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## Could Inflation Stabilization Be Expansionary?

by Michael Bruno and William Easterly

**M**any former socialist countries have recently experienced both a decline in output and high inflation during the transition to a new economic system. Some governments in these countries have been reluctant to pursue a vigorous inflation stabilization policy because they fear that stabilization could shrink output even further. Their concern derives from the well-documented experience of industrial countries. In the United States, for example, the deep 1982 economic contraction has been linked to inflation stabilization by U.S. Federal Reserve Board Chairman Paul Volcker, who eliminated the double-digit inflation rate that had accelerated during the Carter administration.

### Does Stabilization Hurt

Recent evidence suggests a surprising twist: stabilizing from high inflation is not necessarily contractionary, and it may even be expansionary. Stabilization in Argentina, Brazil, and Peru brought rapid output growth once inflation dropped to moderate levels. And development in transition economies, such as Poland, Slovenia, and the Baltic states, seems to

fit the pattern of expansionary stabilization as well.

How could stabilization from high inflation be expansionary? It is not so hard to understand if one considers, how much output usually falls during high inflations. We summarized the average growth rates and inflation rates of

twenty-six countries that had episodes of high inflation over the period 1961-92. (An episode of high inflation is defined as a period of two years or more in which inflation exceeds 40 percent annually.) The following table shows that per capita growth is negative during high inflation crises, but after stabilization growth recovers strongly.

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**Annual averages of 26 countries before, during, and after inflation crises (percent)**

	Inflation	Per Capita Growth
Before first inflation crisis	13	1.6
During inflation crises	155	-1.2
After inflation crises	20	2.6

Recent theories of inflation have focused on the destruction of the normal functioning of the price and credit system during high inflation periods, confirming what Keynes suggested long ago: "As inflation proceeds and the real value of the currency fluctuates wildly from month to month, all permanent relations between debtors and creditors, which form the ultimate foundation of capitalism, become so utterly disordered as to be almost meaningless; and the process of wealth-getting degenerates into a gamble and a lottery."

**Countering Conventional Wisdom**

But negative growth during inflation may be peculiar to massive price increases. At low rates of inflation the economy may be stimulated in the short run through

inflationary demand expansion, so that inflation and growth increase together. Or a favorable external development, such as a fall in oil import prices, could simultaneously slow inflation and accelerate growth. Indeed, there is little evidence that low-to-moderate rates of inflation have any consistent relationship to output growth, positive or negative. In contrast, the negative growth outcomes associated with high inflation are remarkably consistent across time periods and across different samples of data.

Once one accepts that high inflation is associated with output collapse, it is not so surprising that a fall in inflation is associated with rapid output recovery. We analysts of economic data often forget that one way to have rapid growth is first to have rapid decline. This is indeed what we find in looking at the average growth rate of the twenty-six countries, once they have overcome their inflation crisis. After the crises, the average growth rate climbed higher than before the first crisis; output rapidly recovered from its inflation crisis low, and caught up with the pre-crisis trend. These growth recoveries are not just short-lived consumption booms—previous re-

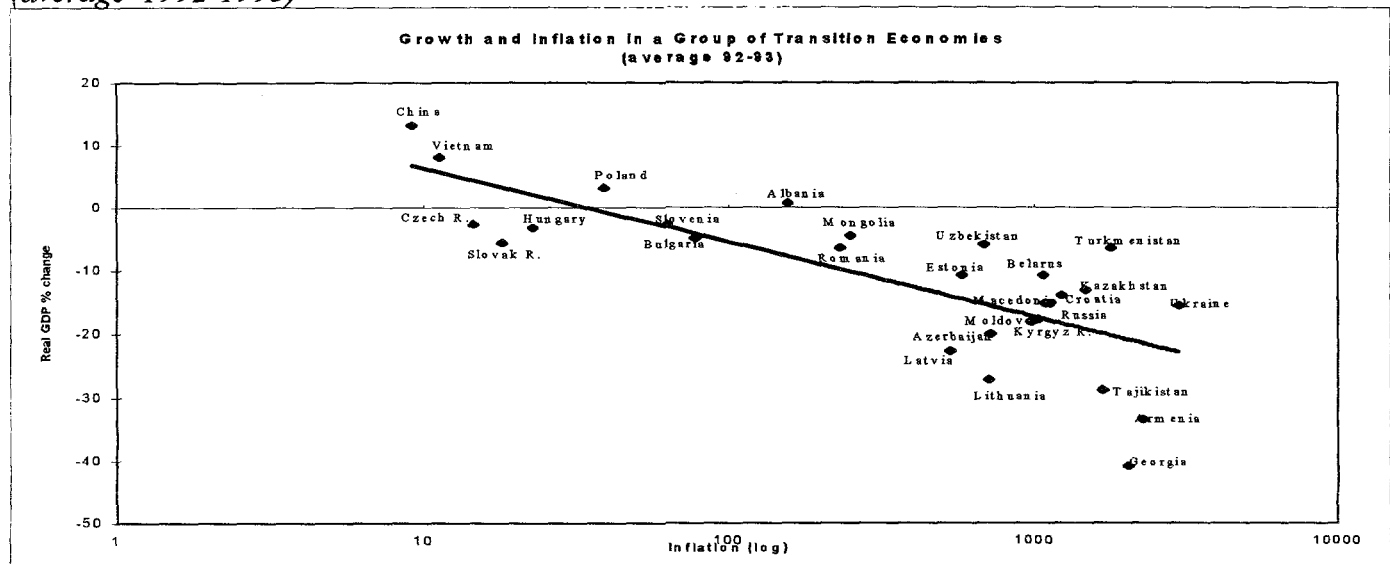
search has suggested that such consumption booms sometimes occur with exchange rate—based stabilization—because the growth recovery lasts over the medium run.

Again, this pattern contrasts with a low inflation scenario, for which there is clear evidence that reducing already low rates of inflation is associated with lower growth in the short-to-medium run. Of course, not every country with high inflation recovers immediately after stabilization begins because country circumstances differ. But, on average, countries that reduce high inflation start to recover once inflation comes down.

Conventional wisdom also holds that inflation stabilization is political suicide. But the conventional wisdom again seems to be false under high inflation: Menem in Argentina and Fujimori in Peru were recently reelected by surprisingly large margins after political campaigns in which they trumpeted their inflation stabilization achievements.

The averages shown in the table above do not include the transition experience of 1990-94 in Central and Eastern Eu-

**Figure 1: Growth and Inflation in a Group of Transition Economies (average 1992-1993)**



Source: the authors.

rope and the countries of the former Soviet Union. The transition economies are of course special in many ways. Yet their inflation and growth experience fits the larger pattern. Figure 1 shows the average growth and inflation rates of transition economies over 1992-93. Economies that still had very high inflation continued their output decline; economies that had already brought inflation to lower levels experienced higher growth than before.

Figure 2 shows the same pattern in the year-by-year experience of five transition economies that successfully brought down inflation to more moderate levels: Estonia, Latvia, Lithuania, Poland, and Slovenia. The growth of each economy declined while the inflation rate was rising. When inflation was reduced, the growth declines were reversed. By 1994 all five economies had positive per capita growth.

Growth after high inflation stabilization has a broader historical precedent. It is often forgotten that three of the legendary East Asian success stories—Japan, the Republic of Korea, and Taiwan, China—began their rapid growth in the wake of stabilization of high inflation during severe postwar crises. Indonesia followed the same pattern a few years later. Two of the fastest-growing industrial countries—Greece and Italy—also began rapid growth after stabilizing the high inflation that accompanied postwar crises. These countries not only caught up to their precrisis (or prewar) trend, but kept growing faster.

### Was Lenin Right?

The historical examples seem to illustrate a principle set out by Mancur Olson: long-run growth can actually be higher after crises, because crises destroy the power of interest groups that block salutary reforms. The countries in our his-

torical examples put into place institutional reforms that enhanced macroeconomic management—such as central bank independence and limitations on government borrowing—and they committed themselves to compete in the global marketplace.

Although it is clear that growth is recovering in the more recent stabilization examples, it is much too soon to tell whether long-run growth acceleration has taken place. As in the historical precedents, many of the Latin American countries recovering from high inflation utilized the crisis atmosphere to put into place more fundamental reforms, including central bank independence and increased integration into international trade. Time will tell whether they too experience sustained higher long-run growth.

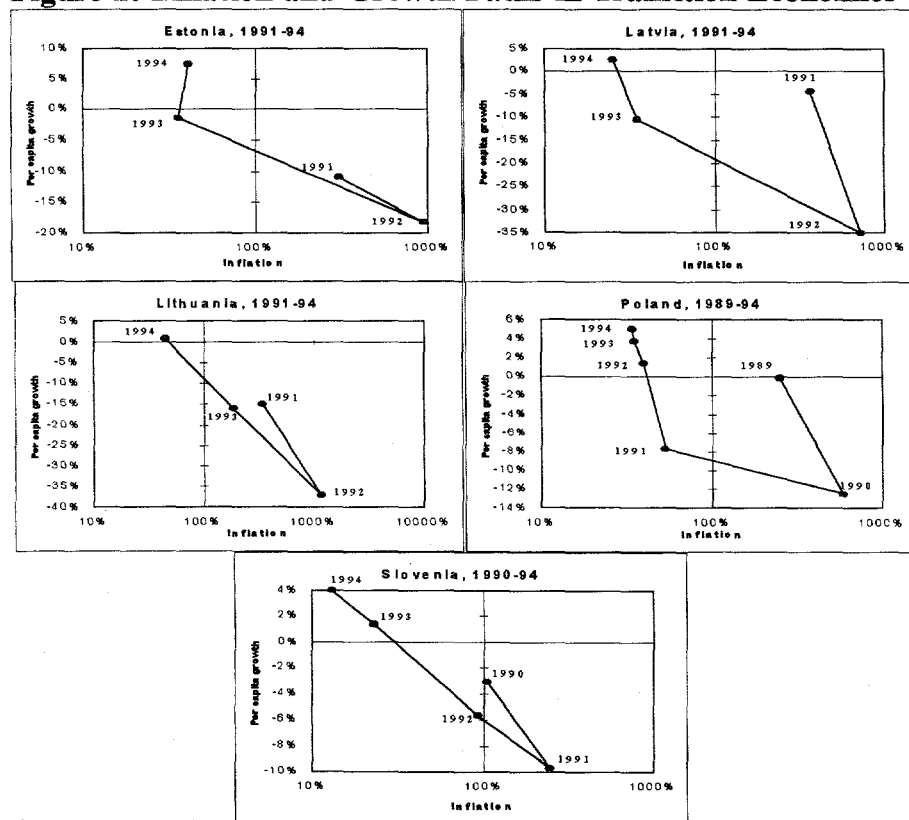
For the transition economies stabilization of high inflation could also provide an opportunity to put in place the foundations of rapid growth for years to come. Keynes attributed to Lenin the view that "there is no subtler, surer means of overturning the existing basis of society than to debauch the currency." The existing basis of society has indeed been overturned in many postcommunist economies. In Russia and other transition economies today, a new basis of society could be laid by stabilizing debauched currencies and beginning growth anew.

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*The article is related to the author's forthcoming working paper "Inflation Crises and Long-Run Growth," July 1995, 30 p.*

**Figure 2: Inflation and Growth Paths in Transition Economies**



Source: the authors.

# The Latin American Experience with Private Pension Funds: Lessons for Eastern Europe

by Jean de Fougères

**T**he latest trends in pension privatization in Latin America were the focus of a recent working retreat held outside Washington D.C. Participants at the meeting, which was organized by the Institute for EastWest Studies, included Central and Eastern European pension experts who are contemplating pension privatization in their countries. Participants agreed that present pension systems throughout the transition economies are unsustainable and that reform is both urgent and unavoidable. This article is

based on the report that was issued after the meeting.

## PAYGO System Unworkable

As the number of workers relative to the number of pensioners (system dependency ratio) declines throughout the world, it is becoming more difficult to keep the prevailing (pay-as-you-go (PAYGO) system alive. In the PAYGO system workers contribute to a pension fund that is drawn on by current retirees, with the expectation that their pen-

sions will be paid in turn by tomorrow's workforce. There are two choices: pensions must be cut or already high payroll taxes must be increased. The first is probably politically unacceptable; the second would cause further misallocation in the labor market, increase tax avoidance, and create a disincentive to work and hire.

In 1980 the government of Chile replaced the bankrupt, government-financed PAYGO pension system with an innovative new structure: a privately

## Transition Economies: Cannot Pay-As-You-Go

Central and Eastern Europe cannot avoid pension reforms. Like the West, they will have to finance the retirement of the post-war, baby-boom generation when the working population is in decline. The ratio of beneficiaries to contributors will worsen with time as a result of demographic trends, low retirement age limits, and a shift toward early retirement due to liberal eligibility requirements. In Hungary the ratio will rise from 59 percent in 1992 to 62 percent in 2016; in Poland the ratio will jump from 49 percent in 1992 to 72 percent in 2020.

### Sobering Data

Transition economies have much higher system dependency ratios than demographic old age dependency ratios:

#### Comparison of Dependency Ratios, 1992 (percent)

Country	SDR	DDR	Difference
Czech R.	49	32	17
Hungary	59	36	23
Poland	49	28	21
Russia	46	31	15
United States	31	30	1
Switzerland	43	34	9

SDR = system dependency ratio (number of pensioners, including widows, orphans,

and disability pensioners, divided by number of contributors).

DDR = demographic old-age dependency ratio (number of people 60 years and older divided by the number of people between 20 and 59 years old).

Source: Dimitri Vittas, World Bank

During the early years of transition the problem of reduced revenues due to declining GDP was exacerbated by the early retirement policies enacted to cushion quickly rising unemployment. Employees also searched for a way to escape the uncertainty of the transition period by seeking disability pensions. Truly poor health causes many to seek disability pensions, but lenient medical examinations enable potentially active workers to quit the system as well, permanently reducing the contribution base. In 1990-93 in Poland, for example, net growth in the number of old-age and disability pensioners reached about 2 million, more than 20 percent of the total number eligible for benefits.

Another major problem that affected pension schemes during the transition period was the lack of a built-in mechanism to index pension benefits. When triple-digit inflation hit many countries of Central and Eastern Europe at the end of the 1980s, benefit increases—introduced ad hoc under social

pressure—did not match the growing needs of the retired population. In 1990-91 the Polish government indexed pensions to wages just as the number receiving benefits exploded; pension expenditures jumped from 8 percent of GDP in 1989 to 16 percent in 1995. In the same period transfers from the state budget to the social security fund grew from 2 percent of total expenditures in 1989 to 20 percent (see box page 6).

