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Transition in the FSU and in sub-Saharan Countries: the Role of Institutions

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Draft. Comments welcome.

Contents

1. Introduction

In this study two regions, the sub-Saharan African (SSA[1] for brevity in the following) and the Former Soviet Union together with the Central Eastern European countries (FSUCEE), are compared. These two regions represent different levels of economic, social and financial development. The FSUCEE seems to gradually achieve the growth rates of the Western Europe whereas in the SSA the economic growth and social development has stagnated and even retarded. The purpose of the study is to examine reasons for this increasing gap, to what extent these two regions share each others' problems and also, to what extent similar remedies could be applied in the both cases. The comparison between these two regions is expected to disclose clearly the significance of the qualities of state institutions to the economic growth and, perhaps, in particular, to equality. It is assumed, that the quality of institutions, measured by means of the economic and political freedom they can deliver, affect major development issues such as economic growth, foreign trade, foreign direct investments (FDI), reduction of poverty and political or exogenous hazards.

As shown in the statistic or table 1, this regional dualism is hardly related to any recent whims of globalisation, growth of international trade or advancement of transport and communications technology, because the differences of the economic growth have persisted the last 150 years.

Table 1. GDP per Capita 1820, 1900 and 1992, in 143 countries
(in constant 1990 Geary-Chamis dollars)*

	1820	1900	1992	1820-1992
Western Europe	1292	3092	18313	1,5
Eastern Europe	1093	3081	5897	1,0
Africa	450	500	1236	0,6
World	554	868	2613	0,9

Remarks: world and average GDP per Capita, 1820-1992 average annual growth is at compound interest during the period. About Geary-Chamis approach, please see Maddison 1995, p. 163.
Source: Maddison 1995, table F-7, p. 224.

Results of the study support views that institutional development matters. Abramowitz (1986), North (1997, 1981, 1990) as well as North and Thomas (1973) are often cited authors stressing the importance of institutions. Also the World Bank devoted its latest World Development Report to the institutional aspects and their relation to economic and social growth (World Bank 2002). The EBRD has elaborated the measurement of institutional factors and their relations to the economic development in the FSUCEE regions.

[1] Nigeria and South Africa are often excluded, because they dominate the region in terms of population, GDP and foreign trade. In this study developments in two major regions, consisting of the FSUCEE) and the SSA, the dominating countries of the Russian Federation and Nigeria will be included, whereas South Africa will be excluded.

An important merit of discussions about the transition process of the former socialist economies was that following the failure of centrally planned command economies the importance of establishment of a well functioning market economy as a development goal became more clear and self-evident, than it had been before. However, in the literature on transition and developing the economies towards free markets, the legal and institutional reforms receded into the background during the first half of the 1990s and were hardly mentioned in reform programs. There was a failure to understand and acknowledge that the institutions, which had served the socialist system, were inadequate and not tuned to serve market economies and that the macroeconomic reforms did not spontaneously and instantly generate new institutions, which could have replaced the old ones.

During the second half of the 1990s increasing acceptance and understanding emerged that institutional reforms are crucial for the success of transition and to the sustainability of market economy (Clement & Murrel 2001, pp. 6-7, EBRD 1998). Moers notes in his recent study that it seems to be gradually recognised that "the standard economic theory is ill suited to explain transition - - (because it) implicitly assumes that the relevant institutions are there, exogenous to the theory, while transition seems mainly a dynamic process of institutional change (Moers 2001, p. 19).

The level of institutional developments does not lend itself to be easily measured. For instance, the EBRD has developed indicia for institutional development and applies the on the FSICEE region, but not on the SSA. Here this question has been approached by picking up Weder's (2001) study of ranking the FSUCEE countries and a number of developing countries (including some SSA countries) by their institutional qualities.

It was then examined, whether the Weder's typology match with recent rankings by economic freedom and financial risk, derived from "2002 Index of Economic Freedom" by O'Driscoll, Homes and O'Grade, and Euromoney, March 2002 edition, respectively. The quality of institutions and state can be assessed, although indirectly, through perceived economic freedoms and financial risks, instead of trying to derive conclusions from direct observations, such as number of public sector employees or public sector share of GDP, organisational structures, etc.

One of the by-products of this approach is that the countries often the both regions represent a heterogeneous group and when ranked by their institutional qualities, the countries of the regions overlap. It follows from this, that from the viewpoint of economic and institutional development these countries, from the poorest SSA country to best performing EU member candidate, represent a continuum (Kornai 2001, Shurke, Weder,). Conceptually, this continuum of countries could be further extended over developed industrial countries, which also continue to develop.

Historically in the development foreign assistance strategies three lines can be discerned. The first line relates to political, second to the western academic developments of growth theories focussing on the question, what factors of production and their combinations were decisive to generate a sustainable economic growth (Harrod and Domar, Solow and others).

The second one is more recent and politically connected to the dissolution of the Soviet Union. In the continuum of social, economic and institutional development the label "transition economies" represents a political category of development thinking, related to the dissolution of the Soviet Union and an emergence a number of independent states and governments and their advancement from plan to market economy. It is benchmarked by the discussion around promotion of macroeconomic reforms (enshrined in the "Washington Consensus") and the discussion on speed of transition ("Big Bang" or shock therapy versus gradualism). Using economic reforms - liberalisation, stabilisation and privatisation - the old institutional structures designed to serve the planned command economy, should be replaced or transformed to serve the market economy.

The antagonism between the shock therapists and gradualists seems to be, in retrospect, academic and Soviet-collapse specific. The main argument was to use fully the window and opportunity and warrant the irreversibility of the development and create adequate critical mass not to loose momentum of the reforms (Balcerowicz 1995, Gaidar 1999). Perhaps the dichotomy was false, as pointed out by Kornai, because the speed is not the primary measure of success (Kornai 2001, p. 60). This discussion was never very actual in the rest of the developing world. Although much interesting modelling work was performed (like the Aghion-Blanchard model of optimal speed of transition), the discussion was to remain more academic. The season of big banging was over during the first half of the 1990s, and the interest was now turned towards the question, how to improve the sustainability of the achieved results. Development of institutions, enforceability of property and contract rights and generating adequate social capital entered to picture during the latter half of the 1990s.

The third one to the new wave - since the 1960s and 1970s - of economic egalitarianism linked with ideas about poverty reduction, income distribution and globalisation. There is also a notion that the development of institutional capacities is important to warrant the sustainability of the achieved results. It is also obvious that the disappearance of East-West controversy makes more room for the attention given to the North-South dimension.

Rich countries tend to restrict immigration and imports of agricultural products using tariffs, subsidies and quality certifications. The poor countries are not able to attract FDI and trade, and thus fail to reach the convergence promised to the developing countries the by the "Washington consensus". The models for development derived from the economic textbooks work well in developed countries and even in the most advanced transition countries, do not help the less developed countries with badly working or non-existent state structures. In the more pragmatic approach to the development, the role and technical and financial assistance to develop state structures and services become central (Scott 2001). The enforceability of clearly defined property rights and maintenance of law and order emerge as main tasks of state, and represent the cornerstone of non-corrupted market economy. As crystallised by Scott: " -- Many observers now admit that the transition economies needed appropriate property rights and an effective state to enforce those rights as much as they needed the liberalisation of prices. Indeed, liberalisation without property rights turned out to be the path to gangsterism, not capitalism. China, with a more effective state, achieved much greater success in its transition than did Russia, even though Beijing proceeded much more slowly with liberalisation and privatisation." (Scott 2001, p. 161).

In section 3 writings of Olson (1995 and 2000) and Hedlund (2001) have served as source for understanding significance of property and contract rights for the growth as a basis of institutional development. Most recent contributions to the analysis on importance of institutional capacity building include the analyses of de Soto (2000) on the bureaucracy's role in hindering the growth of capital, and Easterly on importance of economic incentives may play in the economic growth and development assistance issues.

Presently, there abundant empirical evidence that good governance matters, although the causality is probably recursive: good governance promotes development and economic growth, but probably also rich countries can afford better governance than poor countries (Kaufmann & alia, 1999). This is true particularly, if good governance is considered to include the redistribution of incomes to those in need, the rich countries have more to be redistributed. In section 4 the inter-linked issues on development of institutions, poverty reduction, economic growth, international trade and trade policy, income distribution, indebtedness and globalisation are interlinked and discussed, as they are given much attention in the development literature. The World Bank research of Dollar and Kraay (2001 a and b and 2002 a and b), and others, include many interesting aspects on income distribution, reduction of poverty and real or alleged impacts of globalisation.

2. Institutional differences between the post-Soviet regions and the sub-Saharan Africa (Weder)

The most common definition for transition is the process of converting the centrally planned command economy into a capitalist free market economy. Most conveniently the definition covers all FSU economies and the CEE countries. In the ranking lists describing of the transition progress of the former socialist countries towards market economy, the countries are arranged from the best to worst - or slowest - reformers as follows: 1) CEE countries (Hungary, Poland, Czech Republic, and Slovenia), the Baltic countries (Estonia, Latvia, Lithuania), 3) central CIS (Russia, Ukraine, and Belarus), 4) Caucasus (Georgia, Armenia, Azerbaijan), and 5) Central Asia (Kyrgyzstan, Kazakhstan, Uzbekistan, Tajikistan and Turkmenistan) (for instance the EBRD Transition Report, (Fries & alia, EBRD, p. 27)). The transition literature does not usually extend these rankings beyond the former socialist countries, which gained their independence as a result of the dissolution of the Soviet Union in December 1991. How the transition of other developing countries, like the one of sub-Saharan countries, relates to the transition of the CEE and FSU countries?

