

# Towards a Market Economy

*From the reviewing stand in Moscow's Red Square, visitors can now gaze across the cobblestones, where Soviet tanks and missiles once rumbled by during the Cold War, and see a new row of privately-owned shops. The once-sleepy downtown of Vilnius, Lithuania, is bustling with commercial activity. In Sofia, Bulgaria, young stockbrokers are making trades on the new stock exchange, where listings went from one company to 31 in its first year.*

*From Poland and Slovenia in the west, to Kazakhstan and Russian Siberia in the east, the economic changes in Central and Eastern Europe and Eurasia during the 1990s were profound and, in some cases, astonishing. In 1989, the state controlled almost every aspect of economic activity—bureaucrats set prices, established production quotas for factories and farms, decided which companies got credit and how much, and determined wages and working conditions.*

*Governments owned not only utilities and public transportation, but almost*

*every other economic enterprise as well. Private businesses were banned or severely limited. The region was filled with factories employing thousands of workers they didn't need, to produce shoddy goods that no one wanted. For years, the whole system was propped up by subsidies and noncommercial trading relationships and sustained by wasteful use of energy that polluted the land, air and water.*

*That system crumbled when the Berlin Wall fell and the Soviet Union imploded. Today, the countries of the region are moving—some quickly, and some far too slowly—toward open, market-driven economies. Prices have been freed. State-owned enterprises have been sold to private owners. New economic institutions are leading to improved economic policies and management. A commercial law framework is being put in place and enforced. Sound banking systems and practices are beginning to emerge. Commercial lending to productive private enterprises is growing. Governments are encouraging small and medium enterprises by reducing red tape and improving their tax policies.*

## USAID Programs

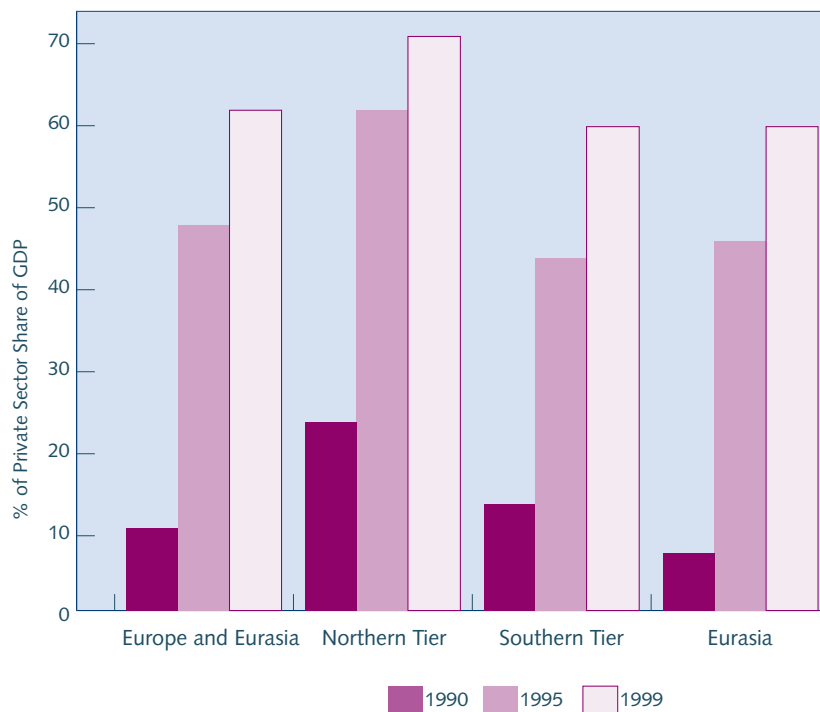
- *Privatization*
- *Fiscal Policy Reform*
- *Financial Sector Reform*
- *New Enterprises*
- *Energy & Environment*

*In the 1990s, USAID supported and accelerated these dramatic changes through the transfer of expertise, best practices and experience. In so doing, USAID built lasting partnerships with the men and women of the region who took the risks and did the hard work needed to transform their countries from old to new economies.*

