

# Overview and Assessment of Economic Reform Concepts and Programs in Belarus

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Economic reform concepts and programs developed to date are different in structure and purposes. They can be divided into three major groups:

1. Program documents from major political parties and presidential candidates;
2. Concepts and programs designed by independent economic experts; and
3. State-sponsored programs of economic reform.

## Program documents of political parties and presidential candidates

Key documents in this group include:

The Program of Reform by the Belarusian Popular Front – 1989<sup>1</sup>. This is the first program of reforms for Belarus, designed by the Belarusian Popular Front even before the breakup of the Soviet Union. Here are some of the basic provisions of this platform:

- Economic independence of Belarus from the Soviet Union's state structures, including abandonment of the centralized system for supplying industrial output to USSR-held funds and Belarus claiming its own right to national resources;

<sup>1</sup> *Сборник альтернативных программ развития Беларуси*. Под ред. В. М. Шлындикова, Мн.: Бестпринт, 2001, p. 7–46.

- Equal co-existence of different types of ownership, including private ownership; the right of employees to choose the form of ownership for (state-owned) companies they work for;
- Independence of enterprises; relations between enterprises are based on the arm's length principle, and on self-financing;
- Introduction of a planned-regulated market mechanism where government bodies issue planning recommendations, design socioeconomic development programs, ensure that various market and business competitors come into play, take measures against monopolies, assist market stabilization, make efforts aimed at reducing prices and ensuring equal conditions for development in various regions, publish regular statistical reports on inflation, living standard changes, personal income in various social groups, foreign trade, etc. The government's main way of regulating the economy is through taxes, subsidies, public procurement and financial leverage.
- Free foreign exchange market;
- Land is to be owned by local councils which lease it to businesses. A single land tax is to be launched, and the tax rate would depend on land productivity.

The program's authors propose that its implementation will resolve main socioeconomic problems, such as housing, food production and manufacturing of consumer products, and eliminate market shortages.

*Assessment:* It was a rather radical platform for the period, since it suggested transforming the socialist planned economy along the market model. The program stipulated basic market economy principles, but failed to specify a sequence of reforms.

The document asserts the country's economic sovereignty and independence of business entities, which is a reflection of the situation prevalent in late 1980s. That was when movements emerged that advocated national independence and democratic changes in the republics of the Soviet Union.

Other important reform programs are The Program of the Belarusian Popular Front<sup>2</sup> and Declaration of Goals and Principles of the United Civic Party<sup>3</sup>. Both documents date back to 1993.

As stated, these documents' main goal is building a 'social market economy' in reaction to the country's general economic instability in 1993, as manifested in high inflation, decreasing production, growing shortages of consumer goods and declining living standards. However, the documents proposed different ways of reaching the same goal.

The Belarusian Popular Front's platform set out the principles of deregulated prices, supporting competition, private ownership of land and means of production, and abolition of public procurements for farms. Much attention was paid to ensuring social justice and protecting domestic producers by means of customs barriers. The program also called for fair and gradual privatization of enterprises, and active structural policy towards savings in energy and consumables in more environmentally friendly manufacturing industries. It suggested tough state regulation of the use and privatization of agricultural land.

*Assessment:* The document expresses support for the State's active role in the economy and a gradual, 'well-considered' and 'socially equitable' process of market transformations. The main drawback of this platform is to be found in the confusion of principles: some are market-oriented, while others envisage active State interventionism in the economy.

The document developed by the United Civic Party stipulates a speedy privatization, abolition of State regulation of prices, freedom of business and comprehensive State support for the growth of private business. The authors are of the opinion that economic growth and improving living standards of various segments in the society had to be the staple tenet for the social market economy. 'If the public pie grows, everyone's share in this pie grows with it'<sup>4</sup> is the program's slogan.

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<sup>2</sup> *Ibid.*, p. 47–102.

<sup>3</sup> *Ibid.*, p. 103–112.

<sup>4</sup> *Ibid.*, p. 109.

In general, those two documents reflect the process of political parties establishing themselves on the country's political scene and, correspondingly, the polarization of public opinion on issues such as market transformations, pace of changes and the State's role in the economy.

Other documents in this repertoire are platforms of presidential candidates for 1994 elections: Alyksandr Lukashenka, Vyachaslaw Kebich, Stanislav Shushkevich, Zyanon Paznyak, Alyksandr Dubko and Vasil Novikau.

Alyksandr Lukashenka's program – called 'Taking The People Away From Disaster'<sup>5</sup> – focuses on difficulties in the country's economic situation and develops the idea of the State's responsibility for resolving economic and societal problems. The program sets out the following measures:

- stabilize prices by establishing State control over price formation, combating unsubstantiated price hikes, enforce penal liability for violations of State price policy;
- strict oversight over the economy via direct control of state-owned enterprises;
- an investment policy based on gradual increase of long-term bank lending, setting interest rates in line with State priorities, designating economic sectors and investment projects for State support;
- consolidate State control over the foreign exchange market by closing all convertible currency outflows abroad, controls over convertible currency assets of Belarusian commercial banks abroad, institute penal and administrative punishment for illegal forex transactions and illegal convertible currency exports;
- prioritize agriculture in State investments by short- and long-term lending, preserve the system of collective (*kolhoz*) and State (*sovhoz*) farms;
- designate housing construction as a priority sector for financing, in close State focus;
- support honest entrepreneurs.

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<sup>5</sup> Тезисы программы кандидата в Президенты Республики Беларусь А. Лукашенко. Отвести народ от пропасти, «Народная газета», № 109 (874) 10 чэрвеня 1994 г.

The program of Alyksandr Lukashenka's main competitor Vyachaslaw Kebich – called 'People of Belarus Should Have a Decent Life, Without Fear of Future, Be Proud of Themselves and Their Motherland!'<sup>6</sup> – points to the need for anti-inflation measures, stabilization of manufacturing output, privatization and retaining State control over key areas of the economy that impact the society, such as fuel and energy, finance, transport, communications, science, education, social welfare, environment and natural resources.

Kebich advocated keeping State control over prices of selected foodstuffs and services, and providing State support for agriculture, with collective and state-owned farms preserved. He proposed that the the president and government's role should be in managing state-owned enterprises, capex projects, subsidies, employment, etc.

In his platform entitled 'Statehood, Democracy and the Market – a Way Towards Prosperity'<sup>7</sup>, Stanislaw Shushkevich stresses that the country's economic crisis has been caused not by reforms, but by absence thereof, and proposes embarking on a firm path of reforms geared specifically to stabilize the Belarusian monetary system, towards a speedy privatization, removing obstacles to the freedom of business, alleviate the tax burden, carry out a structural reform in agriculture by giving farms a free hand in deciding on the form of ownership and type of business operation, stimulate foreign investments and provide targeted social support to the population.

Not unlike like Shushkevich's, the economic program of Zyanon Paznyak<sup>8</sup> speaks in favor of market reforms. It provides a detailed description of the mechanism for introducing Belarus' sovereign currency. A chapter is dedicated to agricultural policy and land issues. The platform allows for undertakings to be free in choosing their type of business and form of ownership, and supports

<sup>6</sup> Праграма Кебіча Вячаслава Францавіча, кандыдата ў Прэзідэнты Рэспублікі Беларусь. Народ Беларусі павінен жыць дастойна, без страху за будучыню, ганарыцца сабой і сваёй Радзімай!, «Народная газета», № 106 (871). 10 чэрвеня 1994 г.

<sup>7</sup> Тэзісы перадвыбарнай праграмы Станіслава Шушкевіча, кандыдата ў Прэзідэнты Рэспублікі Беларусь. Дзяржаўнасць, дэмакратыя, рынак – шлях да дабрабыту, «Народная газета», № 106 (871) 10 чэрвеня 1994 г.

<sup>8</sup> Эканамічная праграма кандыдата ў Прэзідэнты Зянона Пазьняка, «Народная газета», № 106 (871) 10 чэрвеня 1994 г.

private ownership of land, yet points out that ‘a well-considered and firm State policy founded on the precepts of science’<sup>9</sup> has to be pursued in implementing land privatization.

Finally, the program of Alyaksandr Dubko – ‘The Country Needs a Good Stewart’<sup>10</sup> – is even more radical than that of Alyaksandr Lukashenka in its anti-market course. Dubko is entirely against radical market reforms and entrepreneurship. He wishes to keep State ownership of land and speaks in favor of vesting the future president with absolute powers and responsibility.

*Assessment:* All the documents were prepared in times of a profound economic crisis in Belarus, with hyperinflation, decline in output (nearly halved), growing unemployment, deteriorating living standards, and lack of transparency in actions of government agencies in State property privatization. They present a wide range of views on economic reforms, from a radical market reform (Shushkevich) to extremely conservative policies (Dubko). The variety of economic programs put forth by presidential candidates mirrors the polarization of general public views on market transformations. The 1994 presidential election was won by Alyaksandr Lukashenka who, given the economic and political situation of 1994, offered a moderate course steering between radical market changes and a complete restoration of the planned economy.

Although Vyachaslav Kebich, his main competitor, also had a centrist program, Alyaksandr Lukashenka was clearer in his presentation of propositions for economic development, and provided an illustrative description of specific tasks ahead.

Upon electing the first Belarusian president, the country faced a turning point. That was the beginning of a period of strengthening State control over the economy.

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<sup>9</sup> *Эканамічная праграма кандыдата ў Прэзідэнты Зянона Пазьняка*, «Народная газета», № 106 (871) 10 чэрвеня 1994 г.

<sup>10</sup> А. Дубко, *Стране нужен Хозяин*, «Народная газета» № 104 (869) 8 чэрвеня 1994 г.

In December 1994, the United Civic Party at its constituent congress adopted The Platform of the United Civic Party<sup>11</sup>. In response to increasingly stronger State regulation, the program called for ‘far-fetched market reforms in all areas’<sup>12</sup> including price deregulation, financial system stabilization, privatization and restructuring of enterprises, and privatization of land with sale to foreigners.

In October 1995, the United Civic Party passed another program<sup>13</sup>. Unlike its predecessor, the new program speaks merely in terms of ‘establishing an efficient and dynamic social market economy based on private ownership, which could ensure high living standards’<sup>14</sup>. It promotes the idea of low interest-bearing loans to finance housing construction and increasing budget allocations for social welfare out of out of property tax proceeds. According to the platform, such measures can ‘alleviate social tensions resulting from the enrichment of a group of people benefiting from inefficiencies in legislation’<sup>15</sup>. Other points of the new program are similar to those in the previous UCP document.

The Platform of the Belarusian Party of Labor – ‘Towards a Society of Democratic Socialism’ (March 1996)<sup>16</sup> calls for ‘building in Belarus a society based on a multi-structural (i.e. with different forms of ownership) socially oriented market economy’<sup>17</sup>, as well as for ‘transferring the key means of production and land to people to be owned privately, thus ensuring participation of hired workforce in company profits across the nation’s economy’. The Belarusian Party of Labor stands up for ‘each person’s right to work, and strives to ensure full employment in the country’<sup>18</sup>. As the document puts it, the party would warrant the right to work and decent pay primarily by attracting investments into the economy, thereby creating more jobs. The Program also speaks in favor of coordinating activities of the business community, the State and trade unions in order to

<sup>11</sup> *Сборник альтернативных программ развития Беларуси*. Под ред. В. М. Шлындикова, Мн.: Бестпринт, 2001, p. 113–124.

<sup>12</sup> *Ibid.*, p. 117.

<sup>13</sup> *Ibid.*, p. 125–143.

<sup>14</sup> *Ibid.*, p. 129.

<sup>15</sup> *Ibid.*, p. 136.

<sup>16</sup> *Ibid.*, p. 171–191.

<sup>17</sup> *Ibid.*, p. 181.

<sup>18</sup> *Ibid.*, p. 184.

ensure a balanced development of economic sectors, aided by government investments. At the same time, the document points out that ‘the entrenchment of a new economic system would be a long process’<sup>19</sup>.

The Platform of the Belarusian Social Democratic Party (Narodnaya Hramada) adopted at the party’s constituent assembly in June 1996<sup>20</sup> is against ‘both total private ownership and total State ownership of the means of production’<sup>21</sup>. As its ideal, it suggests building a market economy with varied forms of ownership, with focus on social and environmental issues, in which ‘free enterprise is combined with a degree of State regulation of economic growth at a macro-economic level, as necessitated by the nation’s needs’<sup>22</sup>.

*Assessment:* Political parties do not differ in their vision of the economic reform.

The same trend may be observed in programs of candidates at the alternative presidential election in 1999 [which was held pursuant to the 1994 Constitution by those who did not recognize constitutional changes adopted by the controversial referendum of November 1996].

In particular, Mikhail Chyhir’s platform<sup>23</sup> speaks about the need for establishing an open, diverse, socially-oriented market economy. The document’s most important provisions point to stability of the sovereign currency, stability of prices, stopping unsecured lending (‘money printing’), ensuring that the public budget is reasonable, realistic and socially-oriented, preparing regulations to speed up privatization, and pursuing a policy that would combine firm protection of domestic producers with liberalization of domestic and foreign trade.

In fact, the program suggests mere cosmetic changes in the existing economic make-up.

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<sup>19</sup> Ibid., p. 183.

<sup>20</sup> Ibid., p. 144–170.

<sup>21</sup> Ibid., p. 154.

<sup>22</sup> Ibid., p. 154.

<sup>23</sup> Ibid., p. 235–240.



Likewise, the platform of Zyanon Paznyak of the Belarusian Popular Front, another presidential candidate, does not offer radical approaches to market economy<sup>24</sup>.

In his program for the 2001 presidential election<sup>25</sup>, Alyaksandr Lukashenka again confirms his adherence to previously chosen economic priorities, such as stimulating exports and housing construction, support to agriculture including State and collective farms, State regulation of prices, compulsory award of jobs to graduates of State educational facilities, etc. Yet, the program also includes one new point: liberalization of the economy and stimulation of business activity. In general, however, the document does not envisage any material reforms. It does not provide for any serious market reform, instead calling for a forward move as facilitated by 'the country's political and socio-economic stability'<sup>26</sup>.

The platform of Uladzimer Hancharyk<sup>27</sup> calls for eliminating obstacles to business by introducing simple rules for registering new undertakings, safeguarding the banking system's independence, stop extending unsecured loans, reducing the costs and size of government bureaucracy, reducing taxes, simplifying customs procedures, improving foreign trade and allowing state-owned and collective farms to transform ownership. The program is in favor of economic liberalization; however, it does not specify which market transformations are to be put to work. In particular, there is no mention of privatization. Instead, it contains a chapter on technology upgrades in and restructuring of companies by means of domestic and foreign investments.

Similarly, the program of Syarhey Haidukevich does not offer anything novel in the way of economic ideas<sup>28</sup>. It calls for a need to reform the fiscal system

<sup>24</sup> Ibid., p. 241–253.

<sup>25</sup> *Вместе за сильную и процветающую Беларусь! (Предвыборная программа Президента Республики Беларусь А. Г. Лукашенко)*, «Советская Белоруссия» №№ 237–238 (21234–21235) 21 августа 2001 г.

<sup>26</sup> Ibid.

<sup>27</sup> В. Гончарик, *Добро вашему дому! (Тезисы программы кандидата в Президенты Республики Беларусь)*, «Советская Белоруссия», № 250 (21247) 31 августа 2001 г.

<sup>28</sup> *Порядок в стране, достаток в доме. Кандидат в Президенты Республики Беларусь Гайдукевич Сергей Васильевич. Тезисы предвыборной программы*, «Советская Белоруссия», № 239 (21236) 22 августа 2001 г.

along the Russian model, points to the importance of a new investment policy (yet never specifying what this policy should be), and stresses that the country should benefit from its advantageous geopolitical situation. The only aspect that sets it apart from other candidates' platforms is the affirmed support for fostering ecotourism in Belarus.

As outlined above, the programs of different political forces have whittled down to few essential differences, if any.

## **Economic reform concepts and programs developed by independent expert teams**

When set against political party concepts, independent groups of experts may be said to have come up with more professional proposals for a market-oriented transformation of the national economy.

