MONITORING COUNTRY PROGRESS IN CENTRAL AND EASTERN EUROPE & EURASIA

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SUMMARY

I. Introduction and Methodology

This paper presents USAID/E&E's system for monitoring country progress with a focus on developing criteria towards graduation from USAID assistance. Country progress is analyzed in a sequence of steps for twenty-seven countries of the region. First, we look at the progress towards economic reforms and democratization. Progress on both fronts must reach a certain threshold before we can begin to consider graduation.

Next, we look at indications of sustainability; that is, macroeconomic performance and social conditions. Economic reforms need to translate into solid macroeconomic performance if they are to be sustained. Trends in social conditions need to be tracked as well to give us a pulse on the possibilities of economic and democratic "reform fatigue." Social conditions or living standards influence macroeconomic performance, too.

The primary indicators are drawn from standard, well-established data sources that are external to USAID. This edition taps several household surveys as well, partly as a check on the macro indicators. An important step of the process is the holding of annual reviews—one for Central and Eastern Europe (CEE), one for Eurasia—with area specialists from U.S. government agencies.

II. Findings

(a) Economic and democratic reforms

The *Summary Figure* suggests that there are now broadly two country groups differentiated by progress towards economic and democratic reforms, the eight Northern Tier CEE countries and the rest. The distinction between a large middle tier of reformers and a handful of lagging countries, evident in previous summary figures, has blurred.

Particularly with Slovakia now in the "fold," the Northern Tier leaders are more closely aligned in terms of reform progress than ever before. By Freedom House measures, all eight countries—the Czech Republic, Estonia, Hungary, Lithuania, Poland, Slovenia, Latvia, and, most recently, Slovakia—have political rights and civil liberties that are roughly comparable to those found in Western Europe. By EBRD scores, first stage economic reforms (of liberalization and legislation of the commercial law framework) are generally complete. In addition, all the Northern Tier countries are out front of the other transition countries in second stage economic reforms (of institution building and structural change).

Of this group of eight, four countries continue to lead: Hungary, followed by Poland, Estonia, and the Czech Republic. By industrial market economy standards, however, even these Northern Tier leaders have far to go in progress in second stage economic reforms. Nevertheless, all eight countries, alongside Romania and Bulgaria, have now been invited to participate in negotiations toward EU membership. This is strong incentive for further reform progress.

Large differences characterize the reform progress in the remaining nineteen transition countries. A handful of Southern Tier CEE countries lead this group: Bulgaria, Romania, Macedonia, and, now with the favorable change in political regime following Tudjman's death, Croatia is not far behind. Of the Eurasian countries, Moldova and Georgia come closest to this Southern Tier group in reform progress. These seven countries all seem to be moving forward in at least one of the two reform aspects (that is, economically and/or democratically), though the trend is more mixed in the case of Moldova and Georgia.

Russia saw further erosion on balance in reform progress in 1999. Russian civil liberties deteriorated due to growing harassment of ethnic Chechens and increased political interference in the media over the Chechnya crisis. Slight gains in implementing legal reforms were outweighed by continued backsliding in efforts to reform and restructure the banking sector and the private sector more broadly. Some progress in fiscal reforms is reflected in better tax compliance and in a more manageable fiscal deficit.

At the tail end of the reform spectrum are Turkmenistan, Belarus, and Uzbekistan. Reforms in Bosnia-Herzegovina and Tajikistan are not much more advanced. Turkmenistan is one of only thirteen countries worldwide rated by Freedom House to have the fewest political rights and civil liberties in 1999. Basic political rights are nonexistent, and an independent civic life, including a free media, is effectively suppressed. Democratic freedoms in the other lagging countries, particularly in Uzbekistan and Belarus, are not much greater.

In first stage economic reforms, Turkmenistan and Belarus lag behind all other transition countries, and far behind most. In both, government control of prices is extensive. Trade and foreign exchange restrictions are significant. Legal rules are limited in scope and are inconsistent. Turkmenistan is farthest behind all the transition countries in second stage economic reforms, though such reforms in Belarus, Tajikistan and Bosnia-Herzegovina are not much more advanced. In these countries, large scale privatization has either just begun, or, in the case of Belarus, it has stalled. Soft budget constraints are pervasive. Widespread market entry restrictions for firms exist, and, except perhaps for Belarus, competition legislation and institutions do not exist. Banking sectors remain controlled by government.

The differentiation in reform progress between the CEE countries and Eurasia continues to grow. In other words, most of the reform progress in the transition region in 1999 occurred in the CEE countries. Six of the seven countries that experienced gains in both economic and democratic reforms in 1999 are CEE countries: Slovenia, Latvia, Slovakia, Bulgaria, Romania, and Croatia. Tajikistan is the only Eurasian country to have managed progress in both reform domains, though Kazakhstan and Azerbaijan made progress in economic reforms while maintaining no measurable slippage in democratic reforms.

By EBRD and Freedom House measures, reform backsliding in Belarus in 1999 continued a longer-term trend over the transition. In fact, while partial or temporary setbacks in many transition countries have been common, Belarus is distinguished by being the only country that is farther behind in economic reforms today than when the EBRD starting tracking such progress in 1994.

Private sector share of GDP is now roughly sixty-one percent on average for the transition region as a whole. This represents very impressive gains from 1989 when it was probably closer to ten percent of GDP. Nevertheless, seven countries (six Eurasian countries plus Bosnia-Herzegovina) still have economies in which more than fifty percent of economic activity derives from the public sector. Of these seven, Belarus has the largest public sector relative to GDP, at eighty percent. All but Moldova rank at the bottom of the economic reform scores.

Household survey data suggest that, as with economic reforms, it may be helpful to distinguish between first stage and second stage gains in democratic freedoms.[1] One important conclusion from these data is that very impressive political gains have been realized and shared broadly across much of the transition region. However, these are the relatively easy gains (or "first stage" gains) that resulted early on with the collapse of communism: the freedoms to say what one wants; to associate with whomever; to pursue political and religious activities (or, in the case of many, at least at the outset, to choose to be inactive politically). On average, eighty percent of the sample in the fifteen countries felt that these political freedoms were greater under the existing political system than they were under communism, and almost one-half felt the situation was much better in 1998.

"Second stage" political gains, however, have been far more elusive. These are the gains that stem from good governance and hence require institutional development: being treated fairly and equitably by government; having an ally in government to encourage household economic improvement. Overall, forty-one percent of the respondents saw gains in these freedoms since communist days, and only sixteen percent felt the progress was much better. Similarly, a widely shared perception across the region is that corruption is significant and worse than it was under communism, and that government is part of the problem.

More generally, there exists very little trust in key institutions. This includes government, but also private enterprise. Approximately three out of four persons sampled across the countries have little to no trust in key government institutions. The least trust is given to parliament, though civil servants, courts, and police similarly inspire little. While mistrust of formal institutions is highest in Eurasia, it is also a characteristic to varying degrees in CEE. Some of these findings, in fact, contribute to a more sobering

[1] These data are drawn from three household surveys from the Centre for the Study of Public Policy (CSPP) and cover fifteen transition countries: eight Northern Tier CEE countries (the three Baltics were last surveyed in 1996; the Czech Republic, Poland, Hungary, Slovakia, Slovenia in 1998); four Southern Tier CEE countries (Romania, Bulgaria, Yugoslavia, and Croatia in 1998); and three Eurasian countries (Russia, Ukraine, and Belarus, or seventy-three percent of the Eurasian population, in 1998). *Appendix II* elaborates.

view of progress in democratic reforms in the Northern Tier countries than that which is implied by Freedom House's overall ratings.

(b) Macroeconomic performance

Macroeconomic performances in the transition region in 1999 generally exceeded expectations from earlier forecasts. For many of the CEE countries at least, such performances in 2000 are currently poised to be better still. Performances and prospects vary widely, however, and are conditioned largely on progress towards stabilization and structural reforms, as well as the extent and character of a country's integration into the global economy. Similarly, the relatively favorable economic performances in many of the Eurasian countries, Russia foremost among them, may not be sustainable.

In striking contrast to earlier estimates, overall economic activity in the Eurasian countries was greater in 1999 (at 2.7 percent on average) than in any other transition year. Russia's economic growth of 3.2 percent weighed heavily into this population-weighted subregional average.[2] Of all the Eurasian countries, only Ukraine and Moldova failed to register official economic growth in 1999; Ukraine remains the only transition country yet to experience such growth since communism's collapse.

Russia's economic links with its Eurasian neighbors, while still strong, may be weakening. For one, much of the basis for Russia's economic growth in 1999 was due to import-substitution activities. Imports in Russia became more expensive as a consequence of the August 1998 devaluation, and domestic production replaced much of what was previously imported, most of which came from elsewhere in Eurasia. Similarly, the crisis in Russia may have expedited a trend towards greater diversification of trade among most of Russia's neighbors, lessening the reliance on Russia's economy. Available data show exports to Russia as a percent of GDP continuing to fall significantly in many Eurasian countries, particularly in Kazakhstan, Uzbekistan, Armenia, Kyrgyzstan, and more recently, Moldova. Economic ties between Belarus and Russia may be the salient exception to this trend, as support for greater integration between the two countries continues to grow.

Dramatic shifts in the prices of commodity exports for the Eurasian countries continued to factor prominently in economic growth in 1999. The significant reversal in the trend in oil prices (from a thirty percent drop in 1998 to close to a forty percent increase in 1999) boosted export revenues and economic growth in the oil exporting countries of Russia, Kazakhstan, Turkmenistan, and Azerbaijan, and increased import prices and inflationary pressures in the oil-importing countries of Moldova and Ukraine.

In the Southern Tier CEE countries, the Kosovo conflict significantly tempered macroeconomic performances, though not to the extent that was initially estimated. Macedonia and Bulgaria were forecast to be among the hardest hit of the front line states to Yugoslavia. Yet, both experienced moderate economic growth of at least 2.5 percent in 1999. The economies of Bosnia-Herzegovina and Albania grew even more, by eight

[2] Virtually all forecasts one year ago had Russia's economy in 1999 contracting by at least four percent.

percent. Economic activity outpaced initial expectations for a number of related reasons: the Kosovo refugees returned sooner than expected; the frontline economies likely showed greater flexibility in finding export markets (new and old); reform progress was maintained or reform slippage was minimized; and, particularly in the case of Macedonia, opportunities arose from the reconstruction of Kosovo and a large international presence.

Given that the economies of both Romania and Croatia contracted in 1999 (by 3.9 and 2.0 percent, respectively), overall economic activity in the Southern Tier region was flat for the year (at -0.4 percent). However, export markets, particularly those in Western Europe, are strengthening. Partly as a result, and partly from anticipated continuation of recent reform progress, modest recoveries are forecast for the economies of both Romania and Croatia in 2000. For the subregion overall, however, much continues to hinge on developments in Yugoslavia and in the implementation of the Stability Pact.

Economic growth in the Northern Tier CEE countries has slowed considerably in recent years, from 5.7 percent in 1997, to 3.7 percent in 1998, to 2.7 percent in 1999. Much of this has been due to close economic ties to countries that have been experiencing economic slowdown or contraction. In 1999, due to close trade links with the EU, all the countries of the Northern Tier witnessed slower growth, as economic growth in Western Europe slowed (to 2.3 percent), and with it, demand for Northern Tier CEE exports.

Three Northern Tier countries had contracting economies in 1999, Lithuania, Estonia, and the Czech Republic, and two experienced very weak economic growth (of around one percent), Slovakia and Latvia. Partly because of improving economic conditions with trading partners and continued economic reform progress, all are currently forecast to have growing economies in 2000, though only marginally in the case of the Czech Republic and Lithuania.[3] The Czech Republic's economy has been stagnating since 1997.[4] Highest sustained economic growth among the Northern Tier CEE countries has most recently been occurring in Poland, Hungary, and Slovenia, at roughly four percent or higher during the past three years or more.

Inflation rates have come down impressively in most countries since the early 1990s. In fact, seventeen countries have been able to hold inflation in the past two years to close to single-digit levels. Nevertheless, large distinctions in inflation rates remain, particularly between CEE and Eurasia. In particular, all but one of the ten countries that had inflation rates in 1999 close to twenty percent or higher are in Eurasia. Romania, with an inflation rate of forty-six percent in 1999, was the exception.

[3] Of key significance is the rebound in economic growth in the EU, now forecast to be 3.2 percent in 2000. Also important, however, is the improvement in the investment climate as the uncertainties brought on by the Russian financial crisis continue to fade.

[4] Earlier successes by the Czech Republic, characterized by rapid economic growth by 1995 and strikingly low unemployment, proved to be short-lived largely because of the postponement of key, albeit painful, structural reforms. Soft budget constraints early on contributed to growing weaknesses in corporate governance structures, increasing macroeconomic imbalances, and, more generally, a decline in competitiveness. By 1997, tighter bank regulations began to address these problems, though the shakeout due to tighter credit and harder budget constraints on firms also contributed to greater bankruptcies, a decline in output, and, as experienced elsewhere in the region, growing unemployment.

Macroeconomic imbalances continue to be troublesome for a number of transition countries. Most of them are in Eurasia, but neither the Southern Tier nor Northern Tier CEE countries have been immune to these trends. In fact, the Northern Tier fiscal and balance of payments current account deficits on average have been increasing since the mid-1990s; by 1999, they were six percent and 3.9 percent of GDP, respectively.

Seven countries have sustained fiscal deficits greater than five percent of GDP on average since 1997: Albania (11.3 percent); Kyrgyzstan (10 percent); Kazakhstan (7.3 percent); Moldova (6.7 percent); Armenia (5.7 percent); Russia (5.1 percent); and Lithuania (5.4 percent). Seven countries have sustained current account deficits greater than ten percent of GDP since 1995: Bosnia-Herzegovina (thirty-five percent); Armenia (twenty-nine percent); Azerbaijan (twenty-four percent); Turkmenistan (seventeen percent); Kyrgyzstan (fifteen percent); Moldova (fourteen percent); and Lithuania (eleven percent). Armenia, Kyrgyzstan, Moldova, and Lithuania fall into both categories.[5]

Related to deficits is external debt. According to World Bank estimates, the present value of external debt has increased significantly in Eurasia from 1996-1998, but has remained relatively constant (as a percent of GDP) or has decreased (as a percent of exports) in the CEE countries. Servicing the debt remains manageable for most transition countries (*Table 14*), though debt service has increased for many countries in recent years. Hungary, Romania, and Moldova have had the highest debt service in recent years, roughly thirty percent of exports in either 1998 or 1999. Georgia and Lithuania had to service an external debt equal to twenty percent of exports on average in 1998-1999.

(c) Living standards

The standard indicators of social conditions continue to show a large gap between the quality of living in CEE, particularly in the Northern Tier, with that in Eurasia. Household survey data, however, suggest that in some important dimensions this gap may not be quite so large.

Per capita incomes in the Northern Tier countries are almost two times the average per capita incomes in Eurasia and the Southern Tier CEE countries. Per capita income in four Northern Tier countries (in purchasing power parity terms) is close to $10,000 or more: Slovenia ($14,950); the Czech Republic ($12,140); Hungary ($10,230); and Slovakia ($9,720). In contrast, a handful of Eurasian countries have average income levels closer to $1,000 to $2,000: Tajikistan ($1,080); Moldova ($1,900); Uzbekistan ($2,120); Armenia ($2,150); Kyrgyzstan ($2,300); and Azerbaijan ($2,330). Slovenia ranks thirty-three (out of 174 countries) in the UNDP's human development index, comparable to Chile; Tajikistan ranks 108th, and us closest to Algeria and El Salvador.

[5] Reported fiscal deficits often understate the magnitude of the problem. Not captured in these figures are arrears and "off-budget" expenditures.

Official GDP on average in the Northern Tier is greater than pre-transition income levels (*Table 18*). In the Southern Tier countries, 1999 GDP is roughly only three-fourths 1989 income; in Eurasia, it is less than sixty percent.

In general, while virtually all the transition economies had relatively equal income distributions prior to communism's collapse, virtually all have since experienced very significant increases in income inequality. For the Northern Tier CEE countries, where the increase (of about thirty percent from 1989 to 1997) has not been as great as in the other transition subregions, income inequality is now roughly comparable to that found in the advanced industrialized economies. In the Southern Tier CEE and in Eurasia, income inequality increased by more than fifty percent from 1989 to 1997. Income inequality in some of these countries now compares to that found in the most unequal economies worldwide, that is, those in Latin America and in Sub-Saharan Africa. This includes Georgia, Russia, Azerbaijan, Kyrgyzstan, Romania, and Ukraine.

Widely cited income-based poverty estimates for 1993-1995 show one out of ten persons in the Northern Tier is impoverished. In the Southern Tier, it is one out of every four persons; in Eurasia, it is closer to one out of two.

Infant mortality rates have fallen for all the transition countries from 1989 to 1998 except three: Latvia, Ukraine, and Bulgaria. The Northern Tier trends (Latvia notwithstanding) have been particularly impressive. Infant mortality rates were the lowest in the Northern Tier CEE countries at the outset of the transition and have fallen the most there during the transition, by almost one half. Nineteen ninety-eight infant mortality rates in the Northern Tier (at nine deaths per 1,000 live births) are now actually below the OECD average (of ten deaths) and are approaching the EU average (of five deaths). The average rates in Eurasia and the Southern Tier CEE countries are both seventeen deaths per 1,000 live births; i.e., almost twice the Northern Tier rates. They are highest in the Central Asian Republics (twenty-five deaths per 1,000 live births on average), Albania (twenty-five deaths), and Romania (twenty-one deaths). The most significant decline in child mortality rates, as with infant mortality rates, has occurred in the Northern Tier countries, by one-third from 1990 to 1998.

By 1998, life expectancy was close to seventy-three years in the Northern Tier, an increase of four years since 1980 and almost two years since 1989. By comparison, life expectancy in the EU is seventy-nine years on average. Life expectancy in Slovenia and the Czech Republic (both at seventy-five years) come closest to the EU standard. Life expectancy is closer to sixty-seventy years in Eurasia, an insignificant drop since 1980, but a fall of about two and one-half years since 1991-1992. The biggest drops in Eurasia have occurred in Kazakhstan, Ukraine, and Belarus. Life expectancy in the Southern Tier countries falls somewhere between that of the other two subregions, in 1998, almost seventy-one years on average. This is an increase of one year since 1980, but a decrease of about one year since communism's collapse.

Secondary school enrollment has increased from 1990 to 1997 in most of the Northern Tier CEE countries, while decreasing in most other transition countries. Greatest drops have occurred in Albania (by over one-half), Tajikistan, Kyrgyzstan, Georgia, Romania, Azerbaijan, and Kazakhstan. Secondary school enrollment in the Northern Tier CEE (at almost ninety-seven percent) is below the EU average (of one hundred and eight percent). While continuing to drop on average, it is still high in Eurasia (eighty-four percent). At seventy-two percent, it is lowest in the Southern Tier CEE countries. In 1997, only thirty-eight percent of school age children in Albania were enrolled in secondary schools, far and away the lowest enrollment of the transition countries.

Household survey data suggest more nuanced distinctions in living standards across the transition countries. First, the income-based estimates of poverty mentioned above may overestimate the hardships implied in many of the lagging transition countries. Household survey data from the CSPP (referred to in footnote #1), as well as from the Russia Longitudinal Monitoring Survey (RLMS) provide household expenditure patterns that suggest hardships may be less severe or less widespread than that which is implied by the commonly-used poverty rates.[6] The CSPP surveys, for example, ask households the extent to which they are deprived of food, heating and electricity, and necessary clothing. The percent of the population that often is denied these necessities might be a reasonable proxy for poverty rates.

For the CEE countries, the percentage of households often doing without necessity goods is low; only three percent on average often did without food over the course of the month in 1998 prior to being interviewed. For the population sampled in the three Eurasian countries (Russia, Belarus, and Ukraine), the proportion deprived of necessity goods is much higher, not surprisingly. Yet, these proportions are not as high as the income-based poverty rate estimates. In Russia, for example, forty-four percent of the population was estimated to be below the income poverty line in 1995, yet only nineteen percent in 1998 of those sampled were often being deprived of food. Forty-two percent of those sampled in Ukraine were often being deprived of food, not nearly as high as the poverty estimate of sixty-three percent.

The RLMS survey, on the other hand, confirms that poverty in income terms is significant in Russia (thirty-nine percent in November 1998), and has increased dramatically since the beginning of the transition. The RLMS survey also finds that poverty in Russia is becoming increasingly "deep." In particular, almost one-half of those Russians in poverty in 1998 had incomes less than fifty percent of the poverty line. This finding runs counter to the conventional view, which is based on available albeit dated figures (from 1992-1994) for the transition region, that poverty is "shallow" in most of the transition countries; that is, that most of those impoverished have incomes close to the poverty line.

Yet, the RLMS survey also finds expenditure patterns that reveal some very tangible gains among the Russian consumers. In 1992, fifty-five percent of Russian households owned a color TV; in 1998, seventy-four percent did. In 1992, three percent of

[6] The RLMS collects household data on economic and health trends in Russia. It has been coordinated by a University of North Carolina team led by Barry Popkin, and has had two phases of a total of eight survey rounds from 1992 to 1998. *Appendix II* elaborates.

households owned a VCR; this had increased to thirty-two percent by 1998. More impressive perhaps has been the shift to private ownership of houses. In 1992, twenty-five percent of houses were privately owned (and owner-occupied). This had increased to sixty-one percent by 1998.

An important reason why income-based poverty estimates may overestimate hardships in some instances is because of the existence of a large informal economy, which also serves as an informal safety net. Data from the CSPP surveys show that only about twenty percent of the households of the fifteen countries sampled are able to make the necessary purchases from the income derived from jobs in the formal economy alone. However, when one combines formal economic activity with participation in the informal economy (both monetary gains and barter activities), one finds that almost seventy percent of all the households polled are able to get by without drawing on savings or going excessively into debt. By these measures, informal economic activity is significant across the subregions.

The RLMS survey confirms the presence of significant informal economic activity in Russia. In 1998 for the entire sample, thirty-three percent of household income on average was derived from a combination of informal sector activity plus family and charity transfers. The poorest Russians are more dependent on the informal economy (particularly the barter or non-monetary activities) and private safety nets; forty-four percent of income derives from these sources for the lowest income quintile. Home production of food is a key component in this.

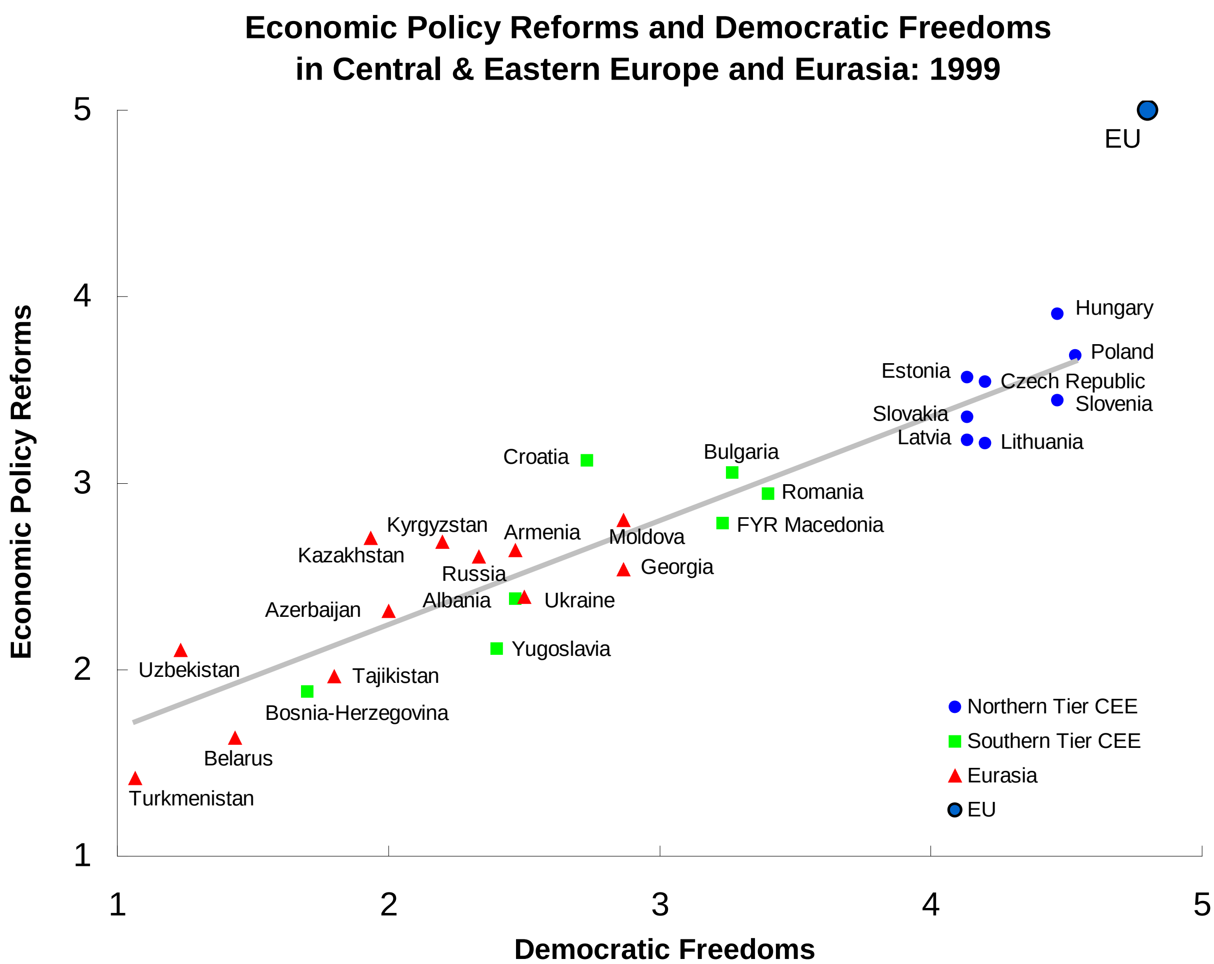
Finally, while income and expenditure patterns for those in the Northern Tier countries generally show hardships to be minimal, and while macroeconomic conditions are generally favorable, these trends do not necessarily translate into satisfied customers of these newly emerging market economies. According to CSPP data, almost sixty percent of those sampled in five Northern Tier countries in 1998 were unsatisfied with their household's economic situation. Fifty-four percent of these persons felt that their economic situation in 1998 had deteriorated since 1993. Less than twenty percent felt it had improved. The proportion of persons in these five Northern Tier countries who would like to see a return to communism remains relatively low (nineteen percent in 1998), but it has been rising; it was fourteen percent in 1995.

III. Concluding remarks

Decisions on the magnitude and duration of U.S. assistance to the E&E region are made on the basis of several factors: (1) progress the country has made toward a sustainable transition to a market-based democracy; (2) strategic importance of the country to the United States; (3) importance of the recipient country to U.S. citizens; and (4) effectiveness of particular assistance activities.

This paper presents an approach to analyzing the first factor. Particular country levels will likely be shaped in part by whether a given country falls into one of several categories, based on the analysis of country performance indicators. Countries ranked near the top of the list are obvious candidates for earlier "graduation." Other countries would seem to fall into one of three categories: (1) those where assistance is least likely to be effective, in which case it may make sense to close those programs down altogether or to keep highly targeted funding at minimal levels until commitment to reform increases; (2) those where reform now appears likely but requires greater resources; or (3) those which possess characteristics that match well with the Agency's priorities for sustainable development programs (i.e., development assistance or DA funding).

Summary Figure



Ratings of democratic freedoms are from Freedom House, *Nations in Transit 1999* (May 2000, forthcoming) and Freedom House, *Freedom in the World 1999-2000* (May 2000, forthcoming), and assess reforms through December 1999. With one exception, economic policy reform ratings are from EBRD, *Transition Report 1999* (November 1999), and cover events through September 1999; economic policy reform rating for Yugoslavia is from Freedom House (May 2000). Economic policy reforms include price liberalization, trade and foreign exchange, privatization, legal, banking and capital markets, enterprise restructuring (credit and subsidy policy), infrastructure, and environmental policy reforms. Democratic freedoms include political rights (free and fair elections; openness of the political system to competing political parties and to minority group representation; governance and public administration) and civil liberties (free media and judiciary; freedom to develop NGOs and trade unions; equality of opportunity and freedom from corruption). Ratings are based on a 1 to 5 scale, with 5 representing most advanced.

MONITORING COUNTRY PROGRESS

I. Introduction

The objective of U.S. assistance to Central and Eastern Europe (CEE) and to the Eurasian countries of the former Soviet Union is to help move these countries far enough along the road to becoming market-based democracies that they can complete the journey themselves. Early expectations were that the duration of assistance to the region would be brief. After ten years, while there are many successes, particularly in the Northern Tier CEE countries, remaining transition challenges are formidable and fluid. The collapse of the Russian financial system in August of 1998 underscored the complexity of the transition task, and conflicts in the Balkans demonstrate how fragile stability can be in this post-Cold War period.

These challenges and others make it all the more essential to closely monitor both the impact of the U.S. assistance programs themselves to maximize their effectiveness, as well as the progress of the countries more generally to determine whether continued assistance is necessary or justified. Program impact monitoring is done by both field missions and Washington-based operating units through a system of setting results targets and annually monitoring progress toward them, and through less frequent special field evaluations. This paper presents USAID/E&E's system for monitoring country progress in twenty-seven countries of the region.[1]

Country progress monitoring is done in part to determine whether the assistance program can be terminated either because: (a) the country is well launched on its way to a successful transition and cessation of assistance will no longer jeopardize that transition (i.e., graduation); or (b) the country is making so little progress that significant resources will have little impact. Monitoring is done semi-annually and results are shared with the State Department Coordinators for U.S. assistance to each of the two regions.

Section II below highlights the methodology. This is followed in *Section III* by analyses in each of the major areas examined: (a) economic policy reforms; (b) democratization; (c) macroeconomic performance; and (d) social conditions. *Section IV* briefly concludes. *Appendix I* elaborates on the rating schemes of the economic policy reform and democratization indicators.

An analysis of household survey data is done in *Appendix II*, and is used partly to provide a check on the validity of the macro data of the body of this paper. An important theme explored is whether the differences in living conditions between those households in the leading and lagging countries are as great as suggested by the macro indicators. There are two main sections to this appendix. First, cross-country trends of household evaluations of economic conditions and political freedoms are analyzed. The second part

[1] While USAID programs are largely complete in the Northern Tier CEE region, monitoring country progress among the USAID "graduates" provides a basis for comparison with the remaining transition countries, and enables us to track possible backsliding among the leaders as well.

focuses on Russia and looks at household evaluations of economic and health trends in Russia from 1992 to 1998.

II. Methodology

Market-oriented reforms and democratization have been the two pillars of USAID's program in the transition countries.[2] This has been combined with a more recent and growing focus on social aspects of the transition.[3] The primary challenge of this analysis thus is essentially to assess the progress across these fronts, with a particular focus on the sustainability of reforms.

Country progress is analyzed in a sequence of steps drawing from standard, well-established data sources that are external to USAID. First, we look at the progress towards economic reforms and democratization. Progress on both fronts must reach a certain threshold before we can begin to consider graduation.

Economic policy reforms are assessed by drawing from EBRD's rating scheme of transition indicators, and supplemented by a similar scheme from Freedom House. Progress in democratic freedoms is determined from Freedom House's rating of civil liberties and political rights, and from an effort on its part to further disaggregate the measurement of such freedoms.

Next, we look at indications of sustainability. Economic reforms need to translate into solid macroeconomic performance. We might expect improved performance to follow reform implementation with some lag. But evidence of good macroeconomic performance would give us more confidence that the reformed economy is self-sustaining.

Furthermore, it is important to underscore that acceptable progress in the reforms must precede good macroeconomic performance. A cross-country snapshot might show one economy outperforming another in part because painful reforms have been avoided in the former. Yet, this is hardly sustainable.

The macroeconomic performance indicators also provide a check on the comprehensiveness of the economic reform indicators. For example, fiscal reform is not adequately addressed in the current mix of economic reform indicators. Yet, insufficient

[2] USAID assistance to the transition countries is funded through the Support for East European Democracy Act (SEED) and the Freedom Support Act (FSA), the latter applying to the Eurasian countries. The SEED Act has two goals: the promotion of democracy and a market-oriented economy. The FSA objectives are broader in scope, including the transition goals of the SEED Act as well as those focused more directly on humanitarian, social, environmental, and trade and investment conditions.

[3] See USAID/E&E, *From Transition to Partnership: A Strategic Framework for USAID Programs in Europe and Eurasia* (December 1999); and the E&E Bureau’s social transition strategy: USAID/E&E, *Transition With a Human Face: Broadening the Benefits of Economic and Political Reform in Central and Eastern Europe and the New Independent States* (August 1999).

fiscal reform is likely to surface in the form of rising fiscal deficits, and this *is* being tracked as an economic performance indicator.

Another means to measure the sustainability of reforms is to assess trends in the quality of living conditions. This is largely addressing the concern of "reform fatigue." It is not enough to have a healthy economy and significant political freedoms if households continue to struggle and living conditions deteriorate. In this scenario, support for reforms also deteriorate. So, too, eventually does the productive capacity of the economy.

Country progress is assessed throughout this report with population-weighted measures of progress of three subregions among the transition economies as well as with comparators outside the region. The Northern Tier Central and Eastern Europe consists of Poland, Hungary, Slovenia, the Czech Republic, Slovakia, Estonia, Latvia, and Lithuania; the Southern Tier CEE consists of Romania, Bulgaria, Croatia, the FYR Macedonia, Albania, Bosnia-Herzegovina, and Yugoslavia; and the Eurasian states consist of the countries formed from the dissolution of Soviet Union less Latvia, Lithuania, and Estonia.

For most indicators, proposed graduation benchmarks are assigned. Some are more arbitrary than others and need to be held to debate. Should a country fail to meet a benchmark, this should signal a "yellow flag" in the mind of the analyst; an aspect that may need to be examined more thoroughly if graduation is being considered on the basis of other evidence. The number of benchmarks a country needs to achieve should vary according to context.

An important step of the process is the holding of annual reviews—one for CEE, one for Eurasia—with area specialists from U.S. government agencies. Soliciting such expert opinion serves as a reality check on the data and our interpretation of it.

Finally, it merits explicitly recognizing that what is occurring in the region is unprecedented, and that there is little if any theoretical and/or empirical basis for devising precise thresholds of reform sustainability. Further, it is reasonable to assume that there is more than one acceptable transition route, or, what may amount to the same, many possible varieties of sustainable market-oriented democracies. This exercise, in short, is likely to be as much art as it is science, and it is important to place the results in this context.

III. Analysis

A. Economic Policy Reforms

Progress towards economic policy reforms is primarily assessed from indicators drawn from the EBRD's annual *Transition Report* (November 1999). Sufficient progress must entail both an adequate threshold of reform as well as a favorable trend over time; that is, no significant policy backsliding.

Twelve economic policy reform indicators, grouped into two stages of reform, are tracked. The indicators are measured on a one-to-five scale, with gradations in between.[4] A "five" represents standards and performance norms typical of advanced industrial economies. In general, depending on the particular indicator, a "3" or a "4" may very well be the threshold that we seek. Descriptions of the rating categories are provided in *Appendix I.*

These indicators focus on critical reform aspects of economic liberalization, structural reform, and institution building in the transition process. Such reforms provide much of the overall enabling environment that is required for the emergence of a vibrant and sustainable market economy. Moreover, strong complementarities exist among them all. This means that possibilities for synergism derive from implementation of the total policy package. The other side to this is the possibility that insufficient progress in one reform aspect may undermine the potential gains from progress of another. As is highlighted below, this latter possibility has become an important characteristic of the reform profile among some of the transition laggards.

First Stage Reforms (*Table 1*). The first stage reforms consist of liberalization of prices, external trade and currency arrangements, privatization of small-scale units, and the establishment of key commercial laws. ***Price liberalization*** focuses on the decontrolling of wages and product market prices, including key infrastructure products such as utilities and energy, and the phasing out of state procurement at non-market prices. ***Trade and foreign exchange reforms*** focus on the removal of trade restrictions (export tariffs, quantitative and administrative import and export restrictions), progress towards membership in the WTO, and improving access to foreign exchange (current and capital account convertibility). ***Small-scale privatization*** includes small firms, small farms and plots of land, and housing. The ***legal reforms for investment*** focus on three laws: bankruptcy, pledge or collateral, and company law.

Alongside the growth of new firms, privatization is an essential aspect of restructuring the economy into one that is private-sector driven. Price liberalization provides the appropriate incentives through market-based prices to better maximize efficiency. Trade and foreign exchange reforms provide further discipline for the private sector through global competition, as well as providing domestic firms with a greater capacity to

[4] In earlier *Transition Reports*, the EBRD assigned a 4* to the highest threshold and provided a separate description of the criteria to achieve that level of progress. For simplicity, their "4*" (which is now a 4+) becomes our "5". All other "+"s and "-"s are measured by adding or subtracting a "0.3", respectively.

compete. Consistent, nondiscriminatory, and transparent legal rules for investment are critical to developing an enabling environment for enterprise restructuring and growth, and improved corporate governance.

These first stage reforms require relatively little institution building and tend to be the easiest to do. However, as underscored by trends in Eurasia since the onset of the global financial crisis in mid-1997, progress in these reform areas can also be prone to setbacks. These dynamics, in fact, help explain why the spread between economic reform progress among the transition leaders and laggards is greatest in trade and foreign exchange reforms.

In the CEE countries, the first stage reforms have generally been adopted rapidly and quite thoroughly. All the CEE countries (for which data are available) [5] have implemented a comprehensive program of price liberalization; other than rents, transport and public utilities, prices are generally set by the market. With the salient exception of Bosnia-Herzegovina (where privatization just began in 1999), most CEE countries have essentially completed small-scale privatization. Progress in 1999 in small-scale privatization continued in Bulgaria, particularly in agriculture and land markets, Romania, and Lithuania. Lithuania is now one of eight CEE countries (Croatia, plus all the Northern Tier CEE countries except Latvia) with standards for and performance of small-scale private enterprise that are typical of advanced industrial economies.

Virtually all quantitative and administrative trade restrictions (apart from agriculture) have been removed in all the CEE countries but Bosnia-Herzegovina. Moreover, additional progress in trade and/or foreign exchange liberalization recently occurred in Bulgaria, Latvia, Estonia, the Czech Republic, and Bosnia-Herzegovina. Nine CEE countries now are members of the World Trade Organization. Latvia became the first Baltic State to join, in February 1999, and Estonia followed suit in November 1999. Seven CEE countries (Hungary, Poland, Slovenia, the Czech Republic, Slovakia, Latvia, and Bulgaria) now have achieved policy standards in trade and foreign exchange systems that are comparable to those of the advanced industrial economies.

Advancements in legal reforms in CEE lag behind the other first stage reforms. For only one-half of the CEE countries does comprehensive legislation exist in at least two of the three areas of commercial law that have been the focus of the EBRD survey: collateral; bankruptcy; and company law. Scores on the extensiveness of commercial laws were adjusted down for both Romania and the Czech Republic in 1999, reflecting more apparent limitations in the scope of these laws as more active efforts are made to apply them. However, notable progress in the legislation of legal reforms in 1999 occurred in many CEE countries, including Slovenia, Slovakia, Latvia, Estonia, and Macedonia. Albania and Bosnia-Herzegovina remain considerably behind all other CEE countries in legal reforms (and behind most of the Eurasian countries); there, the legal rules are limited in scope, and subject to conflicting interpretations.

5 Yugoslavia is not included in EBRD's rating scheme.

The prospects of membership in Western institutions continue to provide strong incentives to reform in the CEE. In this vein, five more CEE countries (Slovakia, Latvia, Lithuania, Bulgaria, and Romania) have recently (in October 1999) been invited to participate in negotiations toward EU membership. This brings the total of CEE countries invited to ten. In addition, negotiations are scheduled to begin soon for a Stabilization and Association Agreement between Macedonia and the EU. This is an intermediate step towards eventual EU membership; that is, a step removed from the Association Agreement obtained by the ten CEE countries referred to above.

In general, progress in the first stage reforms in the Eurasian countries lags considerably behind CEE gains. Overall, this reform gap between the two regions grew in 1999 due to progress in the CEE countries coupled with some backsliding in Eurasia. Macroeconomic trends in Russia, stemming from the banking crisis and default of August 1998, continued to put pressures on neighboring countries throughout 1999 to reverse liberalization gains. In Belarus, existing price controls were further tightened in 1999 and a ceiling on inflation was decreed. Kazakhstan and Uzbekistan levied barriers to trade in the region in early 1999, though these market restrictions in Kazakhstan may have been temporary. In April 1999, Kazakhstan's currency was devalued, and the government announced the elimination of the protectionist policies that had been introduced largely to support the overvalued currency. Of all the transition countries, the economies of Belarus, Kazakhstan, and Uzbekistan have among the highest exposure to the Russian economy through trade.[6] So too does Moldova, and to a lesser extent, Armenia and Georgia. All three of these countries witnessed considerable currency volatility in 1999, yet were able to avoid re-introducing currency controls.

Of the Eurasian countries, Kyrgyzstan has advanced the furthest in first stage reforms, followed closely by Moldova and Armenia. Progress in first stage reforms in these countries is roughly comparable to that found in Macedonia and Romania. For these Eurasian leaders, privatization of small companies with tradable ownership rights is complete (in Kyrgyzstan) or close to completion (in Armenia and Moldova). Substantial progress on price liberalization, including energy prices, has been made. Virtually all quantitative and administrative trade restrictions have been removed. In Armenia and Moldova, comprehensive commercial law legislation exists in a majority of key areas surveyed by the EBRD; in Kyrgyzstan, new or amended legislation has recently been enacted in most areas, though further refinement is needed.

Turkmenistan and Belarus lag behind all other transition countries in first stage reforms, and far behind most. In both, government control of prices is extensive. Trade and foreign exchange restrictions are significant. Legal rules are limited in scope and inconsistent. Overall commitment to reform continues to be very weak.

The most significant gains in economic reforms (first and second round) in 1998 of all the transition countries may have been in Tajikistan. This notable progress continued in 1999. In first round reforms, Tajikistan made steady progress in 1999 in small-scale

[6] See *Table 4* of *Appendix II* in *Monitoring Country Progress* (July 1999).

privatization, and trade and exchange rate liberalization. Several Eurasian countries, including Armenia, Kazakhstan, Uzbekistan, and Azerbaijan, experienced mixed progress in first round reforms in 1999; moving forward on one front, stalling or backsliding on another.

Second Stage Reforms (*Table 2*). The numerous and challenging economic reforms are included in the second stage. In general terms, whereas much of the first stage reforms focus on liberalizing the economy from government intervention, second stage reforms concentrate in large part on building the government's capacity to govern; that is, reconstructing a leaner and more efficient government capable of enforcing the rules and providing the public goods needed for a vibrant market economy to work.

Not surprisingly, progress in the second stage reforms has been slower than that of the first stage reforms. Building institutions and effective regulatory entities by nature is an incremental, long-term process. An important part of this is developing market-oriented behavior (or informal institutions) that is compatible with the new formal institutions.[7]

Furthermore, these second stage reforms require more preparation to build political consensus. They typically generate greater political resistance and uncover stronger vested interests. In fact (and somewhat ironically), some of these vested interests were created in the early stages of reform and liberalization.

We draw from the EBRD to track eight specific reforms that we classify as part of the second stage.[8] ***Large-scale privatization*** includes assessing the extent of the transfer of assets to the private sector, but also the extent of outside ownership and effective corporate governance of such entities. ***Enterprise restructuring reforms*** address effective corporate governance in large part through government actions to tighten credit and subsidy policy at the firm level, enforce bankruptcy legislation, and break up dominant firms. Such reforms, in other words, provide some of the financial discipline needed for vibrant growth of the private sector.

Closely related to these reforms is ***competition policy***, which focuses on the development of legislation and institutions to facilitate the entry of firms, existing, or potential, into existing markets. This includes the promotion of a competitive environment through enforcement actions to reduce the abuse of market power by dominant (or non-competitive) firms. More competitive market structures contribute to more efficient firms.

Banking reform includes progress towards the establishment of bank solvency, well-functioning bank competition coupled with interest rate liberalization, financial deepening and extensiveness of private sector lending, and effective prudential

[7] These informal institutions are what the EBRD refers to as social capital or basic codes of conduct, trust, and co-operative behavior. See EBRD, *Transition Report 1999* (November 1999), p. 5.
[8] The EBRD groups the reforms differently, primarily into three groups: those that pertain to enterprises; markets & trade; and financial institutions. EBRD, *Transition Report 1999* (November 1999), p. 24.

supervision, with movement of laws and regulations towards BIS standards. ***Non-bank financial reforms*** (or capital market reforms) include the development and deepening of securities exchanges, investment funds, private insurance and pensions funds, leasing companies, and associated regulatory framework, with movement of laws and regulations towards IOSCO standards.

The financial system undergirds the market economy. The private sector cannot grow and develop without a sound financial sector. It provides the capital to grow. It provides the discipline for good corporate governance. Nor can there exist a stable macroeconomic framework without a sound financial system, given its importance in overall monetary management. Moreover, an unstable financial sector can lead to crisis, and, in fact, most of the significant economic setbacks that have occurred in the transition economies have been largely triggered by financial crisis. Russia is the most recent example, though economic crises in Bulgaria and Albania in 1996-1997 and backsliding in the Czech Republic in 1997 apply as well.