## FOUNDATIONS FOR A NEW SYSTEM

*Creating a private sector in a former command economy starts with transferring state-owned enterprises into private hands and encouraging the growth of new businesses. For the private sector to succeed, however, a series of changes are required. Laws must be clearly written and fairly enforced by a competent judiciary. Burdensome regulations must be eliminated and competition fostered. Fiscal systems must be reformed to reduce budget deficits and encourage investment. Private businesses need uniform accounting systems in order to prepare financial statements which shareholders and banks can understand. Citizens must gain confidence in financial institutions to promote savings and productive lending. And, good macroeconomic policies and management practices must be adopted to promote non-inflationary growth. During the 1990s, USAID helped transfer thousands of state-owned businesses, farms and housing into private hands. Voucher programs gave many citizens the opportunity to become shareholders of privatized companies. To encourage private sector expansion, USAID supported new legal frameworks, better-functioning government ministries, new tax codes and budget systems, sound financial institutions and professional associations.*

*Statistics for the region are impressive. Twenty-three of the 27 countries have either completed the privatization of state-owned enterprises or have privatization programs well under way. Private enterprises in nine countries have adopted international accounting and auditing standards and two regional federations are promoting the acceptance of such standards in member countries. Modern banking systems have been developed in 21 countries. Fiscal reform, has improved tax collection in 13 countries, and seven have cut their budget deficits to below three percent of GDP.*



Source: EBRD Transition Report (1999)

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### *'The land belongs to me'*

In the former Soviet Union, agriculture was dominated by huge collective farms, where farmers worked as employees of the state. USAID helped Moldova's government break up these collectives, transforming them into smaller farms owned by the people who once labored on the massive, state-owned farms. Eighty-nine percent of the former collective farms were broken up, and today, 730,000 Moldovan farmers are the proud owners of two million individual land parcels. The success of this program was replicated by USAID in Georgia, where all the collective farms are now gone. USAID followed up by helping to register some one million agricultur-

al land parcels, prompting one Georgian land owner to remark, “From now on the land belongs to me. I have five children and six grandchildren. They work the land, and it will provide for us now.”

### Best Accountant of the Year

Ms. Valentina Bezhina, who lives in Kazakhstan’s large industrial Karaganda region, works for the Mediton Corp. In 1999, Mediton attempted to convert its accounting systems to new market-oriented standards, but lacked training or technical support. After this conversion attempt failed, Ms. Bezhina took USAID-sponsored training in financial

“Only private property can turn ‘agricultural workers’ brought up in a communist spirit into farmers like our ancestors used to be, with their careful attitude toward land, agricultural equipment, and quality work...”

— Nicolae Jechiu, Director  
Colnarg-Agro Limited Liability Company, Moldova

and managerial accounting. Soon after, she began to provide numerous useful ideas that improved Mediton’s financial performance, making her a key part of her company’s decision-making process. She became a consultant to several companies, and she won Kazakhstan’s national

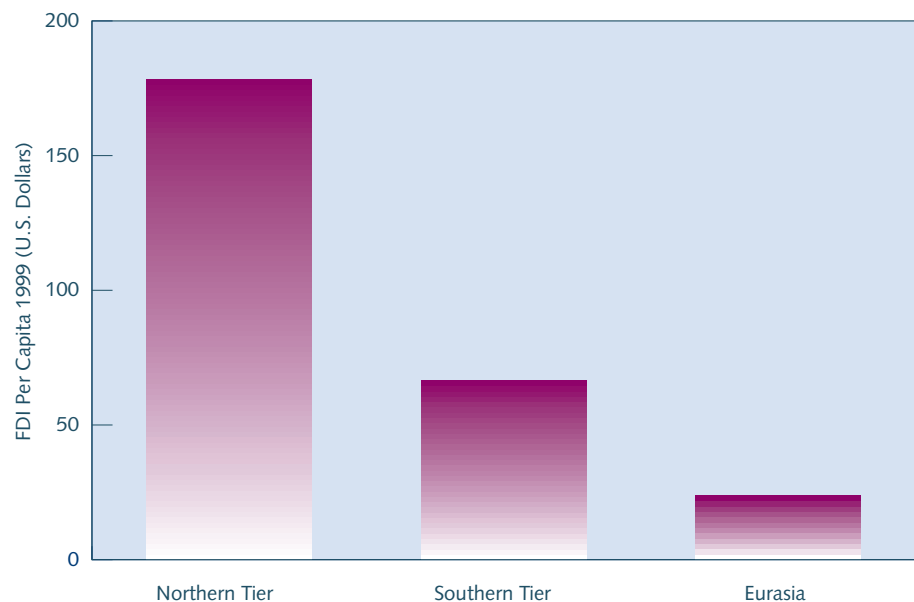
competition for Best Accountant of the Year. USAID efforts to reform accounting in Central Asia have not only had a positive impact on economic development, but have improved the quality and dignity of the lives of thousands of people like Valentina Bezhina.