Proposals for Economic Policy Formulation (Stabilization Phase) were adopted by the Economic Policy and Reform Committee of the 13<sup>th</sup> Supreme Soviet, following their preparation by a group of authors including U. M. Shlyndzikau, L. K. Zlotnikau and N. G. Babrytski in 1996<sup>29</sup>.

The document pointed out that, at the time it was written, negative processes in the Belarusian economy were not stopped: living standards had been deteriorating along with the same trend in GDP formation, while the poor population had been kept on meager subsistence at the expense of using up and eventually wasting fixed assets. The document proposed several principles to underpin economic policies, including that of greater economic freedom, fostering entrepreneurship, protecting private property, private sector formation, supporting the growth of competition, State support for exports and domestic output with export-oriented outlooks, and social stability. The authors claim that the principles could actually be applied once as many as 98 macroeconomic measures are put in place. Along market measures such as price liberalization in the farming sector, reduction of import duties down to WTO standards, and establishing of

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<sup>29</sup> *Сборник альтернативных программ развития Беларуси*. Под ред. В. М. Шлындикова, Мн.: Бестпринт, 2001, p. 254–265.

capital and stock markets, the authors also suggested ‘measures to regulate in inflow of foreign investments in banking and insurance in order to ensure the State’s economic security’, ‘regulation of fuel prices to keep them in line with price levels in the neighboring countries’, ‘limiting the incomes gap between the richest and the poorest to 10 percent during stabilization’<sup>30</sup>.

However, the authors confine themselves merely to enumerating measures to be taken, and do not consider the opportunities, realities, mechanisms, etc. for their implementation. In many cases they stop at flagging up a measure, for example ‘ensuring convertibility of the Belarusian ruble at a fair level’<sup>31</sup>.

*Assessment:* The above document is more of a response to major problems of the Belarusian economy of that time. It lacks a systemic approach to the process of market reform, although such reform is affirmed as being pivotal to its economic policy.

Concept and Program of Economic Reform (by the National Executive Committee) – prepared by a group of authors including S. A. Bahdankevich, U. S. Basharymau, Ya. Ch. Ramanchuk and G. D. Karpenka in 1998<sup>32</sup>.

This document was a response of the National Executive Committee, the shadow cabinet, to curtailing market reforms in the country in 1996–1998 and turning to ‘Socialist’ methods of economic governance. Its first part takes stock of the economic situation in Belarus and points to obstacles in the country’s consistent, long-term economic development. In particular, the authors point to legal nihilism, State monopoly in nearly all areas of economic activity, exclusion of public sector from market mechanisms, lack of market infrastructure or safeguards for private property, poor financial and contractual discipline, lack of effective restructuring and bankruptcy mechanisms, excessive tax burden, non-liberated monetary and lending markets, and lack of a sound, economically founded anti-crisis government program with a team capable of implementing it.

As stated in the document, the main way out of the economic crisis is to use the power of private enterprise and promote economic freedom. The authors be-

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<sup>30</sup> *Ibid.*, p. 257, 262, 264.

<sup>31</sup> *Ibid.*, p. 256.

<sup>32</sup> *Ibid.*, p. 331–341.

lieve that the role of the State should be limited to developing a market-oriented regulatory framework with a level playing field for all undertakings and individuals. They stress that the main idea of market reforms is in achieving the triple target for the transition period: stabilization, liberalization and institutional changes in all economic aspects.

*Assessment:* One essential difference between this and previous document is that it contains a description of financial support for reforms and expected deliverables.

Strategy for Belarus: A Concept of National Development – published by a group of authors including M. I. Hryb, S. Ya. Leushunou, L. F. Zaika, Ya. Ch. Ramanchuk, L. K. Zlotnikau and others in 2000<sup>33</sup>.

Apart from status description of the economic situation and specifying goals and principles of reforms, the document provides a detailed analysis of how the Belarusian economy will develop if the existing economic policy is to be continued. The authors offer their vision of the sequence of reforms, analyze what the general public thinks about the economic situation in the country, and make assumptions as to how the nation would react to their reform ideas. The document reviews all the previous concepts of conducting market reforms in Belarus. It emphasizes the importance of market reforms, and points to the systemic nature of current economic problems in Belarus.

The 'Strategy for Belarus' formulates economic reform goals and principles in monetary, fiscal, trade, investment, price, industrial and agricultural policies; it describes mechanisms of establishing conditions for developing small business and putting safeguards for private property in place. As stated by the authors, the planned measures have to be taken in three phases: firstly, economic liberalization and preparations for the system's stabilization; secondly, stabilization and laying foundations for economic development; and thirdly, institutional transformations, manufacturing sector upgrades and participation in globalization processes.

*Assessment:* The document provides a concept for national economic development, which sets out guidelines for democratic market transformations, but

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<sup>33</sup> Ibid., p. 372–431.

fails to describe a long-term, sustainable socioeconomic model for Belarus, or the mechanisms for conducting reforms in accordance with the measures proposed. Therefore, the document cannot be said to be a comprehensive program of market reform.

The Program of Socioeconomic Reforms for Belarus of the Coordinating *Rada* (Council) of Democratic Forces – drafted by a group of experts headed by P. U. Daneika in 2001<sup>34</sup>.

This document is not really a concept per se; rather, it is an attempt to structure a real program of reforms for Belarus which envisages broad reforms in monetary and fiscal policy, formation of market institutions, development of the private sector, restructuring of industrial and agricultural enterprises, and changes in foreign trade and social policies.

The group of experts sets forth the following goals to be achieved by the reforms: ensuring macroeconomic stability, generating confidence in the national currency among the business community and individuals, matching government spending with budget revenue, reducing tax burden with an expanding tax base, lifting restrictions in setting prices for goods and services, establishing private ownership of land, abolishing ‘money-printing’ practice in extending loans to state-owned farms, providing targeted support to poor social groups; creating an efficient system of occupational training; establishing a mobile labor market force, etc.

Each chapter describes the existing situation, reviews previous developments, sets reform goals in specific areas, offers main reform principles and formulates measures to be taken to achieve the goals.

*Assessment:* Despite a rather detailed description of goals, tasks, objectives, directions and principles for economic reforms, the document lacks an indication of a long-term, sustainable socioeconomic model for Belarus, as well as fails to specify reform phases, expected deliverables and public views on proposed reforms.

<sup>34</sup> *Праграма сацыяльна-эканамічных рэформаў для Беларусі (Каардынацыйная Рада Дэмакратычных Сілаў), Група экспертаў на чале з Данейкам П. У., Мн. 2001, р. 180.*

The document is too focused on existing economic problems in Belarus. It is dominated by the macroeconomic approach to reforms. Meanwhile, it is a valuable attempt to move from general concepts to specific economic reform programs.

An analysis of economic reform concepts and programs prepared by independent groups of experts shows that there has been substantial evolution of such documents from indecisive, contradictory and incomplete to a clearer understanding of the essence of market reforms and, consequently, to more specific and decisive programs of reform. At the same time, the above documents rely heavily on current economic developments. Market reform is often regarded as a 'magic word' resolving existing economic problems.

## State-sponsored programs of economic reforms

A number of State-sponsored reform programs were prepared for Belarus in the 1990s. Most of them saw the light of day in 1996, when official elites and political parties finally parted ways, which is why the government faced the need to step up its own efforts in developing programs of reforms. Below is a review of the most important ones.

A Plan for Financial Recovery Measures in the National Economy by Belarus' National Bank (August 1, 1996, to October 1, 1997)<sup>35</sup>.

The document is a rather in-depth analysis of the country's economic situation in the first half of 1996. It singles out a number of positive trends, such as slower inflation and devaluation processes, slower pace of economic decline, adaptation of undertakings to market conditions, and increase in real personal incomes. At the same time, it points to certain negative trends, such as a sharp decline in capex, worsening foreign trade indicators, yawning trade deficit, growing unemployment, increasing number of unprofitable enterprises and a larger public budget deficit.

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<sup>35</sup> *Сборник альтернативных программ развития Беларуси*. Под ред. В. М. Шлындикова, Мн.: Бестпринт, 2001, p. 266–330.

Against the backdrop of a comprehensive analysis of the economic situation, the National Bank's experts proceed to stating that the main reason behind the crisis is inferior competitiveness of most domestic enterprises and the national economy at large. They explain that such a situation is a legacy of the socialist economy and its general backwardness. Yet, simultaneously, the experts also admit that 'the failure of the government to understand the macroeconomic situation in Belarus, the lack of clarity in choosing ways of reforming the socio-economic relations in a newly-established sovereign Belarus, as well as indecisiveness and inconsistency in conducting economic reforms have been the main reasons for economic crisis symptoms to set in'<sup>36</sup>.

The authors point to the problem of then unreformed real economy, which turned out to be in conflict with the National Bank's course of tight monetary policy and efforts to slow down the inflation and national currency devaluation in 1995–1996. In order to resolve the conflict, the National Bank's document offers a plan with measures aimed at financial recovery in the economy. Part One of the action plan encompasses a range of measures to stimulate capital expenditure projects and improve competitiveness of domestic enterprises. Following this are measures to streamline the social services and welfare system, ensure better regulation of personal income and employment, and support small businesses in job creation initiatives. Parts Three and Four are devoted to issues of improving monetary and exchange policies. The National Bank's experts point out that changes in inflationary processes, namely inflation exceeding devaluation, result in domestic prices nearing world prices and in eroding competitiveness of domestic enterprises in price terms. Part Five includes measures geared to improve the fiscal and budget systems. Their main idea is to lower the taxes for undertakings, and thereby improve tax collection. Part Six pays considerable attention to the need for fostering the growth of a financial market. Part Seven describes measures in foreign trade policy, pointing to the need for supporting national exporters and developing import-substituting output. A special part in the document is made up of institutional pro-

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<sup>36</sup> Ibid., p. 275.

posals which have to precede financial recovery measures in order to work in harmony with them.

*Assessment:* The document offers an in-depth analysis of the reasons underlying the economic crisis of 1996. Still, the proposed program of reforms is rather limited and proposes little else than measures aimed at financial stabilization at the macro-level. Notably, even this program was not implemented at the time.

The following document was prepared in October 1996 – Guidelines for Belarus' Socioeconomic Development in 1996–2000 – approved by a presidential edict # 464, on November 14, 1996.

In accordance with the trend to modify economic policies so as to orientate them more toward social aspects, and in reaction to an unstable economic situation of the early 1990s, the document asserts that the key strategic goal for economic changes is to result in improving living standards of the Belarusian people, gradually bring them to those in well-developed European countries by building a socially-oriented market economy.

In the initial phase of economic transformation, the document envisaged macroeconomic stabilization and setting the stage for economic growth, while the second phase, i.e. post-1997, was to be a period of economic growth. Those two phases had to be completed by the year 2000.

The document describes measures aimed at a structural reconstruction of the economy, including those to improve the operational efficiency of State property, including de-nationalization and privatization, financial recovery of undertakings via restructuring and bankruptcy procedures, effect land reform by introducing private ownership of land, develop small- and medium-sized business and market infrastructure by encouraging competition, and stimulate commodity, financial and labor markets.

The program also envisages measures to develop science and innovation, real sector of the economy and capex activities, as well as calls for adjusting fiscal, price, monetary and forex policies.

Despite a large number of market measures advocated, most tend to be half-hearted solutions. Specifically, the document suggests privatizing only small state-owned companies, while large enterprises are to be denationalized, i.e. they



would turn into joint-stock companies with the controlling stake of the State. The program also says that the State will continue to own large companies for many years to come and, accordingly, a large sector in the economy will be state-owned or controlled. Therefore, there is a call for raising the efficiency of the state-owned sector via streamlining the management of state-owned companies and drafting regulations to improve mechanisms of their operation so as to achieve stable production levels, ensure appropriate discipline amongst employees and management, etc.

Similarly, as proposed, the State intends to play a dominant role in setting prices, i.e. launch market principles but retain levers of State regulation. This is to apply also to developing the real sector of the economy, i.e. prioritize housing construction and farming in economic development, and developing entrepreneurship and SMEs by providing them with consultation services, resources and protection. Similarly, the labor market is to be reformed by guaranteeing young people the right of preferential treatment in job search. There is similar mention of other areas in this context.

*Assessment:* This document offers a moderate program of reforms. It contains an extensive list of vaguely formulated measures, with no specific terms of taking them on board. Consequently, it is difficult to understand whether the program has actually been put to effect.

Due to general financial instability in late 1990s, higher pace of inflation and devaluation, declining exchange rate and consequent increase in physical volume of exports at lower prices, the country's industrial output and GDP growth gained momentum. Therefore, the main target of the '1996–2000 Socioeconomic Development Guidelines', that is economic growth, was formally achieved, albeit without causing market changes, which was why the market processes essentially slowed down in subsequent years.

The macroeconomic stabilization of Belarus has not been achieved to date.

One of the underlying reasons was that another program was heralded for the country – The Program of Belarus’ Socioeconomic Development in 1996–2000, developed by Eduard Eydzin, the president’s economic aide at that time<sup>37</sup>.

Despite never being officially approved by the Cabinet, the program had a most significant impact on the country’s economic policy, even greater than official reform programs.

The program is noted for its expectation of quick results upon its implementation. It was founded on the premise of ‘the State that has a strategic program and a well-organized, productive and efficient government system capable of preventing the economy from collapsing in crisis conditions and of ensuring necessary conditions for an irrevocable transition to a socially-oriented market economy within a short period of time’<sup>38</sup>. Along with privatization and ‘effective support for all bona fide members of the business community’<sup>39</sup>, the program envisaged a number of other measures, such as ‘designating key priority manufacturing industries and output, and establishing a program of targeted centralized State support during a period of stabilization and initial development of the aforesaid manufacturing industries’<sup>40</sup>, low interest-bearing loans to priority industries, protection of domestic producers by customs barriers, flexible State regulation of prices, which ‘is by no means a step back from market mechanisms; on the contrary, it approximates the economy to civilized market practice’<sup>41</sup>.

The program lay the ideological foundation for the government’s economic policy of the late 1990s. The implementation of its principle of ‘creating a system for channeling monies into the economic needs of the day’<sup>42</sup> led to excessive money-printing, exacerbated financial instability, boosted inflation and na-

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<sup>37</sup> *Программа социально-экономического развития Республики Беларусь на 1996–2000 годы (Основные направления)*, Мн. 1996, p. 257.

<sup>38</sup> *Программа социально-экономического развития Республики Беларусь на 2001–2005 годы*, Мн. «Беларусь», 2001, p. 7.

<sup>39</sup> *Ibid.*, p. 67

<sup>40</sup> *Ibid.*, p. 31.

<sup>41</sup> *Ibid.*, p. 101.

<sup>42</sup> *Ibid.*, p. 126.

tional currency devaluation, lowered the Belarusian ruble exchange rate, and prompted sales of Belarusian goods abroad at disadvantageous prices. Despite a growth in export-oriented output and GDP, the average pay in the country fell threefold if expressed at the market ruble-to-US dollar exchange rate.

The program's consequences were partially eliminated, albeit not until the early 2000s, when the government opted for a tighter monetary policy, exchange rate and price liberalization, and improved competitiveness of the domestic output.

The Program of Belarus' Socioeconomic Development in 2001–2005, enacted by a presidential edict # 427 on August 8, 2001<sup>43</sup>, is the government's current program of reform.

It takes stock of the present socioeconomic situation in Belarus, sets out macroeconomic policy objectives and guidelines, and outlines scenarios of the country's economic development during the first five years of the 21<sup>st</sup> century.

Just like its predecessor, the '1996–2000 Guidelines for Belarus' Socioeconomic Development', the new program sets the strategic objective of 'improving the living standards of the Belarusian people to align them to the level of economically developed European countries'<sup>44</sup>. The document emphasizes the need for enhancing the efficiency of the real sector, for technological improvement and modernization of the economy.

Market transformations are outlined in a dedicated chapter. They comprise denationalization, privatization, development of entrepreneurship, promotion of SMEs, market infrastructure formation and human resources development. The document does not offer much novel content on these issues. Again, it advocates 'prudent privatization: 'swift privatization is not envisaged for 2001 to 2005; instead, a gradual approach to reform should be considered...'<sup>45</sup>.