The degree to which ***investment-related legal reforms*** are successfully ***implemented*** is a focus as well. This follows from tracking as part of the first stage reforms, the extensiveness of such reforms—in particular, bankruptcy, collateral, and company law. Here the focus is how clear these rules are (and the degree to which they do not discriminate between domestic and foreign investors), and how well they are administered and supported judicially.

Environmental policy reforms include four components: (a) the degree of adherence to six key international environmental treaties; (b) progress in air and water standards; (c) progress in preparing and implementing national environmental action plans; and (d) an assessment of the extent to which environmental financial incentive mechanisms are used. Progress in environmental reforms contributes directly to progress in other economic reform areas and to productivity gains more broadly.

Finally, the ***restructuring of infrastructure*** includes progress assessed in three aspects of infrastructure reform (tariff reform, commercialization, and regulatory and institutional development) in five infrastructure sectors (telecommunications, electric power, railways, roads, and water and wastewater).[9] Tariff reform includes setting prices that reflect costs, eliminating cross-subsidies, and improving collection rates. Commercialization includes corporatization and the introduction of hard budget constraints and competitiveness pressures, including various forms of private sector participation. Regulatory and institutional development includes the establishment and enforcement of laws that protect consumers (from monopoly power) as well as investors (by promoting fair competition).

The physical infrastructure plays a central role in the productivity of an economy. In general, the transition countries face very significant infrastructure investment requirements (with very limited means to meet them) due to previous policies that grossly distorted incentives. During central planning, some environmental services, such as

[9] Two infrastructure sectors (roads and water & wastewater) were added this year to the three sectors assessed in last year's rating.

water and power, were oversupplied and at prices well below costs (both in an economic and environmental sense), while services such as telecommunications were largely undersupplied.

Judging by industrial market economy standards, all the transition countries still have far to go in progress in second stage economic reforms. The Northern Tier CEE countries, however, come closest. In fact, all the Northern Tier CEE countries are out front of the rest of the transition countries in these second stage reforms. Of this Northern Tier group of eight, four countries continue to lead: Hungary, followed by Poland, Estonia, and the Czech Republic. However, 1999 saw some convergence in reform progress (in first and second stage) in the Northern Tier, as progress in the lagging Northern Tier countries approached that of the leaders.

In at least three of the four leading countries (Poland is the possible exception), more than fifty percent of large-scale state-owned enterprise assets have been privatized in schemes that have generated substantial outsider ownership. In all four countries, there have been significant and sustained actions to harden budget constraints and to promote corporate governance effectively. On competition policy, there has been a substantial reduction of restrictions on firms to enter markets, and some enforcement actions to reduce abuse of market power. Substantial progress has been made in the establishment of bank solvency and of a framework for prudential bank supervision and regulation. In Hungary's case, progress in banking reforms has gone further and includes significant movement of banking laws and regulations towards Bank of International Settlements (BIS) standards and substantial financial deepening. With 1999 progress in bank consolidation and regulation, Estonia is now not far behind.

In all four countries, commercial laws are reasonably clear and administrative and judicial support of the law is reasonably adequate. However, all four countries, particularly the Czech Republic, experienced some backsliding in the effectiveness of legal reforms in 1999. Much of this apparently reflects emerging difficulties encountered by foreign investors in their attempts to enforce their rights as secured creditors and minority shareholders in courts.

As with the first stage reforms, overall progress in second stage reforms in the Southern Tier CEE countries is closer to Eurasian standards than to Northern Tier CEE norms. However, diversity in progress is very large within the Southern Tier. Second stage reform progress in Bosnia-Herzegovina lags far behind all other CEE countries and is comparable to that in Belarus and Tajikistan. In contrast, second stage reform progress in Croatia, Bulgaria, and Romania is only slightly behind Lithuania and Latvia.

In Eurasia, Moldova and Kazakhstan are farthest along in second stage reforms, though behind all but three CEE countries. Among these Eurasian leaders, anywhere from more than twenty-five percent to fifty percent of large-scale state-owned enterprise assets have been privatized or are in the process of being sold, but often with major unresolved issues regarding corporate governance. On enterprise restructuring, there has been moderately tight credit and subsidy policy, but weak enforcement of bankruptcy legislation and little action taken to break up dominant firms. Competition policy legislation and institutions have been set up, and there has been some reduction of entry restrictions or some enforcement action on dominant firms. In bank reforms, significant liberalization of interest rates and credit allocation has taken place, but there has not yet been much progress in the establishment of bank solvency and of a framework for prudential supervision and regulation. Commercial legal rules are reasonably clear, though administration and judicial support of the law is typically inadequate or inconsistent.

Of the Eurasian countries, Kazakhstan may have made the most progress in second stage reforms in 1998-1999. This includes broad advancement in legal reforms (in collateral, company, and bankruptcy laws), as well as gains in environmental policy reform (including a 1999 national environmental action plan) and infrastructure reforms (with the promotion of greater competition in the telecommunication sector through the awarding of new licenses in the cellular segment of the market).

Russia registers second stage progress slightly below the two Eurasian leaders and comparable to that in Macedonia. However, slight gains in implementing legal reforms in 1999 were outweighed by continued backsliding in efforts to reform and restructure the banking sector and the private sector more broadly. Strongly entrenched management and vested interests, particularly in the extraction and banking sectors, continues to afford little protection to creditors and minority shareholders. Widespread asset stripping of large enterprises has accompanied a series of defaults by large corporations and banks. Russia's large current account surplus in 1999 was largely offset by continuing high outflows of private capital, reflecting an absence of confidence in policies and prospects.

Turkmenistan is farthest behind all the transition countries in second stage reforms, though such reforms in Belarus and Tajikistan are not much more advanced. For Tajikistan and Turkmenistan, the privatization of medium and large enterprises has essentially just begun; in Belarus, it remains stalled. In all three countries, few reforms have been implemented to promote corporate governance; soft budget constraints prevail. In Turkmenistan and Tajikistan, widespread market entry restrictions for firms exist, and competition legislation and institution do not exist. Belarus has at least established some competition policy legislation and institutions that has resulted in some reduction of entry restrictions for firms.

Very little progress has been made in all three countries in financial reforms (banks and non-banks). Banking sectors remain controlled by government, though bank restructuring has recently begun in Tajikistan. Few, if any meaningful procedures are in place in order to make commercial laws operational and enforceable in Belarus and Turkmenistan. The commercial legal rules are reasonably clear in Tajikistan, though administrative and judicial support of the laws is inadequate. Overall, in all three countries, little progress in commercialization, regulation, and decentralization has been achieved in infrastructure reform.

Of all the economic policy reforms, financial sector reforms (bank and non-banks), competition policy, and enterprise restructuring reforms tend to lag the most throughout

CEE and Eurasia. Moreover, with the exception of bank reforms, there has been very little progress in these areas since 1998. Bank reforms moved ahead in a number of countries in 1999, though this occurred all in CEE: in particular, in Estonia, the Czech Republic, Slovenia, Latvia, Croatia, Romania, and Bosnia-Herzegovina. By EBRD ratings, the only measurable change in bank reforms in Eurasia in 1999 was backsliding in this domain in Russia and Kyrgyzstan.

Good corporate governance remains a major challenge, particularly in Eurasia. Barter between firms and often with government remains pervasive. Soft budget constraints continue in various forms. A common one is the failure of governments to enforce the payment of public utilities from loss-making enterprises. Finally, the implementation of effective bankruptcy policies remains elusive for many governments. Failure to move forward on many of these reform aspects stems in part from the concern of adverse social consequences and political repercussions if firms are allowed to fail. Yet, the policy failure itself severely undermines the competitiveness of the private sector and its ability to productively engage and support the population.

Trends in Economic Reforms since 1994. *Tables 1* and *2* give us a snapshot of the status of economic reform progress through September 1999, and the direction of change since September 1998. *Table 3* shows the extent to which progress has occurred since 1994.[10] This provides for two types of assessments of relative progress in the medium term: across countries and across reform areas.

Table 3 reveals that the greatest gains in economic policy reforms over this six year period have occurred among some of the “middle-tier” reformers. This includes Georgia, Azerbaijan, Armenia, Kazakhstan, Ukraine, and Moldova, and reflects a combination of similar country characteristics. First, these countries were essentially in the very early stages of reform in 1994 and progress tends to be most evident in the early years when the easiest (first stage) reforms are first undertaken. Second, all of these governments, at least at times, have had sufficient political will and adequate capacity to move forward on the easier reforms.

In contrast, the countries which have made the least progress over this period include countries that have yet to substantially engage in reforms (such as Belarus, Turkmenistan, and Uzbekistan) or have been backsliding notably in recent years (such as Russia) or are among the transition leaders faced primarily with the more difficult second stage reforms (such as the Czech Republic and Poland).

Still, by these measures, only Belarus was farther behind in economic reforms in the fall of 1999 than in 1994. Partial or temporary setbacks in other countries, however, have not been uncommon. On the contrary, starts and stops and occasional backsliding have

[10] As reflected in *Table 3*, the EBRD’s first rating scheme was in 1994 and included nine of the twelve indicators that are currently tracked in *Tables 1* and *2*. In particular, the infrastructure and environmental reform indicators are new since then, and the two legal reform indicators were initially combined into one.

characterized most country transition paths. Moreover, policy stagnation and/or backsliding have been more prevalent since mid-1997 than in the previous four years.

This trend, in fact, meshes with the onset of the global financial crisis and economic slowdown. Even though the global economy was no longer in crisis, the trend of slower reform progress for the transition region overall continued through 1999. This was due in large part because the adverse spillovers from the Russian financial crisis continued to play out in much of Eurasia.

On the other hand, a reform pattern evident prior the global financial crisis also re-emerged in 1999, albeit in modified form. In particular, the economic reform gap between the leaders and many of the countries that trail them decreased. This is because many of the Southern Tier CEE countries (Bulgaria, Romania, and Croatia) made notable progress in 1999 as did the "second tier" Northern Tier (Slovakia, Latvia, Lithuania, and Slovenia), while progress slowed among the transition leaders in Hungary, Poland, and the Czech Republic confronted with increasingly difficult reforms.

Finally, from *Table 3*, what medium term assessments of relative progress across the reform areas can be made? First, since 1994 and overall in the region, small-scale privatization has advanced the most. Moreover, significant progress in this domain has occurred in all three subregions, though particularly in Eurasia and the Northern Tier CEE countries.

Notable medium term progress has also been made in developing a commercial law framework, followed by large-scale privatization. The greatest progress in commercial law reform since 1994 has occurred in the Southern Tier CEE countries, and it has included both stages: legislation and implementation. Eurasia saw significant gains in commercial law reform as well, though mostly in legislation. In contrast, legal reforms in several Northern Tier CEE countries (Hungary, the Czech Republic, and Poland) actually stalled if not regressed, presumably due to growing challenges in implementation.

The least progress in economic reforms since 1994 for the transition region as a whole has occurred in price liberalization, capital markets, enterprise restructuring, and competition policy. For price liberalization, this has largely been due to the fact that much progress had occurred prior to 1994 coupled with more recent backsliding in Eurasia, particularly in Russia. For the other three economic reform areas, relatively little progress has yet to be made for a large majority of the transition countries.

Table 1. First Stage of Economic Policy Reforms

	Small Scale Privatization	Trade and Foreign Exchange	Price Liberalization	Legal Reforms (Extensiveness)	1st Stage Average
Hungary	5.0	5.0	3.3	4.0	4.3
Poland	5.0	5.0	3.3	4.0	4.3
Slovenia	5.0	5.0	3.0	4.0 ↑	4.3 ↑
Czech Republic	5.0	5.0 ↑	3.0	3.3 ↓	4.1 ↑
Slovakia	5.0	5.0	3.0	3.3 ↑	4.1 ↑
Croatia	5.0	4.0	3.0	4.0	4.0
Lithuania	5.0 ↑	4.0	3.0	4.0	4.0 ↑
Latvia	4.0	5.0 ↑	3.0	3.7 ↑	3.9 ↑
Bulgaria	3.3 ↑	5.0 ↑	3.0	4.0	3.8 ↑
Estonia	5.0	4.0	3.0	3.3 ↑	3.8 ↑
FYR Macedonia	4.0	4.0	3.0	3.7 ↑	3.7 ↑
Kyrgyzstan	4.0	4.0	3.0	3.3 ↑	3.6 ↑
Armenia	3.3 ↑	4.0	3.0	3.7 ↓	3.5
Moldova	3.3	4.0	3.0	3.7 ↓	3.5 ↓
Romania	3.7 ↑	4.0	3.0	3.3 ↓	3.5
Kazakhstan	4.0	3.0 ↓	3.0	3.3 ↑	3.3
Albania	4.0	4.0	3.0	2.0	3.3
Georgia	4.0	4.0	3.0	2.0 ↓	3.3 ↓
Azerbaijan	3.0	3.3 ↑	3.0	3.3 ↑	3.2 ↑
Russia	4.0	2.3	2.7	3.7	3.2
Ukraine	3.3	3.0 ↑	3.0	2.0	2.8 ↑
Tajikistan	3.0 ↑	2.7	3.0	2.0	2.7 ↑
Bosnia-Herzegovina	2.0 ↑	2.7 ↑	3.0	2.0	2.4 ↑
Uzbekistan	3.0	1.0 ↓	2.0	2.7 ↑	2.2 ↓
Turkmenistan	2.0	1.0	2.0	...	1.7
Belarus	2.0	1.0	1.7 ↓	2.0	1.7 ↓
CEE & Eurasia	3.9 ↑	3.1	2.8	3.3	3.3 ↑
Northern Tier CEE	5.0 ↑	4.9 ↑	3.2	3.8 ↓	4.2 ↑
Southern Tier CEE	3.7 ↑	4.1 ↑	3.0	3.3 ↓	3.5 ↑
Eurasia	3.6	2.4 ↓	2.7	3.1	3.0 ↓
Industrial Countries	5.0	5.0	5.0	5.0	5.0
Benchmarks	4.0	4.0	3.0	4.0	3.8

Note: On a 1 to 5 scale, with 5 being most advanced. A "↑" indicates an advancement from September 1998 through September 1999. Unless specified, all regional averages in the main body of this report are population-weighted.

EBRD, *Transition Report 1999* (November 1999); legal reform estimates for Tajikistan are from EBRD, *Transition Report 1998* (November 1998).

Table 2. Second Stage of Economic Policy Reforms

	Large Scale Privatization	Enterprise Restruct.	Competitior Policy	Banking Sector	Capital Markets	Legal Reform (effectiveness)	Environment Policy	Infra-structure	2nd Stage Average
Hungary	4.0	3.3	3.0	4.0	3.3	3.7 ↓	4.5	3.7	3.7
Estonia	4.0	3.0	2.7	3.7 ↑	3.0	3.7 ↓	3.8 ↑	3.8 ↑	3.4 ↑
Poland	3.3	3.0	3.0	3.3	3.3	3.0 ↓	4.5	3.4	3.4 ↓
Czech Republic	4.0	3.0	3.0	3.3 ↑	3.0	2.7 ↓	4.3	2.9	3.3 ↓
Slovenia	3.3	2.7	2.0	3.3 ↑	3.0	4.0 ↑	3.0 ↑	3.0	3.0 ↑
Slovakia	4.0	3.0 ↑	3.0	2.7	2.3	3.0 ↑	3.8	2.2	3.0 ↑
Latvia	3.0	2.7	2.7	3.0 ↑	2.3	3.0 ↑	3.5	2.9 ↑	2.9 ↑
Lithuania	3.0	2.7	2.3	3.0	2.7 ↑	3.0	3.3 ↑	2.7	2.8 ↑
Croatia	3.0	2.7	2.0	3.0 ↑	2.3	2.7 ↓	3.3 ↑	2.5	2.7 ↑
Bulgaria	3.0	2.3	2.0	2.7	2.0	3.7 ↓	3.0 ↑	2.7 ↑	2.7 ↑
Romania	2.7	2.0	2.0	2.7 ↑	2.0	3.7 ↓	3.3	3.1 ↑	2.7 ↑
Moldova	3.0	2.0	2.0	2.3	2.0	3.0	3.0	2.3 ↑	2.4
Kazakhstan	3.0	2.0	2.0	2.3	2.0	3.3 ↑	2.3 ↑	2.2 ↑	2.4 ↑
FYR Macedonia	3.0	2.0	1.0	3.0	1.7 ↑	3.7 ↓	2.5 ↑	1.9 ↓	2.3
Russia	3.3	1.7 ↓	2.3	1.7 ↓	1.7	2.3 ↑	3.3	2.3	2.3 ↓
Kyrgyzstan	3.0	2.0	2.0	2.3 ↓	2.0	3.0 ↑	2.0	1.5	2.2
Armenia	3.0	2.0	2.0	2.3	2.0	2.0 ↓	2.0	2.3 ↑	2.2 ↓
Georgia	3.3	2.0	2.0	2.3	1.0	2.0 ↓	2.3	2.5 ↑	2.2 ↓
Ukraine	2.3	2.0	2.0	2.0	2.0	2.0	3.3 ↑	1.7	2.2
Uzbekistan	2.7	2.0	2.0	1.7	2.0	2.3 ↑	2.5 ↑	1.4	2.1 ↑
Albania	2.0	2.0	2.0	2.0	1.7	1.7 ↓	2.5	1.7	1.9
Azerbaijan	1.7 ↓	2.0	1.0	2.0	1.7	2.0	3.0 ↑	1.7	1.9 ↑
Bosnia-Herzegovina	2.0 ↑	1.7	1.0	2.3 ↑	1.0	1.0	2.3	1.6	1.6 ↑
Belarus	1.0	1.0	2.0	1.0	2.0 ↓	2.0	2.5	1.4 ↑	1.6
Tajikistan	2.3 ↑	1.7	1.0	1.0	1.0	3.0	1.8 ↑	1.1	1.6 ↑
Turkmenistan	1.7	1.7	1.0	1.0	1.0	...	1.8	1.1	1.3
CEE & Eurasia	3.0	2.0 ↓	2.2	2.2	2.0	2.6 ↑	3.2 ↑	2.3 ↑	2.4 ↑
Northern Tier CEE	3.6	3.0	2.9	3.4 ↑	3.1	3.1 ↓	4.3 ↑	3.2	3.3
Southern Tier CEE	2.7 ↑	2.1	2.0	2.7 ↑	2.0 ↑	3.2 ↓	3.0 ↑	2.7 ↑	2.6 ↑
Eurasia	2.9	1.8 ↓	2.1	1.8 ↓	1.8	2.3 ↑	3.0 ↑	2.0 ↑	2.2
Industrial Countries	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0
Benchmarks	4.0	3.0	4.0	3.0	4.0	4.0	4.0	3.0	3.6

Note: On a 1 to 5 scale, with 5 being most advanced. A "↑" indicates an advancement from September 1998 through September 1999.

EBRD, *Transition Report 1999* (November 1999); legal reform estimates for Tajikistan are from EBRD, *Transition Report 1998* (November 1998).

Table 3. Change in Economic Policy Reforms: 1994-1999

	1st Stage			2nd Stage						Average
	SSP	PL	TFE	LSP	ER	CP	BR	CM	LR	Change
Georgia	2.0	0.0	3.0	2.3	1.0	1.0	1.3	0.0	0.0	1.2
Azerbaijan	2.0	0.0	2.3	0.7	1.0	0.0	1.0	0.7	2.7	1.1
Armenia	0.3	0.0	2.0	2.0	1.0	1.0	1.3	1.0	0.7	1.0
Kazakhstan	2.0	0.0	1.0	1.0	1.0	0.0	1.3	0.0	1.3	0.8
Ukraine	1.3	0.0	2.0	1.0	1.0	0.0	1.0	0.0	1.0	0.8
Latvia	1.0	0.0	1.0	1.0	1.0	0.7	0.0	0.3	2.0	0.8
Moldova	1.3	0.0	2.0	1.0	0.0	0.0	0.3	0.0	2.3	0.8
Bulgaria	1.3	0.0	1.0	1.0	0.3	0.0	0.7	0.0	1.7	0.7
FYR Macedonia	0.0	0.0	0.0	1.0	0.0	0.0	1.0	0.7	2.7	0.6
Romania	0.7	0.0	0.0	1.0	0.0	1.0	1.0	0.0	1.3	0.6
Albania	1.0	0.0	0.0	1.0	0.0	1.0	0.0	0.7	1.0	0.5
Hungary	1.0	0.3	1.0	1.0	0.3	0.0	1.0	0.3	-0.3	0.5
Tajikistan	1.0	0.3	1.7	0.3	0.7	0.0	0.0	0.0	...	0.5
Slovenia	1.0	0.0	1.0	1.0	0.0	0.0	0.3	0.0	1.0	0.5
Estonia	1.0	0.0	0.0	1.0	0.0	0.0	0.6	1.0	0.7	0.5
Lithuania	1.0	0.0	0.0	0.0	1.0	0.3	1.0	0.6	0.3	0.5
Croatia	1.0	0.0	0.0	0.0	1.0	1.0	0.3	0.3	0.3	0.4
Uzbekistan	0.0	-0.7	-1.0	1.0	1.0	0.0	1.0	0.0	1.7	0.3
Turkmenistan	1.0	0.0	0.0	0.7	0.7	0.0	0.0	0.0	...	0.3
Slovakia	1.0	0.0	1.0	1.0	0.3	0.0	0.0	-0.7	0.0	0.3
Poland	1.0	0.3	1.0	0.3	0.0	0.0	0.3	0.3	-0.7	0.3
Kyrgyzstan	0.0	0.0	1.0	0.0	0.0	0.0	0.4	0.0	1.0	0.3
Czech Republic	1.0	0.0	1.0	0.0	0.0	0.0	0.3	0.0	-1.0	0.1
Russia	1.0	-0.3	-0.7	0.3	-0.3	0.3	-0.4	-0.3	1.0	0.1
Belarus	0.0	-1.3	0.0	-1.0	-1.0	0.0	0.0	0.0	-1.0	-0.5
CEE & Eurasia	1.0	-0.2	0.4	0.6	0.2	0.2	0.3	-0.1	0.8	0.4
Northern Tier CEE	1.0	0.2	0.9	0.4	0.2	0.0	0.4	0.2	-0.4	0.3
Southern Tier CEE	0.7	0.0	0.1	0.9	0.2	0.7	0.7	0.1	1.2	0.5
Eurasia	1.1	-0.3	0.3	0.6	0.2	0.2	0.3	-0.2	1.0	0.4
Benchmark										0 or greater

Note: The sub-headings refer to the following economic reforms: (SSP) small-scale privatization; (PL) price liberalization; (TFE) trade and foreign exchange reforms; (LSP) large-scale privatization; (ER) enterprise restructuring; (CP) competition policy; (BR) bank reforms; (CM) capital market reforms; and (LR) legal reforms (extensiveness & effectiveness). The change is based on a rating from 1 to 5, e.g., a "1.3" score in this table might represent an advancement from 2.0 to 3.3 from 1994 or 1995 to 1999. For most of the indicators, the figures represent change (or absence of change) from 1994 to 1999; for price liberalization, competition policy, legal reforms, and non-bank financial reform indicators, from 1995 to 1999. Environment policy and infrastructure reform are excluded.

EBRD, *Transition Report 1999* (November 1999), and previous editions of the EBRD report.

B. Democratization

Progress towards democracy building is primarily assessed from indicators drawn from Freedom House. First, the status and the change from 1991 through end-year 1999 in political rights and civil liberties are examined. Second, 1998-1999 democratic trends are further disaggregated and reviewed. Perceptions of corruption are also examined, drawing from the work of both Freedom House and Transparency International. As with the economic reforms, sufficient progress in democratization must entail both an adequate threshold as well as no significant deterioration.

Political Rights and Civil Liberties. Six primary criteria go into the determination of ***political freedoms***: (1) the extent to which elections for head of government are free and fair; (2) the extent to which elections for legislative representatives are free and fair; (3) the ability of voters to endow their freely elected representatives with real power; (4) the openness of the system to competing political parties; (5) the freedom of citizens from domination by the military, foreign powers, totalitarian parties, and other powerful groups; and (6) the extent to which minority groups have reasonable self-determination and self-government.

Greater political liberties are part of the end objective of a sustainable transition as well as a means to facilitate the economic reforms needed to achieve the transition. The evidence strongly suggests that the most effective route is one that is facilitated, sooner rather than later, by an open and competitive political system at all levels of government.[11] This system can only be sustained by broad-based participation from a genuinely-empowered electorate.

Ten primary criteria go into the determination of ***civil liberties***: (1) freedom of media, literature, and other cultural expressions; (2) existence of open public discussion and free private discussion including religious expression; (3) freedom of assembly and demonstration; (4) freedom of political or quasi-political organization (which includes political parties, civic associations, and ad hoc issue groups); (5) equality of citizens under law with access to independent, nondiscriminatory judiciary; (6) protection from political terror and freedom from war or insurgency situations; (7) existence of free trade unions, professional organizations, businesses or cooperatives, and religious institutions; (8) existence of personal social freedoms, which include gender equality, property rights, freedom of movement, choice of residence, and choice of marriage and size of family; (9) equality of opportunity; and (10) freedom from extreme government indifference and corruption.

[11] The EBRD provides evidence that political competition, as with economic competition, is key to transition progress. In fact, in contrast to conventional wisdom derived from past experience in other parts of the world, economic progress in the transition region is shown to be more closely associated with frequent political regime turnovers than with the stability or continuity from a strong executive and/or minimal political regime change. Political regime turnovers mitigate the influence of vested interests. See EBRD, *Transition Report 1999* (November 1999), Chapter 5: The Politics of Economic Reform.

Civil liberties are the freedoms to develop views, institutions, and personal autonomy apart from the state. The development of civil liberties, like political liberties, is an end objective in itself. The merits of such liberties as freedom of assembly and open public discussions, and freedom from political terror and war are self-evident.

However, greater civil liberties can also serve as a crucial counterweight or check on governments in societies where political rights are lacking. This counterweight can be found among NGOs (such as free trade unions, professional organizations, and religious institutions) as well as a free media. An independent, nondiscriminatory judiciary is critical for similar reasons.

In addition, civil liberties tend to link quite closely with economic progress. Many--such as greater equality of opportunity, freedom from corruption, the existence of personal social freedoms such as gender equality, property rights, freedom of movement--contribute to a more productive economy as well as a more just one. Similarly, through the political process, pressures from civil society can help push economic reforms along.

Table 4 below highlights Freedom House's assessments of political rights and civil liberties from 1991 through 1999. The range in progress in democratization across the countries is great. At one extreme, there now exist eight transition countries--the Czech Republic, Estonia, Hungary, Lithuania, Poland, Slovenia, Latvia, and, most recently, Slovakia--where political rights and civil liberties are roughly comparable to those found in Western Europe (such as in France, Germany, Italy, and the UK). Three of these countries--the Czech Republic, Hungary, and Slovenia--have maintained this level of freedom since at least 1993. Poland and Lithuania achieved this level in 1995, Estonia in 1996, Latvia in 1997, and Slovakia in 1999. Of these eight countries, only Latvia, Estonia, and Slovakia experienced a temporary relapse in democratic freedoms since 1991 as so measured.

Among these leaders, democracy and freedom prevail. Elections are free and fair, at the national and sub-national levels. Those elected rule. There are competitive political parties, and the opposition has an important role and power. By and large, minority groups have self-determination.[12] In general, there remain deficiencies in some aspects of civil liberties, though most such freedoms exist. The media are generally free. The judiciary is generally independent and nondiscriminatory. NGOs and trade unions are free and able to exist. Personal social freedoms exist, as does freedom from extreme government indifference and corruption.

In contrast, Turkmenistan is among a handful of countries worldwide rated by Freedom House to have the fewest political rights and civil liberties in 1999; one of only thirteen

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[12] Valerie Bunce of Cornell University argues at least implicitly that "electoral inclusion" of minority groups is not adequately captured in the Freedom House scores and hence concludes that "full-scale democracies" (those that are both fully inclusive and fully free) are fewer than the group of eight scored by Freedom House. In particular, this presumably more rigorous standard would exclude Estonia and possibly Latvia. See V. Bunce, "The Political Economy of Post-Socialism," *Slavic Review* Vol. 58, No. 4 (Winter 1999), pp. 756-793.

countries out of 192 countries to receive the poorest score. Democratic freedoms in Uzbekistan, Tajikistan, and Belarus are not much greater than those in Turkmenistan.

In Turkmenistan and Uzbekistan, basic political rights are nonexistent. In the other democratic laggards, the regimes may allow some minimal manifestation of political rights such as competitive local elections or some sort of representation or partial autonomy for minorities. An independent civic life, including a free media, is effectively suppressed in Turkmenistan. In the other lagging countries, citizens are severely restricted in expression and association.

Evidence provided in earlier *Monitoring Country Progress* reports (July 1999 & October 1998) revealed a growing gap in democratic freedoms between the transition leaders and laggards; the "fault line" was roughly between the CEE countries and Eurasia. Continued support for this trend is found in *Table 4*. In particular, eight of the twelve Eurasian countries have experienced a decrease in democratic freedoms since 1991; only Georgia, Moldova, and Armenia have witnessed an overall increase. Of the fifteen CEE countries, only in Albania are there fewer democratic freedoms today than there were in the early transition years (1991-1993). However, at least two other Southern Tier CEE countries have experienced no net gains in democratization since then: Bulgaria and Macedonia.[13] Freedoms have increased in nine CEE countries during 1991-1999. Six of these countries are Northern Tier CEE; the other two Northern Tier countries (the Czech Republic and Slovenia) had already achieved a level of democratic freedom on a par with Western Europe by 1992-1993.

However, when compared to earlier *Monitoring Country Progress* reports, *Table 4* also reveals that much less quantifiable change in democratization took place in 1999 among the transition countries than in previous years. In 1998, for example, political rights and/or civil liberties scores changed for thirteen countries; in 1999, it occurred in only three countries. Slovakia moved forward in political rights with the transfer of governance from Vladimir Meciar to a more reform-minded government. Increases in political rights and civil liberties were posted in Yugoslavia following the war in Kosovo, as opposition to President Slobodan Milosevic's tight rule gained (according to Freedom House) limited momentum. Russian civil liberties eroded due to growing harassment of ethnic Chechens (that stemmed initially from several bombings in August 1999), and increased political interference in the media over the Chechnya crisis and preceding the parliamentary elections in December 1999.

Freedom House also designates general trends in freedoms that are not sufficient in magnitude to change a country's score. In 1999, there were five such trends, all decreases in freedom. Three were in Eurasia: Ukraine; Belarus; and Uzbekistan. Two were in the Southern Tier: Macedonia; and Bosnia-Herzegovina.

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[13] *Table 4* shows that there have been no gains in democratic freedoms in Croatia from 1991-1999 as well. However, with the demise of President Franjo Tudjman and the very recent emergence of a reform-minded government and a new president in Stipe Mesic, this has likely changed.

Democratization Disaggregated. In its forthcoming *Nations in Transit 1999* (May 2000), Freedom House further disaggregates regional democratization trends. *Table 5* displays this effort. Six components of democracy building are rated on a one-to-seven scale in each country. The ratings represent events as of July 1, 1999 and are compared with progress in the spring of 1998. While these ratings are less current than the political rights and civil liberties scores of *Table 4*, they provide a more complete picture of the components of democratization in the region.

The ***political process*** focuses on the extent to which elections are free, fair, competitive, and participatory. ***Civil society*** assesses the status of nongovernmental organizations; the number and nature of NGOs, and the degree of participation. ***Independent media*** attempts to measure freedom from government control (such as legal protection, editorial independence, and the extent of privatization) and the financial viability of private media. ***Governance and public administration*** focuses on legislative and executive effectiveness, and on government decentralization, including the independence and effectiveness of local and regional government. ***Rule of law*** examines constitutional reforms, the development and independence of the judiciary, and the rights of ethnic minorities. Finally, the scope of ***corruption*** (official corruption in civil service; public-private sector links; anti-corruption laws and decrees adopted and enforced) is also assessed.

As expected, general trends between the two Freedom House rating schemes coincide. The country rankings, in particular, are quite similar between the two schemes. In each, the Northern Tier CEE countries are all out in front in democratization. The laggards consist of the Central Asian Republics plus Belarus and Azerbaijan of Eurasia, and Bosnia-Herzegovina and Yugoslavia in CEE.

The more disaggregated scheme of *Table 5* is designed to better capture the specifics of the transition than the worldwide Freedom House estimates of political rights and civil liberties (of *Table 4*). In this context, it is worthy to note two differences between the two measurement schemes. First, the disaggregated measures show a larger gap between the Northern Tier leaders and the rest. Second, there is also greater differentiation within the Northern Tier CEE countries. A significant part of these differences in degree stem from greater weight given to the scope of corruption in the disaggregated ratings.

For the transition region as a whole (as well as for each of the three subregions), the greatest progress has occurred in the political process (towards competitive and free elections) and civil society (or NGO development). The least progress has occurred in efforts to reduce corruption. Gains in the rule of law, independent media, and governance/public administration fall somewhere in between.

Judging from *Table 5*, the Eurasian countries lag most in democratization vis-a-vis the Northern Tier CEE leaders in the severity of corruption (and the government's ability to address it), followed by progress towards developing an independent (financially viable) media and developing a rule of law. The progress gaps between the two subregions in civil society development, political process, and (primarily local) governance/public administration are smaller and roughly comparable to each other.

As shown in *Table 5*, more countries witnessed an increase in democratization (eleven countries) from spring 1998 to July 1999 than did those that experienced a decrease (seven countries). This is a similar pattern to that which occurred in 1996, but a reversal from the more sobering trends in 1997 (in which ten countries saw a decrease in democratic freedoms and six an increase). In general, most of the gains occurred among a middle group of reformers (including the more advanced Eurasian countries of Georgia and Moldova, the Southern Tier CEE countries of Bulgaria and Romania, and the "second-tier" of the Northern Tier CEE countries, Slovakia and Latvia in particular). Progress was less evident among the Northern Tier leaders who have been approaching a democratization "ceiling" for some time. In fact, in the case of the Czech Republic, in particular, some backsliding in democratization was evident. At the other end of the reform spectrum, typically no gains were registered (such as in Turkmenistan and Uzbekistan) or backsliding occurred (such as in Belarus and Bosnia-Herzegovina).

Table 6 examines perceptions of corruption in further detail. It draws from Transparency International's efforts to assess corruption in 1999 across ninety-nine countries of the world.[14] The TI Corruption Perceptions Index (CPI) scores countries in terms of the degree to which corruption is perceived to exist among public officials and politicians. It is a composite index, drawing on seventeen different polls and surveys from ten independent institutions (including the World Bank, the Wall Street Journal, Gallup International, and Freedom House) carried out among business people, the general public, and country analysts. Scores can range from ten (highly clean) to zero (highly corrupt).

Given that the index is an average, the various estimates that go into making this average can vary widely. Overall, however, this composite index corresponds well with Freedom House's assessments (of *Table 5*). In both sets of scores, corruption is perceived to be greatest in Eurasia and lowest in the Northern Tier CEE countries. Corruption in the Southern Tier CEE countries is somewhere in between, but closer in magnitude to Eurasia.[15]

Judging from *Table 6*, corruption in the Northern Tier CEE countries on average is comparable to that of Italy, but significantly greater than EU norms overall. Slovenia has the lowest corruption score of all the transition countries. Twenty-four countries (of the sample of ninety-nine) have lower corruption still; most are OECD members. The scope of corruption in the Southern Tier CEE countries and Eurasia on average may be closer to corruption found in a handful of Latin American countries, including Colombia,

[14] Excluded among the transition countries in this assessment are Tajikistan, Bosnia-Herzegovina, and Turkmenistan.

[15] Three country assessments are significantly different between the two sets of corruption scores. In particular, corruption is judged to be significantly greater in Romania, Georgia, and Azerbaijan in the Corruption Perception Index of *Table 6.* Freedom House ranks Romania 4th out of 27 countries in the severity of corruption; TI's CPI has Romania 12th out of 24. Georgia is 11th by Freedom House and 19th by TI. Azerbaijan is 16th according to Freedom House and 24th (or last) in TI's index.

Venezuela, Bolivia and Ecuador.[16] However, these averages mask large differences. Of the Eurasian countries, Belarus ranks fifty-eighth worldwide, alongside Latvia. In contrast, Azerbaijan and Uzbekistan are ninety-six and ninety-four respectively. Indonesia also ranks ninety-six. Only two countries (Nigeria and Cameroon) are judged to have more corruption.

The 1999 CPI scores are broadly consistent with a worldwide survey cited in the World Bank's *World Development Report 1997* (and included in the *Appendix II: Transition Paths* in *Monitoring Country Progress* (October 1998)). The World Bank survey found that dissatisfaction with corruption among businesses was highest in Eurasia, followed by Sub-Saharan Africa, CEE, Latin America and the Caribbean, and (trailing far behind) the high income members of the OECD. Bearing in mind that the averages mask large differences, the latest CPI scores show corruption also to be greatest in Eurasia. This is followed by Sub-Saharan Africa where corruption is judged to be slightly worse than in Latin America. Corruption is perceived to be lower still in the CEE and far lower in the high income OECD countries.

Finally, *Appendix II* (below) analyzes household survey data in part to further assess political change and reform.[17] Drawing from results in fifteen transition countries, the gains in the "easy" political freedoms (that stem from the collapse of communism) are examined, and compared to the more difficult "second-stage" political freedoms (that stem from better governance). Perceptions of corruption are also assessed. How does corruption and bribe-taking in 1998 compare to that during communist days? Trust in institutions (in government, civil society, and the private sector) is examined. In addition, popular evaluations of current political regimes are compared with perceptions of pre-transition regimes. Finally, drawing on longitudinal assessments from 1994 to 1998, the percent of respondents who prefer a return to communism is tallied.

Briefly, these survey data show that very impressive political gains have been realized and shared broadly across much of the transition region. However, these are the relatively easy gains (or "first stage" gains) that resulted early on with the collapse of communism: the freedoms to say what one wants; to associate with whomever; to pursue political and religious activities (or, in the case of many, at least at the outset, to choose to be inactive politically). On average, eighty percent of the sample in the fifteen countries felt that these political freedoms were greater under the existing political system than they were under communism, and almost one-half felt the situation was much better in 1998.

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[16] The average corruption score for the 16 Latin American countries included in the sample is higher (3.5) than the averages for the Southern Tier CEE countries and Eurasia; that is, corruption is perceived to be lower on average in Latin America.

[17] These data are drawn from three household surveys from the Centre for the Study of Public Policy (CSPP) and cover fifteen transition countries: eight Northern Tier CEE countries (the three Baltics were last surveyed in 1996; the Czech Republic, Poland, Hungary, Slovakia, Slovenia in 1998); four Southern Tier CEE countries (Romania, Bulgaria, Yugoslavia, and Croatia in 1998); and three Eurasian countries (Russia, Ukraine, and Belarus, or 73% of the Eurasian population, in 1998).

“Second stage” political gains, however, have been far more elusive. These are the gains that stem from good governance and hence require institutional development: being treated fairly and equitably by government; having an ally in government to encourage household economic improvement. Overall, forty-one percent of the respondents saw gains in these freedoms since communist days and only sixteen percent felt the progress was much better. Similarly, a widely shared perception across the region is that corruption is significant and worse than it was under communism, and that government is part of the problem.

More generally, there exists very little trust in key institutions. This includes government, but also private enterprise. Approximately three out of four persons sampled across the countries have little to no trust in key government institutions. The least trust is given to parliament, though civil servants, courts, and police similarly inspire little. While mistrust of formal institutions is highest in Eurasia, it is also a characteristic to varying degrees in CEE. Some of these findings, in fact, contribute to a more sobering view of progress in democratic reforms in the Northern Tier countries than that which is implied by Freedom House’s overall ratings.

Table 4. Political Rights and Civil Liberties[1]

	1991		1994		1999[2]		1994-99 Change[3]		1991-99 Change[4]	
	PR	CL	PR	CL	PR	CL	PR	CL	PR	CL
Czech Republic	...	...	1	2	1	2	0	0	0	0
Hungary	2	2	1	2	1	2	0	0	+ 1	0
Slovenia	...	...	1	2	1	2	0	0	0	0
Estonia	2	3	3	2	1	2	+ 2	0	+ 1	+ 1
Latvia	2	2	3	2	1	2	+ 2	0	+ 1	0
Lithuania	2	3	1	3	1	2	0	+ 1	+ 1	+ 1
Poland	2	2	2	2	1	2	+ 1	0	+ 1	0
Slovakia	...	...	2	3	1↑	2	+ 1	+ 1	+ 2	+ 2
Romania	5	5	4	3	2	2	+ 2	+ 1	+ 3	+ 3
Bulgaria	2	3	2	2	2	3	0	– 1	0	0
FYR Macedonia	...	...	4	3	3	3	+ 1	0	0	0
Moldova	5	4	4	4	2	4	+ 2	0	+ 3	0
Ukraine	3	3	3	4	3	4	0	0	0	– 1
Georgia	6	5	5	5	3	4	+ 2	+ 1	+ 3	+ 1
Croatia	...	...	4	4	4	4	0	0	0	0
Armenia	5	5	3	4	4	4	– 1	0	+ 1	+ 1
Albania	4	4	3	4	4	5	– 1	– 1	0	– 1
Russia	3	3	3	4	4	5↓	– 1	– 1	– 1	– 2
Azerbaijan	5	5	6	6	6	4	0	+ 2	– 1	+ 1
Bosnia-Herzegovina	...	...	6	6	5	5	+ 1	+ 1	+ 1	+ 1
Yugoslavia	...	...	6	6	5↑	5↑	+ 1	+ 1	+ 1	0
Kyrgyzstan	3	4	4	3	5	5	– 1	– 2	– 2	– 1
Kazakhstan	5	4	6	5	6	5	0	0	– 1	– 1
Tajikistan	5	5	7	7	6	6	+ 1	+ 1	– 1	– 1
Belarus	4	4	4	4	6	6	– 2	– 2	– 2	– 2
Uzbekistan	6	5	7	7	7	6	0	+ 1	– 1	– 1
Turkmenistan	6	5	7	7	7	7	0	0	– 1	– 2

Region	1991		1994		1999		1994-99 Change		1991-99 Change	
	PR	CL	PR	CL	PR	CL	PR	CL	PR	CL
CEE & Eurasia	3.5	3.4	3.5	3.9	3.6	4.2	– 0.1	– 0.3	– 0.1	– 0.8
Northern Tier CEE	2.0	2.1	1.7	2.1	1.0	2.0	+ 0.7	+ 0.1	+ 1.0	+ 0.1
Southern Tier CEE	4.2	4.4	4.2	3.2	3.1	2.9	+ 1.1	+ 0.3	+ 1.1	+ 1.5
Eurasia	3.7	3.5	3.8	4.5	4.4	4.9	– 0.5	– 0.4	– 0.7	– 1.4
European Union[5]					1.0	1.5				
OECD[6]					1.2	1.7				
Benchmarks					1.0	2.0	0.0	0.0		

Notes: 1Ratings from 1 to 7, with 1 representing greatest development of political rights/civil liberties. 2An ↑ indicates an increase in democratization in 1999 as measured by a change in a political rights or civil liberties score. Freedom House also designates general trends in freedoms that are not sufficient in magnitude to change a country's score. In 1999, there were five such general trends, all decreases in freedom: 1 Macedonia; 2 Ukraine; 3 Bosnia-Herzegovina; 4 Belarus; 5 Uzbekistan. 3A "+" refers to an increase in freedoms. 4The change for Bosnia-Herzegovina, Croatia, FYR Macedonia, Slovenia and Yugoslavia (Serbia & Montenegro) is calculated from 1992 to 1999; this series for the Czech Republic and Slovakia covers from 1993 to 1999. 5All 15 EU members score "1" in Political Rights. In Civil Liberties 8 of the 15 members score a "1"; 6 score a "2" (Belgium, France, Germany, Italy, Spain and the UK); and Greece scores a "3". 6All but three OECD members score a "1" in Political Rights; the exceptions are Turkey ("4"), Mexico ("3"), and Korea ("2").

For Civil Liberties, 15 members score a "1"; 11 score a "2" (Belgium, Czech Republic, France, Germany, Hungary, Italy, Japan, Korea, Poland, Spain, and the UK); Greece scores a "3"; Mexico scores a "4"; Turkey scores a "5".

Freedom House, *Freedom in the World: 1999-2000* (May 2000, forthcoming).