The typology of the CEEFSU countries in table 2 resembles the typologies of the EBRD's "Transition Reports" (the South-East European zone with Balkan countries are left out here) . The UNDP report (1997) also characterises the Czech Republic, Hungary, Poland as Central European states with democratic and institutional traditions that pre-dated Soviet era. Also Estonia, Latvia and Lithuania had pre-Soviet democratic traditions. Russian Federation, Belarus and Ukraine are the core countries of former Soviet Union in the categories 3 and 4. Together with them are lumped the Southern Caucasus and the Central Asian republics. Although the Southern Caucasus countries, Armenia, Azerbaijan and Georgia, and Tajikistan in the Central Asia have been war affected, no CEEFSU countries are ranked to category 5.

Weder grouped 150 countries, including most of the FSU, CEE and SSA countries with respect of their institutional qualities into homogenous groups by using K- means cluster analysis. The clusters were based on a number of criteria (see table 2). Weder chose the criteria from the view point of the market development: (p.4):" The underlying concept is that a market economy can only operate if there are certain rules of the game and, in particular, that property and contract rights have to be defined, and there have to be mechanisms that will credibly enforce them" (Weder 2001, p. 4).

A well working institutional framework guarantees these rights by enforcing them against violation by third parties as well as by the state. For instance, corruption, discretionary action of bureaucrats, unpredictable changes in rules and policies, unreliable judiciaries are all means by which the state can de facto expropriate private agents." By using cluster analysis, the former socialist countries and a number of other developing countries, including a number of sub-Saharan countries were brought to comparative context by arranging them into 5 categories from highest (1.) through intermediate (3.) to lowest (5) level of institutional development and the GDP (table 2).

Table 2. Weder's (2001) typology in the Former Soviet Union (FSU), Central Eastern European (CEE) countries, and in the sub-Saharan African (SSA) countries grouping the countries according to their institutional quality and economic growth in five clusters: 1. Highest, 2. High, 3. Intermediate, 4. Low, and 5. Lowest.

FSU & CEE				
1.	2.	3.	4.	5.
Czech Rep	Latvia	Armenia	Azerbaijan	
Estonia	Lithuania	Georgia	Belarus	
Hungary	Slovak Rep	Kazakhsta	Turkmenistan	
Poland		Kyrgyz Rep	Uzbekistan	
Slovenia		Moldova	Tajikistan	
		Russian Fed.		
		Ukraine		
SSA				
1.	2.	3.	4.	5.
	Botswana	*Benin*	*Angola*	*Sierra Leone*
	Cote d'Ivoi	*Burkina Fa*	*Chad*	*Somalia*
	Gambia	*Cameroon*	*Congo*	*Sudan*
	Ghana	*Gabon*	*Guinea-Bis*	*Burundi*
	Namibia	*Guinea*	*Kenya*	*Cape Verde*
	Tanzania	*Lesotho*	*Liberia*	*Central African Republic*
		Madagask	*Niger*	*Comoros*
		Mali	*Nigeria*	*Congo, Dem. Rep.*
		Mozambiq	*Togo*	*Equatorial Guinea*
		Senegal		*Eritrea*
		Swaziland		*Ethiopia*
		Uganda		*Malawi*
		Zambia		*Mauritania*
		Zimbabwe		*Mauritius*
				Mayotte
				Rwanda
				Sao Tome and Principe
				Seychelles

Based on the results of her analysis Weder notes that

- The EU accession countries, Czech Republic, Estonia, Hungary, Poland and Slovenia, already have institutional capacities are no longer distinguishable from the most advanced industrial countries. In fact, the institutional conditions are no more significantly different from those prevailing in the industrialised countries (Weder 2001, p. 18),
- There are large differences in the institutional performance between the groups of economies of the FSUCEE and the SSA. (p. 3),
- Measured by their institutional quality and GDP, the countries and groups of FSUCEE and the SA countries are overlapping
- The institutional variables are shown to closely associated with investment and growth (p. 4), but the direction of causality is not clear: probably good institutions could be expected to promote economic growth but could the economic growth and investments also promote improvement of the institutional qualities?

To verify, whether the differences in institutional qualities can be observed in economic freedoms and financial country risks, the latest available panel scores of the 2002 Index and Euromoney were inserted in the Weder's typology of institutional quality.

Table 3. Criteria for Institutional Quality (Weder), Economic Freedom (2002 Index) and Financial Coutry Risk (Euromoney)

Institutional Quality, Weder	2002 Index of Economic Freedom	Euromoney, March 2002
Rule of Law	Trade	Political Risk
Low Graft	Tax burden	Economic Performance
Low Regulatory Burden	Government Interventions	Debt Indicators
Accountability and Voice	Monetary Policy	Debt in defoult or rescheduled
Government Effectiveness	Foreign Direct Investments	Credit ratings
Predictability of Rule Changes	Banking and Finance	Access to Bank Finance
Credibility of Gov. Announcements	Wages and Prices	Access to short-term Finance
Information about Changes in Rules	Property Rights	Access to Capital Markets
Consultation	Regulation	Discount for Forfaiting
Property Rights Enforcement	Black Market	
Judiciary Reliability		
Predictability of Bribes		
Freedom from Discretionary Bureaucrats		

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To see how some other indicators relate to Weder's typology (table 3), scores of economic freedoms according to the Heritage Foundation/Wall Street Journal (Freedoms 2002) and financial risks according to Euromoney were assigned to Weder's typology according to individual countries (total scores by country shown in appendix table 2), and averages calculated for the groups of countries as shown in table (table 4 and appendix table 1).

Table 4. Countries grouped by institutional quality (table 2), with average scores by group indicating economic freedom and financial risk

Scores from best to worst	Economic freedom 1-2-3-4-5	Financial risk 100=>0	Nr of countries	
FSUCEE1	2,5	68	5	CEE and Baltics
FSUCEE2	2,6	58	3	CEE and Baltics
FSUCEE3	3,5	32	7	Russia, south Caucasus and Central Asia & Ukraine
FSUCEE4	4,1	29	5	Southern Caucasus and Central Asia & Belarus
FSUCEE5	0,0	0	0	none
FSUCEE TOTAL	3,2	44		
Russia	3,7	36		
Nr of countries			20	
SSA1	0,0	0	0	none
SSA2	3,1	25	6	Coastal West Africa; Namibia and Tanzania
SSA3	3,2	28	14	Uganda, Madagaskar, Zimbabwe, etc
SSA4	2,8	24	9	Nigeria, Congo, Kenya, Angola, etc.
SSA5	4,0-4,3	25	18	Ethiopia, Sudan, De. Rep. Congo, Somalia, small islands
SSA TOTAL	2,7	26		
SSA5 all*	4,0			
SSA5 less islands**	4,3			
Nigeria	3,6	21		
Geand total	2,9		47	

Note: Economic freedoms are rated as "free" being <2.0, "mostly free" 2.0<3.0, "mostly unfree" 3.0<4.0, and "repressed" 4.0-5.0. Financial risks represents a total score of 9 weighted components (see appendix table 1), where the possible maximum score = 100. The 2002 Index criteria have equal weights, whereas Euromoney attaches percentage weights 25-25-10-10-10-5-5-5-5 to the nine criteria (appendix table 1).

Mastertable2002.xls table 3

The rankings by economic and financial freedoms seem to be, by and large, in line with Weder's results particularly as for the FSUCEE countries. The ranking of the FSUCEE countries persists. There are no SSA countries to challenge the accession countries; on the other hand there is number of African countries (mostly war affected) falling behind even the least developed FSUCEE countries. This result is confirmed also some other recent studies (for instance Kolodko's (2002) exercise based on GDP per head in PPP).

There are some striking differences and probably several explanations, why the rankings differ from each other. There is a 'legitimate' reason, that each query also takes somewhat different angle of view by applying different criteria as shown in table 3. The SSA4 scores best being "mostly free" and getting, as a group of countries, better scores that the "mostly unfree" group FSUCEE3 including Russia. The FSU countries, and Russia in particular, developed comprehensive state machinery along the Soviet lines with administrative practices not always conducive to the free market economy, particularly on the local and regional level. On the other hand the state administrative institutions evolved in the SSA4 countries, though not institutionally well developed, sophisticated or efficient ones, are in average more conducive to market economy and freer economies when rated using the criteria of the "2002 Index".

Similarly, ranking countries by financial risk does not match with the Weder's typology: even the least risky African countries are left behind by the most risky FSU countries (with a possible exception of Tajikistan). Looked from the viewpoint of financial risk, the SSA countries do not overlap with the FSUCEE countries. The absence of economic freedoms does not seem to imply that a country is financially risky. There are countries where financial risks are minimised through authoritarian rule shared by a more or less corrupted and rent seeking political elite, which benefits from the sale of oil concessions and other resources abroad (eg Azerbaijan). African countries in similar situation, with weak or less developed institutional structures weakened by corrupted and inept officials in the state machinery, are not necessarily able to protect efficiently enough the foreign financial interests (eg Nigeria).