Ms. Bezhina wins national accounting competition in Kazakhstan.

### Economic Reform Attracts Foreign Investment

On average, the countries that have advanced the most in economic reform have attracted the highest rates of foreign direct investment.



Source: EBRD Transition Report (1999)

## *Restoring Confidence in Latvia's Banks*

In early 1995, Latvia's largest bank collapsed, leading to political and economic turmoil and eroding public confidence in the banks and the government. Within days, USAID-funded banking experts provided assistance to design and set up a depositor pay-out system. This allowed for the orderly and timely repayment of over 13,000 household depositors. Over the longer term, these experts helped the Central Bank establish a bank supervision

system based on international standards and provided practical assistance to upgrade the on-site inspections of the remaining banks. USAID also helped enact regulations that tightened bank risk management and put in place a complete training process for bank examiners. Numerous risky banks lost their licenses. Bad loans dropped significantly. By 1998, Latvia's banks were on the right track. Foreign banks were investing in the banking system, a sure sign of progress. Public confidence returned, with deposits by individuals and companies rising 85 percent between 1995 and 1998.

The Northern Tier countries, which introduced the most wide ranging economic reforms, enjoyed a high average annual growth rate of 5 percent between 1996 and 1998.

## *Stopping a Phony Share Sale*

In April 2000, the management of Ukraine's Stinol Chemicals Plant told the company's minority shareholders that management wanted to issue new shares worth 10 percent of the company's stock price to raise new capital to buy plant equipment. But the move was really a ploy to increase management ownership of the company. The new shares were on sale for only 24 hours, on a first-come, first-served basis and could be purchased only on the premises of the chemical plant. Management grabbed all the shares. The minority shareholders turned to Ukraine's Securities and Stock Market State Commission, a regulatory body set up with USAID assistance. The commission canceled the phony share sale, denounced it as a violation of minority shareholder rights and declared that the law required minority shareholders to have a fair chance to buy into new stock offerings. Shareholder rights were protected thanks to USAID-supported development of new laws and institutions that ensure the proper functioning of securities markets and increase public awareness and investor understanding. Effective protection of shareholder rights is a basic building block of private economic growth.



U.S. Securities and Exchange Commission

Security exchange professionals from Eurasia complete regional training seminar on financial market operations, regulation, and oversight. Over 12,000 financial sector professionals have been trained in Eurasia.