Throughout the region the condition of public finances is worsening, and current old-age security systems are nearing collapse. The implicit pension debt in these countries (the value of the expected benefit rights that workers and pensioners have accrued) has reached crisis proportions. For example, the implicit pension debt is 192 percent of GDP in Hungary and 217 percent in the Ukraine. (Italy, with a debt of 242 percent of GDP is in even worse shape. The ratio is 157 percent in Germany and 89 percent in the United States.) At the same time, interest payments on the external debt in many of these countries compete with pension disbursements for the top expenditure item on the state budget.

administered, national system of mandatory retirement savings that guarantees a minimum pension to all eligible individuals (determined by means testing). Instead of paying a social security tax, employees deposit 10 percent of their monthly wages in an individual investment account bearing their name, at any one of twenty-one private pension funds. The money that accrues in the account during the employee's active career, along with the returns on the investments made by the pension funds, will be used to cover the employee's retirement benefits. As of March 1995 the twenty-one funds had 5 million affiliates and 3 million active contributors and were managing assets worth \$23 billion, or half of Chile's gross domestic product (GDP). On retirement, the average participant receives a pension

equivalent to 70 percent of his or her average annual salary for the ten previous years.

The pension funds are authorized only to invest these savings; they are prohibited from engaging in any other activities. To guarantee a diversified, low-risk portfolio and prevent theft, fraud, or mismanagement, strict government regulations apply, overseen by a special government agency. The funds are required to provide statements to contributors three times a year that disclose the last four monthly contributions paid by employers, the fund's financial performance, and the accumulated balance and rate of return on individual accounts. The government is the insurer of last resort, but individual pension savings are insulated from the budget, and can-

not be used for any but their intended purpose.

### Advantages of the Chilean System

The Chilean system creates a direct relationship between the size of contributions and the size of pension benefits, moving the system from a defined benefit structure to a defined contribution basis. There are several other advantages:

- Employers have less incentive to underreport salaries.
- Individual responsibility and discipline increases because the burden of maintaining an acceptable standard of living during retirement cannot be shifted to others.
- The system is equitable. It is not possible for certain groups of workers to

### Worker Insecurity

Budgetary projections are not the sole rationale for pension reform; the poor service provided by the current system is also part of the reason. Workers do not have a sense of security about their retirement years because of the shortage of resources in the system. Knowing that pensioners are poorly served by the current system and skeptical that they will receive adequate benefits upon retirement, workers are motivated to evade payments altogether, especially since benefits are not clearly linked to contributions. The deficiencies of the system are not the result of low contribution rates, however, but of inefficiency. Although a dominant public plan with high tax rates could function in a command economy, it is dysfunctional in a market economy that relies on incentives, compliance, decentralized capital mobilization, and competition in world markets.

The level of payroll taxes required to support these benefits is enormous: throughout most of Central and Eastern Europe 30 percent of GDP is typically allocated for pensions and another 20 percent for other social insurance. These high rates render labor uncompetitive internationally; dis-

courage labor-intensive investment, which affects unemployment; create employer incentives to conceal labor or evade payments altogether; and encourage financially troubled firms to evade social insurance contributions.

Overhaul of the system is clearly required. But two intergenerational distribution problems hamper the implementation of systemic pension reform:

- Cuts in commitments to the current generation of workers (through an increase in the retirement age and changes in the benefit formula) are needed, perhaps along with cuts in benefits of the current retired generation (through a change from wage to price indexing).
- Governments that are considering the transfer of a portion of the public pay-as-you-go system to a privately administered and funded scheme will still be obliged to fund the pensions of workers who have paid into the state-operated system. But government resources will be limited, since the contributions of new workers will be invested wholly or partially in private individual retirement accounts. Thus the problem for the state is how to pay back its social security debt. Options include reducing public expenditures, issuing government bonds, raising taxes, or selling public assets.

### Convincing Arguments

A shift in the financing mechanism can be justified only if systemic pension reform provides positive outcomes. Both political and economic advantages can be claimed. At the political level, systemic reform:

- suggests a time consistent and, hence, credible policy;
- isolates retirement provisions from political interference to a large extent;
- involves the labor force in financial issues and enterprise performance, reducing the dichotomy between capital and labor.

At the economic level, systemic reform:

- establishes a close link between contribution and benefits;
- furthers and accelerates financial market developments and thus the efficiency of resource allocation;
- stimulates national saving and capital accumulation, and hence contributes to economic growth.

If these beneficial effects are realized, and the Chilean experience suggests they will be then the costs of transition may be reduced.

receive extra benefits, as they did under the old plan.

- Because private pension funds must compete for contributors' money, they have strong incentives to perform well.
- Freed from government management, the pension system gains stability and independence, regardless of a change in government or political will.
- The system is popular with investors, who have a direct, visible stake in the economy, and has spawned a public coalition to support sound economic policies and eliminate inflation.

Argentina, Colombia, and Peru—whose pension systems also faced high dependency ratios and budgetary costs, exac-

erated by inflation and high levels of evasion—recently adopted variations of the Chilean pension system. These countries have maintained government-managed PAYGO systems based on employer contributions while introducing privately managed and publicly regulated pension funds based on employee contributions. Employees were given the choice of either staying in the public system or switching to the private system. In Argentina, beginning in 1996, employees who have opted for the private system will not be able to switch back to the public system. Peru and Colombia, by contrast, allow employees to switch between the public and private

systems at will—that may cause both countries problems.

The two-system approach taken by Argentina, Colombia, and Peru allows the public to diversify its risk through a combination of state and market coverage. Pensioners participating in the capitalized private funds will be relatively safe from any government austerity program aimed at slashing the PAYGO system. At the same time, the government-guaranteed base system will provide a hedge against uncertain investment returns in the private pension funds.

Argentina's twenty-six private pension funds, which are operating with 3.5 mil-

### Pension Woes in Poland

State subsidies to pensions absorb a significant and rapidly increasing part of budgetary expenditures in Poland. The state budget plugs a hole in an expanding pension system that has singularly failed to maintain a satisfactory rate of self-financing.

Coverage has grown especially fast since 1990, when a wide-ranging early retirement program was introduced in anticipation of the employment-shedding that economic transformation was expected to bring. In 1991 alone, this added 500,000 retirees to the system. In 1991-92 the number of pensioners rose by 1.5 million in anticipation of job losses in connection with industrial restructuring. By contrast, the number of pensioners rose by only 1 million throughout the 1980s. The state has also supported widespread privileges in pension policy, allowing many groups of workers (for example miners and teachers) early retirement rights.

Pension contributions cover a sharply declining share of pension spending:

- Contributions to the main (non-agricultural) pension program covered 94 percent of spending in 1985, 83 percent in 1990, and 79 percent in 1995.
- The state budget has always been required to sustain pensions for the agricul-

tural population. Participants' contributions accounted for 25 percent of spending in 1985, falling to 11 percent in 1990, and an estimated 8 percent today. However, the presence of the Peasants' Party in the governing coalition makes the agricultural sector's position an extremely sensitive issue for the government to tackle.

- Many state firms are reported to be in arrears on their pension and social security contributions.

The burden of the pension system on the working population is enormous and growing:

- In 1990-95 the number of pensioners increased by 23 percent. In 1994 there were an estimated 7 million pensioners, representing one-quarter of the adult (over 18 years of age) population. Matters will grow worse as the baby-boom generation approaches retirement.
- An additional 2.6 million people are receiving disability pensions, 70 percent of whom are classified as category 3 (partial disability pensioners). This category is widely recognized as the one most open to abuse.
- A large proportion of the adult working-age population (peasants and the unemployed) though eligible for pension, makes no pension contributions.
- Pensions are generous by international standards. The minimum pension amounts to

around 39 percent of average earnings. Pension values are indexed to wages, which will grow faster than prices over the medium term.

The large and growing number of pensioners and the continuous electoral cycle (parliamentary elections in 1993, local elections in 1994) have impeded the timely resolution of this problem. Finance Minister Grzegorz Kolodko last year proposed that in the 1995 budget pensions be indexed to prices, not average wages. But Leszek Miller, the minister for labor and social affairs, thwarted the plan, and the labor ministry put forward a new pension system: a basic state pension for all (paid by the state budget and guaranteed initially at 30 percent, later at 20 percent of average earnings), supplemented by a system of compulsory contributions and a system of voluntary contributions. Despite the criticisms of the finance ministry, the government approved the plan on May 16. More discussions on pension system reform are expected following the presidential elections in November.

*Based on a recent report by Oxford Analytica, a United Kingdom-based research group.*

lion affiliates and 2 million active contributors, have attracted \$800 million and are expected to be managing \$3 billion by the end of 1995. In Colombia there are currently nine companies with 1.2 million affiliates and \$80 million in assets. Peru's six private pension funds manage \$200 million.

### Pension Reform in Eastern Europe

In Central and Eastern Europe, the establishment of private pension funds has not been accompanied by reform of the PAYGO system. Politicians have delayed reform because drastic cuts and reorientation of public expenditures are politically unpopular.

## Letter to the Editor

### Who Is Responsible for Postcommunist Successes in Eastern Europe?

By Mieczyslaw Kabaj and Tadeusz Kowalik

Professor Jeffrey Sachs ("Post-communist Parties and the Politics of Entitlements" (*Transition*, Vol. 6, No. 3, March 1995) claims that the victory of the left-wing parties in Central and Eastern Europe was the result not of unduly cruel market reforms, but of the actions of postcommunist parties to bring about pensioners' power, while promising to maintain, or increase, the entitlement of the social welfare state. In his opinion the elections in Eastern Europe have become "almost exactly" like those in Western Europe and the United States: dominated by interest group politics.

We do not agree with this assessment. The economic policies of the first democratically elected Polish government and the related social responses are unlike Western norms. We believe that the constant changes in government (six cabinets have been formed since 1989),

Private pension funds in Central and Eastern Europe are less significant than similar funds in Latin America. In Hungary and the Czech Republic participation in private funds is voluntary. Individuals are not allowed to redirect any of their pension contributions to private schemes, and high tax rates crowd out voluntary contributions to private funds. The Czech Republic operates a supplementary system of forty-one funds, which has 1 million participants and expects assets of \$100 million by the end of 1995. Hungary's ninety-three funds have 165,000 affiliates, and \$30 million in assets are forecast for the end

of the frequent elections and negative campaigns, the derailment of the economic policy, and the absence of right-wing parties from the Parliament since 1993, all have their immediate origin in the unduly cruel reforms.

Omitting an analysis of the events that led to an explosion of social expenditures, Professor Sachs claims that the blame should be placed on populist politicians.

But these politicians were responding to the demands of pensioners and peasants, traditionally conservative and protectionist interest groups. It was not careless social policy that led to the expenditure explosion. Instead, it was the unforeseen consequences of the overall economic policy and, in particular, of the stabilization program sponsored by the IMF and vigorously recommended by Professor Sachs.

of 1995. In Russia a presidential decree allowing the formation of private pension funds passed two years ago. But because there was no accompanying regulation, the system is threatened by fraud and public distrust.

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In Poland the ratio of social expenditures to GDP almost doubled between 1990 and 1992, rising from 10.7 percent to 20.1 percent:

Year	Ratio of Social expenditures to GDP (percent)
1989	10.0
1990	10.7
1991	17.0
1992	20.1
1993	20.7
1994	20.2

Source: K. Jedrzejewska, Polish daily "Rzeczpospolita," June 13, 1995.

A plunge in overall demand in 1991 and 1992—triggered by price liberalization, a simultaneous, almost total freeze on wages and other incomes, and the sudden opening of the unprepared Polish economy to foreign competition—caused unemployment to swell and led



many in the work force to choose early retirement.

The initial, excessively high unemployment benefits severely drained the budget. Advocates of the "shock therapy" assumed that rapid restructuring, the dynamics of a free market economy, and a huge inflow of foreign direct investment would contribute to the rapid absorption of the "temporarily" unemployed. However, unemployment turned out to be not only massive but also permanent. As a consequence of the "shock," 5 million Poles (26 percent of the labor force) moved from the production sphere to the redistribution and social spheres. Paradoxically, our liberals, fighting against the "oversocialization" of the economy (Professor Balcerowicz's favorite expression), created a gigantic social welfare state, in which the number of people depending on income redistribution, approaches the number in the active work force that is generating the national product.

It is hard to share Professor Sachs's view that in the postcommunist countries "the living standard of the population did not really drop, if one examines actual household consumption behavior." Even if one accepted his view, the question remains as to whether the distribution of incomes and thus the living standard of various social groups, was unchanged. Numerous analyses indicate that the rapid creation of a market economy and rapid privatization caused considerable stratification—in other words, rapid enrichment of the few and impoverishment of many. The very fact that Polish unemployment reached 16 percent—or, including early retirements, more than 20 percent—resulted in the impoverishment of millions.

Professor Sachs is right in emphasizing that the real wage indices do not take into account the positive effects of the transition from the economy of shortages to a balanced consumer's market. We are not suggesting that either the 1989-93 indices in Poland of real wage dynamics (100, 68, 66, 58, and 55, respectively) or the indices of the incomes from private farming (100, 50, 41, 46, and 48, respectively) accurately reflect the magnitude of decline in these groups' standard of living. Nevertheless, in Poland as well as in all postcommunist countries, apart from the Czech Republic, impoverishment has increased so much that it could not be compensated by the benefits of a balanced market, the reduction of waste, and second economy employment, mentioned by Professor Sachs. The deep decline of monthly food consumption in Polish households, shown below, underlines our argument.

#### Average Monthly Per capita Consumption in Poland

Food item	1989	1994	Change (kilogram)(percent)
Flour	1.14	0.95	-16.7
Bread	6.92	6.9	20.0
Potatoes	8.01	6.84	-14.6
Vegetables	5.06	5.00	-1.2
Fruits	3.00	3.39	13.0
Meat	5.01	4.51	-10.0
Fish	0.46	0.42	-8.7
Oil and fats	1.58	1.41	-10.8
Butter	0.73	0.33	-54.8
Milk (liters)	7.26	5.53	-23.8
Cheese	0.92	0.72	-21.7
Eggs (units)	15.8	12.74	-19.5
Sugar	2.06	1.66	-19.4

Source: 1990 Statistical Yearbook and May 1995 Statistical Bulletin. Central Statistical Office, Warsaw.

It should be noted that the postcommunist countries have already

undertaken certain "reforms" in social services. The increase in social expenditures was accompanied by the opening some social services to the free market. Between 1989 and 1993 the state reduced educational and health expenditures by around 40 percent, shifting part of the costs to household budgets. Since a large part of the population is impoverished, the health and education sector is heavily underfunded and their employees are consequently underpaid. This also affects living standards.