Like other documents for the previous period, the program indicates the government's propensity towards excessive State sponsorship of developing

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<sup>43</sup> *Ibid.*, p. 167.

<sup>44</sup> *Ibid.*, p. 40.

<sup>45</sup> *Ibid.*, p. 66.

entrepreneurship: 'varied and targeted State support will be provided to those entrepreneurs and businesses that engage in capex projects in high-priority areas'<sup>46</sup>. It contains the same vague definitions of measures and fails to specify when measures are to be initiated.

As the document claims, the government plans to continue developing housing construction, yet vouchsafes to abandon money printing as a means of financing housing via lending. It also intends to intensify the structural economic reform, expand the area of market-based pricing and reduce cross-subsidies in the cost of energy for residential and industrial off-takers alike.

In addition, unlike the previous document, the program includes a chapter on developing the stock market.

*Assessment:* The document does not differ in any essential manner from its predecessor for 1996–2000. Both are very cautious and ambiguous in terms of formulating and implementing proposed measures.

## Conclusions

As of today, Belarus does not have an ambitious program of market reforms which would envisage swift moves in Belarusian economic reforms and the country's integration with the international economic set-up. There is no program proposing EU accession as its objective.

A new program should outline a future economic system in Belarus in distinct terms, a system based on market principles without State domination. It would have to formulate a concept of unleashing private initiative as a driving force for developing the national economy. It would also have to reflect changes in the economic situation in Belarus, and emphasize reforms in the real sector, rather than just focus on achieving financial stabilization as former programs did. Apart from domestic changes, it should consider changes in the international economic situation, and the European Union's eastward enlargement in particular.

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<sup>46</sup> Ibid., p. 69.

Growing public acceptance of market reforms and the European integration are important factors that could prompt the drafting of a new program. Therefore, the new program should suggest specific steps in implementing market reforms in Belarus and concrete measures aimed at Belarus' joining the World Trade Organization and the European Union.

An important idea to be incorporated into the future program should be one going beyond a mere achievement of higher living standards as fostered by economic growth and higher personal incomes. It should also comprise the premise of creating comfortable living and working conditions for the population at large, and vesting people with confidence that the future will be brighter than the past.

# 2

## Belarus' Economic Status. Why Is Belarus' Economy In Urgent Need of Reform?

by Vital Silitski<sup>47</sup>

### Current status

Since the 1990's, Belarus has lagged behind other CIS countries in economic reforms. The US-based Heritage Foundation dubbed Belarus' economy 'repressive'. In the early 1990s, the government attempted to carry out reforms, but stopped with Alyaksandr Lukashenka's effective election for president. He sought to retain total control of the economy by stifling the private sector. Repressive measures included nationalizing banks, imposing restrictions on private businesses, resurrecting the planned economy and fueling inflation to boost economic growth.

Structurally, Belarus has a Soviet-type economy. It lacks: a) a market-adjusted manufacturing structure resulting from independent choices of consumers, business and sources of capital. b) unregulated prices, and c) a well-developed labor market.

Institutionally, Belarus has a command economy dominated by the public sector with administrative allocation of financial and physical resources, price controls and unbalanced prices. In addition, the government relied heavily on 'bureaucratic deals', such as the oil-for-goods contracts with the Russian government. In result of such widespread practice, governmental agencies turned

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<sup>47</sup> The author acknowledges the assistance of Pavai Daneyka and Alyaksandr Hatouski in writing up this topic.

into intermediaries dealing in products of state-controlled enterprises. The latter have either lost their right to independently run their business, or deliberately handed business initiative over to the government.

The way the government makes economic decisions is high on economic populism. The government's priority is to see the economy advance and redistribute profits to the public sector's advantage by collecting a tax from private and foreign trade sectors. The policy ignores inflation and budget deficit risks, or takes no account of the external environment or response from contracting partners in business. In an effort to offer additional social security guarantees, Alyaksandr Lukashenka resorted to wage increases that were not supported by an adequate economic growth, aided instead by price and exchange controls, restriction on imports, and expansionary fiscal and monetary policies.

### **The 'economic miracle' or paradoxical growth in a command economy**

Absence of reforms in the Belarusian economy has not led to its collapse, and the government's anti-market policy did not prevent it from growing in late 1990s. Despite macroeconomic instability, high inflation and depreciation of the ruble, the Belarusian economy has been growing since 1996. Against the background of recession continuing in Russia and other former Soviet republics, Belarus' economic recovery seemed to be a miracle.

Nevertheless, Belarus' true economic growth may be questioned, considering the controversies surrounding the credibility of official statistics. For example, the methods of calculating GDP growth, inflation and GDP deflators raise a lot of issues<sup>48</sup>. Still, there was some economic growth in Belarus, but the nature of this growth needs thorough examination. It should be noted that capex on upgrade programs and new product development was negligible. Before the economic recovery, the private sector comprised merely small trade, service and woodworking companies. The fact that most enterprises were public did not make the environment more appealing to potential investors, or

<sup>48</sup> See details: А. Чубрик, *Экономика Беларуси: Статистический обзор*, Дасьледніцкі цэнтар бізнэс-школы ІПМ, аналітычны даклад № 5, Менск: верасень 2001 г.

prompt enterprises to invest in new plant and machinery and manufacture competitive products.

**Table 1. Belarus' Economic Indicators (as share of prior year's indicator)**

	1995	1996	1997	1998	1999	2000	2001	2002
Gross Domestic Product	89.6	102.8	111.4	108.4	103.4	105.8	104.7	104.7
Industrial output	88	104	119	112	110	108	106	104
Agricultural output	95	102	95	99,3	92	109	102	102
Capex on fixed assets	69	95	120	125	92	102	97	103
Cargo shipments	75	87	109	105	96	91	98	109
Retail sales	77	131	118	126	111	112	128	113
Producer's price indices	561	134	188	172	456	286	172	140
Consumer price indices	809	153	164	173	394	269	161	134
Exports to CIS countries	205	124	143	96	70	121	103	99,3
Exports to non-CIS countries	172	106	102	99,3	120	128	101	123
Imports from CIS countries	176	124	127	95	77	142	94	109
Imports from non-CIS countries	194	126	121	104	80	108	96	112

Source – CIS statistics committee

The industrial upturn was attributable to expansionary monetary policies, also used for funding the inefficient agricultural sector and government housing construction projects. Monetary expansion weakened the Belarusian ruble and led to a drop in prices in dollar terms and a rise in exports. Stocks of unsold goods were diminishing; factories operated at full capacity and recalled their employees from forced leave. However, soon it was obvious that it was a fall in the dollar equivalent of salaries and wages, calculated at the market exchange rate, which thwarted prices in dollar terms. People worked more but earned less.

To prevent living standards from declining sharply, the government resorted to price controls. The consumer purchasing power was growing, with wa-



ges decreasing in dollar terms. All these factors discouraged enterprises from producing better goods, and caused shortages in staple goods and agricultural stagnation.

Thus, a rapid yet temporary economic growth was fuelled by populist measures. The growth was too costly and unsustainable. The main objective of Lukashenka's experiment was to resurrect and maintain the Soviet economic model rather than carry out structural reforms in the late 1990s.

Once at its critical point, the dilapidated industrial asset base will be absolutely ineffective, while the external economic environment will develop in a manner disadvantageous to Belarus as neighboring countries, Russia primarily, will outstrip Belarus in terms of economic growth. This means that some day Lukashenka will have to pay a high price for his populist experiment.

The Lukashenka administration was forced to embark on efforts, however feeble, to reform the economy, including ways of limiting the growing money supply, cut State subsidies, unify the Belarusian ruble exchange rates and adopt a crawling exchange rate peg.

By contesting the need for market-oriented changes, the Belarusian authorities failed to lay a solid foundation for sustainable economic growth. Yet, in the short term, the policy was rather effective in terms of maintaining social stability and conserving the existing political situation with silent majority support among the general public. Moreover, by correcting their most absurd mistakes, the authorities managed to avoid a big macroeconomic disproportion that might have triggered off hyperinflation and a major economic crisis.

### **Living standards in an unreformed economy**

Official statistics indicate improvements in living standards for Belarusians. According to the Ministry of Statistics and Analysis, real income more than doubled between 1995 and 2001. The figures also suggest that Belarusians enjoy the highest standards of living ever. Real incomes in 2002 were 30% above the 1990 level. Moreover, real income grew faster than GDP. One may logically assume that the consumption-to-GDP ratio was rising due to a decline in capex

and savings<sup>49</sup>. Another possible explanation is that the official statistics have nothing to do with the real state of affairs in the country. Still, the truth is most likely to reside somewhere halfway between the two possibilities.

Official statistics on living standards and real income raise many questions, especially about the calculation methods used. Real income indicators depend directly on the computation of inflation, while the ministry's methods of determining the latter are rather questionable. There are also other questions. As per the same official statistics, for example, real income increased by 12 percent in January through March 2003. Yet, over the same period, real-term salaries dropped by 5 percent against December 2002 (The nominal salary was up by 3 percent, whereas consumer prices soared by 8.1 percent).

It would be interesting to compare the abstract statistics on real-term income growth with more realistic figures indicative of living standards, which offers a clearer picture for the general public. Let us consider food consumption. Belarusians spent more than half of their personal income on food. As seen in Table 2, the official statistics do not reflect any dramatic decline in food consumption, yet even in the most favorable year 2001, as reflected by official figures, Belarusians consumed much less than in 1990. Consumption was slightly above 1995 levels, but one should bear in mind that a high-calorie diet with high butter and sugar content is typical of countries with low living standards. It should be stressed also that the majority of consumed food was produced in private gardens and allotments. For example, in Minsk (the capital of two million), private holdings accounted for 53 percent of the output of consumed potatoes and 43 percent of vegetables in 2001. In other words, the standard of living does not decline much mostly as people supplement their income by additional work during days off, engaged in what is basically subsistence farming, hardly a proof of the Belarusian economic model's efficiency.

The poverty statistics (Table 3) may also offer a more realistic idea of how large personal incomes were. However absurd it may seem, between 1995 and

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<sup>49</sup> Each official statistical indicator is calculated with the use of different deflators.

**Table 2. Consumption of Staple Food Items**

	1990	1995	1996	1997	1998	1999	2000	2001	2001 as % of 1990 level	2001 as % of 1990 level
Bread	127	121	122	122	118	115	110	105	82.6	86.7
Potatoes	171	182	188	182	173	170	174	172	100.5	94.5
Fruit	78	83	88	88	87	89	93	98	125.6	118.1
Vegetables and berries	38	38	39	37	35	24	25	65	65	
Sugar	49	32	32	34	37	34	34	41	83.6	128.1
Oil	8.6	6.5	6.8	7	6.6	8.3	8.7	10	116.2	153.8
Meat	76	58	60	60	62	62	59	59	77.63	101.7
Fish	19.6	7.3	8.7	8.7	6.1	6.2	9.5	11	56.1	150.7
Milk, liters	428	367	369	350	372	334	295	307	71.7	83.6
Eggs.	325	297	299	296	271	237	224	224	68.9	75.4

Source: the Ministry of Statistics and Analysis of Belarus, author's calculation.

2000 when, as the official statistics have it, real income soared by 70 percent, the proportion of low income households with below-subsistence levels increased instead of shrinking. The Gini index of inequality did not change much over the period.

Yet, the situation did improve in 2001, mainly as a result of short-term political measures (an increase in wages and old age pensions before the presidential elections in a move intended to bolster support for the incumbent president).

However absurd, in 1996 and 1998, at the time of a significant increase in personal incomes, the poverty level also rose. Moreover, for some reason, poverty was rapidly expanding in 1999, while the reported decrease in real income was negligible. In 2000, as claimed in official statistics, income rose by 50 percent against 1995, while the number of low income households sky-rocketed by a factor of three. It means that the official statistics on real income can hardly be a reliable criterion for estimating living standards in Belarus.

**Table 3. Real Income, Poverty and Income Distribution in Belarus**

	1995	1996	1997	1998	1999	2000	2001
Changes in real income (as percentage of prior year's indicator)	-27	17	6	19	-3	20	29
Households with per capita income below subsistence level (as percentage of prior year's indicator)	38.4	38.6	32.1	33	46.7	41.9	28.9
Gini index	26.1	25.4	25.8	28.3	26.9	27	27.8

Source: the Ministry of Statistics and Analysis of Belarus.

Living standards may be estimated by converting salaries and pensions into US dollars. The average monthly pay in November 2002 rose to \$107 after a slump from \$88 to \$36.4 in 1996–2000. However, over the same period, the US dollar equivalent of consumer prices increased twofold, consumer goods prices shat up by 77 percent, prices of consumer services and utilities sky-rocketed six- and 14-fold, respectively.

Moreover, official statistics hardly take into account the higher cost of education and healthcare services. Belarusians saw not only cheap goods but also free education and healthcare vanish. New price markets have emerged, including corrupted ones, but the government does not even intend to legalize them and thus provide real-term social security in the form of education loans or health insurance.

In this context, results of the opinion poll conducted by the Independent Institute of Social Economic and Political Studies (IISEPS) in April 2003 may seem interesting. Only 7 percent of those polled said they were better off lately, while 42 percent stated the opposite. 53 percent were concerned about rising prices of utilities and consumer services, 51 percent were concerned about rising prices of staple goods, 12 percent expressed concern over the introduction of tuition fees, and 24 percent worried about chargeable healthcare services<sup>50</sup>.

<sup>50</sup> Source: IRISEPS, <http://www.iiseps.by/press1.html>, April 29, 2003.

It may be concluded that, firstly, there was no dramatic decline in living standards during Lukashenka's presidency; on the contrary, there was obvious improvement. Secondly, real income growth is certainly overstated in official statistics and may be questionable. Thirdly, the period of rapid economic growth, fueled mainly by political measures, is attributable to years 2000 and 2001, yet not sustained by the government. Finally, living standards did not drop dramatically as the people adapted to existing conditions. It merely goes to say that more people resorted to subsistence farming, but this did not help to improve quality of life or boost economic efficiency.

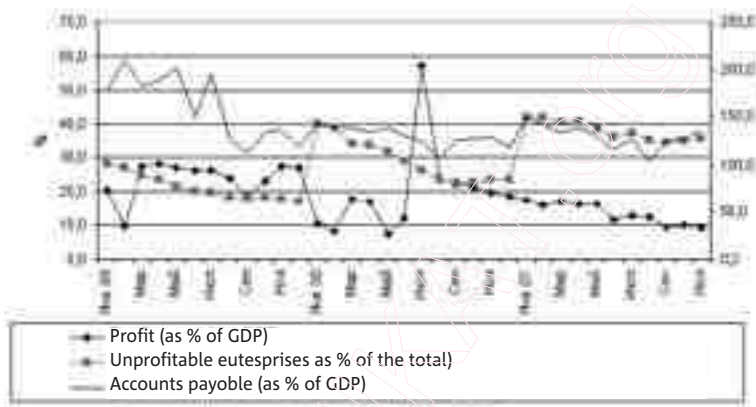
### Real economy crisis

Are there any realistic prospects for a sustainable and dynamic economic development in Belarus? Is it possible to improve living standards within the existing economic system? Belarus' economic outlook is grim.

*Unprofitable enterprises.* The Belarusian government's economic experiment has brought about rapid erosion of profitability in the corporate sector. In the first quarter of 2003, the proportion of those in the red reached 48 percent. Most of these are bankrupt since their total debt exceeds asset value. Moreover, enterprises do not generate much profit from their output as their goods are not competitive at home or abroad. With profitability remaining low, enterprises are not in a position to finance upgrades. Most industrial operators seem hardly able to make it in the future, even if the government sticks to its current policy of supporting the public sector.

A number of factors have contributed to the financial crisis in the manufacturing sector. Some enterprises face difficulties as they had to follow governmental directives geared to increase the output, which was possible only by cutting capex on fixed assets and upgrade programs. Other enterprises fell victim to price controls. When the government was supporting the manufacturing sector with soft loans and redistribution of convertible currency resources, enterprises were not motivated towards making competitive products. As the industrial crisis deepened, the government adopted more sensible macroeconomic policies.