## HELPING ENTREPRENEURS

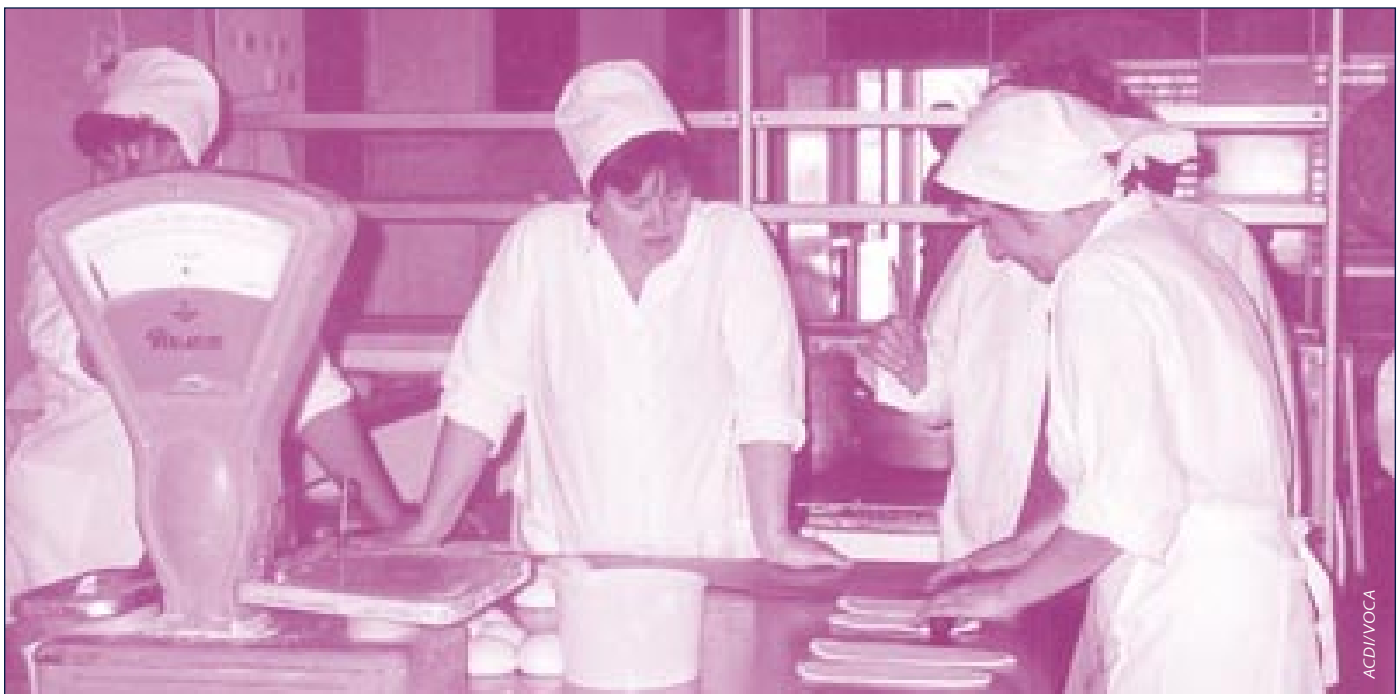
*The collapse of authoritarian rule left most citizens unprepared to operate in a private, market economy. After so many years of state control, it was hard to find people in the region who knew much about starting a business, managing a banking system, investing in a company, figuring out profit and loss, or any of the other basics of a market-based economy. The countries were short on cash as well as knowledge; almost all needed outside investments to get their economies back on their feet. Throughout the decade, USAID helped people who wanted to become entrepreneurs gain the financing, training, new technologies, expertise and experience they needed to build vibrant growing businesses, the cornerstone of a strong market economy.*

### *Twelve Hundred Loaves a Day*

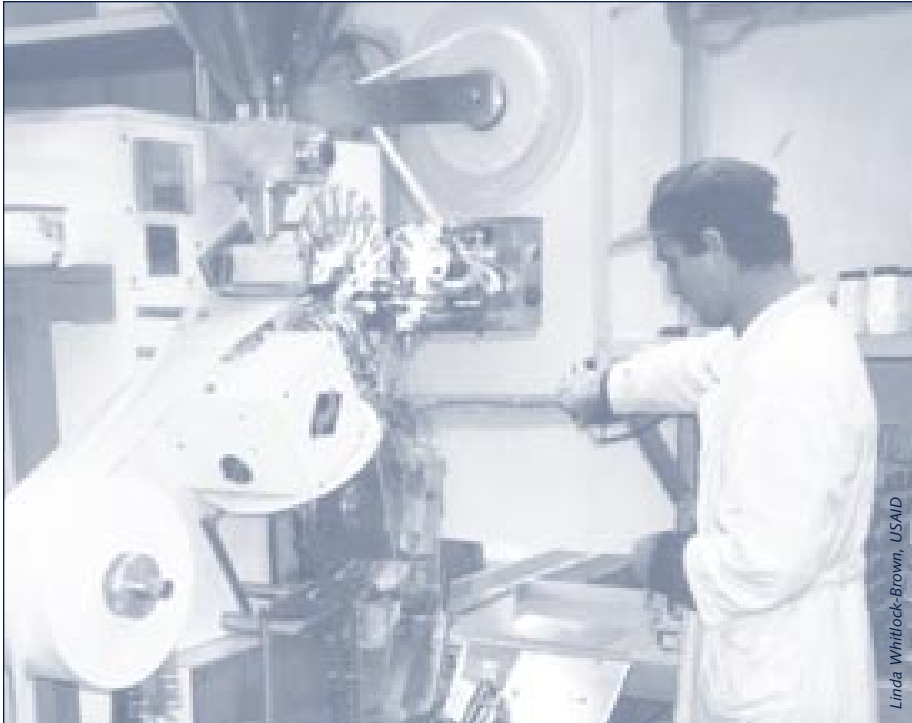
When the Communist system collapsed, Lidiya Tsukrenko's family almost did too. Ms. Tsukrenko, who lives in the little town of Vepryk, Ukraine, about 50 miles south of Kiev, lost her income when the government-owned company she worked