Disappointed voters, worried about poverty and uncertain about jobs, wages, and pensions, led the postcommunist parties to victory. The left-wing parties (postcommunist and peasants' parties) captured more than three-quarters of the farmer vote; almost half the votes of white collar workers without higher education; about 40 percent of the vote of blue collar workers, intellectuals, and pensioners; and one-third of the vote of high school and university students and the self-employed. Thus, apart from the farmers (who generally voted for the peasants' party), the division of electorate did not correspond to the criterion of socio-professional groups. Although the left wing did not win the election, a large percentage of poorer and poorly educated voters have turned their backs on the parties originating from the democratic (post-Solidarity) tradition. Hence, simple analogies to elections in Western countries, where interest groups' voting patterns are well established, are largely confusing.

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## Quotation of the Month: "You Must Have a Message, and Sell It."

*New York Times* correspondent Jane Perlez analyzes the charismatic Prime Minister of the Czech Republic

Vaclav Klaus, the conservative economist who is Prime Minister of the Czech Republic, is on stage in the cultural hall of Sokolov, a coal-mining town where the pollution is so bad the air tastes of grit. He is explaining to an admiring audience how all is well in the land. Unemployment, at 3.3 percent, is the lowest in Europe. Inflation is 10 percent, one of the most moderate rates in the former Eastern bloc. And the country has a healthy budget surplus of \$400 million, the only Central European nation in this enviable position.

The sole dissonant note during the smoothly orchestrated performance comes from some students in the balcony holding up a white banner to protest proposed nationwide fees for university education, and the combative Klaus rises to the provocation.

"Why should anyone in this room pay for the investment in somebody else's future?" asks the Prime Minister, cutting the air with a few karate chops and staring down his young critics. The audience, mostly middle-aged and elderly, likes the jousting and erupts in applause.

Klaus, in a double-breasted blazer that matches his graying hair, sounds like a professor going for the kill. "Every investment costs something," he says. "If you want to invest, you have to pay something first. Then you get your money back." There's not even a whimper from the balcony, the banner disappears and Klaus moves on to another favorite theme, even more radical in a post-Communist society: means-tested welfare and social security benefits.

"I'm convinced not everyone should get them," he says. "Why should the people in this room support the [benefits of the] general director of the porcelain factory? We don't think these people should have them, and I think you all agree." Everyone in the auditorium, most of them members or believers in the Prime Minister's Civic Democratic Party, nods in agreement.

Vaclav Klaus is the most uncommon political leader in Central Europe. He was not a dissident; he was not a reform Communist. In the 1970s and 1980s he developed an affinity for free-market thinkers like Milton Friedman and Friedrich von Hayek as he argued with other junior colleagues in the state bank about the right economic model for a future Czechoslovakia. At 54 he even looks different: none of the overindulgent pudginess, wan complexion or badly cut suits one usually encounters among the bureaucrats of Central Europe.

For the Czech Republic, after more than five years of Klaus's free-market policies, the results are obvious, even in village squares far from Prague's bustle and swagger. With the speedy series of highly organized privatization steps following Communism's fall in 1989, the Government now boasts that close to 80 percent of the economy is wholly or partly privatized, although independent analysts put the figure closer to 60 percent.

So far, in order to maintain social peace, he has maintained much of the safety net. Rent controls, for example, as well as subsidies for electricity and heating have remained in place. This year Klaus

is trying to nibble at the allowances paid to all families for children up to age 18 no matter what the family income. He has introduced legislation gradually to raise the retirement age for women from 55 to 62 and for men from 62 to 65 and to impose means tests for some additional social security benefits.

Klaus was appointed Finance Minister in the heady days of December 1989 and elected Prime Minister in June 1992. Mass privatization, his chief instrument of change, effectively transferred the vast majority of state-owned companies to the private sector by the end of 1994. Under the Klaus plan, every adult could buy a booklet of vouchers for about \$35 and then either invest in a broad-based mutual fund or use the vouchers to bid for shares in individual state enterprises. The strategy gave Czech citizens a large and stable stake in the transformation process.

At the same time, restructuring big enterprises, many of which still retain archaic management and a bloated work force, [has been delayed]. Worse, many newly privatized companies have big, bad debts, which are held by state banks, which in turn own many of the investment funds in which Czechs have invested their vouchers.

The Prime Minister believes the marketplace will take care of everything: "I don't think the free market means high unemployment. I don't think the free market means thousands of bankruptcies a day." He expects that rapid expansion of new businesses, many of them connected to the Czech Republic's tourist boom, will absorb the fallout from

structuring inefficient and costly enterprises, like O.K.D. coal mines in Ostrava, where there are more than 60,000 employees.

Though he had never participated in politics before November 1989, Klaus probably has had the fastest trajectory of any leader in Central Europe. This is largely because he understood, more quickly than Havel and his dissident friends, the need in a modern political party for a power base beyond his expertise as an economist. What was the source of his political instinct? "What you must have as a politician is an un-

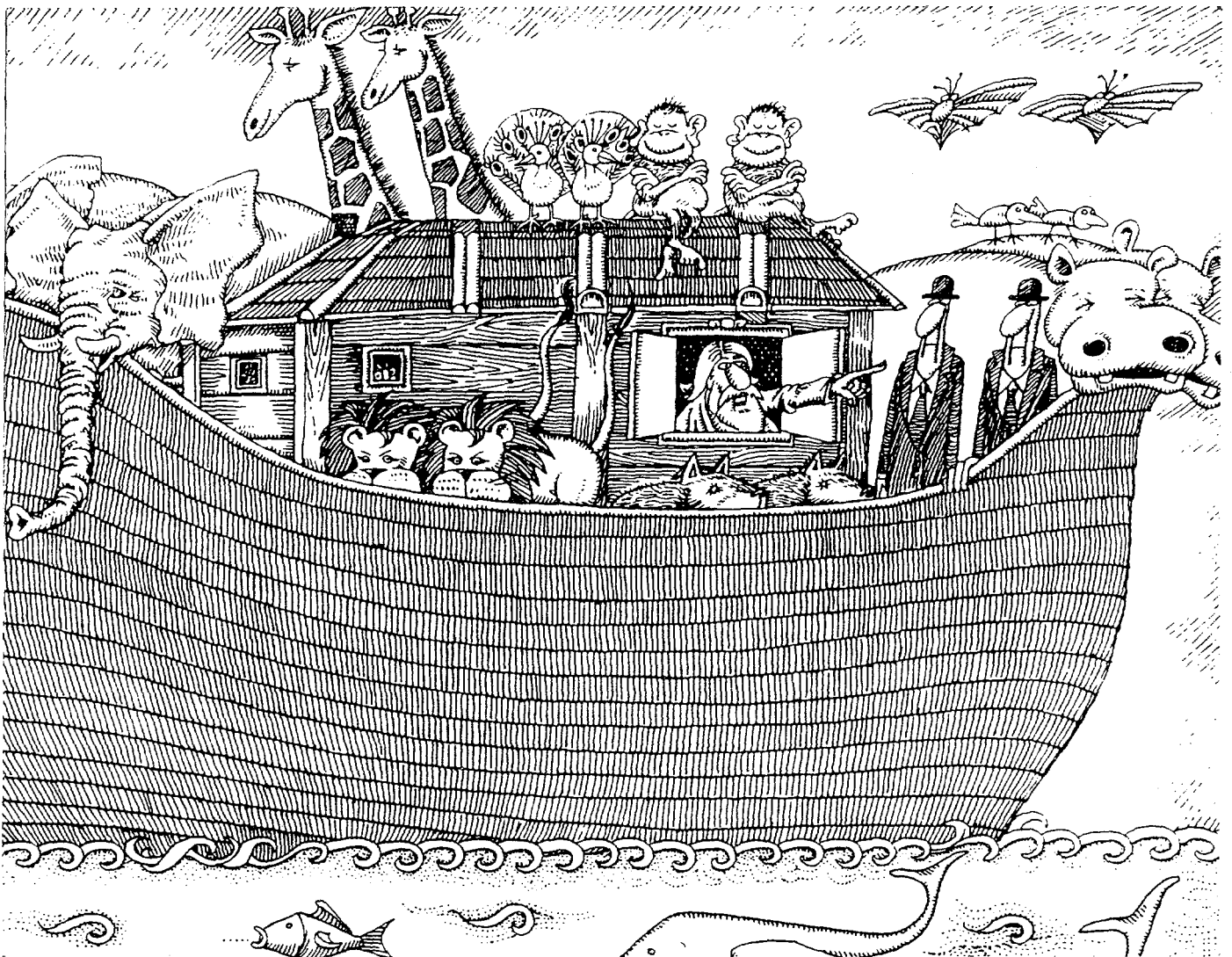
derstanding of the relationship between the citizen and the state. I had been spending all my life studying economics, studying money, public finance. And public finance is nothing else than a sophisticated discussion of the relationship between the individual and the state."

He also understood the need to communicate. "You must have a message and sell it." As a vehicle for his message, he carved a party out of the remnants of Havel's Civic Forum, the opposition grouping that had brought down the Communists. Through his Civic Demo-

cratic Party, Klaus has run a permanent campaign that reaches deeply into the country.

Some economists still believe that Klaus's biggest test is yet to come. How will society react to restructuring and bankruptcies of the newly privatized companies. Klaus "has been more right than wrong" said one Western diplomat. Klaus would surely agree with this assessment.

*Excerpted from "The Fist in the Velvet Glove," New York Times Magazine.*



Noah: "The two economists immediately disembark!"

From the Hungarian magazine *Hocipo*

# Are Russian Enterprises Restructuring?

by Gilles Alfandari and Une Lee

**I**n Russia enterprises are restructuring, even if to a limited extent. That was the general conclusion of a conference, "Russia: Economic Policy and Enterprise Restructuring," held in St. Petersburg on June 12-13, 1995. The conference was organized jointly by the World Bank and Russia's Economic Ministry. Eight of the fourteen conference papers used for their analysis came from a mid-1994 World Bank survey of 439 Russian industrial enterprises. The first comprehensive, randomly selected, representative survey of Russian enterprises, it embraced the major manufacturing industries across economic regions, covering state-owned and privatized firms as well as newly established private firms.

The following is a brief overview of some of the papers presented at the St. Petersburg meeting.

## Trading Wages for Employment

Russian enterprises have been buffeted by a combination of aggregate demand shocks and supply shocks, including the major negative effect associated with the collapse of both the Council of Mutual Economic Assistance (CMEA), and trade among the countries of the former Soviet Union. Industrial production in late 1994 was roughly half of the 1990 level, according to official data. In response to these shocks, Russian enterprises are restructuring. However, progress appears to be uneven across industries and regions, and the extent of restructuring is limited.

Qimiao Fan and Bingsong Fang in their paper report that the majority of enterprises have introduced new products, increased product varieties, and initi-

ated new trading relationships. There is some evidence of layoffs and real wage contraction; between 1990 and 1994 average monthly wages in constant prices decreased by about 15 percent. During the same period, on average, full time employment declined by 10 percent, while the average number of employees who either were working part time or were on unpaid leave increased by more than two-and-a-half times.

Labor sharing is more common than labor shedding, as suggested by Rostislav Kapeliushnikov and Sergei Aukutsionek in their paper, **Russian Enterprises in the Labor Market: Evidence from the Russian Economic Barometer**. They show that the labor utilization rate, reflecting various forms of labor underutilization, including workweek reduction and involuntary leave, fluctuated between 70 and 80 percent throughout 1994.

Labor hoarding is still extensive in Russian enterprises despite some initial adjustment in employment and working hours. Simon Commander, Sumana Dhar, and Ruslan Yemtsov point out in their paper, **How Russian Firms Make Their Wage and Employment Decisions**, that Russian enterprises, most of which are dominated by a coalition of managers and workers, have remained reluctant to lay off workers. Instead, because of the influence of these coalitions, employment and worker welfare are among the enterprises' objectives.

As a pattern of adjustment in Russia, enterprises have partially traded down wages for employment stability. Money wages have remained low and drifted slightly downward in real terms, while their share in total compensation has

declined. Workers' compensation has become increasingly dominated by the nonmonetary components, principally social benefits, provided by the enterprises, including newly established firms. Simon Commander, Une Lee, and Andrei Tolstopienko report in their paper, **Social Benefits and the Russian Industrial Firm**, that the low level of money wages and their diminished share in total compensation generates adverse incentive effects, raising the incentive for workers to stay in benefit-providing firms, while simultaneously delivering low effort in their primary employment. Although low aggregate unemployment levels are maintained, low money wages may ultimately impede effective restructuring and the growth of an autonomous private sector.

## Budget Constraint Leaks

Although government funding for the enterprise sector has hardened significantly since the beginning of the reforms in 1992, access to soft financing is still available through government subsidies, bank loans, and payment arrears (in particular due taxes). However, this softness is sending the wrong signals to managers, allowing chronic loss-makers to survive.

Gilles Alfandari, Qimiao Fan, and Lev Freinkman discuss transfers of the federal government in their paper, **Government Financial Transfers to Industrial Enterprises and Restructuring**. Although these transfers have dropped substantially since 1992, they still accounted for 6 to 7 percent of GDP in 1994. This figure would be much higher if financial transfers of local governments were included. The paper concludes that, in general,

government transfers have not helped enterprise restructuring.

Financial softness can also be manifested through payment arrears. Gilles Alfandari and Mark Schaffer's paper, **On Arrears in Russia**, reviews delayed enterprise payments to suppliers (trade credit in arrears), to the government (tax arrears), and to employees (wage arrears).

The level of involuntary trade credit in Russia, including its portion in arrears, is comparable to OECD averages. Russian authorities, however, should be more concerned with tax arrears, whose flow has been estimated at 2 percent of 1994 GDP. Adding tax arrears to more explicit forms of subsidies, only one-fifth of Russian enterprises can be considered free of subsidies. Tax arrears and other subsidies are also concentrated in firms in financial distress (those with both liquidity and profitability problems). While financially distressed firms account for only 12 percent of the survey sample, they account for 70 percent of tax arrears.

Despite an initially low stock of bad loans and declining volume of directed bank credit, the banking sector constitutes an additional source of softness, as discussed in the paper of Mark Schaffer, Qimiao Fan, and Une Lee. About 25 percent of enterprise debts to banks are overdue. In addition, the flow of bank credit to enterprises in arrears is continuing, aggravated by the general practice of recapitalizing the overdue interest and rescheduling the principal.

Both papers suggest that firms with the greatest bargaining power, in terms of their size, market power, and membership in industrial associations, are most successful in lobbying for government transfers. This view is confirmed by the concentration of subsidies in agricul-

ture, energy, and the military-industrial complex. Similarly, managers use wage arrears to lobby the government for subsidies.

### **Ownership and Institutions**

Has a change in ownership had any effect on firm behavior, given that most of the privatization has been carried out by workers and managers? Ownership change has generally had only weak effects on most performance indicators, including sales, wages, and employment. Apart from the newly established firms, (the topic of the paper by Andrea Richter and Mark Schaffer), the majority of privatized and state-owned enterprises do not differ significantly from each other.

