Journal for Institutional Innovation, Development and Transition Vol. 4, 2000 UDC: 338.97(914.7)

Ten Years of Postsocialist Transition: Lessons for Policy Reform

Grzegorz W. Kolodko*

Summary

In 1989, influential financial organizations, political bodies, and professional economists seemed to agree upon the main points for economic policy reform. This was termed the Washington consensus. Despite the fact that the economic policy of the Washington consensus was initially developed without any concern for post-socialist transformation, as it has turned out these ideas have significantly influenced the path of thought and action in Eastern Europe and the former Soviet Union. Because these policies were not intended for the overhaul of post-socialist countries they have largely fatted.

Transition to a market economy is a lengthy process, comprising various spheres of economic activities. The naive belief that a market economy can be introduced by "shock therapy" is wrong, and in several cases, when attempted, has caused more problems than it has solved. Because a market economy requires adequate institutional structures and appropriate behavior, transition can be executed only in a gradual manner, since these are very gradual processes based upon new organizations, new laws, and the changing behavior of various economic entities.

1. Introduction

The centrally planned economy has ceased to exist. Even in countries still considered socialist (communist), such as China and Vietnam, the mechanism of economic coordination has largely shifted from state intervention to market allocation. Thus, during the 1990s, the process of postsocialist transformation has advanced significantly. About 30 countries in Eastern Europe, the former Soviet Union and Asia are involved in vast systemic changes. Undoubtedly, these changes are leading to fully-fledged market economies, even though the precise outcome of the transformation is not going to be the same for all countries involved. Those who are leaders in transition, and are well-placed geopolitically, are bound to join the European Union in the foreseeable future, whereas others, lagging behind in systemic changes, will remain hybrid systems with the remnants of central planning alongside elements of market regulation and a growing private sector. Some countries will expand quickly and catch up with their developed neighbors within a generation, while others will experience sluggish economic growth and a relatively low standard of living.

* Professor at the Warsaw School of Economics and Visiting Scholar at the International Monetary Fund. The author, a key architect of Polish economic reforms, was Poland's First Deputy Premier and Minister of Finance, from 1994 to 1997. His new book, "From Shock to Therapy. The Political Economy of Postsocialist Transformation" was published in 2000 by the Oxford University Press. This paper is based upon his own economic policy experience and comparative studies, on research undertaken when he was Senior Visiting Scholar at the Economic Policy Department of the World Bank in 1998 and at Yale Univeristy, and on an invited lecture delivered to the conference on "Institutions in Transition" in Maribor, Slovenia, October 6-7,1999. The views presented in this paper are exclusively those of the author and do not reflect the opinion of the IMF, the World Bank, or any other organization or person the author may be associated with.

The main argument in favor of transition was a desire to put the countries in question on the path of sustainable growth. It was assumed that the shift of property rights from the state to private hands, and the shift of the allocation mechanism from state to free market, would soon enhance saving rates and capital formation, as well as allocative efficiency, thus contributing to high-quality growth. Unfortunately, for a number of reasons, this has not occurred. In all transition economies, before any growth has occurred (and in some countries there is no growth yet) there has been severe contraction, ranging from 20 per cent over three years in Poland, to over 60 per cent in ten years in the Ukraine (Table 1). These unfavorable results are the consequence of both the legacy of the previous system and the policies exercised during transition, though it is obvious that the latter are of major importance.

These policies were, to a large extent based on the so-called Washington consensus. The set of policies designed along this line stresses the importance of liberalization, privatization, and opening of postsocialist economies, as well as the necessity of sustaining financial discipline. However, having been developed for another set of conditions, this approach was initially missing crucial elements necessary for systemic overhaul, stabilization, and growth. These elements include institution building, improvement of corporate governance of the state sector prior to privatization, and the redesign of the role of the state, instead of its hasty withdrawal from economic activities. The incorrect assumption that emerging market forces can quickly substitute the government in its role in development of new institutional set up, investment in human capital, and the development of infrastructure, has caused severe contraction and growing social stress. New institutional arrangements are of key importance for successful transformation. A market economy requires not only liberal regulation and private ownership, but also adequate institutions. For this reason, transition can only be executed in a gradual manner, since institution building is a gradual process based upon new organizations, new laws, and the changing behavior of various economic entities.

The need to manage the institutional aspects of transition have been recognized and addressed only in the later stages. There is a need to search for a new consensus on policy reforms necessary for sustained growth. Against the backdrop of recent experience with the crises of several emerging markets (including those in transition countries), the outline of a new consensus - a post-Washington consensus - can be drawn. It points not only to the need for liberal markets and open economies, but stresses the new role of the state, the fundamental meaning of market organizations and the institutional links between them, and the need for more equitable growth.

2. Policy Without Growth: Missing Elements

From the beginning of this decade the so-called Washington consensus has been accepted as common wisdom on policies for movement from stabilization to growth. It was assumed that tough financial policy, accompanied by deregulation and trade liberalization, would be sufficient to conquer stagnation and launch economic growth.

A summary of the 1989 Washington consensus was given by John Williamson (1990), who outlined the proposed set of policies, stressing the importance of the organizations involved.[1] He enumerated 10 points that, at the time, seemed to be agreed upon by influential

[1] There has always been a question as to the actual existence of a Washington consensus. Was a consensus achieved, or was the effort just an intention and well-motivated attempt? In fact, the latter is the case. "There is no standard terminology for these sets of doctrines, and various practitioners advocated these doctrines with varying degrees of subtlety and emphasis. The set of views is often summarized as the 'Washington consensus", though to be sure, there never was a consensus even in Washington (let alone outside of Washington) on the

financial organizations, political bodies, and professional economists:

- *Fiscal Discipline.* Budget deficit... should be small enough to be financed without recourse to the inflation tax...
- *Public Expenditure Priorities.* Expenditure should be redirected from politically sensitive areas ... toward neglected fields with high economic returns and the potential to improve income distribution....
- *Tax Reform.* Tax reform involves broadening the tax base and cutting marginal tax rates. The aim is to sharpen incentives and improve horizontal equity without lowering realized progressivity....
- *Financial Liberalization.* The ultimate objective of financial liberalization is market-determined interest rates, but experience has shown that, under conditions of a chronic lack of confidence, market-determined rates can be so high as to threaten the financial solvency of productive enterprise and government.
- *Exchange Rates.* Countries need a unified (at least for trade transactions) exchange rate set at a level sufficiently competitive to induce a rapid growth in non-traditional exports and managed so as to ensure exporters that this competitiveness will be maintained in the future.
- *Trade Liberalization.* Quantitative trade restrictions should be rapidly replaced by tariffs, and these should be progressively reduced until a uniform low tariff in the range of 10 percent (or at most around 20 percent) is achieved....
- *Foreign Direct Investment.* Barriers impeding the entry of foreign firms should be abolished; foreign and domestic firms should be allowed to compete on equal terms.
- *Privatization.* State enterprises should be privatized.
- *Deregulation.* Governments should abolish regulations that impede the entry of new firms or that restrict competition, and then should ensure that all regulations are justified by such criteria as safety, environmental protection, or prudential supervision of financial institutions.
- *Property Rights.* The legal system should provide secure property rights without excessive costs and should make such rights available to the informal sector.