for couldn't make payroll. To earn the cash the family needed, Ms. Tsukrenko got financing from a local source, bought used equipment and started the VITA Bakery in 1995, milling flour in the barn of her small farm and baking bread in her kitchen. She was soon making 300 loaves of bread a day, but realized she had to expand to survive. In 1997, Ms.

Tsukrenko applied for a \$12,000 loan from a USAID-financed loan company. That loan helped her buy a larger flour mill. Before long, she had more than doubled her production of flour and boosted her bread production to 1,200 loaves per day. The bakery now employs 10 people, and Ms. Tsukrenko has never missed a loan payment.



U.S. volunteers help small entrepreneurs, such as these Eastern European bakers, expand marketability of goods through management and production improvements.



Linda Whitlock-Brown, USAID

Small herbal tea business in the Russia Far East purchases new equipment with grants available for non-traditional timber products

*Since 1989, ten Enterprise Funds supported by USAID have invested \$900 million in 16 countries, helping to preserve or create 150,000 jobs.*

### *The 'Dream' Bank*

While Kyrgyzstan's bazaars look colorful and inviting, they can be a hard place to make a living. In 1996, Ryla Primvirdieva began selling rice in the bazaar of Osh, a small market city. At first, she earned a profit of just \$2 per day, barely enough to buy bread and tea for herself and the two young daughters and daughter-in-law she

was supporting. Then she heard about the FINCA Village Banking program. Financed through USAID, the program helps women like Ms. Primvirdieva with small loans, as well as training, advice and a savings program.

Ms. Primvirdieva seized the opportunity, and with 11 other women she organized a village bank called Kyigal ('Dream'). Her first loan allowed her to buy one to two sacks of rice each week, doubling her profits. She qualified for a second FINCA loan of \$57, plus \$25 borrowed from the bank members' collective savings. The new financing has allowed her to increase her inventory again, boosting her daily profit to \$6. She now has savings, and her additional income allows her to purchase luxuries she could not afford only a few months earlier—butter, sugar and meat.

### *Sewing Success*

As she worked at the state sewing factory in Khabarovsk in the Russian Far East, Olga Asmolina dreamed of owning her own dress shop. When private businesses began to sprout up, she realized she had a golden opportunity. She started by renting a small room with sewing machines. In 1998, Ms. Asmolina decided that she would need a loan to survive and grow. She went to Working Capital Russia, a USAID-sponsored program to help new businesses, and received a \$1,000 loan. Soon she had enough business to hire nine employees, including two of the town's best tailors. When the financial crisis hit Russia in August 1998, Ms. Asmolina had to reschedule her payments, but she managed to pay off the loan by the end of the year. She now has three tailors working for her, has added a fashion salon and fitting room, and has upgraded her equipment and product line. Her dream is a reality.

### *Support Services Reach Entrepreneurs*

USAID has helped small and medium-sized businesses across the region grow and develop. In Bulgaria, for instance, a consortium of USAID-funded organizations has trained more than 10,000 entrepreneurs and created or saved over 14,000 jobs. Nine Business Service Centers in Ukraine and Moldova have reached over 35,000 entrepreneurs. Thirty-five percent of those clients have been women.

## *Volunteering to Help*

When Mitch Kam, a 33-year-old American volunteer with the MBA Enterprise Corps, arrived in Kielce, Poland, in 1994, he knew he had his work cut out for him. Revenues at the Piasecki Company, a 300-person, family-owned construction company, were declining. Mr. Kam stayed a year, advising senior management on marketing, management, strategic planning, finance and organizational design issues. By 2000, Piasecki had grown to more than 800 employees with annual revenues of more than \$60 million, making it the seventh-largest general contractor in Poland. Piasecki now is traded on the Warsaw Stock Exchange.