John Earle, Saul Estrin, and Larisa Leshchenko wrote **Ownership Structures, Patterns of Control, and Enterprise Behavior in Russia**. They suggest three reasons that ownership has not changed enterprise behavior: ownership has not yet translated into control, budget constraints have remained soft, or privatization is too recent to have influenced behavior. They also suggest that the Russian mass privatization program may have done little to challenge insider-controlled firms. In their view, encouraging market competition and ensuring the tradability of ownership rights could stimulate the emergence of more effective ownership structures.

Barry Ickes, Randi Ryterman, and Stoyan Tenev explore whether market structure has affected Russian enterprises' inclination to adopt some kind of adjustment strategy. Their paper, **On Your Marx, Get Set, Go: The Role of Competition in Enterprise Adjustment**, is based on a 1994 survey of 150 enterprises in five Russian oblasts.

They conclude that an enterprise will be less likely to adjust if it depends too much on trading partners. Competition can either enhance or block the adjustment preference of an enterprise: if competition is too intense, enterprises will be less likely to enter the restructuring process. One possible explanation is that the destabilizing nature of intense shocks can hinder rather than promote restructuring. The authors suggest that enhanced information, improved legal and financial institutions, and better physical infrastructure can balance some adverse consequences of the shock.

Most authors agreed that the adjustment process in Russia has proceeded since the beginning of reform. Enterprise restructuring occurred primarily in the passive sense: firms responded in the aftermath of the shocks. That restructuring has so far been limited is probably not surprising.

The ownership changes have been very recent, the economic environment is still unstable, and the basic market institutions and infrastructure are still at an early stage of development. Clear property rights and harder budget constraints are required. In addition, there is an obvious need for the government to fill the present institutional vacuum.

*Copies of the conference papers can be obtained from Yolanda Gedse, Room H-2025X, The World Bank, 1818 H Street, N.W., Washington, D.C. 20433, tel. (202) 473-7034, fax (202) 477-3288, (Email: YGedse@Worldbank.org @internet). (It is expected that selected conference papers will be published in a book.)*

# World Development Report 1995: Workers in an Integrating World

The World Bank released, in late June, its 1995 *World Development Report* dealing with labor issues. Some of the most important thoughts, conclusions, and statistics from the 250-page volume are summarized below, with special attention to issues related to transition.

## Postsocialist Workers, Unite!

Of the world's 2.5 billion workers, 1.4 billion live in countries struggling with transition from central planning or high degrees of protectionism. Moves from central planning to market systems, and from protectionism to openness, are key to increasing opportunities and incomes. Economic reform can create opportunities for some workers, but it can have wrenching effects on others. But the costs lie in the disease, not the medicine: effective reform brings gains for workers. Governments can reduce the costs of transition by supporting mobility (reforming housing markets), providing transfers (through unemployment insurance or public works), and equipping workers for change (through training and education).

In the short term workers often feel the pain as real wages fall, unemployment rises, and employment shifts toward informal activities. In Bulgaria, the Czech Republic, Poland, Romania, and Russia official statistics show that real wages fell between 18 and 40 percent in the first year of transition. Moving the economy as quickly as possible toward a new growth path is key to minimizing the pain and social costs of adjustment. In this process macroeconomic stability and credibility of the overall reform are critical.

Structural change will hurt workers, either temporarily if reallocations are involved, or permanently if labor productivity is below what earlier wages justified. The main challenge is to allow the transformation to a private economy while minimizing social dislocations and transitional costs in unemployment.

In transition economies wages have exhibited a fair degree of downward flexibility; the challenge is to increase mobility across sectors. Nonwage labor costs are high and should be reduced in the context of comprehensive reform of social insurance schemes. Unions are expected to continue playing a positive role at the firm level in improving workers' wages and conditions. However, they are likely to continue opposing rapid reforms unless the workers that stand to lose receive proper support and compensation.

## Political Economy



"We returned to economic planning; systematically we give up everything."

From the Hungarian magazine *Hocipo*

There is a serious risk of a stalled or incomplete transition if social tensions are not addressed. Managing the social dimension of the transition, maintaining the quality of social services, enabling rapid job creation, and avoiding the spread of poverty are all key goals, but they must also be balanced with fiscal probity to ensure both social and macroeconomic stability.

## Blame Domestic Policy

- Countries that engaged in the international economy and relied heavily on domestic markets achieved the most rapid growth in wages and jobs. Where exports have risen fast, so have real wages.
- International competition has undoubtedly increased over the past two decades, but current import levels with developing countries—at about 3 per-

cent of industrial countries' GDP—are too small to account for much of the woes in the industrial-countries' labor market. The occasional sharp rise in unemployment in these countries owes more to reduced demand for unskilled labor, due to technological change combined with rigid wage and social security systems, than to competition from cheap labor in emerging economies. The key to helping the unskilled in industrial countries lies in domestic policy.

- Industrial countries already reap benefits from the integration of developing and transition countries into the global economy, as these countries are purchasing a large and growing share of industrial country exports. Expansion of trade brings all workers immediate gains through lower prices for consumer goods and enables workers to move, over time, into better jobs, instead of remaining hostage to domestic demand.

- For emerging and industrial economies alike, investing in education and training gives people skills that they can transfer from job to job and improves workers' ability to perform standard tasks, to process and use information, and to adapt to new technologies and production practices.

### Stronger Labor Force

- Twenty years ago two-thirds of the world's workers were largely cut off from international markets by protectionism and central planning; by 2000 more than 90 percent of the world's labor force will be working in countries with strong links to the global economy.

- Over the next three decades the world's present 2.5 billion labor force (almost twice as large as in 1965) will increase by another 1.2 billion. Ninety-nine percent of that rise will be in low- and middle-income countries.

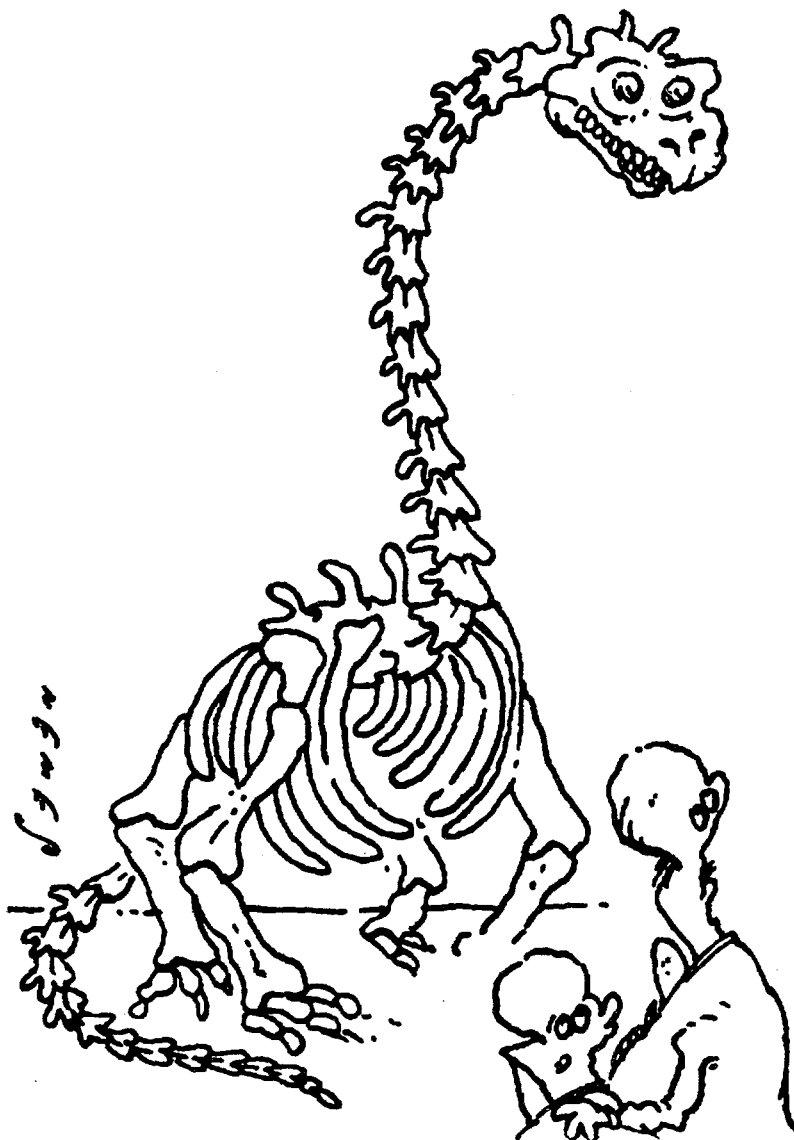
- Well over half the world's working-age population of 2 billion people live in low-income economies where average income per person was below \$695 in

1993. Another 600 million live in middle-income countries and a fortunate 300 million live in high income countries with an annual income per person of around \$8,830 in 1993. Some 120 million workers—3 percent of the working-age population—are unemployed globally.

- In low-income countries 61 percent of the labor force work in agriculture and 22 percent are employed in rural non-farm jobs, or obtain urban informal employment. Only 15 percent of workers

have formal wage contracts—mainly in industry and services. In high-income countries only 4 percent work on the land, 27 percent in industry, and 60 percent in services.

World Development Report 1995: Workers in an Integrating World (New York: Oxford University Press, 1995). To order: World Bank Publications (see ordering information under New Books and Working Papers section).



**"They lived peacefully for millions of years, then one came forward with an economic stabilization package."**

From the Hungarian daily *Vilaggazdasag*

# Book Review

## Anders Aslund: How Russia Became a Market Economy

reviewed by Martin Schrenk

Anders Aslund was one of the best known foreign advisors to the Russian government in 1991-94, the most turbulent period of transition. His recent book is a record of this adventure, a personalized account that leaves the reader with no doubts about the author's loyalties and convictions. Aslund wrote the book immediately after his departure from Moscow and wrote it quickly. Not meant to be a detached academic treatise, the book aims to reach a nontechnical audience, which is both its strength and weakness.

As the past tense in the title indicates, Aslund believes that Russia has indeed crossed the Rubicon, and become a market economy. Products, labor, capital and property are allocated by markets, although—as he readily admits—often by highly imperfect markets. Aslund firmly believes that the basic institutions for a democratic regime have also been put firmly into place. His criticisms on particular issues should be seen against this underlying optimism.

While the book does not offer new analytical insights, it gives a first-hand insider report of the chaotic, stop-go process of system change, sometimes propelled, sometimes stalled by the shifting alliances and clique-fighting of an unhomogeneous leadership (which is itself constantly changing) and by shifting access of various players or groups to the President, the ultimate arbiter. Since this is the least understood aspect of transition in Russia, even the expert will find illuminating new facts to better our

understanding of the confusing events in Russia and their eventual outcomes.

### Old New Elite?

The role assigned to the old elite (senior civil servants, party officials, and senior managers) shows the strength and weakness of this personal approach that allows the author to characterize the old elite as rent-seeking, corrupt, criminal,

by the old elite were true, would not these same people become the new business elite, the core of the new money aristocracy? The huge and sudden accumulation of wealth in Russia certainly could not be explained by the "virtue of thrift." Last century's ruthless businessmen in the United States or the contemporary "nouveau riche" of Latin America suggest that the characteristics assigned to Russia's old elite, rather than being system-specific, are symptoms of what Gunnar Myrdal called the "weak state." The chapter on privatization refers repeatedly to the "socially corrosive distributional result" of rapid privatization. It seems that the ambiguity surrounding this core problem points to important issues not yet thoroughly plumbed by socioeconomic research.

In contrast to the new business elite, the new political elite receives considerable attention. In the author's view successful transition can only be carried out by a small minority of "reformist technocrats." He consequently rejects the view that speed and technocratic decisionmaking are by definition undemocratic. His argument might be interpreted as advocacy of authoritarian rule justified by the difficulties of establishing effective government in the absence of democratic traditions. Aslund believes that nobody above the age of 40 can understand the challenges of transition, since they have not been exposed to modern social science during their formative years. It will take decades, maintains Aslund, to train enough lawyers to create an effective

HOW RUSSIA  
BECAME A  
MARKET  
ECONOMY  
ANDERS ASLUND

vicious, and asocial, and to accuse them of large-scale theft of social property and being the principle obstacle to system transformation.

But while demonizing the old elite, the book has little to say about the ethics of the emerging, new, business elite, although the chapter on privatization reveals the author's considerable unease about how to handle this issue. For if the alleged massive theft of social property



Russian "culture of law" in commercial matters.

### It's a Cultural Thing

In Aslund's world cultural change in the broad sense plays a central role in the transition process. While he sees rudimentary democratic structures and the basic market institutions as now formally and firmly in place, he still considers the state as inherently weak because of the fragility of the new culture and the tiny size of the technocratic elite. He therefore proposes "far-reaching deregulation and laissez-faire" economics as the only feasible interim solution, using the analogy of developments in Western Europe and the United States during the nineteenth century. It is not clear whether this proposal is meant to exploit the institutional void boldly by letting loose entrepreneurial activism.

Throughout the book, particularly in Chapter 6, privatization is pronounced the real success story of system reform. Aslund's criterion of success is apparently the share of firms that have been privatized under one or the other option of the Privatization Law (or the share of workers in such firms). The relevance of this formal criterion for success or failure of the ultimate purpose of system reform—emergence of a vibrant market economy—will undoubtedly be questioned by many readers. But Aslund himself recognizes that the legal act of privatization is inconsequential, in the absence of efficient primary and secondary securities markets, and an efficient and liquid banking sector ready to provide long-term financing.

Aslund concludes with an excellent chronology of events since the beginning of the transformation but fails to explain why the estimated cumulative contraction of GDP reached 33 percent in 1990-94 (table 8-2), although employment declined by only 6 percent (table 8-1). It

is possible that either productivity (output per man-hour) or the average number of active man-hours plummeted, which would suggest burden sharing among workers.

Alternatively, a large number of workers could have been unemployed in fact but counted as employed. At any rate, the differences between output and employment trends is clearly an important issue for assessing progress and success of transition.

### Searching for a Threshold

Most observers, including Aslund, seem to agree that transformation is not sustainable politically unless the accompanying social costs are kept below a critical threshold. While this level cannot be determined through economic analysis, extension of the qualitative argument to an explicit cost-benefit analysis would be feasible in principle but has never been tried.

Aslund offers some interesting observations for such an analysis. According to his evidence, in 1994 real wages were only 10 percent less than in 1987, although an adjustment for improved selection of consumer goods and the end

of a shortage economy (and of long lines) brings the margin down further.

But the comparison of costs and benefits should also consider the cutback or elimination of earlier free, or inexpensive, services. The balance is further complicated by the implications of shifts in income and wealth distribution, accompanied by rapid privatization. Aslund deserves credit for addressing this issue, which has been ignored or dismissed by most authors.