(Williamson 1997, p. 60-61)

Later, mainly under the influence of the experience with overhauling the Latin American economies over the first half of 1990s, and taking into consideration the lessons learned from Eastern Europe and the former Soviet Union, the new agenda was presented. While it includes obvious points from earlier thought, there are certain new concerns and emphases. Again, 10 points were raised:

---

appropriateness of these policies." (Stiglitz 1998b, p. 58)

- Increase saving by (inter alia) maintaining fiscal discipline.
- Reorient public expenditure toward (inter alia) well-directed social expenditure.
- Reform the tax system by (inter alia) introducing an eco-sensitive land tax.
- Strengthen banking supervision,
- Maintain a competitive exchange rate, including both floating and the use of the exchange rate as a nominal anchor.
- Pursue intra-regional trade liberalization.
- Build a competitive market economy by (inter alia) privatizing and deregulating (including the labor market).
- Make well-defined property rights available to all.
- Build key institutions such as independent central banks, strong budget offices, independent and incorruptible judiciaries, and agencies to sponsor productivity missions.
- Increase educational spending and redirect it toward primary and secondary school.

(Williamson 1997, p. 58)

The new items on this agenda correctly address the issues of institution building, environmental protection, and investment in education, yet they are still missing some points of great importance which are especially pertinent to transition economies. First of all, dealing with corporate governance reform in the state sector before privatization is not mentioned, nor is the behavioral aspect of institution building. Also, the necessity for equitable growth is still overlooked. The shortest point on the agenda of the early Washington consensus, i.e., "Privatization. State enterprises should be privatized," is in reality a long-term policy challenge. Even if there is a sound commitment to privatize quickly and extensively-which is not always the case-it is not feasible, for both technical and political reasons. There are also the issues of sequencing, pace, distribution of costs and benefits, and the efficient exercise of corporate governance.

The partial failure of the Washington consensus with regard to transition economies must be linked to the neglect of the significance of institution building for the onset of growth, even if economic fundamentals are, by and large, in order. Institutions change very slowly, but they have a strong influence on economic performance.[2] Such an oversight explains why so many Western scholars initially did not properly understand the real problem. Expectations of growth were based on the assumption that market institutions, if they had not yet appeared automatically, would somehow rise up soon after liberalization and stabilization measures were executed. It was believed that if policies were put in place to secure the progress of stabilization and enhance sound fundamentals, the economy should regain momentum and

[2] As the 1993 Nobel Laureate in Economics states:".. .Western neo-classical economic theory is devoid of institutions, it is of little help in analyzing the underlying sources of economic performance. It would be little exaggeration to say that, while neo-classical theory is focused on the operation of efficient factor and product markets, few Western economists understand the institutional requirements essential to the creation of such markets since they simply take them for granted. A set of political and economic institutions that provides low-cost transacting and credible commitment makes possible the efficient factor and product markets underlying economic growth." (North 1997, p. 2)

start to develop quickly. However, what actually happened was much more depressing. Because of a vacuum with neither a plan nor a market system, production capacity was utilized even less than previously, savings and investments began to decline, and instead of fast growth there was deep recession. Instead of sustained growth, liberalization and privatization without a well-organized market structure led to extended contraction. This was not only the legacy of a socialist past, but also the result of current policies. A lack of institutional development turned out to be the missing element in transition policies based on the Washington consensus.

Under some circumstances, though not in every case, the manner of reasoning characteristic of the Washington consensus may be relevant to the challenges faced by distorted and less developed market economies. The early Washington consensus was actually aimed at countries that already had a market economy, and were not just in transition to such a system.[3]

At the outset of transition, the only relatively developed part of a market infrastructure was a commodities trading network, but even this was operating under chronic shortages. A capital market structure was nonexistent. The lack of financial intermediaries discouraged accumulation and worsened allocation of savings. Thus, immediately after the collapse of socialism, the lack of proper regulation of the emerging capital market and the dearth of such key organizations as investment banks, mutual funds, a stock exchange, a security control commission, etc, caused distortions that could not be offset by liberalization and privatization. A social security system protecting against unemployment did not exist, because it was not needed in a full-employment economy. Also, a process of retraining professionals to enable them to work in the market environment was needed. This takes years, and thus it would be much wiser to manage the processes of liberalization and privatization at a pace compatible with the speed of human capital development. Otherwise, loosened market forces will not be able to shape economic structures and processes, and raise competitiveness and ability to grow.

There seems to be a growing agreement that the early Washington consensus must be revised and adjusted toward actual challenges and new circumstances. If it is going to work, elements so far missing must be included. These elements concern institutional arrangements, though not exclusively. Some other elements were missing regarding the overhaul of the Latin American debt crisis, others in the case of counteracting the Eastern Asia's contagion, and still others in fighting the Eastern European transitional depression. In the latter, eight elements are of key importance:

- The lack of organizational infrastructure for a liberal market economy.
- Weak financial intermediaries unable to efficiently allocate privatized assets.
- A lack of commercialization of state enterprises prior to privatization.
- Unqualified management unable to execute sound corporate governance under the conditions of a deregulated economy.

---

[3] Joseph Stiglitz (1998a), while stressing the importance of governments as a complement to markets, points out that the consensus achieved in the late 1980s and early 1990s between the United States Treasury, the IMF, and the World Bank, as well as some influential think tanks, was catalyzed by the experience of Latin America in the 1980s. He claims that for this reason countries facing different challenges have never found satisfactory answers to their most pressing questions in the Washington consensus.