Slovenia is considered safer for foreign investors than Armenia, which scores "mostly free" with regard economic freedoms, whereas Slovenia with relatively restrictive trade regime and governmental fiscal burden is ranked behind of Armenia as "mostly unfree". Here again, Slovenia, having a less corrupted but costlier state administration is considered more conducive for investors than freer, institutionally weaker Armenia, poorly endowed with oil and other natural resources.

There may be some other reasons explaining anomalies in the rankings of countries. The marching order of the 20 FSUCEE countries is fairly well established and stable during the past ten years and the panellists must be aware of this. In contrast, the ranking of the SSA countries remains more ambiguous because the marching order of the 44 SSA countries is more ambiguous and changing and may not be so well established in the minds of panellists. Being politically and economically more unstable, the latest developments in each country are likely have more weight in the assessments and more frequently change the ranking.

Also, the group averages of both regions include small and big countries with equal weight, which may distort the picture. Some African 'honkongs' pop up and catch top scores (Mauritius and Seychelles) hiding some major actors of the region. Russia's GDP in 2000 accounted for 37% of the FSUCEE region's total GDP of 684 billion dollars at current prices, the GDP of Nigeria's accounted for 21 % of the SSA's 881 billion dollars.[2] Nigeria and Russia have almost equal scores and ranked accordingly to be "mostly unfree" economies. Both of them have been ranked to be "mostly unfree" or "repressive" with regard of almost every individual criterion. With respect to financial risks, Russia leaves Nigeria far behind (appendix table 1), as does the entire FSUCEE region the SSA region (table 3).

The 2002 Index of Economic Freedom does not rank eight sub-Saharan countries, recently or still affected by war or severe social disorder. These countries are African countries, are Democratic Republic of Congo (formerly Zaire), Sudan, Eritrea, Somalia, Angola, Burundi, Liberia and Sierra Leone. Including

[2] Regional averages weighted by country GDP's would not bring any essential change to the ranking.

these countries and assigning each of them the lowest score of 5 for economic freedom, the total score of group 5 becomes 3.9. Leaving out the midget-state islands, such as Mauritius, Seychelles, Sao tome and Principe, many of which have at least moderate scores, the average total score goes down to 4.3,indicating "repressed" economic situation. Lumping the both groups together allows slightly higher average of 3.9.

The ratings of economic freedoms have improved since 1996 fastest in the CEE and Baltic countries, around 3 per cent a year, whereas the improvement has been more modest in the Rest of the region. In Russia, the ratings have worsened by 1 per cent a year. In the SSA the improvement has been somewhat more modest than in the FSUCEE. The most prominent improvement in ratings have taken place in the groups SSA3 and SSA4. In the SSA Botswana, Mali, Ivory Coast and Namibia obtained improved rating particular from reduction of black markets. None of the SSA countries obtained rating of "free", but first time some of the countries (Botswana, Ivory Coast, Mali and Namibia) are ranked as "mostly free".[3] The property rights, regulation and black markets, but also banking and access for the FDI, continue to be rated as the most depressing factors both in the FSU and SSA countries.

3. Role of institutions in promoting markets and economic growth

3.1 State and government

The terms ‘state’ and ‘government’ and 'public sector' are used interchangeably in the textbooks. In the standard usage of the Anglo-Saxon literature, the government quite often refers to the political leadership named according to the president or prime minister, but quite often the references to the "Russian government" or "U.S. government" seem to include, more or less implicitly, the political leadership and the entire state apparatus. Quite often the political management is referred, although the success or failure of government or political management usually may depend on the availability of support of state institutions, or lack of this support (Marangos 2002). For the purposes of this study, however, there is a need to differentiate between the terms state and government, and also between strong government and large government.

‘State’ denotes the territory and the administrative machinery available for high-level political decision makers (head of state, government) of a society to exercise sovereign political power. The machinery consists of ministries, central offices and central bank, army, police, customs, tax authorities and security services, or more generally institutions, which represent security, continuity and technical-administrative know how of people, which is not changed due to political elections.[4] There are number of services,

[3] In this study South Africa, also with rating of "free", is not counted as SSA country.

[4] State can be understood as a social contract between members of a group of people deciding to organise structures to maintain law and order, protect themselves by army and police force against external threats, produce basic indivisible infrastructures like transport networks, production of energy and take care of basic health and social services etc. The state consists of

which are often provided by state, but are in some countries provided by private enterprises, often as a result of privatisation (postal services, railways).

State consists of institutions and organisations: Institutions represent the formal and informal rules of the game affecting economic performance and costs of production and transactions. Organisations consist of groups of indivieuals bound togeher by common objective function, like maintenance or changing the institutions by accordingly enforcing the formal and informal rules. The state is governed through ministries and executive organs under them, but usually also the legislative bodies, supported by political parties. Settlement of disputes and application of law belongs to independent judiciary bodies (1997).

The term 'government' is used to denote political rule and administration, that is, system or form by which a society is ruled. It is part of the state machinery, but narrower and changing according to the results of political elections. The government consists of people receiving and leaving their posts as a result of political elections (president, ministers, members of parliament and their personal assistants in the central, regional and local government).

Normally governments or rulers come and go, but states are more long-lived. Still, he states may be born or ended by a war or peacefully as a result of historically exceptional development, like the termination of the Soviet Union or East Germany).[5] The state of the Soviet Union ceased *de jure* on 21 December 1991, during Gorbachev's reforms lessened the possibilities to monitor the doings of rent seeking bureaucrats at lower levels of hierarchy. This corroded the authority structures of institutions and incentives of individual bureaucrats acting in the machinery. They started their opportunistic 'bank runs' to expropriate the state assets. This undermined the state's autonomy (to formulate its policy preferences independently from societal interests) and capacity (to successfully achieve the goals it chooses to pursue), central elements of the authority structures of state institutions. Subsequently, the Soviet state machinery was disintegrated, with exception of the army, prior to the de jure end of the Soviet state (Solnick 1998). Unfortunately, the administrative traditions resiliently burdened by the excessively opportunistic behaviour introduced in the Russian state administration many unfortunate Soviet legacies, like excessive bureaucracy, corruption, patronising and coercive treatment.

In Africa the end of the European colonialism marked the birth of new independent states. Since their independence the African countries have experienced numerous changes of their political leaders and governments, while the states remain. Many of the African states are weak not very well established as a result of war or if challenged by large ethnic groups within the territory. This is the case when the state has not been able to generate enough social capital through democratic practices to persuade all its members to share the values. Instead, an authoritarian government may, by using force and violence and repressing the political freedoms, impose values not shared by a large part of population. Sometimes the change of ruler of rulers may be reflected through the change of in name of the state (Zaire to Democratic Republic of Congo). Quite often as major part of the institutions, the officials, and the administrative practices remain unchanged, though the rule may have changed.

Many African political leaders and others believed that only gaining the independence and making plans and programs would solve problems (also Olcott). As it turned out, the declaration of independence is not a political solution, independence solves nothing by definition. It is just a change of juridical status. It is not a source of better life for the citizens. It does not necessarily imply any greater independence for na-

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large machinery with large powers to enforce the law and order and to run these functions under the auspices of ministries and contemporary government. The state comprises also independent judicial system.

[5] For example, the state of the Soviet Union ceased *de facto* through the Minsk declaration of 8 December 1991 about establishment of the CIS, signed by Yeltsin (the Russian Federation), Shushkevitsch (Belarus) and Kravchuk (Ukraine)(Izvestiya 9 December 1991), and as a state *de jure* on 21 December 1991 through the declaration of Alma-Ata (Izvestiya 23 December 1991); its territory was narrowed down to the territory of the Russian Federation. The last government of the Soviet Union, with prime minister V. Pavlov, were fired in August 1991. In fact, the Soviet Union had no prime minister proper during the last months of its existence. Pavlov was followed by Ivan Silayev, who was acting prime minister of the Russian Federation up to 20 September 1991. The actual power had been taken by Boris Yeltsin. Yeltsin took over the position of the prime minister of the sovereign Russian Federation in September 1991, and was thereafter followed by Gaidar in June 1992.

tionalities, ethnic groups or individual people. Poor maybe grow poorer and rich richer. It may be important to the ruling group of country, who may use the arguments above to appease the population in the beginning. This goes for African countries, in particular. The problems were lack of investments in education, lack of interest in raising the levels of living standards and reduction of unemployment, and solving the problems of the sluggish economic growth (Smirnov 1999, p. 150).

In Africa, the European colonial powers drew the boundaries to suit their mutual convenience without regard to local traditions or ethnicity. When the colonial powers left Africa during the twenty years after the end of the Second World War, 22 states emerged from French colonisation, 21 for British, 5 from Portuguese, 3 from Belgian 2 from Spanish (Maddison). The access of people with education and administrative experience was scarce. The new political leaders had to create national solidarity and stability from scratch. These developments were disturbed by the cold war rivalry,. China, the Soviet Union, East European countries and Cuba supplied military aid, assimilating the political leaderships in Africa with the conflict of interests. According to Maddison (p. 56): “ - - Suddenly, these countries had to create a political elite, staff a national bureaucracy, establish a judiciary, create a police force and armed forces, send out dozens of diplomats, find school teachers and build up health services. The first big wave of job opportunities strengthened the role of patronage and rent seeking, and reduced the attractions of entrepreneurship. The existing stock of graduates was too thin to meet the new demands and there was heavy dependence on foreign personnel.”

