

Strategies for Economic Reform in Former Communist Countries of Central and Eastern Europe

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Abstract: *European integration has always been driven by political factors, starting with the desire to prevent another European war until the desire to share the benefits of integration with the new democratic countries of central and Eastern Europe. But while goals have always been political, the means have always been economical ones.*

Keywords: *European integration, political goals, economic goals, single market*

Introduction

Within the process of the European integration there were basically three great progresses, namely:

1. Formation of the Customs Union between 1958 and 1968, which led to the removal of tariffs and quotas on intra-Community trade.
2. The single market program, implemented between 1986 and 1992 (although there are elements implemented today) that eliminated non-tariff barriers and many of liberalized movement of capital and services in the EU.
3. The creation of Economic and Monetary Union, which integrated the currencies of most member countries and released by the ECB, the single currency.

The Former Socialist Countries of Central and Eastern Europe and the European Integration

The former socialist countries of Central and Eastern Europe have had to go through the process of economic reform to achieve convergence with European economies. According to the monitoring from the part of the IMF (International Monetary Fund) there was applied a strategy of rapid adjustments, unknown until then in the world-which provided a mass privatization of the economy, with a rapid pace.

Poland, Hungary, Czech Republic, Slovakia, Slovenia switched to rapid privatization of economies, but growth periods was short and the recovery process was marked by unexpected macroeconomic instability. This led the Czech Republic to reassess the model of rapid privatization.

The best performances of Poland and Hungary led to the conclusion that the success of the transition depends, above all, of the rapid creation of institutional legal conditions, micro- and macro-economic assessments, capable to determine the development of a new private sector for the Foreign Direct Investments.

We must not forget that Poland and Hungary have benefited from an aid for economic reconstruction-Phare - program - since 1989, from the part of the European Union. In Poland and Hungary, price liberalization policies were adopted earlier, with budget constraints and growing competitive pressure on state enterprises. In Poland, for example, privatization has been slow, but rapid growth in the private sector has provided its share in GDP of 65% in 1999.

Polish authorities took into account that public investment can not be replaced by private ones and European money can not replace reforms. "In Poland, economic growth was not brought by European money (only by European money - we say), but the reforms that we made" -says the Polish prime minister. He also adds: "If you want to analyze the success of an economy you have to look carefully at small companies. At the same time one must pay attention to the education system and if job offer corresponds with the market demands".

Poland is the star of the region in terms of absorption of European funds. This is because it has a division that provides administrative regions with autonomy, well trained staff and administrative structures immune to the changes of the government. Poland has benefited in the period 2004-2006 of European funding of about 6 billion Euros, over passing the Czech Republic and Slovakia.

In the first two years of EU membership, Poland co-financed more than 75,000 economic projects, which led to a significant improvement in the labour market by creating new jobs.

In this process, the municipalities, as local authorities were the promoters of European funds, benefiting from the basic infrastructure.

For the period 2007-2013, operational programs were built so that the activities undertaken to complement one another, i.e. between the operational programs at national and regional level be a real convergence, allowing full absorption of EU funds and thus growth. In this period they were invested over 100 billion Euros, of which 68 billion European funds. They have resulted in: 600 km of railways; highways, massive investments in education, IT, health.

Polish state protects strategic sectors of the economy, no longer agreeing participations to the greatest state companies - leaving the neoliberal policy so far. In 1997, Poland listed on the Warsaw Stock Exchange the KGHM Company – the largest copper mining company in the segment and the third in the sector of Europe silver (about 18,000 employees). Currently the company is controlled by the Polish government in percentage of 31.7%. In 2010, it earned a record profit of 1.18 billion Euros, compared with one in 1999 almost nonexistent. This fact demonstrates that the government can control a company, owning less than 50% of the equity and respecting the rights of minority shareholders.

This example highlights a grim reality existence, especially in Romania, namely that the privatization of state enterprises was not absolutely necessary - as the IMF argued - in the process of economic reforms.

More important was the **quality of privatizations**. In most of times, the speed of privatization, accompanied by bad faith and personal interests – sacrificed the quality of privatization.

Hungary also passed through economic and social agony during 1990-1994 when it lost 70% of sales markets in the East, more than 800,000 jobs were abolished, and Russian oil and gas have ceased to be "sponsored". 12% average unemployment, high inflation, devaluation of the forint, price increases – all these also made the transition very difficult in Hungary.

Although in the early years after 1990 it has invested over \$ 70 billion (FDI) -Hungary was suffocated by foreign debt, which in 1989 was of \$ 10 billion. In 1995 it was introduced the **austerity program**, the budget deficit was reduced and was temporarily dropped the financial assistance of the IMF. Government's privatization program was completed in 1998, but foreigners controlled 70% of financial institutions, 66% of industry, 90% in telecommunications, 50% of trade.

In 2008, a new government loan of 25 billion dollars from the IMF to restore investor confidence proved not to be auspicious. Consumption has fallen sharply, unemployment increased, the currency was devalued. In 2012 Hungary was suffocated by a foreign debt of 187 billion, representing 115% of GDP.