- A lack of institutional infrastructure for competition policy.
- A weak legal framework and judiciary system, and a consequent inability to enforce tax code and business contracts.
- Poor local government, unprepared to tackle the issues of regional development.
- A lack of non-governmental organizations (NGOs) supporting the functioning of the emerging market economy and civil society.

In postsocialist countries, however, organizations essential to a market economy were either distorted or did not exist, so the economy could not expand.

3. Toward a New Consensus

Since the mid 1990s, the Bretton Woods organizations have started to pay more attention to the way market structures are organized as well as to the behavioral aspects of market performance. A number of less developed and transition economies have learned quickly that there is no sustained growth without sound fundamentals. Later, it was learned and emphasised that the market and growth need both liberalization and organization. Now, due to the experience of transitional contraction, and because of conclusions drawn from the East - Asian crisis, we have learned that even with sound fundamentals, i.e., a balanced budget and current account, low inflation, a stable currency, liberalized trade, and a vast private sector, there will not be sustained growth if these favorable features are not supported by an appropriate institutional setup. Actually, without such a setup, the fundamentals themselves will become unsound and unsustainable, which has been proved time and again by actual developments, for instance, in the Czech Republic or more recently in Brazil.

Rather than a permanent agreement between principal partners, the process of developing new consensus must involve a constant search for such agreement as well as a quest for new partners. A good example of such progress is the World Bank's 1996 Annual Development Report, devoted entirely to the transition from plan to market (World Bank 1996), and the September 1996 IMF Interim Committee Declaration on a Partnership for Sustainable Global Growth (IMF 1996). The latter statement may be seen as a modified version of the early Washington consensus. Among eleven points, six are of special relevance to the situation of transition economies. Point one stresses that monetary, fiscal, and structural policies are complementary and reinforce each other. Point three claims that there is a need to create a favorable environment for private savings. Point seven accentuates that budgetary policies have to aim at medium-term balance and a reduction in public debt, while point nine says that structural reforms must be supplemented with special attention paid to the labor markets. Point ten stresses the importance of good corporate governance, and point eleven cautions against corruption in the public sector and money laundering in banks, warning that their monitoring and supervision must be strengthened.[4]

However, the Washington consensus is not an official position taken by any particular organization or institution. It is rather a gathering of policy options agreed upon by important partners to such an extent that the agreement may be considered a consensus. Yet there is still a search for agreement between the organizations as well as among the policymakers, policy-

---

[4] Other points, also important for sustainable development, address the issues of exchange rate stability, disinflation, resisting protectionist pressure, progress toward increased freedom of capital movement, and fiscal adjustment by reducing unproductive spending while ensuring adequate investment in infrastructure.

oriented researchers and advisors. Being personally involved in all three, i.e., research, advice giving, and policy-making, it was quite interesting for me to receive a reaction to the outcome of my involvement from the author of the Washington consensus. John Williamson[5] stressed that:

I was particularly pleased that you have tried to define an alternative to big bangery in terms of a more careful design of individual policy components rather than generalized go slow ("gradualism").[6] On just about all the individual items you identify, certainly including protection and privatization, I agree with you in retrospect, and indeed I would have agreed with you at the time...

But in all honesty I have to confess that I still worry that had I been in the place of Balcerowicz (who was the minister of finance in Poland in 1989-91) I might not have put together the decisive package that I think in retrospect Poland needed at the time, and that laid the foundation for your successful period in office. Perhaps one needed a little bit of overkill to make it emotionally possible for your allies to accept that the world had changed, and even to give you the opportunity of correcting their excesses and in the process winning their acceptance of the new model? It reminds me of the situation in my home country: 1 am much more comfortable with Tony Blair than with Mrs. Thatcher, but I am not sure that we could have had him without her.

This time, psychological and political, rather than economic and financial, arguments are given as decisive factors favoring the radical set of policies undertaken at the beginning of the 1990s. Nonetheless, it seems that we still differ as to the evaluation of the scope and costs of that overkill. Was it only "a little bit" of otherwise necessary measures, as one may still believe, or was it a serious excess of unnecessary radicalism, as apparantly proved elsewhere (Kolodko 1991, Nuti 1992, Rosati 1994, Poznanski 1996, Hausner 1997)?

When ideas and strategies involving more gradual change, and the active involvement of the state in institutional redesign in postsocialist transition economies, were expounded for the first time (Kolodko 1989 and 1992, Laski 1990, Nuti 1990, Poznanski 1993), and when they were later implemented in Poland (Kolodko 1993, 1996 and 1999), they were unorthodox and controversial, with respect to the Washington consensus. In fact, these new ideas did not so much endorse more gradual change, but recognized that the necessary changes would be time-consuming by their very nature. In 1997 and 1998, however, even in official international circles, there were widespread signs that a new consensus is emerging, and that it is, to a certain extent, based on the ideas implemented in Poland in 1994-97 (Kolodko and Nuti 1997). Thanks to its multi-track approach, Poland is now recognized to have avoided the adverse experience of other transition economies. The new ideas and policies, developed under the "Strategy for Poland", were to some extent elaborated against the mainstream of the early Washington consensus and now have contributed significantly to its revision.

In the aftermath of the Southeast Asian crisis, as it has spread beyond anybody's expectation, the train of thought has also begun to change track among the most influential

---

[5] Direct communication between the authors.

[6] This alternative regards policy reorientation executed under the medium-term transition and development program "Strategy for Poland" (Kolodko 1996), when the author was Poland's First Deputy Premier and Minister of Finance in 1994-97. The outline and implementation of this program compared with the earlier policies are described as The Polish Alternative in Kolodko and Nuti (1997).

opinion leaders in the international financial community. This has been accompanied by a much belated onset of doubt about the accuracy of the recipe proposed for postsocialist emerging markets, especially for the most important one, i.e., Russia.[7] All the while, the Bretton Woods organizations were insisting upon, and determining their financial involvement based on tough fiscal and monetary policy. If it was a period of 10 per cent GDP decline, or a period of 10 percent expansion, there was always pressure to bring the fiscal gap down and keep the real interest rate up. Even when the budget deficit was smaller than that of industrial countries and the real interest rate was so high that it was not possible to contain the deficit further, due to the soaring costs of servicing the public debt, there was a permanent requirement of continuing fiscal and monetary tightness. A high real interest rate is fine for portfolio investors (through interest rate differentials), but at the cost of both the budget, i.e., taxpayers, and the business sector, owing to the crowding out effect.