Anders Aslund's, *How Russia Became a Market Economy*, is published by Brookings Institution, Washington, D.C., 1995, 378 p.

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*Martin Schrenk is Economist in the Transition Economy Division, the World Bank.*



From the Russian daily *Kommersant*

## Milestones of Transition

**Croatia's** economy has achieved a high degree of economic liberalization compared with Europe's other transition economies, senior World Bank researcher Martha de Melo told an international conference in Dubrovnik. She is co-author (with Cevdet Deniz and Alan Gelb) of the Bank's forthcoming study "From Plan to Market: The Patterns of Transition," which appraises countries based on a liberalization index (covering prices, trade, exchange rates, privatization, and reflecting the duration as well as the intensity of reforms), comparable to such indicators as growth and inflation. According to this index, Croatia ranks high on the list, in part because of early reform measures introduced before the split of the former Yugoslav Republic.

Capital flight from **Russia** amounted to some \$80 billion by the end of 1994, according to the head of the Russian bureau of Interpol Y. Melnikov, who said capital continued to leave the country at \$1.5 billion per month in 1995.

**Russia's** first-half GDP fell 6 percent from a year earlier, compared with a 15-percent drop for all of last year. Russia's GDP stood at 606 trillion rubles (\$134.6 billion) in the first half of 1995, while industrial output—at 420 trillion rubles (\$93.3 billion)—dropped 3 percent over the same period, according to Prime Minister Viktor Chernomyrdin, who quoted these figures in his address to the Duma on July 19. The economy is now shrinking at the lowest rate since the Soviet breakup. In June the GDP rose 3 percent over the previous month. But the inflation rate, expected to slow to 5.0 or 5.5 percent in July, did not approach the average monthly rate of 1 percent envisioned by the IMF in April for in the second half of this year. Despite unexpectedly high inflation, since early May, the ruble has gained back 12.5 percent

of its value against the dollar, trading well within the band that the Central Bank promised to defend through October.

**Russia's** draft 1996 budget envisages revenues of 355 trillion rubles (\$79 billion), expenditures of 440 trillion rubles (\$98 billion), a budget deficit equal to 4 percent of GDP, and inflation of no more than 2 percent a month, Finance Minister Vladimir Panskov announced in early July. Spending on health, education, and other social spheres will increase. More money is being allocated to convert the military-industrial complex and to high-technology projects. The deficit, moreover, is to be covered from noninflationary sources, with an emphasis on domestic rather than foreign borrowing. In recent months the government has reduced its wage debt to 100-200 billion rubles and had sent 306 billion rubles to the regions to ease social tensions, Panskov added.

**Russia** will not import grain this year despite one of the worst droughts in 20 years, Deputy Prime Minister Aleksandr Zaveryukha said on July 25, citing good prospects for the grain harvest in Siberia. But since spring sowing in Siberia was delayed this year, late ripening could mean problems in the event of early snow.

The **Russian** Federation Council fixed the subsistence minimum for 1996 at 218,000 rubles (\$48) per month. This figure is the basis for determining minimum salaries, pensions, scholarships, and eligibility for social support. The subsistence minimum will be quarterly indexed to the inflation rate. On July 19 the lower house of parliament raised both the minimum wage and minimum pension to 55,000 rubles (\$12) a month, as of August 1. The minimum monthly wage currently stands at 43,000 rubles

(\$10) and the average monthly wage at 495,000 rubles (\$109).

**Russia** extracted 2.5 percent less gas and oil in the first half of 1995 than it had during the same period in 1994, Russian radio reported July 19. The only bright spot in this picture was firms that received Western investment, whose production increased during the same period.

**Russia** plans to raise its value-added tax (VAT) rate from 20 percent to 21 percent beginning in January 1996, Finance Minister Vladimir Panskov announced on July 21. Russia's 1995 budget foresees 50 trillion rubles in VAT revenues out of a total anticipated tax revenue of 128 trillion rubles.

In **Russia** more than 14,000 individuals and firms evade taxes entirely. This evasion costs the government some 7.3 trillion rubles, said the head of the Federal Tax Police, Sergei Almazov, on July 20. The tax police have been able to do little to combat this rising tide of evasion because the government gave it only 23.6 percent of the money it needed. Almazov also lashed out at the Duma for passing a law that gives tax evaders the same punishments as it accords to those who engage in illegal hunting or cruel treatment of animals.

The **Russian** government approved a list of strategic companies to be held back from privatization this year, paving the way for the sale of 6,000 other companies beginning in August. The government, which earned 104 billion rubles from privatization in the first half of this year, is timing the sales to coincide with an expected investment boom in early autumn.

**Poland** took a step forward in its mass privatization plan by beginning to allo-

cate leading (33 percent) shares in 413 participating state enterprises (worth \$3 billion) by lottery to 15 national investment funds run by joint domestic-foreign management firms. On July 18 fund managers completed the selection process ahead of schedule. Tradable certificates, entitling the bearers to one share in each fund, are expected to go on sale to 28 million eligible Poles in mid-November. The sale price will equal 5 percent of the average wage. More than 4,400 enterprises, with a book value of \$35 billion, still remain in the public sector.

**Polish** Finance Minister Grzegorz Kolodko said he is determined to bring down inflation to 20 percent by the end of 1995 but warned that success would come at the price of a slowdown in exports and growth later in the year. Planned measures include liberalization of some food imports, more intervention in the food market, tighter wage and price controls, and stricter budgetary discipline to allow the zloty to rise. Consumer prices rose by 1 percent in June, the lowest monthly rate since August 1991. Industrial production was up 11.7 percent over June 1994.

How is **Poland** doing in comparison to other Eastern European countries? The report of the Polish Central Planning Office issued on July 6 says that Polish and Slovenian 1994 growth rates, at 5 percent, were the highest in the region. Poland and Estonia are expected to take first place in 1995, with growth rates of 6 percent. Polish exports rose 22 percent in 1994, but Slovakia, Hungary, and Romania registered even greater growth. Inflation in Poland in 1994 was 32.2 percent compared with 10.2 percent in the Czech Republic and 320 percent in Russia. With regard to unemployment, Poland placed seventh in Europe as a whole (with Macedonia, the rump Yugoslavia, and Spain topping the list). Poland was the only country in the re-

gion whose foreign debt decreased, despite being the second largest in the region in relation to GNP (42 percent), second only to Hungary's (72 percent). Poland's budget deficit amounted to 2.7 percent of GNP in 1994 compared with 10.4 percent in Hungary and 9.3 percent in Russia.

According to the Overseas Private Investment Corporation, U.S. investment in **Poland** tops \$1 billion, making the United States the largest investor in Poland.

In a public opinion poll conducted in **Poland** in June by the Center of Public Opinion Research (OBOP), a majority of respondents (53 percent) were for legalizing abortion if the woman was in difficult conditions. Women do not generally differ in their opinions from men. The oldest and youngest Poles are least inclined to support the legalization of abortion, Rzeczpospolita reported on July 17.

The **Czech** Statistical Office (CSU) predicted that GDP would grow by about 4 percent in 1995 and between 4.4 and 5.2 percent in 1996. Unemployment should rise to 3.8 percent in 1995 and to 4 to 4.8 percent in 1996. The rate of inflation is expected to drop from the present 10 percent to 9.5 percent in 1995, and to 8.5 to 9 percent in 1996. Nominal wages will grow by about 16 percent a year, so that the annual growth of real wages will grow 6 to 7 percent. It is expected that the increase in household incomes will push private consumption up by 6.6 percent in 1995, and by 7.2 to 7.8 percent in 1996.

In June the **Czech** trade deficit widened further, with a monthly 9.2 billion koruna (\$354 million) deficit taking the first-half deficit to 46.9 billion (\$1.8 billion). The data for June show no sign that the trade balance will begin to improve in the near term, government officials predict. Ex-

port growth from January to June was only 6.4 percent as against import growth of 32.4 percent.

**Czech** wage regulations were lifted on July 12. Wages have been controlled since July 1993 for firms with more than 25 employees, with rises pegged to inflation and company performance. In another development the Czech parliament passed a law to raise the pension age gradually over the next 12 years. The pension age for men will be raised from 60 to 62 by the year 2007, while women—who were allowed to retire between age 53 and 57, depending on how many children they have—will now be pensioned off no earlier than age 57 to 61.

On June 29 **Czech** lawmakers voted to reduce taxes further than the government had requested. From next year, therefore, the highest rate of income tax will fall from 43 percent to 40 percent (for people earning more than 564,000 koruny annually). The threshold for paying tax was raised by 2,400 koruny to 26,400 koruny annually, and the bands for lower income tax rates were widened. Company tax was reduced from 41 percent to 39 percent. Only taxes on cigarettes, nonleaded petrol, and sparkling wine went up. Finance Minister Ivan Kocarnik said the tax reduction would take 22.5 billion koruny out of the state budget.

On July 7 the **Czech** government approved a deal for three international oil companies—Shell, Agip, and Conoco—to take a 49 percent interest in the two biggest Czech refineries. These companies will pay a total of \$173 million outright, and investment over the next five years is estimated to total up to \$500 million.

**Czech** Economics Minister Karel Dyba announced that the state would sell a 27 percent stake in SPT Telecom, the tele-

communications monopoly, to Swiss Telecom and PTT Netherlands for 1.32 billion dollars. Although holding a minority stake, the Western firms will take three of the five seats on the company's management board, giving them day-to-day control of the company.

Foreign direct investment totaled \$117.2 million in the first quarter of 1995, up 37 percent from the same period last year, the Czech National Bank reported. Germany accounted for 43.6 percent of the total 1995 first quarter inflows, followed by the United States (33 percent) and Austria (6.8 percent). Construction, banks, and insurance companies were the most attractive sectors. (FDI reached \$862.4 million in 1994 and since 1989 has totaled \$3.22 billion.)

Latvia has opened its first fully functioning stock exchange since 1940, when Soviet authorities closed the Riga bourse.

As of June 30 about 5,620 of Lithuania's 6,700 state-owned enterprises marked for privatization had been sold.

EU Agriculture Commissioner Franz Fischler warned that the eastward enlargement of the European Union would disrupt the Common Agricultural Policy. Enlargement will therefore have to be outside the CAP altogether, involve a separate CAP for the new entrants, or be phased in over a long transition period, the Commissioner stated. His comments followed the release of the EU Commission's reports, which paint a bleak picture of agriculture in 10 central and Eastern European countries. The recent crisis in agriculture in these countries has resulted in a steep fall in production, consumption, and exports. All Central and Eastern European countries, with the exception of Hungary, are net importers of agricultural products from the EU.

In May Hungary's industrial production rose 13.4 percent over that of April and was 15.1 percent higher than in May 1994. Industrial production was 9.7 percent higher in the first five months of this year than at the end of 1994. Hungary's trade deficit stood at \$2.3 billion at the end of June, with exports reaching \$5.3 billion in the first six months and imports \$7.6 billion. Hungary's stalled privatization program appears poised for recovery. Western investors are back, and Hungary's efforts to allay fears that it risked becoming the Mexico of Eastern Europe seem to be paying off, according to the *International Herald Tribune* in a July 22-23 article.

Hungary's recently approved privatization program foresees the sale of Hungarian Electricity (MVM), Hungarian Oil (MOL) regional gas suppliers, and Antenna Hungaria. At the sale of MOL, a share package of 50 percent plus one vote would be offered for potential buyers. But to prevent rival foreign oil producers from gaining majority stakes, only bids by financial investors would be accepted. MOL would remain a national oil company, but with the state's shareholding cut to 25 percent of the shares plus one vote. Most shares of Hungarian Electricity could be privatized. In the first stage 48 percent of MVM's shares would be put up for sale, and potential investors would have an option to obtain further ownership before December 31, 1997. Power stations, which would be fully privatized, including the shares owned by local authorities, would be sold in share packages of 33 to 38 percent equity in the first stage of their privatization. Local authorities would be able to buy up to 25 percent of power station shares and 40 percent of gas supply company shares. The forthcoming energy price increase will be unaffected by privatization. Electricity and gas fees are scheduled to go up by 8 percent in September 1995, by

another 25 in March 1996, and by 18 percent in October 1996.

The rump Yugoslav currency, the so-called "super dinar" is currently trading at 2.3 to 2.5 to the German mark, reported the Belgrade daily *Nasa Borba*. When introduced in January 1994, the new dinar was pegged to the value of the mark at an exchange of 1:1. Central bank governor (and former World Bank official) Dragoslav Avramovic acknowledges that three years of trade sanctions have flattened the economy but says that the situation has stabilized, and rapid recovery is expected once the embargo ends. Avramovic, who masterminded the program and created the super dinar that rescued the country from hyperinflation, says that the budget must be kept balanced to prevent a return of inflation.

Chinese inflation fell to 18.5 percent in the first half of this year, down from 20 percent last year. Economic growth was 10 percent in the first half, showing the signs of a slow-down. But Chinese economists warn that the strong yuan threatens to turn China's 1994 \$5 billion trade surplus into a deficit this year.

China's State Planning Commission Chief Chen Jinhau said that the ninth Five-Year Plan, due to start in 1996, will focus on making industry more efficient and on improving industry's technical capabilities. Privatization of state-owned enterprises is not the first goal. "We need more efficiency, quality, and technical progress. That will be our focus," said Chen.

Beijing's slow revenue collection and rising state wage bill continued to create a budget deficit of 9.1 billion yuan in the first five months of 1995. Ma Jiantang, senior official of the Development and Research Centre, called the deficit alarming. Usually, there are surpluses in the first half of the year.

The **Slovak** parliament eliminated the mass voucher privatization scheme and approved a new privatization law. Under the new plan the 3.5 million Slovak citizens who have already signed up for voucher privatization will each receive government bonds (worth up to 10,000 koruny) with maturities of up to five or six years, backed by sales of property by the state. Prime Minister Vladimir Meciar, stated on Slovak Television that the government would acquire golden shares in strategically important state enterprises such as power, gas, weapons, and chemical facilities.

**Slovakia's** industrial production grew at an annual rate of 7.6 percent in March, a 1.2 percent increase over the rate for 1994, according to the Statistical Office. Unemployment fell to 14.6 percent, down from 15.2 percent in January. Hard currency reserves at the National Bank reached \$2 billion, up from \$1.7 billion at the end of 1994. The Slovak currency strengthened to 29.4 koruny to the dollar in March, an improvement over the rate of 32 koruny in 1994. Annual inflation fell from 11.7 percent in 1994 to 11.3 percent. Slovakia's GDP grew at an annual rate of 4.8 percent in 1994, a substantial gain over the negative 4.1 percent rate of the previous year.