3.2 Social capital

Social capital, the democratically consolidated political will of people, is formed through political parties, NGOs, interest groups and mass media to parliament, which legislates it into enforceable norms. The norms are enforced by ministries with sector responsibilities. The pattern is often replicated on regional and local levels, to which parts of the decision-making and enforcement powers have been delegated. The president or king remains as the formal head of the state, whereas prime minister is the head of the government with mission of the political authorisation to implement the mission given him through the democratic elections. Deficit of social capital explain much of the institutional backwardness in the SSA, in the CEE and FSU. The CEE and Baltic countries are often said to be in better position, than Russia and new independent states, because been neighbours of Western European countries and having had period of free market economy in the past.

Formation of party system is essential, because it serves as a base for selection of members to parliament. In a developing or transitional economies a large number of factions related to political leaders or irrelevant and sometimes less serious issues.[6] The large number of factions with limited programs only confuse and frustrate potential voters and ultimately fails to create social capital. The essential dimension in creation of social capital is by democratic means achieved compromise about division of funds between growth supporting investments and production of public goods and services. The trade unions, where the employees and employers agree on wages, supplement the system. The demarcation line goes between the defenders of free markets maximising the economic growth versus the redistribution of the results of the economic growth to increase the well-being of population (or rightist-leftist, republicans-democrats, tory-labour etc.). Mechanisms to create social capital are necessary, because the redistribution represents an infringement of private property rights and economic freedoms, but do not exclude the possibility that optimally the redistribution also supports the economic growth by reducing political instability and creating purchasing power.

[6] For instance, the beer drinkers party, was one of the 78 parties, movements and unions, between which the Russian voter had to choose in the Russian parliamentary elections in 1995, (www.nns.ru/parties/parties.html).

Due to absence of social capital created by democratic freedoms the dictatorships have been short-lived, in the historical perspective. Authoritarian states tend to become corrupted and having leaders, governing by terror by means of strong propaganda and limited civilian rights, army, police and secret police against the political opposition and dissidents. In a number of African countries and in Caucasus or Central Asian countries there exists a strong presidential rule governed by president and his office, while government, parliament and parties work under the president's surveillance and serve as the window dressing to gain the acceptance in the eyes of western societies and aid organisations. The dictatorships both in Africa and in the CEE and FSU have implied full stop or backlash in the development of market supporting institutions and administrative practices. Currently, the most obvious example of dictatorship is Belarus, with declining economy and financing its budget mainly by exports of weaponry.

All CEE countries and the Baltic countries have been able to generate enough social capital to operate as genuine democracies. Aside of the CEE countries, virtually all FSU and SSA countries are clan states despite their formally democratic constitutions and institutions. Clans (families or regionally organised families), consisting of informal groups or networks, appropriate the property and convert them into power (or other way round). In Russian transitional systems well-placed individuals concentrated assets in their own hands taking advantage of uncertain property rights, under-developed legal systems, and poor investment conditions (Johnson 1997, p. 360). As a result of Soviet era institutional legacies and difficulties in the economic transition in January 1995 there were one hundred financial-industrial organisations including 9 banks, 98 enterprises employing 365000 workers. In April 1997 there were 62 financial-industrial organisations including 77 banks, 856 enterprises employing 3.2 million workers (Johnson 1997, p. 337). The difficulties of transitional condition implied uncertain property rights, underdeveloped legal system and poor investment conditions, which allowed well-placed individuals to take assets in their own hands (360).

Åslund found a connection between corruption and the size of the public sector: the larger the public sector’s share of the GDP, the more there is room for corruption, because a large corrupted sector makes the country more corrupted than a small corrupted public sector. As Åslund concludes self, the statistical material is not quite convincing, because the share of the public sector of GDP is in the CEE countries 40% but for instance, in Armenia, Georgia and Kyrgyzstan 25% and in Tajikistan and Turkmenistan 20% allowing us to conclude, that the latter countries were less corrupted than the former ones. (pp. 152-154).

On the other hand, for instance La Porta et alia found consistent evidence that better performing governments are often larger and note, that labelling big government to bad government can be highly misleading. The number of ministries, state committees and governmental departments do not vary much by the size of the country; however, a large territory my require hierarchical structures to make the public services available to all (UNDP 1997, pp. 16-22). In a welfare state a relatively large bulk of existing legislation predetermines major the level of government expenditures. The governments are tied by this legislation and can usually only marginally change the size of the budget.

The size of the state is quite often determined by the size of the territory. To extend supply of public services over a large territory requires large officialdom and infrastructures (buildings, transport and communications). Often the institutional structure has central, regional and local levels. If sparsely populated, the expenditures per capita may be heavy. The expenditures also depend on degree of diversification, quality and degree of privatisation of the public services.

The state may be small or large. It may be strong (function efficiently and well) or weak (function inefficiently particularly if contaminated by personal rent-seeking and corruption. Provided that state acts observing values and incentives shared by citizens, it may create enough social capital to persuade citizens to agree on high tax rates, necessary to cover high expenditures. Citizens may freely opt for heavy state structures and associated high taxes, should they feel that their welfare optimum (including also security, environment, social safety nets) is not warranted by free maximisation of private profits (Easterly, UNDP 1997).

In sum and schematically, there are good states S_g and bad states S_b as well as good governments G_g and bad governments G_b. In this context, 'good' ($_g$) may be defined as efficient, non-corrupted, benign or treating rightfully and with respect all subjects, has strong social capital, and supports the growth and development of corporate sector. 'Bad' ($_b$) would stand for the exact opposite. Then G_gS_g would represent a developed welfare state, where the government takes good care of all physical and juridical persons and the public sector share of the GDP might be fairly large and legitimately, but not necessarily. G_bS_b can still accommodate many SSA countries. The G_gS_b comes close to Russian situation, where corrupted state with Soviet legacies bogs down even good reforms by not enforcing the legislation, particularly in the area of property and contract rights. The CEE, and Baltic countries are on their way towards G_gS_g, whereas rest of the non-Russian FSU (with possible exception of Belarus, Ukraine, and Turkmenistan) have started to take distance by developing their institutional capacities with support of the western technical assistance. Finally, the G_bS_g might be fairly rare and describe situation, where an authoritarian regime is about to take over the power by transforming the S_g into S_b.

Formerly centrally planned economies differ from other developing countries in having inherited large institutional structures, created by state. The share of state sector of the value added was 96% in the Soviet Union in 1996, more than 90% in Czechoslovakia, East Germany and Bulgaria, around 80% in Poland and 60-70% in Hungary in the 1980s. In the OECD countries the share was less than 20% excluding the government services but including commercial state owned enterprises. In African countries the share of the government is varied from close to zero up to 30% of GDP in the 1980s. For example, the share of the state sector in Malawi was 25% in 1984, in Kenya 15% in 1984 and 10% in Niger in the 1980s.

The distinction between government and state is important. The Russian government presently has a reform oriented government, but it still has Soviet state machinery and growing officialdom.[7] One reason is the increased independence of regions and localities to govern the entire Russian territory. It still is not able to serve the ends of free market economy. In so doing it has prohibitively slowed down the development the Russian corporate sector as well as growth and diversification of foreign trade through bureaucratic customs procedures. The enforcement of property rights its still unclear despite the recent reform legislation. It still will take decade or two, before the Russian officialdom in the state machinery and judiciary learns and agrees to enforce the prevailing legislation without bribes and cronyism, as friendly and benign civil *servants*, not as powerful administrators and bureaucrats.

Many African states' institutional capacities are still missing or inadequate. Many states are too weak to defend their own citizens against natural catastrophes or misuse of political power. Nor are they able to provide adequate infrastructures and public services not to support their economy, or attract FDI. They may not have adequate human and financial resources or even be sovereign on their own territory. Parts of population living within the boundaries of the territory may not be covered of any public, or private, for that matter, services. As noted above, however, there are big differences between the SSA states as to their institutional qualities, institutions based economic freedoms and financial risks due to corruption and absence clear and enforceable property rights.

[7] The officialdom of the Russian state machinery consists of 3 million administrators and bureaucrats (excluding army, education, health and social services), twice as many as ten years ago.

3.3 Economic freedom, property rights and rule of law

Economic freedoms

Having defined the concepts of economic freedom, property rights and rule of law, and their functional relationships as a base of state and state institutions will be further elaborated. Hoskins & Eiras (2002) the economic freedom includes the exclusive right of individuals to use their resources as they see fit as long as they do not violate someone else's rights, and the ability of individuals to transfer or exchange these rights on a voluntary basis. The enforcement of these economic rights is necessary condition for existence of market economy. On the other had, these freedoms are constrained by the amount and quality of the property, which belongs to an individual. Poor people have therefore little, if any, economic freedom, because their resources on which they can apply "their exclusive right" are small. A popular of vulgar misinterpretation is economic freedoms is also, particularly economies in transition, that money gives freedom and power, in particular, without regards of others' rights. Excesses are made possible by badly defined and perceived property rights and faltering rule of law. This is not correct, because the market economy does not pretend to be without restrictions. *The market economy is considered to be least restrictive, because, if orderly enforced, it can be expected to provide equal opportunities to all.* Everyone has a chance to maximising one's economic freedoms through earning more money, wealth, though without violating the others rights to do the same. What the market economy does not promise, is equal income, and wealth to everyone.