The importance of a change in corporate governance-as opposed to a mere transfer of property titles-is now being recognized even by previously keen supporters of rapid, mass privatization. There is no clear evidence that privatized enterprises perform better than state enterprises just as a result of privatization.[8]

After the laissez-faire of the early transition, values of cooperation and solidarity are being rediscovered.[9] Although it should be obvious from the outset that transition based upon a sort of laissez-faire must bring "intolerable inequities and instability" (Kolodko 1999), it is still not acknowledged widely enough, and such an obvious conclusion is still challenged. The World Bank 1996 *World Development Report* emphasizes very strongly the need for social consensus, though it was very difficult to reach as such, considering the falling output and growing inequality in transition economies.[10]

---

[7] A consensus has not yet been agreed upon, but lessons are gradually being learned. It is now admitted that, "The benefits brought by short-term international lenders are questionable: they do not provide new technology, they do not improve the management of domestic institutions; and they do not offer reliable finance of current account deficit. In countries with high savings rates, they also increase already excessive investment rates. To manage the inflows, borrowers may have to accumulate huge reserves... The Asian saga proves, once again, that liberalization of inadequately regulated and capitalized financial system is a recipe for disaster." (Wolf 1998).

[8] Nicholas Stern (1996, p. 8) points to the process of restructuring, which ...itself will be a major and fundamental task involving investment, hard decisions and dislocation. It will be much less painful if economic growth, effective corporate governance and well-functioning safety nets are established. Thus good corporate governance of the public enterprises and sound competition policy are at least as essential for recovery as privatization and liberalization.

[9] Even billionaire financier George Soros has not hesitated to admit that, "Although I have made a fortune in the financial markets, I now fear that the untrammeled intensification of laissez-faire capitalism and the spread of market values into all areas of life is endangering our open and democratic society.. .Too much competition and too little cooperation can cause intolerable inequities and instability." (Soros 1997).

[10] "Establishing a social consensus will be crucial for the long-term success of transition - cross-country analyses suggest that societies that are very unequal in terms of income, or assets tend to be politically and socially less stable and to have lower rates of investment and growth". (World Bank 1996).

Table 1: Recession and Growth in Transition Economies, 1990-97

Countries	Years of GDP decline	Did GDP fall after some growth?	Average annual rate of GDP growth			1997 GDP index (1989 = 100)	Rank
			90-93	94-97	90-97		
Poland	2	no	-3.1	6.3	1.6	111.8	1
Slovenia	3	no	-3.9	4.0	0.0	99.3	2
Czech Republic	3	**yes***	-4.3	3.6	-0.4	95.8	3
Slovakia	4	no	-6.8	6.3	-0.3	95.6	4
Hungary	4	no	-4.8	2.5	-1.1	90.4	5
Uzbekistan	5	no	-3.1	-0.3	-1.7	86.7	6
Romania	4	**yes**	-6.4	2.1	-2.2	82.4	7
Albania	4	**yes**	-8.8	4.9	-2.0	79.1	8
Estonia	5	no	-9.7	4.1	-2.8	77.9	9
Croatia	4	no	-9.9	3.0	-3.4	73.3	10
Belarus	6	no	-5.4	-2.6	-4.0	70.8	11
Bulgaria	6	**yes**	-7.4	-3.6	-5.5	62.8	12
Kyrgyzstan	5	no	-9.3	-2.4	-5.8	58.7	13
Kazakhstan	6	no	-6.7	-6.0	-6.3	58.1	14
Latvia	4	**yes**	-13.8	2.2	-5.8	56.8	15
Macedonia	6	no	-12.9	-0.8	-6.9	55.3	16
Russia	7	**yes***	-10.1	-53	-7.7	52.2	17
Turkmenistan	7	no	-4.5	-12.5	-8.5	48.3	18
Lithuania	5	no	-18.3	0.5	-8.9	42.8	19
Armenia	4	no	-21.4	5.4	-8.0	41.1	20
Azerbaijan	6	no	-14.5	-5.7	-10.1	40.5	21
Tajikistan	7	no	-12.2	-8.4	-10.3	40.0	22
Ukraine	8	no recovery	-10.1	-12.1	-11.1	38.3	23
Moldova	7	**yes***	-12.6	-10.2	-11.4	35.1	24
Georgia	5	no	-24.1	2.9	-10.6	34.3	25

Source: National statistics, international organizations and author's own calculations

Note: *GDP contracted again in 1998

It is now somewhat accepted that in economies still affected by structural rigidities, such as formal and informal indexation and sluggish supply response, once inflation has fallen well below *a.* threshold of about 20 per cent, attempts at speeding up disinflation would have significant, perhaps intolerable costs - as, for instance, in Romania in 1998-99 - certainly higher than the moderate, but steadily falling, inflation actually experienced by some countries leading in transition, and those recently following Poland's path. What counts is that inflation should continue to fall steadily and noticeably, without ever accelerating again. Such a process of disinflation contributes not only to an increased credibility of the government and monetary authorities, but secures the predictability of economic developments and creates a better business environment and confidence on the international scene.

The prerequisite for an enhanced savings ratio, i.e., faster than income increase, is a growth of real income, stabilization, and optimistic expectations. Only against such a background can the propensity to save steadily increase. The 1996 EBRD *Transition Report,* which is devoted to infrastructure and savings, stresses the equal role of increasing government savings-especially through the overhaul of social security and pension systems, and more broadly based taxation at lower rates-and the development of contractual savings and life insurance. From this perspective, the pressure for high and positive real interest rates has been grossly misplaced. The fiscal and quasi-fiscal activities of central banks, notably in the emerging economies and especially in postsocialist countries, have attracted considerable attention (Fry 1993). In particular, the costs of sterilization policies, which are the result of excessive interest rate differentials and/or of undervalued currencies, have come to the fore, e.g., the OECD country study of the Czech Republic (OECD 1996). It turns out that, for a considerable time, the central banks of both the Czech Republic and Poland have wasted about 1 per cent of GDP with their unfortunate sterilization policies (Nuti 1996).

The Washington consensus is not an official position taken by any particular organization or institution, it is rather a gathering of policy options agreed upon by important partners to such an extent that the agreement may be considered a consensus. This time, along with the continuous leading role of the Washington-based organizations, especially the IMF and the World Bank, it must encompass more partners. Other international organizations, like the UN, OECD, WTO, ILO, and EBRD, should play a bigger role than they have thus far. Also, regional organizations, like ASEAN in Asia, CEFTA in central Europe, or the CIS in the former Soviet Union, should be better prepared to present their purpose in the global forum and to try to influence the process of changing the international financial and economic order. Some international NGOs ought to be more influential too.