After eight years, Viktor Orban comes back in 2010, to the leadership of Hungary being considered an "Hugo Chavez of Central Europe". He accused EU that it would be an "empire of bureaucrats" and criticized the IMF and the US. With a majority of two thirds in Parliament, he decided to return to the advantages of regional economic development and launched in 2010 the doctrine of "**opening to the East**" - Russia, the former socialist countries, Central Asia and China.

Since 2006 it was created a Hungary-Russia intergovernmental commission for trade and economic cooperation. The trade exchanges with Russia have reached over 11 billion of dollars in 2012.

Ireland, Portugal, Hungary, Greece drew alarm signals that the European Union is not a "zone of wealth" for everyone. Less developed countries will not be able to keep up with the Western European hard core, which crystallized in a half-century of "economic symbiosis" with American support.

In the Czech Republic, in the first years after 1990, the banking sector has experienced strong expansion. Besides the five state banks, drawn from the Central Bank, many private banks were created as a result of permissive regime for obtaining licenses. Since banks were also shareholders of the companies they have granted loans without sufficient guarantees. At the same time, banks have become the managers of the privatization funds. This situation has generated a crisis of the banking system amplified by the competition of foreign banks and their subsidiaries.

In 1996, it switched to a stabilization program banks (some were closed, others were withdrew license) providing a volume of assets of \$ 1 billion. They took over nonperforming loans at nominal value by one-bank Ceska Finnci- which obliges itself to recover the bulk of loans from businesses deadbeats. But we managed not only in a small percentage of loss (of 38% of GDP) recovered from the state budget.

However, it is worth noting that throughout the transition period (1992-1997) bank deposits were completely designated (about 70% of GDP) for lending the economy- being the highest in Central and Eastern Europe. Even if a quarter of the volume of these loans was extended to state companies, their situation was not as desperate as in the case of Bulgaria or Romania, where a large proportion of these assets have never been recovered.

In 1994, it was listed on the Prague and Warsaw stock exchange the largest state company in Central and Eastern Europe – CEZ - when the government sold a minority stake, through a mass privatization program. Czech government today still holds 69% of share capital.

But the Czech government was focused on selecting a powerful and independent management, which was properly stimulated to increase the company's value on the market. The company has evolved from a net profit of 116.4 million Euros (in 1999), at 1.87 billion Euros (in 2010) - the absolute record. CEZ has adopted a strategy of regional expansion, becoming one of the largest utility companies operating in Central and Eastern Europe, with a strong presence in Romania.

The program of mass privatization in Bulgaria was implemented in the period 1996-1997, being inspired from the program in the Czech Republic, but it also had its own components that have allowed learning from the failures of others.

For example, Bulgarians have noticed that in Czech Republic mutual funds were created by privatization and established institutions to deal with these funds, before launching mass privatization program.

In mass-privatization in Bulgaria-was made by buying state enterprises by the employees and their managers. This method proved ineffective due to lack of availability among future shareholders.

In July 1997, the Bulgarian economy is on the brink of bankruptcy because the socialist government of that time **stopped practical reform process and passed to subsidize massive state sector**, which attracted huge budget deficits. Budget appropriations granted by the Central bank to increase salaries led to unbearable inflationary pressures and huge budget deficits.

At the recommendation of the IMF, the authorities accept a monetary council that would halt the worsening situation. We mention that the main reasons for the establishment of a Monetary Council in a country there are necessary:

- Limited access to international financial markets;
- The lack of government credibility;
- Crisis of domestic financial resources.

The Monetary Council that has acted in similar situations in Latin America and the Baltic countries withdraws to the Central Bank all the responsibilities in controlling over the money supply and sets an exchange rate of national currency against the German currency. It also, do not leave any leeway for the government to control wages and prices.

Finally, the Monetary Council had only a semi success. It **was a necessary, but not sufficient, condition for economic recovery**. This fact has proven that **the real issue is not primarily economic or monetary**, but real shortcomings related to poor management of the country, budget resources, ineffective public institutions, and government's inability to secure a viable strategy and communist mentality which still longer manifested both in Bulgaria and in Romania. Not coincidentally we are at the tail of Europe.

And even **WE DO NOT DESERVE** this place!

The excess of legislation, completed with the high level of taxation and bureaucracy - are the elements that form a **vicious circle** indestructible and extremely harmful to the functioning of the market economy.

Moreover, the **exercise of government coercion** (through taxation) diminishes profits and deters investors. Moreover, the **distortion of competition** by imposing rules that serves the interests of some at the expense of decreasing property of others, causing economic instability and decline in the market competitive game.

Economic sciences demonstrate that social order is not compatible with the coercive power of the state. **Market must be free!**

In society, freedom means the legitimate right of every person on its properties. In the **economy**, freedom means respect for property.

Conclusions

Finally, I will quote the words of a former prime minister novel "The state policies came to be dictated by international creditors of Romania. Everything is imposed from outside. IMF comes with budget constraints, of salary nature. Following the advice of Western institutions, the state has lost sight of national competitive industries that have disappeared since the 1990s".

Supplementary recommended readings

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