The principle of freedoms without violation of the others' corresponding freedoms is incorporated in the principle of 'rule of law'. Essential feature in the rule of law is that both rulers and those to be ruled have equal obligations, particularly with respect to the property and contract rights. The political and economic freedoms are optimised and risks for potential investors minimised, provided that there exist adequate institutional base to run a market economy. Such an adequate institutional base calls for property and contract rights and rule of law. These are preconditions for creation of good bureaucracy aiming and creation of wealth through operational capital markets including land, real estate and all other kind of property values. Such a good bureaucracy needs to be supported not only by independent and non-corrupt judiciary, but also other public and private institutions. The question then arises - and is raised by de Soto and a number of other writers, why the transitional and developing world has, by and large, failed in developing institutional base conducive to free market economy while the developed industrial countries have succeeded in doing that.

The property consists of material and immaterial property. Material property is more of less obvious comprising of land, and man-made structures and pieces of any kind. Immaterial values extend to a person's professional, religious and political opinions hand his right to express them (intellectual rights). They include also safety and liberty of his person, free use of his faculties and free choice of the objects on which to employ them. Based on this Hoskins and Eiras conclude, for instance, that workers, for example, should be able to work 12-14 hours a day and seven days a week if they choose to do so. Government or trade union interference in the form of heavy taxation or requirements for minimum wages, minimum annual vacation and other similar rules, infringes the property rights and slows down the economic growth. According to Hoskins and Eiras, " - Regulation affects economic activity because it interferes with private property rights … by attempting to modify, supplant, or replace market outcomes with outcomes mandated by government." (Hoskins and Eiras 2002, p. 42). - These extensions of the economic freedom lead to the neo-liberal model, where the share of the state and its influence has to be minimised. The subject will be recapitulated later on.

Property rights

Sven Hedlund describes well the development of the philosophy of ownership and contract rights from the antique and Roman times. The medieval era of feudalism seems to be watershed between the west and east. In the west lord and vassal had mutual rights and obligations and the vassals had right and implicit duty to rebel if lord failed to hold the contract. Numerous rebellions served to reinforce the contractual aspects. In Russia again, the ruler not only held autocratic power but also laid claims on all productive assets. Thus even the nobility could only possess as compensation for life long service, but not to own it. In the Russian case the laws were instrument of power, in contrast to western or Roman law, where the rules were made by the elected representatives of people so as to regulate the relations between citizens and relations between them and their government. In Russia the law served as an administrative device, not as a set of rules governing the position and acts of state officials. In sum, the west inherited the tradition of rule of law, the east the rule by law Hedlund 2001, pp. 217-222).

The institutions carried these legacies up to 21st century. The contemporary competitive market economies are essentially operated in rules based societies with enforceable contractual property rights. The Soviet regime introduced collective ownership, use of which was dictated by Communist party by means of centrally planned huge bureaucracy. Despite the emergence of state and government, there were no private property or contractual rights. As Hedlund puts it, " In such a (Soviet) system, as it had been in old Russia, there can be no rights, only mercy" (Hedlund 2001, p. 224). This system, in the absence of private property to be taken care and defended, in the absence of free competition and incentives, the system could be run by administrative orders, and lubricated by bribes, corruption (blat) and personal relations and networks, and barter (Pipes 1974, Olson 1995). Collective ownership led to bad maintenance and deterioration of property; the lack of individual host implied an incentive for theft.

Olson (1995) notes that Stalin established in the twenties extremely repressive system from the viewpoint of private ownership (where the autocrat expropriated virtually all natural and tangible capital stock by levying a 100 per cent wealth tax and then to invest these resources to product capital goods. This explains the extraordinarily high capital accumulation in the former Soviet Union financed by tax receipts by an amount almost equal to all non-labour income. Stalin used implicit taxation by taking virtually all profits of state-owned enterprises instead of explicit taxes on individuals. Olson notes that no other autocrat in the history has succeeded in this scale state banditry and the to increase savings, investment and national output (446). Besides the forced labour, also all other labour was made available at a fairly low cost through collectivisation of labour and life.

Olson notes that when an autocrat insists on obtaining 100 per cent of the rents, profit, and interest earned by the natural resources and tangible capital of his domain and also sets the wages of workers in order to maximise the implicit tax on labour, there is *almost no private property or privately managed production to be guarded by subjects in their own self-interest*. The fixed assets, inventory, and inputs of every significant enterprise belong to the autocrat, who is then *the only person who has an automatic incentive to keep them from being stolen*---". In contrast in the market economy based on private ownership "--each subject tends to protect his property, and this makes it possible for a traditional autocrat to keep theft among his subject within bounds and also limits the exposure of his officials to bribery (Olson 1995, p. 455)."

For these reasons the growth of the Soviet economy was fairly rapid during the first decades due to the high rates of investments, despite of the slow growth of the total factor productivity. By virtue of these efforts, the Soviet Union was build a basic heavy infrastructures consisting of power stations and transmission line, transport infrastructure of railroads and channels, and still since the sixties and seventies, a comprehensive oil and gas pipeline networks. The backlash and decline of the Soviet economy was created due to the fact, that the implicit taxation ran against the incentives of workers and mangers in the bureaucracies, which colluded to start siphoning. The separate collusion and special-interest organisations ceased to share the encompassing interest of dictator and the politburo at the centre to increase the productivity of the society.

What the Russian feudalism and Soviet system did to ownership rights or responsible governance in the FSUCEE area was accomplished by colonialism in Africa. The African countries are young ones, their independence goes back 30-40 years, and colonial boundaries divided population, ethnic groups and resources arbitrarily. Also rapid growth of population created disproportion to resources and disability to create economic growth in per capita terms (Smirnov 1999, pp. 143-144).

Colonialism did not acknowledge or honour pre-colonialist property rights, but sooner served as an example of predatory extraction of natural resources and labour force without any responsibility of obligations to the local population. The development of Botswana offers an interesting exception. According to Acemoglu & alia (2002), the good institutions (private property rights and rights to invest) have been in place and enabled to conduct good economic policies. As a result, Botswana had exceptionally high growth rates (7.7 % in 198) and reached PPP-adjusted income per capita of 5 796 in 1998, nearly four times the African average.

The inherited pre-colonial institutions placed constraints on political elites. Secondly, the British colonialism was only marginally interested in Botswana and therefore did not destroy the institutions. Maintenance and strengthening of the property rights both against state expropriation and predation by private agents was in the interest of the cattle breeding rich elite, which had also possibilities to accumulate their property via investments. Botswana is rich in diamonds, which constitute a good base for economy. On the other hand, there are other countries (Democratic Republic of Congo, Liberia or Senegal) also rich in diamonds and other resources, which have served as sources of problems and reasons for their dismal economic and political records.

Also the comparison with other SSA states confirms the importance of the pre-colonial institutional inheritance not perverted by colonialism. Although Somalia is relatively homogenous nation, it came to preserve dysfunctional institutional inheritance. Somalia an population share nomadic institutional structure with identities of culture, language and religion, but inherited factional conflicts originating from the perennial competition between clans over scarce resources. The institutions did not place constraints on political elites fighting against each other and forming coalitions along clan lines. The Boer War and the British support to the political leadership of Lesotho during that time undermined the traditional *kgotla* institutions of Lesotho, which had placed constraints on political leaders. Also the evidence about institutional developments of Ghana and Ivory Coast bear evidence, that the lack of constraints on the political leadership creates political and economic instability and leads lower rate of economic growth (Acemoglu & alia, 2002).

There any property in transitional economies and developing world, not having clear and transparent property and contract rights - and subsequently also the economic freedoms would be ambiguous and restricted (de Soto 2000, Olson 2000). Hedlund (2001) points out that in the absence of solid and enforceable property legislation and a benign bureaucracy to enforce it, there cannot - by definition - exist property, but only possessions in a way like (citing Olson) "the dog possesses a bone". Taken literally, there is no property in developing countries, but only possessions. There are two consequences: first, the material capital in transitional and developing economies is dead, stalemated, due to high costs of bad bureaucracy. Second, the size of non-legal economy is large, because most of the enterprises cannot afford to pay the costs of legalising their entry (or the exit or any other dealings, for that matter).

The legitimacy of bureaucracy

Freedoms do not materialise when an adequate institutional set-up is missing. De Soto points out in his important book that bad bureaucracies prohibit capital from growing, but growth of capital cannot be guaranteed without good bureaucracy. A good bureaucracy has to be based on unambiguously defined enforceable property, contracting rights and rule of law. Property as an economic concept represent the transformation of the physical property objects into shares, bonds, deeds, bills of sale or other kind of claims or contract carrying all essential information from the qualities of the underlying physical objects, based on which their economic or commercial value can be derived. Fixing the economic potential of assets by describing the property's economic and social qualities and registering it, the property is brought "from the material world into the conceptual universe where the capital lives" (de Soto p. 42).

A good bureaucracy 1) integrates dispersed information onto one system to make the property information standardised and universally available, 2) makes people accountable implying that each property has to have an owner who can be located, 3) networks people, 4) protects transactions, and 5) makes assets fungible. The fungibility implies that any physically monolithic bloc of property, once transferred to "the conceptual universe where the capital lives" can be divided in shares to be sold to different owners and included to their respective portfolios consisting of different kind of property values. The security of both the ownership and transactions transferring the ownership rights have to be publicly and privately guaranteed and insured. Awareness about easily accessible conveyer belt markets with standardised procedures and low transaction costs contains also an incentive to take care and improve the material property, because the improvement can be expected to be reflected in the market value of the paper at its sale. In Russian privatisation process, much of the property was purchased at low prices (for instance in closed auctions) just to get it sold at higher price without any improvement of the underlying real property.