Thus the search for the new consensus must rely not only on the quest for new policies agreed in Washington, but also on the policies agreed between Washington and other important places in different parts of the global economy. There are many hints that such a process is on the way, but there is much more yet to be accomplished.

4. Intellectual or Political Controversies?

Intellectual misunderstandings result from political antagonism, and the difference is more about conflicts of interests than about alternative theoretical concepts and scientific explanations. Of course, it does happen that policy mistakes occur due to a lack of experience and proper knowledge, but more often this confusion stems from obedience to a particular group of interests, or to "theoretical schools", that happen to be ideological and political lobbies too.

John Williamson (1990) points to "political" and "technocratic" Washington, stressing their different priorities and policy options. However, there are important divisions not only between the "political" and "technocratic" parts of Washington, but also within them. What makes the picture still more complex, is the fact that some of the actors on the so-called "technocratic" side of the scene do play, even if unintentionally, political roles as well. This is also true with regard to the Bretton Wood organizations, especially the IMF. Their influence, and the consequences of their policies, simply have such serious implications for particular countries and regions, if not the entire global economy, that sometimes they have much more to say -and decide-than what may be seen as purely "technocratic" concerns. The position of the IMF towards large countries in transition, such as Russia and Ukraine, are the best cases in point here.

But the issue is even more complex than that, because-aside from intellectual controversies and different normative values-there are also different political, economic, and financial interests involved. Otherwise it would be impossible to interpret why erroneous policies continued, in many cases, even after it was obvious that they were wrong.[11]

Therefore, in designing good policy, it is important not only to be right but also to be

[11] This was the case, for instance, with early liberalization and stabilization policy in Poland in 1989-1992, the neglect of corporate governance in the Czech Republic in 1993-96, the Russian privatization of 1994-98, executed with the active involvement of politically connected informal institutions, and with fraudulent Albanian financial intermediaries in 1995-97, which were tolerated until the whole economy eventually collapsed.

able to enforce the preferred policies. Often it happens that the strongest lobby is not where truth and logic are, but where power and money are. Therefore, true reforms, those that facilitate the public interests of the many as opposed to the particular interests of the few, must always be thought of as a means to long-term targets, i.e., sustained growth. Otherwise, there will be fictitious "progress" reflected in an artificial improvement of the situation. A sound fiscal stance, low inflation, a stable exchange rate, and overall financial stabilization are only the means of economic policy, while sustained growth and a healthier standard of living are its ends. Yet after several years of exercising these policies, neither growth nor a higher standard of living has been achieved in transition countries. Important changes like privatization and liberalization are merely instruments, not targets. If the share of private sector, the scope of trade liberalization, or the deregulation of capital transfers are bigger than they would be without these policies, but at the same time economic contraction is deeper, or growth more sluggish, and the standard of living deteriorating, then the overall situation is worse, not better. Yet, often, economic status is judged from the perspective of a particular group of interests, and this perspective is presented as a picture of the general economic situation. Too much attention is focused on the means that, hypothetically, should lead to an improvement of efficiency and competitiveness, instead of concentrating on the outcome of these exercises. Such bias leads to policy distortion, and the tools becoming the goals themselves, without sufficient concern about their impact on the real economy.

So, while evaluating the actual standing of an economy and policy, one must consider not only what is examined, and by what means it is scrutinized, but also whom is carrying out such an evaluation. It is obvious that, for instance, the evaluations of Moody's rating agency and the Russian trade unions must be as different as the interests of the Morgan Stanley investment bank and the Siberian miners.

Hence, the aims of development policy are more comprehensive, and their interpretation is changing even among those who subscribed to the Washington consensus, primarily the World Bank. Not only should a balanced economy and sustained growth be of serious policy concern, but also standard of living improvement, distribution of income, the environment, and, last but not least, democracy itself.[12] Yet now even the IMF is trying to join the club and claim that it too would like to aim at a fairer distribution of the fruits of growth, if only the advised policies would deliver some.[13] However, there is still a long distance to travel from the emerging intellectual consensus to a real political agreement about appropriate policy reforms and actions. And, of course, even if intellectual consensus is closer than before, controversies regarding different normative values and contradictory interests do remain.

---

[12] Our understanding of the instruments to promote well-functioning markets has also improved, and we have broadened the objectives of development to include other goals, such as sustainable development, egalitarian development, and democratic development". (Stiglitz 1998a, p. 1). True, the World Bank always was more inclined toward social issues and development of human capital than other international financial institutions, unlike just any other bank. Usually banks look to profits, not to the human development index as an indicator of their success. It must be acknowledged that the World Bank has become involved in a number of projects, not only in transition economies, that serve to increase standards of living and decrease poverty.

[13] Stanley Fischer, the IMF First Deputy Managing Director, himself concerned about equitable growth for a long time, has raised the question Why do equity considerations matterfor the Fund? And then has answered that: "First, as a matter of social justice, all members of society should share in the benefits of economic growth. And although there are many important arguments about precisely what constitutes a fair distribution of income, we accept the view that poverty in the midst of plenty is not socially acceptable. But, second, there is also an instrumental argument for equity: adjustment programs that are equitable and growth that is equitable are more likely to be sustainable. These are good enough reasons for the IMF to be concerned about equity considerations - whether it be poverty reduction or concerns about income distribution in the programs the IMF support." (Fischer 1998, p. 1).

5. Transition as a Process of Systemic Redesign

The only chance for the ultimate success of transformation is to design suitable institutions, which often must be developed from the beginning. In the case of postsocialist countries, some took a course of gradual, perhaps even excessively slow, liberalization and privatization. Though this was followed by relatively milder contraction, it also caused a delay of crucial structural reforms. Nevertheless, if the given time is used for appropriate institution building, it can pay off later. If, however, the time of gradual liberalization is wasted from the perspective of institutional reforms, than the chance for long-term expansion is indeed weak. Some countries followed a path of rapid change. Although under these circumstances contraction was more severe in early stages, later institution building was often more advanced.

Government involvement in the process of comprehensive institution building is of vital importance. Thus, if the state fails to design a proper institutional setup, then market failures prevail and informal institutionalization takes over. Instead of a sound market, in the words of the chief economists of the World Bank and the European Bank of Reconstruction and Development, a "bandit capitalism" emerges.[14] A system where "only the stupid pay taxes", the contracts are not executed as agreed, or the payments are not made on time, is hardly a market economy. It is rather chaos stemming from institutional disintegration.

