Introduction and Overview

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In the countries of Central and Eastern Europe, as in other countries with a past of state socialism and central planning, the political revolutions of the late 1980s brought about dramatic and rapid changes in the economy. In allocating their resources, firms and households had to face the emergence of markets and challenges from foreign competitors. In financial institutions, the mono-banking system was broken up and replaced by Western-type central and commercial banks. Capital markets came into being. New fiscal structures, on the revenue as well as expenditure side, were introduced. Individual property rights were established, and mass-privatization efforts commenced. Simultaneously, macroeconomic stabilization was needed and external shocks – for example, the demise of the CMEA – had to be absorbed.

This transition of Central and East European countries to market economies has not been smooth. Despite all political efforts, and apparently unrelated to the specifically chosen sequence and speed of reform measures, an output decline set in, encompassing nearly all sectors of the economy.

Based on official estimates, the size of the decline in real GDP since 1989 looks discouraging (*Figure I.1*). Until 1993, average output for the Central and East European reform countries decreased by well over 20%. The fall in real industrial production was even stronger, and the average production level reached in 1993 corresponds to only some 60% of the 1989 figures (*Figure I.2*). As expected, the unemployment rate increased within four years from practically nil to levels experienced recently in many Western industrialized countries (*Figure I.3*).

In all reform countries, the reduction in industrial output was much stronger than in the overall economy, suggesting that important changes in the economic structure have already taken place. Particularly, since prior

R. Holzmann et al. (eds.), Output Decline in Eastern Europe, 1-12.

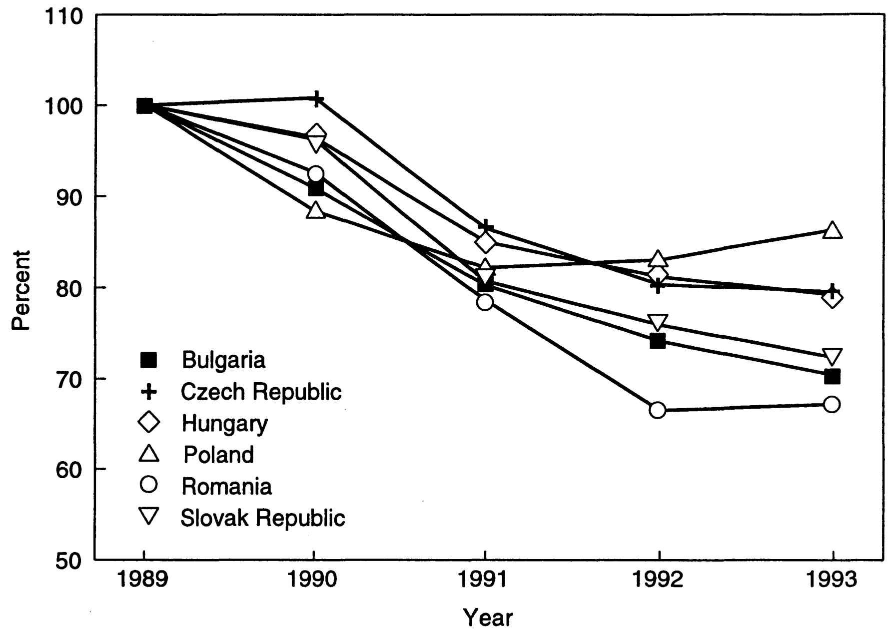

Figure I.1. Real GDP change from 1989 to 1993 (1989 = 100). Source: Statistical tables, *The Economics of Transition*, **1**(4) 1993; KOPINT-DATORG, 1994, *Konjunktúrajelentés* 1994/1 (Report on Business Tendencies 1994/1), Institute for Economic and Market Research and Informatics, Budapest, Hungary.

industrial output had to a large degree been associated with wasteful investments, military expenditures, large stock-building, and environmental problems, the fall may have had a smaller detrimental effect on actual consumption than the figures on output decline suggest.

Yet, despite these common trends, a mixed situation has evolved, with signals of both hope and dismay; as the reform process progresses, the economic performance has become less similar among reform countries. In a few countries, output decline has started to be reversed and growth is picking up (in Poland since 1992 and apparently in Albania, Romania, and Slovenia in 1993); in two other countries (Hungary and the Czech Republic) output decline seems to have been halted in 1993 and growth prospects are evident for 1994; the data for two further countries (Bulgaria and the Slovak Republic) indicate no bottoming out of output decline and gloomy prospects for a few more years.