Table 5. Democratization Disaggregated

Country	Political Process	Civil Society	Independent Media	Govt/Public Administration	Rule of Law	Corruption	Average	Change (1998-99)
Poland	1.3	1.3	1.5	1.8	1.5	2.0	1.7	···
Slovenia	2.0	1.8 ⇧	1.8	2.3 ⇧	1.5	1.0	1.8	⇧
Hungary	1.3	1.3	2.0 ⇩	2.5 ⇩	1.8	2.3	1.8	⇩
Czech Republic	2.0 ⇩	1.5	1.8 ⇩	2.0	2.5 ⇩	3.3	2.2	⇩⇩
Lithuania	1.8	2.0	1.5	2.5	2.0	3.5	2.2	···
Estonia	1.8	2.8 ⇩	1.8	2.3	2.0 ⇧	3.5	2.3	···
Latvia	1.8 ⇧	2.3	1.8	2.5	2.0 ⇧	3.5	2.3	⇧
Slovakia	2.0 ⇧	2.3 ⇧	2.3 ⇧	3.0 ⇧	2.5 ⇧	3.8	2.6	⇧⇧
Romania	2.8 ⇧	3.0 ⇧	4.0	3.5 ⇧	4.3	3.0	3.4	⇧
FYR Macedonia	3.0 ⇧	3.0 ⇧	3.0 ⇧	3.0 ⇧	4.0 ⇧	5.0	3.5	⇧⇧
Bulgaria	2.3 ⇧	3.8	3.5	3.8 ⇧	3.5 ⇧	5.0	3.6	⇧
Georgia	4.0 ⇧	4.0 ⇧	3.8 ⇧	4.5 ⇧	4.0 ⇧	5.0	4.2	⇧
Moldova	3.0 ⇧	3.5 ⇧	4.0 ⇧	4.5	4.0	6.0	4.2	⇧
Croatia	4.3	3.5	5.0 ⇩	4.0	4.8	5.0	4.4	···
Ukraine	3.5	4.0 ⇧	4.8	4.8	4.5 ⇩	6.0	4.6	···
Russia	4.0 ⇩	4.0	4.8 ⇩	4.5	5.0 ⇩	6.0	4.7	⇩
Armenia	5.5 ⇧	3.5	4.8 ⇧	4.5	4.8 ⇧	5.8	4.8	⇧
Albania	4.0 ⇧	4.0 ⇧	4.3 ⇧	4.8 ⇧	5.0 ⇧	7.0	4.8	⇧
Kyrgyzstan	5.0	4.5	5.0	4.8 ⇩	5.0 ⇩	7.0	5.2	⇩
Azerbaijan	5.5	4.5 ⇧	5.5	6.3	5.5	6.0	5.5	···
Yugoslavia	5.0	5.3 ⇩	5.5 ⇩	5.0	5.5 ⇩	7.0	5.5	⇩
Kazakhstan	6.0 ⇩	5.0	5.5	5.0 ⇧	5.3	7.0	5.6	···
Tajikistan	5.5 ⇧	5.3	5.8 ⇧	6.3 ⇧	5.8 ⇧	6.0	5.8	⇧
Bosnia-Herzegovina	5.5 ⇩	5.0	5.0 ⇩	6.3 ⇩	*6.0*	7.0	5.8	⇩
Belarus	6.8 ⇩	6.0 ⇩	6.8 ⇩	6.3	6.5 ⇩	4.8	6.2	⇩
Uzbekistan	6.5	6.5	6.5	6.0 ⇧	6.5	7.0	6.5	···
Turkmenistan	7.0	7.0	7.0	6.8	6.8	7.0	6.9	···

	Political Process	**Civil Society**	**Independent Media**	**Govt/Public Administration**	**Rule of Law**	**Corruption**	**Average**	**Change (1998-99)**
CEE & Eurasia	3.8 ⇩	3.8 ⇧	4.4 ⇩	4.3	4.5 ⇩	5.3	4.3	···
Northern Tier CEE	1.5	1.5	1.7	2.1 ⇩	1.8	2.5	1.8	···
Southern Tier CEE	3.5 ⇧	3.8 ⇧	4.4 ⇩	4.1	4.6	4.8	4.2	···
Eurasia	4.5 ⇩	4.4 ⇧	5.1 ⇩	4.9 ⇧	5.1 ⇩	6.1	5.0	⇩

Note: On a scale from 1 to 7, with 1 representing most advanced--or, in the case of corruption, most free. A "↑" indicates an increase in democratization since 1998; a "↓" signifies a decrease. In the summary column of change from 1998 to 1999, one arrow represents a change greater than 0.1 and less than 0.5; two arrows represents change greater than 0.5. Data cover from 1998 to July 1, 1999. Change calculation does not include the corruption component since the methodology for assessing corruption has been slightly modified. Rule of law rating for Bosnia-Herzegovina is for 1998.

Source: Freedom House, *Nations in Transit 2000* (May 2000, forthcoming).

Table 6. Transparency International's 1999 Corruption Perceptions Index

	Score	Worldwide Rank		Score	Worldwide Rank
Slovenia	6.0	25	Denmark	10.0	1
Estonia	5.7	27	Germany	8.0	14
Hungary	5.2	31	USA	7.5	18
Czech R.	4.6	39	Japan	6.0	25
Poland	4.2	44	Costa Rica	5.1	32
Lithuania	3.8	50	Italy	4.7	38
Slovakia	3.7	53	Jamaica	3.8	50
Belarus	3.4	58	Senegal	3.4	58
Latvia	3.4	58	Colombia	2.9	72
Bulgaria	3.3	63			
			Vietnam	2.6	75
Macedonia	3.3	63	Ecuador	2.4	82
Romania	3.3	63	Kenya	2.0	90
Croatia	2.7	74	Indonesia	1.7	96
Moldova	2.6	75	Cameroon	1.5	99
Ukraine	2.6	75			
			EU	7.6	
Armenia	2.5	80			
Russia	2.4	82			
Albania	2.3	84			
Georgia	2.3	84			
Kazakhstan	2.3	84			
Kyrgyzstan	2.2	87			
Yugoslavia	2.0	90			
Uzbekistan	1.8	94			
Azerbaijan	1.7	96			
CEE & Eurasia (n=24)	3.2				
N.Tier CEE (n=8)	4.6				
S.Tier CEE (n=6)	2.8				
Eurasia (n=10)	2.4				

The TI Corruption Perceptions Index (CPI) scores countries in terms of the degree to which corruption is perceived to exist among public officials and politicians. The 1999 CPI ranks 99 countries. It is a composite index, drawing on 17 different polls and surveys from 10 independent institutions (including Freedom House, World Bank, Wall Street Journal, and Gallup International) carried out among business people, the general public, and country analysts. Scores can range from 10 (highly clean) to 0 (highly corrupt).

Transition country ratings are given equal weight in the regional averages.

C. Summary of Economic Reforms & Democratization

Table 7 and *Figure 1* provide an overall picture of the status of the economic policy reforms and democratic freedoms in the transition countries. With one country exception, the economic policy reform ratings represent an equally weighted average of all twelve EBRD policy indicators (that is, from both stages).[18] The democratic freedom ratings draw from both Freedom House sources. Specifically, the six democratization components of *Table 5* are averaged for each country, and then compressed into a one-to-five scale with five representing the most advanced (or most free). This is to better align with the similar economic policy reform scale. These scores are then adjusted with the more recent 1999 democracy trends of *Table 4.*[19] The use of both Freedom House scores combines a more accurate differentiation of democratic progress between countries (from *Table 5*) with the latest quantifiable changes in trends (from *Table 4*).

Previous versions of *Figure 1* in earlier *Monitoring Country Progress* reports have all revealed three country groups differentiated by progress towards economic and democratic reforms. However, there was also an emerging trend that surfaced at last look (in July 1999) that showed that the large middle group of reformers was beginning to "spread out"; that is, evidence of growing differentiation in reform progress in this group. This has continued and has now blurred the distinction between the middle group and the laggards in particular.

However, the distinction in reform progress by region, and specifically between CEE and Eurasia, continues to grow. With three exceptions (Tajikistan, Kazakhstan, and Azerbaijan), reform progress in 1999 in Eurasia was mixed at best; that is, either backsliding occurred in economic reforms or democratic reforms or both, or in the case of Turkmenistan (where reforms can hardly slide back), no measurable change took place. Russia and Belarus experienced backsliding in both economic and democratic reforms.

In CEE, three Northern Tier leaders (Hungary, Poland, and the Czech Republic), showed some reform slippage as they continue to address the most difficult second-stage reforms. Of the remaining twelve CEE countries, ten advanced in 1999 in at least one reform domain (without slipping in the other), and six (Slovenia, Latvia, Slovakia, Bulgaria, Romania, and Croatia) progressed in both economic and democratic reforms.[20] Bosnia-Herzegovina and Yugoslavia are the two salient CEE exceptions; both trail far in reform progress from the rest of CEE and both witnessed mixed progress in reforms in 1999.

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[18] The economic reform score for Yugoslavia is drawn from Freedom House, *Nations in Transit* (May 2000). *Monitoring Country Progress* (October 1998) elaborates on Freedom House's methodology and compares its economic reform rating scheme with the EBRD scores.

[19] Country ratings were increased (decreased) by 0.4 if democratic freedoms (either political rights and/or civil liberties) increased (decreased) by 2 Freedom House scores. This happened only in the case of Yugoslavia (CL and PR both increased by one). Country ratings were increased (decreased) by 0.2 if democratic freedoms increased (decreased) by 1 FH score. Such an increase occurred only in Slovakia. The only comparable decrease occurred in Russia. Finally, country ratings were increased (decreased) by 0.1 if FH indicated a trend toward increase or decline in freedom, but not of sufficient magnitude to change a country's rating from the previous year, 1998. This meant decreases in the scores for Macedonia, Ukraine, Bosnia-Herzegovina, Belarus, and Uzbekistan.

[20] The available data show Croatia moved forward recently in economic reforms, but had no measurable progress in democratization. The democratization rating, however, precedes the death of President Tudjman and the favorable change in political regimes in Croatia.

These recent reform dynamics reflect a mixture of two trends in the past. First, as occurred prior to the global financial crisis and its spillover to Russia, a group of middle-tier reformers appear to be gaining on the reform leaders. However, this middle group now consists primarily of CEE countries. This reflects in part impressive reform gains in much of the Southern Tier CEE in the wake of the Kosovo crisis. It also reflects further “clustering” of reform progress among the Northern Tier CEE countries. The clearest manifestation of this is the impressive gains in Slovakia, now no longer a Northern Tier outlier in *Figure 1* (as was the case in previous versions).

The second trend is a continuation of reform stagnation in Eurasia that surfaced with the Russian financial crisis. Many countries in Eurasia, in other words, seem to continue to be vulnerable to events in Russia; the economic and political links among the Eurasian countries remain strong.

Table 7 shows that while the average ratings for economic policy reforms and democratic freedoms are the same for the transition region as a whole (that is, "2.7" out of a possible "5" for each), the variation in progress is significantly greater in the case of democratic reforms. The reform leaders have democratic freedoms roughly on a par with some Western democracies, while the democratic laggard, Turkmenistan, scores among the least democratic countries worldwide. In economic policy reforms, however, even the Northern Tier CEE countries still have far to go to reach the standards in the industrial market economies. This is particularly evident in the second stage economic reforms.

There continues to be a close correspondence between progress in economic and democratic reforms. Greater progress in one domain is closely linked with greater progress in the other. In general, *Table 7* shows relatively small differences in country rankings between economic and democratic reforms. Kazakhstan is the most significant exception, followed by Kyrgyzstan and Croatia. All three countries are relatively further ahead in economic reforms than in democratization. Kazakhstan, for example, ranks fourteenth in economic reform progress, but only twenty-second in democratization.

Comparing *Figure 1* to earlier versions in previous reports reveals a strengthening of the link between economic and democratic reforms as the transition proceeds. More countries are falling closer to the “best-fit” line. This includes countries identified in earlier reports as outliers to the trend. Slovakia is the most notable example, as progress in democratization there has in important respects caught up with gains in economic reforms. Though not captured in the 1999 data, this seems likely to be occurring presently in Croatia as well.

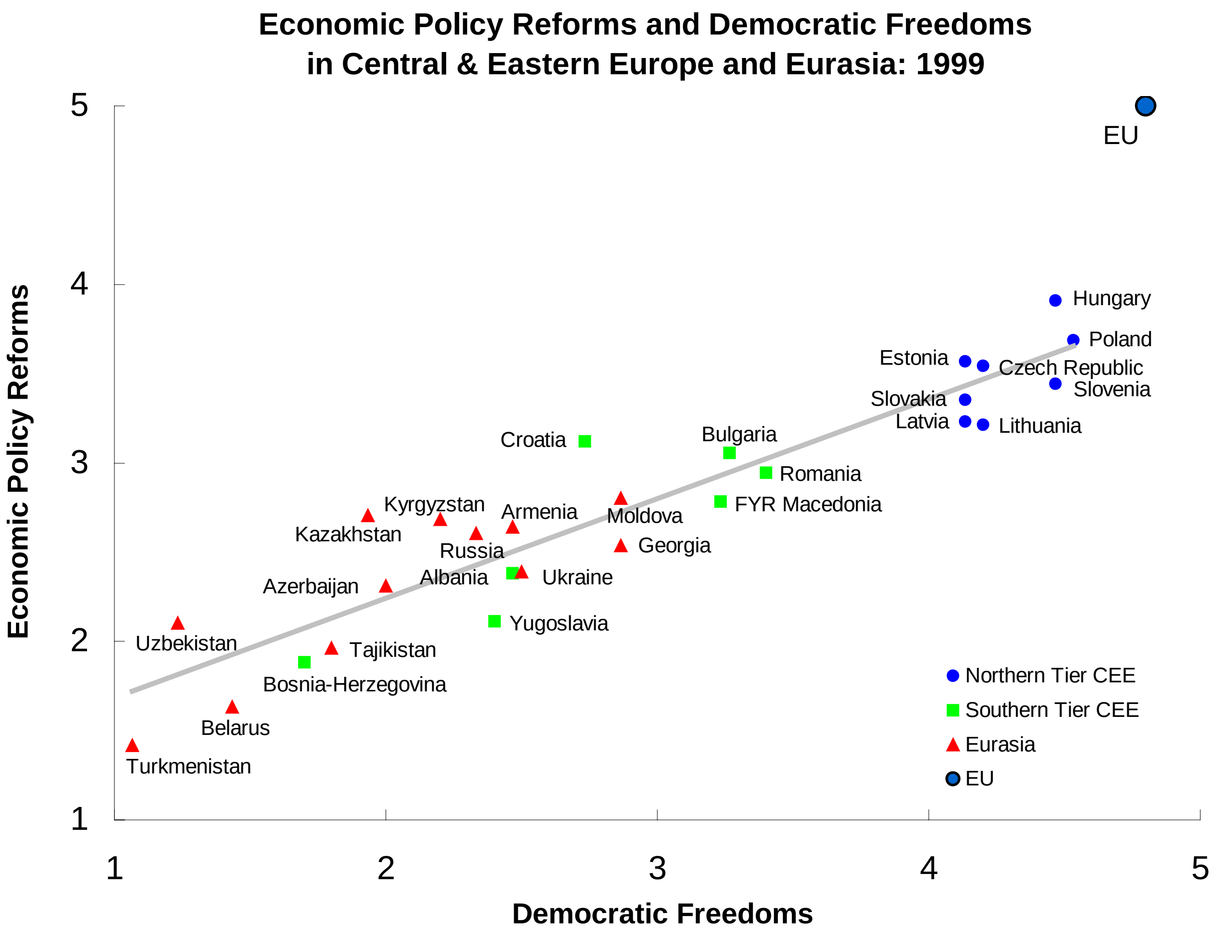
Finally, *Figure 2* provides a dynamic picture of the transition reforms since 1994 in four transition countries (Poland, Slovakia, Russia, and Belarus) which have followed four distinct reform paths.[21] Reforms in Poland have moved steadily forward, though measurable progress has slowed. This reflects both success (democratic freedoms are approaching a limit by worldwide standards) and growing challenges (that come with the implementation of more difficult economic reforms). In general, this is a typical Northern Tier CEE reform path.

Progress in reforms in Belarus, in striking contrast, has consistently regressed since 1994, both in economic and democratic reforms. Belarus is approaching a reform limit of another sort; there is little "room" to backslide much further. This path, however, is more the extreme scenario; it is not typical.

[21] The method to measure reform progress in *Figure 2* was, out of necessity, simplified from that of *Figure 1* to capture estimates of earlier years. Hence, the 1999 scores in *Figure 2* differ slightly from those of *Figure 1*.

In important respects, the routes taken by Russia and Slovakia are more typical of transition progress for the large majority of the transition countries, those whose reform progress falls in between that found in Belarus and Poland. In Russia and Slovakia, change has been far from linear and steady; progress anything but a "straight line." Reforms in Slovakia are now of Northern Tier standards, but not without backsliding in democratization in earlier years. In Russia, impressive gains in reforms in earlier years (in democratization prior to 1994 and in economic reforms from 1994 to 1997), have since given way to backsliding in both
domains

Figure 1.



Ratings of democratic freedoms are from Freedom House, *Nations in Transit 1999* (May 2000, forthcoming) and Freedom House, *Freedom in the World 1999-2000* (May 2000, forthcoming), and assess reforms through December 1999. With one exception, economic policy reform ratings are from EBRD, *Transition Report 1999* (November 1999), and cover events through September 1999; economic policy reform rating for Yugoslavia is from Freedom House (May 2000). Economic policy reforms include price liberalization, trade and foreign exchange, privatization, legal, banking and capital markets, enterprise restructuring (credit and subsidy policy), infrastructure, and environmental policy reforms. Democratic freedoms include political rights (free and fair elections; openness of the political system to competing political parties and to minority group representation; governance and public administration) and civil liberties (free media and judiciary; freedom to develop NGOs and trade unions; equality of opportunity and freedom from corruption). Ratings are based on a 1 to 5 scale, with 5 representing most advanced.

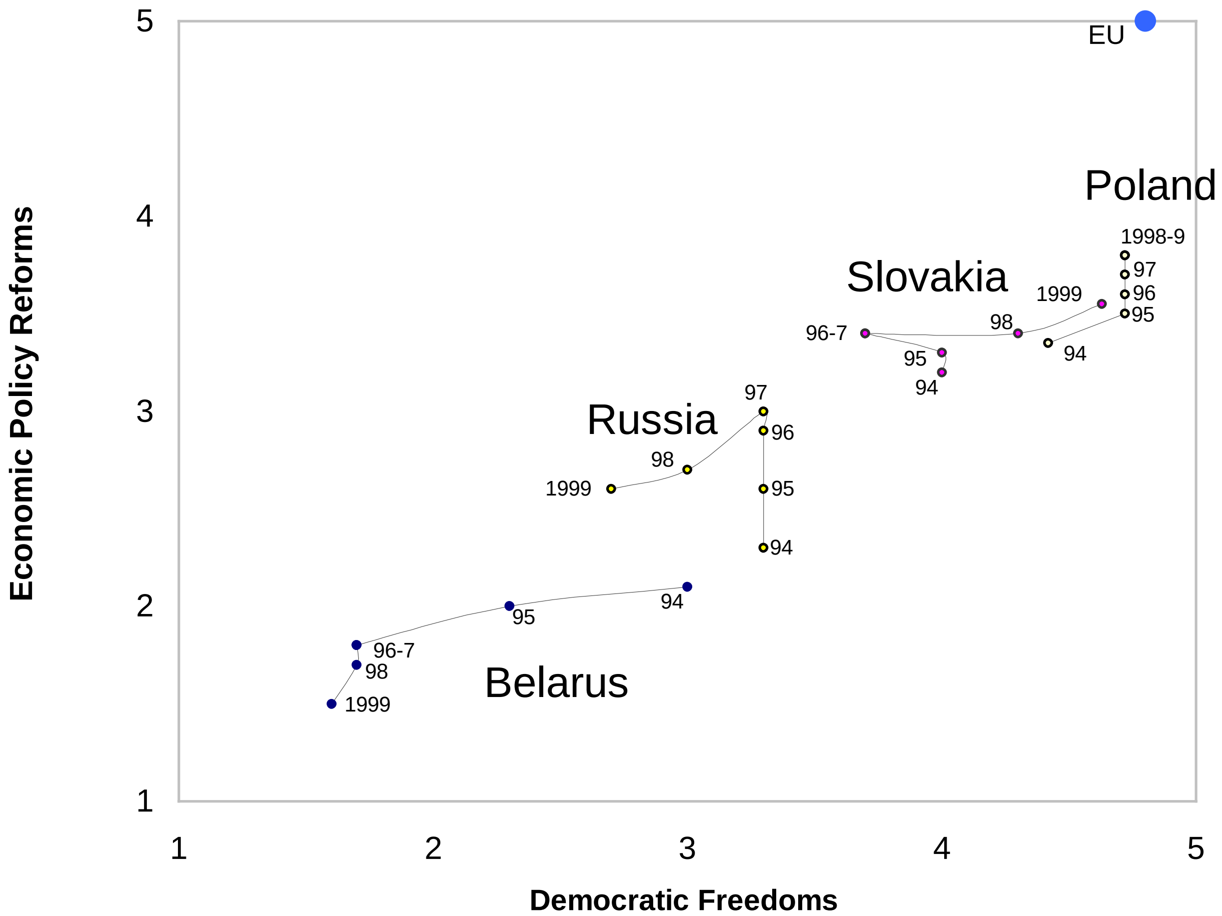
Table 7. Economic Policy Reforms and Democratic Freedoms in Central & Eastern Europe and Eurasia: 1999

Economic Policy: Country	Rating (1 to 5)	Ranking	Democratic Freedoms: Country	Rating (1 to 5)	Ranking
Hungary	3.9	1	Poland	4.5	1
Poland	3.7	2	Hungary	4.5	1
Estonia	3.6	3	Slovenia	4.5	1
Czech Republic	3.5	4	Czech Republic	4.2	4
Slovenia	3.4	5	Lithuania	4.2	4
Slovakia	3.4	5	Estonia	4.1	6
Latvia	3.2	7	Latvia	4.1	6
Lithuania	3.2	7	Slovakia	4.1	6
Croatia	3.1	9	Romania	3.4	9
Bulgaria	3.1	9	Bulgaria	3.3	10
Romania	2.9	11	FYR Macedonia	3.2	11
Moldova	2.8	12	Georgia	2.9	12
FYR Macedonia	2.8	12	Moldova	2.9	12
Kazakhstan	2.7	14	Croatia	2.7	14
Kyrgyzstan	2.7	14	Ukraine	2.5	15
Armenia	2.6	16	Albania	2.5	15
Russia	2.6	16	Armenia	2.5	15
Georgia	2.5	18	Yugoslavia	2.4	18
Ukraine	2.4	19	Russia	2.3	19
Albania	2.4	19	Kyrgyzstan	2.2	20
Azerbaijan	2.3	21	Azerbaijan	2.0	21
Yugoslavia	2.1	22	Kazakhstan	1.9	22
Uzbekistan	2.1	22	Tajikistan	1.8	23
Tajikistan	2.0	24	Bosnia-Herzegovina	1.7	24
Bosnia-Herzegovina	1.9	25	Belarus	1.4	25
Belarus	1.6	26	Uzbekistan	1.2	26
Turkmenistan	1.4	27	Turkmenistan	1.1	27

	Economic Policy Rating (1 to 5)	Democratic Freedoms Rating (1 to 5)
CEE & Eurasia	2.7	2.7
Northern Tier CEE	3.6	4.4
Southern Tier CEE	2.7	3.1
Eurasia	2.5	2.2
European Union	5.0	4.8
OECD	--	4.6

Ratings of democratic freedoms are from Freedom House, Nations in Transit 1999 (May 2000, forthcoming) and Freedom House, Freedom in the World 1999-2000 (May 2000, forthcoming), and assess reforms through December 1999. With 1 exception, economic policy reform ratings are from EBRD, Transition Report 1999 (November 1999), and cover events through September 1999; economic policy reform rating for Yugoslavia is from Freedom House (May 2000). Ratings are based on a 1 to 5 scale, with 5 representing most advanced.

Figure 2. Economic Policy Reforms and Democratic Freedoms in Central & Eastern Europe and Eurasia: Selected Countries, 1994 to 1999



Source: EBRD, Transition Report (various years); Freedom House, Freedom in the World (various years). Ratings are based on a 1 to 5 scale, with 5 representing the most advanced

D. Sustainability

In this section, we weigh the economic and democratic reforms against the macroeconomic and microeconomic evidence. Economic policy reforms need to translate into good macroeconomic performance. Yet, this is not enough. The benefits at the macro level must also be reasonably well distributed and need to translate into social conditions that at the least are not significantly deteriorating. Otherwise, the reforms may stall for lack of support, fiscal sustainability may be jeopardized, and, even more fundamentally, overall productivity may be slowed.

The quality of these data is an important issue, and numerous caveats apply. Credible cross-country comparisons are oftentimes difficult because the quality of data still varies widely throughout the transition region. In general, data for the CEE countries tend to be better than those for the Eurasian countries. Accurate time-series assessments can be difficult as well. Earlier year calculations (such as measuring inflation) sometime differ from those in latter years. Data for previous years are often subject to revisions. In the economic domain, it is widely recognized that unofficial economic activity is very significant, and this by definition is not captured in the official statistics. Nor are the important and very substantial qualitative changes adequately reflected in the figures. Data which attempt to reflect social conditions, particularly of those populations most vulnerable in the transition, are generally only available with considerable lag, and often fail to adequately differentiate between subnational groups. It should go without saying that conclusions need to be based on a variety of evidence if possible.

1. Macroeconomic Performance.

Tables 8 through *15* and *Figures 3* through *7* highlight macroeconomic performance. Fundamental to sustaining reforms is sustained **economic growth** at some moderate rate or greater. As evident in *Table 8*, the Northern Tier countries had been achieving this, at growth rates of close to four percent or more from 1994-1998. This was well above EU growth rates. However, the more recent 1997-1999 trend reveals economic growth slowing considerably; from 5.7 percent in 1997, to 3.7 percent in 1998, and to 2.7 percent in 1999. Much of this was attributed to close economic ties to countries that had been experiencing economic slowdown or contraction. The Baltic countries experienced slower economic growth in 1998 due to close ties to a Russia in crisis. Moreover, due to close trade links with the EU, all the countries of the Northern Tier witnessed slower growth in 1999 as economic growth in Western Europe slowed (to 2.3 percent in 1999), and with it, demand for Northern Tier CEE exports.

Highest sustained economic growth among the Northern Tier CEE countries has most recently been occurring in Poland, Hungary, and Slovenia. Poland's performance in this regard has been most impressive; annual economic growth in Poland has ranged from roughly four to seven percent since 1993. The basis for most of the economic growth in 1999 in these three countries was from domestic demand; that is, domestic investment and consumption. Of these three leaders, in fact, only Hungary had a growing export sector in 1999.

Three Northern Tier countries had contracting economies in 1999, Lithuania, Estonia, and the Czech Republic, and two experienced very weak economic growth (of around one percent), Slovakia and Latvia. Partly because of improving economic conditions with trading partners and continued economic reform progress, all are currently forecast to have growing economies in 2000, though only marginally in the case of the Czech Republic and Lithuania.[22] The Czech Republic's economy has been stagnating since 1997.

For the Southern Tier CEE as a whole, strong economic growth in 1994-1996 gave way to economic stagnation in 1997-1999. This turn around was largely due to economic and political troubles in Romania, and more recently, the Kosovo crisis. Still, the (population-weighted) subregional average masks wide diversity. The economies of Bosnia-Herzegovina and Albania grew by eight percent in 1999, while the economies in Romania and Croatia contracted, by 3.9 and 2.0 percent respectively in 1999.

Moreover, while the Kosovo conflict significantly tempered macroeconomic performances, some of the earlier estimates of the war's economic impact on the region proved to be overly pessimistic.[23] Macedonia and Bulgaria were forecast to be among the hardest hit of the front line states to Yugoslavia. Yet, both experienced moderate economic growth of at least 2.5 percent in 1999. In the case of Macedonia, the economy rebounded in part due to opportunities from reconstruction of Kosovo. Bulgaria's economic growth has been driven largely by domestic demand, including a significant acceleration in domestic fixed investment in the second half of 1999, coupled with an increase in foreign direct investment. Continued forward movement in reforms, particularly in Bulgaria, has contributed to the relatively favorable macroeconomic developments.

As in the Northern Tier, there are some indications that macroeconomic conditions are improving in the Southern Tier in 2000. Export markets, particularly those in Western Europe, are strengthening. Partly as a result, and partly from anticipated continuation of recent reform progress, modest recoveries are forecast for the economies of both Romania and Croatia in 2000. Overall, however, much continues to hinge on

[22] The basis for greater economic growth in the Northern Tier due to improved external circumstances continues to strengthen. Of primary importance is the rebound in economic growth in the EU, now forecast to be 3.2 percent in 2000.
[23] See in particular: IMF, *The Economic Consequences of the Kosovo Crisis—An Updated Assessment* (May 25, 1999). Also, *Appendix II* of *Monitoring Country Progress* (July 1999) provides a synthesis of the preliminary estimates of the economic spillovers to the region from Kosovo.

developments in Yugoslavia and the West's response to the Kosovo crisis in the Stability Pact.

In striking contrast to earlier estimates, overall economic activity in the Eurasian countries was greater in 1999 (at 2.7 percent on average) than in any other transition year.[24] Prior to 1999, only in 1997 did official economic activity expand (albeit less than one percent) on an annual average basis in Eurasia. In 1999, ten of the twelve Eurasian countries experienced economic growth. Russia's economy expanded by 3.2 percent. Ukraine and Moldova were the exceptions. Ukraine continues to have the only transition economy yet to experience official economic growth since communism's collapse.

As in the past, events in Russia have continued to significantly influence both the (population-weighted) regional averages, as well as real economic events in much of Eurasia. Nevertheless, the economic links between Russia and most of its neighbors seem to be weakening, though this needs to be more rigorously examined. Much of the basis for Russia's economic growth in 1999 was apparently due to import-substitution activities, which in turn were spurred by the August 1998 devaluation of the ruble in Russia. Imports in Russia became more expensive as a consequence of the devaluation, and domestic production replaced much of what was previously imported. This is supported by the current account data. Russia experienced a very large current account surplus (of 10.8 percent of GDP) in 1999 despite a contracting export sector (of two percent) and overall economic growth of over three percent.

In addition, the crisis in Russia may have expedited a trend towards greater diversification of trade among many of Russia's neighbors, lessening the reliance on Russia's economy. Belarus is probably the salient exception in this regard, as support for greater integration between Russia and Belarus continues to grow.[25]

Dramatic shifts in the prices of commodity exports for the Eurasian countries continued to factor prominently in economic growth in 1999. The significant reversal in the trend in oil prices (from a thirty percent drop in 1998 to close to a forty percent increase in 1999) boosted export revenues and economic growth in the oil exporting countries of Russia, Kazakhstan, Turkmenistan, and Azerbaijan, and increased import prices and inflationary pressures in the oil-importing countries of Moldova and Ukraine.[26]

[24] The previous *Monitoring Country Progress* (July 1999), drawing primarily from the EBRD's *Transition Report Update 1999* (May 1999), estimated an economic contraction of 2.8 percent for the Eurasian countries overall in 1999.

[25] The proportion of exports to Russia has decreased substantially for a number of Eurasian countries, particularly Kazakhstan (from 43% of total exports in 1994 to 18% in 1999), Uzbekistan (from 40% in 1994 to 19% in 1998), Armenia (35% in 1994 to 15% in 1999), and Kyrgyzstan (30% in 1994 to 16% in 1998). The percent of exports to Russia decreased significantly in Ukraine from 40% in 1994 to 22% in 1997, but increased slightly to 23% in 1998. Belarus and Moldova continue to have the greatest exposure to Russia in export terms. Fifty-one percent of Moldova's exports went to Russia in 1994; this increased to 58% in 1997, but then decreased substantially to 41% by 1999. In contrast, 47% of Belarus' exports went to Russia in 1994. This increased to 65% in 1997, and increased even slightly further to 66% in 1998.

[26] Fifty-two percent of Turkmenistan's exports in 1997 were energy products (oil and gas); in Azerbaijan, 35%; Kazakhstan, 23%; and Russia, 21%. Forty-nine percent of Ukraine's imports in 1997 were energy; in Moldova, it was 33%.

On the other hand, prices of non-oil commodity exports--such as cotton and certain metals, including gold and aluminum, which are key to several countries of the region--continued to decline, on the heels of an overall drop in the price of non-oil commodities of fifteen percent in 1998. This likely affected economic activity adversely in cotton-exporting Uzbekistan, Tajikistan, and Turkmenistan, and metal-exporting Russia, Kazakhstan, and Kyrgyzstan.[27]

Four Eurasian countries have been able to sustain economic growth rates of roughly three percent or higher over the medium term (that is, for at least three years): Azerbaijan; Belarus; Georgia; and Armenia. For the three Caucasus countries in particular, part of this is in response to a very substantial drop in economic activity at the outset of the transition (see *Figure 4*). While economic growth in Belarus has slowed in recent years (and inflation continues to increase significantly), overall economic performance in Belarus (at least as depicted by the official statistics) continues to defy expectations given the absence of reform progress.

Figures 3 and *4* look at real GDP patterns over the transition. *Figure 3* reveals three distinct tracks among the three subregions of the transition countries. The Northern Tier economies are now back to pre-transition income levels (on average) after a drop in GDP of about twenty percent at the outset of the transition. The Eurasian economies experienced a much more significant drop in GDP since communism's collapse (of about fifty percent), and have so far recovered very little. The initial income drop and subsequent recovery in the Southern Tier countries falls in between the patterns of the other two subregions. The Southern Tier pattern is also distinguished by a notable setback in 1997 in economic growth.

Figure 4 distinguishes further between GDP patterns among the twenty-seven transition countries. Seven patterns are identified, and range widely: from a small income drop and full recovery (in five Northern Tier countries); to a very large income drop (of close to seventy-five percent) followed by good recovery (in the Caucasus in particular); to an insignificant income drop and minimal economic growth subsequently (in Uzbekistan).

Annual **inflation** rates much above the single-digit range erode business confidence, and the ability and incentive to invest and expand at the enterprise level. *Table 9* and *Figure 5* show that considerable progress towards controlling inflation has occurred in a majority of the transition countries. In fact, seventeen countries have been able to hold inflation in the past two years to close to single-digits levels.

Nevertheless, while inflation rates have come down impressively in most countries since the early 1990s, large distinctions in inflation rates still remain, particularly between CEE and Eurasia. More specifically, all but one of the ten countries that had inflation rates in

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[27] Fifty-eight percent of Uzbekistan's exports in 1997 were textiles (cotton and wool); in Tajikistan, 41%; and Turkmenistan, 27%. Thirty-four percent of Russia's exports in 1997 were metals; in Kazakhstan and Kyrgyzstan, it was 32%.

1999 close to twenty percent or higher are in Eurasia. Romania, with inflation of forty-six percent in 1999, is the exception. Similarly, all seven countries that witnessed a notable increase in inflation from 1998 to 1999 are in Eurasia.

The decline in inflation among the Northern Tier CEE countries has been a steady, incremental trend, falling on average about four to five percentage points annually since 1994 to an annual rate in 1999 of less than seven percent. In the Southern Tier CEE, inflation fell significantly in Bulgaria, Albania, and Romania in 1998 after sharp increases in all three countries in 1997. Discounting Yugoslavia, for which data are not available, 1999 inflation rates in the Southern Tier were very low (five percent or less) in all countries but Romania.

Trends in 1998 inflation rates in Eurasia were largely tied to exchange rate movements that in turn were linked to economic turmoil in Russia. In particular, the large depreciation of the Russian ruble contributed to depreciation of currencies in other Eurasian countries that are closely linked to Russia. More expensive imports, in turn, filtered through these economies and, alongside fiscal imbalances, contributed to inflation rate increases.

Similar inflationary pressures--from macroeconomic imbalances, currency price trends, and high import prices—contributed to inflation increasing in 1999 in Belarus, Ukraine, Moldova, Kyrgyzstan, Turkmenistan, Georgia, as well as in Russia. Of all the transition countries in 1999, inflation was far and away the highest in Belarus (294 percent). Of the Eurasian countries, inflation has been lowest in Azerbaijan, Armenia, and Kazakhstan, at single-digit rates in 1998-1999. These low inflation rates have been facilitated by tight monetary policy.

Budget deficits (*Table 10*) that remain high fuel inflation and unproductive activity, particularly if financial markets are not well functioning. If in fact the financial markets are well established, high budget deficits may ultimately crowd out potential private sector investors from such markets. More generally, as witnessed in the case of Russia, persistently high budget deficits can seriously undermine investor confidence. With the recent development of securities markets, a number of countries have been able to finance deficits in a noninflationary manner at least in the short-term. But, such an approach is unsustainable if reducing the structural deficit is not tackled; all the more so if the share financed by foreign portfolio investors is significant.

Overall, fiscal balances have improved substantially during the transition, from a population-weighted average fiscal deficit in the range of twenty-four percent in 1992 to 7.2 percent in 1994 to 5.4 percent in 1997 to 2.9 percent in 1999. Moreover, many earlier estimates of 1999 fiscal deficits now seem to be too high. This is particularly true for several Southern Tier countries, which survived the Kosovo conflict better than was anticipated by many forecasters. Bulgaria stands out in this regard: forecast in May 1999 to incur a 1999 fiscal deficit of 3.8 percent, it is now estimated to have incurred a slight surplus of 0.3 percent.

In addition, the most recent estimate of Russia's 1999 fiscal deficit (1.7 percent of GDP) is considerably lower than that (of six percent) from the EBRD in its November 1999 *Transition Report. S*ome recent progress in fiscal reform in Russia has no doubt contributed to a more manageable fiscal deficit. The IMF reports that public revenues have increased as a percent of GDP, partly because of better tax compliance, and partly because a higher proportion of taxes is being paid in cash (and less through barter).

On the other hand, fiscal deficits have increased significantly in 1999 in a number of Northern Tier countries, in particular, Lithuania (to 8.6 percent of GDP), the Czech Republic (five percent), Estonia (4.8 percent), and Latvia (3.8 percent). Fiscal deficits on average in the Northern Tier were 3.9 percent of GDP in 1999. This is higher than the regional averages of the Southern Tier and Eurasia, and is the first time such a trend has occurred in the transition.

Of greater concern are the handful of countries that have maintained an unsustainably high fiscal deficit over the years. Seven countries have had a fiscal deficit greater than five percent of GDP for at least three years on average. Among these, Albania continues to sustain the highest fiscal deficits: 11.3 percent from 1997 to 1999. Lithuania is the other CEE country in this group. Five are Eurasian countries (Kyrgyzstan, Kazakhstan, Moldova, Armenia, and Russia).

Table 11 shows trends in domestic investment and the share of the economies in private sector hands. The **private sector share of the economy** is a rough proxy for the extent of economic restructuring, either through the privatization process or the growth of new private-sector firms. Those economies where private sector output predominates are much more likely to generate momentum towards greater economic expansion overall.

Nineteen countries of the region in fact now have a private sector generating at least fifty percent of GDP. The average for all of CEE and NIS is sixty-one percent. This represents very impressive gains; in 1989, the region's private sector share was probably closer to ten percent of GDP (*Figure 6*).

Most OECD economies have private sectors that range from seventy to eighty-five percent of GDP. Seven transition countries (five Northern Tier countries, Russia, and Albania) now have private sectors that meet this threshold. The private sector share of GDP is highest in Hungary and the Czech Republic (both at eighty percent). Slovenia's private sector as a share of GDP is fifty-five percent. This is the lowest among the Northern Tier countries, though perhaps not much different from that of its neighbors, Austria and Italy.

Seven countries (Bosnia-Herzegovina plus six Eurasian countries) still have economies in which more than fifty percent of economic activity derives from the public sector. In Belarus, the public sector constitutes eighty percent of GDP. Of these seven countries, all but Moldova rank at the bottom on the economic reform scores of *Table 7*.

Domestic investment (*Table 11*) contributes to the productive capacity of the economy and hence helps provide the momentum that is necessary for sustained economic expansion further down the road. Not surprisingly, domestic investment as a percent of GDP is highest among the Northern Tier countries (twenty-six percent of GDP). This is higher than the proportion found among the advanced economies (nineteen percent of GDP), though not as great as that in the East Asian developing countries (thirty-six percent). Gross domestic investment is closer to twenty percent of GDP on average in the Eurasian and Southern Tier CEE countries.

Eleven countries have witnessed an increase in the share of domestic investment in GDP over the transition, though the largest increases have occurred mostly in the Northern Tier CEE countries. This includes Slovakia, Poland, and Slovenia, but also Croatia. The largest decreases have occurred mostly in Eurasia. If the figures are credible, there has been substantial erosion of investment in Armenia and Kazakhstan.[28]

Trends in **labor productivity**, or output per employee, can provide important insights into the extent to which firms are restructuring (*Table 12* and *Figure 7*). The efficiency gains from an increase in productivity can stem from a number of factors, including fewer excess workers, greater skilled and/or motivated workers, improved capital stock, and/or a greater capacity to manage.

Among the CEE countries, labor productivity growth over the transition has been particularly impressive in Hungary and Poland and, to a lesser extent, in Slovenia. All three countries have industry productivity levels that far exceed such levels at the outset of the transition. Poland and Hungary have been able to sustain high productivity growth rates since 1992, and Slovenia since 1993. Moreover, while much of the earlier year productivity gains stemmed from labor shedding (or employment reduction), much of the more recent gains have stemmed from relatively rapid output growth. Productivity gains in the Southern Tier countries (for which data are available) and in the Czech Republic have been much more modest.

To a large extent, the productivity patterns as displayed in *Figure 7* reflect the GDP patterns as shown in *Figures 3* and *4*. This may be more evident in the case of many Eurasian countries where output changes have been much more dynamic than labor market trends; that is, where labor markets have been relatively stagnant, characterized by minimal labor shedding, mobility, and/or turnover. For example, as with patterns in output, rapid productivity growth in recent years in Kyrgyzstan, Azerbaijan, and Belarus comes on the heels of very significant productivity drops in earlier transition years. This scenario may suggest that recent labor productivity gains in these countries are more a reflection of output recovery than of any significant enterprise restructuring.

Productivity levels in Uzbekistan are higher today relative to pre-transition levels in large part because, as with GDP, productivity dropped insignificantly in Uzbekistan in the

[28] Interpreting domestic investment figures is particularly precarious in no small part because estimates are very volatile; that is, they are subject to frequent revisions, for back years as well as for the most recent years.

early transition years. More generally, the economic data for Uzbekistan suggest that it is in a transition category all its own. Salient in this regard is insignificant progress in economic reforms with a relatively low private sector share of GDP, on the one hand, yet little change in economic activity (neither collapse nor robust economic and productivity growth) and virtually no official unemployment.

How and to what extent these economies integrate into the world economy figure prominently into the type of their transition path and its sustainability. *Tables 13* through *15* highlight some key aspects of this integration: export growth and openness to trade; current account balances; institutional integration; foreign direct investment; and external debt.

Table 13 looks primarily at trade data and current account balances. The gains from trade can be substantial, and range from the tangible (of increasing an economy's quantity and quality of available goods, including capital goods) to the intangible (of providing incentives and a constituency to maintain the market-based reforms which also serve as pre-requisites to institutional integration with the industrial market economies).

There are also downsides to integrating into the world economy through trade. For example, when one or more economies incur economic difficulties or a slowdown, these troubles spill over to trading partners. In addition, economies that produce a high proportion of commodity exports are vulnerable to volatile commodity prices. These tendencies have been important factors for the prospects for many of the transition economies, particularly those of the former Soviet Union, during the global (and Russian) financial crisis and its aftermath.

These factors become evident when one looks at export growth and current account trends. Overall **export growth** for the entire transition region slowed considerably from the 1995-1997 average of twelve percent (from *Monitoring Country Progress*, October 1998) to an average of two percent from 1996-1998. This is largely because exports contracted by seven percent in the region as a whole in 1998. Eleven of the twelve Eurasian countries witnessed a shrinking export sector in 1998. Eight Eurasian countries, including Russia, saw exports fall in 1998 by more than ten percent. In contrast, exports grew by more than ten percent in 1998 in six of the eight Northern Tier CEE countries, all but Lithuania and Slovenia.

1999 saw somewhat different export sector dynamics in the region. In Eurasia, exports contracted slightly (by one percent) overall in 1999. Even though the Russian economy expanded in 1999, its export sector contracted by two percent. The export sectors of those Eurasian countries most closely linked to the Russian economy also contracted: Moldova’s export sector fell by twenty-seven percent; Belarus’ by sixteen percent. On the other hand, with the exception of Russia, the major oil-exporting countries of Eurasia saw their export sectors growing, in step with growing oil prices. In particular, Turkmenistan’s export sector grew by seventy-nine percent in 1999, and Azerbaijan’s by twenty-five percent. Kazakhstan’s export sector grew slightly, by one percent.

About two-thirds of the economies in CEE saw exports contract in 1999. As noted earlier, much of this was due to slower economic growth in Western Europe. The majority of CEE exports go to Western Europe. Of the Northern Tier countries, only Hungary experienced anything resembling robust export growth in 1999 (ten percent). In addition, for the Southern Tier countries, access to Western Europe markets and to intra-regional markets was impeded due to the Kosovo conflict. Some trade--particularly along the Danube River--remains impeded. Yet, despite the interruption due to war, exports apparently grew in 1999 by roughly fifteen percent in both Albania and Bosnia-Herzegovina. As with Macedonia, some of this growth may have stemmed from the reconstruction of Kosovo in the second half of the year.

The Northern Tier CEE countries are the most outward-oriented; their merchandise exports plus imports on average equaled thirty-five percent of (purchasing power parity) GDP in 1998. Such **openness to trade**, to some extent, is a reflection of the competitiveness of an economy (though smaller economies also tend to be more open out of necessity). The Northern Tier average on this score is roughly comparable to the average of the advanced economies (thirty-eight percent of GDP), though it falls short of the EU average of fifty-four percent. The Eurasian countries and the Southern Tier CEE countries generally have considerably smaller trade sectors than do the Northern Tier CEE countries; sixteen percent and twenty percent of GDP on average, respectively. The large majority (seventeen) of the transition countries saw their trade share of GDP fall in 1998, an outcome which stemmed largely from the global financial crisis.