Such institutional pathologies could arise as a result of transition-by-chance, as opposed to transition-by-de-sign. In several cases inaccurate transition policy has led to such adversity. Without the knowledge of how a new system works, and without a vision of how to get to that system, there is no way to accomplish the target on time and in good shape. Transition becomes protracted: costs are higher than necessary, while results are not as good as they could be under alternative scenarios - the recession lasts longer, recovery comes later, and output expands more slowly (Poznanski 1996).

Proper institutional design is paramount during the time of transition. At the same time, its accomplishment is more difficult than elsewhere, because of institutional discontinuity. The market also needs a proper legal environment, one that is able to support the execution of market rules, the enforcement of contracts, and the correct behavior of economic agents (firms, households, organizations, and the government). For these reasons, transition calls not for a dismissal of government, but for its streamlining and adjustment to the new circumstances.[15] Unfortunately, the state's ability to address the issue of law enforcement is much weaker during transition than it was under state socialism. It is also weaker than under the governments of traditional market economies, with mature civil societies and well-functioning institutions. Postsocialist states have been deliberately weakened by neo-liberal policies, often undertaken with the official support of the governments of leading industrial

[14] "It is easy to identify institutional arrangements that work well: each partner does what it is supposed to do, there is good coordination, little conflict and the economy grows smoothly and rapidly. We can also recognise ill-functioning institutional arrangements: change is inhibited by bureaucratic requirements or there is "bandit capitalism" with pervasive corruption and deceit." (Stern and Stiglitz 1997, p. 20).

[15] The World Bank, unlike the advocates of market fundamentalism, admits that: "The state makes a vital contribution to economic development when its role matches its institutional capability. But capability is not destiny. It can and must be improved if governments are to promote further improvements in economic and social welfare (...) Three interrelated sets of institutional mechanisms can help create incentives that will strengthen the state's capability. These mechanisms aim to: (i) Enforce rules and restraints in society as well as within the state, (ii) Promote competitive pressures from outside and from within the state, and (iii) Facilitate voice and partnership both outside and within the state." (World Bank 1997).

countries and international organizations.[16] As for new partnerships between market players, that is precisely what gradual institution building is about. In the long-term, such partnerships enhance the environment for growth, but in the initial stages ongoing changes can destabilize existing links between partners involved in economic activities. The old relationships cease to exist, while the new ones are only in *statu nascendi.* Thus active state participation is needed, since market relations are often associated with inappropriate events owing to the activities of various lobbies and informal organizations, including organized crime.

The new institutional set up must be founded on the basis of new organizations that did not exist-since they were not needed-under the centrally planned state economy. Transition calls not only for a new legal system, but also for learning a new type of behavior. Enterprises, banks, the civil service and state bureaucracy, even households-must all quickly learn how to perform under the circumstances of the new reality, i.e., the emerging market system. Political leaders in postsocialist countries do not have, as Moses did, 40 years to turn their people around. To accelerate this process and cut the costs of institutional and cultural adjustment requires special training and education efforts by political and intellectual elites, and non-governmental organizations (NGOs). The Bretton Woods institutions are contributing to this acceleration. After seeing that providing new skills and knowledge is sometimes more important than just lending money, they have started to pay much more attention to technical assistance and professional training.

We speak of building institutions, but in reality, they must be learned. This is the process. By the very nature of this long-term and complex process, it can not be carried forward in a radical way. It takes time and is costly in both the financial and the economic sense. It is risky and can expose a country to social and political tensions. Only part of the multi-layer transition process, namely liberalization linked to stabilization, can be exe-cuted-if political conditions permit-in a radical manner. Even this is not an imperative, but a policy choice depending on the scope of monetary and fiscal disequilibria, and on the range of social tolerance. As for structural adjustment, institutional reform, and behavioral change, they will take a long time under any conditions. The difficulties have not derived, however, from a lack of knowledge of how the market works, but from a difficulty in knowing how to get to a market system from the specific situation of the late socialist economies.

Simultaneously, a process of learning by doing is taking place. Both in the East and West previous theoretical explanations and pragmatic approaches have evolved significantly Professionals from transition countries have gained knowledge of market performance. Great political and intellectual debates, training at home and abroad, and simple experience of the process, have brought tremendous progress vis-a-vis the qualifications of researchers, entrepreneurs, and political elites. Professionals from developed countries, including government representatives dealing with transition, experts of international organizations, and the business community, have learned about the specific circumstances of transition. They have been able to absorb knowledge on various features of postsocialist realities, and have understood that one should attack the challenges in a somehow different, rather unorthodox way. Major lessons about the significance of institution building for durable growth have been learned at last, and the proper policy conclusions seem to have been drawn. Thus, with much

[16] For example, the Russian government is weak and unable to collect due taxes not because of the legacy from the communist period, but owing to an ill-advised liberal approach and incorrect deregulation and privatization. Now it is difficult to bring things under the sovereignty of the new state, because the situation has been allowed to get out of control of the old state, mainly because of mismanaged liberalization and the manner in which institutional redesign occurred.

better coordinated international assistance, transition policies have shifted in the right direction in a number of countries.

In countries that enjoyed a relatively liberal system under socialism, the process of learning proceeds much faster. If there was already a private sector and decentralized management of state companies, learning new methods of corporate governance is smoother. If there was already a two-tier banking system, learning sound commercial banking is easier. If there was already an antitrust body, this previously relatively useless organization (because of shortages) now must regulate well-supplied markets to make them truly competitive.

In countries which had traditional centrally planned regimes until the late 1980s, learning is slower. This factor explains the differences in the economic performance of such neighbors as Hungary, on one hand, and Romania, on the other. The faster the process of institution building, the better the environment for business activity, and hence for growth. Government guidance and intervention can hasten the whole process, as in Poland in the 1990s, but if mismanaged, as it was over the same period of time in Russia, can spoil it too. Nonetheless, such a risk cannot be an excuse for state withdrawal from these activities. The risk calls for wise guidance and rational intervention.

From a very long-term viewpoint, the system's design plays an instrumental role in expansion and development. In the very long term, the transition should be seen as a major instrument of development policy. Systemic changes that do not lead to durable growth and sustainable development do not make sense. When one set of solutions has ceased to serve the purpose, another must replace it and take over. Hence, the system ought to be flexible enough to meet the challenge of changing circumstances. However, the system itself cannot serve as a substitute for good policy. In history we can see that it is most frequently sufficient to improve policies, with-

out overhauling an entire system. Of course, during transition there is also room for better or worse economic policy, for wise or not-so-wise government action, and for various forms of involvement of the international community.