Diagram. Profit and Debt indicators of the Belarus' Economy



Source: The Ministry of Finance of Belarus

In fact, the governments' objective to achieve full employment has indeed brought about the crisis. Enterprises had to keep redundant labor force in employment or, in other words, to maintain low output and efficiency. During Lukashenka's presidency, the official unemployment rate dropped from 4 percent in 1995 to 2 percent in 2000. Yet, according to independent researchers, hidden unemployment was on the rise<sup>51</sup>. In 2000, just one in four unemployed persons was captured by the official system. As the financial crisis progresses, hidden unemployment was rising. In 2002, compensation arrears amounted to 20 percent of the payroll, and the debt was cleared only by the year's end. Yet, the arrears shot up again in April 2003 to reach 7.5 percent in result of the government's failure to reform the real economy.

<sup>51</sup> In 1997, the government introduced new rules for granting unemployment benefits that discouraged the jobless from registering with employment centers ( A. Соснов, *Государственная социальная политика: белорусский вариант* [в:] *Белорусская экономика: от рынка к плану, 1995–2000*, т. 1, р. 17).

*In need of investments.* Lack of capital expenditure aggravated the crisis in the real economy. As seen in Table 4, capex remains one of the most burning issues for the Belarusian economy. Capex in the manufacturing sector in 2002 was just over half of the 1989 volume, with the industrial output far exceeding peak levels of Soviet times, if official statistics are to be believed. In other words, the Belarusian economy is eating into its fixed assets.

**Table 4. Investments in Belarus**

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002
Investment in GDP, %						18.4	15.6	18.6	22.6	20.6	19.8	17.8	16.6
In manufacturing						10.8	9.8	11.2	13.9	11.7	11.4	10.9	10.3
Non-manufacturing						7.6	5.8	7.4	8.7	8.9	8.4	6.9	6.3
Investment growth (1989=100)	109	113	80	68	61	42	40	48	60	55	56	54	56
In manufacturing	105	109	66	57	51	36	37	42	53	46	48	49	52
Non-manufacturing	116	121	112	94	83	56	48	62	76	77	77	68	68

Source: the Ministry of Statistics and Analysis, author's calculations.

In fact, the government provoked acute capex shortages in order to boost economic growth and maintain high consumption figures during populist campaigns. In 2001, the reported GDP growth was as low as 4 percent, whereas real wages increased by as much as 23 percent. The Lukashenka government's effort to achieve growth by all means made it much more difficult for investment-starved enterprises to replace their obsolete equipment, which has led to its further depreciation. Although Table 5 does not include equipment wear and tear figures, it should be noted that, in 2002, an average of 80 percent of plant and machinery was worn out.

The Belarusian government's populist investment policies, which included housing construction programs, the Minsk Ring Road, redevelopment of the Independence Square or National Library projects were a major cost to the taxpayer. In addition, the government allocated considerable funds for irrational import substitution programs.

**Table 5. Equipment Depreciation in Various Industries**

	1990	1995	2001
Average	39.8	56.5	61.4
Power generation	46	51.8	59.8
Fuel	68.2	58.8	66.4
Metallurgy	18.4	44	45.7
Petrochemical	58.6	67.5	69.9
Equipment manufacturing	45.3	56.3	63.7
Timber	50.2	49	59.6
Building materials	47.2	49.8	56.1
Light industry	38.8	54.3	57.1
Food processing	36.3	47.9	47.1

Source: the Ministry of Statistics and Analysis of Belarus.

Foreign direct investments are another problem<sup>52</sup>. Belarus ranks last among East European countries in terms of FDI per capita. Russian gas giant Gazprom's investment in the Yamal–Western Europe pipelines accounted for greater part of total foreign investments.

<sup>52</sup> The government claimed that FDIs totaled \$700 million in 2002. The amount, however, includes loans of \$400 million and nearly \$200 million in proceeds from the sale of the government's stake in the Russian oil company Slavneft. Part of those monies was spent to pay off the country's debt for energy resources.

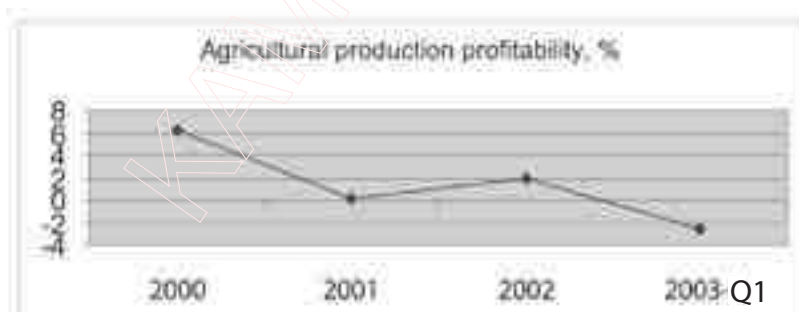


**Table 6. Foreign Direct Investments in Belarus**

	1993	1994	1995	1996	1997	1998	1999	2000	2001
Annual FDI growth, \$ mio	17	10	14	104	351	208	444	118	108
Cumulative increase, \$ mio	17	27	41	145	496	704	1148	1266	1374
FDI per capita, \$	1.7	2.7	4.1	14.5	49.6	70.4	114.8	127	137.4

Source: NBB, UNCTAD, author's calculations.

*Agricultural decline.* The Belarusian agriculture is in a problem situation, with profitability just over 2 percent (2.5 percent in Q1'2003). In order to support Belarusian agricultural producers, the government restricts imports, thus forcing Belarusian consumers to pay higher prices for domestically-produced food. The agricultural sector suffered heavy losses due to the government's populist intention to control prices in order to keep up the living standards of the urban population. Huge agricultural subsidies could not make up for the losses even in part. The agriculture is still paying the cost of this policy.



Source: the Ministry of Statistics and Analysis of Belarus.

*Foreign trade deficit.* In 2002, Belarus' deficit with Russia officially totaled \$822 million (ca. 7 percent of the GDP). A major disproportion in foreign trade balance illustrates problems in entering external and retaining domestic markets. Despite the talk of Belarus' great scientific potential, high-tech commodities accounted for just 4 percent of total exports, i.e. at a level similar to that in developing countries. Belarus' main exports to Western countries included raw materials, potassium salts, timber and products such as textiles, that do not require high technology input.

Belarus' exports to non-CIS countries doubled from 1998 to 2002, largely owing to effectively seizing an opportunity for processing more Russian oil and exporting it to Europe, and due to higher global oil prices.

**Table 7. Foreign Trade of Belarus, 1995–2002**

	1995	1996	1997	1998	1999	2000	2001	2002
Total	10367	12591	15990	15619	12583	15972	15626	17078
Exports	4803	5652	7301	7070	5909	7326	7448	8098
Imports	5564	6939	8689	8549	6674	8646	8178	8980
Balance	-761	-1287	-1388	-1479	-765	-1320	-730	-882
With CIS countries	6704	8334	11196	10714	7911	10469	10197	10677
Exports	3027	3764	5379	5160	3622	4399	4491	4461
Imports	3677	4570	5817	5554	4289	6070	5706	6216
Balance	-650	-806	-438	-394	-667	-1671	-1215	-1755
With non-CIS countries	3663	4257	4794	4905	4672	5503	5429	6401
Exports	1776	1888	1922	1910	2287	2927	2957	3637
Imports	1887	2369	2872	2995	2385	2576	2472	2764
Balance	-111	-481	-950	-1085	-98	351	485	873

Source: the Ministry of Statistics and Analysis of Belarus.

Foreign trade figures clearly explicitly show the results of political isolation and the government's failure to reform the economy. In 2002, foreign trade de-

ficit with Russia exceeded \$1.8 billion. The fact that Russia sold mainly energy resources to Belarus points to the Belarusian economy remaining energy-intensive and dependent on prices of natural resources in Russia. Attempts to find new external markets helped the country to reduce the trade deficit. Yet, with the prospect of EU enlargement, the likelihood of keeping the competitive edge of Belarusian products remaining in these markets is low, considering that a lion's share of Belarusian commodities is sold at dumping prices.

### **Problem areas of government control over the economy**

*Macroeconomic instability.* As stated above, the economic policy implemented in Belarus throughout most of the last decade was not aimed at macroeconomic stability. Despite the reported 34-percent annual inflation for 2002 turning out to be at an all-time low for the independent country, Belarus experienced the highest depreciation of the national currency among the post-Soviet nations. However, attempts were made at macroeconomic stabilization, but with each time that political stakes were getting high, the government pulled out of unpopular measures. The first realistic attempt was made in 1994 and 1995 following a 53.5-percent rise of consumer prices in August 1994. It was only then that Belarus started to put an independent monetary policy in place.

With the national currency established, the government began taking measures to prevent money supply from growing. Real-term interest rates reached a viable level, which was sufficient to keep monetary growth in the economy in check. An important component of the government's financial stabilization program consisted in fixing the ruble exchange rate to the US dollar at 11,500 rubles in March 1995. Since prices continue to rise, albeit at a relatively slow pace, and the National Bank sold convertible currencies to all willing buyers at a fixed rate, convertible currency demand lost its thrust and the foreign exchange market stabilized.

At the same time, against the background of a considerably slower price rise, contradictions emerged between the monetary policy of the time and the unreformed real economy. A fixed exchange rate in an inflationary environment spur-

red a growth of prices in US dollar terms. Due to the price factor, unreformed enterprises which manufactured obsolete, low quality products suffered from their competitive edge waning in effect. Late 1995 and early 1996 were the time of a major crisis for Belarus. Enterprises operated only two or three days a week, and hidden unemployment spread throughout the economy.

The government changed its economic priorities in 1996. Governmental agencies focused on supporting the real economy by trying to increase housing construction and agricultural output. Money-printing followed suit, and negative consequences were not long in coming. The CPI rose from 39.3 percent in 1996 to 63.1 percent in 1997, 181.7 percent in 1998, and 251.2 percent in 1999. Real-term interest rates turned negative again, and market forex rates escalated.

The task of keeping the lid on inflation was removed from the National Bank and delegated to the Ministry of Economy, which began to combat price hikes with administrative mechanisms available to it, such as capping markups, the industrial producer price index, prices for so-called 'consumer goods and services of general social import'. This resulted in consumer goods shortages, deteriorating quality, numerous price structure and financial flow deformations.

This state of affairs was further upsed by the fact that the National Bank's legal status prompted it to acting as a market player in the overall game of economic growth rather than safeguarding stability of the national currency. Due to its statutory reporting to the president and the Council of Ministers, the National Bank had to directly support a number of government programs for several years and extend low-interest loans to state-owned firms. Naturally, this led to general distrust in the country's banking sector, the assets of which in 2000 totaled slightly more than \$ 0.5 billion, i.e. the asset size of a Polish bank. In fact, banks served as an ancillary device in the life support system for the state-owned economic sector. A considerable rise in personal bank deposits was enabled only after real-term interest rates overshot the inflation rate again. It took several years for Belarusian authorities to accept the idea that there is immediate relationship between the rise in domestic lending and price hikes<sup>53</sup>.

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<sup>53</sup> The National Bank has and is continuing with a highly contradictory task for itself and other banks, i.e. increasing lending support in the economy and, simultaneously, restricting money supply,

In addition, due to the government's reluctance to curb climbing of forex rates, the National Bank effectively set its official rate plus those of commercial banks. In 1999, the official US dollar rate was three times below the then-black market rate, thus causing a severe convertible currency shortage in the country. For the necessary imports, such as energy resources, medicines, grain, sugar et al, the government required that the exporters sell a considerable part of their hard currency proceeds to the National Bank at the official exchange rate. Control was established over exports and imports. Thus, between 1996 and 1999, economic stabilization and liberalization were brought to a halt. The more the government interfered in the economy the more economic stability was lost, which only strengthened government pressure and exacerbated economic instability.

It was only at the end of 2000 that the government in fact recognized the unofficial ('black') market exchange rate as a the market's benchmark and gradually started raising the National Bank's official rate to match it. The government also restricted inflationary lending in financing agriculture sector and housing construction, and established strict money supply control. The National Bank's refinance rate was raised considerably, and real-term interest rates were jacked up above the inflation.

Macroeconomic stability prospects gained in viability in 2000 and 2001 in result of relative financial stabilization and waning inflation. However, the Belarusian economy proved to be unable to contain these processes even at this slow pace, as provided for in official economic programs. For instance, in the first quarter of 2003, consumer prices reportedly rose by more than 10 percent against an 18 to 24 percent forecast for the entire year. Moreover, the first six months of the year saw symptoms of loosening the macroeconomic discipline. The National Bank increased its direct lending to support the real economy. Given that, in April 2003, the president vested the government with an unrealistic task of reaching an eight-percent GDP growth per annum, prior years' inflationary methods are likely to be used again to boost the economy. Should this be the case, inflation will not take long to accelerate.

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*Monetarnaya Politika v Respublike Belarus (Monetary Policy in the Republic of Belarus)*, by I. Rusakevich, *The Belarusian Economy: From Market to Planning, 1995–2000*, Volume 1, p. 12.

Spurred by high inflation, the economy moved towards dollarization. Until recently, and especially before 2000, the Belarusian ruble was used by the people solely in routine daily transactions, with the trend lasting for several years. All larger transactions were made in convertible currencies, mostly the US dollar, or in Belarusian rubles with prices fixed in the dollar equivalent. Moreover, the Belarusian ruble was not much used for the purpose of saving. Personal bank deposits denominated in convertible currencies largely exceeded those in the Belarusian ruble. The situation changed notably only in 2001 and 2002, when a trend started for ruble-denominated bank deposit rates to be more appealing than foreign currency interest rates. However, there is a genuine threat that the Belarusian ruble's trend of the past two years to appreciate, where currency depreciation has been much slower than price rises, coupled with signs of the government's return to an inflationary monetary policy and the growing import surplus, may provoke a renewed steep decline of the Belarusian ruble in the immediate future.

*Budget.* Belarus' state system of finance is the main source of disequilibrium in the economy. The consolidated budget suffers from chronic deficit which is financed by inflationary methods. Table 8 illustrates a marked quasi-fiscal deficit which is several times above the externally reported figure of the 'official' deficit. In 2000 and 2001, owing to the National Bank's tighter monetary policy, quasi-fiscal transactions reduced in numbers. However, the practice of financing government expenditure from inflation-inducing revenue or, in plain terms, by reaching into people's pockets by spinning the money-printing press, has not been abandoned, yet.

**Table 8. Official and Quasi-Fiscal Deficits**

	1996	1997	1998	1999	2000
Official deficit	-1.9	-2.2	-2.4	-2.9	-0.6
Quasi-fiscal deficit	-3.4	-5.8	-5.0	-4.2	-0.9

Source: *Ekonomika Belarusi: Statistichesky Obzor (The Economy of Belarus: Statistical Review)*, by A. Chubryk, the Research Center for Privatization and Management Institute's Business School, Analytical Report No. 5, Minsk, September 2001.

The Belarusian government's fiscal policy has two distinguishing features. On the one hand, it is irrational in prioritizing government spending. This, above all, applies to social programs. With close to six million people entitled to various benefits, their average amount does not exceed a few dollars per capita. Consequently, government programs cannot cope with combating poverty. As seen in Table 9, the main path in income redistribution via the State and its social programs is 'from the poor to the rich', the only exception being subsidies to maintain low food prices that, at any rate, have been dramatically reduced lately.

**Table 9. Distribution of Social Benefits to Households by Quintile Groups (Quintile groups ranked by the total amount of social benefits received)**

Quintile group	Bottom	Second	Third	Fourth	Fifth
Food	2	3	1	4	5
Public transport	5	4	3	1	2
Public utilities	5	4	1	3	2
Drugs	5	4	2	3	1

Source: Choices for the Future, Belarus National Human Development Report 2000, p. 45.

The table ranks the quintile groups by amounts of social benefits received. For example, rating in 'Drugs' suggests that the highest consumption is attributed to the wealthiest and the lowest level to the poorest (the fifth quintile group).