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*A USAID-supported NGO set up micro-loan institutions that created over 40,000 jobs in the region. More than half the loans have gone to women.*

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## *The Dairy Improvement Campaign*

In Albania, USAID has worked with Land O'Lakes, Inc., to aid rural women, who are traditionally in charge of the family cows. USAID and Land O'Lakes teamed to create the Dairy Improvement Campaign, which helps women learn how to produce more and better cow's milk. The campaign provided information and training on cow nutrition, disease prevention, reproduction and sanitation. As a result, women are earning more money and

## *World Trade Organization (WTO) Membership*

Becoming a member of the WTO lowers barriers to trade and provides increased opportunity for economic growth through exports. WTO membership indicates that a country's trade and investment laws encourage foreign investment and promote domestic entrepreneurs. To date, USAID programs have helped 11 countries achieve full membership: Czech Republic, Hungary, Romania, Slovakia, Poland, Slovenia, Bulgaria, Kyrgyzstan, Estonia, Latvia, and Georgia.



Albanian women learn new milk filtering techniques

enjoying higher status. In addition to the economic and food security impacts of the campaign, other organizations are using the new dairy producers' network, which

has grown to over 8,000 women, to deliver information to women on a wide range of health and social issues.

## ENERGY AND ENVIRONMENT

*One of the best kept secrets during the Soviet era was the environmental toll of decades of authoritarian rule: rivers and lakes fouled by industrial plant runoff and raw sewage, poisoned soil, polluted air and the threat of exposure to nuclear waste. Much of the damage was caused by the inefficient production and wasteful use of energy, encouraged by the lack of economic value placed on natural resources. Poorly managed energy monopolies as well as artificially low prices set by government contributed to pollution. The damage was compounded by government indifference and suppression of public opinion. The green movements in the countries of Central and Eastern Europe during the 1980s were among the first attempts at citizen participation. USAID built on this momentum and supported new government agencies and private groups working to raise public awareness about the environment, address existing environmental “hot spots,” and reduce the possibility of additional environmental damage. As part of a U.S. Government team, USAID has worked tirelessly to promote nuclear safety in the region. USAID has improved energy efficiency through restructuring, commercialization and privatization of the energy sector and the development of appropriate regulatory oversight for these new market-oriented systems.*

### *Metering Natural Gas for Conservation*

During the Soviet period, the price of natural gas was kept so artificially low that Russians joked it was cheaper to leave a gas stove on all the time than to waste matches lighting it. The result, of course, was that huge amounts of natural gas were wasted. Although the wholesale price of gas rose after 1991, consumers did not conserve, mainly because most Russian apartments do

not have individual gas meters. A USAID program that links a U.S. utility and Russian counterpart is helping to change that. Vladmiroblgaz and Brooklyn Union Gas have conducted a pilot residential metering project designed to determine how best to improve revenue collection and conserve energy. With USAID financing, 500 meters were purchased and installed in apartments just east of Moscow. Natural gas consumption dropped dramatically. Since then, the pilot

program has been expanded. The Vladmiroblgaz-Brooklyn Union Gas program and others like it are now helping conserve natural resources in cities across Russia.

### *The New Energy Regulators*

Breaking apart old energy monopolies and replacing them with market-oriented systems required a new approach to regulation and oversight in the energy sector. In addressing this challenge, USAID has supported the creation of independent energy regulatory bodies in 14 countries. These new entities operate according to modern and transparent regulatory practices, including increased public participation and less political interference. With help from USAID, the new regulators have developed a regional network to discuss common concerns and link to the U.S. regulatory community.



Representatives from Kyivenergo, a local utilities company in Ukraine, discuss safety performance issues with their U.S. partners at the PP&L, Inc. power plant in Allentown, PA.



