25 Years of Transition in Post-Communist Europe – Successes and Disappointments

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Guest speakers Bikas Joshi, the Head of the Resident Representative Office of the IMF in Moscow and James Roaf, Senior Resident Representative heading the IMF's Regional Office for Central and Eastern Europe in Warsaw presented highlights from their IMF report on the transitions and reforms that took place after the fall of the Berlin Wall in post-communist European countries. Zsolt Darvas, Senior Fellow at Bruegel, then presented a supplement to the report.

Bikas Joshi started with an outline of the general trajectory taken by the transition countries over the past 25 years. 1989-93 saw a fall in output from the initial dislocation, followed by higher growth rates through the rest of the 90s for countries that adopted bolder reforms. 2000-2007 brought an unmitigated boom from capital inflows with average growth at 6%, accompanied by growing imbalances due to heavy borrowing for consumption and construction industries. These imbalances, combined with the global financial crisis, caused large output declines in 2007-2009, especially in the Baltics. The region is now seeing recovery and growth, but not as high as in the mid-2000s.

Joshi noted that one of the first challenges faced by authorities in the transition was reigning in high inflation that came with the departure from centrally controlled prices. Institutions necessary to control inflation, such as independent central banks, did not exist, and part of the IMF's role was to provide programs that would establish central banking rules and generally address capacity needs.

Another early task was determining whether to drop the ruble for a national currency and what to use for a nominal anchor. Joshi noted that there was a variety of experimentation both across countries and within, as different approaches were tested. There was slow appreciation in real exchange rates across countries until the crisis, while those that chose floating rates saw higher magnitude fluctuations in times of booms and busts. He also suggested that joining the Euro Area has been a natural exit from hard pegs for some countries.

In general, Joshi remarked, those that adopted fast reforms, such as the Baltics and Central European countries, saw greater benefits compared to CIS countries and non-EU Southeast European countries. Easy reforms included the liberalization of prices, trade regimes, and the privatization of small enterprises, while hard reforms involved institutional changes such as implementing large scale privatization (which was not a choice for most countries).

Roaf spoke about the impact of greater integration with Western Europe since the 2000s. 10 transition countries since 2000 have been admitted to the EU, and accession has brought with it EU funding, institutional and legal developments, and greater liberalization. Roaf noted that increased trade flows have been an unambiguous benefit (although more so for export oriented countries). Furthermore these connections are mainly with Western Europe and Russia, while inter-region flows are small. The increase in capital flows, however, was accompanied by unsustainable lending booms into consumption, retail and real estate, and consequently, large current account deficits. Roaf also pointed out that the CE and Baltic countries that implemented rapid reforms are now closer to the EU15 countries than former comecon (Council for Mutual Economic Assistance) partners in terms of indicators associated with a country's state of development.

Darvas then showed that in terms of GDP per capita (as a percentage of EU10) going back to 1980, half the transition countries are lower or at the same relative level as they were in 1989 (although concerns about the reliability of the early data were raised). Furthermore, in comparing the growth of GDP per inhabitant in countries relative to their capital, Darvas suggested that certain regions have been left behind compared to the capitals and inequality has increased. He also noted that trust in the EU (as measured by the Eurobarometer survey) declined heavily during the crisis and is still somewhat lower than in 2004, possibly suggesting that transition countries' expectations have not been met.

Event notes by Allison Mandra