On the other hand, this government's fiscal approach to all undertakings irrespective of their form of ownership results in a high level of taxation, approximately 40 percent of GDP. This, above all, stems from the large number of elevated taxes. There were a total of 39 various taxes at the national and local levels in 2001. That is why tax evasion has taken on mass scale; consequently, diligent taxpayers have to shoulder yet a heavier tax burden. In addition, the high level of taxation forces businesses into the shadow economy, which in certain sectors has already equaled the official economy in value terms.

**Table 10. Share of the Shadow Economy by Sector, as a % of Official Levels\***

Sector	Average percentage
Goods	55
Services	65
Construction	80
Trade	55
Transportation	66

\* The percentage indicator shows the share of the shadow turnover in the sector against the official one. For instance, the construction sector's unofficial turnover totals 80 percent of figures captured in official statistics.

Source: *Usloviya dlya Chastnogo Biznesa v Belarusi (Conditions for Private Enterprise in Belarus)*, by P. Daneiko, *The Belarusian Economy: From Market to Planning, 1995–2000*, Privatization and Management Institute, Minsk, 2002.

Among other factors, this state of affairs is due to absence of a realistic approach in formulating and implementing the budgetary policy, as illustrated by frequent overestimates of the economic growth and budget revenue. The resulting budget gaps are mostly offset by new taxes and customs duties being launched, predatory customs methods and – a recent phenomenon – downright extortion of contributions from various social groups, from business owners to students.

The existence of special purpose undertakings that report to president's governmental agencies which in turn control the most lucrative financial and commodity flows, coupled with un-accountable presidential and off-budgetary funds – whereby the 'official' budget automatically loses a considerable part of lease proceeds – forces the government to tighten its budgetary and financial policy even further.

*Methods of controlling the economy.* Belarusian economic liberalization of the early 1990s was forced by pressure from the external environment and influen-



led by examples of the neighboring countries. This may explain the government's indecision and half-hearted measures pursued in market-oriented reforms in Belarus. A large-scale price liberalization was in fact a knock-off effect of price liberalization in Russia with which Belarus shared the ruble zone at that time. However, despite declarations of moving towards free price formation in January 1992, prices for so-called 'goods of social import' such as bread, meat and dairy products, products for children, utilities and transportation – continued to be regulated. With economic ties severed with former USSR republics, foreign trade was liberalized at a relatively fast pace. At the same time, the Belarusian government was very reluctant in abandoning the centralized public procurements system for domestic market needs. Public procurements of industrial goods were eradicated in 1994, while the practice still continues in agricultural products and government control over the consumer/retail market. A large-scale economic liberalization promised by President Lukashenka in 2001 has in fact materialized only in the form of partial price liberalization. Between 1999 and 2003, the list of government-regulated prices was cut from 33 to eight items.

The government continues to throw stumbling blocks to the development of private enterprise. These include:

1. Lack of legal guarantees for private ownership and their relevant statutory regulation. However recognized – as officially asserted – private ownership does not enjoy true protection. Private and NGO property is subject to arbitrary confiscation by governmental agencies, as testified by the government's right to introduce its golden share in private companies and instances of its retro-active application, ordinances resulting in squeezing small-scale wholesale and retail operators from business with no compensation for the losses, President Lukashenka's decree allowing extrajudicial appropriation, orders to contribute property and funds as required by State needs, e.g. for sowing and harvesting campaigns, etc. This state of affairs discourages both domestic and foreign business communities from investing in the Belarusian economy.
2. Ambiguous, inconsistent, unpredictable and unstable regulations. For instance, there are about 280 laws, bylaws and ordinances that apply to

pricing. Fiscal and accounting regulations change several times in a year. This entails additional transaction expenses for conducting business. The situation is mainly due to the president's decision-making monopoly, as Lukashenka has usurped the right to issue edicts and decrees superior to laws passed by the legislature.

3. Excessive bureaucratization of the economy. The government continues to impose new barriers for starting-up private businesses. This may be illustrated by the need to obtain a license for ca. 180 types of business activities, and restrictions on private enterprise in sectors where the government endorses the interests of State monopolists.
4. Support for the predominant status of the state-owned sector. Statism in the Belarusian economy increasingly engenders crisis trends. Private business generates just over 20 percent of the country's GDP, i.e. the least among the region's transitional economies.

Denationalization and privatization peaked between 1991 and 1994, yet they were spontaneous and unorganized processes at the time. The government auctioned off enterprises or allowed for employees of a contractor-run enterprise to buy it out. Large enterprises were transformed into joint stock companies in which the government retained a stake, with the other shares distributed among the employees and put up for general sale.

Despite 1993 and 1994 being widely regarded as the golden age of Belarusian privatization, the years did not yield impressive results. A government program envisaged turning two-thirds of fixed assets in undertakings and organizations into non-State property in terms of value, including 10 percent in 1993. In reality, a paltry one percent of all State property was denationalized and privatized throughout year. In 1994, the government set out the ambitious target of privatizing 20 percent of all State property. However, after Alyaksandr Lukashenka's election for president that summer, the Belarusian authorities' approach to privatization changed radically. The Auditing Chamber started scrutinizing the rightness of privatization projects carried out in 1991 and 1992 according to standards established in 1994. Authorities started to annul municipal property auctions. By September 1994, about half of the targeted enterprises had been

withdrawn from the process of transformation into joint stock companies. Although Belarus' privatization did peak in 1994, only one-fourth of the targeted 20 percent of the fixed assets changed hands in result of the reform that year.

The following year, privatization was on the wane. In March 1995, the government revoked the licenses of all the 37 specialized investment funds set up to carry out coupon privatization. The president signed an edict titled 'On the Regulation of State Property Management', whereby all transactions involving State property exceeding 10,000 times the minimum monthly income required presidential endorsement. The State Property Ministry was thereby restricted in its powers. In the summer of 1995, due to the industrial sector's crisis, the trend was to re-nationalize. Employees of several joint stock companies who experienced pay delays petitioned the government to restore state ownership in their enterprises and provide them with support and preferential treatment. On January 1, 1998, the president proclaimed the State's right to the golden share that entitled the government to determining the corporate development strategy even with a minor public stake. The country's macroeconomic situation changed considerably. The government's inflation-inducing monetary policy and less rigorous tax and social security deductions from state-owned enterprises were conducive to preserving state-owned property status, which further abated the privatization process. A mere 94 enterprises changed their form of ownership in 2001, as compared to 177 in 2000, 307 in 1999, and 329 in 1998.

A total of 5,476 undertakings were reformed in terms of ownership between 1991 and 2001. Of this number, trade operators totaled 25.1 percent (1,372 entities), with 12.9 percent (707) in agricultural undertakings, 12.2 percent (670) in utilities, 10.4 percent (569) in industrial enterprises, 9.9 percent (536) in retail services, 4.9 percent (270) in public catering establishments, and two percent (112) in transport and communications.

In 2002, deceleration of inflation, increased fiscal pressure on businesses, rise in the real foreign exchange rate of the Belarusian ruble, increase in the dollar equivalent of monthly income, the resulting dampening of competitive strength, and greater numbers of unprofitable enterprises elicited renewed interest in ownership reforms, soliciting strategic investors and in privatization in

general. The government initiated joint stock company transformation of national petrochemical giants such as Azot and Khimvalakno in Hrodna, Palimir and Naftan in Navapolatsk, the Belshyna tire factory in Babruysk, the Horizont television factory and the Beltransgaz gas pipeline operator under pressure from Russia. However, the government is still reluctant to go ahead with privatization. In most cases, it offers small stakes for sale, intends to retain control over the enterprises by imposing numerous additional conditions for the prospective buyer. Some of these conditions seem absurd. For instance, Baltika, a leading Russian brewery, was told to build an ice-hockey arena 'for workers' when expressing interest in acquiring the Krynitsa brewery in Minsk. There is a realistic threat that if this approach to privatization continues, investors will be hard to come by in a few years, if at all, as the financial condition of enterprises due in for privatization deteriorates and their production facilities soon wear out.

## Reform Incentives

### Price of reform delays

Inevitably, the fundamental incentives in opting for an economic development strategy are driven by aspirations to attain higher living standards, establishing a favorable environment that would foster societal development founded on the well-being of each individual. As stated above, the existing economic model cannot contain these needs. This begs a question of what there is to be lost and won for Belarus if the country eschews economic reforms and preserves the existing economic model for as long as possible. In our opinion, key effects of shunning reforms are the following:

- A chronic lagging of Belarus behind developed Western countries and its immediate neighbors with starting conditions similar to those of Belarus of a few years past. Belarus has lost its reputation of the most rapidly developing former USSR republic; instead, since 2000, it ranks among the region's slowest economic growers. In 2001, it had the lowest economic growth rate among CIS countries. To prove the alleged Belarusian economic miracle, it has become common practice for government statisticians to compare Belarusian indicators with those of Russia to show advantages of the official economic course. However, the same approach may now be used to reveal the drawbacks and potential negative consequences of the strategy geared at putting reforms on hold. Economic stagnation will

turn Belarus into a lesser developed, Third World-type country. Technology and know-how disparities between the nation's economy and those of the developed Western countries or even the neighboring nations will widen. Belarus has already begun losing the capacity to position itself in the international labor market and adapt to global economic processes. The country's economy is becoming highly exposed to external crises; in fact, it is turning into a transit Third World periphery, with all the economic ailments characteristic of such countries.

- Given the market orientation of the neighboring economies, the Belarusians' belief in the Soviet-style mode of living, fostered also throughout the last decade, and its possible continuation may be a fallacy. The government has already proven to be incapable of ensuring an appropriate degree of social security and subsidizing out-of-pocket payments for social services. Belarusians may find themselves in a situation where socialism is ultimately wiped out, and a market-based system spurring them to shoulder responsibility for their own living conditions and income is not yet established due to the current government's anti-market policies.
- Belarusians will have to live in increasing poverty. In 2001 and 2002, the decline in living standards became increasingly noticeable. In January 2003 alone, real-term personal income dropped by some 10 percent. Given the financial standing of industrial giants, a sharp rise in unemployment seems inevitable. In these circumstances, degradation of the Belarusian society, a demographic crisis, self-destruction of the nation's intellectual potential and brain drain may potentially assume devastating proportions.

### **A market reform model: motivators behind the options**

One important motivating factor in choosing an economic reform strategy is the desire to see an operating and efficient economy, capable of ensuring the country's sustainable development. Lessons learned from previous reforms in

post-Communist countries suggest that not all reform models may be best suited for achieving this goal.

Transitions of former socialist countries spawned two types of market economies. One of them can be defined as democratic capitalism. This economic system is mostly characterized by stable, transparent and fair rules of the game for all market players. It emerged in Central European and Baltic states whose political and economic systems copy patterns of Western democracies in their basic aspects. Success of these countries' economic models is attested by their accession to the European Union, OECD and NATO.

The basic precept for democratic capitalism is the individual whose well-being can be realistically achieved in an economic system founded on economic freedom and private ownership. Free market and private enterprise make up a system of incentives for participants of economic process that enable satisfaction of personal aspirations and interests of people by producing goods with value adequately determined in free exchange, this being the free market principle, and whose income and property are protected from confiscation, this being the principle of inviolability of private property. The main function of government in this system is to protect ownership rights and ensure compliance with contractual obligations, which sets the stage for a stable and predictable economic growth. The government's social function is anchored in the principle of assisting those who are in actual need of welfare, rather than in unsystematic distribution of resources which frequently enriches the wealthy and impoverishes the poor.

The other model born in transition is referred to as oligarchic capitalism. It is characteristic for government's excessive interference in the economy so as to further interests of a small group of people in power or those enjoying preferential treatment from government, as well as by widespread use of administrative methods in controlling economic processes. Oligarchic capitalism has taken root in Russia, the Ukraine, most of other CIS countries and some European countries. This model serves not so much general public interests as those of a certain group of people claiming the right to speak on public behalf who amalgamate with State bureaucracy by using mechanisms of clientage and corruption.

Oligarchic capitalism is spawned mainly by half-hearted, 'doctored' economic reforms. Unlike the comprehensive economic reforms which breed a system of well-founded economic motivators for individuals and undertakings, warrant circulation of unbiased information on the economic situation and establish risk-reducing institutional mechanisms, 'doctored' reforms result in there being a hybrid model with features of a market economy, albeit in a system of business incentives suggesting that the success of private enterprise depends almost entirely on 'snouts at the trough' strategies, access to distribution of public funds and resources that may fall into private hands only by bureaucratic permission. This system dampens motivation for creative work, as all undertakings thus fall into two categories: those on the receiving end of government privileges and those cramped by the government for the benefit of the privileged. It is precisely this model that engenders the notorious practice in Russia of delaying payments to doctors and teachers despite oil prices (Russia's key export commodity) currently standing at \$30 per barrel, in a country boasting its billionaires. Belarus' incorporation into the Russian Federation will i.a. lead to entrenching the model of oligarchic capitalism, thus dooming the nation for Third World status for years to come, if not permanently.

### **The pro-European option and European integration as an incentive for economic reforms**

Europeanization of the Belarusian economic model is the fundamental factor enabling a civilized pro-European choice for Belarus. The European integration of Belarus cannot happen without restructuring the economy and public governance aimed at facilitating complete integration with the European economic space. This goal could be achieved through an economic strategy aimed at establishing a functional market economy capable of sustaining competitive pressure in the single European market. Internal adoption of EU laws would cause domestic economic processes to be regulated along the same standards as in the European Union. In macroeconomic policy terms, the country's monetary and lending system should meet the criteria set for accession to the



European Monetary Union. These are the following: high degree of price stability (with deviations not exceeding 1.5 percent of the average European level), capping public debt at 60 percent of GDP, stable interest rates and a stable exchange rate.

Certainly, there are hindrances on Belarus' way towards Europe. The main ones are inherent in the country. To join the European home of nations, it is necessary to ensure that its values, rules and standards become common practice and part of tradition in Belarus. This is a complicated and lengthy process requiring strong political will inside the country as well as the government's consistent efforts in enacting proper laws and establishing adequate political and market institutions. Another barrier is on the European Union's side. The difficulty of the task is due to the fact that the Belarusian public will have to overcome EU skepticism about this country. However, it is possible if, above all, the Belarusian society becomes inherently European, i.e. reaches civilization and cultural standards characteristic of any democratic country with a market economy and due respect for democratic freedoms and human rights.

Major factors that will determine ways of rapprochement between Belarus and the European Union will include the presence of political will in the country to go ahead with radical economic reforms. If this is in place, Belarus will be able to have an efficient economy capable of ensuring long-term economic growth.

In this event, the nation might choose between joining the EU and building its relations with it, as does Norway for instance. However, in either case the country's alignment with European laws would proceed rather quickly. Adoption of some of the *acquis communautaire* that would negatively impact business incentives could be postponed, or it could be adopted in more liberal versions. Adoption of European laws, or the opportunity to assume responsibilities of an EU member state, i.e. application of the *acquis communautaire*, would not only mean that Belarus may enjoy membership in the Union but also, if not chiefly, that the country has put an efficient economic policy to work.

The goal of ensuring sustainable development of Belarus and the country's Europeanization would be attained if the country adopts an economic strategy based on the following principles:

- **Market economy.** In the future, the Belarusian economic model should certainly be based on the tenets of private ownership and free market. This implies maximum privatization of state-owned property and curbing government interference in the economy. Low living standards on the one hand and global economic realities, of which Belarus will inevitably be part on the other, suggest that the country will not have strong government, which currently redistributes up to 50 percent of GDP, especially given that the Belarusian economy is yet to receive powerful impetus for a civilized development. In the foreseeable future, Belarus is likely to have to diminish the role of government, whose interference in the economy would whittle down to a few basic functions plus an inconsiderable role of welfare provider.
- **Openness.** Being a small economy, Belarus will have to be integrated with the international market. Its ability for successful adaptation to a highly competitive market environment will depend on the degree to which the government's economic policy will promote international integration, open the country for trade and investments, free movement of goods, services and capital. An economic strategy based on aspirations to autocracy, domestic market protection, import restrictions, and excessive expectations for public support would be a dead-end policy sidetracking the economy into stagnation.
- **Competitiveness.** This implies economic de-monopolization and furthest possible reduction of government intervention otherwise aimed at restricting business operations, nurturing and keeping 'national champions' afloat and supporting selected companies. Competitiveness of the Belarusian economy is the pre-condition for enhancing competitive strength of undertakings by fostering a system of incentives geared at stepping up efforts in productivity, investments and innovation.