Prohibitive and corrupted bureaucracy precludes the capita from growing. In the primitive bureaucracy the burden of proof lies on the citizen, not on officials.[8] That implies, in practice, that every citizen is considered by state official a potential criminal until he is able to produce required documents and verifications to comfort the official. Often the official has vested with wide powers of deliberation to decide the, which opens the doors for corruption, and underline the importance to know the "right persons". Hence, the officials (in customs, police, tax office) have a strong incentive to maximise his administrative power and extract bribes, because he knows, that there are no risks of complaints, but "only mercy". Such a bureaucracy is inefficient and costly; main reason why a major part of entrepreneurs and other agents in the transition and developing economies opt for staying extralegal.[9]

Another important technical reform, necessary for creation of the "conceptual universe where the capital lives" is introduction of the international accounting standards. The introduction of international accounting standards requires purely technically, several years. People have to be trained, data collection rearranged, internal and external audit function established and organised. To make well-defined property rights transparent, property values and changes of those values must be in books. When buying or selling the property, all claims affecting the value of the property must be found in the books. Audited accounts, indicating profitability, liquidity and solvency and value of the collateral as well as project analysis about

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[8] The individual's supremacy over the state and the separation of powers are enshrined in the constitution of the Russian Federation. In practice these stipulations are watered down through other legislation related to vertical power structures and dictatorship of law (Berezovsky 2002).

[9] The Goskomstat makes an allowance for shadow economy of about 25% to the GDP statistics, though according to some experts, this allowance should be larger, perhaps 50% added to the registered GDP. Due to the prohibitively costly entry, most enterprises start and also keep their transactions stay extralegal, although hey were not illegal (tax or customs duty evasion). In the beginning of 2001 there was 2.9 million firms, of which 51% did not give profit and loss calculations of balance sheets. Of the Russian firms ¼ or around 740000 enterprises are located in Moscow. Of these enterprises 65 % do not file in any tax declarations, and about 70% of them do not pay any taxes (Rytkönen 2001).

the profitability of the project to be funded should be available for a prudential bank director or loan officer in commercial bank. Awareness about competition should provide enough incentives to ensure that the funds will be then allocated efficiently. For the time being in most FSU and SSA countries "business plans" are prepared describing eloquently the firm and its past and planned activities, but the bottom line, information based on audited standardised book keeping, remains missing.

De Soto's notion of the importance of replacing restrictive bureaucracies with liberal ones is noteworthy and also conducive in promoting property, replacing the incentives to co-operation to grow the economies through market economic practices. Problem is, that to create them takes decades and can be disrupted in the weak states. There are disputes to be solved about assigning property rights to new settlements, to squatters, often infringing the rights of former owners. The technical implementation of the infrastructure "universe where capital lives" may take decades to implement in any country; another decade is perhaps needed before a credible and liquid market will emerge.

3.4 State and markets

The juxtaposition state and market is unnecessary and can be grossly misleading. Particularly at the beginning of the 1990, when faced with the state run socialist countries, reformers insisted a minimalist state and encourage sharp reduction in government and public expenditure, leading deterioration of the quality of public administration (UNDP 1997). The state exist to promote and co-operate with market. The markets consist of consumers and investors, employees and entrepreneurs, physical and juridical persons, and the state's task is to protect and advance their interests within a framework of democratically agreed rules.

Quite often the development literature neglect the historical fact that the state has been there at the outset to arrange the provision of the basic material infrastructures: energy production and distribution, transports and communication, and the basic local or municipal utilities. It organises the enforcement of security, enforcing law and order (police and army), as well as basic judicial educational and health services. The primary initiative has come from the state, and only once the private sector and markets are made more functional, traditionally state run functions have been increasingly privatised. Still, the courts, army and police forces, or, for instance, lighthouse services, are publicly produced. The private initiative has been more casual and supplementary in the beginning but increased, once the market has started to in crease. In the absence of well functioning legal markets and badly functioning state in the FSU, mafia takes care of some services, which in more developed societies with well functioning state and a corporate sector, sophisticated enough to share a part of supply of public services.

In the historical perspective, the military and economic rivalries between the European nation-states prompted the national states to develop agriculture, commerce, technological innovation , for instance, in areas of shipping and weaponry. To make the capital to earn interest forced the political leaders (rural nobility) to allow the private entrepreneurs (merchants in cities) to have power and wealth. This led then to development of banks, firms and stock markets, and in general, reallocation of society's resources both in public and private hands to mobilise these resources to earn returns and accumulate wealth. The conceptions of time and competition were introduced, while these developments were not observable in Asia or Africa (Scott 2001, 172-173). With emigration from Europe these developments were transplanted to Northern America.

Demand for market-supporting institutions may arise from the creation of markets; the supply of institutions depends on the governments and its responsiveness to introduce benign governance in the state administration. The state is expected to withdraw from direct interference and directing economic activities by restrictions and regulations and, instead, create a supportive attitude towards markets and private entrepreneurs and provide them with equal access to public services) (EBRD Transition Report, Fries & Raiser & Melvin (EBRD)(p. 39).

Since the Cold War period bi-polar thinking that had a strong influence in a number of SSA countries, the the dissolution of the Soviet Union marked an improvement in the general political climate and economic thinking. This has led to growth of output and real capital income as well as some social improvement. Countries, which have pursued reforms by promoting the market economy and liberalised the foreign trade for more than ten years, are Botswana, Mauritius and Uganda, and later joined by Benin, Burkina Faso, Mozambique, Senegal and Tanzania).

Still in the 1970s and much of the 1980 most African countries governments used to control prices, interest rates and exchange rates and to restrict production, distribution and trade to achieve economic and social progress (Smirnov). At the same time governments pursued expansionary fiscal and monetary policies and financed the budgetary and public enterprise deficits by domestic and foreign borrowing. This, aggravated with corruption, negligence of social services development, political instabilities led to the situation in which the countries turned into heavily indebted and poor countries. In fact, most African countries resisted adopting the market oriented policies and reforms, which led to stagnation of decline of their economies and increase of poverty (Calamitsis 2001, p. 11).

Development of markets are based on institutions, which reduce transaction costs caused by inadequate information, define and enforce property rights and minimise barriers to entry of new participants. Institutions assist to manage risks from market exchange, increase efficiency and raise returns. Formal institutions include rules written into the law, codified and adopted by governments and public and private institutions and organisation, informal institutions refer to unwritten rules of game based on cultural tradition, religious or ethnic ties and trust. Governments play an important role in providing public goods such as defining property right and judicial services to enforce these rights and establish the rule of law (World Bank WDR 2002, pp. 5-7). Competition between firms catalyses the development of corporate law (World Bank WDR 2002, pp. 20-21)

Weak institutions hurt poor people. Demand for bribes and unofficial fees hit hardest poor people, because they cannot protect themselves from crime. Growth supporting market institutions can reduce their vulnerability. For instance, financial institutions may help to reduce risks by allowing then to diversify their savings and smooth their consumption over good times and bad (World Bank WDR 2000/2001)

In his critics of the de Soto's book, Woodruff (2001) maintains that de Soto makes land titling "to sound like a free lunch" but does not seem to take into account wider needs for creation a modern market econ omy, like improvement of legislation (p. 1223). It is a 'single-bullet' theory of development failing to see, that reality is much more complex (Samuelson 2001, p. 211). On the other hand, de Soto does not explicitly refute other necessary institutional capacity building. If constructively understood, de Soto's point is , that land titling locates on the critical path of the transition.

A ancillary, reform necessary to support de Soto's system would be, for instance, introduction the international accounting standards, as banal as it may sound. Enforcement the IAS system is also a technical requirement, a 'single bullet' idea. Without them, also other institutions, listed below, would not function properly and efficiently. A firm cannot be managed in a market environment without knowing the profitability, liquidity and solvency. A bank can hardly reasonably evaluate the creditworthiness of a potential borrower. Standard accounting system is a vital part of the economic transparency and information to transfer the price signals to economic agents so as to affect on their behaviour. the necessity of large legislative work is necessary and building a executive and judicial capacity and the necessity of the comprehensive and time consuming work. The idea of standardisation should be also extended to production, because harmonisation of standards forms a base for development and growth for international trade.

Also de Soto's "conceptual universe where the capital lives" requires at lest following institutions or activities to function:

- Stable money: there must be adequate amount of means of payment (coins, notes, cards, cheques, electronic money) serving as legal and generally accepted medium of exchange for settlement of any claims, unit of account and store of value. This implies also sound macro-economic policies from the government.
- Rights: a deal must have a legal contractual base. They must be sanctions and procedures and institutions to enforce them, that is, a non-corrupted judiciary.
- Ownership: buyers and sellers must know, what they own and are entitled to sell. A comprehensive register, accessible for all, must exist.
- Financial transparency of government, private enterprises and financial institutions to ensure the information base to enable competition and financial discipline.
- Information systems: sales promotion, advertising. Buyers and sellers must find each others
- Financing and bank services: access to finance (availability of loans or equity capital. There must be a reliable and fast payment transfer system.
- Insurance: the parties of a deal must be able to get insured against credit and payment risks. The property insurance must be available.

In a well-developed private the agents have incentives to obey rules, because it minimises public sector interventions, often replaced by a trustful dialogue between the government officials and representatives of the corporate sector.