**Uzbek** officials and the director of Japan's Mitsubishi, Sinroku Morohase, held talks on the construction of a natural gas pipeline to run through Turkmenistan, Uzbekistan, China, the Korean Peninsula, and Japan. Construction is expected to begin in 2000. The total estimated cost of the project—which would initially move 18 billion cubic meters of gas per year—is \$9.5 billion. In other developments Uzbekistan lifted all restrictions on the purchase of foreign currency from commercial banks as of July 1.

On July 3 **Ukraine's** Leonid Kuchma appointed a new government. As he explained it, the change represented a shift away from strict monetarism toward deep industry restructuring. But the course of economic reform will stay on track. Kuchma also reduced the number of deputy prime ministers from nine to five.

**Ukrainian** lawmakers approved the main principles of the 1996 budget with the aim of stabilizing the economy and reducing inflation. The package envisages a budget deficit of 6 percent of GDP, lower subsidies, cuts in defense spending, the abolition of preferential tariffs, and the imposition of new license fees for manufacturing alcoholic and tobacco products. They also adopted a new law on education that continues to guarantee free state-secondary education but no longer provides for free universal higher education.

Leonid Kuchma announced that **Ukraine's** new currency, the hryvna, will be introduced perhaps as early as September. The precise date will be determined once Ukraine establishes a \$1.5 billion stabilization fund to back the currency. He also said the fact that the karbovanets has stabilized at around 150,000 karbovantsi to the dollar may allow Ukraine to proceed with monetary reform. The monthly inflation rate dropped to 4.6 percent in May. Since reaching a high of 21.2 percent in January, inflation has fallen steadily throughout this year.

The **European Union** will release a \$130 million grant, plus a further \$520 million from Euratom, to co-fund the closure of the Chernobyl nuclear plant. Western estimates put the cost of decommissioning the damaged plant at \$1.7 billion and of building the new plant at a further \$2 billion. The G-7 countries offered Ukraine \$400 to 500 million in grants and \$1.5 billion in loans for the

project. Ukraine calculates the final cost of the shutdown at \$4 billion. The timetable calls for Unit No. 1 to be shut down in 1997 and Unit No. 3 by the end of 1999. But Ukrainian officials say this deadline can be met only with substantial Western assistance.

**Viet Nam's** economic growth, in recent years averaging about 8 percent annually, will rise to 9 percent this year and 9.5 percent next year, making it Asia's growth leader.

From July 17 the **Bulgarian** National Bank cut its prime interest rate by five points to 39 percent, down from 72 percent at the beginning of 1995. The rate might fall to 27 to 30 percent by the end of the year, National Bank Governor Todor Valchev said. The rate was reduced because inflation is relatively low. In June it was 0.5 percent, the lowest since the beginning of economic reform in 1991. Inflation for the first half of 1995 totaled 15.2 percent, as opposed to 59.4 percent in the first half of 1994. Inflation has dropped along with the sharp drop in the population's buying power and the imposition of restrictive policies. The National Statistical Institute expects inflation to fall to about 40 percent in 1995, down from 121.9 percent the previous year.

In mid-July **Algeria** adopted a privatization law allowing the government to sell off to the private sector state-owned small and medium-size companies in agriculture, commerce, transport, services, and tourism but not in oil, gas, and other strategic industries. Algerian economists say the absence of a stock market and a modern banking system in Algeria will slow any privatization program. Political unrest and a lack of finance has meant that the economy has been working at only 50 percent of capacity. More than 1.5 million (mostly young) Algerians are unemployed (see also page 24).

## World Bank/IMF Agenda

### IMF Management Welcomes Russian Ruble Corridor

"The IMF management welcomes the progress made by the Russian authorities under their current economic program," stated Stanley Fischer, First Deputy Managing Director of the International Monetary Fund (IMF), commenting on the July 5 exchange rate action of the Russian authorities. Effective from 6 July to 1 October, an ex-

change rate corridor has been set against the dollar with a ceiling of 4,300 rubles and a floor of 4,900 rubles. This corridor is backed by \$10 billion in Central Bank reserves. In the past several weeks, the ruble has gained 12.5 percent, rising from an April 29 record low of 5,130 rubles to the dollar. By declaring the ruble corridor, the Central Bank is committing itself to the unlimited purchase and sale of dollars on the foreign exchange market to support the ruble within a set range.

### World Bank Rehab Loan to Russia's Gas Network...

The World Bank has approved a \$106.5 million loan to finance rehabilitation of the gas network in Volgograd and energy conservation measures in nine other locations. The focus of the current World Bank loan is on increasing demand-side improvements rather than on expanding an already abundant gas supply. With three-quarters of the investment directed at cutting consumption, the project should

### World Bank Hikes Lending for Transition Economies

World Bank Group lending commitments to Central and Eastern Europe and the former Soviet Union jumped by 20 percent to \$4.2 billion in the fiscal year ending June 30, 1995. The Bank approved 58 projects, according to the recent Bank report on its overall lending activities.

The Group's loan approvals totaled \$22.5 billion in the past financial year (FY), compared to \$20.8 billion in FY94 and \$23.7 billion in FY93. With loans totaling \$3 billion, China was the biggest borrower, a position it has held for the third consecutive year. It is followed by Mexico, India, Russia, and Argentina.

Three-fourths of the loans, totaling \$16.9 billion, were allocated at market rates among 134 programs of the World Bank; another \$5.7 billion were awarded in IDA credits to support 108 projects. Totals for FY94 were \$14.2 billion for 124 IBRD projects and \$6.6 billion for 104 IDA projects.

### World Bank Group's Lending to European and FSU Transition Countries (FY 1990-95)

(US\$ million)

Country	1990	1991	1992	1993	1994	1995	Cumulative
Albania	-	-	41	44	47	67.4	199.4
Bulgaria	-	17	250	178	148	125	718
Croatia	-	-	-	-	128	120	248
Czechoslovakia	-	450	-	-	-	-	450
Czech Republic	-	-	246	-	80	-	326
Hungary	366	550	200	413	129	38	1696
Poland	781	1440	390	900	146	215	3872
FYR Macedonia	-	-	-	-	80	123	203
Romania	-	180	650	120	401	55.4	1406.4
Slovak Republic	-	-	-	-	135	-	135
Slovenia	-	-	-	-	80	-	80
Yugoslavia	-	300	-	-	-	-	300
Armenia	-	-	-	12	28	116.7	156.7
Azerbaijan	-	-	-	-	-	81.8	81.8
Belarus	-	-	-	-	170	-	170
Estonia	-	-	-	30	50	30	110
Georgia	-	-	-	-	-	103.1	103.1
Kazakhstan	-	-	-	-	274	283.1	557.1
Kyrgyzstan	-	-	-	60	78	77	215
Latvia	-	-	-	45	25	53	123
Lithuania	-	-	-	60	26	32	118
Moldova	-	-	-	26	60	90	176
Russia	-	-	-	1370	1520	1741.3	4631.3
Turkmenistan	-	-	-	-	-	25	25
Ukraine	-	-	-	27	-	646	673
Uzbekistan	-	-	-	-	21	226	247
<b>Total</b>	<b>1839</b>	<b>2937</b>	<b>1777</b>	<b>3285</b>	<b>3626</b>	<b>4181.4</b>	<b>17645.4</b>

Source: World Bank

lead to increased energy efficiency and safety of gas distribution.

### **...But Oil Project in Danger**

Western Siberia's oil producer Varyeganneftegaz may have to delay the second stage of a \$170 million project funded by the World Bank because they have run out of money, said Rustam Tukhvatullin, general director of the company, at a London industry conference. The company was one of three producers to benefit from the Bank's first \$610 million worth of oil rehabilitation loans to Russia, having secured a loan in August 1993 to repair existing oil wells and drill new ones. The company has just over \$60 million left of the original \$170-million loan for the second stage of the project the company claims. It will not be able to use the remainder of the loan unless the Russian government grants it exemption from customs duties on imports (imposed in January) and substantially reduces oil export taxes.

### **Railway Loan to Bulgaria on Track**

On July 7 the World Bank approved a \$95-million loan to Bulgaria to help the country restructure its railway system. The loan will cover track renewal, procurement of computers, training, and the installation of modern signaling and telecommunications equipment. The Bulgarian parliament recently passed a new railway law governing the relationship between the state and the railways. The total cost of the project is estimated at \$296 million, with the Bulgarian State Railroads, the EU's PHARE program, and the EBRD providing the balance. A World Bank mission in preparation for a finance and economy structural adjustment loan recently discussed with Bulgaria its progress in privatization, reform of the banking system, financial stability, and the financial discipline of state-run enterprises.

### **Qualified Praise for Poland**

"Poland does not need balance of payments loans from the World Bank. At this stage of economic development, loans should be tailored to meet concrete sectoral needs," said World Bank Director Kemal Dervis during a visit to Warsaw, where a Bank delegation was reviewing the country's economic situation and absorption of Bank loans. To date, Poland has used only \$1.8 billion of the \$3.9 billion of World Bank funds made available to it. Polish Finance Minister Grzegorz Kolodko also said that Poland had used those loans best designed for "microeconomic rather than for general purposes." Dervis praised Poland's booming economy but suggested that the government encourage further modernization and privatization in the agricultural sector, reform small and ailing cooperative banks, and make sure that the forthcoming reform of the social security system did not lend to higher inflation.

Poland's finance ministry and the World Bank are now discussing a \$150 to \$200 million loan to help the government restructure the ailing mining sector.

In other developments, Poland has repaid \$1 billion of an IMF stand-by credit early (received last year to help finance a rescheduling of London Club debt). Polish Central Bank deputy president Witold Kozinski said. On July 21 Poland notified the IMF that it accepted Article VIII obligations, making the zloty convertible for current international transactions.

### **Romania Talks with World Bank**

Talks in Washington between the World Bank and a Romanian delegation headed by Finance Minister Florin Georgescu and National Bank Governor Mugur Isarescu have produced no immediate

results. The Bank's press release, of July 11, 1995 refers to a "number of steps" needed before negotiations on a proposed financial and enterprise sector adjustment loan could start, relating primarily to the government's privatization program and the restructuring of state enterprises. (According to reports from Bucharest, Romania's main privatization agency has sold 1,000 state companies in two years and plans to privatize 1,500 more in 1995. The value of the privatization vouchers each citizen aged 18 and over will receive has been set at about 1 million lei (\$485). The vouchers may not be sold but may be traded for stocks.

### **World Bank to Finance Ukrainian Gas Plan**

Ukraine will suggest the World Bank lend \$500 million to improve the country's gas transit infrastructure, Deputy Minister of Finance Boris Sobolev said at a recent London conference on investment opportunities in Ukraine. The Ukrainian government said the \$2.1 billion it had received in IMF support had helped lower inflation from 5.8 percent in April to 4.6 percent last month. But, President Leonid Kuchma warned, Ukraine could not reduce monthly inflation to 1 to 2 percent by the end of 1995. He called for new talks with the IMF.

### **IMF Support For Armenia...**

On June 28 the IMF approved a \$69-million, 12-month stand-by credit to Armenia, together with a second drawing of about \$27 million under the systemic transformation facility. The money is supporting the 1995-96 economic program to reduce inflation to 1 percent a month by the end of 1995 and to even lower rates next year. Inflation-adjusted growth in Armenia is projected at 5 percent for 1995 and 8 percent next year.



### ....and Georgia

On June 28 the IMF approved a \$113 million, 12-month stand-by credit to Georgia together with a second drawing of about \$44 million under the systemic transformation facility to achieve 10 percent growth in 1996 (after an expected decline of 5 percent this year). Earlier, on June 23, the Georgian parliament passed a law that establishes the legal framework for an independent central bank. Georgian leader Eduard Shevardnadze said in a national radio address that the government plans to use the IMF support to introduce a new currency, to be called the lari.

### Lending China \$3 Billion Annually

The World Bank expects to provide about \$3 billion in loans to China in each of the next three years to support activities in infrastructure, poverty reduction, environmental protection, and education said Pieter Bottelier, chief of the Bank's Beijing office. About five or six loan projects are expected to be approved by the Bank in the second half of this year.

### World Bank Supports China's Anti-Poverty Plan ...

The World Bank on June 15 approved a \$247.5 million project to support China's anti-poverty program in 35 mountainous and remote counties of the South West region. The \$200 million IDA credit and \$47.5 million World Bank loan will support a program to create job opportunities and build up the local infrastructure for more than 2.5 million people.

### Revitalizing Inland Waterways...

China is modernizing its enormous system of inland waterways through a \$577 million construction program intended to take sea-going vessels deep into land-locked areas. The World Bank has put up \$210 million toward the project.

### ...and Fighting Against Iodine Deficiency

About 400 million Chinese are endangered by iodine deficiency, which can cause goiter, enlarged thyroid glands, dwarfism, intellectual impairment, stillbirths, and other diseases. On June 28 a World Bank loan of \$7 million and IDA credit of \$20 million were approved to support salt iodization, packaging facilities, and technical assistance. The loan will cover nearly 18 percent of the \$152 million needed for China to achieve the universal iodization of salt by the end of 1996, which could eliminate iodine deficiency disorders by 2000.

### China Ready for Oil and Gas Regulation

Within a year China is expected to complete drafting a petroleum law aimed at attracting foreign investors to its huge oil industry, World Bank official Hossein Razavi said at an energy privatization conference in London. "The petroleum law basically would give a clear framework to private investors, so that when they come to the country, they will know what the terms of the relationship are." The World Bank was working with China on a study regarding the restructuring of the state-owned China National Petroleum Corporation (CNPC). This study laid the groundwork for the development of the gas sector and for a regulatory system.

### Lending to Viet Nam in 1995

The World Bank will lend about \$400-450 million to Viet Nam largely for rural development projects, announced Russell Cheetham, Vice President for East Asia and the Pacific, at the Hanoi signing of two new IDA credits. Of these, \$165 million will go to upgrade the electricity network and another \$100 million to restore the irrigation systems "The economy in Viet Nam is doing

well. With GDP growth at 9 percent, the budget deficit is under control and declining," said Cheetham. These two agreements bring World Bank commitments to Viet Nam to \$740 million since lending resumed in November 1993.

### IFC Invests in Viet Nam's Private Port

The International Finance Corporation will invest in Vietnam's first private sector port project. Under the agreement, signed on June 22, the Baria Serece Joint Venture Company (BSJVC)—owned jointly by Vietnamese and foreign investors—will build a deep-water port capable of handling ships of up to 40,000 tons on the Thi Vai River 70 kilometers from Ho Chi Minh City. The port will have bulk handling facilities and an annual capacity of 600,000 tons. The total project cost is estimated at \$10 million. IFC will provide \$3 million and is expected to syndicate an additional \$2 million with Banque Indosuez. The Norwegian Agency for Development (NORAD) will also provide a \$2 million loan.