With these conditions in place, public oversight in the economy should be based on the following principles:

- **Rule of law.** Economic processes should be regulated by acts of Parliament, rather than bureaucratic directives of the executive. The govern-

ment's key function should be to safeguard ownership rights and fulfil contractual obligations.

- **Transparency.** An economy can be efficient only if it functions on a level playing field for all undertakings. Decision-making in the economic policy should be transparent and accountable to the general public instead of being hinged on isolated interests of those closely connected to bureaucrats who leverage government's intervention in the economy for furthering their own business agenda. Discretionary powers of the State machinery, such as the arbitrary right to grant various privileges and concessions, state aid, access to public resources etc. should be minimized.
- **Stable and predictable regulations.** Undertakings operating in a market environment should be rid of excessive transactional expenses due to frequent and arbitrary changes in regulations governing business activity.

These principles are implementable only in an efficient democratic system warranted by genuinely independent legislative and judicial powers, and with public oversight of political process.

# 2

## An Ideal Economic Model for Belarus

by Uladzimer Kalupaieu  
and Uladzimer Valetka

Below is a description and clarification of a market economy model that is alternative to the one currently in force in Belarus. The proposed model envisages tapping into the country's domestic potential and latent opportunities; it is underpinned by the principle of an open economy. It would enable FDI flows into the Belarusian economy and ensure its growth within the shortest possible time, thereby raising living standards.

### **Economic reform objective**

The need for economic reform ensues from the fact that, with ongoing liberalization in international economic relations, closed economies i.e. those lacking modern technologies and management methods are fundamentally unable to compete with developed countries in domestic and international markets alike. With economic openness, conformity to patterns of international division of labor and high asset productivity as pre-conditions, high living standards may be a reality.

To achieve such living standards is the main objective for Belarusian economic reforms.

### **Fundamental economic model principles:**

- economic efficiency, which cannot be attained without a free market and private ownership. One of the necessary conditions in this regard is a har-

monious interaction between the government and market players, where the government contributes to enhancing efficiency of market operations by setting up an appropriate legal framework and market economy infrastructure.

- free competition; above all, this implies free market access for undertakings, guarantees for and protection of a level playing field for all market players. This leads to legalizing ‘shadow’ businesses and abolishing preferences enjoyed by ‘law-abiding’ state-owned enterprises.
- maximum openness, meaning not only transparency of limits to enterprise, but also openness in a broader context of traditions, business practice and the law, as technological progress is contingent on harmony in political and economic relations.

In addition, this model calls for undertaking an efficient social policy which should be purpose-specific to the maximum possible degree and tied to the degree of economic performance. In general terms, this implies the priority of generating the nation’s wealth over its distribution.

In the proposed model, a market economy is primarily viewed as safeguarded economic freedom that manifests itself in:

- the right to increase personal wealth at one’s discretion (freedom of consumption);
- the business owner’s right to use their time, labor, funds and entrepreneurial skills at their discretion (freedom of business, freedom of choosing occupation and place of work, freedom to use property);
- the right of entrepreneurs to manufacture and sell goods at their own risk (freedom to manufacture and trade);
- the right of each buyer and seller of goods or services to achieve the desired purpose (freedom of competition).

These freedoms may only be limited in cases of breach of third sector’s rights, constitutional provisions or legally established civilized rules of the game for engaging in business.

As expounded on in Sections 1–4 above, the legal framework in this economic model should contain provisions that foster choices and are related to the

flow of goods, free movement of people, freedom to provide services and liberalization of capital flows.

One fundamental principle for this economic model is that economic freedom is an integral part of political freedom, and only in a developed democracy can one assess, formulate and modify business-related provisions and regulations that prove inefficient in business practice. Economic freedoms should also be combined with responsibilities: the government should be responsible for economic policy-making and stable market operation; the National Bank should ensure a stable currency, and private businesses ought to focus on results of their economic operations.

The essence of the described model is in multiple exercise of the fundamental business transaction – that of buying and selling to mutual benefit of the parties. For this purpose, it is necessary to enable the following:

Firstly, both the seller and the buyer should know what it is exactly that they possess and what they can acquire. This calls for specifying and protecting the ownership rights system by means of the law.

Secondly, there is a need for certain formalized transaction methods to be put into place that ensure performance of buy and sell contracts, and settlement of resulting disputes. For this, there should be contracts, laws, courts, a commercial code, etc.

Thirdly, it is necessary to keep account of what market participants transact, hence the need for a system of accounts and records allowing for monitoring asset and liability movements, corporate earnings, revenue, expenses and profit trends.

Fourthly, in order to avoid barter, which dampens manufacturing productivity and prevents adequate evaluation of changes in customer needs, market participants should have a stable currency acting as legal tender, accounting measure and means of accumulating wealth.

Putting the aforementioned conditions in place by government, combined with further development of market relations, will bring about a developed banking and financial system which will ensure the operation of businesses and insurance and advertising industries.

Thus, successful development of a market economy requires stable and efficient basic market components such as competition, the institution of ownership, small businesses, a banking sector with sufficient lending resources, flexible labor and capital markets, labor market movements, a stock market, pension and investment funds, etc.

A stable and transparent operation of these market infrastructure components and the enactment of unambiguous laws and regulations to govern economic activities will contribute to minimizing expenses related to conducting lawful business transactions (transaction expenditure).

### **The role of government**

Regulations that govern the operation of market players will be developed with maximum participation of the Parliament and non-governmental organizations, rather than merely ministries and other governmental agencies that are not interested in increasing their current regulatory workload or being truly accountable for the documents they issue. To prevent the cost of setting up and running a legal framework that governs business operations from exceeding their actual economic effect, plans are designed to achieve maximum clarity and transparency of the legal framework and market institutions, and to clearly describe and specify government functions.

### **Peculiarities of reform**

Many Belarusians believe that it is easier to endure financial hardship in a non-market economy than in a market one on the premise that ‘we’re all in this together’. The economic policy pursued by current government contributes much to tenacity of this conviction.

Belarusians will not be able to discard this stereotype without an economic revival and effective implantation of market institutions and principles in all their relevant aspects.

In contrast to the idea of market relations as stated before, the focus is on a broader interpretation of their social function, ensured both by normative ele-

ments (the constitution, general rights, laws, system of regulations) and informal methods of enforcing market rules.

Aside from limitations inherent in an economy (limited resources), legally set standards and limitations should establish a system of economic incentives and trends for efficient economic growth.

Entrepreneurship and the ability to learn are long-lasting personal qualities and Belarusians certainly have not lost them. Yet, decades of the Communist rule have distorted notions and standards characteristic of market behavior. In order to truly embed standards of market behavior, effective statutory mechanisms must be laid down to discourage disruption of market relations. This primarily calls for a judicial system reform with a view to restoring public trust in the law, confidence in its effective operation and enforcing accountability for one's acts. If a power, especially the judiciary, is not competent and independent, enacting good laws will help little if slack compliance undermines confidence in them.

The civil service reform is yet another prerequisite for economic transformations; it should be embarked on to warrant loyalty and stability of state machinery in implementing reforms and stabilization efforts. Measures should be taken to improve skills of government officials and reduce their numbers. Financial incentives to civil servants would be an important factor in increasing their liability for consistent implementation of economic policies and regulations.

Consequently, undertakings would be issued with established rules of the game that would prevent profiteering at the customer's expense. Failure to comply would entail business closure.

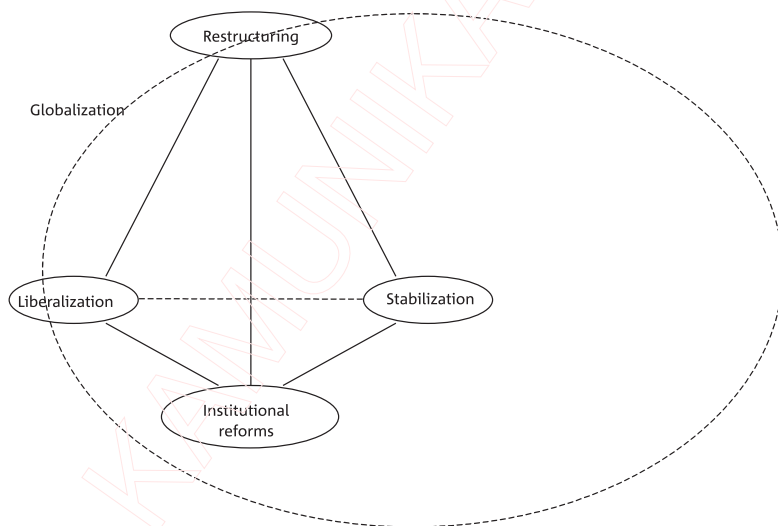
The model's fundamental ideas and long-term advantages would be communicated to the general public via the media, schools and at training and retraining courses. The objective is to encourage business initiatives in people that run counter to expectations of better living standards being provided by the State, rather than individual work and entrepreneurial efforts. Initially, it is necessary to research possible ways of arguing with the general public to explain who benefits from the absence of market mechanisms and is interested in preserving low transaction costs. The government would vow accountability for reforms and publish a program with measures to alleviate their social consequences.



## Reform program

Implementation of an economic model, once selected, entails the following reformist actions: 1) liberalization of economic relations; 2) institutional reforms and establishment of a system that complies with market economy principles; 3) macroeconomic stabilization; 4) structural transformation of the manufacturing sector and the economy at large. All elements of the transformation impact one another simultaneously, are influenced by other areas and aspects of reforms (so-called transformation tetrahedron).

### Illustration. Market Reform Directions in a Globalized Environment



Effective structural transformations in the economy would only be possible as a result of successful implementation of other types of reforms. In addition, all transformation efforts are subject to controversial influence of globalization.

In all the aforementioned aspects, reforming implies relentless and consistent rapprochement to a liberal market economy through methodical continuation of previously started reforms.

**Liberalization** should include:

- ultimate abolition of remaining administrative centralized control of the economy, transition to planning at the level of undertakings, optimized operation of governmental agencies (e.g. currently, there exist seven concerns and three ministries governing the operation of 2,500 enterprises in the industrial sector alone);
- business deregulation, i.e. exercise of the principles underlying the freedom of establishment, level playing field, and competition among market participants regardless of ownership status;
- transition to deregulated pricing, including ‘prices of goods of social import’; gradual increase of out-of-pocket payments for utilities and public transportation to match 100 percent of the cost, with parallel reduction of government spending for these sectors. Prices fixed by natural monopolies would be under public control. Public procurements would be allowed only if made at market prices;
- elimination of various State monopolies including utility services, transportation, energy supply, healthcare and education by means of privatization and free access of private operators to these sectors;
- foreign trade liberalization, abolition of import duty on foods, reduction of import duty on other goods from 10–12 percent to the average prevalent in EU member states and WTO (four to six percent); elimination of non-tariff foreign trade restrictions such as licensing, quotas, complicated procedures for certification, transportation, etc.; recognition of international standards and quality certificates;
- freedom of wealth formation and use of disposable income;
- expansion of the free market area by developing markets other than for goods and services: labor, real estate, capital, information, advertising, insurance and social services.

The objective for liberalization is to lay foundations for market self-regulation, itself the basis for fostering competition as the most efficient system of distributing resources, encourage efforts to improve the quality of goods and services and increase efficiency in the use of manufacturing assets, and turn effective demand into the single most important regulator of growth rate and output mix.

To ensure that market players enjoy economic freedoms for the consumer's benefit and do so in the most efficient way, it is necessary to reach macro-economic stabilization along with institutional reforms in the economic system that sets out rules of the game.

Market institutions and infrastructure should develop along the following lines.

1. **Privatization** (reform of ownership relations) and establishment of an efficient system to protect owners' rights, effective creation of a land market and housing privatization.

*The privatization concept.* Regulation of ownership relations and establishing rules to be applied in State property restructuring and privatization is key at the time of market transformation. If restructuring does not bring about its logical effect, i.e. emergence of a competent owner, a reasonable economic policy is out of the question because any economic policy in that case would be detrimental to the economic interests of that kind of owners in effect. By seizing a market niche, such an owner is ready to reinvest their earnings and may be partnered with the government in industrial restructuring.

The emergence of a competent owner is currently impeded in Belarus by:

- procrastinated privatization, or sectoral agencies' efforts to slow down the ownership reform in enterprises within their remit, as privatization narrows the scope of undertakings under their control. Only 25 out of the initial 145 state-owned enterprises (17 percent) were restructured in 2001 against 44 percent in 2000, and 62 percent in 1999;
- flawed and unstable regulations that govern private enterprise;
- flawed regulations governing privatization (limited methods, no levers against state-owned enterprise managers' efforts to hamper privatization,

- questionable asset valuation and property appraisal system, imposition of a heavy social/welfare burden on new owners);
- government intentions to use privatization proceeds merely to solve current financial and other problems, particular to bridge budget gaps or dispose of unprofitable plants.

However, privatization is the best method for economic recovery, as private investors are the ones most capable of analyzing market opportunities in the most adequate manner.

The following privatization rules could be proposed:

- viable medium-sized and large state-owned enterprises should be restructured and privatized under the supervision of a special agency accountable to the Parliament (for instance, the Privatization Department) and reporting to the relevant sectoral ministry;
- Uncompetitive, resource-intensive and environmentally hazardous enterprises should be shut down. This also applies to inefficient links in technological chains that may be substituted by foreign suppliers. This should be a gradual process the social consequences of which should be alleviated at every opportunity.

To privatize consistently, it is necessary to:

- prioritize the Privatization Law over all other acts governing privatization;
- abandon the approach to transforming state-owned firms into government-controlled joint stock companies whereby it is seen as special and ultimate form of denationalization; rather, it should be regarded as an interim privatization stage;
- ensure efficient application of the bankruptcy procedure to guarantee that the bankrupt enterprises and entities interested in keeping them afloat will be able to use all economically viable methods to continue manufacturing and other types of business;
- opt for ‘cash’ privatization on a competitive basis as the main privatization method; refrain from granting any privileges to employees of companies under privatization. In tune with the principles of market econo-

my and justice, it is necessary to ensure that '*mayomast*' (property) privatization coupons are used as a means for investment solely at auctions, along with the underlying funds, rather than exchanged for shares at par. In addition, it would be advisable to allow the use of '*mayomast*' coupons for privatizing housing stock by tenants.

- lift the ban on the sale of shares previously acquired by private individuals on preferential terms, abolish the golden share rights;
- simplify the privatization procedure. Existence of two separate agencies for restructuring and sectoral issues is by no means justifiable. Insofar as possible, the role of governmental agencies must be reduced as, by the sheer virtue of controlling entities, they are not interested in seeing them privatized. The right to the final decision to privatize should be delegated to the Privatization Department which could be established as a successor to the Department for State Property Management at Ministry of the Economy;
- ensure a level playing field in privatization rights for foreign and domestic players. Should the new owner guarantee capital expenditure on fixed assets, the asking price of the enterprise due for privatization could be reduced;
- allow potential new owners to use borrowed funds for privatization purposes;
- promote market valuation of enterprises under privatization by appraisers independent from potential buyers and the government. Enterprises with a market value close to zero should be sold for a token payment;
- reduce to three years the deadline for petitioning for contracts to be ruled void.

Efficiency of reforms aimed at stabilization largely depends on underlying financial support. That is why cash privatization proceeds should be collected in a special privatization fund that should be part of budget revenue. Proceeds from this fund and foreign loans would be used for social reforms, stabilization measures, and increasing foreign assets in the banking sector. At the same time, high debt would impede growth in privatized enterprises. In order to offset mu-

tual debt between enterprises, the Privatization Department should develop a system for debt payment by enterprises with a more stable financial position, i.e. those where receivables exceed payables. Debt could also be settled from proceeds of the privatization fund, whose additional source of finance would come from asset sales of bankrupt enterprises.