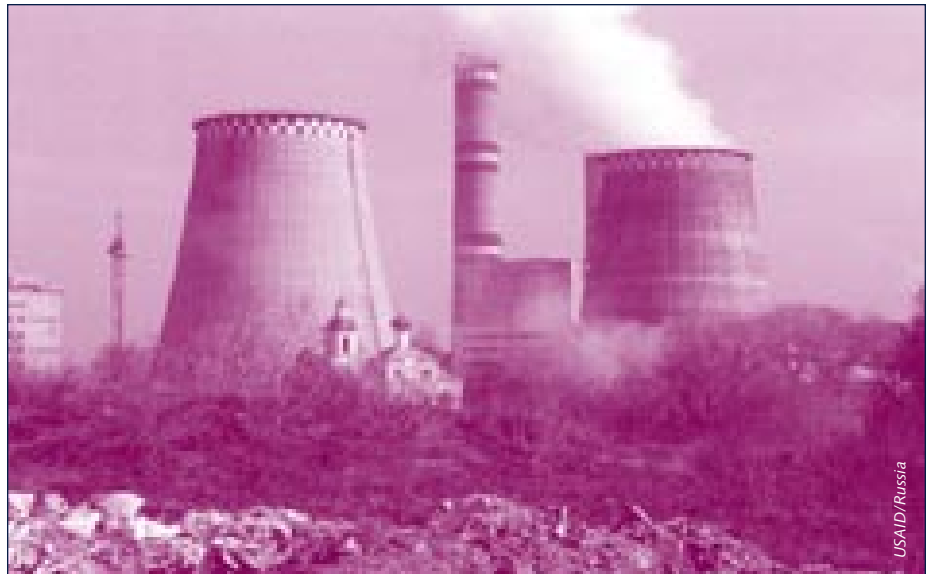
## *Improved Environmental Management*

Citizen organizations were among the first to call attention to environmental issues in the region. By joining forces with independent media these groups became a strong voice for change. Citizen advocacy combined with USAID technical assistance has helped the development and adoption of new laws and policies in resource management. Sound environmental frameworks are now in place in many countries, including Estonia, Hungary, Poland, Romania, and Slovakia. Groundbreaking forestry codes have been adopted in Russia. The Czech Republic and Poland have produced unprecedented levels of investments in environmental improvements.

## *New Technologies to Treat Wastewater*

A high-tech Hungarian environmental engineering firm plans to float a revolutionary new wastewater treatment plant on the Danube River in 2001, thanks to USAID's environmental partnership program, EcoLinks. Managed by the Institute of International Education, this program helps businesses and municipalities develop market-based solutions to environmental problems. The Hungarian firm, Organica Ecotechnologies, received the first EcoLinks Quick Response Award of \$5,000 and used it to visit an environmental company in Vermont, Ocean Arks International, which had developed a system to use biological technology to treat wastewater.

After the U.S. visit, Organica executives



The introduction of a water filtration and leakage control system in Novokuznetk, Russia, reduced pollution and saved the city money.

applied for and won a \$50,000 challenge grant from EcoLinks to prepare a feasibility study to assess the new technology. A joint venture of international investors heard about the program and decided to invest in Organica. With its new funding, Organica is planning to install its own treatment plant on a 176-foot-long barge. The floating wastewater facility will treat more than 8,800 cubic feet of raw sewage every day.

## *Promoting Nuclear Safety*

The devastating explosion at the Chernobyl nuclear power plant in Ukraine, in 1986, released high levels of radiation which eventually killed construction workers at the plant. Airborne contamination spread to parts of Europe, Eurasia, and the Middle East, causing considerable damage to soil and vegetation, natural fauna, and livestock. It exposed the local population to elevated levels of radioactivity, resulting in the evacuation of over 100,000 people from the Chernobyl area. Twelve years after the accident, significant health problems continue to

emerge, including thyroid cancers and childhood birth defects.

The imperative to avoid another Chernobyl accident has been a vital factor behind the commitment of Western leaders and the international community to address nuclear safety in the region. USAID has worked closely with the U.S. Departments of State and Energy and the National Regulatory Commission to mobilize resources from 30 countries to support safer procedures and structures at operating plants and decommission high-risk nuclear reactors. USAID has collaborated on multilateral efforts, such as the Nuclear Safety Account and the Shelter Implementation Fund at the European Bank for Reconstruction and Development. As a result of this work, commitments have been made by Ukraine, Lithuania, Bulgaria and Slovakia to close their oldest nuclear reactors. Chernobyl is scheduled to shut down by the end of 2000.