6. Policy Conclusions

1. The main policy conclusion - and the key implication of the post-Washington consensus - is that *the institutional arrangements are the most important factor for progress toward durable growth.* What is taken for granted in some market economies, i.e., an institutional setup sufficient for far reaching liberalization and free market performance, must be created, often from the outset, in countries moving from statist, centrally planned economies. If there is a choice between developing these institutional arrangements spontaneously (by chance) or in a way directed by the government (by design), then the latter option is preferable in the case of postso-cialist countries. The governments of industrial countries and international organizations must, however, assist several governments in these attempts.

2. *The size of the government is less important than the quality of its policy and the manner of change of government size.* In transition economies the issue is not just downsizing the government, but a deep restructuring of the public finance system and a change in the policy targets and means. Basically, fiscal transfers should be redirected from non-competitive sectors toward institution building (including behavioral and cultural changes), investment in human capital, and hard infrastructure. Attempts to downsize the government

through cuts in budgetary expenditure can cause more harm than good; the issue is that often the government cannot be downsized without causing contraction and a deterioration of the standard of living. It must be considered that creative downsizing should occur only when the economy is on the rise, though most often the strongest attempt to do so is undertaken during a period of deep contraction.

3. *Unlike certain liberalization measures, institution building, by its very nature, must be a gradual process.* Thus feedback between specific "inputs" to this process and its "output" must be monitored constantly and policies must be adjusted and corrected. In postsocialist transition there are many uncharted waters where one should not rely on misguided analogies with experience from distorted market economies. One must consider the specific features of the type of emerging market. Therefore it is necessary to orchestrate some institution building innovation in a way previously unseen in other places. This is true first regarding privatization and the development of capital markets.

4. *If institutional arrangement is neglected and left to the spontaneous processes and unleashed forces of liberalized markets, then informal institutionalization fills the systemic vacuum.* Extreme cases here are widespread corruption and organized crime. These are the two main maladies in countries after liberalization and privatization under weak governments. Sometimes governments are weak not because they are too large, but because they were forced to become smaller too early, that is, before the infant market was able to substitute for the state. Prematurely, or too extensively, downsized government is not strong enough and so the market expands in the informal sector (shadow economy), while difficulties mount in the official economy. Subsequently profits accrue to the informal sector, but revenues fall in the official sector, with all the negative consequences for the budget and social policy. Thus the market works in such a way that profits are privatized, but loses are socialized in a politically unsustainable way.

5. *In transition economies policies must transform and streamline the judiciary system to serve the needs of the market economy.* This is a great challenge, since the old system of contract execution under planned allocation has ceased to exist, but a new system of contract implementation under market rules and culture has not yet matured. The establishment and development of new law-e.g., trade and tax code, capital market regulation, property rights protection, competition and anti-trust rules, banking supervision, consumer protection, environmental protection-are even more important and ought to be addressed before privatization of state assets and liberalisation, since the latter can contribute to sound growth only if the former is secured.

6. *A shift of competence and power from the central government to local governments is necessary for deregulation of the postsocialist economy.* Such a shift means moving the public finance system toward decentralization, and streamlining local governments by giving them larger fiscal autonomy, otherwise the process of weakening the central government is not matched by enhancement of local governments. The joint position of both levels of government must be seen as an integrated entity needed for the sake of gradual institution building.

7. *There is an urgent necessity to accelerate the development of non-government organizations.* Next to the private sector and the state, this is the third indispensable pillar of a contemporary market economy and civic society. With a lack of a range of NGOs, which are supposed to take care of various aspects of public life, there is a continual tension between the state and society. The expanding private sector does not provide a sufficient or satisfactory

solution to this problem. A growing part of international technical, financial, and political assistance must be channeled into enhancing NGOs, otherwise the infant market economy and democracy in post-socialist countries will not evolve fast enough and the transition will be incomplete.

8. *During transition income policy and government concern for equitable growth are very significant.* Whereas increasing inequity is unavoidable during the initial years of transition, the state must play an active role, through fiscal and social policies, in controlling income dispersion. If disparity growth is tolerated for a number of years during contraction, when the standard of living is improving for a few and declining for many, then the political support fur the necessary reforms will evaporate. Hence, large inequities turn against crucial institutional and structural reforms.

9. *Postsocialist Transition to the market is taking place at a time of worldwide globalization, hence opening to, and integration with, the world economy is an indispensable part of the whole endeavor.* Yet these processes must be managed carefully, and in a gradual manner, with special attention to short-term capital How liberalization. It must be monitored and controlled by the countries' fiscal and monetary authorities, with the support of international financial institutions, e.g., the IMF and BIS. Institution building must first be sufficiently advanced, stabilization having been consolidated into stability otherwise the societies of young emerging markets and democracies are not going to be supportive of the introduction of market mechanism, or integration with the world economy, and they may even become hostile toward such changes.

10. *International organizations should not only support, but also insist on, further regional integration and co-operation*. If growth is expected to be durable and fast, it requires export expansion, which will dependon strong regional links. Thus it calls for institutional support, such as export-import banks, commodity exchanges, credit insurance agencies, and the like. This should be the main institution building concern of the EBRD, supported by directed lending from this bank and by its technical assistance.

11. *The Bretton Woods organizations should reconsider their policies toward transition economies.* If the IMF mainly takes care of financial liquidity, currency convertibility, fiscal prudence and monetary stabilization, the World Bank should further focus attention mainly on conditions for equitable growth and sustain-able development. There is an inclination to confijse the ends with the means of the policy, to subordinate long-term development policy to short-term stabilization policy. Hence, in the future, fiscal and monetary policies must be subordinated to development policy, not vice versa. There is a need for World Bank performance criteria describing socio-economic development as much as there is such a need for the traditional IMF fiscal and monetary criteria. The new set of criteria should always stress the implication of well advised financial policies for growth, capital allocation, income distribution, and the social safety net. The World Bank should not accept and support policy reforms and actions that, while aiming at financial stabilization, may lead to social dcstabilization resulting from lack of growth, spreading poverty, increasing inequality, and divestment in human capital.

