PART ONE

The Challenge of Transition

COUNTRIES EMBARKED ON TRANSITION FROM VERY different starting points. This part of the Report first considers the patterns and progress of reform, broad outcomes, and the influence of country-specific factors relative to the choice of policies (Chapter 1). The core reforms in transition include liberalizing prices, markets, and new business entry, and implementing programs to regain or preserve price stability. But countries cannot ignore their history and geography, and this legacy, together with political developments, profoundly affects both the relative importance of different market reforms and how policymakers approach them.

Liberalization and stabilization are closely interrelated (Chapter 2). The freeing of markets is the basic enabling reform from which all the potential benefits of transition flow. But market price signals cannot do their work in an environment of
severe macroeconomic imbalances and high inflation. Stabilization is thus a vital complement to liberalization in fostering productivity and growth during transition—and beyond.

Creating property rights and incentives and a mostly private economy is a second challenge (Chapter 3). Here, too, initial conditions matter. Some transition countries will have a much more urgent need to privatize than others. But there can be competing objectives and difficulties in creating an effective and popular program.

A third major challenge—vital for social and political as well as economic reasons—is to relieve poverty and address the other ill effects of transition on particular groups (Chapter 4). Many gain from transition, and depending again on the starting point and context for reforms, transition can be accompanied by declining poverty from day one. But the vast adjustments involved in a change of economic system can also have adverse implications for many. The losses they suffer need to be addressed through effective social policies and measures that encourage sustained growth.