### OECD: Foreign Aid Shrinks

The Organization for Economic Cooperation and Development (OECD) says rich countries last year reduced real development aid as a proportion of their total income to the lowest level since the oil shock of 1974. According to a report of the OECD's Development Assistance Committee (DAC), total flows of official aid to poor countries directly, or through multilateral organizations, like the World Bank, rose in 1994 by 2.4 percent to \$58.8 billion. But adjustments for inflation and currency movements left real 1994 aid lower by a 1.8 percent. The overall ratio of aid to gross national product in donor countries reached a 21-year low of 0.29 percent. The top donor countries were: Japan (\$13.2 billion, up 8 percent over the previous year);

the United States (\$9.9 billion, which represents just 0.15 percent of its gross national product, the lowest ratio of the DAC's 21-member countries); France (\$8.5 billion); and Germany (\$6.8 billion). While France's contribution rose 3 percent, Germany's share fell by 7 percent.

### **IFC Boosts Infrastructure Loans**

In line with recent widespread moves to transfer the role of improving infrastructure to the private sector, International Finance Corporation infrastructure loans have tripled over the past five years. IFC is shifting its sphere of activities to emerging markets such as Asia, the former Soviet Union, and Eastern Europe. The destinations of loans are also changing as the private sector in different countries acquires fund-raising capabilities. In East Asia, the main recipients of IFC loans are India, Viet Nam, and China rather than the Republic of Korea, Malaysia, and Thailand, which were once the principal destinations.

### **Social Investment Fund in Nicaragua**

Nicaragua's economic reforms are bringing down inflation and beginning to spur growth. On July 11, to help sustain poverty alleviation and social protection programs during the reform period, IDA approved a \$30-million credit to help finance a second social investment fund project. In other news, Nicaragua plans to buy back up to \$1.7 billion of its debt with commercial banks, Nicaraguan Foreign Minister Ernesto Leal said in Washington. Leal told a news conference that he will sign an agreement with the World Bank, which will act as an agent in the buy-back operation. Nicaraguan Ambassador Roberto Mayorga said that funds for the buy-back will come from concessional loans from the World Bank.

### **Kyrgyzstan: IFC Invests in Gold Mining...**

The IFC said it will invest \$40 million in the first private sector gold mining venture in Kyrgyzstan, a \$360 million project being developed by Kumtor Gold Company. This will be the IFC's first investment in the Kyrgyz Republic since it became a member of the institution in 1993. The IFC will lend Kumtor \$30 million of its own funds and take a \$10 million quasi-equity stake. The IFC said the Kumtor gold deposit was the largest in the world, with geological reserves of about 16.6 million ounces of contained gold. Of these reserves, 9.3 million ounces were minable by open pit methods.

### **...and IDA Doles out Money for Agro-Privatization**

On June 28, IDA approved a \$45-million, agricultural privatization and enterprise adjustment credit for Kyrgyzstan to foster the development of land markets, the privatization of large conglomerates, and the elimination of price and trade distortions.

### **Eliminating Soviet Nuclear Reactors**

Wealthy industrialized nations should take a new approach toward solving the critical problem posed by the 19 potentially dangerous, Soviet-designed nuclear reactors still in operation, declared Robert Ebel, director of energy and national security at the Washington-based Center for Strategic and International Studies. In a recent op-ed to the *Financial Times*, he suggests using Russia's extensive stockpile of refined uranium either to raise money or to guarantee loans from such international financial institutions as the World Bank and IMF.

### **Capital Shots to Algeria's Ailing Economy**

Creditor nations meeting in Paris agreed to reschedule \$7.5 billion of Algeria's debts (total public debt stands at \$29.4 billion) for 15 years, due between June 1995 and May 1998—the span of Algeria's latest economic reform support package from the IMF. Interest payments were not rescheduled, except for what is due in the first year. Payments will now not begin until November 1999, and the last cash is due in 2011. The IMF earlier lent Algiers a \$1.8 billion stand-by loan over three years to support free-market reforms. Beset by bloody opposition from Moslem fundamentalists, a slump in prices for its main export, natural gas, and facing a hump in debt payments to Western creditors, the army-backed government finally turned to the outside for help in early 1994. A one-year, \$1 billion package was awarded by the IMF last year, followed by a \$5 billion rescheduling of 1994-95 debts by the Paris Club (similarly for 15 years). After long negotiations, commercial bank creditors in May agreed to delay payments on \$3.2 billion of debts due from 1994 to 1997.

### **Roads and More Roads—That's What Albania Needs**

Albania reported that 421 people died in 559 traffic accidents last year, but Western observers put the true figure 10 times higher, reports the *Guardian*. The number of vehicles in Albania has soared from 5,000 in 1992 to 160,000 today. But progress to improve and build roads has been painfully slow. Albania is one of Europe's smallest countries, yet Albanians joke it is the biggest because it takes so long to get around. The World Bank has already approved about \$79.5 million for road-building as necessary to

trade and tourism. The Albanian roads system remains the poorest in Europe.

### Short and Sweet

The World Bank's International Finance Corporation), with an equity investment of up to \$5 million, will establish a capital fund and a capital development company in the **Russian Far East** to supply a broad range of investment banking services—including corporate finance and restructuring and privatization advice—mainly for the region's transport sector.

On July 19 the Paris Club agreed to reschedule over 15 years the \$300 million official debt of the **former Yugoslav Republic of Macedonia**, Finance Minister Jane Miljovski announced.

**Mongolia's** national poverty alleviation program, with help from a \$10 million IDA credit approved July 6, aims to create employment opportunities for the poor, raise enrollment in basic education, reduce maternal and other mortality, and provide assistance to handicapped and mentally retarded children.

**Moldova** adopted the Article VIII of the IMF, making the Moldovan leu convertible for current transactions at a rate of 4.6 lei to the dollar. The Moldovan currency is the 103rd world currency to acquire limited convertibility.

On June 28 IDA approved a \$61 million credit to eliminate the acute water shortage and upgrade the water supply system in **Azerbaijan's** capital city, Baku. An IDA \$18-million credit, approved July 25, will support government efforts to privatize state-owned industry, strengthen the finance ministry and central bank, and create the legal and regulatory framework to develop a market economy.

## Conference Diary

### For the Record

#### **International Energy Workshop** June 20-22, 1995, Laxenburg, Austria

The topic of this conference was global energy projections and policy issues in greenhouse gas (GHG) mitigation, which were discussed by over 100 international energy experts. It was held at the Laxenburg Conference Center of the International Institute for Applied Systems Analysis (IIASA) in Laxenburg, Austria. The conference attracted energy analysts from all over the world, who met to compare worldwide projections on developments in the energy sector (in such areas as crude oil prices, economic growth, primary energy consumption and production, and energy trade). The program covered global energy projections, nonfossil primary energy sources, energy developments in Eastern Europe and countries of the former Soviet Union, and policy issues in GHG mitigation and the regional distribution of costs and benefits.

*Information: Ms. Elisabeth Krippel, Office of Public Information, IIASA, A-2361 Laxenburg, Austria, tel. (43) 2236-73149, Email: krippel@iiasa.ac.at.*

### Forthcoming

#### **Exchange Rates, Capital Flows, and Monetary Policy in a Changing World Economy** September 14-15, 1995, Texas, USA

Conference will be held at the Federal Reserve Bank of Dallas with discussions on exchange rates and mon-

etary policy, optimal exchange rate policy for stabilizing inflation in developing countries, exchange rates and economic growth, integrated financial markets and foreign exchange regimes, international capital flows, and central bank coordination in the midst of exchange rate instability. *Information: Agnes Mitchell, Public Affairs Department, 10th Floor, Federal Reserve Bank of Dallas, 2200 N. Pearl Street, Dallas, Texas 75201, USA, tel. (800) 333-4460.*

#### **Banking and Finance in the Baltics, 1995**

September 27-29, 1995, Riga, Latvia

This conference will discuss the present financial situation in the Baltics, prospects for development, and the way relations could be developed between the financial sectors of the Baltics, the CIS, and Western countries. Topics will include investment in the Baltics, capital markets, banking and the financial situation in the Baltics, development perspectives and monetary policy, information technology, payment cards, nonbanking finance sector, cooperation between Baltic and Western banks and international funds, and banking education and staff development. *Information: Latvian Business School (LBS) Exhibitions and Conferences, 1 M. Pils St., Riga, Lv1050, Latvia.*

#### **World Bank-IMF Annual Meetings**

October 10-12, 1995, Washington, D.C., USA

**Energy and Telecoms in Transition Countries**

October 21-23, 1995, Bratislava, Slovakia

Organized by the Center for Economic Development and ACE Phare and coordinated by Oxford University. *Information: Andrej Juris and Eugen Jurzyca, Center for Economic Development, fax: (427) 201-5487.*

**Telecommunications in Central and Eastern Europe**

October 25-26, 1995, Warsaw, Poland

Sponsored by the Adam Smith Institute, topics related to telecommunications include: current and future trends, legal and regulatory aspects, financial issues, privatization of local telecommunications networks and equipment facilities, competition or cooperation between the main local and the regional operators, technical solutions, and a country-by-country focus.

*Information: Cristina Pesici-Watts or Jenny Pitts, Adam Smith Institute, 11-13 Charterhouse Buildings, London EC1M 7AN, England. tel. (0171) 490-3774, fax (0171) 490-8932.*

**Bankruptcy Regulation in Slovakia**

October 26-27, 1995, Bratislava, Slovakia  
*Information: Andrej Juris and Eugen Jurzyca, Center for Economic Development, fax (427) 201-5487.*

**Doing Business in China and Hong Kong**

October 26-27, 1995, San Francisco, USA

Sponsored by the Institute for International Law and Business, the conference will focus on the following

topics: China's entry into U.S. securities markets; privatization opportunities and problems, regulation of real estate projects, recent joint ventures in China, developments in China's financial laws, negotiating business contracts, expanded protection for U.S. intellectual property rights through laws and international agreements, structuring agreements with China, tax planning, and recent developments in the Chinese economy.

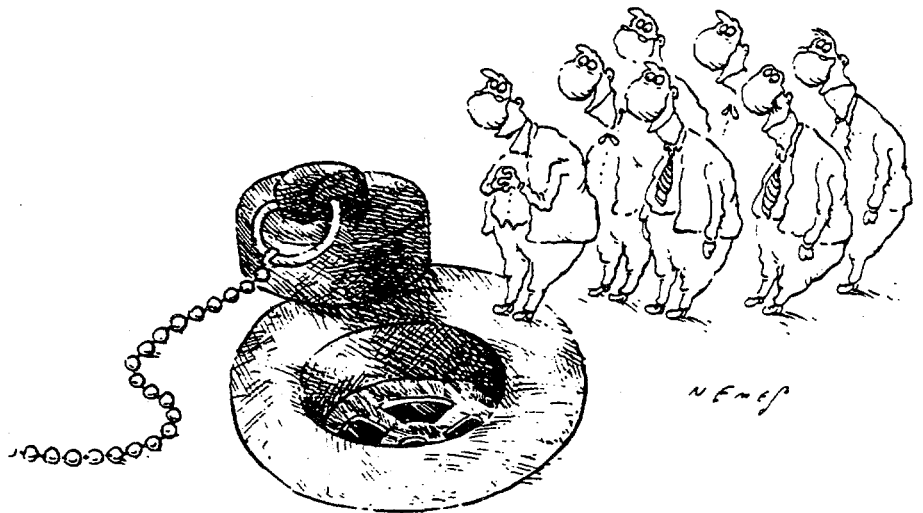
*Information: American Conference Institute, 175-Fifth Avenue, Suite 2182, New York, New York 10010, tel. (416) 927-7936, fax (416) 927-1563.*

**International Business Transactions**

October 30-31, 1995, Chicago, USA

Sponsored by the Institute for International Law and Business, topics will include: rules affecting the transfer of goods, services, people and money; the Foreign Corrupt Practices Act; choosing the appropriate structure for the business relationship; international intellectual property and technology transfer issues; financing international projects.

*Information: American Conference Institute, 175-Fifth Avenue, Suite 2182, New York, New York 10010, tel. (416) 927-7936, fax (416) 927-1563.*



"Good news gentlemen, I see the light at the end of the tunnel."

From the Hungarian magazine *Hocipo*

## New Books and Working Papers

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### World Bank Publications

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Ira W. Lieberman, Andrew Ewing, Michal Mejstrik, Joyita Mukherjee, and Suhail Rahuja, **Mass Privatization in Central and Eastern Europe and the Former Soviet Union: A Comparative Analysis**, Studies of Economies in Transformation no. 16, 1995, 104 p.

Authors examine approaches to mass privatization adopted in the Czech and Slovak Republics, Poland, Lithuania, and Russia. Each stage of the process—from the initial distribution of vouchers to the post-privatization implications for capital market development and restructuring—is described in detail. A number of theoretical issues relating to portfolio analysis, corporatization, and investment funds are discussed to emphasize the importance of state involvement in mass privatization programs.

Philippe H. Le Houverou, **Investment Policy in Russia**, Studies of Economies in Transformation no. 17, 1995, 88 p.

The role of government in investment financing is the center of public debate on economic policy in the former Soviet Union. The author examines five key

aspects of economic policy and investment: price distortions; uncertainty; inflation; the legal, regulatory, and security framework; and the tax regime. The study also outlines the principles and major building blocks of a new market-based investment policy in the FSU, the scope of government-financed investment, and the management and instruments of that investment.

Jonathan Klavens and Anthony Zamparutti, **Foreign Direct Investment and Environment in Central and Eastern Europe: A Survey**, 1995, 70 p.

Analyzes the results of a 1992 survey that asked 1,000 multinational corporations about the importance of environmental issues to investment decisions. Most large corporations looked thoroughly at environmental issues when it came to making decisions about where to invest. Environmental problems have discouraged a number of investors across different industries, mainly because of concern about liability for past pollution at industrial sites.

### Institute for East-West Studies

Kálmán Mizsei and Andrzej Rudka, **From Association to Accession: The Impact of the Association Agreements on Central Europe's Trade and Integration with the European Union**, Institute for East-West Studies, 1995, 181 p.

To order: Institute for EastWest Studies, (New Address!) 700 Broadway, 2nd Floor, New York, New York 10003, USA, tel. (212) 824-4100, fax (212) 824-4149.

### Institute of Economic Studies

Pavel Jirkovsky, and Jiri Gelny, **Does the Czech Republic Need a Legislative Act Limiting the Composition of Washing and Cleaning Materials?** Institute of Economic Studies, Universitas Carolina Pragensis, Prague, May 1995, 24 p.

Radomir Sabela, Terézia Hrnčirová, and Josef Vais, **Process of Privatization in The Field of Industry and Trade in the Czech Republic**, Institute of Economic Studies, Universitas Carolina Pragensis, Prague, June 1995.

