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Institutional and political aspects of reform preparation and implementation

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10 mins

The 1990s were the decade when the world told post-communist countries how to manage reform preparation and implementation.

The 2000s are the decade when this region tells the world how to do it – and especially how the old EU can transform its economy the way that the Central and East European countries have done.

Lessons of the reform process so far, for the next generation of reformers (in the Balkans and wider Europe) and for international institutions:

- Conditionality can be very effective in guiding reforms and ensuring effective implementation. But it only works under particular circumstances: where there is a clear linkage between reform and reward (IMF, WB, some parts of EU accession process), and where the conditionality is consistent across countries and across time.

- Aid is much less important than trade in cementing reforms in place. But external aid is important as a signal to private sector investors of international organisations' approval of reforms.

- Public and transparent methods of monitoring progress are vital – although there is room for improvement in the methods employed by the EU and EBRD.

- The private sector is at least as important as public policy in keeping reforms on track. Foreign investors reward reforms by putting their money where mouth is, so that governments can show a dividend to voters. And FDI is vital to ensuring that there is a virtuous circle between successful reforms, foreign investment and further reforms.

Lessons for the EU-15 countries:

- Countries are not good at policing themselves. Some external anchor for reforms is essential. The EU accession process provided that in Central and Eastern Europe (CEE). But the EU does not provide a good anchor for its old member-states: the Stability and Growth Pact debacle shows this. Finance ministers are not good at holding their peers to account, because they are all afraid of being in the same position themselves and having to rely on the mercy of their counterparts.

- The EU needs to develop a more credible, independent institution to be the impartial enforcer of the rules – in this case, agreed targets for economic reform. The Commission has had only partial success in playing that role: it is subject to political influence, and its means of enforcement are legal rather than political or market-driven. The ECB can inflict pain on finance ministers through higher interest rates, which have an immediate effect, whereas a long legal process instigated by the Commission does not have the requisite disciplinary effect on national governments.

- It is very difficult to set up sticks and carrots for structural reforms, because they depend so much on the individual country, and because the costs and benefits are only visible over the longer-term, beyond the horizon of the next election. The government that grasps the nettle of serious reform will almost certainly be punished for it at the polls, so structural reforms have to be explained to the voters as part of a long-term strategy.

- However, benchmarking and peer pressure can have some impact. The EU has discovered benchmarking by accident: no minister likes to find his country at the bottom of a league-table, whether on employment, education or competitiveness. NGOs can play an effective role too, because they don't pull their punches: the CER's annual 'Lisbon scorecards' have named and shamed countries for four years now, and they have received more press coverage than the Commission's annual report on progress on the Lisbon agenda.

- Naming and shaming countries can encourage them to reform more effectively – but only if governments are held to account by their domestic press and voters at home. To achieve that, the reform process has to be high-profile, and it must be guided by measurable targets. The parts of the Lisbon process that are measurable have had more success than those where progress is hard to assess.

- Finally, new members can shame some of the old ones because of their success in some parts of the Lisbon agenda – especially market liberalisation. In other areas, they have a long way to go – especially on labour markets and sustainable development, where their performance is worse than that of the old EU-15. But the EU needs to be careful not to apply blanket measures to countries that seem to have similar problems: labour markets in CEE have different problems from those in the EU-15, and the remedies need to reflect those differences. What is needed in CEE is not deregulation of labour markets – as in Germany and other EU-15 countries – but an increase in labour mobility, by improving transport infrastructure and making housing markets more flexible.