The applicability of de Soto's ideas is its in other cultural contexts deserves a note of caution. In many of the SSA countries people are deeply rooted in their families, their tribes and their ancestors. Individuals consider themselves as a part of a collective. They don not consider themselves to be personally responsible, or to be relied or follow any other disciplines than those determined by their religion or their group. The concept of private property may be vague for them. Freedom, including the economic freedom, is determined and perceived through the collective (family, clan, tribe, ancestry, religious group). Positive economic incentives (Easterly) do no necessarily energise them, because they may be completely subservant and satisfied with the amenities they obtain as a members of their collective. Collective ownership discouraging competition is still deeply rooted in the FSU and SSA regions including also part of the Islamic world. While waiting the economic freedoms, private property rights and the rule of law, adequate to support the western type markets, to get rooted in these regions, it is sobering to remember that many of the basic disciplines and market supporting institutional capacities took centuries to be developed, although they had their own unique cultural roots in common history of Europe (Samuelson 2001).

4. State capacity's significance to major development issues

4.1 The FSUCEE and SSA introduced

In the sub-Saharan Africa more than 300 million people live on less than 1 USD/day or 48% of population live in extreme poverty – relatively more than in any other region of the world. The corresponding percentage for the FSU is less than 10% of the total population, indicating that less than 30 million people live there in extreme poverty. The region's share of the world trade has dwindled, FDI is at a very low level and the income gap in relation to more advanced countries has further widened. Africa has missed out the benefits of globalisation.

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In contrast, the FSUCEE region has advanced well - perhaps over expectations - towards market economy. Now, after ten years, the most advance countries of the region, the CEE and Baltic countries, are assessed to be matured enough to join the European Union. Also the Russia has made substantial progress having had strong economic growth with surplus of foreign trade, consolidated state budget and strengthened its foreign exchange reserves. Impressive amount of reform oriented legislation has been delivered. The weak capacity of its state institutions to enforce laws and function properly is seriously hampering the growth of free markets. This is accompanied by deterioration of the social conditions and health situation.

The number of people living in the sub-Saharan Africa increased from 508 million in 1990 to 643 million in 1999 the average annual growth rate being 2.6 % (world's 1.4% during the same period). The share of people living on less than as dollar a day, that is, in absolute poverty, was 48% of total sub-Saharan population in 1990, and 46% in 1999.[10] The average growth of the poor population during the following ten years ranges from 1.3 to 3.3% a year. The life expectancy decreased in the SSA while in developing countries it increased. About 79% of adults and 80% of children with HIV in the world live in the SSA (Wolfenson 2001).

Table 5 SSA and FSU in light of selected indictors

Selected statistics	SSA	FSU	SSA/FSU
Population, total (mill), 2000	659	290	2,3
- average annual growth 1990-2000	2,6	0,0	
Land area (sq km)(mill)	24	22	1,1
GDP (current US$)(bln), 2000	322,2	392,2	0,8
GDP/capita, (current US$), 2000	489	1352	0,4
- GDP/capita (constant 1995 prices), 1992-1999	0,0	-1,5	
Exports of goods and services (current US$)(bln), 1999	87,1	249,5	0,3
Exports of goods and services, % of GDP, 1999	26,9	46,3	
Foreign debt, total (DOD, current US$)(bln), 1999	216,4	217,8	1,0
Foreign debt, % of GDP	66,8	40,4	

Sources: **The World Bank** (World Bank 2002), "Building Institutions for Markets", *World Development Report 2002*, World Bank & Oxford University Press, Washington D.C. 2002 Statistical Tables, and World Bank (World Bank CD-ROM 2001), and the Win*STARSv4.2:2001 World Development Indicators CD-ROM, author's calculations. The annual growth rates are computed using compound interest formula and using the values of the first and last year of the period instead of selecting these points from the least-squares regression trends (as done by the World Bank to eliminate the undue influence of exceptional values).

Table 5 and appendix table 3 provide a broad view about the areas to be compared in terms of the magnitudes and developments of some economic key factors. The sub-Saharan Africa (SSA) and the former Soviet Union (FSU) cover roughly equally large areas, but the SSA accommodates more than twice the population of the FSU region. While the population growth of the FSU has nearly stagnated in 1990-2000, and increased from 289 million in 1990 to 290 million in 1999. In contrast, the population in the SSA grew rapidly at a rate of 2,6 per cent during the same period. The zero growth was caused by the negative growth rate of the age group less than 15 years, whereas the old age group has increased slightly. The population of the SSA grows annually in average more than 2 per cent in all age groups.

Out of the total of 42 heavily indebted poor countries (HIPC) as of March 2002, 34 were amongst the 47 sub-Saharan African countries (http://www.worldbank.org/hipc/country-cases/country-cases.html). For-

[10] The World Bank estimates, that 1.2 billion people or 20% of world's population live on less than 1 dollar a day.

eign debt forgiveness is about to be considered also to a number of FSU countries. The heavily indebted poor countries of HIPCs consist of 41 poorest and bankrupt countries. The about 600 million citizens earning les than 1 dollar a day in these countries owe about 170 billion dollars to foreign creditors. Almost all HIPC countries have very low GDPs and do earn enough from exports to be able to service their foreign debts. The HIPC governs would loose their ability to fight against poverty if foreign debt servicing would eat up major part of the budget revenues (Thomas 2001).

4.2 Economic growth

The economic growth, foreign trade, distribution of income and reduction are interrelated issues and subject to discussions on the ways and means of reduction of poverty and solutions for alleged problems caused by globalisation. The comparison of growth, trade and income distribution between the three major categories - industrial countries, FSUCEE or the countries in transition, and the sub-Saharan countries, and also between the countries within these groups, reveal major differences in the institutional development, which justify the conclusion, that the level of the institutional development plays a major role. The liberal governments may not immediately generate economic growth by increasing foreign trade, but instead influence by creating new or converting the existing state machinery gradually more conducive to development of market economy, creation of good business climate, and accumulation of social capital adequately to make these developments sustainable.

Institutions are necessary to support markets. Markets are based on institutions, which reduce transaction costs caused by inadequate information, define and enforce property rights and minimise barriers to entry of new participants. Institutions assist to manage risks from market exchange, increase efficiency and raise returns. Formal institutions include rules written into the law, codified and adopted by governments and public and private institutions and organisation, informal institutions refer to unwritten rules of game based on cultural tradition, religious or ethnic ties and trust. Governments play an important role in providing public goods such as defining property right and judicial services to enforce these rights and establish the rule of law. Competition between firms catalyses the development of corporate law (World Bank WDR 2002, pp. 20-21)

High quality institutions are considered to promote economic freedoms, and well-established economic freedoms go hand in hand with rapid economic growth (O'Driscoll et alia 2002, Scott 2001). The FSU countries lag behind the industrial developed countries both with respect of economic freedoms and economic growth. Obstacles, like adverse administrative traditions of state machinery, undefined property rights or excessive corrupted bureaucracy discussed in the preceding sections, may hinder the developments of good institutions. There are other obstacles adversely affecting economic growth and foreign trade. Unfavourable economic developments may discourage the development of institutions as much as undeveloped institutions may hinder the economic growth. Therefore, discussion on obstacles of economic growth and trade is in place here.

Drastic differences in the growth developments can be observed between Africa and Europe or Africa and Eastern Europe in the long run (tables 1 and 6). The sub-Saharan Africa has failed to launch economic growth. It has virtually disappeared from the economic, particularly from financial statistics. They have been moving very slowly towards market economy, with a far slower pace than Russia or the CEE countries.

Table 6 GDP and population of the SSA and Russia 1960-1999

GDP per capita (constant 1995 US$)	1960	1970	1980	1990	1999
Russian Federation	1279	2050	3163	3668	2211
Sub-Saharan Africa	477	619	670	597	561
Coefficients of multiplication (RF/SSA)	2,7	3,3	4,7	6,1	3,9
Population, total (mill)					
Russian Federation	120	130	139	148	146
Sub-Saharan Africa	223	288	380	508	643
FSU	212	242	264	284	285
Coefficients of multiplication (RF/SSA)	1,1	1,2	1,4	1,8	2,3

The GDP per capita of Western Europe was less than three times the African GDP per capita in 1820, six times in 1900, and in 1992 almost fifteen times. As can be seen in table 1, Africa had not yet quite reached the GDP per capita, which Western Europe had more than 170 years ago. The hardly reflects differences in natural resources or climatic conditions alone. Maddison lists a number of other factors, like the growth of capital stock in the, improvement in human capital, interaction between economies, the structural change from agricultural to industrial and service sectors United States and Europe but not in Africa. La Porta, Lopez-de-Silanes, Shleifer and Vishny (1998) found a number of other factors, like ethno-linguistic heterogeneity, legal origin, religion and history matter in shaping the government, and establish - based on their own and other studies with similar results - that the importance of good government appears to be a well established proposition.

Often richly endowed countries have majority of their citizens poor, or even getting poorer (Russia, Romania, or Democratic Republic of Congo (Zaire). Most of the African countries suffer from failures in state and institutional capacity building. In some cases countries with market supporting state institutions may depend on the quality of the policy conducted by their governments. Also the government policies may explain differences. Lee Hoskins and Ana I. Eiras have compared Australia and Argentina with fairly similar in terms of natural resources but Australia having its GDP/capita 2.7 times the GDP per capita of Argentina, while this ratio was 1.6 in 1900. They concluded that the main difference between that the difference in the speed of growth arose from institutions, and particularly the more open liberal trade policy of Australia during the past 25 years (Hoskins & Eiras 2002).