There is a fairly close fit between the relatively autarchic economies (those with small trade sectors) and the poorest economies (those with the lowest per capita income). This is particularly evident from the 1997 data; that is, prior to the trade contraction that occurred nearly across the board due to the global slowdown. Six countries in 1997 had trade sectors (exports plus imports) that were smaller than fifteen percent of the economy: Albania; Georgia; Armenia; Uzbekistan; Azerbaijan; and Kyrgyzstan. Average per capita income of these six countries is about $2,500 in purchasing power parity terms. Of all the remaining transition countries, only in Tajikistan and Moldova is per capita income lower than this average.

To some extent, as the economies climb out of the “transition trough” and incur robust economic growth, **current account deficits** can be expected, and may reflect positive developments (*Table 13*). Such deficits may be temporary if much of the imports are capital goods that in turn spur an increase in competitiveness and exports. This is likely to be happening in some CEE countries, in the Northern Tier CEE in particular. In addition, current account deficits are less burdensome if, as is the case in many Northern Tier CEE countries, they can be financed in large part by FDI inflows.

Nevertheless, macroeconomic stability can be at significant risk in the presence of large current account deficits, particularly if they are sustained over several years. In this context, about one-half (thirteen) of the transition countries have been sustaining current account deficits greater than five percent of GDP on average since 1995. The highest deficits have been sustained in Bosnia-Herzegovina (thirty-five percent of GDP from

1995-1999), followed by five Eurasian countries: Armenia (twenty-nine percent); Azerbaijan (twenty-four percent); Turkmenistan (seventeen percent); Kyrgyzstan (fifteen percent); Moldova (fourteen percent); and Lithuania (eleven percent of GDP).

The Northern Tier countries have not been immune to large current account imbalances. In fact, the extent to which these balances have deteriorated is striking: from a deficit of one percent of GDP in 1994-1996 on average to six percent in 1999. Poland, Lithuania, Latvia, and Slovakia all had current account deficits roughly equal to or greater than five percent of GDP in 1999.

Russia was the only transition country in 1999 to incur a current account surplus--a very large one, in fact, close to eleven percent of GDP. As alluded to earlier, this was due to very significant import "compression," as domestic production replaced much of what was previously imported.

An important means to catalyze the reform progress and to lock-in the gains from reforms is through the institutionalization of global integration, or **memberships in international organizations**. For our purposes, this includes membership or participation towards membership in the OECD, the World Trade Organization, NATO, and the European Union. As shown in *Table 13*, institutional integration, as so defined, is taking place almost exclusively among the CEE countries, and primarily still in the Northern Tier. The Czech Republic, Hungary, and Poland are now members of both the OECD and NATO. In addition, these three countries plus Slovenia and Estonia were invited in 1997 to participate in the next round of negotiations towards EU membership. In October 1999, five more transition countries were invited to participate: Slovakia, Latvia, Lithuania, and two Southern Tier countries, Romania, and Bulgaria.

As a preliminary step towards this invitation, the EU had previously negotiated Association Agreements (AA) with all ten of these countries. More recently, Macedonia has become the first country of a newly designated West Balkan region to begin negotiations with the EU towards a Stabilization and Association Agreement (SAA), a step removed from an AA.

Estonia, Latvia, and Kyrgyzstan are the most recent members in the region to join the World Trade Organization. Of the ten WTO members in the transition region, Kyrgyzstan is the first from Eurasia.

Foreign direct investment (FDI) is key to the transition (*Table 14*). It helps meet the substantial fixed investment needs of the region that arise from obsolete fixed capital stocks and inadequate infrastructure. It does so without adding to the external debt burden. In the context of highly volatile short-term capital flows, it is a stabilizing influence. And, it brings with it some very important externalities, including access to advanced technology and export markets, and exposure to advanced management and marketing techniques. Not only does FDI follow reforms, it contributes towards catalyzing and sustaining them, as well.

The volume of net FDI inflows for the region in 1999 has been estimated to be roughly the same as that in 1998, or high relative to earlier years. Almost sixty percent of all FDI inflows since 1989 have occurred from 1997-1999. The Northern Tier CEE countries continue to receive the lion's share of FDI: on a per capita basis, eight times more than in Eurasia, and roughly three times more than in the Southern Tier CEE countries. Hungary has attracted the greatest cumulative FDI per capita of all the transition countries since 1989, though the Czech Republic and Estonia are not far behind, given the significant FDI flows to both in 1998-1999.

FDI flows to Russia in 1999 resumed the very modest levels attained in 1997. Overall, since 1989, only five transition countries have received less FDI per capita than Russia: Ukraine, Belarus, Tajikistan, Uzbekistan, and Bosnia-Herzegovina. Foreign direct investment in Eurasia continues to be largely in response to opportunities to exploit energy resources, as evident in the relatively high FDI levels in Azerbaijan and Kazakhstan.

1999 FDI in the Southern Tier CEE fell short of the levels in 1998 due largely to the Kosovo conflict. End-year 1999 estimates show that all the Southern Tier countries but Bulgaria saw lower per capita FDI flows in 1999. Per capita FDI flows continue to be far larger in Croatia than elsewhere in the Southern Tier.

The importance of a sustainable **external debt** position has increased in the wake of the global financial crisis (*Tables 14 & 15*). Overall, total external debt as a percent of exports has been increasing in a large majority of transition countries in recent years. In fact, from 1995-1998, it increased in twenty countries. Only in Hungary, Poland, Latvia, Bosnia-Herzegovina, and Belarus was the total external debt to export ratio lower in 1998 than in 1995. An important part of this broader trend of increasing debt relative to exports has been slow growing or even contracting exports.

Of the three subregions, the 1998 average total external debt as a percent of exports was highest in the Southern Tier CEE (at 172 percent), and comparable to the average for the developing countries (of 173 percent). The Eurasian average was slightly lower, though debt by this measure has been increasing the most rapidly in Eurasia since at least 1995.

The World Bank uses an indebtedness classification scheme to monitor difficulties in external debt management. This scheme is based on the present value of debt.[29] Evidence from developing countries has shown that debt service difficulties become increasingly likely when the ratio of the present value of debt to exports reaches 200 percent and the ratio of debt service to GNP exceeds forty percent. Drawing from this experience, the World Bank has classified countries with a present value of debt service greater than 220 percent of exports or eighty percent of GNP as severely indebted; countries that were not severely indebted but whose present value of debt service

[29] The present value of debt is defined as the sum of short-term debt plus the discounted sum of total debt service payments due on public, publicly guaranteed, and private nonguaranteed long-term external debt of the life of existing loans.

exceeded 132 percent of exports or forty-eight percent of GNP as moderately indebted; and countries that did not fall into the above two groups as less indebted.

By these criteria, two transition countries in 1996 were severely indebted (Bulgaria and Bosnia-Herzegovina) and four were moderately indebted (Hungary, Macedonia, Georgia, and Kyrgyzstan). This had increased by 1998 to at least three countries that were severely indebted (Bulgaria, Macedonia, and Turkmenistan; data are not available for Bosnia-Herzegovina) and six that were moderately indebted (Hungary, Russia, Moldova, Georgia, Kyrgyzstan, and Tajikistan). By these measures, external debt has increased significantly in Eurasia from 1996-1998, but has remained relatively constant (as a percent of GDP) or has decreased (as a percent of exports) in the CEE countries.

Servicing the debt remains manageable for most transition countries, though debt service has increased for many in recent years. Hungary, Romania, and Moldova have had the highest debt service in recent years, roughly thirty percent of exports in either 1998 or 1999. This amount is slightly above the developing countries' average (of twenty-eight percent). Georgia and Lithuania had to service an external debt equal to twenty percent of exports on average in 1998-1999. The lowest debt service is found in Belarus and Albania.

Table 8. Growth in Real GDP (%)

	1992	1993	1994	1995	1996	1997	1998	1999	1997-1999 average
Bosnia-Herzegovina	…	…	…	21.0	69.0	30.0	18.0	8.0	18.7
Azerbaijan	-22.6	-23.1	-19.7	-11.8	1.3	5.8	10.0	7.4	7.7
Belarus	-9.6	-7.6	-12.6	-10.4	2.8	10.4	8.3	3.0	7.2
Georgia	-44.8	-25.4	-11.4	2.4	10.5	11.0	2.9	3.0	5.6
Poland	2.6	3.8	5.2	7.0	6.1	6.9	4.8	4.1	5.3
Kyrgyzstan	-19.0	-16.0	-20.0	-5.4	7.1	9.9	2.3	2.2	4.8
Armenia	-52.6	-14.8	5.4	6.9	5.8	3.1	7.2	4.0	4.8
Hungary	-3.1	-0.6	2.9	1.5	1.3	4.6	4.9	4.1	4.5
Estonia	-14.2	-9.0	-2.0	4.3	3.9	10.6	4.0	-1.3	4.4
Latvia	-34.9	-14.9	0.6	-0.8	3.3	8.6	3.6	0.8	4.3
Slovenia	-5.5	2.8	5.3	4.1	3.5	4.6	3.9	3.8	4.1
Slovakia	-6.5	-3.7	4.9	6.9	6.6	6.5	4.4	1.0	4.0
Uzbekistan	-11.1	-2.3	-4.2	-0.9	1.6	2.4	4.4	4.1	3.6
Tajikistan	-29.0	-11.0	-18.9	-12.5	-4.4	1.7	5.3	3.7	3.6
Lithuania	-21.3	-16.0	-9.5	3.5	4.9	7.4	5.1	-3.3	3.1
Albania	-7.2	9.6	9.4	8.9	9.1	-7.0	8.0	8.0	3.0
FYR Macedonia	-8.0	-9.1	-1.8	-1.2	0.8	1.5	2.9	2.5	2.3
Croatia	-11.7	-8.0	5.9	6.8	6.0	6.5	2.3	-2.0	2.3
Kazakhstan	-2.9	-9.2	-12.6	-8.2	0.5	2.0	-2.5	1.7	0.4
Russia	-14.5	-8.7	-12.7	-4.1	-3.5	0.8	-4.5	3.2	-0.2
Bulgaria	-7.3	-1.5	1.8	2.1	-10.1	-7.0	3.5	2.5	-0.3
Czech Republic	-3.3	0.6	3.2	6.4	3.8	0.3	-2.3	-0.5	-0.8
Turkmenistan	-5.3	-10.0	-18.8	-8.2	-8.0	-26.1	5.0	16.0	-1.7
Ukraine	-13.7	-14.2	-23.0	-12.2	-10.0	-3.2	-1.7	-0.4	-1.8
Moldova	-29.1	-1.2	-31.2	-3.0	-8.0	1.3	-8.6	-5.0	-4.1
Romania	-8.8	1.5	3.9	7.1	4.1	-6.9	-5.4	-3.9	-5.4
Yugoslavia	-27.9	-30.8	2.7	6.0	5.9	7.5	2.6	...	...

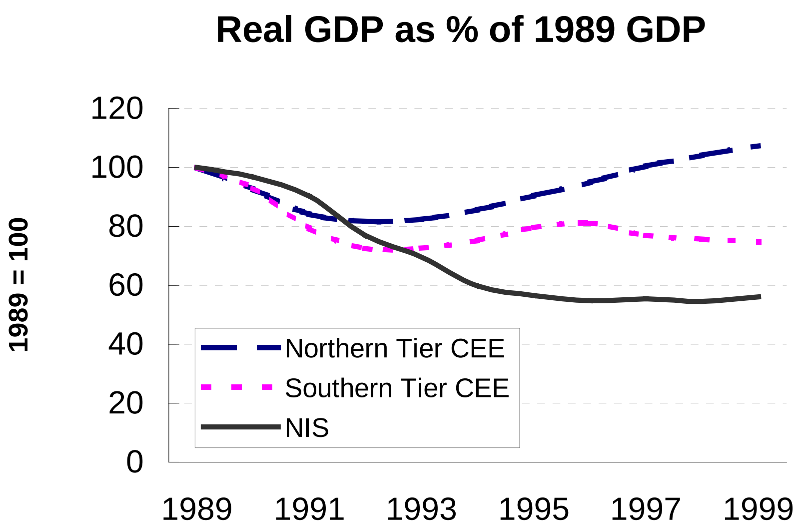
Regional Averages	1992	1993	1994	1995	1996	1997	1998	1999	1997-1999 average
CEE & Eurasia	-12.4	-7.7	-8.8	-2.2	-0.4	1.5	-0.3	2.4	1.2
Northern Tier CEE	-2.6	0.4	3.6	5.6	4.9	5.7	3.7	2.7	4.0
Southern Tier CEE	-12.8	-6.7	3.6	6.8	6.8	-0.2	0.8	-0.4	0.1
Eurasia	-14.9	-10.0	-14.4	-5.9	-3.2	0.8	-1.6	2.7	0.7
European Union	1.2	-0.4	2.8	2.4	1.7	2.6	2.7	2.3	2.5
Advanced Countries	2.1	1.4	3.3	2.7	3.2	3.3	2.4	3.1	2.9
Developing Countries	6.4	6.4	6.7	6.1	6.5	5.8	3.2	3.8	4.3

Benchmarks (a) 3 years positive economic growth, (b) 3 year average growth rate of 2% or more

EBRD, *Transition Report 1999* (November 1999); IMF, *World Economic Outlook* (April 2000); ECE, *Economic Survey of Europe* (1999, No. 2); and most recent IMF and EIU country reports.

These figures should be interpreted only as indicative of broad ordesr of magnitude. An important reason for this is that informal economic activity is largely not reflected in the numbers.

Figure 3.

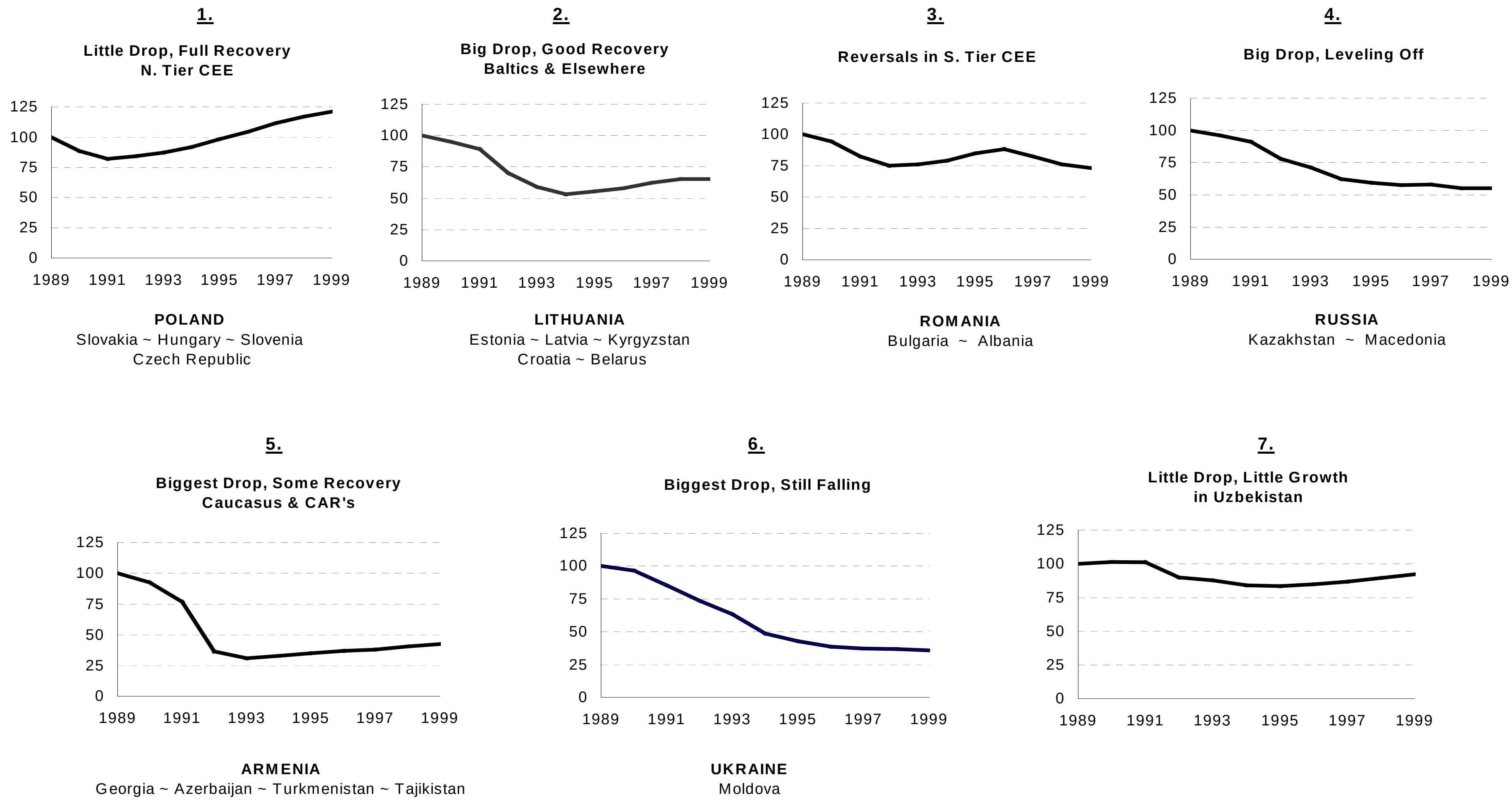


Source: EBRD, *Transition Report 1999* (November 1999).

Figure 4.

GDP Patterns

Real GDP as % of 1989 GDP



Note: Charts reflect representative country patterns, for example; Poland, Lithuania, Romania etc..
Source: EBRD, Transition Report 1999 (November 1999)

Table 9. Inflation

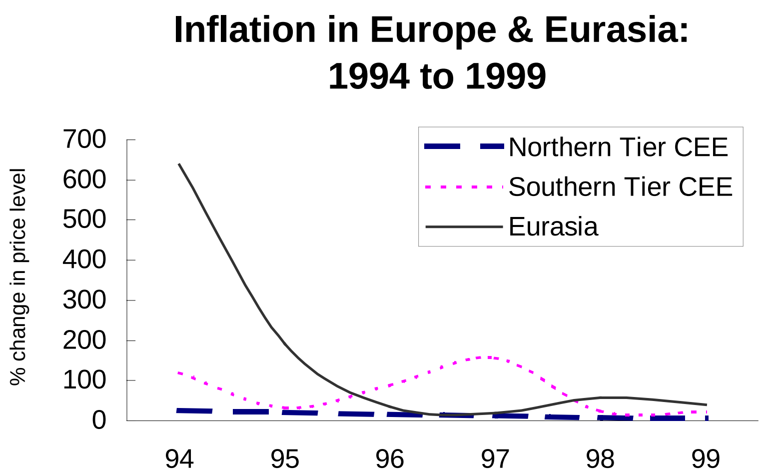
	1994	1995	1996	1997	1998	1999	1998-99	1997-99
Azerbaijan	1,664	412	20	4	-1	-9	-5	-2
FYR Macedonia	126	16	2	2	-1	0	-1	0
Croatia	98	2	4	4	6	4	5	5
Lithuania	72	40	25	9	5	1	3	5
Latvia	36	25	18	8	5	3	4	5
Estonia	48	29	23	11	8	3	6	7
Czech Republic	10	9	9	9	11	2	7	7
Slovenia	22	14	10	8	8	6	7	7
Slovakia	13	10	6	6	7	11	9	8
Armenia	5,273	177	19	14	9	1	5	8
Bosnia-Herzegovina	780	-4	-25	14	10	5	8	10
Georgia	15,607	163	39	7	4	19	12	10
Kazakhstan	1,880	176	39	17	7	8	8	11
Poland	32	28	20	15	12	7	10	11
Hungary	19	28	24	18	14	10	12	14
Ukraine	891	376	80	16	11	23	17	17
Albania	23	8	13	33	21	-1	10	18
Moldova	330	30	24	12	8	39	24	20
Kyrgyzstan	190	39	30	26	12	37	25	25
Turkmenistan	1,798	1,005	992	84	17	24	21	42
Uzbekistan	1,568	305	54	71	29	29	29	43
Russia	307	197	48	15	28	86	57	43
Tajikistan	350	610	418	88	43	28	36	53
Romania	137	32	39	155	59	46	53	87
Belarus	2,200	709	53	64	73	294	184	144
Bulgaria	96	62	123	1,082	22	0	11	368
Yugoslavia	7.9E+10	72	91	23	30	...	...	...

REGIONAL AVERAGES	1994	1995	1996	1997	1998	1999	1998-99	1997-99
CEE & Eurasia	781	199	61	51	23	49	36	41
Northern Tier CEE	28	24	18	13	11	6	9	10
Southern Tier CEE	167	38	52	284	36	24	30	115
Eurasia	1,073	277	74	24	24	64	44	37
European Union	3.0	2.9	2.5	1.8	1.4	1.4	1.4	1.5
Advanced Countries	2.6	2.6	2.4	2.1	1.5	1.4	1.5	1.7
Developing Countries	55.1	22.9	15.1	9.5	10.1	6.5	8.3	8.7
Benchmarks							< 10.0	< 15.0

Retail/consumer prices, annual average. Regional averages exclude Yugoslavia.

EBRD, *Transition Report 1999* (November 1999); IMF, *World Economic Outlook* (April 2000); ECE, *Economic Survey of Europe* (1999, No. 2); and most recent IMF and EIU country reports.

Figure 5.



Source: EBRD, *Transition Report 1999* (November 1999).

Table 10. Fiscal Balance as Percent of GDP

	1992	1993	1994	1995	1996	1997	1998	1999	1997-99 average
Bulgaria	-5.2	-10.9	-5.8	-6.4	-10.4	-3.0	1.0	0.3	-0.6
Estonia	-0.3	-0.7	1.3	-1.3	-1.9	2.2	-0.3	-4.8	-1.0
Belarus	0.0	-1.9	-2.5	-1.9	-1.6	-0.7	-0.3	-3.0	-1.3
Slovenia	0.2	0.1	-0.3	-0.5	-0.2	-1.7	-1.4	-0.9	-1.3
Croatia	-3.9	-0.8	1.6	-0.9	-0.4	-1.3	0.6	-3.6	-1.4
Latvia	-0.8	0.6	-4.0	-3.9	-1.7	0.1	-0.8	-3.8	-1.5
Turkmenistan	13.2	-0.5	-1.4	-1.6	-0.2	0.0	-2.7	-4.0	-2.2
Bosnia-Herzegovina	...	...	-17.0	0.0	-4.0	-2.0	-3.0	...	-2.5
Poland	-6.7	-3.1	-3.1	-2.8	-3.3	-3.1	-3.0	-3.3	-3.1
Ukraine	-25.4	-16.2	-9.1	-4.9	-3.2	-5.6	-2.7	-1.1	-3.1
Romania	-4.6	-0.4	-1.9	-2.6	-4.0	-3.6	-3.3	-2.7	-3.2
Czech Republic	-3.1	0.5	-1.1	-1.8	-1.1	-2.1	-2.6	-5.0	-3.2
Uzbekistan	-18.4	-10.4	-6.1	-4.1	-7.3	-2.3	-3.8	-3.8	-3.3
Azerbaijan	...	-15.3	-12.1	-4.9	-2.8	-1.7	-4.2	-4.0	-3.3
FYR Macedonia	-9.6	-13.8	-2.9	-1.2	-0.5	-0.4	-1.7	-7.8	-3.3
Georgia	-25.4	-26.2	-7.4	-4.5	-4.4	-3.8	-4.4	-3.7	-4.0
Tajikistan	-30.5	-23.4	-5.4	-11.9	-5.8	-3.3	-3.8	-5.0	-4.0
Hungary	-7.2	-6.6	-8.4	-6.4	-3.0	-4.8	-4.8	-3.9	-4.5
Slovakia	...	-7.0	-1.3	0.2	-1.9	-4.4	-5.8	-3.6	-4.6
Russia	-42.6	-15.9	-9.7	-5.9	-9.1	-8.1	-5.4	-1.7	-5.1
Lithuania	0.5	-3.3	-5.5	-4.5	-4.5	-1.8	-5.8	-8.6	-5.4
Armenia	-13.9	-54.7	-10.5	-11.0	-9.3	-5.9	-5.2	-6.1	-5.7
Moldova	-26.2	-7.4	-8.7	-5.7	-6.7	-7.5	-8.1	-4.5	-6.7
Kazakhstan	-7.3	-4.1	-7.5	-2.7	-4.7	-6.8	-8.0	-7.0	-7.3
Kyrgyzstan	-17.4	-13.5	-11.6	-17.3	-9.5	-9.0	-9.9	-11.2	-10.0
Albania	-20.3	-14.4	-12.4	-10.3	-12.1	-12.6	-10.4	-10.9	-11.3

REGIONAL AVERAGES	1992	1993	1994	1995	1996	1997	1998	1999	1997-99 average
CEE & Eurasia	-23.9	-11.5	-7.2	-4.8	-6.0	-5.4	-4.2	-2.9	-4.2
Northern Tier CEE	-5.3	-3.1	-3.4	-3.0	-2.7	-3.0	-3.4	-3.9	-3.4
Southern Tier CEE	-6.2	-4.4	-3.2	-3.7	-5.4	-3.8	-2.5	-3.1	-3.2
Eurasia	-31.1	-14.7	-8.7	-5.5	-6.9	-6.3	-4.7	-2.6	-4.5
European Union	-5.2	-6.3	-5.6	-5.4	-4.3	-2.5	-1.6	-0.8	-1.6
Advanced Countries	-4.2	-4.7	-4.0	-3.8	-3.1	-1.7	-1.2	-1.0	-1.3
Developing Countries	-3.0	-3.2	-2.7	-2.7	-2.4	-2.6	-4.0	-4.4	-3.7
European Union Target									-3.0
Benchmark									-3.0

EBRD, *Transition Report 1999* (November 1999); IMF, *World Economic Outlook* (April 2000); and most recent IMFand EIU country reports.
Fiscal balance is overall general balance (i.e. all levels of government).

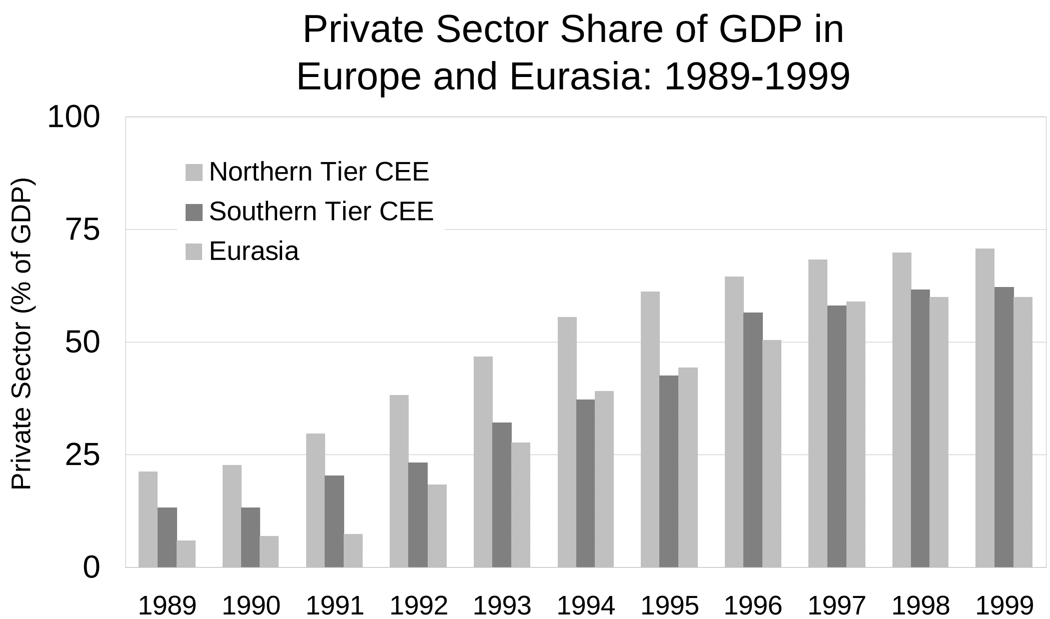
Table 11. Domestic Investment and Private Sector Share of GDP

Country	Gross Domestic Investment 1990	1994	1997	1999	1990/94-1997/99	Private Sector Output 1996	mid-1999
		% of GDP			% change	% of GDP	
Czech Republic	26	30	31	…	19	75	80
Hungary	…	26	16	…	-38	70	80
Albania	…	…	…	…	…	75	75
Estonia	24	26	29	23	-4	70	75
Slovakia	31	29	39	…	26	70	75
Lithuania	…	14	17	…	21	70	70
Russia	29	22	19	17	-41	60	70
Latvia	28	23	29	…	-14	60	65
Poland	21	16	26	27	29	60	65
Romania	20	20	19	…	-5	60	60
Armenia	44	11	9	…	-80	50	60
Croatia	14	14	24	25	79	50	60
Georgia	19	20	22	…	16	50	60
Kyrgyzstan	23	15	19	…	-17	50	60
Bulgaria	21	14	15	16	-24	45	60
FYR Macedonia	24	18	20	…	-17	50	55
Ukraine	23	24	18	…	-22	50	55
Slovenia	21	20	25	27	29	45	55
Kazakhstan	23	6	13	…	-43	40	55
Moldova	19	19	20	…	5	40	45
Uzbekistan	31	…	35	…	13	40	45
Azerbaijan	…	24	27	…	13	25	45
Bosnia-Herzegovina	…	…	…	…	…	...	35
Tajikistan	…	22	…	…	…	20	30
Turkmenistan	…	…	…	…	…	20	25
Belarus	22	33	25	…	14	15	20

REGIONAL AVERAGES	1990	1994	1997		1990-1997/99	1996	mid-1999
		% of GDP			% change	% of GDP	
CEE & Eurasia	26	20	21	…	-19	54	61
Northern Tier CEE	23	21	26	…	13	64	70
Southern Tier CEE	20	18	19	…	-5	57	59
Eurasia	27	22	20	…	-26	50	59
Advanced Economies			19			70-85	
Developing Countries			25				
Sub-Saharan Africa			18				
East Asia/Pacific			36				
Benchmarks		*GDI/GNP > 25%*			*no decline*	*more than 70%*	

Source: EBRD, *Transition Report 1999* (November 1999); *World Development Report 1999/2000* (August 1999); World Bank, *World Development Indicators* (April 2000); and most recent IMF and EIU country reports.

Figure 6.



Source: EBRD, *Transition Report* (November 1999 and earlier editions).

Table 12. Labor Productivity

Region/Country	1990	1991	1992	1993	1994	1995	1996	1997	1998	1996-98[1] average	1998/1989[2] (%)
	Labor Productivity in Industry (% change)										
Kyrgyzstan	-0.4	7.4	-23.7	-17.0	-14.5	-25.8	16.5	48.8	18.0	27.8	88
Azerbaijan	-3.5	7.3	-19.0	-12.0	-21.0	-16.6	16.1	17.3	3.0	12.1	68
Belarus	3.6	0.7	-3.5	-7.5	-13.2	-0.9	4.7	18.6	11.3	11.5	111
Estonia	...	-3.2	-30.3	-5.1	0.9	-5.6	7.5	22.4	4.0	11.3	...
Croatia	-10.4	-13.1	-0.8	-2.8	1.6	5.8	11.4	14.1	7.3	10.9	110
Poland	-19.7	0.0	12.5	13.8	13.0	6.3	9.1	10.5	5.5	8.4	157
Latvia	...	4.8	-28.0	-19.4	2.1	13.5	11.2	10.2	3.5	8.3	...
FYR Macedonia	-7.5	-9.6	-10.0	-10.4	-4.9	3.1	9.2	8.2	6.5	8.0	83
Armenia	-9.9	-0.2	-41.4	0.4	7.4	20.0	20.2	-2.2	4.8	7.6	84
Hungary	-4.0	-8.3	4.0	16.3	14.7	10.5	4.4	11.7	6.6	7.6	168
Kazakhstan	0.7	-2.3	-10.5	-1.0	-21.2	0.9	2.9	17.3	1.8	7.3	85
Lithuania	...	...	...	-23.1	-11.1	13.9	9.5	0.8	8.1	6.1	...
Slovenia	-7.9	-2.0	-3.0	6.7	11.4	7.2	6.6	5.2	5.2	5.7	132
Slovakia	-4.0	-15.7	7.3	-1.1	9.0	4.0	2.5	4.8	9.1	5.5	114
Ukraine	3.7	-4.0	-1.8	-1.9	-21.4	-4.0	3.1	6.1	6.6	5.3	84
Uzbekistan	0.4	0.5	-1.7	2.3	10.5	-1.6	4.1	6.3	5.3	5.2	129
Czech Republic	0.6	-19.3	-0.2	-0.5	7.9	8.1	2.6	5.6	5.1	4.4	107
Romania	-21.1	-18.7	-10.0	10.4	8.6	16.1	5.3	3.8	3.2	4.1	91
Russia	2.1	-5.5	-14.6	-11.2	-11.5	4.6	1.3	7.9	-0.3	3.0	74
Moldova	0.9	-4.4	-25.5	7.3	-23.1	11.8	7.9	8.0	-9.2	2.2	70
Georgia	...	-14.9	-12.1	-5.4	-21.0	2.9	21.2	-16.2	-0.5	1.5	...
Bulgaria	-8.6	-5.3	-3.1	-2.8	12.6	7.3	2.1	-3.4	-4.4	-1.9	93
Turkmenistan	-0.5	9.4	-12.3	-5.9	-22.9	-6.3	19.6	-29.8	...	-5.5	54
Tajikistan	-1.5	-1.7	-22.5	8.2	-22.5	-3.2	-23.1	-16.6	...	-14.3	39

REGIONAL AVERAGES	1990	1991	1992	1993	1994	1995	1996	1997	1998	1996-98[1] average	1998/1989[2] (%)
	Labor Productivity in Industry (% change)										
CEE & Eurasia	-2.5	-4.9	-7.9	-3.0	-6.5	3.2	4.1	7.6	3.0	4.9	92
Northern Tier CEE	-12.5	-5.2	6.4	7.7	10.4	7.4	7.1	9.2	5.9	7.4	139
Southern Tier CEE	-16.3	-14.6	-7.3	4.7	7.9	12.2	5.6	3.7	2.2	3.8	94
Eurasia	1.7	-3.5	-11.5	-6.8	-12.9	1.0	3.2	7.7	2.3	4.4	81

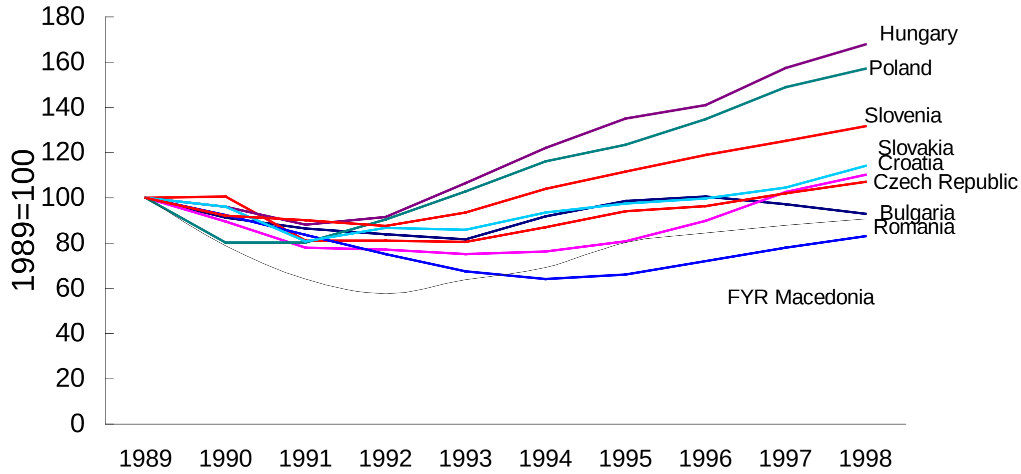
[1]1995-1997 for Tajikistan and Turkmenistan. [2]1997/1989 ratio for Tajikistan and Turkmenistan.

EBRD, *Transition Report 1999* (November 1999).

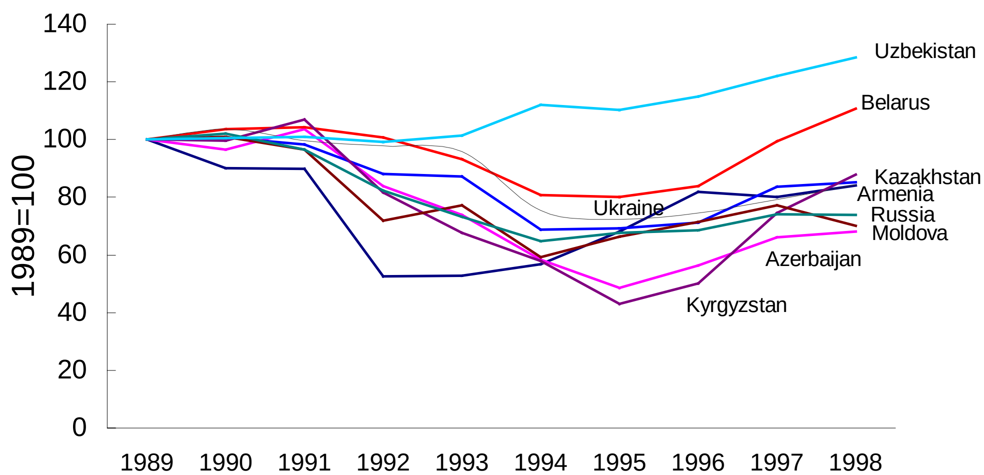
Note: Productivity is calculated as the ratio of industrial production to industrial employment.

Figure 7.

Labor Productivity in Central & Eastern Europe: 1989 to 1998



Labor Productivity in Eurasia: 1989 to 1998



EBRD, *Transition Report* (November 1999).

Table 13. Integration into the World Economy (I)

Country	Export Growth (avg annual %) 1996-1998	Export Growth 1999	Openness to Trade (% of PPP GDP) 1997	1998	Current Account Balance (% of GDP) 1995-1997	1998	1999	Institutional Integration 1999
Hungary	18	10	55	42	-3.8	-4.9	-4.4	(1) (2) (3) (4) (5)
Czech Republic	7	3	48	44	-5.4	-1.9	-1.0	(1) (2) (3) (4) (5)
Poland	10	-1	27	26	0.2	-4.4	-7.6	(1) (2) (3) (4) (5)
Estonia	17	-6	92	58	-8.5	-9.2	-4.1	(2) (4) (5)
Slovenia	3	-7	76	67	0.1	0.0	-2.4	(2) (4) (5)
Slovakia	8	-5	51	46	-6.3	-10.4	-4.9	(2) (4) (6)
Latvia	14	-7	45	37	-4.6	-9.5	-8.7	(2) (4) (6)
Bulgaria	-7	-9	25	23	1.7	-2.3	-5.2	(2) (4) (6)
Romania	2	1	20	15	-6.1	-7.0	-4.1	(2) (4) (6)
Lithuania	14	-14	57	40	-9.9	-12.1	-10.9	(4) (6)
FYR Macedonia	3	-8	45	...	-6.4	-9.0	-4.1	(4)
Kyrgyzstan	12	12	12	12	-15.8	-16.7	-12.0	(2)
Croatia	0	-7	54	44	-7.7	-7.1	-6.5	
Ukraine	-1	-5	39	19	-2.9	-3.1	-1.1	
Belarus	15	-16	32	24	-4.0	-6.6	-2.8	
Turkmenistan	-31	79	32	15	-8.4	-45.8	-16.2	
Moldova	-3	-27	32	20	-9.6	-17.6	-20.3	
Tajikistan	-6	11	22	25	-10.3	-10.8	-2.9	
Russia	-2	-2	21	14	1.9	0.9	10.8	
Kazakhstan	5	1	19	18	-3.6	-5.6	-1.8	
Azerbaijan	1	25	13	14	-20.8	-33.1	-23.6	
Uzbekistan	-5	-12	13	15	-4.9	-4.7	-5.5	
Armenia	-6	5	12	13	-30.8	-26.7	-25.8	
Georgia	10	5	11	8	-7.0	-7.5	-6.4	
Albania	3	16	11	11	-9.5	-6.3	-8.6	
Bosnia-Herzegovina	78	15	...	...	-40.7	-32.0	-21.0	
Yugoslavia	37	...	...	...	...	...	...	
CEE & Eurasia	2	-1	27	20	-2.8	-4.4	0.4	
Northern Tier CEE	11	0	40	35	-2.4	-5.1	-6.0	
Southern Tier CEE	8	0	25	20	-7.9	-6.1	-5.0	
Eurasia	-1	-1	24	16	-2.1	-3.9	2.8	
European Union	6.7	5.2	51	54		1.0	1.0	
Advanced Economies	6.6	3.2	39	38		1.6	1.4	

Benchmarks	(a) 3 year average export growth > 5%
	(b) 3 year average current account balance no worse than -5%

Note: Openness to trade is the sum of merchandise exports plus imports expressed as a percentage of purchasing power parity GDP. Institutional integration refers to membership or participation in (1) OECD, (2) WTO, (3) NATO, (4) Europe Agreements with EU, (5) invited to participate in July 1997 in negotiations toward EU membership, (6) invited to participate in October 1999 in negotiations toward EU membership. Current account figures for Bosnia-Herzegovina exclude official transfers.
Source: EBRD, *Transition Report 1999* (November 1999); IMF, *World Economic Outlook* (April 2000); and World Bank, *World Development Indicators 2000* (April 2000); ECE, *Economic Survey of Europe* (1999, No. 2); and most recent IMF and EIU country reports.

Table 14. Integration into the World Economy (II)

Country	Foreign Direct Investment (net inflows per capita)			External Debt (% of exports)			
				Debt		Debt Service	Debt Service
	1989-1999	1998	1999	1995	1998	1998	1999
Hungary	1,779	143	152	247	129	30	…
Czech Republic	1,307	242	340	77	89	15	…
Poland	557	171	168	197	149	12	14
Estonia	1,201	408	248	17	108	8	8
Slovenia	703	78	107	36	55	13	8
Slovakia	419	94	93	66	112	15	15
Latvia	706	93	64	105	93	14	…
Bulgaria	244	49	85	191	235	19	16
Romania	260	91	60	87	116	24	30
Lithuania	527	257	112	31	94	18	22
Kyrgyzstan	86	11	14	143	203	9	…
Croatia	604	183	160	72	178	13	15
FYR Macedonia	136	87	15	88	106	10	…
Ukraine	64	14	12	57	85	15	14
Belarus	63	14	18	56	36	2	…
Turkmenistan	180	25	23	26	249	…	…
Moldova	114	20	38	91	207	28	…
Tajikistan	27	6	5	105	207	13	…
Russia	85	8	24	148	202	17	17
Kazakhstan	420	67	48	96	136	…	…
Azerbaijan	507	129	99	62	101	8	14
Uzbekistan	32	7	9	51	112	14	…
Armenia	133	68	44	137	363	12	…
Georgia	117	44	19	338	353	17	22
Albania	145	13	13	333	424	6	5
Bosnia-Herzegovina	…	29	17	2,211	352	17	8
Yugoslavia	…	…	…	…	…	…	…
CEE & Eurasia	260	54	57	124	160	17	…
Northern Tier CEE	840	175	178	159	127	15	…
Southern Tier CEE	260	82	66	127	172	19	…
Eurasia	109	18	24	114	166	17	…
Developing Countries				168	173	27	28
Benchmarks	debt service less than 20%						

Note: Foreign direct investment figures for 1989-1999 are cumulative. Data for Bosnia-Herzegovina exclude capital transfers for reconstruction. Debt service as a % of current account revenues. The IMF estimates the 1999 debt service for the transition region to be 18% of exports.

Source: EBRD, *Transition Report* (November 1999); IMF, *World Economic Outlook* (April 2000); and the most recent IMF and EIU country reports.

Table 15. Integration into the World Economy (III)

Country	Present value of External Debt in 1996		Present value of External Debt in 1998		
	% of GNP	% of Exports	% of GNP	% of Exports	Debt Category
Hungary	41	158	63	107	Moderately
Czech Republic	62	70	45	95	Less
Poland	31	102	28	71	Less
Estonia	9	14	13	15	Less
Slovenia	21	36	…	…	…
Slovakia	41	66	45	68	Less
Latvia	9	20	11	22	Less
Bulgaria	89	151	79	160	Severely
Romania	23	89	26	98	Less
Lithuania	16	35	17	35	Less
FYR Macedonia	74	106	87	140	Severely
Kyrgyzstan	37	130	50	135	Moderately
Croatia	24	56	31	71	Less
Ukraine	18	48	29	70	Less
Belarus	4	21	5	13	Less
Turkmenistan	18	39	83	289	Severely
Moldova	39	92	58	106	Moderately
Tajikistan	24	69	40	143	Moderately
Russia	25	97	62	186	Moderately
Kazakhstan	14	48	25	79	Less
Azerbaijan	10	45	25	52	Less
Uzbekistan	9	56	15	93	Less
Armenia	27	114	30	120	Less
Georgia	26	209	25	141	Moderately
Albania	32	101	20	74	Less
Bosnia-Herzegovina	53	408	…	…	…
Yugoslavia	…	…	…	…	…
CEE & Eurasia	26	87	43	126	
Northern Tier CEE	35	93	35	84	
Southern Tier CEE	41	129	40	108	
Eurasia	21	79	45	139	

Benchmark	below the "moderately indebted" threshold (i.e., debt < 132% of exports)

Note: The debt classification is per the World Bank. Countries with a present value of debt service greater than 220% of exports or 80% of GNP were considered severely indebted; countries that were not severely indebted but whose present value of debt service exceeded 132% of exports or 48% of GNP were classified as moderately indebted; countries that did not fall into the above two groups were classified as less indebted. The present value of debt is the sum of short-term external debt plus the discounted sum of total debt service payments due on public, publicly guaranteed, and private nonguaranteed long-term external debt over the life of existing loans.