12. *The interactive processes of learning-by-monitoring and learning-by-doing continue and will last for several years.* After all, even if there is - as indeed there seems to be - a growing chance for some kind of the post-Washington consensus, this must be seen as a process, and not as an act. Such an emerging consensus must indeed be accomplished among many more partners than just the important organizations based in Washington. Otherwise,

the policies agreed upon in Washington will not be able to deliver what they assume elsewhere. Furthermore, what may be agreed upon currently, must be revised often if conditions and challenges change, as they have done recently and undoubtedly will do again and again in the future. Thus the quest for a comprehensive and implementable consensus on policies facilitating sustainable growth must continue.

References

Fischer, Stanley. 1998. "Opening Remarks." Presented to the conference on Economic Policy and Equity. Washington, D.C.: The International Monetary Fund. June 8-9.

Fry, Maxwell. 1993. The fiscal abuse of central banks. IMF Working Paper 93/58. Washington, DC.: International Monetary Fund.

Hausner, Jerzy. 1997. "The Political Economy of the Socialism's Transformation", Conference paper UNU/ WIDER Project Meeting: Transition Strategies, Alter-natives and Outcomes. Helsinki 15-17 May.

IMF. 1996. Partnership far Sustainable Global Growth. Interim Committee Declaration. Washington, D.C.: International Monetary Fund. September 29.

Kolodko, Grzegorz W. 1989. Reform, Stabilization Policies and Economic Adjustment in Poland, WIDER Working Papers WP 51. Helsinki: World Institute for Development Economics Research of the United Nations University January.

Kolodko, Grzegorz W. 1991. "Inflation Stabilization in Poland: A Tear After". Rivista at Politica Economica No. 6 (June): 289-330.

Kolodko, Grzegorz W 1992. "From output collapse to sustainable growth in transition economies - the fiscal implications". Washington, D.C.: International Monetary Fund. December.

Kolodko, Grzegorz W1993. "A Strategy for Economic Transformation in Eastern Europe."Most, Vol. 4. No. 1:1-25.

Kolodko, Grzegorz W. 1996. Poland 2000. The New Economic Strategy. Warsaw: Poltext.

Kolodko, Grzegorz W. 1998. "A Plan for Russia, " The Harriman Review, Special Issue: The Russian Economy in Crisis". Columbia University, New York, December, pp. 24-27.

Kolodko, Grzegorz W. 1999. From Shock to Therapy. The Political Economy of Postsocialist Transformation. Oxford: Oxford University Press (forthcoming!).

Kolodko, Grzegorz W and D. Mario Nuti. 1997. The Polish Alternative. Old Myths, Hard Facts and New Strategies in the Successful Transformation of the Polish Economy. WIDER Research for Action 33. Helsinki: The United Nations University World Institute for Development Economics Research.

Mantes, Manuel. 1997. "Vietnam: Is There a Socialist Road to the Market?". Conference paper. UNU/WID-ER Project Meeting: Transition Strategies, Alternatives and Outcomes. Helsinki 15-17 May.

North, Douglass C. 1997. The Contribution of the New Institutional Economics to an Understanding of the Transition Problem. WIDER Annual Lectures 1. Helsinki: United Nations University World Institute for Development Economics Research. March.

Nuti, D. Mario. 1990. Crisis, Reform and Stabilization in Central Eastern Europe: Prospects and Western Response. In La Grande Europa, La Nuova Europa: Op-portunita e Riscbi. Sienna: Monti Dei Paschi Di Sienna. November.

Nuti, D. Mario. 1992. "Lessons from Stabilization and Reform in Central Eastern Europe." CEC Working Papers, 92 (May). Brussels: Council of the European Community.

Nuti, D. Mario. 1996. "Exchange Rate and Monetary Policy in Poland 1994-96, or the Case for Privitising the National Bnak of Poland." Conference paper. Helsinki: UNU/WTDER Project Meeting: Transition Strategies, Alternatives and Outcomes. 15-17 May.

OECD. 1996. Czechoslovakia. 1996. OECD Economic Surveys. Paris: Organisation for Economic Co-operation and Development.

PlanEcon. 1998a. Review and Outlook for the Former Soviet Union. Washington, D.C.: PlanEcon, Inc. October.

PlanEcon. 1998b. Review and Outkok for Eastern Europe. Washington, D. *C.:* PlanEcon, Inc. December.

Poznanski, Kazimierz. 1993. Poland's Transition to Capitalism: Shock and Therapy. In Stabilization and Privatization in Poland. Edited by K. Poznanski. Boston: Kluwer Academic Publishers.

Poznanski, Kazimierz. 1996. Poland's Protracted Transition. Institutional Change and Economic Growth. Cambridge: Cambridge University Press.

Rosati, Dariusz. 1994. "Output Decline during Transition form Plan to Market". Economics of Transition Vol. 2 No. 4: 419-42.

Soros, George. 1997. "The capitalist threat". The Atlantic Monthly. February.

Stern, Nicholas. 1996. "The transition in Eastern Europe and the former Soviet Union: some strategic lessons from the experience of 25 countries over six years". Conference paper. OECD/CCET Colloquium. Paris. 29-30 May.

Stern, Nicholas and Joseph E. Stiglitz. 1997. A framework for a development strategy in a market economy: objectives, scope, institutions and instruments. EBRD Working paper 20. London: European Bank for Reconstruction and Development. April.

Stiglitz, Joseph E. 1998a. More Instruments and Broader Goals: Moving Toward the Post-Washington Consensus. WIDER Annual Lectures 2. Helsinki: United Nations University World Institute for Development Economics Research. January.

Stiglitz, Joseph E. 1998b. "Economic Science, Economic Policy, and Economic Advice". Conference paper. Annual Bank Conference on Development Economics on Knowledge for Development. Washington D.C.: The World Bank. April 20 and 21.

Williamson, John. 1990. "What Washington Means by Policy Reform." In John Williamson, editor, Latin American Adjustment: How Much Has Happened? Washington, D.C.: Institute for International Economics.

Williamson, John. 1997. "The Washington Consensus Revisited". In Louis Emmery (ed.). Economic and Social Development into the XXI Century. Washington, DC: Inter-American Development Bank.

World Bank. 1996. From Plan to Market. World Development Report 1996. Washington, D.C.: The World Bank.

World Bank. 1997. The State in a Changing World. World Development Report 1997. Washington, D.C.: Oxford University Press for the World Bank.

JEL classification: N10, O47, **P24**

Keywords: **transition, liberalization, institution-building, resession, growth**