

# MONITORING COUNTRY PROGRESS

## *I. Introduction*

The objective of U.S. assistance to Central and Eastern Europe (CEE) and to the Eurasian countries of the former Soviet Union is to help move these countries far enough along the road to becoming market-based democracies that they can complete the journey themselves. Early expectations were that the duration of assistance to the region would be brief. After ten plus years, while there are many successes, particularly in the Northern Tier CEE countries, remaining transition challenges are formidable and fluid. The collapse of the Russian financial system in August of 1998, for example, underscored the complexity of the transition task, and ongoing conflicts in the Balkans demonstrate how fragile stability can be in this post-Cold War period.

These challenges make it all the more essential to closely monitor both the impact of the U.S. assistance programs themselves to maximize their effectiveness, as well as the progress of the countries more generally to determine whether continued assistance is necessary or justified. Program impact monitoring is done by both field missions and Washington-based operating units through a system of setting results targets and annually monitoring progress toward them, and through less frequent special field evaluations. This paper presents USAID/E&E's system for monitoring country progress in twenty-seven countries of the region.<sup>1</sup>

Country progress monitoring is done in part to determine whether the assistance program can be terminated either because: (a) the country is well launched on its way to a successful transition and cessation of assistance will no longer jeopardize that transition (i.e., graduation); or (b) the country is making so little progress that significant resources will have little impact. Monitoring is done annually and results are shared with the State Department Coordinators for U.S. assistance to each of the two regions.

*Section II* below highlights the methodology. This is followed in *Section III* by analyses in each of the major areas examined: (a) economic policy reforms; (b) democratization; (c) macroeconomic performance; and (d) social conditions. *Section IV* briefly concludes. *Appendix I* elaborates on the rating schemes of the economic policy reform and democratization indicators.

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<sup>1</sup> While USAID programs are largely complete in the Northern Tier CEE region, monitoring country progress among the USAID "graduates" provides a basis for comparison with the remaining transition countries, and enables us to track possible backsliding among the leaders as well.

## ***II. Methodology***

Market-oriented reforms and democratization have been the two pillars of USAID's program in the transition countries.<sup>2</sup> This has been combined with a more recent and growing focus on social aspects of the transition.<sup>3</sup> The primary challenge of this analysis thus is essentially to assess the progress across these fronts, with a particular focus on the sustainability of reforms.

Country progress is analyzed in a sequence of steps drawing from standard, well-established data sources that are external to USAID. First, we look at the progress towards economic reforms and democratization. Progress on both fronts must reach a certain threshold before we can begin to consider graduation.

Economic policy reforms are assessed by drawing from EBRD's annual rating scheme of transition indicators, and supplemented by a similar scheme from Freedom House.<sup>4</sup> Progress in democratic freedoms is determined from Freedom House's annual worldwide rating of civil liberties and political rights, and from an effort on its part to further disaggregate and better target the measurement of such freedoms in the transition region.<sup>5</sup>

Next, we look at indications of sustainability. Economic reforms need to translate into solid macroeconomic performance. We might expect improved performance to follow reform implementation with some lag. In time, however, evidence of good macroeconomic performance would give us more confidence that the reformed economy is on a sustainable path.

Furthermore, it is important to underscore that acceptable progress in the reforms must precede good macroeconomic performance. A cross-country snapshot might show one economy outperforming another in part because painful reforms have been avoided in the former. Yet, this is hardly sustainable.

The macroeconomic performance indicators also provide a check on the comprehensiveness of the economic reform indicators. For example, fiscal reform is not adequately addressed in the current mix of economic reform indicators. Yet, insufficient fiscal reform is likely to surface in the form of rising fiscal deficits, and this *is* being tracked as an economic performance indicator.

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<sup>2</sup> USAID assistance to the transition countries is funded through the Support for East European Democracy Act (SEED) and the Freedom Support Act (FSA), the latter applying to the Eurasian countries. The SEED Act has two goals: the promotion of democracy and a market-oriented economy. The FSA objectives are broader in scope, including the transition goals of the SEED Act as well as those focused more directly on humanitarian, social, environmental, and trade and investment conditions.

<sup>3</sup> See USAID/E&E, *From Transition to Partnership: A Strategic Framework for USAID Programs in Europe and Eurasia* (December 1999); and the E&E Bureau's social transition strategy: USAID/E&E, *Transition With a Human Face: Broadening the Benefits of Economic and Political Reform in Central and Eastern Europe and the New Independent States* (August 1999).

<sup>4</sup> See EBRD, *Transition Report 2000* (November 2000), and Freedom House, *Nations in Transit 2001* (forthcoming).

<sup>5</sup> See Freedom House, *Freedom in the World 2000-2001* (May 2001), and *Nations in Transit 2001* (forthcoming).

Another means to measure the sustainability of reforms is to assess trends in the quality of living conditions. This is largely addressing the concern of “reform fatigue.” It is not enough to have a healthy economy and significant political freedoms if households continue to struggle and living conditions deteriorate. In this scenario, support for reforms also deteriorates. So, too, eventually does human capital and, from that, the productive capacity of the economy.

Country progress is assessed throughout this report with population-weighted measures of progress of three subregions among the transition economies as well as with comparators outside the region. The Northern Tier Central and Eastern Europe (CEE) subregion consists of Poland, Hungary, Slovenia, the Czech Republic, Slovakia, Estonia, Latvia, and Lithuania; the Southern Tier CEE countries consist of Romania, Bulgaria, Croatia, the FYR Macedonia, Albania, Bosnia-Herzegovina, and Yugoslavia; and the Eurasian states consist of the countries formed from the dissolution of Soviet Union less Latvia, Lithuania, and Estonia.

For many indicators, proposed graduation benchmarks are assigned. Some are more arbitrary than others and need to be held to debate. Should a country fail to meet a benchmark, this should signal a “yellow flag” in the mind of the analyst; an aspect that may need to be examined more thoroughly if graduation is being considered on the basis of other evidence. The number of benchmarks a country needs to achieve should vary according to context.

An important step of the process is the holding of annual reviews—alternating the focus between the CEE and Eurasian countries—with area specialists from U.S. government agencies. Soliciting such expert opinion serves as a reality check on the data and our interpretation of it.

Finally, it merits explicitly recognizing that what is occurring in the region is unprecedented, and that there is little if any theoretical and/or empirical basis for devising precise thresholds of reform sustainability. Further, it is reasonable to assume that there is more than one acceptable transition route, or, what may amount to the same, many possible varieties of sustainable market-oriented democracies. This exercise, in short, is likely to be as much art as it is science, and it is important to place the results in this context.