Source: World Bank, World Development Indicators 2000 (April 2000).

2. Social Conditions

Ultimately, the sustainability of the transition hinges on the well being of the individual. Humanitarian considerations are important. However, equally if not more compelling are the links between living standards, popular expectations, and the level of public support for economic and political reforms--reforms which have coincided with, if not contributed to, both a dramatic initial drop in overall income and significant increases in income inequalities and poverty in most cases. The links between macroeconomic performance and social conditions may grow in importance as well, particularly in a setting of sustained deterioration of social conditions. Productivity is eroded or stifled in such a setting.

Tables 16 through *22* and *Figures 8* through *11* highlight social conditions. **Unemployment** is a real concern, and for many transition countries, it remains a growing concern. In fact, unemployment rates reached double-digit levels in 1998 on average for the whole of the transition region for the first time since the transition began (*Table 16*).[30] Unemployment rates increased in all three subregions in 1998. For the Northern Tier CEE countries, this reverses a trend of steadily falling rates since 1993. Furthermore, of the nine CEE countries for which 1999 unemployment data are available, only in Slovenia have unemployment rates fallen since 1998.

While significant subregional differences in labor market adjustments remain, *Figure 8* does show a broad trend towards convergence in open unemployment rates between the CEE countries and Eurasia. Much of this is due to rising official unemployment rates in Eurasia, particularly in Russia (to 12.4 percent in 1998), Georgia (14.5 percent in 1998), and Azerbaijan (19.3 percent in 1997).

Nevertheless, the most recent data show unemployment rates to be less than five percent for the rest of Eurasia. Lower unemployment rates in much of Eurasia may reflect a combination of phenomena. One may be simply poorer data. Another aspect is probably due to a continuing differentiation in how labor markets are adjusting between CEE and much of Eurasia. In particular, underemployment (in the form of fewer work hours, involuntary leave and wage arrears) in Eurasia may to some extent continue to exist in lieu of greater open unemployment. Similarly, the degree of open unemployment currently experienced in CEE and some of Eurasia may be an indication of what is to come in the rest of Eurasia. That is, if these reform laggards succeed in moving forward in the transition reforms, unemployment will likely continue to rise.

Unemployment rates are highest in the Southern Tier, and particularly in those countries that were part of the former communist Yugoslavia: forty percent in Bosnia-Herzegovina; thirty-five percent in Macedonia; twenty-seven percent in Yugoslavia (Serbia and Montenegro); and twenty percent in Croatia.[31]

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[30] Part of the reason the regional average increased in 1998 was the inclusion for the first time of very high unemployment rates in Bosnia-Herzegovina and Yugoslavia.
[31] Slovenia's low unemployment rate is an exception to the unemployment trends among the former republics of communist Yugoslavia.

The 1998 Northern Tier unemployment rate average of 9.8 percent was slightly higher than the EU average of 9.6 percent. Three Northern Tier countries have managed to keep unemployment rates well below the EU and Northern Tier averages over the past several years: the Czech Republic (5.4 percent from 1996-1998); Lithuania (6.4 percent in 1996-1998); and Slovenia (7.5 percent in 1996-1998). However, unemployment continues to climb in the Czech Republic (to 8.5 percent in 1999).

A critical consideration is the extent to which these unemployment figures represent the same people from year to year. In other words, how long are people typically unemployed? With official safety nets disappearing, we know that unemployment is a crucial determinant of poverty. Monitoring **long-term unemployment** is hence important, and *Table 17* addresses this aspect in part for many of the CEE countries. At this point, we can only sketch a rough picture; these data need to be updated and extended to the Eurasian countries. Forty-four percent of the unemployed in 1996 in the eight CEE countries for which data are available were unemployed for more than one year. This represents a large increase from 1992 when one in four of the unemployed was long-term unemployed, though a slight decrease from 1995. It is interesting to note that the proportion of long-term unemployment in some countries of Western Europe was also greater in 1996 than in the early 1990s. This trend, in other words, has not been solely a transition phenomenon. Long-term unemployment may be particularly troublesome for Macedonia and Albania, though more recent data are needed to reassess these earlier trends.[32]

Tables 18 and *19* shed light on living standards through indicators of income. From *Table 18*, we see that **average income** in the transition economies remains significantly below that in the advanced economies. In purchasing power parity (PPP) terms, average income in the transition region is slightly more than one-fourth the EU average. Furthermore, average income varies widely among the transition countries. Per capita income in four Northern Tier countries is close to $10,000 or more: Slovenia ($14,950); the Czech Republic ($12,140); Hungary ($10,230); and Slovakia ($9,720). In contrast, a handful of Eurasia countries have average income levels closer to $1,000 to $2,000: Tajikistan ($1,080); Moldova ($1,900); Uzbekistan ($2,120); Armenia ($2,150); Kyrgyzstan ($2,300); and Azerbaijan ($2,330). In general, subregional average per capita income is roughly comparable in the Southern Tier and Eurasian countries, and slightly more than one-half the levels on average compared to the Northern Tier countries.

What may be more important for our purposes is how the income levels have changed during the transition, and how it has been distributed within countries. Other things equal, the greater the income disparities and collapse in incomes, the more pronounced are the hardships and the greater is the likelihood of "reform fatigue."

[32] At least in the case of Macedonia, entrance into and out of the labor market is very restricted, and the majority of the unemployed consists of new entrants to the labor force; relatively young Macedonians who have not yet landed a job.

In this regard, it is significant to note (as shown in *Table 18*) that only a handful of countries have regained pre-transition (official, inflation-adjusted) income (Poland, Slovenia, and Slovakia), or have come close to regaining it (the Czech Republic and Hungary). Of the Northern Tier CEE countries, Latvia and Lithuania still have incomes considerably below pre-transition levels. Average income in Latvia in 1999 was only fifty-nine percent of 1989 income, a level more characteristic of the Eurasian countries than Northern Tier CEE.

The 1999 average income in the Southern Tier CEE was roughly only three-fourths of 1989 income. Eurasia lags even more: 1999 income in the Eurasian countries on average was fifty-six percent the income level of 1989. The range among the Eurasian countries is particularly large: current official income in Uzbekistan is ninety-two percent of 1989 income; in Moldova and Georgia, it is only a third.

It is widely recognized that unofficial economic activity is very significant in virtually all the transition countries, and that unofficial income has likely greatly offset official income losses. Measuring the informal economy is by definition very difficult, though there are a variety of ways to get at rough orders of magnitude. Some stem from analyzing household survey data (which is done in some detail in *Appendix II*).

An increasingly common "back-of-the-envelope" technique to measure unofficial economic activity is to compare officially measured economic activity with electricity consumption. From this approach, one finds that many of those countries that have experienced a particularly large decrease in official economic activity have also seen relatively large increases in unofficial economic activity. Drawing from estimates by Johnson, Kaufmann, and Shleifer (1997), for example, one finds that unofficial economic activity in Eurasia is almost twice as large relative to official GDP as it is in CEE. In Eurasia, it was almost forty percent of official GDP on average in 1995 (and still rising); in the CEE, it was closer to twenty percent (and falling).[33]

We can fill in the picture further with **income distribution** data. In general, while virtually all the transition economies had relatively equal income distributions prior to communism's collapse, virtually all have since experienced very significant increases in income inequality. For the Northern Tier CEE countries, where the increase (of about thirty percent from 1989 to 1997) has not been as great as in the other transition subregions, income inequality is now roughly comparable to that found in the advanced industrialized economies. To some extent, then, the increase in inequality in these advanced transition economies is arguably an expected byproduct of developing a market-oriented economy. Nevertheless, the speed of this "adjustment" even in the

[33] S. Johnson, D. Kaufmann, and A. Shleifer, "Politics and Entrepreneurship in Transition Economies," *Working Paper Series*, No. 57, The William Davidson Institute, University of Michigan (1997). A recent study by F. Schneider and D. Enste compares the work by Johnson et. al. with that of others, and synthesizes the literature: "Shadow Economies: Size, Causes, and Consequences," *The Journal of Economic Literature*, 38 (March 2000), pp. 77-114. *Appendix II* of *Monitoring Country Progress* (January 1998) also summarizes the Johnson study.

Northern Tier may be unprecedented. To compare, income inequality increased by only two percent in the EU from 1986 to 1993.

In the Southern Tier CEE and Eurasia, income inequality increased by more than fifty percent from 1989 to 1997. Income inequality in some of these countries now compares to that found in the most unequal economies worldwide, that is, those in Latin America and in Sub-Saharan Africa. This includes Georgia, Russia, Azerbaijan, Kyrgyzstan, Romania, and Ukraine.

Poverty has increased substantially in the transition region. *Table 19* shows the increase in income estimates of poverty through 1995. Unfortunately, more recent comparable cross-country updates do not exist. However, *Figures 9* and *10*, which draw from the 1996-1998 household survey data of *Appendix II*, provide some basis to judge the credibility of the income poverty estimates. Further elaboration is provided in the appendix.

According to *Table 19*, four out of every ten persons in the transition region were poor (that is, earned less than four dollars a day) during the 1993-1995 period. However, this average masks very wide variation, by country and by groups within countries. Poverty remained negligible in Slovenia, the Czech Republic, and Slovakia. In contrast, at least seven transition economies, all Eurasia, had poverty rates equal to or greater than fifty percent: Tajikistan, Kyrgyzstan, Moldova, Ukraine, Kazakhstan, Turkmenistan, and Azerbaijan. Poverty in Russia (forty-four percent in 1995) may not be much lower. In fact, on average, one of every two persons in Eurasia was poor in 1993-1995. In the Northern Tier CEE countries, it is closer to one of every ten persons, and in the Southern Tier, one out of every four.

Table 19 also reveals that poverty places a disproportionate burden on certain segments of society. The poverty estimates for children and the elderly cannot be directly compared with the countrywide estimates since different methods are used. However, a comparison between poverty among children and the elderly and how those rates have changed since 1989 is very revealing.

In general, the data suggest that poverty has been much greater among children than it has been among the elderly. This is the case in six of the eight countries for which data exist for 1992-1995. By this measure, poverty among Russian children increased from forty percent to over sixty percent since roughly 1990; from two percent to over forty percent in Bulgaria; from nine percent to thirty-five percent in Romania; and from eight percent to twenty percent in Poland.

Poverty rates for the elderly on average in this limited sample are one-half those for children. Among the Northern Tier countries, poverty among the elderly is low and may actually have decreased: from four percent in 1989-1992 to three percent in 1992-1995. It may be that the elderly in some of these countries remain politically strong enough to be able to favorably influence pension rates and eligibility.

Some observers have contended that these poverty data overestimate the hardships in the lagging transition countries. Throughout Eurasia, in particular, in the countryside as well as in urban areas, people by and large continue to get by. Some of this can be explained by unofficial sources of income and subsistence activities that are not captured in the "official" poverty rates cited above. On the other hand, it has also been observed that these income measures (of *Table 19*) underestimate the scope of poverty in some of the leading transition countries; and that the relatively favorable macroeconomic performances in the Northern Tier countries have not translated into negligible poverty rates.

Figures 9 and *10* shed some light on both types of observations. *Figure 9* maps the poverty rates (of *Table 19*) with household assessments of "coping strategies" in fifteen countries. Data on the latter are from three household surveys conducted during 1996-1998 by the Centre for the Study of Public Policy. As noted in *Appendix II*, those households which are engaged in "unsustainable" coping strategies (that is, drawing on savings and/or borrowing significantly) are headed toward poverty if they are not already in poverty. Generally, however, the proportion in poverty should be some subset of these households (that are not coping sustainably), and certainly no greater.

Yet, as shown in *Figure 9*, in a handful of countries, the proportion of those estimated to be in poverty exceeds the proportion of those with unsustainable strategies. This includes poverty estimates in two Baltic countries (Estonia and, to a lesser extent, Lithuania), as well as in Ukraine and Russia.

On the other hand, *Figure 9* may suggest that income poverty estimates in some of the Northern Tier CEE countries are understating the hardships that are being incurred. In the Czech Republic, Hungary, Slovenia, and Slovakia, income poverty (as of 1995) was estimated to be negligible, from one to two percent of the population. Yet, the percent of the population in these countries which is not coping sustainably ranges from nineteen percent in the Czech Republic to twenty-nine percent in Slovakia.

A similar approach is applied in *Figure 10* in which poverty rates are compared to 1998 household self-assessments of the frequency of being deprived of food during the month prior to being queried in ten transition countries. The percentage of households having to often do without food might be a reasonable proxy for the poverty rate. In this light, the low income poverty estimates (of *Table 19*) for Slovenia, the Czech Republic, Slovakia and Hungary square quite nicely with the low percentage of households (from one to five percent) in these countries having to often do without food. The two data sets do not mesh as conveniently for the other countries. In particular, the income estimates of poverty exceed the proportion of those households often having to do without food. This gap is particularly large in the case of Russia, Ukraine, and Romania. In Russia, for example, forty-four percent of the population was estimated to be below the income poverty line in 1995, yet only nineteen percent in 1998 of those sampled were often being deprived of food. Again, on this basis of comparison, income poverty estimates appear to be overestimating the hardship in Russia and elsewhere.

Table 20 highlights trends in infant and child mortality rates. **Infant mortality rates** have fallen for all the transition countries from 1989 to 1998 except three: Latvia, Ukraine, and Bulgaria. The Northern Tier trends (Latvia notwithstanding) have been particularly impressive. Infant mortality rates were the lowest in the Northern Tier CEE countries at the outset of the transition and have fallen the most there during the transition, by almost one half. Northern Tier infant mortality rates in 1998 (nine deaths per 1,000 live births) are now actually below the OECD average (10 deaths) and are approaching the EU average (5 deaths). The average rates in Eurasia and the Southern Tier CEE countries are both seventeen deaths per 1,000 live births; i.e., almost two times the Northern Tier rates. By these World Bank estimates, infant mortality rates are highest in the Central Asian Republics (twenty-five deaths per 1,000 live births on average), Albania (twenty-five deaths) and Romania (twenty-one deaths).[34]

Trends in **child mortality rates** (of children under five years of age) may be a better gauge of living standards than infant mortality trends. Overall, while child mortality rates have fallen in most transition countries since 1990, the decline has not been as large as that of infant mortality rates. This is primarily because child mortality rates in Eurasia on average have declined only marginally, from thirty-three deaths in 1990 to thirty-two deaths in 1998. Current child mortality rates in Eurasia on average are slightly below those found in Latin America and the Caribbean (where they are thirty-nine deaths per 1,000). Far and away the largest increase in child mortality rates during the transition has occurred in Belarus, increasing by over forty percent from 1990 to 1998, though remaining below the Eurasian average.

As with infant mortality rates, the most significant decline in child mortality has occurred in the Northern Tier countries, by one-third from 1990-1998. At eleven deaths per 1,000 in 1998, this rate nevertheless remains almost twice that found in the industrialized countries. Slovenia and the Czech Republic are the only transition countries that have child and infant mortality rates comparable to the EU.

Life expectancy trends have diverged widely between the three transition subregions with the collapse of communism (*Table 21*). This divergence contrasts with life expectancy patterns in the decade prior to communism's demise. In particular, with the exception of Armenia, life expectancy remained steady or increased throughout the communist world in the 1980s.

During the early transition years, life expectancy fell fairly uniformly in virtually all the countries, even in the Northern Tier CEE countries. However, this fall was particularly short-lived for persons in the Northern Tier. By 1996, life expectancy in the Northern Tier countries on average was higher, for both males and females, than it had been at the outset of the transition. It had risen slightly for females in the Southern Tier from 1989 to 1996, and had declined by one year for Southern Tier males. The greatest drop in life

[34] UNICEF estimates show infant mortality rates to be higher than World Bank measures in countries of the former Soviet Union and in the Southern Tier CEE. The largest discrepancies are found in estimates of the Central Asian Republics; 1998 infant mortality rates on average in these five countries is roughly fifty deaths per 1,000 live births according to UNICEF, and twenty-five deaths by World Bank estimates.

expectancy has occurred in Eurasia, particularly among males. However, at least among Russian males, this seems to have bottomed out.

By 1998, life expectancy was close to seventy-three years in the Northern Tier, an increase of four years since 1980 and almost two years since 1989. By comparison, life expectancy in the EU is seventy-nine years on average. Life expectancy in Slovenia and the Czech Republic (both at seventy-five years) come closest to the EU standard. Life expectancy is closer to sixty-seven years in Eurasia, an insignificant drop since 1980, but a fall of about two and one-half years since 1991-1992. The biggest drops in Eurasia have occurred in Kazakhstan, Ukraine, and Belarus.

Finally, life expectancy in the Southern Tier countries falls somewhere between that of the other two subregions, in 1998, almost seventy-one years on average. This is an increase from life expectancy in 1980, but a decrease of about one year since communism's collapse.

As with physical capital, human capital is important for its direct effect on economic sustainability (*Table 22)*. It too, however, can provide indications of trends in living standards. **Secondary school enrollment** has increased from 1990 to 1997 in most of the Northern Tier CEE countries, while decreasing in most other transition countries. The greatest drops have occurred in Albania (by over one half), Tajikistan, Kyrgyzstan, Georgia, Romania, Azerbaijan, and Kazakhstan. Secondary school enrollment in the Northern Tier CEE (at almost ninety-seven percent) is below the EU average (of one hundred and eight percent). While continuing to drop on average, it is still high in Eurasia (eighty-four percent). At seventy-two percent, it is lowest in the Southern Tier CEE countries. In 1997, only thirty-eight percent of school age children in Albania were enrolled in secondary schools, far and away the lowest enrollment of the transition countries.

Table 22 also includes UNDP's **Human Development Index** (HDI) scores and rankings for the transition countries. *Figure 11* compares these measures of human development with reform progress. The HDI is based on three indicators: longevity, as measured by life expectancy; educational attainment, as measured by a combination of adult literacy (two-thirds weight), and combined primary, secondary and tertiary enrollment ratios (one-third weight); and standard of living, as measured by real GDP per capita (PPP$). The HDI ranges from zero to one; the higher is the value, presumably the greater is the human development. The UNDP classifies 174 countries into three categories in the *Human Development Report 1999*: high; medium; and low human development. It is based on 1997 data. Due to significant changes in the methodology of constructing the most recent HDI, strict comparisons with scores from previous years should not be made.

Human development is considered high in four transition countries (Slovenia, Czech Republic, Slovakia, and Poland), and medium in the rest. Slovenia ranks the highest, 33 out of 174. By this measure, the Northern Tier countries on average have a level of human development comparable to that found in Costa Rica.

The Eurasian countries have the lowest HDI rating of the three transition subregions on average, though the differences in scores among the Eurasian countries are large. Among them, Belarus has the highest human development, less than Croatia, but greater than Lithuania, and ranking 60^{th} worldwide. Tajikistan ranks the lowest of all the transition countries, 108^{th} worldwide, and comparable in human development to that in El Salvador and Algeria.

Finally, *Figure 11* provides a picture as to how closely HDI scores map with progress in economic and democratic reforms.   There is strong evidence that progress in reforms leads to better macroeconomic performance. *Figure 11* provides evidence that reform progress and human development are also linked. In general, the reform leaders are countries with the highest human development, and the reform laggards are those with the lowest human development.

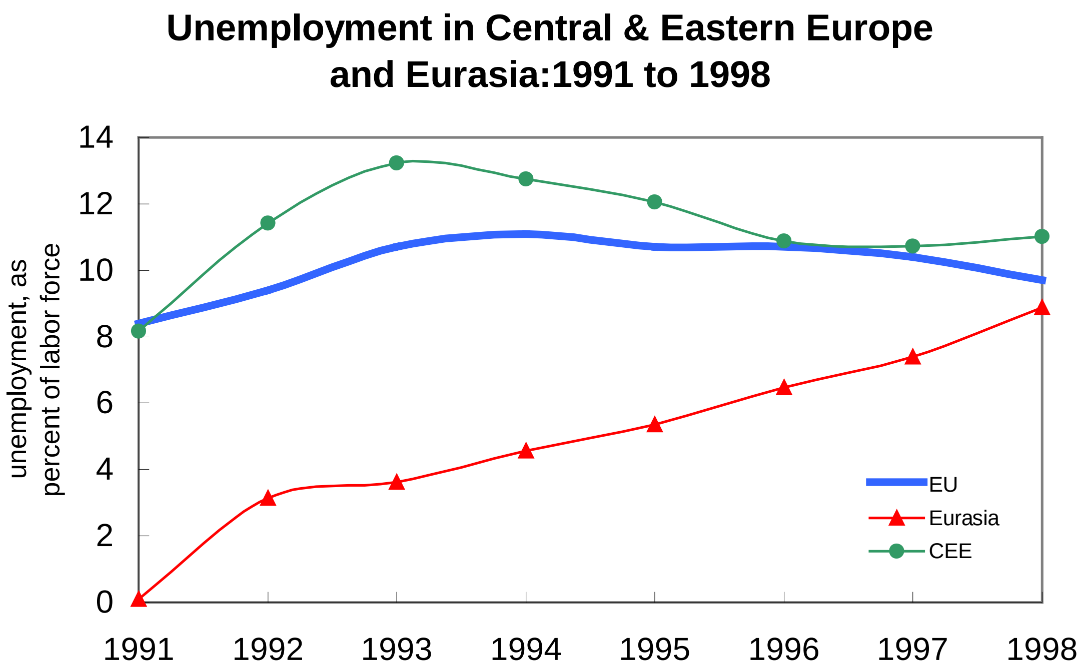
Human development scores are grouped into three categories (separate from the UNDP's grouping): high; medium, and low. The five countries where human development is high are all out front in reforms. All the countries with low human development are in the bottom half of the reform spectrum. However, countries characterized by middle human development vary widely by reform progress, and range from Belarus at the lower end of the reform spectrum, to the three Baltic countries, which are all among the reform leaders.

Table 16. Unemployment Rate

	1991	1992	1993	1994	1995	1996	1997	1998	1999	1996-1998* (average)
CEE										
Czech Republic	4.1	2.6	3.5	3.2	2.9	3.5	5.2	7.5	8.5	5.4
Lithuania	0.3	1.3	4.4	3.8	6.2	7.0	5.9	6.4	...	6.4
Slovenia	7.3	8.3	9.1	9.0	7.4	7.3	7.4	7.9	7.4	7.5
Romania	3.0	8.2	10.4	10.9	9.5	6.6	8.9	10.3	11.0	8.6
Estonia	...	...	6.5	7.6	9.7	10.0	9.7	9.6	11.0	9.8
Hungary	7.4	12.3	12.1	10.4	10.4	10.5	10.4	9.1	9.6	10.0
Poland	11.8	13.6	16.4	16.0	14.9	13.2	10.5	10.4	13.0	11.4
Slovakia	...	...	12.2	13.7	13.1	11.1	11.6	11.9	...	11.5
Bulgaria	11.1	15.3	16.4	12.8	11.1	12.5	13.7	12.2	16.0	12.8
Albania	8.9	27.9	29.0	19.6	16.9	12.4	14.9	17.7	...	15.0
Latvia	0.6	3.9	8.7	16.7	18.1	19.4	14.8	13.8	...	16.0
Croatia	13.2	13.2	14.8	14.5	14.5	16.4	17.5	17.2	20.1	17.0
FYR Macedonia	19.2	27.8	28.3	31.4	37.7	31.9	36.0	34.5	...	34.1
Bosnia-Herzegovina	...	...	...	...	...	...	...	38.0	40.0	...
Yugoslavia	...	...	...	...	...	...	...	27.0	...	...
Eurasia										
Uzbekistan	0.0	0.1	0.3	0.4	0.4	0.4	0.4	0.6	...	0.5
Moldova	...	0.1	0.7	1.1	1.4	1.8	1.6	...	...	1.6
Tajikistan	...	0.3	0.8	1.2	1.3	1.6	1.8	3.1	...	2.2
Ukraine	0.0	0.3	0.3	0.3	0.5	1.3	2.3	3.7	...	2.4
Belarus	0.1	0.5	1.4	2.1	2.7	3.9	2.8	2.3	...	3.0
Kyrgyzstan	0.0	0.1	0.2	0.7	3.0	4.5	3.2	...	...	3.6
Kazakhstan	0.0	0.5	0.6	0.8	1.7	3.6	4.1	3.7	...	3.8
Armenia	4.0	1.8	5.3	6.7	6.7	9.2	10.7	9.3	...	9.7
Georgia	0.2	2.3	6.6	3.6	2.6	12.0	5.1	14.5	...	10.5
Russia	0.0	4.8	5.3	7.1	8.3	9.2	10.9	12.4	...	10.8
Azerbaijan	...	15.4	16.0	15.2	17.0	19.4	19.3	...	...	18.6
Turkmenistan	2.0	...	...	...	3.0	...	...	...	...	...
CEE & Eurasia	2.4	5.4	6.4	6.9	7.3	7.8	8.4	10.0	...	8.5
Northern Tier CEE	8.8	10.6	12.5	12.4	11.9	11.0	9.6	9.8	...	10.1
Southern Tier CEE	7.1	12.8	14.6	13.4	12.4	10.7	12.7	16.3	...	12.2
Eurasia	0.1	3.1	3.6	4.6	5.4	6.5	7.4	8.9	...	7.5
Advanced Economies	6.5	7.2	7.6	7.4	7.0	7.1	6.8	6.7	6.4	6.9
USA	6.9	7.5	6.9	6.1	5.6	5.4	4.9	4.5	4.2	4.9
EU	8.4	9.4	10.7	11.1	10.7	10.7	10.4	9.7	8.9	10.3
Benchmarks										< 10.0

*1995-7 for Azerbaijan, Kyrgyzstan, and Moldova. Regional averages for Southern Tier CEE and CEE & Eurasia in 1998 include Bosnia-Herzegovina and Yugoslavia; the 1998 average unemployment excluding Bosnia-Herzegovina and Yugoslavia are 13.3 for Southern Tier CEE and 9.3 for CEE & Eurasia. EBRD, *Transition Report* (November 1999); IMF, *World Economic Outlook* (April 2000); ECE, *Economic Survey of Europe* (1999, No. 2); and most recent IMF and EIU country reports.

Figure 8.



Note: The increase in the CEE average in 1998 is due in part to the inclusion for the first time of high unemployment rates in Bosnia-Herzegovina and Yugoslavia.
Source: EBRD (November 1999); IMF (April 2000).

Table 17. Long-Term Unemployment in CEE

Country	% of Labor Force 1992	1993	1994	1995	1996	% of Total Unemployed 1992	1993	1994	1995	1996	Percent Change: 1992 to 1996
Albania	...	18.9	...	...	...	...	65	...	...	...	...
Bulgaria	...	8.7	7.6	7.3	8.0	...	53	59	66	64	21
Croatia	7.7	8.6	8.0	...	...	58	58	55	...	...	-5
Czech Republic	0.4	0.7	0.7	0.9	1.2	14	19	22	31	33	136
Estonia	...	...	...	...	...	...	...	...	...	...	...
Hungary	2.2	4.0	4.3	5.0	5.5	18	33	41	48	52	189
Latvia	...	...	...	...	...	...	...	...	...	...	...
Lithuania	...	...	...	...	...	...	...	...	...	...	...
FYR Macedonia	23.9	24.6	27.6	30.9	25.8	86	87	88	82	81	-6
Poland	3.3	5.9	6.1	6.3	5.0	24	36	38	42	38	58
Romania	1.7	...	4.9	4.5	2.8	21	...	45	47	42	100
Slovakia	...	4.0	5.9	7.1	6.2	...	33	43	54	56	70
Slovenia	5.3	7.9	8.2	7.4	7.4	46	55	57	53	53	15
Northern Tier CEE	2.7	4.7	5.0	5.3	4.7	22	33	37	43	41	87
Southern Tier CEE	4.2	12.2	7.1	6.8	5.5	31	60	52	54	50	59
CEE Overall	3.2	6.3	5.8	5.8	4.9	25	39	42	46	44	76
France	3.7	3.9	4.7	5.3	4.7	36	34	38	40	38	6
Germany	2.5	3.6	4.2	4.5	...	33	36	38	40	...	21
Spain	8.6	11.4	13.6	13.1	...	47	50	56	57	...	21
Sweden	0.4	0.9	1.4	1.2	1.4	8	11	17	16	17	113
UK	...	...	...	...	2.9	30	38	40	38	36	20
Benchmark	Long-term unemployment less than 8% of the labor force										

Note: The long-term unemployed are those who are unemployed for more than one year. Percent change figures cover the period for which data are available.
Source: World Bank, *World Development Indicators 1998* (March 1998); C. Allison and D. Ringold, *Labor Markets in Transition in Central and Eastern Europe: 1989-1995;* World Bank, Social Challenges of Transition Series (December 1996); and Bureau of the Census, *Populations at Risk in CEE: Labor Markets*, No. 2, prepared for USAID/ENI/PCS (February 1995).

Table 18. Income and Its Distribution

	1999 Average Income		Distribution of Income				1999/1989
	US$	PPP$	89/90	92/93	96/97	89 - 97 % change	GDP (%)
Poland	4,070	7,850	21	26	30	35	122
Slovenia	10,150	14,950	22	28	31	34	108
Slovakia	3,740	9,720	20	…	…	…	101
Hungary	4,700	10,230	29	32	35	19	99
Czech Republic	5,120	12,140	20	26	26	26	95
Albania	880	3,090	…	…	…	…	93
Uzbekistan	990	2,120	…	…	…	…	92
Belarus	2,250	6,500	23	40	…	54	79
Croatia	4,530	6,570	…	…	…	…	76
Estonia	3,320	7,460	…	…	…	…	75
Romania	1,310	5,350	16	23	42	90	73
FYR Macedonia	1,320	4,330	22	27	26	17	69
Bulgaria	1,250	4,800	21	25	29	31	68
Lithuania	2,460	6,070	26	37	35	30	63
Kyrgyzstan	390	2,300	26	45	43	49	62
Kazakhstan	1,360	4,390	…	…	…	…	62
Latvia	2,440	5,830	24	28	34	34	59
Russia	2,330	6,380	27	46	48	56	57
Yugoslavia	1,270	…	32	33	34	6	52
Turkmenistan	460	3,680	…	…	…	…	51
Azerbaijan	520	2,330	28	…	46	49	47
Tajikistan	380	1,080	…	…	…	…	44
Armenia	480	2,150	26	37	38	38	42
Ukraine	980	3,120	25	36	41	48	36
Georgia	1,000	3,530	30	40	50	50	34
Moldova	360	1,900	25	44	39	44	30
Bosnia-Herzegovina	990	…	…	…	…	…	…
CEE & Eurasia	2,130	5,620	25	38	42	49	67
Northern Tier CEE	4,290	8,940	22	28	31	31	107
Southern Tier CEE	1,510	5,150	21	26	37	54	74
Eurasia	1,690	4,820	26	43	46	53	56
Advanced Economies	25,510	23,200		32		3	
EU	22,441	20,031		28		2	
Benchmark	(a) current year GDP equal to 85% of 1989 GDP						

Note: Average (or per capita) income is measured in US$ converting through official exchange rates; and through purchasing power parity (PPP) figures, using 1998 World Bank figures and updating to 1999 with 1999 economic growth rates. The per capita income estimate for Yugoslavia is for 1998. Income distribution is measured by the gini coefficient, which ranges from 0 to 100; the higher the figure, the greater the inequality. The percent change in earnings distribution is for 1989-1995 for Armenia and Moldova. For the Advanced Economies and the EU, percent change in income distribution is roughly from 1986 to 1993.

EBRD, Transition Report (November 1999 and previous editions); World Bank, World Development Report 1999/2000 (August 1999); P. Gottschalk and T. Smeeding, "Cross-National Comparisons of Earnings and Income Inequality," Journal of Economic Literature 35 (June 1997), pp. 633-687' IMF, World Economic Outlook (April 2000); ECE, Economic Survey of Europe (1999, No. 2); UNICEF, TransMonee Database (1999); World Bank, World Development Indicators (April 2000).

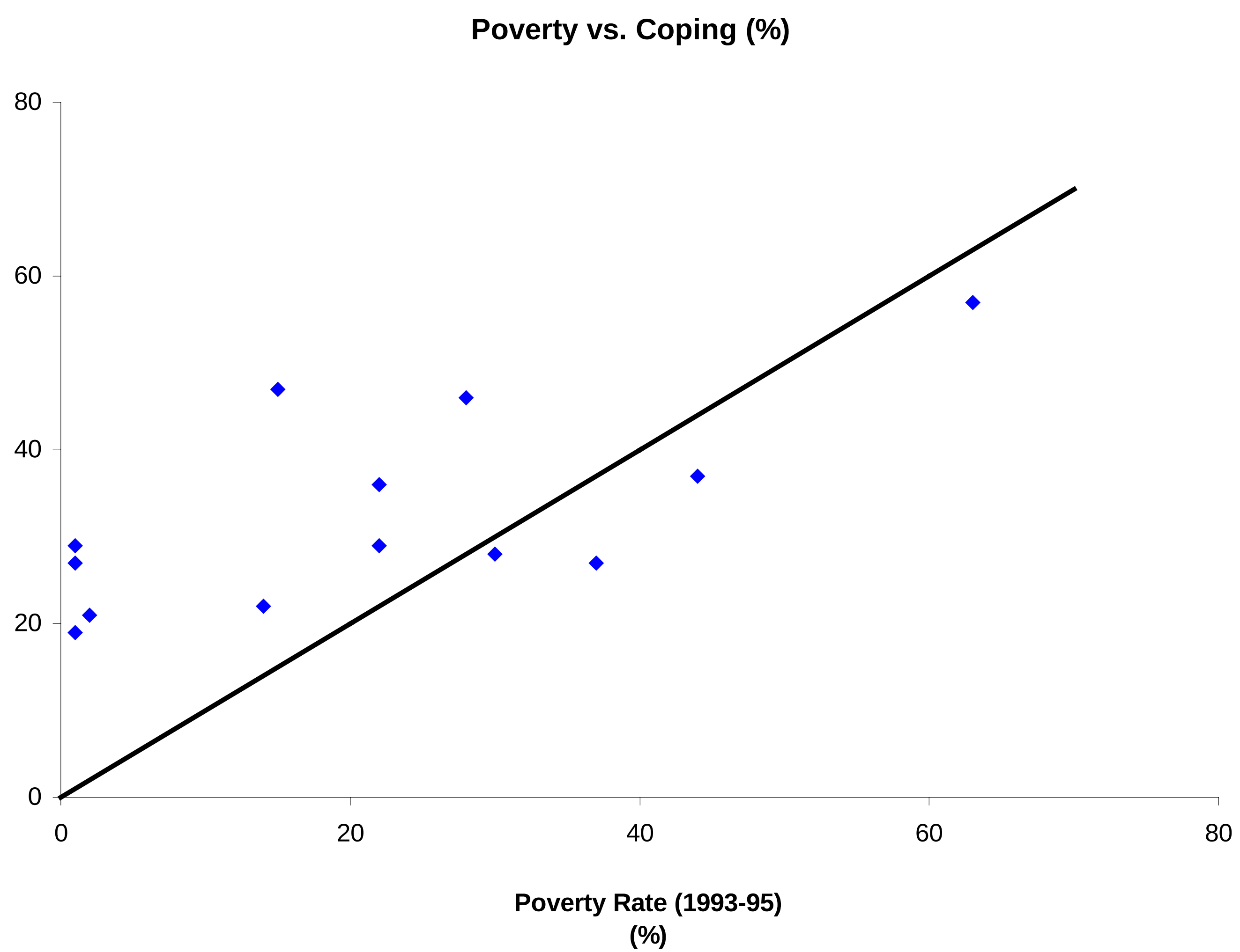
Table 19. Poverty
Percent of Population Living in Poverty

Country	Children 1989-1992	Children 1992-1995	Elderly 1989-1992	Elderly 1992-1995	Overall 1987-1988	Overall 1993-1995
Czech Republic	0	1	0	1	0	< 1
Slovakia	0	9	0	1	0	< 1
Slovenia	8	…	7	…	0	< 1
Hungary	2	7	1	1	1	2
Poland	8	20	5	3	6	14
Bulgaria	2	43	4	28	2	15
Belarus	…	…	…	…	1	22
Latvia	51	…	15	…	1	22
Romania	9	35	12	19	6	28
Lithuania	…	…	…	…	1	30
Estonia	27	34	38	38	…	37
Uzbekistan	…	…	…	…	24	39
Armenia	…	…	…	…	…	40
Georgia	…	…	…	…	…	40
Russia	40	62	23	34	2	44
Azerbaijan	73	…	65	…	…	50
Turkmenistan	…	…	…	…	12	57
Kazakhstan	…	…	…	…	5	62
Ukraine	…	…	…	…	2	63
Moldova	3	…	3	…	4	66
Kyrgyzstan	…	…	…	…	12	86
Tajikistan	…	…	…	…	…	100
Albania	…	…	…	…	…	…
Croatia	…	…	…	…	…	…
FYR Macedonia	…	…	…	…	…	…
CEE & NIS	28	46	17	24	4	40
Northern Tier CEE	7	14	4	3	3	11
Southern Tier CEE	7	37	10	21	5	24
NIS	41	62	24	34	4	50
UK					1	
Turkey					31	
Malaysia					15	
Brazil					33	

Note: Overall poverty rates for most countries measure the percent of population below poverty line of $120 per capita per month at 1990 international prices; for Armenia, Azerbaijan, Georgia and Tajikistan the poverty threshold is $100 per month. For children and elderly, the poverty threshold is roughly 25 percent of the average 1989 wage, and hence is not directly comparable with overall poverty rates.

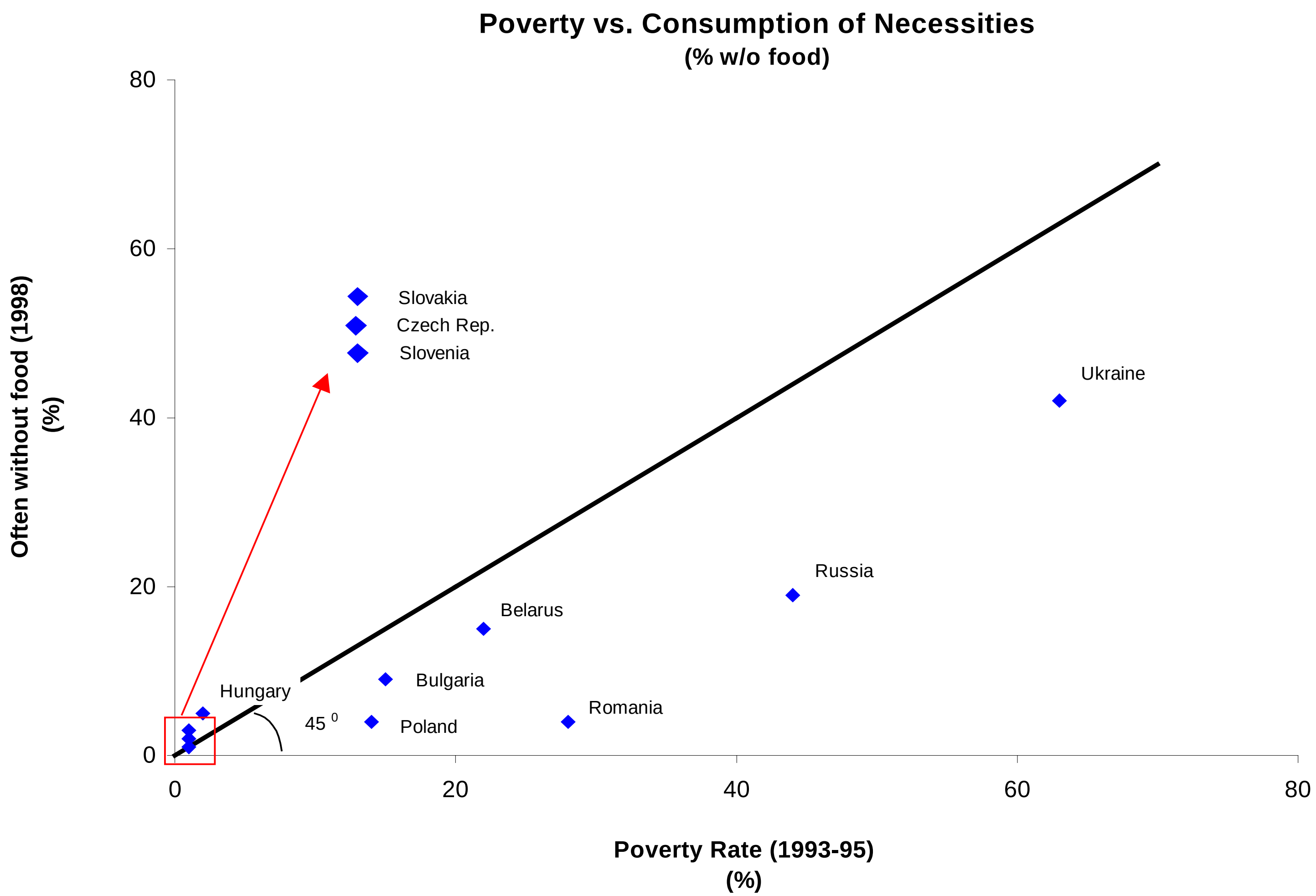
Source: Branko Milanovic, *Income, Inequality, and Poverty during the Transition from Planned to Market Economy* (World Bank, 1998); UNICEF, *Poverty, Children, and Policy: Reponses for a Brighter Future*, Economies in Transition: Regional Monitoring Report 3 (1995); UNDP, *Poverty in Transition?* (July 1998); UNDP, *Human Development Report 1997* (May 1997); and Bureau of the Census, *Populations at Risk*, No. 5, for ENI/PCS (July 1996).

Figure 9.



Poverty vs. Coping (%)
80
60
40
20
0
0
20
40
60
80
Poverty Rate (1993-95) (%)

Figure 10.



Data on the percentage of households in 1998 having to often do without food are from two household surveys: R. Rose & C. Haerpfer, *New Democracies Barometer V: A 12 Nation Survey*, CSPP, #306 (1998); and Rose, *New Russia Barometer Trends Since 1992*, CSPP, #320 (1999).

Poverty rates measure the percent of population below a poverty line of $120 per capita per month at 1990 international prices. Data are from Branko Milanovic, *Income, Inequality, and Poverty during the Transition from Planned to Market Economy* (World Bank, 1998).

Table 20. Infant and Child Mortality

	Infant Mortality				Under 5 Yrs. mortality rates		
	1989	1993	1998	% Change 1989-98	1990	1998	% Change 1990-98
Slovenia	8	7	5	-38%	9	5	-44%
Czech Republic	10	9	5	-50%	11	6	-45%
Croatia	12	10	8	-33%	13	9	-31%
Slovakia	14	11	9	-36%	15	10	-33%
Poland	19	16	10	-47%	19	11	-42%
Hungary	16	13	10	-38%	16	11	-31%
Bulgaria	14	16	14	0%	18	17	-6%
Bosnia-Herzegovina	18	23	13	-28%	22	19	-14%
Yugoslavia	29	22	13	-55%	30	21	-30%
Estonia	15	16	9	-40%	22	22	0%
Latvia	11	16	15	36%	20	22	10%
Ukraine	13	15	14	8%	22	22	0%
Georgia	20	18	15	-25%	29	23	-21%
Lithuania	11	16	9	-18%	21	23	10%
Romania	27	23	21	-22%	32	24	-25%
Russia	18	20	17	-6%	26	25	-4%
FYR Macedonia	37	24	16	-57%	41	27	-34%
Belarus	12	13	11	-8%	19	27	42%
Armenia	20	17	15	-25%	31	30	-3%
Moldova	..	22	18	-16%	37	35	-5%
Albania	31	33	25	-19%	41	37	-10%
Kazakhstan	26	28	22	-15%	48	43	-10%
Azerbaijan	26	28	17	-35%	44	46	5%
Uzbekistan	38	32	22	-42%	58	58	0%
Kyrgyzstan	32	32	26	-19%	83	66	-20%
Turkmenistan	55	46	33	-40%	76	72	-5%
Tajikistan	43	47	23	-47%	78	74	-5%
CEE & Eurasia	20	20	16	-20	29	27	-7%
Northern Tier CEE	16	14	9	-20	17	11	-35%
Southern Tier CEE	24	21	18	-26	28	22	-21%
Eurasia	21	22	18	-14	33	32	-3%
LDCs			60		104	95	-9%
Middle-income			35		…	…	…
Latin Amer. & Carib			…		53	39	-26%
Sub-Saharan Africa			…		180	173	-4%
OECD			10		…	…	…
Industrialized countries			…		9	6	-33%
EU			5		…	…	…
Benchmarks			30	no worsening			

Note: Infant mortality rate is per 1,000 live births; and life expectancy is in years. The OECD infant mortality rate average is significantly pulled up by 2 members: Turkey at 40 and Mexico at 31. Percent change in infant mortality is calculated from 1993 to 1998 for Moldova.