Trade arrears in enterprises where payables exceed receivables could be netted by offering a stake in these indebted enterprises to commercial banks, should they find it beneficial. In exchange for loan payments due, the lending banks would be given shares. It would be advisable to restrict participation of government-controlled banks in these transactions.

2. **Land Reform.** The objective of land reform is to create conditions for farmers to choose forms and methods of land management, to be provided for by the Land Code. Private ownership of land would be introduced. In rural areas, land and other assets would be handed over to private owners with no compensation by means of distribution in the form of land and property shares. New owners would have the right to:

- a) quit the collective or state farm, withdraw their land and property shares, start their own farms or joint agricultural undertakings;
- b) delegate the right to manage their property to a newly elected management of an agricultural cooperative replacing the local collective farm, with the prospect of receiving a share in the profit generated by management of business,
- c) lease out their land and property shares,
- d) sell their shares.

Land Register (cadastre) appraisal of the country's land resources would be completed. Owners who possess land in excess of an established standard (one to three hectares) would pay property tax of no less than two percent of the land market value irrespective of land use.

## **Institutional measures**

The government would regulate business activities, i.e. develop and enact regulations to establish rules of behavior and relationships among market partici-

pants in production, financial, external economic and other relations, for which it is necessary to adjust the civil, commercial, fiscal, budget and land codes. This would eventually lead to laying down business rules in tune with market economy principles, including the legal basis for protecting ownership, for bankruptcy, competition, antimonopoly activity, protection of rights of investors and contracting parties, insurance business, etc. All ownership rights should be firmly warranted by the law, safeguarded from breach and protected by the State.

The government would promote genuine competition in the economy at large, a natural stimulus for businesses to improving the quality of products, increase output, boost labor productivity, reduce primary costs and lower prices. Regulations concerning state competition policy should above all govern agreements concluded with a view to restricting market access and operation of state monopolies and state-owned enterprises that enjoy preferential treatment.

In this regard, the government would harmonize the 1990 Law 'On Enterprises in the Republic of Belarus' with international standards and enact regulations governing intellectual property rights.

An economic and legal environment would be established for the growth of market participants well adapted to market conditions and able to operate in a market environment efficiently. These include undertakings, research and development organizations, banks and investment funds, stock exchanges, brokerage houses, dealerships, employment centers, insurance companies, social security and pension funds, auditing and consulting companies, advertising agencies, etc. The government would facilitate market access for newly established undertakings, i.a. by way of a simple notification principle in registering small businesses.

Institutions and new rules would be established for implementing the State's social and economic policies at various levels of government (national, regional, and local). The main objective here would be to develop local government and self-management, delegate powers to this level along with funds necessary to solve local problems and satisfy major social and economic needs of local communities.

The government would establish and foster non-State bodies for regulating the economy and the market, such as trade unions, business community, con-

sumer organizations, scientific associations, etc; develop international institutions, improve the system for staff training and retraining with a view to developing a sense of responsibility for personal career among labor market participants who would be capable of thinking strategically, operating in a global market environment and oriented towards innovation in production.

It should be borne in mind that liberalization measures geared to reform the economic system may be embarked on instantly, e.g. import duty could be abolished as soon as a law is enacted to this effect, whereas institutional transformations are a medium-term process at the least. To prepare and comprehensively examine institutional innovation, put it to effect, detect and remove shortcomings, establish efficient market institutions is a time-consuming effort. Reform of the real economy, i.e. restructuring of the manufacturing sector, is the lengthiest part of reforms. Changes should be instituted in parallel and according to a systematic program.

The length of transformation depends in equal measure on efficient establishment of market institutions and macroeconomic stabilization, to be conducted in parallel to launching the market institutions.

## **Stabilization**

The following actions should be taken to stabilize the economy:

- a) price reform;
- b) currency reform and a sustainable monetary policy;
- c) tax reform and a balanced fiscal policy;
- d) a market-oriented income policy.

Ad a). Price reform

No government can fully satisfy consumer demand and please all consumers. Absence of an effective price system prevents consumer preferences from being identified. The goal of the price reform is to deregulate prices and limit administrative intervention in the economy. The government should retain control over electricity, gas, heating, public transport and telecommunications prices for some time. Prices will differ depending on consumer groups and the



level of consumption. Electricity and heating rates to the residential segment will be higher than those for industrial consumers. Yet, simultaneously, subsidies to manufacturers will be replaced by household subsidies which will be phased out as incomes increase. In result of the reform, subsidized and market-based prices will gradually approximate the same level.

#### Ad b). Currency reform and monetary policy

A strong national currency is a pre-requisite for achieving economic growth and competitiveness, and for consolidating positions in the global marketplace. A government-forced growth of output via currency depreciation will not help to address the main issue of overcoming technological backwardness, boost productivity and set the stage for raising living standards.

Belarus is the only former Soviet republic lacking a truly sovereign national currency; in fact, preparations are underway for replacing it with a foreign currency. The country has no treasury to speak of since the annual inflation has been in excess of 30 percent ever since Belarus gained independence. The lending system is underdeveloped because of the ruble depreciation.

Since expectations concerning the inflation and depreciation of the ruble are high and set to continue, the main criterion for selecting a monetary policy should be its efficiency in achieving monetary stability.

This is possible by adopting a strict currency board regime. The National Bank should stop printing money. To make this regime effective, the currency board holds foreign currency reserves (or gold or some other liquid asset) at a fixed exchange rate equal to at least 100% of the domestic currency's value. The central bank may issue currency only for converting domestic into foreign currency. When buying foreign currency to support the ruble, the National Bank withdraws the corresponding amount from circulation. This will help to approximate domestic inflation and interest rates to those of the country whose currency the ruble is pegged to.

The currency board should be established by the law 'On Stable National Currency', which would ban government interference in monetary policies. This would prevent the government from demanding loans supporting the economy when monetary policies are tightened.

High inflation in Belarus is not attributable to monetary factors alone. It is also related to high manufacturing costs resulting from lack of competition, non-productive manufacturing technologies, excessive fixed asset depreciation, insolvency crisis and barter settlements.

The currency board system should be accompanied by a fiscal reform, tight budgetary constraints on undertakings and adoption of a balanced budget to prevent Belarusian goods from losing their price-related competitive edge.

There are two relatively stable currencies, the dollar and the euro, to which the Belarusian currency can be pegged. Although the US dollar dominated Belarus' foreign trade in the last decade, it is time for the National Bank to peg the ruble to the euro and conclude a currency board agreement with the European Central Bank.

Over the past few years, Belarus' economy has been slowly shifting from dollarization to euro-ization. Belarus' foreign trade is focusing on European markets: in 1997-2000, Europe accounted for 70 percent of Belarus' foreign trade with EU members, with candidate countries totaling as much as 30 percent.

With the start of real-term privatization and structural reforms, Belarus will be gradually involved in European political and economic integration. Trade with the EU will rise, while exchange with economically retarded CIS countries will be on the wane. The share of euro-denominated forex transactions will grow. The euro peg will become an effective mechanism for spurring Belarus' euro market and help to restore the Belarusian ruble as the currency of choice for households and businesses.

The potential of this monetary policy will be easier to fully realize as the financial system develops, and financial institutions, the currency and the stock exchange function more effectively.

#### Ad c). Tax reform and fiscal policies

The adjustment of public finance to market economy requirements should proceed in parallel with currency stabilization and tight budgetary constraints on undertakings. This is a crucial phase in stabilization as economic liberalization and market openness call for structural reforms and trigger off bankruptcies resulting in a sharp drop in inland revenue from the public sec-

tor. At the same time, the government will need to spend heavily on reforming the system for public governance, developing market infrastructure, supporting social service establishments, and providing unemployment benefits for redundant workers as the unemployment rate may hit 20 percent (1 million people) in the reform's first year. To avert a fiscal crisis which may be caused by declining output and tax revenue, the government will need to resort to cuts in spending, provide transparency in expenditure, phase out hidden subsidies such as arrears, barter transactions, subsidized household utility rates or cross-subsidies among various consumers groups designed to keep unprofitable operators afloat.

The fiscal reform should establish a mechanism for identifying and separating revenue and expenditure, ensuring budgeting transparency at all levels, impose legal budget deficit caps, and enhance the role of direct taxation in order to provide local budgets with greater financial independence.

To boost tax revenue, the government may expand the taxation base and sell state-owned enterprises. The government would have to stop supporting state-owned agro-industrial conglomerates (support there totaled 32 percent of GDP in 2002), and stop financing housing development with public money.

Unfinished housing construction and other projects with over three years in implementation and less than a 70-percent completion rate should be frozen. The government will need to cut numbers of army servicemen and expenditure on governmental institutions and the defense.

It would be advisable to deprive the government of the right to award undertakings with tax and customs duty exemptions. The parliament alone should have the right to approve exemptions when adopting the annual budget.

The reform should lead to fiscal decentralization and greater financial independence of local authorities. Utility companies should pay all taxes to local budgets. This would encourage local governments to adopting utility sector restructuring programs, expand the taxation base and develop local infrastructure.

The current tax system consists of 36 taxes collected by central and local budgets. The overall fiscal burden (incl. social security contributions) nears 50 percent.

The current fiscal system has the following drawbacks:

- it slows down economic growth;
- dampens the job creation potential among individuals and undertakings;
- does not encourage business owners to paying taxes and legalize their income; instead, it forces them into the shadow economy;
- creates conditions for unfair competition;
- impairs the competitive edge in business;
- slows down structural reforms;
- discourages foreign investors.

The tax reform and fiscal policies should be in line with the following principles:

- taxes should play an exclusively fiscal role, i.e. should guarantee collection of funds to finance public expenses. They should not be used as a means to adjust industrial output;
- neutrality and equitable treatment (all should pay taxes with no exception);
- the tax burden should not slow down economic growth;
- efficient administration (tax collection cost should be limited);
- simplicity and transparency (the purpose of taxes should be clear and the public should know how tax revenue is spent);
- single taxation (the same taxation base should not be taxed several times).

The government should reduce the overall tax burden and cut spending. The following taxes should remain in place after the tax reform:

- personal income tax;
- social tax;
- property tax;
- value-added tax (VAT) on goods and services;
- excise;
- customs duty.

It is necessary to adopt a pro-rata income tax to encourage business. During stabilization, it would be reasonable to set a higher property tax to achieve optimum distribution of tax revenue. As financial stability is achieved and emergence of the middle class is fostered, the government should seek to lower the property tax and customs duties, followed by reducing other taxes.

In particular, the standard VAT rate should be gradually reduced to 16–18 percent, while income tax rates should be cut to 10–15 percent. The overall tax burden on salaries should drop from 40 to 30 percent.

Early steps should include abandoning the 2.5-percent tax collected by local funds to support agricultural producers, and the 2-percent tax collected at the central level to support agricultural producers and agrarian sciences. A 1-percent cut in these taxes reduces the overall tax burden by 1.3–1.5 percent.

To make it easier for Belarusian companies to operate in international markets, inland revenue authorities should be prepared to cooperate with their opposite numbers in EU member states. In particular, lawmakers should bear in mind that indirect taxes (VAT and excise) and their collection principles are harmonized by various EU regulations. The same holds true for the direct capital gains tax.

#### Ad d). Income policies

To support financial stabilization, it is necessary to freeze wages and salaries so as to ease inflationary pressures (stop wages and prices from spiraling). The government should guarantee minimum income for vulnerable groups and make sure that its rise will be mirrored by an adequate rise in productivity. The government needs to set an acceptable rate of unemployment benefits to add transparency and predictability to the labor market. Unemployment benefits should be paid no longer than six months per year. It is necessary to stop payments of social benefits for those who do not need them. Wage increases should be related to greater productivity. To be able to earn additional income, households should have an opportunity to choose between keeping their savings in banks and entrusting them to institutional investors. Individuals should be guaranteed the right to divest shares regardless of the terms and conditions on which they were acquired.

## Structural reform strategy

Stabilization, liberalization and the establishment of market institutions are preconditions for an effective structural economic reform, raising economic efficiency and living standards.

### The real economy

Economic reform implies step-by-step implementation of the following objectives:

- financial and macroeconomic stabilization – curb inflation by pursuing sound monetary policies that rule out unsubstantiated money-printing practices and are conducive to monetization of the economy (insufficient liquidity in the real economy is an obstacle to a smooth self-adjustment of market mechanisms); offset overdue debt (the government pays the amounts due to companies from funds raised by selling property of bankrupt operators);
- create an environment for economic growth (competition and higher mobility of resources as enabled by various types of exchange), improve investment and depreciation policies, radical change in manufactured goods and services mix (restructuring), award public contracts via competitive procedures;
- integrate the national economy with the international labor market – join the WTO, phase out tariff restrictions, lift non-tariff restrictions, allow foreign companies to participate in tenders for public procurements, improve customs clearance procedures, and obtain an international credit rating;
- create a setting for sustainable development and adoption of environmental standards, develop the small business sector and the transport and tourism infrastructure, and diversify energy supplies;
- create scientific, technical and social preconditions for the economy's transition into the postindustrial (information) stage of development: train highly skilled employees, motivate researchers to integrating with

the manufacturing sector, raise the share of R&D spending from 0.9 percent of GDP today to 1.8–2 percent of GDP (the average R&D spending in EU countries).

State aid to enterprises should be based on the following principles:

- Financial support should be limited. The government along with other parties concerned may partially finance R&D, and R&D-intensive, environmental, and regional infrastructure development projects.
- State aid should be transparent and subject to close and permanent scrutiny.

## Industrial policies

The main principle underlying industrial policies is to avoid putting the spanner in the works of market mechanisms. Therefore, the industrial policy concept should underscore its systemic nature and orientation towards fostering a general environment for economic growth.

Industrial policies should not be targeted at specific industries, undertakings or regions, but equally affect all market participants that constitute the economic, institutional, organizational and legal environment for their efficient operation. These policies will be pursued mainly at the macroeconomic level.

Their purpose will be to warrant a level playing field for all players, as assisted by financial stabilization and privatization.

Industrial policies should provide for organizational and financial assistance in restructuring enterprises that are fundamental for the economy of towns and cities.

## Methods of pursuing industrial policies

Informational methods. The government must provide businesses with scientifically substantiated statistics on the business environment, including the global dimension, so that they may opt for better manufacturing, investment, innovation and trade solutions. The public should have access to economy, industry and regional surveys, forecasts, market research and consulting services.

Macroeconomic regulation methods should be aimed at maintaining financial stability, reducing the budget deficit and inflation and strengthening the national currency.

Resource methods pertain to the system of government contracts in the first place, and also to the formation of investment and export risk insurance funds, personnel training and retraining, and social security guarantees.

Institutional methods should adjust and improve the system as a whole. Use of institutional methods does not imply spending to support the system's constituent parts such as industries, undertakings and regions, but rather provide legal guarantees for labor relations.

The above-mentioned reforms (liberalization, institutionalization and stabilization) should provide an environment for restructuring the industries. The government should be equipped with a restructuring concept in order to limit line ministries' ability to lobby their interests by introducing additional taxes, extending soft loans, imposing import quotas etc. In this respect, it is necessary to point to an integral criterion of restructuring efficiency, this being a rise in manufacturing asset productivity, i.e. increase in the number of undertakings with above-average productivity or return on investments. The manufacturing asset productivity would be higher if products were competitive and in continuous demand in the domestic and foreign markets.

### **Obstacles to restructuring**

There are three types of obstacles that should be overcome for a successful restructuring of the real economy. These are:

- Institutional constraints resulting from non-systemic reforms: lack of competition and well-developed fundamental market institutions such as owners, the SME sector, the banking sector with sufficient lending resources, flexible capital and labor force markets etc. The current ambiguous legal framework complicates business operation and decision-making at the micro-level, increases transaction costs and impairs competitiveness.
- Financial constraints manifest themselves in a shortage of investments and ineffective use of available capital. An open economy, stable legislation, and



- a low tax burden would attract foreign direct investments and loans and induce the government, banks and undertakings to using their funds effectively.
- Technological constraints require rapid response to changes in prices of raw materials, energy resources and other cost factors, as well as the use of inter-industry connections. Enterprises will need advanced technologies that would enable them to use the available raw materials (wood potassium salt etc.) more effectively. Due to absence of basic raw resources, Belarus should develop and pursue projects to procure raw materials abroad, in particular in Russia e.g. develop oil fields and other natural reserves, attract private capital and bolster partnerships in technological initiatives with other countries.

