimbursement and legal proceedings against key figures responsible for the scam (RFE/RL Newline, vol. 1, no. 28, part II, May 12, 1997). Although the initial response by the ruling Socialist Party has not been to play the national card by hardening policies toward the Albanian minority in Macedonia, the security implications of promised early elections in November 1997 are unpredictable, especially in the context of Macedonian student anti-Albanian demands during demonstrations this spring and opposition parties' attempt to take advantage of the student movement.

The bottom line for post-communist politicians and societies struggling to make painful transitions to democracy and the market beyond the once 'iron curtain' is that economic, political and traditional military security concerns have become entangled-- as a Serbian village proverb might put it--like a pig's intestines. Moreover, there is substantial tension between internal security and the economic rules of the game as established by international financial power brokers. While international money lenders were free with their advice about the dangers of get-rich-quick schemes, they do not appear to have had particularly helpful suggestions for alternatives that would allow politicians who played by their economic rules to help their increasingly impoverished voters survive.

Indeed, to whatever degree post-communist security is a matter of psychological credibility, the damage from the economic collapse in Albania goes beyond the Berisha regime to tar Western financial and political advisors that attempted to turn Albania into a showcase of beneficial multinational influence. There are reports that the U.S. and Europe treated Albania “like a colony . . . The United States put advisers in the Presidency and Ministries of Finance and Defense. Italy advised the Privatization Ministry, and Germany helped out in the Ministry of Interior” (Perlez, 1997). Attacking Berisha for ramming through an inadequate election law (RFE/RL Newslines, vol. 1, no. 30, part II, May 14, 1997) will not answer questions about the shared responsibility of Western influence for fathering what appears to be an at least temporarily abortive effort to give birth to a democratic Albania with a functioning market economy.

References

Carswell, John. *The south sea bubble*. London: Cresset Press, 1960.

Çela, Blerim. "I Do Not Believe the Money-Borrowing Firms Will Go Bankrupt." *Albania*, 21 November 1997, p. 3.

Consumers' Research. "On-Line Investment Schemes." *Consumers' Research Magazine*, August 1994, 77(8), p. 19.

Done, Kevin and Hope, Kerin. "Violence As Forth Albania Fund Collapses." *Financial Times*, 6 February 1997, p. 2.

Economist Intelligence Unit. *Country Report: Romania, Bulgaria, Albania*. 4th quarter 1994 ed. New York: The Economist, 1994.

Emshwiller, John R. "What Is There to Do On a Sweltering Day in Palm Desert, Calif.?" *Wall Street Journal*, 12 July 1996, p. 1.

Eremia, Mirela. "Scandal and Scrutiny Rock Romania Banks." Reuter European Business Report, 22 July, 1996.

Friedman, Milton. "In Defense of Destabilizing Speculation," in *The optimum quantity of money, and other essays*. Chicago: Aldine, 1969, pp. 285-91.

Goga, Tiberiu. "Caritas-UI Ne Va Ajuta Intotdeauna, Daca Ramanem Alaturi De El." *Mesagerul transilvan*, 11 November 1993, p. 3.

Hedges, Chris. "A Flurry of Violence As Another Balkan Ethnic Hot Spot Smolders." *New York Times*, 11 May 1997, p. Y4.

Hockstader, Lee. "Albania Dreams Shatter in Pyramid Schemes' Fall." *The Washington Post*, 2 February 1997, p. A32.

Iliazi. "Vefa's Business and the Pyramids of the Press." *Albania*, 2 November 1996, p. 3.

Kallamata, Arben. "Foul Political Speculation Over Moneylending." *Albania*, 14 November 1996, p. 3.

Kindleberger, Charles P. *Manias, panics, and crashes: A history of financial crises*. Second ed. New York: Basic Books, 1989.

Kling, Arnold. "Make Money Fast."

<http://nearnet.gnn.com/gnn/meta/finance/feat/archives.focus/pyramid.html>, 1996.

Lewis, Paul. "U.N. Backs Sending Troops to Restore Order in Albania." *New York Times*, 29 March 1997, p. 4Y.

Maniu, Mircea T. and Mueser, Peter R. "Pyramid Schemes and Individual Investment in the New Free Economies of Eastern Europe: The Case of 'Caritas' in Romania." Paper presented at the Central Slavic Conference Panel: Economic Security and Public Policy, Columbia, Missouri, October 1996.

Minsky, Hyman P. "The Financial Instability Hypothesis: Capitalist Processes and the Behavior of the Economy," in Charles P. Kindleberger and Jean-Pierre Laffargue, eds., *Financial crises: Theory, history and policy*. New York: Cambridge University Press, 1982.

Mihu, Achim. "Caritas, Objectiv Pentru Cercetarea Stiintifica." *Mesagerul transilvan*, 5 November 1993a, pp. 1,3.

Mihu, Achim. "Primele Rezultate Ale Cercetarii Sociologice Asupra Caritas-Ului." *Mesagerul transilvan*, 7 December, 9 December 1993b.

Morris, Seymour. "Caritas: The Best Thing That's Happened to Romania." *Business Tech Romania*, September/October 1993, 1(13), p. 7.

Mueser, Peter R. and Franz, Charles. "Fenomenul 'Caritas'." *Business Tech International*, 1993a, 13, pp. 34-35.

Mueser, Peter R. and Franz, Charles. "Investment and Pyramid Games in Post-Communist Romania." *Business Tech Romania*, September/October 1993b, 1(13), pp. 7,12.

Nehra, Gerald P. "Ponzi or Pyramid." <http://www.ultimate.org/nehra.ponzi.html>, 1996.

Perlez, Janet. "Pyramid Scheme a Trap for Many Romanians." *New York Times*, 13 November 1993, pp. 1, 47.

Perlez, Janet. "Albania Is Cast Adrift." *New York Times*, 29 March 1997, p. E3.

Reuter. "Rumania to Ask Budapest to Extradite Pyramid Boss." 28 December, 1995.

Russell, Francis. "Bubble, Bubble-No Toil, No Trouble." *American Heritage*, February 1973, 24(2), pp. 74-80, 86.

Shafir. "The Caritas Affair: A Transylvania 'Eldorado'." *RFE/RL Research Report*, 24 September 1993, 2(38), pp. 23-27.

Toader, Sergiu. "'Caritas' Pregateste Autonomia Ardealului." *Evenimentul zilei*, 20 August 1993, p. 3.

Todosiciuc, Toni. "Jocurile De Intrajutorare Din Intreaga Tara Se Prabusesc." *Evenimentul zilei*, 11 February 1994.

Verdery, Katherine. "Faith, Hope, and Caritas in the Land of the Pyramids, Romania, 1990-1994," in *What was socialism, and what comes next?* Princeton, N.J.: Princeton University Press, 1996, pp. 168-203.