World Bank, *World Development Indicators 2000* (March 2000). Under 5 mortality rates are from UNICEF, *State of the World's Children 2000* (Janurary 2000)

Table 21. Life Expectancy

	Life Expectancy										
	Male			Female						% change	% change
	1989	1997	% change	1989	1997	% change	1980	1989-92	1998	1980-98	1989-98
Czech Republic	68	71	3.5	75	78	2.8	70	72	75	7.1	4.2
Slovenia	69	71	3.2	77	79	2.5	70	73	75	7.1	2.7
Armenia	69	70	1.9	75	77	3.5	73	70	74	1.4	5.7
Bosnia-Herzegovina	69	..	...	74	..	...	70	71	73	4.3	2.8
Croatia	68	68	0.1	76	77	1.7	70	73	73	4.3	0.0
FYR Macedonia	70	70	0.7	74	75	1.5	72	72	73	1.4	1.4
Georgia	68	69	0.6	76	77	1.5	71	72	73	2.8	1.4
Poland	67	69	2.5	76	77	2.0	70	72	73	4.3	1.4
Slovakia	67	69	3.0	75	77	1.7	70	71	73	4.3	2.8
Albania	70	69	-1.1	76	75	-1.1	69	72	72	4.3	0.0
Lithuania	67	66	-1.5	76	77	0.7	71	71	72	1.4	1.4
Yugoslavia	69	70	1.3	74	75	1.2	70	72	72	2.9	0.0
Azerbaijan	66	67	1.5	74	75	0.5	68	71	71	4.4	0.0
Bulgaria	69	67	-2.0	75	74	-0.9	71	72	71	0.0	-1.4
Hungary	65	66	1.5	74	75	1.8	70	71	71	1.4	0.0
Estonia	66	64	-1.9	75	76	1.7	69	70	70	1.4	0.0
Latvia	65	64	-2.3	75	75	-0.4	69	69	70	1.4	1.4
Romania	67	65	-2.1	73	73	0.4	69	71	69	0.0	-2.8
Tajikistan	66	66	-1.1	71	71	0.6	66	69	69	4.5	0.0
Uzbekistan	66	66	0.2	72	72	0.4	67	69	69	3.0	0.0
Belarus	67	63	-6.3	76	74	-2.6	71	71	68	-4.2	-4.2
Kyrgyzstan	64	63	-2.5	72	71	-0.6	65	66	67	3.1	1.5
Moldova	66	63	-4.0	72	70	-2.8	66	68	67	1.5	-1.5
Russia	64	61	-5.0	75	73	-1.9	67	69	67	0.0	-2.9
Ukraine	66	62	-6.2	75	73	-2.9	69	70	67	-2.9	-4.3
Turkmenistan	62	62	0.8	68	69	1.3	64	66	66	3.1	0.0
Kazakhstan	64	60	-6.6	73	70	-3.4	67	68	65	-3.0	-4.4
CEE & Eurasia	66	64	-2.7	74	74	-0.8	68.3	70.0	68.9	0.8	-1.6
Northern Tier CEE	67	68	2.2	75	77	1.9	70.0	71.6	72.9	4.1	1.7
Southern Tier CEE	68	67	-1.1	74	74	0.2	69.7	71.6	70.8	1.5	-1.1
Eurasia	65	62	-4.3	74	73	-1.7	67.6	69.2	67.4	-0.2	-2.5
LDCs		63			66.6						
Middle-income		67			71.4						
OECD		73			79						
EU		74			81						
Benchmarks			no worsening			no worsening					

World Bank, *World Development Indicators 2000* (April 2000); UNICEF, *State of the World's Children* (Jan. 2000)

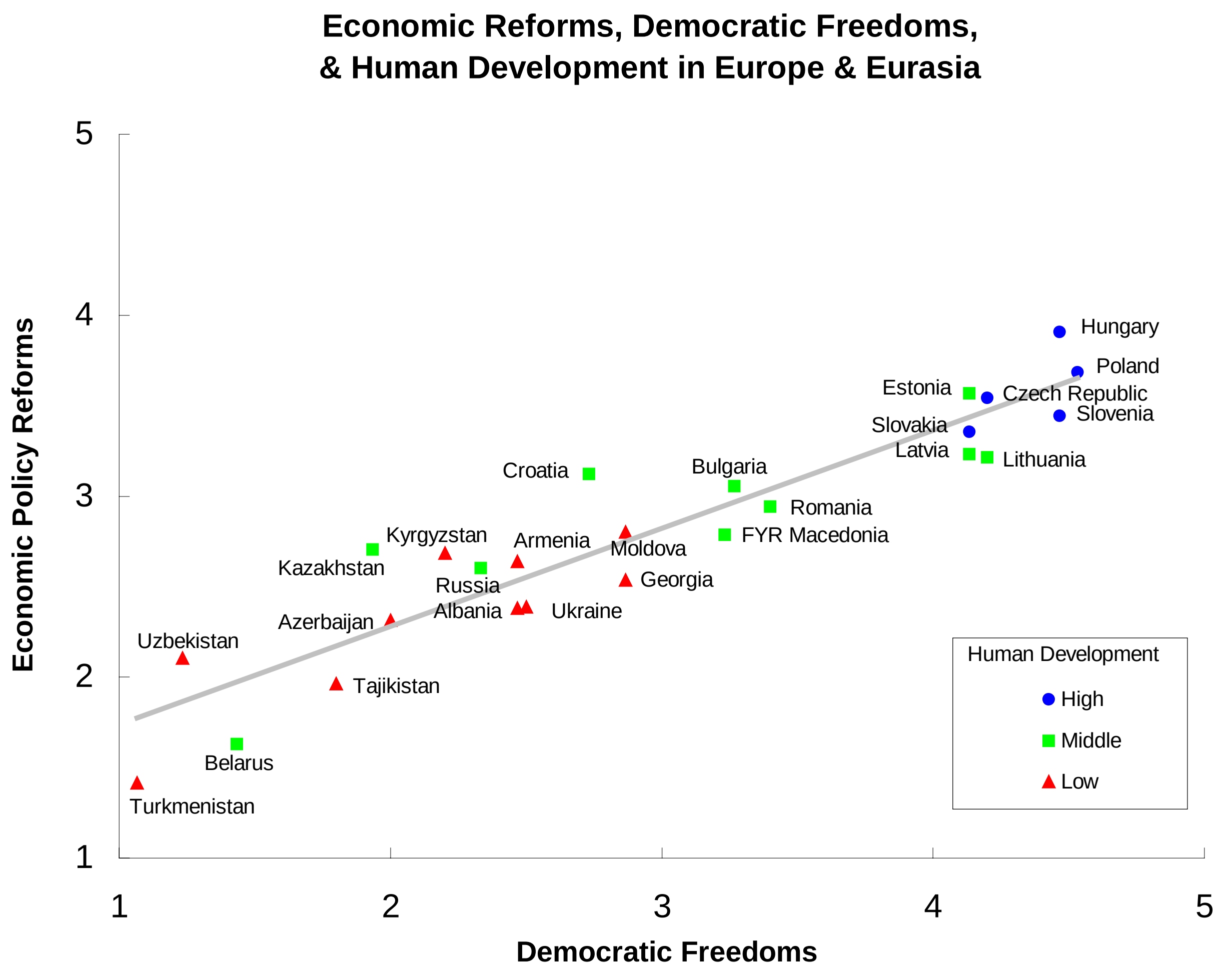
Table 22. Human Development

Country	Secondary School Enrollment (% of age group) 1990	1993	1997	% change	Human Development Index 1997 Score	Rank
Slovenia	91.1	90.3	91.7	0.7	0.845	33
Czech Republic	91.2	91.8	*98.7*	8.2	0.833	36
Slovakia	..	88.6	94.0	6.1	0.813	42
Poland	81.5	93.9	*97.6*	19.8	0.802	44
Hungary	78.6	94.3	*97.8*	24.4	0.795	47
Estonia	101.9	93.9	103.8	1.9	0.773	54
Croatia	76.2	82.8	81.8	7.3	0.773	55
Belarus	93.0	90.9	92.9	-0.1	0.763	60
Lithuania	91.9	80.9	86.3	-6.1	0.761	62
Bulgaria	75.2	70.1	76.8	2.1	0.758	63
Romania	92.0	79.4	78.4	-14.8	0.752	68
Russia	93.3	87.0	..	-6.8	0.747	71
FYR Macedonia	55.7	57.3	62.9	12.9	0.746	73
Latvia	92.7	87.0	83.7	-9.7	0.744	74
Kazakhstan	98.0	92.0	87.0	-11.2	0.740	76
Georgia	95.0	77.0	77.0	-18.9	0.729	85
Armenia	..	88.0	90.0	2.3	0.728	87
Ukraine	92.8	91.2	..	-1.7	0.721	91
Uzbekistan	99.0	94.0	94.0	-5.1	0.720	92
Turkmenistan	..	..	..	...	0.712	96
Kyrgyzstan	100.0	90.0	79.0	-21.0	0.702	97
Albania	78.3	41.2	37.5	-52.1	0.699	100
Azerbaijan	90.0	87.0	77.0	-14.4	0.695	103
Moldova	80.0	84.0	80.5	0.6	0.683	104
Tajikistan	102.0	82.0	78.0	-23.5	0.665	108
Yugoslavia	…	…	62.0	…		
CEE & Eurasia	90.4	87.0	86.5	-2.9	0.749	
Northern Tier CEE	84.2	92.3	96.5	14.7	0.803	
Southern Tier CEE	79.5	71.4	71.7	-8.7	0.751	
Eurasia	94.0	88.5	86.9	-6.5	0.734	
European Union	96.7	108.4	108.4	12.1	0.903	...
Costa Rica	…	…	…	...	0.801	45
Thailand	…	…	…	...	0.753	67
Jamaica	…	…	…	...	0.734	82
Benchmark	no decline in enrollment					

The HDI ranges from 0 to 1; the higher the value, the greater the human development.

Source: World Bank, *World Development Indicators* (April 2000); UNESCO/USAID, *Global Education Database 1998* (May 1999); UNDP, *Human Development Report* (June 1999).

Figure 11.



Ratings of democratic freedoms are from Freedom House (*Nations in Transit 1999* and *Freedom in the World 1999-2000*). Economic policy reform measures are primarily drawn from EBRD, *Transition Report 1999*. Ratings are based on a 1 to 5 scale, with 5 representing most advanced.

Human development is measured by the UNDP's Human Development Index (HDI) in its *Human Development Report 1999*. The HDI is based on three indicators: longevity, as measured by life expectancy; educational attainment, as measured by a combination of adult literacy and combined primary, secondary, and tertiary enrollment ratios; and standard of living, as measured by real per capita GDP ($PPP).

IV. Concluding Remarks

Decisions on the magnitude and duration of U.S. assistance to the transition region are made on the basis of several factors:

(a) progress the country has made toward a sustainable transition to a market-based democracy;

(b) strategic importance of the country to the United States;

(c) importance of the recipient country to U.S. citizens; and

(d) effectiveness of particular assistance activities.

This paper has presented an approach to analyzing the first factor. The second and third are not as readily quantifiable but are matters of judgment that are regularly considered, along with the first, in making country-level budget decisions. The fourth factor, based on both regular reporting against strategic objective targets and on occasional field-based evaluations, is used primarily to inform the allocation of country budget levels among strategic objectives but is also a basis for determining whether a country assistance program is having enough impact to warrant continuation.

USAID collects, analyzes, and reports on the country performance indicators two times a year. Inter-agency reviews are held as a means to assess the data and to better take stock of progress in the region. These data are also provided to the State Department-based Coordinators for U.S. Assistance to CEE and Eurasia and discussed with them when country planning levels are determined.

The overall ratings of the transition countries in terms of economic policy reforms and democratic freedoms (as depicted in the *Summary Figure*) provide a rough guide to policy in this regard. Countries with the highest ratings are obvious candidates for earlier "graduation." Countries with the lowest ratings would seem to fall into one of three contrasting categories: (1) those where assistance is least likely to be effective, in which case it may make sense to close those programs down altogether or to keep highly targeted funding at minimal levels until their commitment to reform increases; (2) those where reform now appears likely but requires greater resources; or (3) those which possess characteristics that match well with the Agency's priorities for sustainable development programs. Countries in the middle are likely candidates for continuing programs through existing funding mechanisms, as long as the assistance is effective and Congress continues to appropriate funds for this purpose.

MONITORING COUNTRY PROGRESS
IN CENTRAL AND EASTERN EUROPE
& EURASIA

APPENDIX I: REFORM INDICATORS

USAID / E&E / PCS
Office of Program Coordination and Strategy
Bureau for Europe & Eurasia
U.S. Agency for International Development

May 2000

A. Economic Policy Reforms: Indicators & Description of EBRD's Rating Categories

First Stage Reforms

Small-scale Privatization

1 Little progress
2 Substantial share privatized
3 Nearly comprehensive program implemented, but design or lack of government supervision leaves important issues unresolved (e.g. lack of tradability of ownership rights)
4 Complete privatization of small companies with tradable ownership rights
5 Standards and performance typical of advanced industrial economies: no state ownership of small enterprises; effective tradability of land

Price Liberalization

1 Most prices formally controlled by the government
2 Price controls for several important product categories, including key infrastructure products such as utilities and energy; state procurement at non-market prices remains substantial
3 Substantial progress on price liberalization including for energy prices; state procurement at non-market prices largely phased out
4 Comprehensive price liberalization; utility pricing ensuring cost recovery
5 Standards and performance typical of advanced industrial economies: comprehensive price liberalization; efficiency-enhancing regulation of utility pricing

Trade & Foreign Exchange System

1 Widespread import and/or export controls or very limited legitimate access to foreign exchange
2 Some liberalization of import and/or export controls; almost full current account convertibility in principle but with a foreign exchange regime that is not fully transparent (possibly with multiple exchange rates)
3 Removal of most quantitative and administrative import and export restrictions (apart from agriculture) and all significant export tariffs; insignificant direct involvement in exports and imports by ministries and state-owned trading companies; no major non-uniformity of customs duties for non-agricultural goods and services.
4 Removal of all quantitative and administrative import and export restrictions (apart from agriculture) and all significant export tariffs; insignificant direct involvement in exports and imports by ministries and state-owned trading companies; no major non-uniformity of customs duties for non-agricultural goods and services
5 Standards and performance norms of advanced industrial economies: removal of most tariff barriers; membership in WTO

Extensiveness of Legal Reform for Investment:

1 Legal rules concerning pledge, bankruptcy and company law are very limited in scope. Laws impose substantial constraints on the creation, registration and enforcement of security over movable assets, and may impose significant notarization fees on pledges. Company laws do not ensure adequate corporate governance or protect shareholders' rights. Bankruptcy laws do

not provide for certainty or clarity with respect to the definition of an insolvent debtor, the scope of reorganization proceedings or the priority of distribution to creditors following liquidation. Laws in these substantive areas often have not been amended to approximate those of more developed countries and the laws that have been amended contain ambiguities or inconsistencies.

2 Legal rules concerning pledge, bankruptcy and company law are limited in scope and are subject to conflicting interpretations. Legislation may have been amended but new laws do not necessarily approximate those of more developed countries. Specifically, the registration and enforcement of security over movable assets has not been adequately addressed, leading to uncertainty with respect to the registration and enforcement of pledges. Pledge laws may impose significant notarization fees on pledges. Company laws do not ensure adequate corporate governance or protect shareholders' rights. Laws may contain inconsistencies or ambiguities concerning, inter alia, the scope of reorganization proceedings and/or the priority of secured creditors in bankruptcy.

3 New or amended legislation has recently been enacted in at least two of the three areas that were the focus of this survey--pledge, bankruptcy or company law--but could benefit from further refinement and clarification. Legal rules permit a non-possessory pledge over most types of movable assets. However, the mechanisms for registration of the security interest are still rudimentary and do not provide parties with adequate protection. There is scope for enforcement of pledges without court assistance. Company laws may contain limited provisions for corporate governance and the protection of shareholders' rights. Bankruptcy legislation contains provisions for both reorganization and liquidation but may place claims of other creditors in priority to those of secured creditors in liquidation.

4 Comprehensive legislation exists in a least two of the three areas of commercial law that were the focus of this survey--pledge, bankruptcy and company law. Pledge law allows parties to take non-possessory pledges in a wide variety of movable property and contains mechanisms for enforcement of pledges without court assistance. The legal infrastructure, however, is not fully developed to include a centralized or comprehensive mechanism for registering pledges. Company laws contain provisions for corporate governance and the protection of shareholders' rights. Director and officer duties are defined. Bankruptcy law includes detailed provisions for reorganization and liquidation. Liquidators possess a wide variety of powers to deal with the property and affairs of a bankrupt.

5 Comprehensive legislation exists in all three areas of commercial law--pledge, bankruptcy and company law. Legal rules closely approach those more developed countries. These legal systems have a uniform (i.e., centralized registration) system for the taking and enforcement of a security interest in movable assets and also provide for adequate corporate governance and protect shareholders' rights. In particular the rights of minority shareholders are protected in the event of the acquisition by third parties of less than all of the shares of a widely held company. Bankruptcy law provides in a comprehensive manner for both reorganization and liquidation. Liquidators possess a wide variety of powers and duties to deal with the property and affairs of a bankrupt, including wide powers of investigation of pre-bankruptcy transactions carried out by the debtor. There are specialized courts that handle bankruptcy proceedings. Liquidators must possess certain minimum qualifications

Second Stage Reforms

Large-scale Privatization

1 Little private ownership
2 Comprehensive scheme almost ready for implementation; some sales completed
3 More than 25 percent of large-scale state-owned enterprise assets privatized or in the process of being sold, but possibly with major unresolved issues regarding corporate governance
4 More than 50 percent of state-owned enterprise assets privatized in a scheme that has generated substantial outsider ownership
5 Standards and performance typical of advanced industrial economies: more than 75 percent of enterprise assets in private ownership with effective corporate governance

Governance & Enterprise Restructuring

1 Soft budget constraints (lax credit and subsidy policies weakening financial discipline at the enterprise level); few other reforms to promote corporate governance
2 Moderately tight credit and subsidy policy but weak enforcement of bankruptcy legislation and little action taken to break up dominant firms
3 Significant and sustained actions to harden budget constraints and to promote corporate governance effectively (e.g. through privatization combined with tight credit and subsidy policies and/or enforcement of bankruptcy legislation)
4 Strong financial discipline at the enterprise level; substantial improvement in corporate governance through government restructuring program or an active corporate control market; significant action to break up dominant firms; significant new investment at the enterprise level
5 Standards and performance typical of advanced industrial economies: effective corporate control exercised through domestic financial institutions and markets, fostering market-driven restructuring

Competition Policy

1 No competition legislation and institutions; widespread entry restrictions
2 Competition policy legislation and institutions set up; some reduction of entry restrictions or enforcement action on dominant firms
3 Some enforcement actions to reduce abuse of market power and to promote a competitive environment, including break-ups of dominant conglomerates; substantial reduction of entry restrictions
4 Significant enforcement actions to reduce abuse of market power and to promote a competitive environment
5 Standards and performance typical of advanced industrial economies: effective enforcement of competition policy; unrestricted entry to most markets

Banking Reform

1 Little progress beyond establishment of a two-tier system
2 Significant liberalization of interest rates and credit allocation; limited use of directed credit or interest rate ceilings

3 Substantial progress in establishment of bank solvency and of a framework for prudential supervision and regulation; full interest rate liberalization with little preferential access to cheap refinancing; significant lending to private enterprises and significant presence of private banks
4 Significant movement of banking laws and regulations towards BIS standards; well-functioning banking competition and effective prudential supervision; significant term lending to private enterprises; substantial financial deepening
5 Standards and performance norms of advanced industrial economies: full convergence of banking laws and regulations with BIS standards; provision of full set of competitive banking services

Non-Bank Financial Institutional Reform

1 Little progress
2 Formation of securities exchanges, market-makers and brokers; some trading in government paper and/or securities; rudimentary legal and regulatory framework for the issuance and trading of securities
3 Substantial issuance of securities by private enterprises; establishment of independent share registries, secure clearance and settlement procedures, and some protection of minority shareholders; emergence of non-bank financial institutions (e.g. investment funds, private insurance and pension funds, leasing companies) and associated regulatory framework
4 Securities laws and regulations approaching IOSCO standards; substantial market liquidity and capitalization; well-functioning non-bank financial institutions and effective regulation
5 Standards and performance norms of advanced industrial economies: full convergence of securities laws and regulations with IOSCO standards; fully developed non-bank intermediation

Effectiveness of Legal Rules for Investment

1 Commercial legal rules are usually very unclear and sometimes contradictory. The administration and judicial support for the law is rudimentary. The cost of transactions, such as creating a pledge over a movable asset is prohibitive so as to render a potentially extensive law ineffective. There are no meaningful procedures in place in order to make commercial laws fully operational and enforceable. There are significant disincentives for creditors to seek the commencement of bankruptcy proceedings in respect of insolvent debtors.
2 Commercial legal rules are generally unclear and sometimes contradictory. There are few, if any meaningful procedures in place in order to make commercial laws operational and enforceable.
3 While commercial legal rules are reasonably clear, administration or judicial support of the law is often inadequate or inconsistent so as to create a degree of uncertainty (e.g., substantial discretion in the administration of laws, few up-to-date registries for pledges).
4 Commercial laws are reasonably clear and administrative and judicial support of the law is reasonably adequate. Specialized courts, administrative bodies or independent agencies may exist for the liquidation of insolvent companies, the registration of publicly traded shares or the registration of pledges.

5 Commercial laws are clear and readily ascertainable. Commercial law is well supported administratively and judicially, particularly regarding the efficient functioning of courts, liquidation proceedings, the registration of shares and the orderly and timely registration of security interests.

Environmental Policy Reform. The environmental policy reform indicator is drawn from EBRD (November 1999 and 1997). Four components go into it as shown in *Table 1* below. The first is the degree of adherence to six key international environmental treaties: the Convention on the Wetlands of International Importance; the Convention on International Trade in Endangered Species of Wild Fauna and Flora; the Montreal Protocol for the control of CFC emissions; the Convention on Climate Change; the Convention on Biodiversity; and the Convention on Environmental Impact in a Transboundary Context. Countries are put into three groups on the basis of their progress towards signing and ratifying these treaties.

The second component attempts to measure progress in air and water ambient and emission (effluent) standards. Three levels of progress are identified: (1) the maximum permissible concentrations (MPC) system in place, broadly based on the former Soviet system; (2) a new system is being introduced, either as an evolution of MPC or in order to meet EU requirements; and (3) essentially new standards system is in place, often following EU requirements.

The third component attempts to measure progress in preparing and implementing national environmental action plans (NEAPs). Countries either have a NEAP planned or under preparation; or they have a NEAP prepared and under implementation.

Finally, the fourth component tries to assess the extent to which environmental financial mechanisms are used. From an EBRD questionnaire sent to the authorities in charge of the environment in each of the countries, information on four instruments were compiled: (1) existence of an environmental fund for channeling the money collected in fees and fines to environmental investments; (2) provision of taxes/other penalties or financial incentives for energy and resource efficiency; (3) waste and pollution reduction; (4) the use of clean technologies. Countries were grouped in two: those in which three or more financial instruments are in place; and those with less than three instruments in place.

Appendix I. Table 1. Environmental Policy Reform

	Treaties	Standards	NEAPs	Financial Instruments	Average
Hungary	5	5	4	4	4.5
Poland	5	5	4	4	4.5
Czech Republic	4	5	4	4	4.3
Estonia	4	3	4	4	3.8
Slovakia	4	3	4	4	3.8
Latvia	5	3	4	2	3.5
Croatia	4	3	2	4	3.3
Lithuania	4	1	4	4	3.3
Romania	4	3	4	2	3.3
Russia	4	1	4	4	3.3
Ukraine	4	1	4	4	3.3
Azerbaijan	3	1	4	4	3.0
Bulgaria	5	1	4	2	3.0
Moldova	3	1	4	4	3.0
Slovenia	3	3	4	2	3.0
Albania	3	1	4	2	2.5
Belarus	3	1	4	2	2.5
FYR Macedonia	3	1	4	2	2.5
Uzbekistan	3	1	4	2	2.5
Bosnia-Herzegovina	1	...	2	4	2.3
Georgia	4	1	2	2	2.3
Kazakhstan	2	1	4	2	2.3
Armenia	3	1	2	2	2.0
Kyrgyzstan	1	1	4	2	2.0
Tajikistan	2	1	2	2	1.8
Turkmenistan	2	1	2	2	1.8
CEE & Eurasia					**3.2**
Northern Tier CEE					**4.3**
Southern Tier CEE					**3.0**
Eurasia					**3.0**

Note: On a 1-5 scale with 5 the most advanced. See text for an elaboration of the components.

Source: EBRD, *Transition Report* (November 1999 and November 1997).

Infrastructure. This indicator averages EBRD ratings for reform progress in five infrastructure sectors: telecommunications, railways, electric power, roads, and water & waste water. The component scores are provided in Table 2 below:

(a) Telecommunications

1 Little progress in commercialization and regulation, i.e., minimal degree of private sector involvement, strong political interference in management, lack of cost-effective tariff-setting principles and extensive cross-subsidization. Few other institutional reforms to encourage liberalization envisaged, even for mobile phones and value-added services.

2 Modest progress in commercialization, i.e., corporatization of the dominant operator and some separation of operation from public sector governance, but tariffs still politically determined.

3 Substantial progress in commercialization and regulation. Full separation of telecommunications from postal services, with reduction in the extent of cross subsidization. Some liberalization in the mobile segment and in value-added services.

4 Complete commercialization (including the privatization of the dominant operator) and comprehensive regulatory and institutional reforms. Extensive liberalization of entry.

5 Implementation of a coherent and effective institutional and regulatory framework (including the operation of an independent regulator) encompassing tariffs, interconnection rules, licensing, concession fees and spectrum allocation. Existence of a consumer ombudsman function.

(b) Railways

1 Monolithic organizational structures. State railways still effectively operated as government departments. Few commercial freedoms to determine prices or investments. No private sector involvement. Cross-subsidization of passenger service public service obligations with freight service revenues.

2 Laws distancing rail operations from the state, but weak commercial objectives. No budgetary funding of public service obligations in place. Organizational structures still overly based on geographic/functional areas. Separation of ancillary businesses but little divestment. Minimal encouragement of private sector involvement. Initial business planning, but targets general and tentative.

3 Laws passed to restructure the railways and introduce commercial orientation. Separation of freight and passenger marketing groups grafted onto tradition structures. Some divestment of ancillary businesses. Some budgetary compensation for passenger services. Design of business plans with clear investment and rehabilitation targets. Business plans designed, but funding unsecured. Some private sector involvement in rehabilitation and/or maintenance.

4 Laws passed to fully commercialize railways. Creation of separate internal profit centers for passenger and freight (actual or imminent). Extensive market freedoms to set tariffs and investments. Medium-term business plans under implementation. Ancillary industries divested. Policy development to promote commercial (including private) rail transport operations.

5 Railway law exists allowing for separation of infrastructure from operations, and/or freight from passenger operations, and/or private train operations. Private sector participation in

ancillary services and track maintenance. Establishment of rail regulator and/or implementation of access pricing and/or plans for a full divestment and transfer of asset ownership, including infrastructure and rolling stock.

(c) Electric power

1 Power sector operated as a government department; political interference in running the industry. Few commercial freedoms or pressures. Average prices below costs, with external and implicit subsidy and cross-subsidy. Very little institutional reform with monolithic structure and no separation of different parts of the business.
2 Power company is distance from government. For example, established as a joint-stock company, though there is still political interference. Some attempt to harden budget constraints, but management incentives for efficient performance are weak. Some degree of subsidy and cross-subsidy. Little institutional reform; monolithic structure with no separation of different parts of the business. Minimal private sector involvement.
3 Law passed which provides for full-scale restructuring of the industry, including vertical unbundling through accounting separation, setting up of regulator with some distance from the government, plans for tariff reform if effective tariffs are below cost, possibility of private ownership and industry liberalization. Little or no private sector involvement.
4 Law for industry restructuring passed and implemented providing for: separation of the industry into generation, transmission and distribution; setting up of a regulator, with rules for setting cost-reflective tariffs formulated and implemented. Arrangements for network access (negotiated access, single buyer model) developed. Substantial private sector involvement in distribution and/or generation.
5 Business separated vertically into generation, transmission and distribution. Existence of an independent regulator with full power to set cost-reflective tariffs. Large-scale private sector involvement. Institutional development covering arrangements for network access and full competition in generation.

(d) Roads

1 There is minimal degree of decentralization, and no commercialization has taken place. All regulatory, road management and resource allocation functions are centralized at ministerial level. New investments and road maintenance financing are dependent on central budget allocations. Road user charges are based on criteria other than relative costs imposed on the network and road use. Road construction and maintenance are undertaken by public construction units. There is no private sector participation. No public consultation or accountability take place in the preparation of road projects.

2 There is a moderate degree of decentralization, and initial steps have been taken in commercialization. A road/highways agency has been created. Initial steps have been undertaken in resource allocation and public procurement methods. Road user charges are based on vehicle and fuel taxes but are only indirectly related to road use. A road fund has been established but it is dependent on central budget allocations. Road construction and maintenance is undertaken primarily by corporatized public entities, with some private sector participation. There is minimal public consultation/participation and accountability in the preparation of road projects.

3 There is a fairly large degree of decentralization and commercialization. Regulation, resource allocation, and administrative functions have been clearly separated from maintenance and operations of the public road network. Road user charges are based on vehicle and fuel taxes and fairly directly related to road use. A law has been passed allowing for the provision and operation of public roads by private companies under negotiated commercial contracts. There is private sector participation either in road maintenance works allocated via competitive tendering or through a concession to finance, operate and maintain at least a section of the highway network. There is limited public consultation and/or participation and accountability in the preparation of road projects.

4 There is a large degree of decentralization of road administration, decision-making, resource allocation and management according to government responsibility and functional road classification. A transparent methodology is used to allocate road expenditures. A track record has been established in implementing competitive procurement rules for road design, construction, maintenance and operations. There is large-scale private sector participation in construction, operations and maintenance directly and through public-private partnership arrangements. There is substantial public consultation and/or participation and accountability in the preparation of road projects.

5 A fully decentralized road administration has been established, with decision-making, resource allocation and management across road networks and different levels of government. Commercialized road maintenance operations are undertaken through open and competitive tendering by private construction companies. Legislation has been passed allowing for road user charges to fully reflect costs of road use and associated factors, such as congestion, accidents and pollution. There is widespread private sector participation in all aspects of road provision directly and through public-private partnership arrangements. Full public consultation is undertaken in the approval process for new road projects.

(e) *Water and Waste water*

(1) There is a minimal degree of decentralization, and no commercialization has taken place. Water and waster-water services are operated as a vertically integrated natural monopoly by a government ministry through national or regional subsidiaries or by municipal departments. There is no, or little, financial autonomy and/or management capacity at municipal level. Heavily subsidized tariffs still exist, along with a high degree of cross-subsidization.

(2) There is a low level of cash collection. Central or regional government controls tariffs and investment levels. No explicit rules exist in public documents regarding tariffs or quality of service. There is no, or insignificant, private sector participation.

(3) There is a moderate degree of decentralization, and initial steps have been taken in commercialization. Water and waste-water services are provided by municipally owned companies, which operate as joint-stock companies. There is some degree of financial autonomy at the municipal level but heavy reliance on central government for grants and income transfers. Partial cost recovery is achieved through tariffs, and initial steps have been taken to reduce cross-subsidies. General public guidelines exist regarding tariff-setting and service quality but these are both still under ministerial control. There is some private sector participation through service or management contracts or competition to provide ancillary services.

(4) A fairly large degree of decentralization and commercialization has taken place. Water and waste-water utilities operate with managerial and accounting independence from municipalities, using international accounting standards and management information systems. A municipal finance law has been approved. Cost recovery is fully operated through tariffs and there is a minimum level of cross-subsidies. A semi-autonomous regulatory agency has been established to advise on tariffs and service quality but without the power to set either. More detailed rules have been drawn up in contract documents, specifying tariff review formulae and performance standards. There is private sector participation through performance standards. There is private sector participation through the full concession of a major service in at least one city.

(5) A large degree of decentralization and commercialization has taken place. Water and waste-water utilities are managerially independent, with cash flows—net of municipal budget transfers—that ensure financial viability. A municipal finance law has been implemented, providing municipalities with the opportunity to raise finance. Full cost recovery exists and there are no cross-subsidies. A semi-autonomous regulatory agency has the power to advise and enforce tariffs and service quality. There is substantial private sector participation through build-operate-transfer concessions, management contracts or asset sales to service parts of the network or entire networks. A concession of major services has taken place in a city other than the country’s capital.

(6) Water and waste-water utilities are fully decentralized and commercialized. Large municipalities enjoy financial autonomy and demonstrate the capability to raise finance. Full cost recovery has been achieved and there are no cross-subsidies. A fully autonomous regulator exists with complete authority to review and enforce tariff levels and performance quality standards. There is widespread private sector participation via service management/lease contracts, with high-powered performance incentives and/or full concessions and/or divestiture of water and waste-water services in major urban areas.

Appendix I. Table 2. Infrastructure

	telecom	power	rail	roads	water/waste	**average**
Estonia	4.0	3.0	4.0	...	4.0	**3.8**
Hungary	4.0	4.0	3.3	3.3	4.0	**3.7**
Poland	3.3	3.0	3.3	3.3	4.0	**3.4**
Romania	3.0	3.0	4.0	2.3	3.0	**3.1**
Slovenia	2.3	2.3	3.3	3.0	4.0	**3.0**
Czech Republic	4.0	2.0	2.3	2.3	4.0	**2.9**
Latvia	3.0	3.0	3.3	2.3	3.0	**2.9**
Bulgaria	3.0	3.0	3.0	2.3	2.0	**2.7**
Lithuania	3.3	2.3	2.3	2.3	3.0	**2.7**
Croatia	2.3	2.3	2.3	2.3	3.3	**2.5**
Georgia	2.0	3.0	3.0	2.0	...	**2.5**
Armenia	2.3	3.0	2.0	2.3	2.0	**2.3**
Russia	3.0	2.0	2.3	2.0	2.3	**2.3**
Moldova	2.3	3.0	2.0	2.0	2.0	**2.3**
Kazakhstan	2.3	3.3	2.0	2.0	1.3	**2.2**
Slovakia	2.3	2.0	2.0	2.3	...	**2.2**
FYR Macedonia	2.0	2.3	2.0	...	1.3	**1.9**
Albania	1.3	2.0	2.0	2.0	1.3	**1.7**
Azerbaijan	1.3	2.0	2.0	1.3	2.0	**1.7**
Ukraine	2.3	2.3	1.3	1.3	1.3	**1.7**
Bosnia-Herzegovina	1.3	2.0	2.0	...	1.0	**1.6**
Kyrgyzstan	2.0	2.3	1.3	1.0	1.0	**1.5**
Belarus	2.0	1.0	1.0	2.0	1.0	**1.4**
Uzbekistan	2.0	1.0	2.0	1.0	1.0	**1.4**
Tajikistan	1.3	1.0	1.0	...	...	**1.1**
Turkmenistan	1.0	1.0	1.3	1.0	1.0	**1.1**
CEE & Eurasia						**2.3**
Northern Tier CEE						**3.2**
Southern Tier CEE						**2.7**
Eurasia						**2.0**

Note: On a 1-5 scale with 5 the most advanced. See text for an elaboration of the components.

Source: EBRD, *Transition Report* (November 1999).

B. Democratic Freedoms: Elaboration of Freedom House's Rating Scheme of Political Rights and Civil Liberties

Freedom House annually rates political rights and civil liberties separately on a seven-category scale, 1 representing the most free and 7 the least free. The 1999-2000 Survey included 192 countries and/or territories. The 1-to-7 rating is derived by country teams awarding from 0 to 4 raw points per checklist item (shown below). The highest possible score for political rights is 32 points, based on up to 4 points for each of eight questions. The highest possible score for civil liberties is 52 points, based on up to 4 points for each of thirteen questions. Under the methodology, raw points correspond to category numbers as follows:

Political Rights category number	Raw points
1	28-32
2	23-27
3	19-22
4	14-18
5	10-13
6	5-9
7	0-4

Civil Liberties category number	Raw points
1	45-52
2	38-44
3	30-37
4	23-29
5	15-22
6	8-14
7	0-7

Political Rights checklist

1. Is the head of state and/or head of government or other chief authority elected through free and fair elections?
2. Are the legislative representatives elected through free and fair elections?
3. Are there fair electoral laws, equal campaigning opportunities, fair polling and honest tabulation of ballots?
4. Are the voters able to endow their freely elected representatives with real power?
5. Do the people have the right to organize in different political parties or other competitive political groupings of their choice, and is the system open to the rise and fall of these competing parties or groupings?

6. Is there a significant opposition vote, de facto opposition power, and a realistic possibility for the opposition to increase its support or gain power through elections?
7. Are the people free from domination by the military, foreign powers, totalitarian parties, religious hierarchies, economic oligarchies or any other powerful group?
8. Do cultural, ethnic, religious and other minority groups have reasonable self-determination, self-government, autonomy or participation through informal consensus in the decision-making process?

Civil Liberties checklist

1. Are there free and independent media, literature and other cultural expressions? (Note: In cases where the media are state-controlled but offer pluralistic points of view, the Survey gives the system credit).
2. Is there open public discussion and free private discussion?
3. Is there freedom of assembly and demonstration?
4. Is there freedom of political or quasi-political organization? (Note: This includes political parties, civic associations, ad hoc groups and so forth.)
5. Are citizens equal under the law, with access to an independent, nondiscriminatory judiciary, and are they respected by the security forces?
6. Is there protection from political terror, and from unjustified imprisonment, exile or torture, whether by groups that support or oppose the system, and freedom from war or insurgency situations? (Note: Freedom from war and insurgency situations enhances the liberties in a free society, but the absence of wars and insurgencies does not in itself make an unfree society free.)
7. Are there free trade unions and peasant organizations or equivalents, and is there effective collective bargaining?
8. Are there free professional and other private organizations?
9. Are there free businesses or cooperatives?
10. Are there free religious institutions and free private and public religious expressions?
11. Are there personal social freedoms, which include such aspects as gender equality, property rights, freedom of movement, choice of residence, and choice of marriage and size of family?
12. Is there equality of opportunity, which includes freedom from exploitation by or dependency on landlords, employers, union leaders, bureaucrats or any other type of denigrating obstacle to a share of legitimate economic gains?
13. Is there freedom from extreme government indifference and corruption?

Political Rights

1 Generally speaking, places rated 1 come closest to the ideals suggested by the checklist questions, beginning with free and fair elections. Those elected rule. There are competitive parties or other competitive political groupings, and the opposition has an important role and power. These entities have self-determination or an extremely high degree of autonomy. Usually, those rated 1 have self-determination for minority groups or their participation in government through informal consensus. With the exception of such entities as tiny island

countries, these countries and territories have decentralized political power and free sub-national elections.

2 Such factors as gross political corruption, violence, political discrimination against minorities, and foreign or military influence on politics may be present, and weaken the quality of democracy.

3 , 4, and 5. The same factors that weaken freedom in category 2 may also undermine political rights in categories 3, 4, and 5. Other damaging conditions may be at work as well, including civil war, very strong military involvement in politics, lingering royal power, unfair elections and one-party dominance. However, states and territories in these categories may still have some elements of political rights such as the freedom to organize nongovernmental parties and quasi-political groups, reasonably free referenda, or other significant means of popular influence on government.

6 Typically, such states have systems ruled by military juntas, one-party dictatorships, religious hierarchies and autocrats. These regimes may allow only some minimal manifestation of political rights such as competitive local elections or some degree of representation or autonomy for minorities. Category 6 also contains some countries in the early or aborted stages of democratic transition. A few states in Category 6 are traditional monarchies that mitigate their relative lack of political rights through the use of consultation with their subjects, toleration of political discussion, and acceptance of petitions from the ruled.

7 This includes places where political rights are absent or virtually nonexistent due to the extremely oppressive nature of the regime or extreme oppression in combination with civil war. A country or territory may also join this category when extreme violence and warlordism dominate the people in the absence of an authoritative, functioning central government.

Civil Liberties

1 This includes countries and territories that generally have the highest levels of freedoms and opportunities for the individual. Places in this category may still have problems in civil liberties, but they lose partial credit in only a limited number of areas.

2 Places in this category, while not as free as those in 1, are still relatively high on the scale. These countries have deficiencies in several aspects of civil liberties, but still receive most available credit.

3 , 4, and 5. Places in these categories range from ones that receive at least partial credit on virtually all checklist questions to those that have a mixture of good civil liberties scores in some areas and zero or partial credit in others. As one moves down the scale below category 2, the level of oppression increases, especially in the areas of censorship, political terror and the prevention of free association. There are also many cases in which groups opposed to the state carry out political terror that undermines other freedoms. That means that a poor rating for a country is not necessarily a comment on the intentions of the government. The rating may simply reflect the real restrictions on liberty which can be caused by non-governmental terror.

8 Typically, at category 6 in civil liberties, countries and territories have few partial rights. For example, a country might have some religious freedom, some personal social freedoms,

some highly restricted private business activity, and relatively free private discussion. In general, people in these states and territories experience severely restricted expression and association. There are almost always political prisoners and other manifestations of political terror.

9 At category 7, countries and territories have virtually no freedom. An overwhelming and justified fear of repression characterizes the society.

C. Democratic Freedoms Disaggregated: Elaboration of Freedom House's Rating Scheme in its Nations in Transit 2000

In its *Nations in Transit 2000*, Freedom House measures progress towards democratic freedoms by assessing a series of questions in six categories: (1) political process; (2) civil society; (3) independent media; (4) governance and public administration; (5) rule of law; and (6) corruption. Progress towards each category is rated on a seven-category scale, 1 representing the most advanced and 7 the least advanced.

<u>Political process</u>

(1) When did national legislative elections occur? Were they free and fair? How were they judged by domestic and international election monitoring organizations? Who composes the government?
(2) When did presidential elections occur? Were they free and fair?
(3) Is the electoral system multiparty-based? Are there at least two viable political parties functioning at all levels of government?
(4) How many parties have been legalized? Are any particular parties illegal?
(5) What proportion of the population belongs to political parties?
(6) What has been the trend of voter turnout at the municipal, provincial and national levels in recent years?

<u>Civil Society</u>

(1) How many nongovernmental organizations have come into existence since 1988? How many charitable/nonprofit organizations? How many were there last year? Are they financially viable?
(2) What forms of interest group participation in politics are legal? Which interest groups are active politically?
(3) Are there free trade unions? How many workers belong to these unions? Is the number of workers belonging to trade unions growing or decreasing?
(4) What is the numerical/proportional membership of farmers' groups, small business associations, etc?

<u>Independent Media</u>

(1) Are there legal protections for press freedoms?
(2) Are there legal penalties for libeling officials? Are there legal penalties for "irresponsible" journalism? Have these laws been enforced to harass journalists?

(3) What proportion of the media is privatized? What are the major private newspapers, television stations, and radio stations?
(4) Are the private media financially viable?
(5) Are the media editorially independent? Are the media's news gathering functions affected by interference from government or private owners?
(6) Is the distribution system for newspapers privately or governmentally controlled?
(7) What proportion of the population is connected to the Internet? Are there any restrictions on Internet access to private citizens?
(8) What has been the trend in press freedom as measured by Freedom House's *Survey of Press Freedom*?

Governance and Public Administration

(1) Is the legislature the effective rule-making institution?
(2) Is substantial power decentralized to subnational levels of government? What specific authority do subnational levels have?
(3) Are subnational officials chosen in free and fair elections?
(4) Do the executive and legislative bodies operate openly and with transparency? Is draft legislation easily accessible to the media and the public?
(5) Do municipal governments have sufficient revenues to carry out their duties? Do municipal governments have control of their own local budgets? Do they raise revenues autonomously or from the central state budget?
(6) Do the elected local leaders and local civil servants know how to manage municipal governments effectively?
(7) When did the constitutional/legislative changes on local power come into effect? Has there been a reform of the civil service code/system? Are local civil servants employees of the local or central government?

Rule of Law

(1) Is there a post-Communist constitution? How does the judicial system interpret and enforce the constitution? Are there specific examples of judicial enforcement of the constitution in the last year?
(2) Does the constitutional framework provide for human rights? Do the human rights include business and property rights?
(3) Has there been basic reform of the criminal code/criminal law? Who authorizes searches and issues warrants? Are suspects and prisoners beaten or abused? Are there excessive delays in the criminal justice system?
(4) Do most judges rule fairly and impartially? Do many remain from the Communist era?
(5) Are the courts free of political control and influence? Are the courts linked directly to the Ministry of Justice or any other executive body?
(6) What proportion of lawyers is in private practice? How does this compare with the previous year?
(7) Does the state provide public defenders?
(8) Are there effective antibias/discrimination laws, including protection of ethnic minorities?