### **Restructuring principles**

Key restructuring principles are openness, reliance on new and advanced technologies, resource conservation and environmental safety.

Openness is essential for Belarus' presence in economic globalization. Lower import duties are a key factor for raising living standards owing to lower prices of imported goods and overall economic modernization, if one is to rely on the premise that imported equipment is usually better. The open economy would encourage companies to manufacturing globally competitive goods. As domestic markets saturate, exports will rise (in Belarus, exports have been growing over the recent years due to lower domestic consumption and national currency depreciation.)

Specialization: inferior industrial efficiency calls for replacing inefficient technological elements (primarily domestic manufacturers) by foreign suppliers. At the same time, specialization in the manufacturing of certain parts and components would help to attract FDIs.

Reliance on new and advanced technologies is a key restructuring principle. It will help to consolidate competitive advantages of the economy. As a rule, technology-intensive industries are not usually associated with multiplication effects as they were not originally well connected with other branches. Therefore, technology-intensive industries should be the driving force for the economy,

the main consumer of other industries' output, e.g. the construction industry. It is necessary to boost total technology-intensive share of GDP which shrank from 2.3 percent in 1990 to 0.8–0.9 percent at present.

Resource conservation and environmental safety: considering the limited supply of domestic raw materials, fuel and energy resources (not more than 30 percent of domestic demand), and high production costs in the manufacturing sector (74 percent in 2000), the restructuring strategy should be closely related to the resource-saving policy.

The relationship between the government's environmental and restructuring policies, launch of environmentally friendly technologies should reduce the share of resource-intensive industries in the country's total. At present, raw material, fuel and energy consumption in Belarus is twice as high as in developed countries. The experience of transition economies has pointed to a need for adopting a law to encourage efficient use of raw materials and energy.

### **Financial sector reform**

The financial sector reform should be closely related to currency stabilization policies and will depend on successful reform of the real economy.

The purpose of the banking sector reform should be to increase its lending capacity. This cannot be done without a strong national currency and a financially stable banking system.

The following steps should be taken to reform the banking sector:

- ensure independence of the National Bank from the executive pursuant to a national currency law that has yet to be adopted. This step calls for changes to the Banking Code whereby the parliament will appoint National Bank governors and deliberate on central bank's audit reports. A law should be passed to prohibit the National Bank from printing money to finance budget deficit;
- open the way for private investments in six largest state-controlled banks that account for about 90 percent of the sector's total assets;

- balance household deposit and lending interest rate policies, as banks currently offer attractive interest rates for households and excessive loan interest rates to corporate clients;
- forbid government forcing the banks to lend to certain sectors or enterprises, and ensure that the government settles bad debts resulting from compulsory lending to state-owned enterprises;
- abandon the current 50 percent limit on foreign capital presence in the banking system;
- have the country's banking system rated by international financial institutions;
- create a competitive environment in the banking sector to encourage banks to cut costs and fees, adopt international payment, auditing and reporting standards.

The reform should include efforts to encourage the development of stock and insurance markets on the basis of stable and transparent legislation harmonized with EU laws.

The following steps should be taken to develop the stock market:

- lift restrictions on professional dealers and brokers accessing the stock market, with simultaneous tightening of requirements for stock market dealers and brokers. To this end, the Securities Commission should be vested with greater powers;
- lift the 15-percent tax on personal income from securities and temporarily exempt corporate stock market dealers from taxing securities transactions;
- offer freedom of choice to individuals in divesting securities;
- broadly advertise public offerings of shares in profitable companies;
- prepare for integration with the European stock market.

### **Foreign trade policies**

Consistent reforms will allow for bridging the GDP gap between Belarus and most EU countries. Belarus will continue to export commodities to CIS co-

untries, but the proportion of exports to Europe and countries outside the CIS should rise from 35 percent to 60-65 percent. The exports of services should increase from 62 to 80 percent, combined with a rise in exports to former Soviet Union republics.

Belarus needs to join the WTO to see a removal of non-tariff barriers to exports of textiles, chemical products, potassium fertilizers and steel.

To re-orient exports westward, the country will need to reduce the ratio of cross-industry exchanges (trade in products of various industries) and encourage trading goods of the same industries to expand trade volumes and increase specialization. Intra-industry trade exceeds 70 percent of total trade, mainly among developed countries.

Export re-orientation will be fostered by modernization and technological advancement, involvement in multi-national R&D projects, acquisition of Belarusian companies by international corporations, and by the growing purchasing power of EU countries, which currently far exceeds the spending power in Russia and other CIS countries.

The reforms should allow for the country to achieve European standard of living and facilitate its convergence with the EU economies.

### **Reform of industries**

In absence of large domestic investors, large-scale industries (petrochemical and machinery manufacturing) are likely to be controlled by foreign investors with the government retaining a stake. At the early stage of the reform, it is advisable to foster an environment for attracting domestic investments (including household savings) in sectors producing goods in large demand domestically and in external markets such as consumer goods, the woodworking industry and R&D-intensive sectors (integrated circuits, computer software, medical and environmental equipment, bio-technologies, production of new materials etc.). These industries should continuously pursue specialization as encouraged by increasing international intra-industry trade.

Medium-sized private businesses may take over some consumer and R&D industries with a short payback period that do not require major capital expen-

diture. An upturn in these industries, some of which are labor-intensive, would help to ease labor market tensions caused by the reform. Technological development, along with a rise in highly skilled labor force and growth of infrastructure, will cause high-tech exports to increase from current 3.7 percent to 10–15 percent. In a more distant future, competitive industries will help the country to discover new niches and gain the competitive edge on a global scale.

### **Agriculture**

For the time being, Belarus' collective and state farms are not profit-driven; rather, they operate to support agricultural infrastructure.

Since rural population stands at 29 percent of the country's total, a reform of collective and state-owned farms should be accompanied by transfer of their social and welfare functions to local authorities. At an early stage, agricultural reform would boil down to denationalizing collective farm property and setting aside up to 30 percent of infertile soil from agricultural production (for forestation). Proceeds from the lease of land and other natural resources (property tax) should replace a considerable part of tax revenue. Unlike most other taxes, lease payments do not contain the production element and do not distort resource distribution. Lease proceeds would allow for the government to reduce agricultural subsidies to 5–10 percent, in line with WTO requirements. To employ excess labor force in rural areas, authorities will need to create jobs in non-agricultural sectors such as tourism, small businesses and hunting. Belarus will need to open its agricultural market to ensure sufficient food supplies and fully tap into the capacity of food processing plants.

As the land market develops and land becomes available to private owners and local governments, rural areas are more likely to attract investments both in non-agricultural sectors (restoration of historical monuments, tourism, transportation and leisure infrastructure development) and high agricultural technologies (production of renewable energy resources – ethyl alcohol, oils, GM-crops, creation of a gene pool).

## **Transportation, construction**

Development of transport infrastructure and the construction industry spur economic growth, as the experience of EU expansion suggests.

The role of transit of goods and services would increase as Belarus' economy opens up. The need for improving the transit infrastructure urgently calls for intensifying the construction business. The country may see a rise in the population as a result of labor force migrations from Russia and other CIS countries.

However, these industries should give priority to local labor force and domestically manufactured products (building materials, trucks and construction equipment). The adoption of new building technologies will benefit housing renovation and utility sector upgrading projects.

The expansion of transport services network could create new jobs.

## **Fuel and power generation industry**

The present state of Belarus' fuel and power generation industry highlights the need for saving fuel and electricity. The country's power generation facilities are in a critical condition: power generation units at the two largest hydropower plants are worn out, while most power plants using liquid fuel were built some 40 years ago. Belarus will need to replace 80 percent of its power generation plant and machinery before 2010. Most power plants are using expensive fuel like gas or oil.

Construction of a nuclear power plant does not seem to be the advisable option as the cost of nuclear power is high. Therefore, in the near term Belarus should increase electricity imports (which rose by 15.3 percent in 2001 to 8.3 billion kW/h, i.e. 25 percent of total power consumption). However, power plants should start replacing their worn-out equipment now. This will require private investments. In an open power and heat generation market, privatization of old facilities and greenfield investments should encourage competition.

## Telecommunications

Despite some hardships, the telecommunications sector has been vigorously developing over the past few years. The number of telephone users rose by 80 percent between 1990 and 2002. Mobile telephony and Internet have been expanding, with the number of cellular subscribers rising to 600,000.

Reform priorities should include privatizing state-controlled companies and creating a competitive environment. Also, state-controlled media must be privatized.

\* \* \*

The economic reform plan presented above seeks to achieve European living standards as fast as possible. The reform's main goal is to restore or set up effective market institutions that would help businesses in using their potential effectively, buy new technologies and know-how that enhance competitiveness on a global scale. All basic principles of this economic model, i.e. economic performance in market conditions, private ownership, free competition and an open domestic market, are designed to achieve that goal. Economic freedom will be mirrored by the government's responsibility for economic policies, markets and currency stability, and private companies' responsibility for their performance and earnings.

An effective, targeted social assistance that is commensurate with the nation's wealth is intended to cushion shocks of economic reform in the mid-term. Therefore, the government should seek to set the framework for boosting productivity, growth of small business, and inflow of foreign capital and technologies.

Market mechanisms should be established irrespective of economic and political support from the EU. However, close and mutually beneficial economic ties between Belarus and the enlarged EU would be conducive to the country's economic growth. While pursuing the above-mentioned reforms, the government should focus on developing the labor market, which implies prospects for employment opportunities and establishing a mechanism for effective use of individual energy and creative initiative.

## Labor market

### by Andrei Shabunia

The purpose of labor market reform is to limit government regulation and offer greater freedom to labor market participants. Relations between employers and employees should be governed by the law of supply and demand.

It is impossible to boost economic performance without giving employers and employees an opportunity to negotiate and conclude wage agreements.

The labor market policy should ensure:

- employment for job seekers;
- streamlining the employment structure;
- a free choice of occupation and job.

The labor market policy should incorporate the four pillars of the European employment strategy:

- employability;
- entrepreneurship;
- adaptability;
- equal opportunities.

In this respect, steps to be taken at the reform's first stage should be aimed at developing those labor market aspects that encourage occupational activity and high degree of employment.

In terms of steps to encourage occupational activity and employment, the prime necessity is to change labor legislation to limit government regulation of the labor market. Legislation at variance with market conditions may impair labor force mobility and obstruct the flow of labor force from the declining to growing industries.

Efforts to promote labor force mobility would be geared to:

- establish contractual working arrangements as the main mechanism to regulate relations between the employer and the employee;
- simplify employment and employee redundancy regulations (which should provide for collective, individual, written and oral agreements of limited duration, facilitate laying off workforce for employers, diminish



- the role of trade unions and employment centers in concluding employment contracts);
- enable flexible forms of employment (part-time, occasional employment, work from home, subcontracted employment etc.);
  - abolish compensation capping in private companies;
  - minimum compensation binding for all undertakings regardless of ownership status should be adjusted by government directives rather than automatically;
  - abolish regulations that restrict companies' right to fix and adjust compensation. Wage increases should depend on labor productivity and financial position of firms;
  - obligate the management, especially in large companies, to provide advance notice of planned closures or large-scale redundancies, so that measures could be taken to address unemployment;
  - introduce a flat-rate income tax of 13–15 percent;
  - cut indirect taxes on labor force to 30 percent, including those charged to employees;
  - reduce job creation costs (especially costs of low-skilled jobs).

## Development of SMEs

The small and medium-sized business sector can potentially create more jobs than any other sector of the economy.

The following steps should be taken to foster entrepreneurship:

- register new businesses pursuant to the principle of notification, rather than authorization;
- abolish the regulation preventing companies from registering official seat at residential premises (domicile);
- reduce the minimum capital requirement;
- lift restrictions on the maximum authorized number of employees hired by entrepreneurs in the small business sector;

- ensure that companies are registered with business regulation and tax authorities of the same location to reduce bureaucracy, and adopt a single list of documents to be attached to the business establishment application;
- abolish the regulation requiring firms to engage in all types of business activity referred to in the founding deed;
- enhance legal guarantees whereby companies may be closed by their owner's decision, by a body authorized by the owner, or by a court of law;
- set up regional centers for supporting SMEs and develop the micro-lending network;
- develop a system of financial incentives for those investing in human resources, including in employee training.

### **Flexibility of authorities (the Ministry of Labor and Social Security and state employment centers)**

It is impossible to abandon administrative intervention in the labor market completely. The government's policy in this respect may be 'passive' or 'active'. The passive policy of mitigating unemployment is limited to traditional measures such as registering the jobless, paying unemployment benefits and running unemployment insurance schemes. The government should pay particular attention to monitoring the labor market, sharing information on labor market conditions and forecasting company closures and layoffs.

Active policies imply influencing the labor market by stimulating demand and adjusting supply.

Measures to address unemployment include:

- increased funding for training and retraining, youth employment programs and programs to avoid long-term unemployment;
- developing a community work plan for the jobless;
- offering loans to the unemployed wishing to start up a business;
- providing financial support to selected unprofitable enterprises to maintain a level of employment. Support should be limited for time and provided in areas with low labor force mobility (e.g. due to housing shortages) or for enterprises that play a key role in the local economy.

Employment centers should receive adequate funding irrespective of the number of applications from job seekers they handle.

Bolstering labor force mobility is crucial for a flexible labor market. The following steps should be taken:

- abolish the *propiska* system whereby state-owned enterprises and establishments cannot offer jobs to people coming from other locations, along with other regulations that limit employment opportunities;
- orientate the training and retraining system toward labor market demand. Retraining programs, especially ones that offer good employment prospects, should be partly financed by trade unions or trainees;
- limit the amount of compensation paid to laid-off workers.

### **Reform of the unemployment insurance system**

Unemployment benefits and the procedure for receiving benefits should stimulate the jobless to searching jobs. The period of benefit payments should be limited to three or six months. A grant scheme may be introduced to replace benefits for those who wish to improve their skills.

### **Reform of social partnership (tripartite dialogue)**

Work to develop and implement employment policies should involve the government, trade unions and employers. None of the parties involved should have exclusive decision-making rights. Negotiations should cover issues such as compensation, employment, training and retraining programs, and access to labor market statistics.

Yet, tripartite arrangements should not necessarily be given a prominent role as they may impair labor market flexibility.

### **Non-discrimination in the labor market**

Efforts include promoting equality of men and women, encouraging employment of women, fostering an environment for active occupation of the disabled and women during and after maternity leaves.

The government's employment policies should be aimed at achieving higher living standards and human resources development in a highly performing economy.

Funds for employment programs should be transferred to local organizations responsible for their implementation. A special agency should coordinate all programs at the national level. Despite sizeable spending, results of labor market policies are not always visible. However, this does not diminish their role in combating unemployment, a phenomenon that humiliates people, breeds psychological problems for families of the jobless and stirs social unrest.

Decisions to earmark funds for a specific employment program should be made with due consideration of all possible benefits and problems. For instance, if a region with high unemployment has considerable economic potential, it makes sense to offer community work for the jobless to improve local infrastructure. If the potential is low, it is reasonable to subsidize employers to sustain the employment level.

The employment strategy should promote educated and highly skilled labor force, while the labor market should be responsive to economic changes.

All elements of the labor market policies, such as registration of job seekers, retraining and active forms of countering unemployment, should be closely inter-related and interface with other economic policies. The employment programs should not be in any way inferior to economic policies; instead, they should be part and parcel of the government's overall economic strategy.

The reform should shape a flexible labor market that is responsive to demand and supply changes. The labor market should create and eliminate jobs with as little government intervention as possible. It should not restrict occupational and geographic mobility of the labor force.