To order: Institute of Economic Studies, Universitas Carolina Pragensis, Smetanovo nábr. 6, CZ-110 01 Prague 1, Czech Republic, tel. (422) 2481-0804, fax (422) 2481-0987.

### OECD Publications

**Agricultural Policies, Markets and Trade in Central and Eastern European Countries (CEECs), Selected New Independent States (NIS), Mongolia and China: Monitoring and Outlook 1995**, OECD, May 1995.

Some Central and Eastern European countries are looking forward to eventual succession to the European Union. But there are large differences in the agricultural support systems and levels of assistance between individual transition economies and the European Union. For example, the EU's Producer Subsidy Equivalent (measuring the value of monetary transfers to agricultural production from consumers and taxpayers) for 1993 was 49 percent, whereas it was 16 percent in Poland. In Russia, Ukraine, Kazakhstan, and Belarus many former collectives and state farms reor-

ganized into joint-stock farms without changing their internal structures or operating procedures.

*To order: OECD Press Division, 2 rue André Pascal, 75775 Paris cedex 16, France, tel. (331) 4524-8088, fax (331) 4524-8003.*

### International Labor Office

**Viet Nam: Labor and Social Issues in a Transition Economy**, International Labor Office, East Asia Multidisciplinary Advisory Team (EASMAT) Bangkok, 1994, 44 p.  
[Foreword from Director Assefa Bequele]

As Viet Nam's public sector retrenched, adjusting to market realities in 1988-91, it cut 820,000 employees of state enterprises and 320,000 civil servants. A further 20 percent was cut in 1992. Open unemployment (about 6 percent) has now emerged, further complicated by the return of 250,000 migrants from Eastern Europe and the demobilization of over 500,000 soldiers. Living standards have declined, and by 1993 the purchasing power of civil servants and workers in state enterprises had fallen by a third from levels of 1985. Availability of health and education services also deteriorated.

Suggested policies for the longer term stress the need for 10 percent real annual GDP growth to stabilize unemployment at the present level (the labor force is growing 3 percent per year), labor-intensive public works programs, and increased support for agriculture. For the short term proposals include the promotion of small enterprises, training programs to enhance workers' skills, and a national network of labor exchanges.

*To order: International Labor Organization, Regional Office for Asia and the Pacific, G.P.O. Box 1759,*

*Bangkok 10501, Thailand, tel. (662) 282-9161, fax (662) 267-8043.*

Lin Lean Lim and Gyorgy Sziraczki (editors), **Employment Challenges and Policy Responses: Chinese and International Perspectives**, International Labor Office, Beijing, 1995, 127 p.

China's gradual move toward a more open, market-oriented economy has been accompanied by severe employment problems. These include continuous labor supply pressure, large-scale rural underemployment, rising urban unemployment, massive and uncontrolled labor mobility from rural to urban areas, huge labor surpluses and low efficiency in state-owned enterprises, and growing income differentials between different segments of the population. Some of these problems originate from the rapid growth of the working-age population. Others are the negative side effects of the economic, employment, and enterprise reforms implemented since the early 1980s.

To address its employment problems, the Chinese government has introduced various labor market regulations, institutions, and policies designed to enrich and regulate the labor supply, enhance labor demand, and improve the labor-market process. This volume is based on the papers presented at the National Seminar on Employment Promotion via Active Labor Market Policies in China, held in Hangzhou November 7-11, 1994. The seminar was jointly organized by the Ministry of Labor, the Labor Market Policies Branch of the ILO, and the ILO Area Office in Beijing.

Richard Jackman, **Economic Policy and Employment in the Transition Economies of Central and Eastern Europe: What Have we Learned?** International Labour Review, Geneva, Switzerland, vol. 133, no. 3, 1994.

Martin Godfrey, **The Struggle Against Unemployment: Medium-Term Policy Options for Transitional Economies**, International Labour Review, ILO, Geneva, Switzerland, vol. 134, no. 1, 1995.

*To order: International Labor Review, ILO, Geneva, Martha Loutfi, Chief Editor, fax. (4122) 799-6260. e-mail: loutfi@hq1.ilo.ch.*

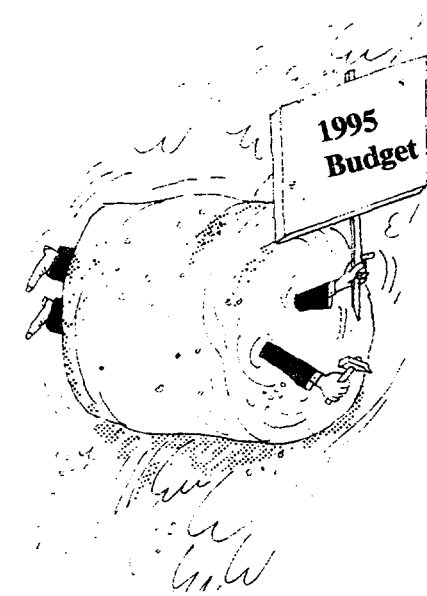
### WIIW Publications, Vienna

Maciej Krzak, **The Experience of East European Countries with Different Exchange-Rate Regimes**, WIIW no. 217, April 1995, 19 p.

Gábor Oblath, **Economic Growth and Fiscal Crisis in Central and Eastern Europe**, WIIW no. 218, May 1995, 37 p.

How is it that the Czech economy does not face serious fiscal problems but both the Bulgarian and Hungarian economies do? The Czech fiscal policy tended to be more "conservative" than policies

### Snowball Effect



From the Hungarian magazine **Uritok**

pursued in the other two countries during transition. The Czech Republic did not inherit huge foreign debts. Its budget was balanced, and the interest payment on its public debt is therefore negligible. But in Hungary and Bulgaria, these payments reached high proportions. In the Czech Republic profit tax revenues are still significant, while in the other two countries, tax revenues have fallen dramatically (Bulgaria) or became negligible (Hungary). The Czech Republic tried to avoid mass bankruptcies and high increases in unemployment. So that, relative to GDP, its citizens' social security contributions (revenues) are higher and their social expenditures lower than in the two other transition economies.

In Hungary and Poland the primary budget balance (which ignores interest payments), related to overall economic performance, has improved significantly. In Hungary the overall budget deficit increased from 5.0 to 5.5 percent of GDP between 1993 and 1994, due to the higher interest, but the primary balance turned from a deficit of 0.5 percent of GDP to a surplus of 1 percent of GDP. Similar trends have been observed in Poland.

Attempts to cut budgetary imbalances with drastic fiscal policies can be counterproductive. Oversimplified and orthodox explanations are not likely to work in the transition period, and economic improvement has little to do with conventional recommendations, presenting major challenges for the economist profession.

*To order: Vienna Institute for Comparative Economic Studies, P.O. Box 87, A-1103 Vienna, tel. (431) 782-567, fax (431) 787-120.*

#### Other Publications

**Business in the Russian Free Market**, the Mir House, Inc., Kansas City,

USA, 1995, 227 p.

*To order: The Mir House, 8919 Parallel Parkway, Suite 560, Kansas City, Kansas 66112-1655, USA, tel. (800) 3-Russia or (913) 299-2143, (Email: 6520928@mcimail.com).*

William D. Coplin and Michael K. O'Leary (editors), **East Europe and the Republics: A Political Risk Annual**, Political Risk Services, June 1993, 305 p. *To order: Political Risk Services, 6320 Fly Road, Suite 102, P.O. Box 248, East Syracuse, New York, 13057-0248, tel. (315) 431-0511, fax (315) 431-0200.*

Stephany Griffith-Jones and Zdenek Drábek (editors), **Financial Reform in Central and Eastern Europe**, Institute of Development Studies, Sussex, November 1994, 288 p.

Examines banking reforms in Eastern Europe with emphasis on the bad domestic debt situation. Case studies of the Czech, Hungarian, and Polish capital markets are complemented with relevant experiences of developing countries.

*To order: Jackie Pary, Macmillan, Houndmills, Basingstoke, Hants RG7 2JX, United Kingdom, tel. (44-256) 29242, fax (44-256) 28339.*

Marvin Jackson, Jenő Koltay, and Wouter Biesbrouck (editors), **Unemployment and Evolving Labor Markets in Central and Eastern Europe**, LICOS Studies on the Transitions in CEE, 4, Avebury, (U.K.\U.S.\Hong Kong\Singapore), 1995, 227 p.

This fourth volume in a series produced by the Leuven Institute for Central and East European Studies discusses structural changes in the labor markets of Hungary, Czech Republic, Slovakia, Slovenia, Poland, and Romania. (The three preceding volumes covered agri-

culture and food, company management and capital markets, and competition and marketization.) The book contains "Unemployment and employment policy in Central and Eastern Europe: Similarities and Differences," by Jenő Koltay; "Romania: The Challenge of Unemployment," by Mihaela Miron; "Recent Labor Market Developments in Former Czechoslovakia," by Alena Nesporova; "Unemployment in Transition Economies: The Case of Slovenia," by Sonja Drobnic and Veljko Rus; "Unemployment in Poland in the Period of Transition," by Janusz Witkowski; and "Unemployment and the Prospects for Employment Policy in Hungary," by János Kollo.

*To order: Avebury, Gower House, Croft Road, Aldershot, Hampshire Bull 3HR, England, or Ashgate Publishing Co., Old Post Road, Brookfield, VT 05036-9704, tel. (802) 276-3162, fax: (802) 276-3837.*

Josef Langer and Wolfgang Poellauer (editors), **Small States in the Emerging New Europe**, Eisenstadt, Verlag für Soziologie, 1995, 424 p. *To order: Josef Langer, Institut fuer Soziologie, Universitaet Klagenfurt, A-9020 Klagenfurt, Universitaetsstrasse 67, Austria, or write to the publisher: Verlag fuer Soziologie, Haydnegasse 12, A-7000, Eisenstadt, Austria, (Email: josef.langer@uni-klu.ac.at).*

Françoise Lemoine, **CEE Exports to the EC (1988-1993): Country Differentiation and Commodity Diversification**, CEPII no. 94-15, December 1994, 71 p. *To order: CEPII, Centre D'Etudes Prospectives et D'Informations Internationales, 9 rue Georges Pitard, 75740 Paris Cedex 15, France, tel. (331) 4842-6464, fax (331) 5368-5501.*

**Poland—International Economic Report: 1994-95**, World Economy Research Institute, Poland, 1995, 234 p.



After an overview of the Polish transformation process, the report analyses the stabilization and system reform measures taken in 1994 and summarizes the outlook for 1995. The final section focuses on selected issues, such as the zloty's convertibility, Poland's membership in the EU, and the income and spending of young Polish consumers. *To order: World Economy Research Institute, Warsaw School of Economics, Rakowiecka 24, 02-554, Warszawa, Poland, tel. (4822) 489-132, (4822) 491-251, ext. 370, 371, fax (4822) 489-132, (4822) 495-312.*

Chenggang Xu, **A Different Transition Path: Ownership, Performance, and Influence of Chinese Rural Industrial Enterprises**, Garland Publishing, Inc., New York, 1995, 172 p.

*To order: Garland Publishing, Inc., 717 Fifth Avenue, Suite 2500, New York, New York 10022 USA, tel. (212) 751-7447, fax (212) 308-9399.*

Irene Norlund, Carolyn L. Gates, and Vu Cao Dam, **Viet Nam in a Changing World**, Nordic Institute of Asian Studies, Curzon Press, 1995, 293 p.

#### Newsletters, Special Issues

**MOCT-MOST Economic Policy in Transitional Economies, Special Issue, The Role of the International Organizations in the Transition: Economic Challenges, Financial Support and Targets, Editor: Roberta Benini**, Volume 5, No.2, 1995. Kluwer Academic Publishers, 1995, 262 p.

Excerpts the chapter, "The World Bank in Eastern Europe and the FSU," by Kemal Dervis, Marcelo Selowsky, and Christine Wallich: The World Bank's key challenge in dealing with transition economies has been to calibrate the

volume and composition of assistance needed so that it complements domestic reform and is socially and economically less costly and more sustainable. Financial assistance that is premature may delay reform and lead to capital flight, adding to debt rather than to economic growth and public welfare. When a country's need is exceptionally large, it may threaten the portfolio of the Bank and increase the cost of borrowing for other members.

Restructuring and growth in transition countries will depend on addressing demand-side constraints—such as lack of macroeconomic stability, insufficient liberalization, and a weak legal framework—that impair the business environment, the desire to invest, and supply-side constraints on the availability of resources—such as a lack of credit to enterprises and key public infrastructure needed to complement the growth of the private sector.

If the unstable economic environment impairs the process of restructuring, investment, and private sector growth, credit lines could remain undisbursed, balance of payments financing could result in capital flight, and investments end up in underused infrastructure. The Bank has to recognize that legal and institutional development, crucial for economic reform, will take time to yield results and cannot be accelerated with large amounts of financial support. Technical assistance faces absorptive-capacity limits.

*To order: Roberta Benini, Editor MOCT-MOST Nomisma, Economic Research Institute, Strada Maggiore, 44, 40125 Bologna, Italy, tel. (3951) 6483-340, fax (3951) 223-441.*

**International Agriculture and Trade Reports: Former USSR**, Situation and Outlook Series no. WRS-95-1, U.S. Department of Agriculture, Washington, D.C., May 1995, 40 p.

Over the past three years food production, consumption, and import demand has changed significantly in the FSU countries. Livestock has fallen and as a consequence, grain demand has dropped. Extra-FSU grain imports fell from a yearly average of 20-30 million tons in the 1980's, to about 3 million tons in 1994-95. Russian food imports have shifted over the past three years from bulk commodities to processed food products. Russia is now the number one importer of U.S. poultry parts and one of the world's largest markets for U.S. snack foods. But as Russian producers have lost markets to imported foods, some have improved quality and packaging to compete with imports.

With the tightening of fiscal and monetary policies, government handouts declined steeply. In 1995 the agricultural sector should receive 13.3 trillion rubles (\$2.7 billion) in direct federal budget subsidies (most aimed at inputs for livestock producers), or about 2 percent of projected GDP. This is a drop from 1992 and 1993, when agricultural subsidies accounted for about 19 and 5 percent of GDP respectively. Producers still receive centralized (subsidized) credits and subsidies from off-budget accounts.

Ukraine's tight fiscal and monetary policies could eventually eliminate federal procurement of agricultural commodities and sharply curtail subsidies and soft credits to agriculture. But while liberalized foreign trade will expose Ukrainian food producers to foreign competition, Ukraine could become a net exporter of grain before the end of this century.

*To order report series (also includes reports on China and Europe): Economic and Research Service, NASS, 341, Victory Drive, Herndon, Virginia 22070, tel. (800) 999-6779/(703) 834-0125 or fax (703) 834-0110.*

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**Focus: The Russian Far East and the Environment.** *Russian Far East Update* (U.S.) 5(6):7-10, June 1995.

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