Corruption

(1) What is the magnitude of official corruption in the civil service? Must an average citizen pay a bribe to a bureaucrat in order to receive a service? What services are subject to bribe requests--for example, university entrance, hospital admission, telephone installation, obtaining a license to operate a business, applying for a passport or other official documents? What is the average salary of civil servants at various levels?

(2) Do top policy makers (the president, ministers, vice-ministers, top court justices, and heads of agencies and commissions) have direct ties to businesses? How strong are such connections and what kinds of businesses are these?

(3) Do laws requiring financial disclosure and disallowing conflict of interest exist? Have publicized anticorruption cases been pursued? To what conclusion?

(4) What major anticorruption initiatives have been implemented? How often are anticorruption laws and decrees adopted?

(5) How do major corruption-ranking organizations like Transparency International rate this country?

MONITORING COUNTRY PROGRESS
IN CENTRAL AND EASTERN EUROPE
& EURASIA

APPENDIX II: HOUSEHOLD SURVEYS

USAID / E&E / PCS
Office of Program Coordination and Strategy
Bureau for Europe & Eurasia
U.S. Agency for International Development

May 2000

I. Introduction

This appendix looks at parts of the micro story of the transition by assessing trends from household surveys. Criticisms of some of the macro data, such as those data found in the body of the *Monitoring Country Progress*, have included two types of observations. One is that the macro numbers overestimate the extent of hardship that has been endured in many households, particularly among those in the lagging transition countries. This presumably stems in large part because the official statistics and the monetary aggregates fail to capture the significant unofficial economic activity and, more generally, household coping mechanisms. The second type of observation applies primarily to the transition leaders and argues that the quality of life as suggested by the macro statistics is actually overestimated on some dimensions. The primary logic here may be along the following lines. Relatively healthy economies do not necessarily translate into healthy and reasonably content citizens, particularly in the context of an unprecedented pace of change. Secondarily, perhaps, national aggregates oftentimes mask wide differences within countries. Taken together, these two types of observations, if true, would suggest that the differences in living conditions between those in the leading and lagging countries are not as great as suggested by the macro indicators. The household survey data should be able to partly address this working hypothesis.

There are two main parts to this appendix. The first assesses trends across much of the transition region drawing primarily from three sub-regional household surveys by the Centre for the Study of Public Policy (CSPP) at the University of Strathclyde in Glasgow in collaboration with the Paul Lazarsfeld Society in Vienna. Richard Rose is the director of the CSPP. The second section focuses on Russia and uses a time series data set from the Russia Longitudinal Monitoring Survey (RLMS). A University of North Carolina team led by Barry Popkin has coordinated all phases of the RLMS since 1992. A final section attempts to synthesize the main findings from the data.

II. Cross-country Trends

Ten of the following eleven tables of this section are drawn from at least one of three household surveys by CSPP.[1] All three surveys ask comparable questions (on economic behavior and expectations; political evaluations and governance; poverty and coping) in samples of about 1,000 respondents (or, in the case of Russia, at least 2,000). The intent of the sampling procedure was to pick a sample of respondents that is statistically reliable for generalizing to national populations. In each country, face-to-face interviews were conducted by an established survey institute according to a multi-stage random probability sample stratified by regions, urban and rural population and small administrative districts (e.g., a ward or village) that can serve as a primary sampling unit. Within each primary sampling unit an average of ten interviews were conducted;

[1] *Table 10* examines food expenditures as a percent of total consumption by drawing from a data set used by the UNDP in its *Transition 1999: Human Development Report for Europe & the CIS* (1999).

respondents were drawn from a register of residents or households by an appropriate random method, such as selecting within the household the next member to have a birthday.[2]

The *New Democracies Barometer* (NDB) began in 1991 and now covers eleven transition countries from the Europe and Eurasia region: Belarus; Bulgaria; Croatia; the Czech Republic; Hungary; Poland; Romania; Slovakia; Slovenia; Yugoslavia; and Ukraine. There have been five NDB rounds of surveys; the most recent during the winter and spring of 1998. The three Baltic countries are included in the *New Baltic Barometer (NBB)*. There have been three NBB rounds; in 1993, 1995 and 1996. Trends in Russia have been addressed in the *New Russia Barometer* (NRB). There have been seven rounds of the NRB from 1992 to 1998.[3]

The tables that follow look first at various political aspects of the transition followed by perceptions about the economic situation and expenditure patterns. While most of the Eurasian countries are not represented in these samples, the large majority of the population in Eurasia (seventy three percent, or those populations of Russia, Ukraine, and Belarus) is included. The 1998 responses pre-date the Russian August 1998 devaluation and crisis.

Table 1 underscores that the gains in many aspects of political freedoms, the "easy" gains, have been very impressive across much of the transition region. Specifically, citizens in fifteen countries were asked if political freedoms have increased since communist days in terms of feeling free to: (a) say what one thinks; (b) join any organization one wants; (c) take an interest in politics (or to be apolitical); and (d) practice a religion. The variation of the responses to each question in each country was relatively small and the responses to the four questions were hence averaged for each country. On average, eighty percent of the sample in the fifteen countries felt that these political freedoms were greater under the existing political system than they were under communism, and almost one-half felt the situation was much better "now."[4] Only three percent of the total sample felt these freedoms were greater in the communist days. Moreover, there is relatively little variation of results across the countries; these sentiments are shared fairly uniformly across the fifteen countries.[5]

Table 2 attempts to quantify progress in the gains in political freedoms that stem from better governance; in effect, second stage political freedoms. People in eleven countries were asked in 1998 how the political system compared then to that in the communist days

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[2] R. Rose and C. Haerpfer, *New Democracies Barometer V: A 12-Nation Survey*, CSPP, #306 (1998), p. 7.
[3] For further elaboration of the methodology of the CSPP surveys, see their web site at http://www.strath.ac.uk/Departments/CSPP/.
[4] The respondents in the three Baltic countries answered these questions in 1996; all others answered them in 1998.
[5] It may be worth noting that the particular answers in some of the following tables reflect change and not the level of progress. Hence, for example, it is likely that the gains in political freedoms depicted in *Table 1* are greatest in Romania in no small part because the political climate in Romania during communism (that is, under Ceausescu) was more oppressive than in most countries included in the sample.

in three ways: (a) can ordinary citizens influence what government does? (b) can people live without fear of unlawful arrest? and (c) are people treated equally and fairly by the government? As expected, progress in these types of freedoms is much more modest than the easier political gains depicted in *Table 1*. Overall, less than half (forty-one percent) of the respondents saw gains in these freedoms since communist days, and only sixteen percent felt the progress was much better. As measured, twenty percent felt that political freedoms from better governance have decreased since communism. Moreover, the variation across countries is large. In Ukraine, more people feel that these second stage freedoms were greater under communism than they are now. In Romania, over seventy percent of the respondents see advancement in these freedoms while only twelve percent feel the situation has worsened.

Table 3 looks at perceptions of corruption and underscores the challenges of better governance. In all countries surveyed, a majority of persons sampled say the level of corruption and the taking of bribes has increased during the transition. Overall, one half of those polled say it has increased a lot, and only five percent say it has decreased. The perceived increase is the greatest in Ukraine, followed by Romania, Yugoslavia, and Slovakia. Results are only marginally more encouraging in the Northern Tier CEE countries than elsewhere.

Corruption and governance are examined from a somewhat different angle in *Table 4* and *Figure 1*. Here an attempt is made to measure peoples' trust in institutions (and in people), an important aspect of social capital.[6] Respondents were asked their degree of trust in a variety of government institutions (including the police, the courts, civil servants, and parliament) and institutions of civil society (church, press, trade unions) as well as private enterprise and even people in general.[7] In sum, trust is very low and this aspect of social capital is quite weak, particularly as pertains to government institutions. As measured, roughly three out of four persons sampled across the countries have little to no trust in key government institutions. The least trust is given to parliament, though civil servants, courts, and police similarly inspire little. Trust in government institutions is lowest in the Eurasian countries of Ukraine and Russia. Trust in civil servants and parliament is strikingly low in Ukraine: only four percent of those polled in Ukraine have at least a modicum of faith in civil servants, and eight percent in parliament. However, mistrust in formal institutions is also a characteristic to varying degrees in Central and Eastern Europe.

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[6] The EBRD refers to social capital as "informal institutions" or the basic codes of conduct, trust, and co-operative behavior. See EBRD, *Transition Report 1999* (November 1999), p.5.

[7] Respondents were trusting if their answer was in the top three categories of a seven-point scale, where one represents no trust and seven great trust.

Civil society institutions fare somewhat better, particularly the church and to a lesser extent the press. Mistrust is not primarily directed to government, however. Private enterprise continues to be viewed with a great deal of skepticism by many, particularly in Russia and Ukraine where crime and corruption and mafia connections are pervasive. Overall, roughly three-fourths of all surveyed in the twelve countries expressed little trust in private enterprise.

Table 5 captures some of this skepticism in institutions by comparing popular evaluations of political regimes in 1996 in the Baltic countries and 1998 elsewhere with that of pre-transition regimes. Overall, the approval ratings of past, communist regimes are slightly higher than approvals of the more recent political regimes, though variation is great across countries. Approval of the recent regime is highest in Poland and Romania (both at sixty-six percent), and lowest in Ukraine (twenty-two percent) and Croatia (twenty-seven percent)[8]. Approval of the pre-transition communist regime is highest in the three Eurasian countries surveyed (Ukraine at eighty-two percent, Russia at seventy-two percent, and Belarus at sixty percent) as well as in Yugoslavia (sixty-two percent).

Perceptions of economic conditions are captured in *Tables 6* and *7* (and *Figure 2*). The majority of persons sampled (sixty four percent) felt their economic situation in 1998 was worse than it was five years earlier (*Table 6*). It is striking, particularly given that five of the twelve countries in this average are Northern Tier CEE countries, that only one in six persons felt it had gotten better. Perceptions of trends in economic conditions are the most dismal in Ukraine (only four percent saw an improvement) and the most favorable in the Czech Republic (where twenty-nine percent saw an improvement). Some cross-country results may be surprising. Perceptions of economic conditions in Russia are relatively favorable, second only to the Czech Republic by this measure, though these perceptions pre-date the August 1998 crisis. In contrast, perceptions in Hungary are strikingly pessimistic; seventy-two percent of those polled in Hungary felt that their economic situation in 1998 had deteriorated since 1993, while only eight percent saw improvement.

Table 7 shows a higher level of satisfaction in current economic conditions than would seem to be implied in the data of *Table 6*, revealing that people's expectations may actually be quite low. In particular, while only one in six persons see improvement in economic conditions since 1993, twice that number of people, or one in three, nevertheless are satisfied with their current economic situation. However, very few persons (only three percent) are very satisfied. The results differ greatly across the countries. A majority of persons in Slovenia and the Czech Republic are satisfied. Satisfaction levels in Poland, Slovakia, and (oddly) Belarus not far behind.[9] To contrast, only one in ten persons in Bulgaria were satisfied with their economic situation in 1998; and only fifteen percent in Ukraine.

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[8] The "recent" regime in Croatia refers to the previous government run by Franjo Tudjman.

[9] Perhaps expectations in Belarus are particularly low. Only nine percent of Belarusians sampled saw an improvement in their economic condition. Yet, forty-three percent were satisfied!

Do these generally discouraging perceptions of economic conditions and relatively favorable views of past communist regimes translate into a desire to go back to communism? For most people, it does not (*Table 8* and *Figure 3*). Roughly, only one in five persons in the CEE countries polled want to see communism return. In the three Eurasian countries, however, the percentage is considerably higher, from thirty-three percent in Belarus to fifty-one percent in Ukraine. Moreover, virtually all the countries for which time series are available have witnessed an increase in the proportion of the population wishing for a return to communism since 1995. Only in Bulgaria, do the data show a decrease. In Russia, support for communism has steadily increased from twenty-seven percent of the population polled in 1994 to forty-one percent in 1998.

The prevalence of informal economic activity and private safety nets to help mitigate the high costs incurred from the transition are a significant reason often cited as to why there aren't more people seeking a return to the past and/or more aggressively blocking change towards the new system. *Table 9* provides some support for this view. According to these data, not many households can survive adequately on formal employment alone. On average, only about twenty percent of the households of the fifteen countries sampled are able to make the necessary purchases from the income derived from jobs in the formal economy alone. However, when one combines formal economic activity with participation in the informal economy (both monetary gains and barter activities), one finds that almost seventy percent of all the households polled are able to get by without drawing on savings or going excessively into debt. Market employment contributes more to the household's livelihood in the Northern Tier CEE countries than it does elsewhere, particularly in Eurasia. However, *Table 9* also suggests that informal economic activity is important for a significant portion of households in the Northern Tier CEE countries as well as those in the other subregions.

Table 9 also gives us some basis to judge the credibility of poverty estimates based on income. Those households which are engaged in "unsustainable" coping strategies (that is, drawing on savings and/or borrowing significantly) are headed toward poverty if they are not already in poverty. Generally, however, the proportion in poverty should be some subset of these households, and certainly no greater. In this context, how do the income-based poverty estimates given in the body of this *Monitoring Country Progress* compare to the percent of "unsustainable" households of *Table 9*?[10] In a handful of countries, the proportion of those estimated to be in poverty exceeds the proportion of those with unsustainable strategies. In other words, income-based poverty estimates look to be overestimates by this account. This includes two Baltic countries (Estonia and to a lesser extent, Lithuania), as well as Ukraine and Russia.[11]

[10] The income-based poverty estimates used in the body of this paper are from B. Milanovic, *Income, Inequality, and poverty during the Transition from Planned to Market Economy* (World Bank, 1998). The poverty rate is defined as the percentage of the population below the poverty line of $120 per capita per month at 1990 international prices.

[11] In Ukraine, for example, the percent of households with unsustainable coping strategies is fifty-seven percent. This suggests that the poverty rate in Ukraine should be something short of that. Yet, the income-based poverty rate (as of 1995) was estimated to be sixty-three percent.

On the other hand, income-based poverty estimates in some of the Northern Tier CEE countries may be understating the hardships that are being incurred. In the Czech Republic, Hungary, Slovenia, and Slovakia, income-based poverty (as of 1995) was estimated to be negligible, from one to two percent of the population. Yet, the percent of the population in these countries which is not coping sustainably ranges from nineteen percent in the Czech Republic to twenty-nine percent in Slovakia.

Table 10 gives us another rough proxy for poverty rates and trends. Food expenditures as a percent of total consumption are calculated by the UNDP for eighteen transition countries for much of the transition period. High proportions of food expenditures signal hardships. Poor households will typically spend fifty percent or more on food. On average, a sample of households in these eighteen countries spent thirty-five percent of their budget on food at the outset of the transition. This did not vary greatly between the transition subregions. However, since then, from roughly 1990 to 1997, food expenditures as a percent of total consumption have risen significantly in Eurasia, moderately in the Southern Tier CEE countries, and only marginally in the Northern Tier CEE countries. Food consumption is proportionately highest in Azerbaijan (seventy-eight percent), followed by Moldova (sixty-eight percent), suggesting considerable hardships. In two countries, Slovenia and Poland, the proportion of household expenditures on food declined from 1990 to 1997, suggesting improvements in living standards. In Hungary, the percentage share of household consumption of food was the same (at thirty-three percent) in 1997 as it was in 1991.

Finally, *Table 11 s*hows the percentage of households in 1998 in twelve countries having to often do without food, heating and electricity, and necessary clothing. For the CEE countries, the percentage of households often doing without necessity goods is low. This is particularly the case for food (three percent often did without food over the course of the month in 1998 prior to being interviewed) and heating and electricity (also three percent). Twelve percent of those sampled in the CEE countries had to often make do without purchasing needed clothes. By these measures, households in Bulgaria endured much higher hardships than in other CEE countries; thirty-six percent of Bulgarian households sampled, for example, had to often do without needed clothing. Hardships have also been significantly higher in the three Eurasian countries polled: Belarus, Russia, and Ukraine. By this norm, living standards are far lower in Ukraine than in any of the other countries sampled; more than forty percent of Ukrainian households had to often do without food and close to sixty percent without needed clothing.

Appendix II, Part I: Cross-Country Surveys

Table 1. The gains in the "easy" political freedoms (% of respondents)

How does the present political system compare to that in the communist days?
The average response to four statements:

(1) Everybody is free to say what he or she thinks.
(2) People can join any organization they want.
(3) Each person can decide whether or not to take an interest in politics.
(4) Everybody is free to decide whether or not to practice a religion.

	Much worse now	Somewhat worse	Worse	Much better now	Somewhat better	Better
Romania	0	2	2	68	23	92
Lithuania						85
Bulgaria	1	2	3	53	31	84
Czech R.	0	2	2	51	33	84
Latvia	…	…	…	…	…	83
Poland	0	2	2	48	34	82
Slovakia	1	2	3	50	32	81
Estonia	…	…	…	…	…	81
Hungary	0	2	2	49	31	80
Yugoslavia	2	3	6	39	40	79
Slovenia	2	3	4	38	36	74
Ukraine	1	3	4	39	35	74
Russia	…	…	…	…	…	73
Belarus	1	2	3	39	33	72
Croatia	2	4	6	33	36	69
CEE & Eurasia (n=11 or 15)	1	2	3	46	33	80
N.Tier CEE (n=8)	…	…	…	…	…	81
S.Tier CEE (n=4)	…	…	…	…	…	81
Eurasia (n=3)	…	…	…	…	…	73

R. Rose & C. Haerpfer, *New Democracies Barometer V: A 12-Nation Survey* , CSPP, #306 (1998); Rose, *New Russia Barometer Trends Since 1992* , CSPP, #320 (1999); Rose, *Baltic Trends: Studies in Co-operation, Conflict, Rights and Obligations* , CSPP, #288 (1997).

Responses were provided in 1996 by the Baltic participants; 1998 by all others. Countries are given equal weight in the sub-regional averages in all the tables of this appendix.

Table 2. The gains in political freedoms from better governance (as % of respondents)

How does the political system in 1998 compare to that in the communist days?
The average response to three statements:
(1) Ordinary people can influence what government does.
(2) People can live without fear of unlawful arrest.
(3) Everybody is treated equally and fairly by the government.

	Much worse now	Somewhat worse	Worse	Much better now	Somewhat better	Better
Romania	4	8	12	43	28	71
Poland	4	8	12	21	31	52
Bulgaria	6	9	15	19	28	47
Slovenia	6	12	18	17	26	43
Czech R.	6	15	21	12	30	42
Hungary	7	10	16	15	25	40
Yugoslavia	11	15	26	9	26	35
Slovakia	11	16	26	8	25	33
Croatia	10	12	22	11	21	32
Belarus	6	9	15	11	19	29
Ukraine	17	16	33	10	14	24
CEE & Eurasia (n=11)	8	12	20	16	25	41
N.Tier CEE (n=5)	7	12	19	14	27	42
S.Tier CEE (n=4)	8	11	19	21	26	46
Eurasia (Belarus & Ukraine)	11	13	24	10	17	27

R. Rose & C. Haerpfer, *New Democracies Barometer V: A 12-Nation Survey* , CSPP, #306 (1998).

Table 3. Perceptions of corruption in 1998 (% of respondents)

By comparison with the former Communist regime, would you say that the level of corruption and taking bribes has:

	Decreased a lot	Decreased a little	Decreased	Same	Increased a lot	Increased a little	Increased
Poland	1	11	12	37	28	24	52
Slovenia	6	8	14	28	35	23	58
Croatia	1	5	6	28	44	22	66
Czech R.	0	5	5	24	44	26	70
Belarus	1	4	5	25	54	16	70
Bulgaria	---	3	3	25	49	22	71
Hungary	0	2	2	20	58	19	77
Slovakia	1	3	4	15	55	26	81
Yugoslavia	0	2	2	17	64	17	81
Romania	1	2	3	12	66	19	85
Ukraine	0	1	1	11	75	12	87
CEE & Eurasia (n=11)	1	4	5	22	52	21	73
N.Tier CEE (n=5)	2	6	7	25	44	24	68
S.Tier CEE (n=4)	1	3	4	21	56	20	76
Eurasia (Belarus & Ukraine)	1	3	3	18	65	14	79

R. Rose & C. Haerpfer, *New Democracies Barometer V: A 12-Nation Survey* , CSPP, #306 (1998).

Table 4. Trust in Formal Institutions

Percent trusting government institutions in 1998:

	Police	Courts	Civil Servants	Parliament	Average
Romania	41	40	50	31	41
Croatia	47	39	34	26	37
Hungary	35	39	32	25	33
Slovakia	30	35	28	25	30
Poland	32	30	28	25	29
Slovenia	34	29	34	20	29
Czech R.	29	25	27	15	24
Belarus	21	28	11	28	22
Bulgaria	27	19	18	21	21
Yugoslavia	24	17	19	18	20
Russia	18	24	---	13	18
Ukraine	12	15	4	8	10
CEE & Eurasia (n=12)	29	28	26	21	26
N.Tier CEE (n=5)	32	32	30	22	29
S.Tier CEE (n=4)	35	29	30	24	29
Eurasia (n=3)	17	22	8	16	17

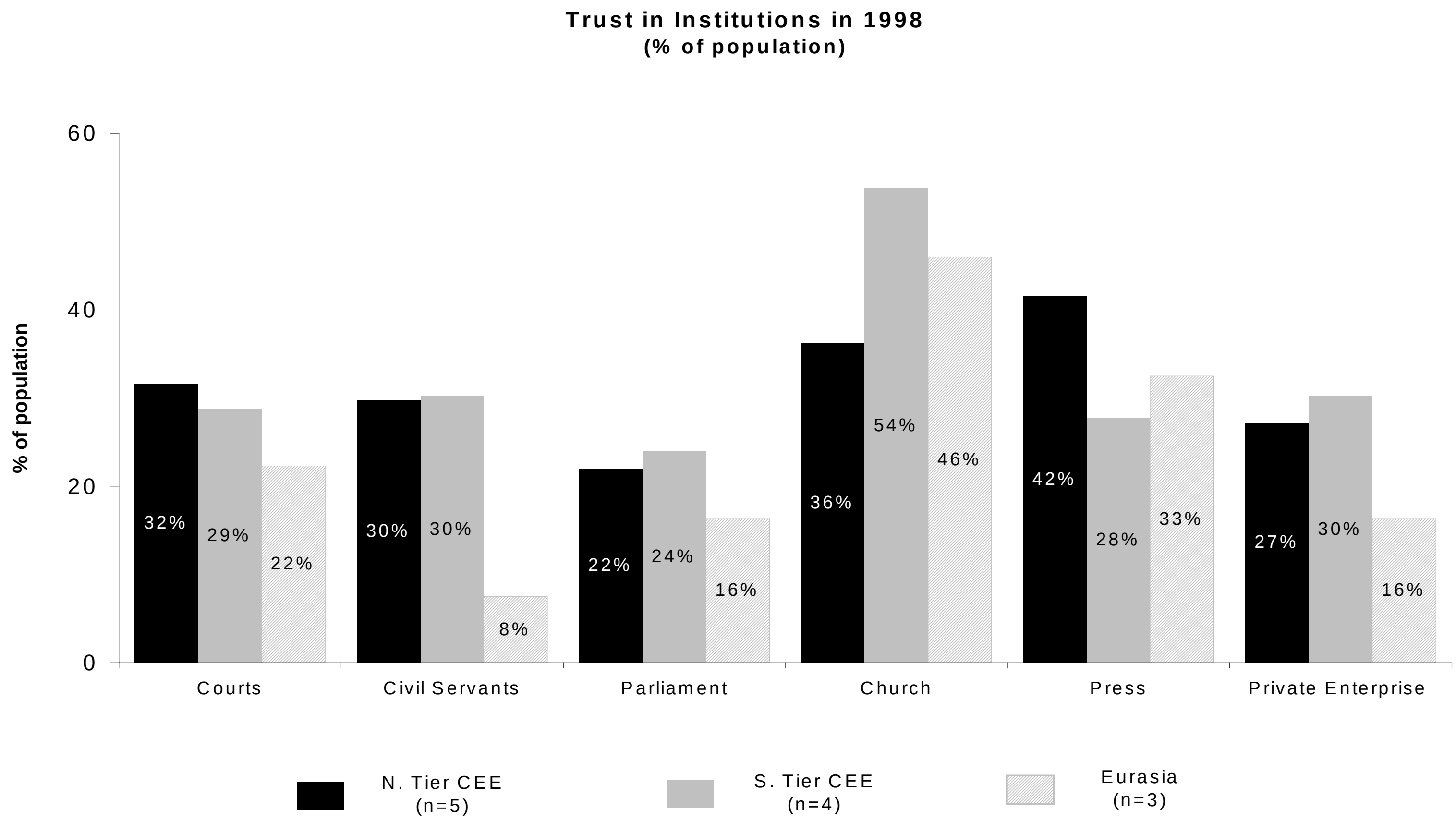
Percent trusting civil society & private sector in 1998:

	People	Church	Press	Trade Unions	Private Enterprise	Average
Romania	35	77	46	34	45	47
Belarus	67	60	36	24	22	42
Czech R.	55	29	48	28	34	39
Poland	52	51	42	26	21	38
Croatia	57	56	20	31	26	38
Hungary	52	37	42	15	32	36
Yugoslavia	53	56	18	15	28	34
Ukraine	63	48	29	14	16	34
Slovenia	50	22	42	25	27	33
Slovakia	39	42	34	28	22	33
Bulgaria	39	26	27	12	22	25
Russia	---	30	---	14	11	18
CEE & Eurasia (n=12)	51	45	35	22	26	35
N.Tier CEE (n=5)	50	36	42	24	27	36
S.Tier CEE (n=4)	46	54	28	23	30	36
Eurasia (n=3)	65	46	33	17	16	31

R. Rose & C. Haerpfer, *New Democracies Barometer V: A 12-Nation Survey* , CSPP, #306 (1998); Rose, *New Russia Barometer Trends Since 1992* , CSPP, #320 (1999).

Respondents were trusting if their answer was in the top 3 categories of a 7 point-scale, where 1 represents no trust and 7 great trust.

Figure 1.



Data are from two household surveys: R. Rose & C. Haerpfer, *New Democracies Barometer V: A 12-Nation Survey*, CSPP, #306 (1998); and Rose, *New Russia Barometer Trends Since 1992*, CSPP, #320 (1999). Northern Tier CEE countries are the Czech Republic, Poland, Slovenia, Slovakia, and Hungary; Southern Tier CEE countries are Romania, Bulgaria, Croatia, and Yugoslavia; and Eurasia countries are Russia, Belarus, and Ukraine.

Respondents were trusting if their answer was in the top 3 categories of a 7 point-scale, where 1 represents no trust and 7 great trust.

Table 5. Popular evaluations of political systems: pre-transition & current

I. Where approval of current regime is greater than that of the pre-transition regime.

	Percent approving of:	
	Pre-transition regime	Current regime
Poland	30	66
Romania	38	66
Estonia	38	62
Bulgaria	43	58
Czech R.	31	56
Slovenia	42	51
Slovakia	46	50

II. Where approval of current regime is less than that of the pre-transition regime.

	Percent approving of:	
	Pre-transition regime	Current regime
Hungary	58	53
Belarus	60	48
Lithuania	48	39
Russia	72	36
Latvia	53	34
Yugoslavia	62	33
Croatia	41	27
Ukraine	82	22
CEE & Eurasia (n=15)	50	47
N.Tier CEE (n=8)	43	51
S.Tier CEE (n=4)	46	46
Eurasia (n=3)	71	35

R. Rose & C. Haerpfer, *New Democracies Barometer V: A 12-Nation Survey* , CSPP, #306 (1998); Rose, *New Russia Barometer Trends Since 1992* , CSPP, #320 (1999); Rose, *Baltic Trends: Studies in Co-operation, Conflict, Rights and Obligations* , CSPP #288 (1997).

Data are for 1996 for the 3 Baltic countries; 1998 elsewhere.

Table 6. Perceptions of economic conditions: 1998 vs. 1993

How does your current economic situation compare to that of 5 years ago?

	Worse	Same	Better
Czech R.	46	26	29
Russia	56	16	28
Poland	50	24	26
Slovenia	50	28	22
Romania	59	20	21
Bulgaria	60	19	21
Slovakia	54	27	19
Croatia	70	18	12
Belarus	79	12	9
Hungary	72	19	8
Yugoslavia	86	8	5
Ukraine	90	6	4
CEE & Eurasia (n=12)	64	19	17
N.Tier CEE (n=5)	54	25	21
S.Tier CEE (n=4)	69	16	15
Eurasia (n=3)	75	11	14

R. Rose & C. Haerpfer, *New Democracies Barometer V: A 12-Nation Survey* , CSPP, #306 (1998);
Rose, *New Russia Barometer Trends Since 1992* , CSPP, #320 (1999).

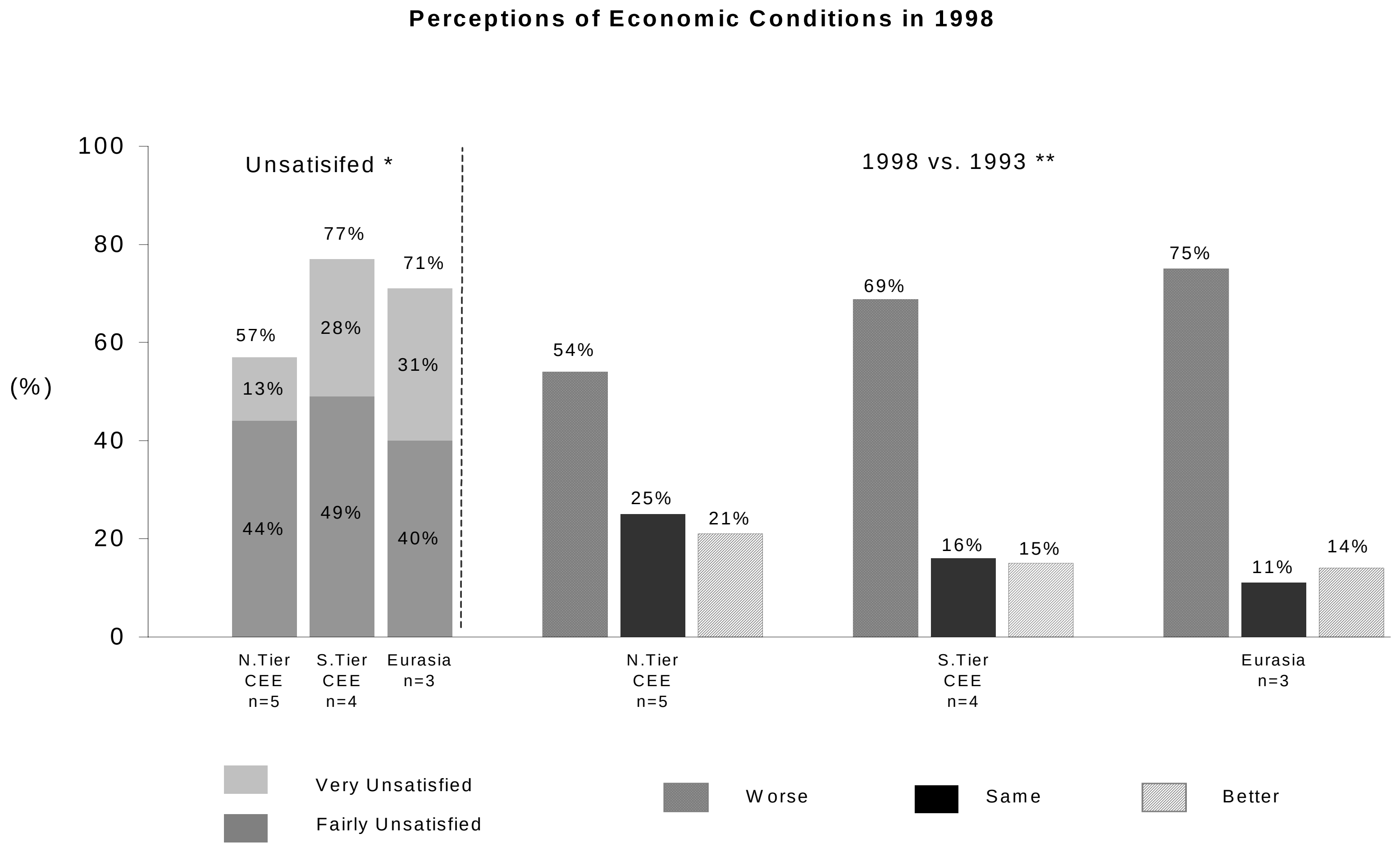
Table 7. Perceptions of economic conditions in 1998

How do you rate your household's economic situation today?
Percentage of respondents who feel it is:

	Very unsatisfactory	Fairly unsatisfactory	Unsatisfactory	Very satisfactory	Fairly satisfactory	Satisfactory
Slovenia	7	40	47	8	46	54
Czech R.	8	39	47	2	50	52
Poland	12	44	56	2	42	44
Belarus	19	39	58	6	37	43
Slovakia	9	51	60	3	38	41
Romania	16	50	66	3	30	33
Russia	18	54	72	1	26	27
Croatia	31	45	76	4	21	25
Hungary	29	47	76	1	23	24
Yugoslavia	28	49	77	2	20	22
Ukraine	57	27	84	2	13	15
Bulgaria	38	52	90	1	9	10
CEE & Eurasia (n=12)	23	45	67	3	30	33
N.Tier CEE (n=5)	13	44	57	3	40	43
S.Tier CEE (n=4)	28	49	77	3	20	23
Eurasia (n=3)	31	40	71	3	25	28

R. Rose & C. Haerpfer, *New Democracies Barometer V: A 12-Nation Survey* , CSPP, #306 (1998); Rose, *New Russia Barometer Trends Since 1992* , CSPP, #320 (1999).

Figure 2.



* "How do you rate your household's economic situation today?" ** "How does your current economic situation compare to that of 5 years ago?"

Data are from two household surveys: R. Rose & C. Haerpfer, *New Democracies Barometer V: A 12-Nation Survey*, CSPP, #306 (1998); and Rose, *New Russia Barometer Trends Since 1992*, CSPP, #320 (1999). Northern Tier CEE countries are the Czech Republic, Poland, Slovenia, Slovakia, and Hungary; Southern Tier CEE countries are Romania, Bulgaria, Croatia, and Yugoslavia; and Eurasia countries are Russia, Belarus, and Ukraine.

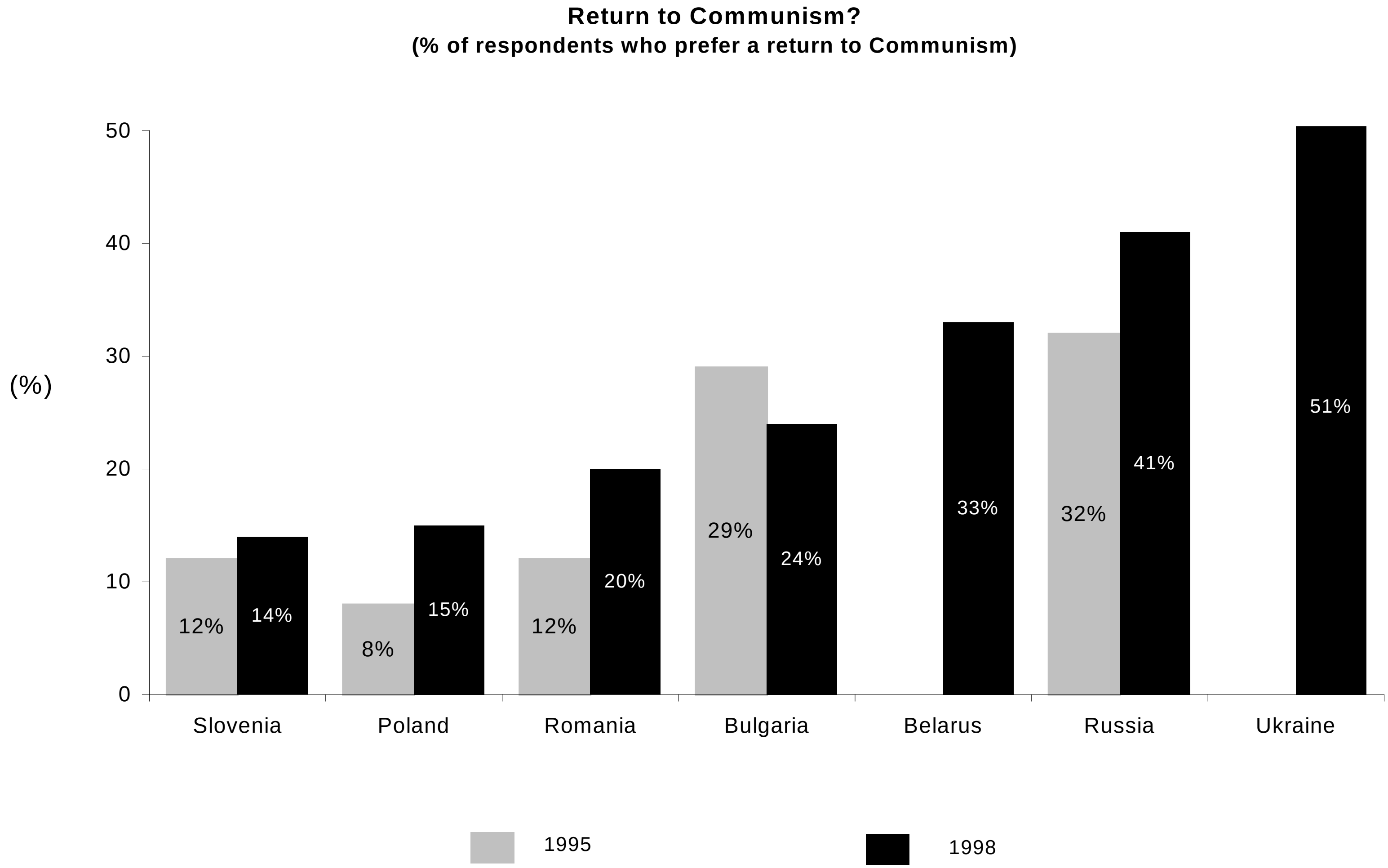
Table 8. Return to communism?

Percent of respondents who prefer a return to communism:

	1994	1995	1996	1998
Baltics (n=3)	---	6	6	---
Slovenia	---	12	---	14
Croatia	---	---	---	14
Poland	---	8	---	15
Czech R.	---	10	---	16
Romania	---	12	---	20
Hungary	---	20	---	23
Bulgaria	---	29	---	24
Slovakia	---	19	---	29
Yugoslavia	---	---	---	30
Belarus	---	---	---	33
Russia	27	32	39	41
Ukraine	---	---	---	51
N.Tier CEE (n=5)	---	---	---	19
S.Tier CEE (n=4)	---	---	---	22
Eurasia (n=3)	---	---	---	42

R. Rose & C. Haerpfer, *New Democracies Barometer V: A 12-Nation Survey* , CSPP, #306 (1998); Rose, *New Russia Barometer Trends Since 1992* , CSPP, #320 (1999); Rose, *Baltic Trends: Studies in Co-operation, Conflict, Rights and Obligations* , CSPP, #288 (1997).

Figure 3.



Data are from two household surveys: R. Rose & C. Haerpfer, *New Democracies Barometer V: A 12-Nation Survey* , CSPP, #306 (1998); and Rose, *New Russia Barometer Trends Since 1992* , CSPP, #320 (1999).

Table 9. Household Coping Strategies

	Percent of respondents w/ sustainable strategies			Percent w/
	(a) w/ job alone	(b) with portfolio	total	un-sustainable strategies
Czech R.	35	46	81	19
Hungary	22	57	79	21
Poland	25	52	77	22
Yugoslavia	30	45	75	26
Estonia	30	43	73	27
Slovenia	33	40	73	27
Lithuania	30	42	72	28
Latvia	16	55	71	29
Slovakia	30	41	71	29
Croatia	14	55	69	31
Belarus	15	49	64	36
Russia	11	52	63	37
Romania	8	46	54	46
Bulgaria	9	45	54	47
Ukraine	4	39	43	57
CEE & Eurasia (n=15)	21	47	68	32
N.Tier CEE (n=8)	28	47	75	25
S.Tier CEE (n=4)	15	48	63	38
Eurasia (n=3)	10	47	57	43

R. Rose & C. Haerpfer, *New Democracies Barometer V: A 12-Nation Survey* , CSPP, #306 (1998); Rose, *New Russia Barometer Trends Since 1992* , CSPP, #320 (1999); Rose, *Baltic Trends: Studies in Co-operation, Conflict, Rights and Obligations* , CSPP, #288 (1997).

Data are for 1996 for the 3 Baltic countries; 1998 elsewhere. Coping with job alone means sufficient income from regular job to buy needed things. With portfolio: while household does not earn enough from regular jobs (to avoid dissavings), it does so with a combination of official and informal economic activities. Unsustainable strategies: savings are being spent and/or money is borrowed.

Table 10. Food expenditures
(% of total consumption)

	1990/91	1992	1994	1996/97	1990-97 change
Slovenia	25	26	26	23	-2
Slovakia	28	30	32	32	4
Poland	48	40	35	33	-15
Hungary	33	---	34	33	0
Estonia	---	---	---	39	---
Russia	29	41	39	39	10
Macedonia	---	45	45	45	---
Yugoslavia	36	46	51	47	11
Latvia	---	---	---	48	---
Kyrgyzstan	33	49	49	49	16
Belarus	27	33	49	51	24
Lithuania	34	59	57	52	18
Bulgaria	38	43	45	54	16
Turkmenistan	36	39	52	54	18
Ukraine	---	---	---	57	---
Romania	---	---	---	58	---
Moldova	---	---	---	68	---
Azerbaijan	53	64	74	78	25
CEE & Eurasia	35	43	45	48	10
N.Tier CEE	34	39	37	37	4
S.Tier CEE	37	45	47	51	14
Eurasia	36	45	53	57	21

UNDP, Transition 1999: Human Development Report for Europe & the CIS (1999).

Table 11. Consumption of necessities

Percentage of households in 1998 having to often do without:

	Food	Heating & Electricity	Necessary Clothing
Slovenia	1	0	2
Slovakia	3	1	7
Croatia	1	4	7
Romania	4	3	7
Czech R.	2	3	8
Poland	4	3	11
Yugoslavia	2	2	16
Hungary	5	4	16
Belarus	15	2	28
Russia	19	5	32
Bulgaria	9	10	36
Ukraine	42	15	59
CEE (n=9)	3	3	12
Eurasia (n=3)	25	7	40

R. Rose & C. Haerpfer, *New Democracies Barometer V: A 12-Nation Survey* , CSPP, #306 (1998); Rose, *New Russia Barometer Trends Since 1992* , CSPP, #320 (1999).

III. Russia

The following ten tables draw from the Russia Longitudinal Monitoring Survey (RLMS) and analyze economic and health trends in Russia in some detail. The RLMS has been coordinated by a University of North Carolina team led by Barry Popkin and has had two phases of a total of eight survey rounds since 1992. A focus of Phase I (rounds I-IV) was to help build the institutional capacity within Russia, primarily with the Russian State Statistical Bureau (Goskomstat), to create a truly nationally representative sample. Roughly, 7,000 households were surveyed in two hundred secondary sampling regions found within twenty primary sampling units throughout Russia during these rounds. During Phase II (rounds V-VIII), which began in 1994, the sample size decreased (to a minimum of 4,000 households), but the number of primary sampling units was doubled to enhance the representativeness of the survey. Interviews during each round were completed with the original sample dwelling unit. While there was some turnover of residences in these dwellings, this method did allow for some panel analysis; that is, tracking the behavior and responses of the same people over time.[12]

Table 12 and *Figure 4* look at how household income is derived and how that has changed during the transition in Russia through November 1998.[13] Foremost among the trends observed is the significant drop in the proportion of public sector income in Russian households from forty-seven percent in 1992 to twenty-eight percent in 1998. This in itself suggests significant economic restructuring over this period. However, much of the re-orientation of income sources has gone from the public sector to the informal economy, and particularly to the noncash or barter economy. The informal economy represented nine percent of household income in 1992 and twenty-three percent in 1998. While the proportion of official private sector wages increased from 1992-1998, this income remained only eight percent of household income on average in 1998. Government transfers remained large; thirty-one percent of total household income in 1992 and the same in 1998. Roughly, one-third of household income for the average Russian is from formal economy wages, one-third is from the informal sector plus family and private transfers, and one-third is from government transfers.

Table 12 (with *Figure 5)* also looks at these income categories for the top and bottom population quintiles by income in 1998. The poorest Russians are more dependent on the informal economy (particularly the barter or non-monetary activities of the informal economy) and private safety nets; over forty percent of income derives from these sources. Moreover, twenty-five percent of their income comes from government transfers. This is below the national average (of thirty-one percent) and reveals that government assistance is not targeted on the most vulnerable. Lastly, the Russians with the highest income receive a higher proportion of private sector wages (fourteen percent), but are also very much involved in informal economic activities (twenty-six percent of income). Both proportions are above the national average.

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[12] Further elaboration of RLMS' method is found at the following web site: http://www.cpc.unc.edu/projects/rlms/.

[13] The last round (of November 1998) hence captures some of the impact from the crisis triggered by the August 1998 devaluation.

Income-based poverty, countrywide and within six major regions in Russia, is examined in *Table 13* and *Figure 6*. The poverty measures adjust for regional prices and food baskets, and household economies of scale. Extreme poverty is defined as income less than fifty percent of the poverty line. RLMS estimates that thirty-nine percent of Russians were poor in November 1998.[14] This is a significant increase from an eleven percent poverty rate in 1992, though the pace of increase has slowed since 1996. Extreme or deep poverty increased disproportionately to almost one-half of all those considered poor. In 1998, this translated into roughly seventeen percent of the total population.

Children are particularly vulnerable. Over half of all children surveyed in 1998 were poor, and almost one-half of them were in extreme poverty. To contrast, the poverty rate of pensioners is, at twenty-six percent, considerably below the national average. Moreover, the poverty rate of the elderly has declined since 1996. There are also proportionately fewer of the elderly in deep poverty.

Perhaps the most striking observation as regards the subregional poverty rates is the absence of significant differences in poverty rates across geographic regions in Russia. In particular, four of the six regions have poverty rates that are quite close to each other, and to the national average (ranging from thirty-seven to forty percent). The two regional exceptions are no surprise. Poverty is lowest in Moscow and St. Petersburg areas; twenty-two percent in 1998, and highest (at forty-seven percent) in the North Caucasus region.

Labor market trends are examined in *Table 14* and *Figure 7*. Open unemployment continues to rise in Russia, and in 1998 was close to eleven percent according to RLMS.[15] It is commonly observed that more workers than that are effectively without wages, either because they have been put on involuntary unpaid leave or because they are owed wages. When one factors these workers into the picture, one finds that more than twenty-eight percent of the workforce in November 1998 was without wages for at least the past month. However, hidden unemployment (those on involuntary unpaid leave) has become relatively insignificant. In 1992, it was 2.6 percent of the workforce, about one-half the open unemployment rate. In 1998, however, it was less than one percent of the work force, or about only five percent of open unemployment. Wage arrears, in contrast, were high in 1998 (seventeen percent of the sampled workforce had not been paid in the month prior to being interviewed), though not as high as they were in 1996 (over twenty-one percent). By November 1998, sixty-four percent of the labor force had wages owed to them. Labor force participation has dropped from eighty-seven percent in 1992 to almost eighty-three percent in 1998, a trend which is consistent with a growing informal economy.

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[14] This is somewhat below the estimate of 44% in 1995 provided in the body of Monitoring *Country Progress* and drawn from Branko Milanovic from the World Bank.

[15] The EBRD in its *Transition Report 1999* calculates official unemployment to be 12.4% in 1998.

Expenditure patterns are explored in *Tables 15* through *18* and *Figures 8* and *9*. *Table 15* examines household expenditures in constant rubles (that is, discounted for inflation) disaggregated by key categories. *Table 16* and *Figure 8* measure these same categories but as a proportion of total expenditures. From *Table 15*, we see overall household expenditures initially rose from 1992 to 1994, perhaps as a function of pent-up demand and stockpiled rubles "under the mattress." However, since 1994, overall household expenditures have fallen greatly; thirty percent from 1992 to 1998, and twenty-four percent from only October 1996 to November 1998. Since 1996, in fact, expenditures fell across the board except for the home production of food.

Table 16 shows the significant increase in home production of food in proportionate terms, from six percent of all household expenditures on average in 1992 to thirteen percent in 1998. Total food consumption is very high, though declining by RLMS measures.[16] In 1998, more than one-half of household expenditures was devoted to food. For the bottom quintile of the Russian population, this proportion is much higher still, close to seventy percent, suggesting significant hardship.

Table 17 looks at Russians' ownership of durable goods and provides for a more tangible feel of living standards trends, at least for some Russians. While a growing and significant portion of the Russian population has fallen into poverty since the transition began, the data of *Table 17* suggest a more encouraging counter-balancing trend: namely, a growing and significant portion of Russians have also been benefiting in important respects. In particular, from 1992 to 1998, almost twenty percent more Russians came to own a color TV: almost three out of four households sampled in 1998 owned a color TV. Only three percent of the population owned a VCR in 1992. This increased to thirty-two percent in 1998. Ownership of cars or trucks increased from seventeen percent of households in 1992 to almost twenty-five percent in 1998. If the levels remain relatively low, the trends over time, nevertheless, are encouraging.

Trends in home ownership are also encouraging (*Table 18*). Private home ownership increased from twenty-eight percent of the sampled households in 1992 to sixty-six percent in 1998. One downside with this trend, however, has been the growth in delinquent household payments of rents and/or utilities, from twenty-two percent of all households in 1995 to thirty-eight percent in 1998. The amount owed has also increased, doubled in fact.

Finally, *Tables 19*, *20*, and *21* provide data on health trends in Russia. The nutritional status of children and the elderly is the focus of *Table 19*. The picture is mixed. The total percent of malnourished children under the age of two was largely the same in 1992 as it was in 1998, that is, fourteen percent. The total percent of malnourished children from ages two to six has decreased from sixteen percent to ten percent in these years.

[16] RLMS estimates of food expenditures as a percent of total consumption in Russia vary considerably from the UNDP estimates cited in *Table 10* of *Part I* of this appendix. Food expenditures are proportionately much higher in the RLMS estimates, though this may be because home food production is not included in the UNDP numbers. Perhaps of greater significance is the variance in trends over time. According to RLMS, food expenditures have fallen proportionately from 1992 to 1998; according to the UNDP, they have been rising.

However, since October 1996, malnourishment has increased in both groups. For the elderly, being overweight has been a concern for many. The proportion of overweight elderly Russians increased from sixty percent in 1992 to nearly sixty-nine percent in 1998. Still, this is down slightly since 1996.

Table 20 reports that more than four in ten Russians consider themselves to have chronic or frequent illnesses. While extraordinarily high, this proportion is nevertheless down some from December 1994 for both urban and rural populations when the question was first asked.

Finally, *Table 21* looks at trends in alcohol drinking and cigarette smoking. There may be two overall striking findings in these data. One is the significant gap in life styles as it pertains to health between adult males vs. adult females and teenagers. There are almost six times more adult male smokers than there are adult female smokers, and four times more than teenagers. Of those who smoke, adult males smoke about two times more than adult females and teenagers. Almost seventy percent of adult males drink alcohol, in contrast to forty-four percent of the adult females and seventeen percent of teenagers. Again, of those who partake, it is the adult males who partake far more; from four to five times more grams of alcohol per day as compared to adult females and teenager. This life style no doubt has played a hand in the precipitous drop in male life expectancy that occurred in the early years of the transition.

The second salient finding, however, is that most of the trends show mitigation in these unhealthy activities. This is particularly so for the percent of alcohol drinkers. As high as it was in 1998, it was higher still, particularly among adults, at the outset of the transition. Sixteen percent fewer adults considered themselves drinkers in 1998 than in 1992. The trends for teenagers are consistently favorable. Among them, there were fewer smokers and drinkers in 1998 as compared to 1992. Of those who drank and smoked in 1998, they smoked less and drank less than did those teenagers in 1992.

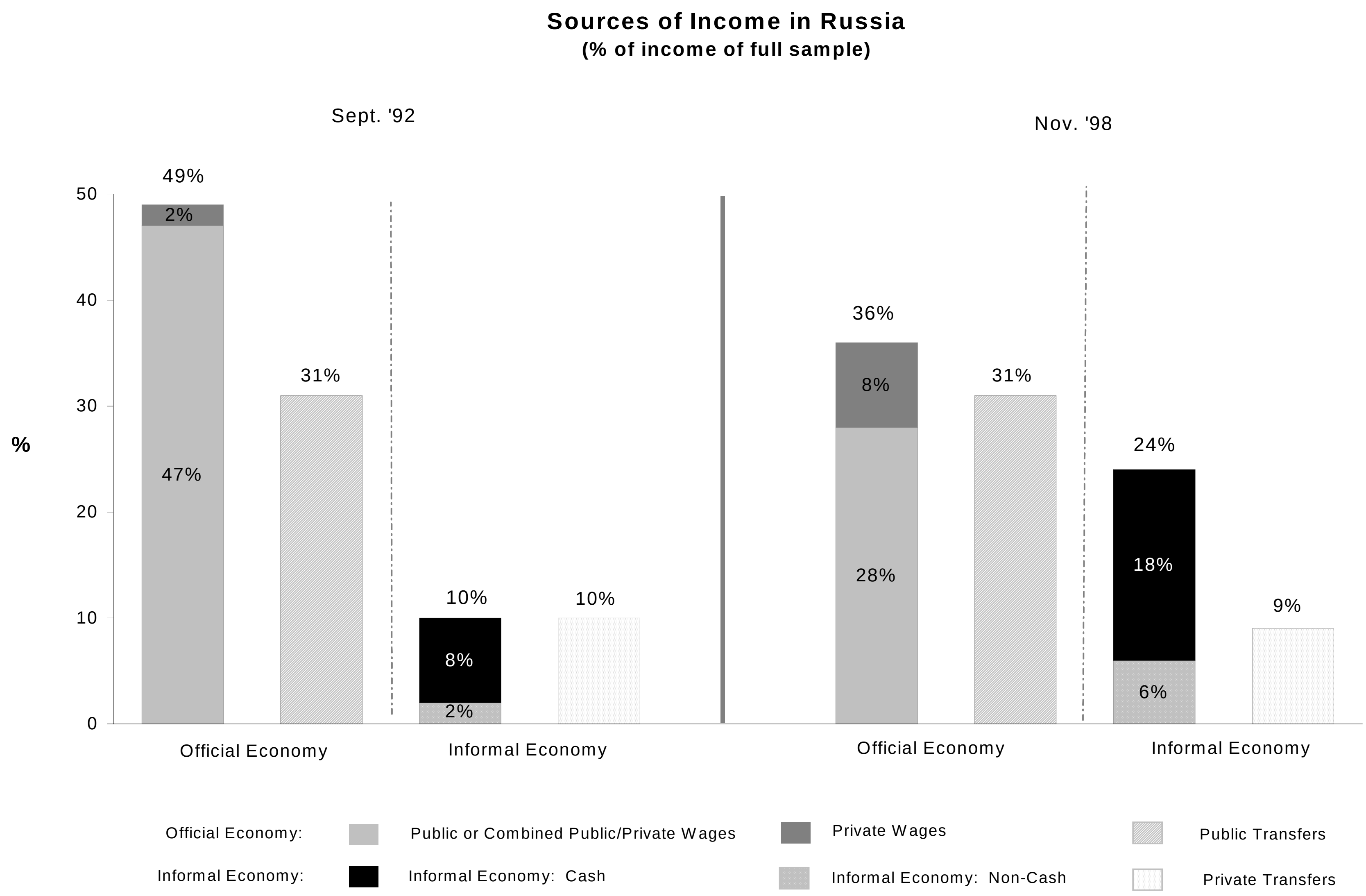
Appendix II, Part II: Russia

Table 12. Sources of income (%)

	Sept. '92	Dec. '94	Oct. '96	Nov. '98	'92-'98 change	Bottom Quintile November 1998	Top Quintile November 1998
Official wages	49	40	39	36	-13	32	45
(of which:)							
public or combined pub./priv.	47	32	30	28	-19	27	31
private sector	2	8	9	8	6	5	14
Informal economy	9	16	22	23	14	31	26
(of which:)							
cash	2	5	7	6	4	5	9
noncash	8	11	16	18	10	27	17
Family & charity transfers	10	8	10	9	-1	12	10
Personal belongings sales	1	1	1	1	0	1	2
Government transfers	31	34	27	31	0	25	16
Rental property & dividends	0	1	1	1	1	0	1
Total	100	100	100	100		100	100

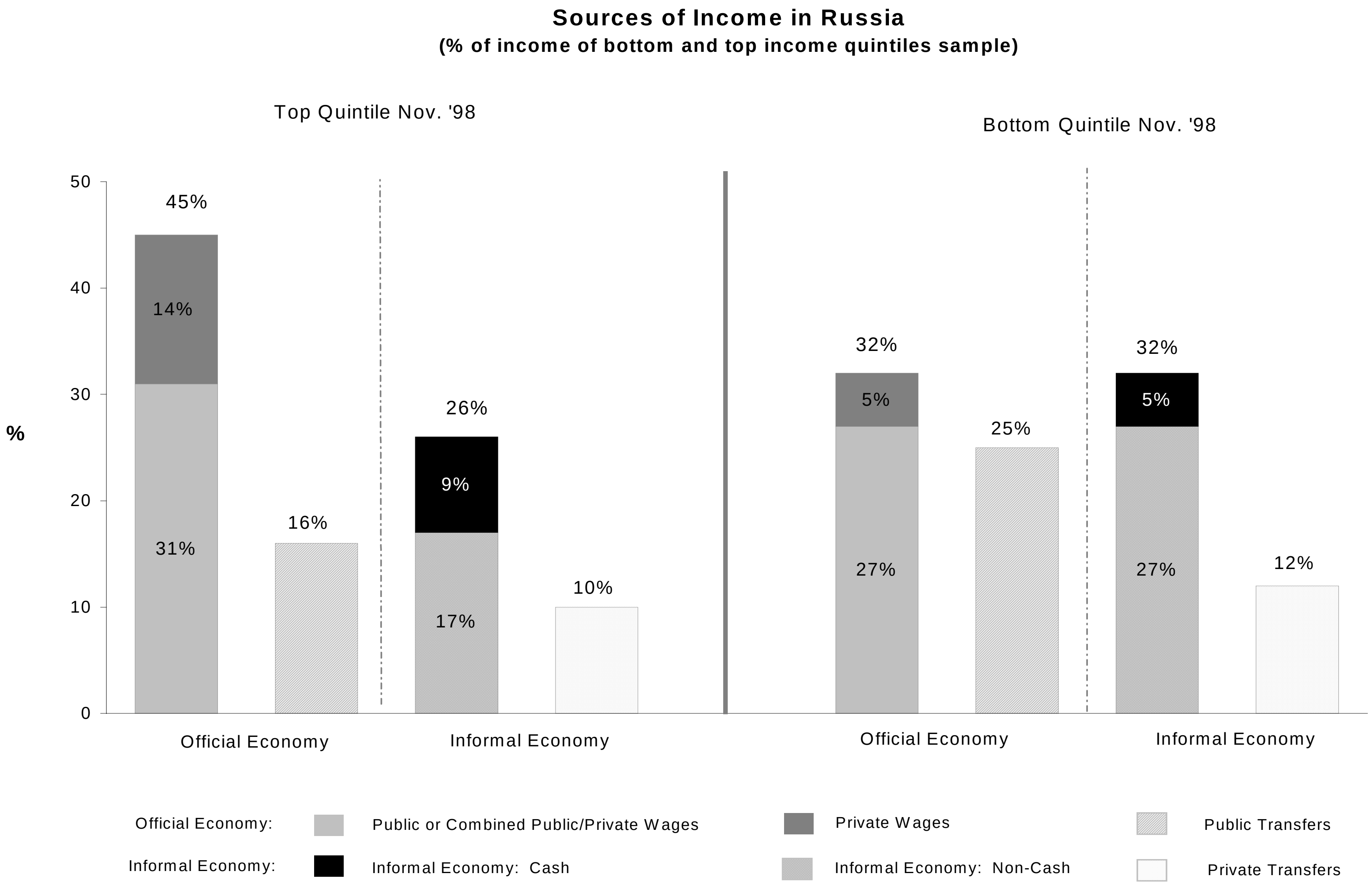
Mroz, Mancini, & Popkin, Monitoring Economic Conditions in the Russian Federation.
The Russia Longitudinal Monitoring Survey 1992-1998 (1999).

Figure 4.



Mroz, Mancini, & Popkin, *Monitoring Economic Conditions in the Russian Federation* . The Russia Longitudinal Monitoring Survey 1992-1998 (1999).

Figure 5.



Mroz, Mancini, & Popkin, *Monitoring Economic Conditions in the Russian Federation* . The Russia Longitudinal Monitoring Survey 1992-1998 (1999).

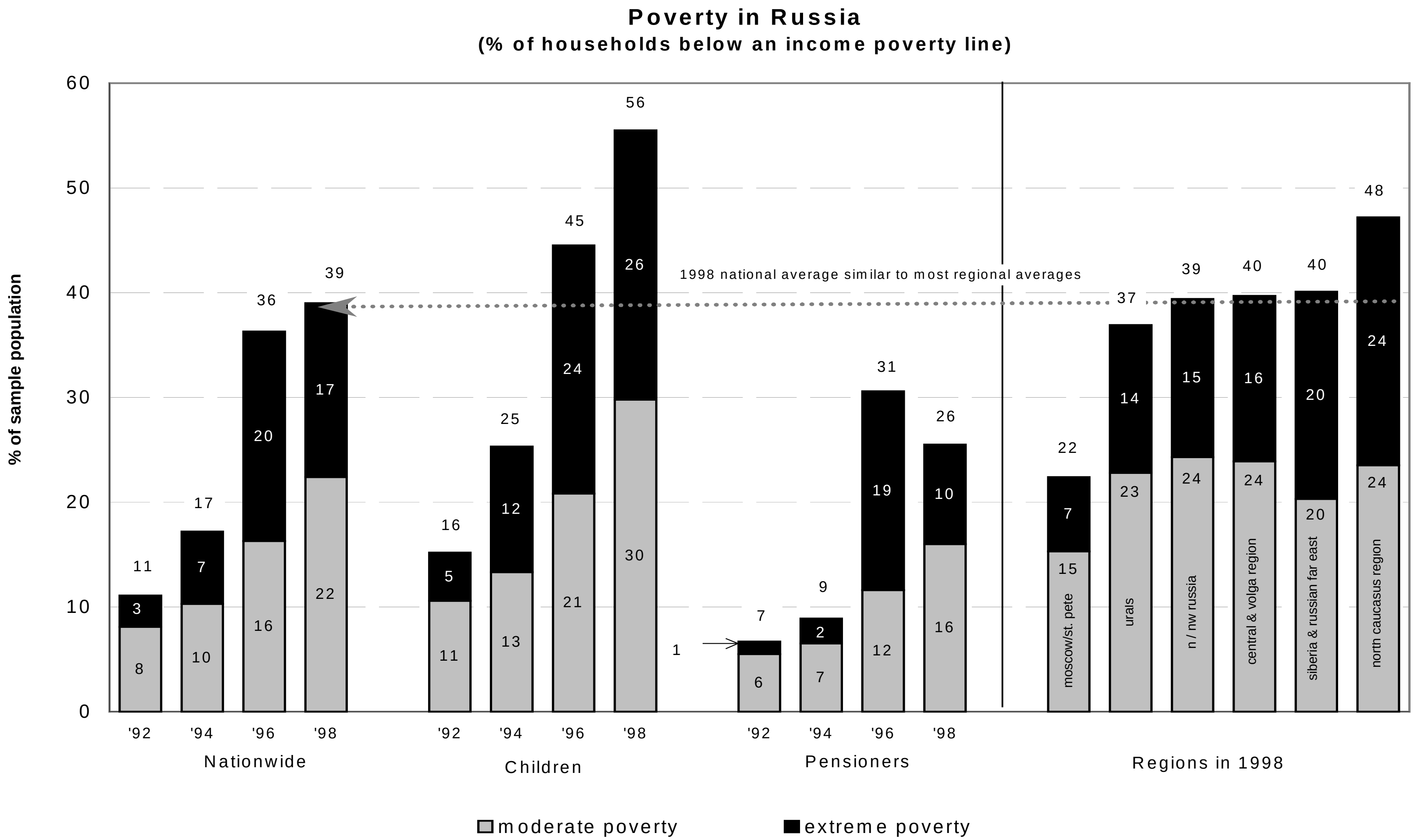
Table 13. Poverty in Russia
(percent of households below an income poverty line)

	Sept. '92	Dec. '94	Oct. '96	Nov. '98
Country-wide sample	11.1	17.2	36.3	39.0
extreme poverty	3.0	6.9	20.0	16.6
Children	15.2	25.3	44.5	55.5
extreme poverty	4.6	12.0	23.7	25.7
Pensioners	6.7	8.9	30.6	25.5
extreme poverty	1.2	2.4	19.0	9.5
Regions:				
1. Moscow & St. Petersburg				
all households	10.2	10.4	12.6	22.4
extreme poverty	3.0	2.9	6.1	7.1
2. North & North West				
all households	12.5	17.0	35.8	39.4
extreme poverty	3.5	8.3	13.3	15.1
3. Central Black Earth, Volga-Vaytski, & Volga Basin				
all households	9.7	16.4	35.4	39.7
extreme poverty	2.3	6.5	19.3	15.8
4. North Caucasus				
all households	15.8	20.7	44.1	47.2
extreme poverty	5.0	7.5	28.0	23.7
5. Urals				
all households	9.5	16.0	34.8	36.9
extreme poverty	1.9	7.3	17.3	14.1
6. Siberia & Far East				
all households	10.8	21.2	44.2	40.1
extreme poverty	3.3	8.6	26.4	19.8

Mroz, Mancini, & Popkin, Monitoring Economic Conditions in the Russian Federation.
The Russia Longitudinal Monitoring Survey 1992-1998 (1999).

The poverty measures use a poverty line based on adjustments for economies of scale, oblast-level prices, and regional food baskets.
Extreme poverty is income less than 50% of the poverty line.

Figure 6.



The poverty measures use a poverty line based on adjustments for economies of scale, oblast-level prices, and regional food baskets. Extreme poverty is income less than 50% of the poverty line.

Mroz, Mancini, & Popkin, *Monitoring Economic Conditions in the Russian Federation.* The Russia Longitudinal Monitoring Survey 1992-1998 (1999).

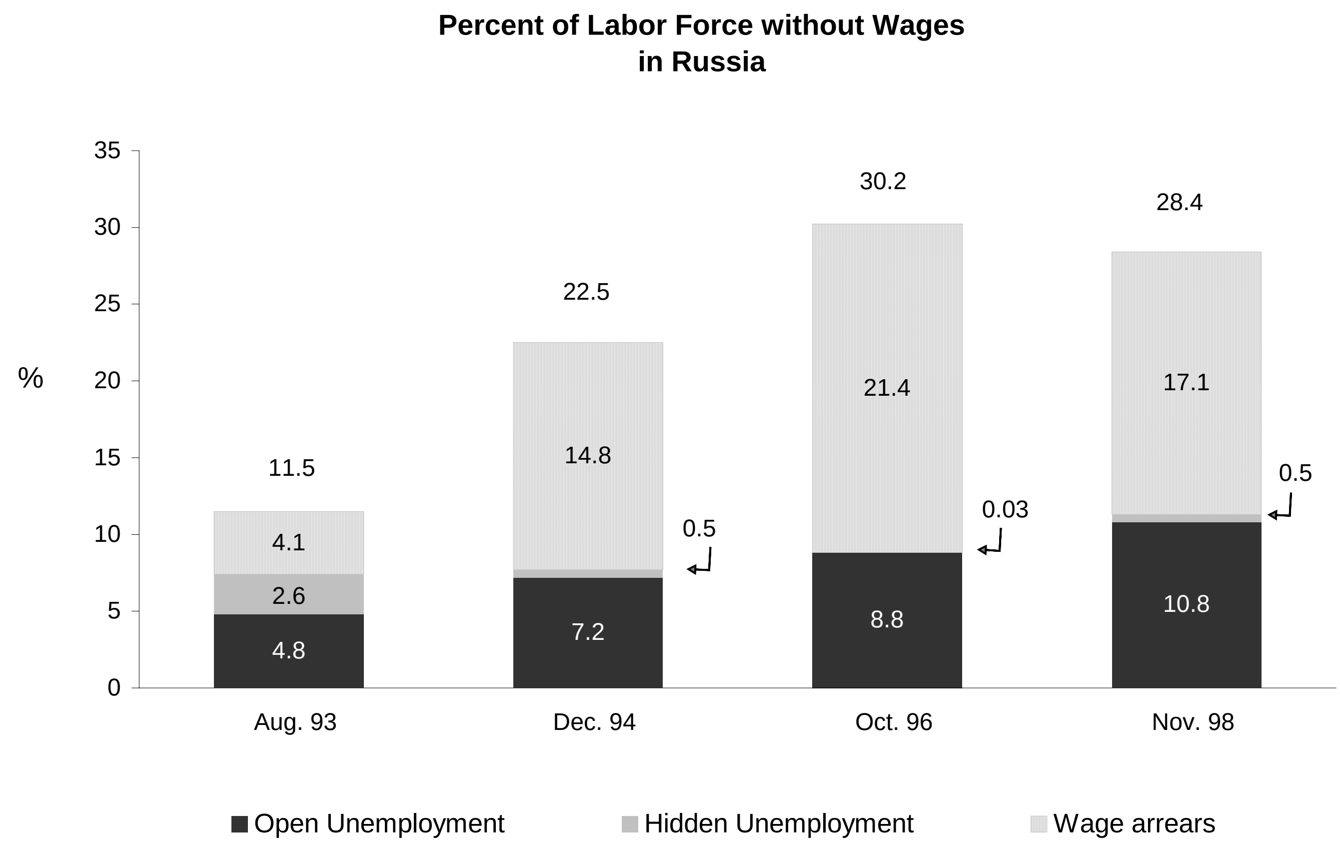
Table 14. Labor market trends in Russia (%)

	Sept. '92	Aug. '93	Dec. '94	Oct. '96	Nov. '98
1. Open unemployment	5.6	4.8	7.2	8.8	10.8
2. Hidden unemployment	---	2.6	0.5	0.0	0.5
3. Wage arrears:					
(a) Workers who haven't been paid in past month	5.8	4.1	14.8	21.4	17.1
(b) Workers owed wages	---	---	38.1	54.1	63.9
4. Percent of labor force without wages (1+2+3a)	---	11.5	22.5	30.2	28.4
5. Percent unemployed more than 3 months	---	50.7	78.5	79.4	74.0
6. Labor force participation	86.7	84.6	85.7	84.5	82.6

Mroz, Mancini, & Popkin, Monitoring Economic Conditions in the Russian Federation.
The Russia Longitudinal Monitoring Survey 1992-1998 (1999).

Hidden unemployment is involuntary unpaid leave.

Figure 7.



Hidden unemployment is involuntary unpaid leave. Wage arrears: workers who haven't been paid in the past month.

Mroz, Mancini, & Popkin, Monitoring Economic Conditions in the Russian Federation. The Russia Longitudinal Monitoring Survey 1992-1998 (1999).

Table 15. Expenditures in Russia
(in 1992 rubles)

	Sept. '92	Dec. '94	Oct. '96	Nov. '98	'92-'98 % change	'96-'98 % change
Food	5,170	5,801	4,155	3,147	-39	-24
(of which) home production	524	841	618	746	42	21
Alcohol	291	288	173	113	-61	-35
Tobacco	154	119	123	116	-25	-6
Clothing	824	810	655	613	-26	-6
Fuel	107	238	245	147	37	-40
Rent & utilities	115	194	300	247	115	-18
Services & recreation	150	754	1,030	644	329	-37
Durables	433	1070	671	478	10	-29
Misc.	898	343	177	190	-79	7
Total	8,142	9,617	7,529	5,695	-30	-24
Savings	167	495	215	173	4	-20

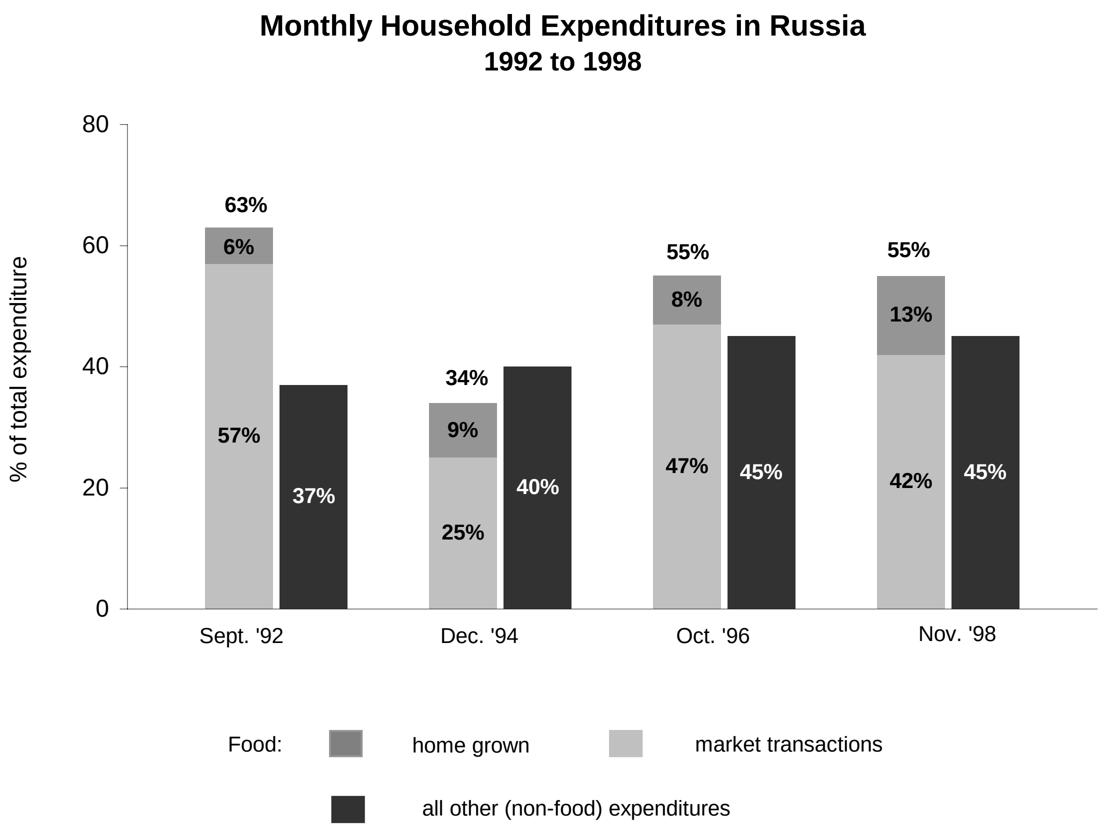
Mroz, Mancini, & Popkin, Monitoring Economic Conditions in the Russian Federation.
The Russia Longitudinal Monitoring Survey 1992-1998 (1999).

Table 16. Expenditures in Russia
(as percent of total)

	Full Sample						Bottom Quintile	Top Quintile
	Sept. '92	Dec. '94	Oct. '96	Nov. '98	'92-'98 % change	'96-'98 % change	November 1998	
Food	63	60	55	55	-8	0	69	43
(of which) home production	6	9	8	13	7	5	20	8
Alcohol	4	3	2	2	-2	0	1	2
Tobacco	2	1	2	2	0	0	3	2
Clothing	10	8	9	11	1	2	6	13
Fuel	1	2	3	3	1	-1	2	3
Rent & utilities	1	2	4	4	3	0	7	3
Services & recreation	2	8	14	11	9	-2	10	13
Durables	5	11	9	8	3	-1	0	16
Misc.	11	4	2	3	-8	1	1	5
Total	100	100	100	100	---	---	100	100
Savings	2	5	3	3	1	0	0	5

Mroz, Mancini, & Popkin, Monitoring Economic Conditions in the Russian Federation.
The Russia Longitudinal Monitoring Survey 1992-1998 (1999).

Figure 8.



Mroz, Mancini, & Popkin, *Monitoring Economic Conditions in the Russian Federation.* The Russia Longitudinal Monitoring Survey 1992-1998 (1999).

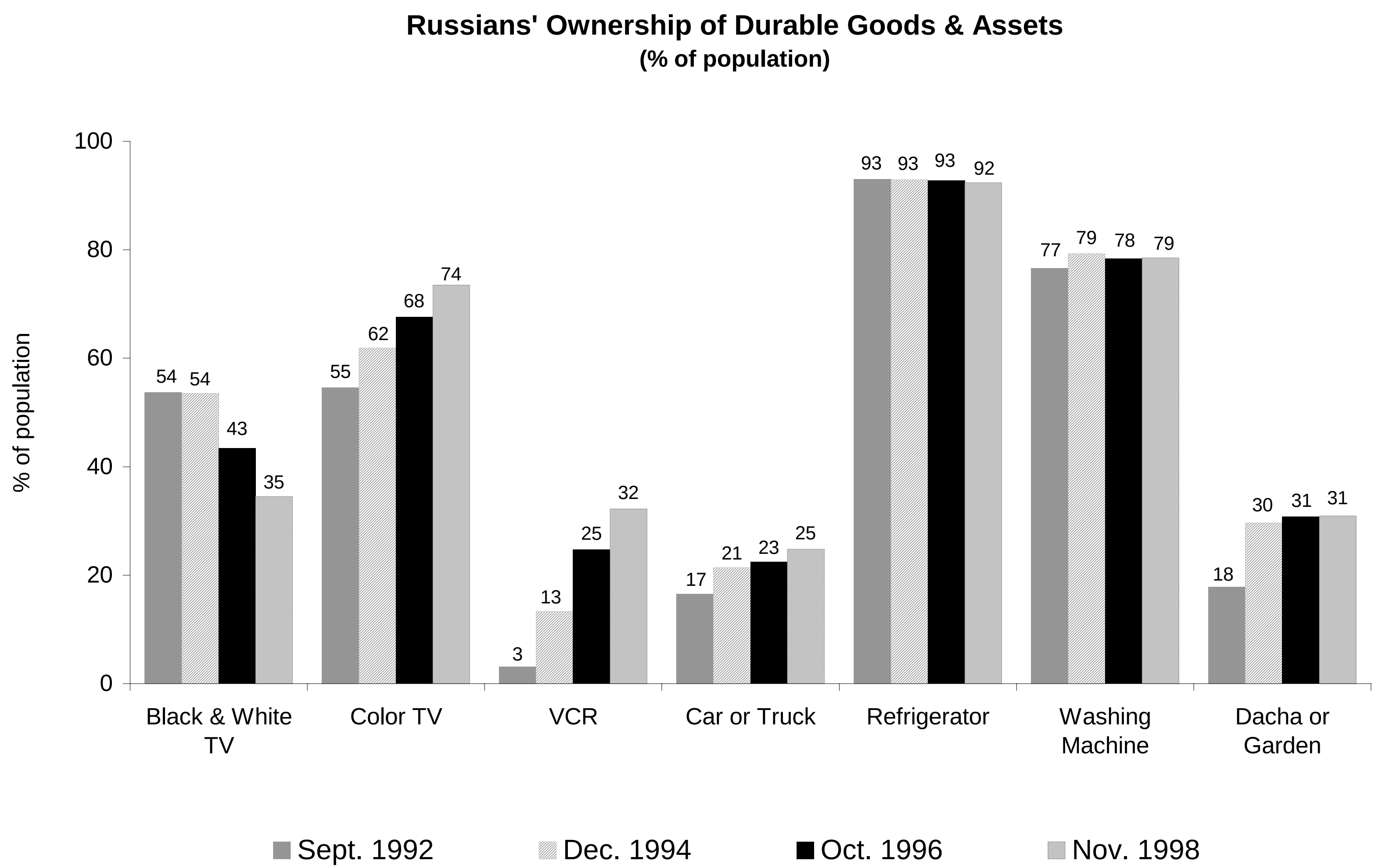
Table 17. Russians' ownership of durable goods and assets (percent of population)

	Sept. '92	Dec. '94	Oct. '96	Nov. '98	1992-98 difference	1992-98 difference
Television						
Black & White TV	54	54	43	35	-19	-9
Color TV	55	62	68	74	19	6
VCR	3	13	25	32	29	8
Car or truck	17	21	23	25	8	2
Refrigerator	93	93	93	92	-1	0
Washing machine	77	79	78	79	2	0
Dacha or garden	18	30	31	31	13	0

Mroz, Mancini, & Popkin, Monitoring Economic Conditions in the Russian Federation.
The Russia Longitudinal Monitoring Survey 1992-1998 (1999).

Dacha includes garden or country house; proportion of ownership is calculated for urban households only.

Figure 9.



Mroz, Mancini, & Popkin, *Monitoring Economic Conditions in the Russian Federation* . The Russia Longitudinal Monitoring Survey 1992-1998 (1999).
Dacha includes garden or country house; proportion of ownership is calculated for urban households only.

Table 18. Housing ownership and payments in Russia (%)

	Sept. '92	Oct. '95	Oct. '96	Nov. '98
Private ownership:				
Owner-occupied	25	54	56	61
Rented from other individuals	2	5	5	5
Sub-total	28	59	61	66
Collective ownership:				
Enterprise or state	66	37	34	30
Cooperative	4	0	1	0
Sub-total	69	37	35	30
Other:				
Live in a dormitory	3	4	4	4
Total	100	100	100	100
Households that owe rent and/or utilities		22	29	38
Amount owed (in months of ave. bill)		2	3	4

Mroz, Mancini, & Popkin, Monitoring Economic Conditions in the Russian Federation.
The Russia Longitudinal Monitoring Survey 1992-1998 (1999).

Table 19. Nutritional status of children and the elderly in Russia (%)

	Sept. '92	Dec. '94	Oct. '96	Nov. '98	1992-98 difference	1992-98 difference
Children (0-24 months)						
Wasted	6	7	2	2	-3	1
Stunted	9	16	8	12	3	4
Total malnourished	14	23	10	14	0	4
Children (25 months-6 yrs.)						
Wasted	6	5	2	2	-4	1
Stunted	10	11	6	8	-2	2
Total malnourished	16	16	8	10	-6	3
Adults (60+ yrs.)						
Overweight I	36	38	38	37	1	-1
Overweight II	23	27	32	32	9	0
Total overweight	59	65	70	69	10	-1

Children with stunted growth are considerably below average in height for their age, which indicates chronic malnutrition. The prevalence of wasting is an indication of acute malnutrition and is apparent in a child with considerably lower weight for his/her age. The division of adults into various weight groups is based on Body Mass Index categories as recommended by WHO: 18.6-25 (normal); 25.1-30 (category I overweight); and >30 (category II overweight).

N. Zohoori, Monitoring Health Conditions in the Russian Federation.
The Russia Longitudinal Monitoring Survey 1992-1998 (1999).

Table 20. Russians with self-reported chronic or frequent illness (% of population)

	Dec. '94	Oct. '95	Oct. '96	Nov. '98	1994-98 difference
Urban population	49	43	45	44	-5.5
Rural population	46	39	43	42	-4.2

N. Zohoori, Monitoring Health Conditions in the Russian Federation.
The Russia Longitudinal Monitoring Survey 1992-1998 (1999).

Table 21. Drinking and Smoking in Russia

	Sept. '92	Dec. '94	Oct. '96	Nov. '98	1992-98 difference
Percent of smokers					
Adult males	60	61	63	62	2
Adult females	7	10	10	10.9	3.6
Teenagers	17	20	20	15.2	-1.6
Cigarettes per day (for smokers)					
Adult males	16	15	16	15.2	-0.9
Adult females	8	8	9	8.9	0.8
Teenagers	8	8	8	6.7	-1.1
Percent of alcohol drinkers					
Adult males	85	75	71	69.1	-15.6
Adult females	59	45	44	43.5	-15.9
Teenagers	25	23	23	17	-8.2
Grams of alcohol per day (for drinkers)					
Adult males	29	41	41	37.1	8.5
Adult females	9	8	8	8.6	-0.3
Teenagers	11	10	9	7.8	-3.5

Mroz, Mancini, & Popkin, Monitoring Economic Conditions in the Russian Federation.
The Russia Longitudinal Monitoring Survey 1992-1998 (1999).

IV. Summary Observations

What can be said in summary first as pertains to the wider sample of countries from these household survey results? One, very impressive political gains have been realized and shared broadly across the transition region. These are the relatively "easy" gains that resulted early on with the collapse of communism: the freedoms to say what one wants; to associate with whomever; to pursue political and religious activities (or, in the case of many, at least at the outset, to choose to be inactive politically).

"Second stage" political gains, however, have been far more elusive. These are the gains that stem from good governance and hence require institutional development: being treated fairly and equitably by the government; having an ally in government to encourage household economic improvement. In fact, a widely shared perception across the region is that corruption is significant and worse than it was under communism, and that government is part of the problem. More generally, there exists very little trust in key institutions. This includes government, but also private enterprise. Both are viewed with much suspicion. Moreover, this is not a trend confined to Eurasia. More than four in ten persons surveyed in 1998 in the Northern Tier CEE countries felt that corruption and bribe-taking had increased a lot since communist days, and more than one in four persons in these countries had little trust in private enterprise.

Self-perceptions of economic conditions are generally quite dismal. In 1998, across the twelve countries surveyed, only one in six persons saw improvement in their household's economic situation as compared to five years before. It was only marginally better among the Northern Tier CEE participants (one in five persons).

But expectations are low as well. In fact, even though only one in six persons see improvement in economic conditions since 1993, twice that number of people, or one in three, are satisfied with their current economic situation. Moreover, most persons do not want to see communism return. Still, there is considerable difference on perspectives towards communism across the countries. Preference towards going back to the old system is much stronger in Ukraine, Russia, and Belarus than in the Northern Tier countries. In Ukraine, more than one in two persons preferred a return to communism when asked in 1998. In Russia, twenty-seven percent of the population wanted a return to communism in 1994; in 1998, it was forty-one percent. Such preferences are growing elsewhere as well. Time has been no ally in this regard.

Mitigating some of the transition costs if not the skepticism, at least in the short term, has been a large and vibrant informal economy and significant informal safety nets (from family and friends). Overall, across the fifteen countries surveyed, only about twenty percent of the households are able to get by on a sustainable basis (that is, without drawing on savings or going significantly into debt) through formal economy jobs only. Yet, almost seventy percent of households can get by in this manner when the complete portfolio of economic activity (from the informal economy as well as the formal) is factored in. In addition, the percentage of households that have had to often do without needed goods, particularly in the CEE countries, is quite low. For example, only three percent of households in the nine CEE countries surveyed had to often do without food over the course of the month in 1998 prior to being interviewed.

Those being deprived of needed goods are proportionately more numerous in some of the Eurasian countries. The situation in Ukraine is the worst of the countries included in the survey; forty-two percent of households there often did without food in 1998, fifteen percent often did without heating and electricity. Still, these numbers do not seem to "add up" to the deprivation that is implied in Eurasia from many of the official income-based poverty estimates. In Ukraine, for example, income-based poverty has been estimated to be at least sixty percent of the population, which is a proportion higher than those sampled households which have often had to do without necessary goods.

In contrast, while many persons in the leading transition countries are doing well materially (coinciding with relatively healthy macro-economies and low income-based poverty estimates), this has not yet translated into many satisfied customers of the market economy. In fact, almost sixty percent of those surveyed in the Northern Tier countries in 1998 said they were not satisfied with their economic condition.

What do we find when we look closer at Russia? First, a review of some of the more sobering news. Poverty in income terms is significant, and it has increased dramatically since the beginning of the transition, though the increase has slowed since 1996 (and the RLMS estimate of thirty-nine percent in 1998 is less than estimates from other sources). The RLMS survey also finds that poverty in Russia is becoming increasingly "deep." In particular, almost one-half of those Russians in poverty in 1998 had incomes less than fifty percent of the poverty line. This finding runs counter to the conventional view, which is based on available albeit dated figures (from 1992-1994) for the transition region, that poverty is "shallow" in most of the transition countries; that is, most of those impoverished have incomes close to the poverty line. As shown in *Monitoring Country Progress* (July 1999),[17] there is a close relationship between poverty rates and the poverty gap (or depth). If poverty rates have continued to rise since the early transition years, as is likely the case at least in much of Eurasia, then more recent estimates of the poverty gap will likely yield results similar to that found in RLMS.

Children are particularly vulnerable. Over half of all children surveyed in 1998 were living in households below the poverty line, and almost one-half of them were in extreme poverty.

We know that labor market trends are closely linked to poverty. However, open unemployment is only part of the labor market story. In Russia, open unemployment in 1998 (at eleven percent of the labor force) accounted for less than half of the total percent of those in the labor force who were failing to receive wages. In fact, by November 1998, almost sixty-four percent of the labor force in Russia had back wages owed to them and yet were continuing to work.

[17] *Monitoring Country Progress in CEE and the NIS* (July 1999), p. 34 and *Figure 4*.

The proportion of Russians with self-reported chronic or frequent illness remains extraordinarily high. In 1998, almost forty-four percent of the urban population surveyed placed themselves in this category, while forty-two percent of the rural response was of this kind. Some of this must surely be linked to the continued unhealthy life styles of many Russians, and, in particular, of the adult males who continue to smoke and drink far more than adult females and teenagers.

There is some relatively encouraging news as well. As is evident in the cross-country household survey data, informal economic activity and family safety nets in Russia seem to be playing a key role in mitigating hardship. For the population quintile in Russia with the lowest income, over forty percent of income derives from these sources. Growing one's own food is particularly key. This may explain, in part, why malnourishment in children has actually decreased somewhat since 1992 despite the fact that so many of them live in households with income below the poverty line.

A look at expenditure patterns reveals some very tangible gains among the Russian consumers. In 1992, fifty-five percent of Russian households owned a color TV; in 1998, seventy-four percent did. In 1992, three percent of households owned a VCR; this had increased to thirty-two percent by 1998. More impressive perhaps has been the shift to private ownership of houses. In 1992, twenty-eight percent of houses were privately owned. This had increased to sixty-six percent by 1998.

Finally, it seems significant to note that life style trends among Russia's teenagers, at least as pertains to alcohol drinking and cigarette smoking, are not following the path of many of the older Russians, particularly the adult males. Both the number of teenage drinkers and smokers and the amount of drinking and smoking among those teenagers who do engage have declined during the transition.