When the transition started in the FSUCEE region, the GDP fell in all countries. In the 1990's, a U-shaped curve resulted if year 1990 is the base year. Some economies (Russia, Ukraine, Moldova, Kazakhstan, Tajikistan and Turkmenistan) were slower in their recovery forming a L-shaped curve (p.120). The Central European and Baltic economies were fastest in their recoveries and almost reached the 1990-level. The official statistics may give a misleading picture about the actual developments. In fact, in many of the countries there might have been instant growth instead of contraction (Åslund 2002, p.121, Easterly 2001). The actual production and growth of the GDP of the Soviet-Russia may not have fallen to the extent, depicted by the flawed, politically pragmatic or straightforward dishonest statistics shows.[11]

[11] Åslund concludes, that the SU was much worse shape than the official statistics indicates and, on the other had, some remarkable growth, not reflected in the statistics, may have taken place in the 1990. In the Soviet economy there were strong incentives to cheat, that is, to give higher production figures exceeding the actual ones, whereas in transitional economies the statistical book keepers were not prepared to record new enterprises, majority of which opted for not giving any information to evade taxes and high costs of registration. After the dissolution of Soviet Union there might have been some disarray having negative impact on production. Part of this disarray might have been caused also by the old inertia of the conservatives disapproving trying to resist or boycott the new system. There was also some actual decrease of defence production and consumption. The Soviet defence expenditure was estimated to be more than 22% of GDP, but fell down to 2-3% GDP for Russia in the beginning of the 1990s. (Åslund 2002, p. 131). According to other estimates of Hildebrandt (1982), the historical long-term growth trend of defence expenditures by 4-5% a year reduced the annual growth rate of the Soviet economy by 1/10-1/5 percentage point and consumption by more than 0.5 percentage point in the 1990s.

In Botswana, Mauritius and Uganda, any downward bend or contractions are not visible transition stated more than 10 years, followed by Benin, Burkina Faso, Mozambique, Senegal and Tanzania. No clear U-shape pattern is visible in the GDP statistics of the SSA countries. The GDP (per capita at constant 1995 prices) has in some cases first decreased during the first part of the 1990's (bottoming 1992-1994) and then started to grow (Côte d'Ivoire, Gabon, Cameroon, Togo, Angola, Niger Mali, Swaziland). Even in these cases the U shape (for good performers, like the CEEs of Baltics, having reached or about to reach the 1990 –level) or L –shape (for poorer performers) is not clear, but either very mild and, in some cases, with downward bending again in 1998-2000 (Gabon, Niger, Swaziland, Lesotho). In other cases, the growth of the GDP has been monotonous (Benin, Ghana, Guinea, Lesotho, Uganda) or decreased (Sierra Leone, Zambia, Madagascar, Mozambique, Nigeria) or close to zero with minor irregularities (Chad, Guinea-Bissau, Nigeria, Republic of Congo, Zimbabwe) (Calamitsis 2001, World Bank Development Statistics)

The countries of the SSA region bear evidence that the economies do not need to grow (Olcott 2001). They may deteriorate as well. Development is a time consuming and lengthy process. The average annual growth per capita of SSA countries was 0.9 per cent during 1820-1992 (table 1), -0.1 per cent 1973-1992 and –0.9 per cent 1980-1990, lagging behind corresponding for world totals of 1.2, 1.2 and 0.4 respectively. Chart 1 in the Appendix illustrates the more recent development of the sub-Saharan countries. Almost all of them have lagged behind their maximum growth figures in the past.

A large number of different reasons have been proposed for the slow growth of Africa. David Bloom and Jeffrey Sachs Africa is geographically disadvantaged (Bloom & Sachs 1998). Easterly and Levine argue that Africa's problem is its high ethnic diversity by complicating co-operation (Easterly & Levine 1997). High rate of population growth is costly in per capita terms, but on the other hand the bad economy maybe the reason of the baby boom. Having prospect for rise of standard of living, families start to prefer less children to provide them with higher educational standards (Collier 1998, p. 275, Collier & Gunning 1999). Collier argues, that a low level of political rights is the reason. The predominant causes for civil wars are poverty and lack of political rights (voting rights).

In the SSA the GDP growth per capita remained zero due to the strong population increase. In the FSU again, despite the stagnated population growth the GDP per capita decreased in the 1990s. The GDP of the SSA in 2000 accounted 60 per cent of the GDP of the FSU. Although the exports from the SSA countries increased rapidly during the second half of the 1990s and, at any rate, faster than the export of goods and services from the FSU, they still remained at a low level and constituted over one third of the exports from the FSU in 1999.

The 1980s was a decade of crises; it was "a lost decade" (Smirnov 1999, p. 166). The problem was the neglected agricultural sector. The lack of resources prohibited the increase of productivity in agriculture. Fluctuation of production and instability characterised the agricultural sector, and perpetuated deficits in the foodstuff supplies led to food imports. Recovery, however, started during the latter half of the 1980s. Improvement of the industrial production took place in 1986-1995. It was based on growth of processing industries in the SSA countries. In 1986-1990 the average annual growth of the GDP coincided with the annual growth of population (Smirnov 1999).

During the 1980s the SSA countries started also to listen more carefully the advise by the IMF and WB and social-economic reforms were launched such as privatisation, liberalisation, property rights enforcement and reduced interventions of state in the private business. Social safety nets were established, structural distortions corrected, macro-economic reforms were implemented to pave the road for market economy. Financial sector was strengthened and markets were opened for the FDI (Smirnov 1999, pp. 168-169).

The Soviet economy had grown since the 1920's by virtue of the strong capital accumulation in industries, which absorbed the inefficiently employed people from agriculture and created rapid growth of consumption and investment. The decline of the economy since the 1970s was due to inability of the planned system to adapt its direction in the new situation(Allen 2001, Cohn 2001). There were a number of associated factors like decline in both labour and total factor productivity. Productivity decline was caused partially of exogenous problems like bad weather conditions hitting the agricultural and agro-industrial production, recession of the western economies during the second half of the 1970's reducing their Soviet imports and reduced Soviet hard currency earnings, and finally slow down in population movement from low productivity agriculture to higher productivity industrial sectors. In addition the raw material base west from Urals was becoming depleted and the capital stock particularly in transport and energy production and distribution.

The Soviet economy was not able to take advantage of the technology transfers from the West. The heavy planning bureaucracy contributed decisively to the downturn of productivity, through co-ordination problems, and deterioration of discipline in labour and plan enforcement. This was reflected, amongst other things, in the excessive growth of unfinished construction. Soft budget constraints turned of a socialist firm insatiable as to the demand for material, labour, and capital inputs and created the "economy of shortage". The economic failures together with observed growth of the underground capitalism, corruption and perceived double standards eroded the Soviet citizens confidence in their political and economic system (Allen 2001, Levine 1983).

The most recent developments in Russia call for focussing on reform for the heavy public administration and restructuring the heavy energy and transport sectors. The Russian government has reformed important part of legislation including tax laws, the labour and land codes, laws on deregulation and pension system reform, customs code, bankruptcy legislation, electricity sector reforms. Still the harder part, the administrative reforms remain, trade liberalisation and reform of natural monopolies and banking sector. The personal rent seeking and corrupted practices as well as further increased administration hinder these reforms. The public administration has grown heavier. The number of administrators was 0.8 million in 1980, about 1.5 million consisting 2.1% of all employees in the Soviet Union in 1991, and 2.9 million or 4.5% of all employees in 2000 (Goskomstat 2001, p. 141)[12].

African countries have not been able to take advantage of the capital flows in the form of job creation, transfer of technology, managerial and organisational skills. Africa is a continent with weak economic and political management, poor infrastructure and inadequate legal framework (Ajayi 2001). Political and economic instability, cumbersome tax regulations, inadequate infrastructure and corruption The situation is more or less similar in the FSU due to the bad quality governance of the state structures, particularly in the local and regional levels, due to treatment of minority owners in Russian companies and due to protective attitudes of Russian governments in their production sharing agreements policies.

4.3 Trade and trade policy

International trade and the economic growth go hand in hand in the long-term developments. According to Dollar and Kraay found out that a 20 percentage points increase in the trade share of the GDP increases growth by between 0.5 and 1 percentage points a year. This effect is both statistically significant and economically meaningful. No reverse causation from growth to trade could not be observed.

From 1820 to 1914 international trade grew faster than the global economy (trade from 2% of world income in 1820 to 18% in 1914. Since then up to 1950 the trade grew slower than income (World Wars, Great Depression) but started again to expand faster between industrialised countries due to trade liberalisation (GATT). International capital flows returned to 1914 level in 1980. Since then the international

[12] The reason for the large increase is not clear. Allegedly it relates to President Vladimir Putins efforts to stabilise by expanding the bureaucracy (Berezovsky 2002). The figures represent administrators and bureaucrats only, because they exclude the civil servants employed in the social sector, health services, education, science, culture etc. To get enlisted to the government is difficult for young well-educated applicants, because the loyalty still takes the precedence over the competence in the Russian administration (Wehner 2002).

capital flows have chanced their nature from infrastructure financing into FDIs to manufacturing and services (Dollar & Kraay 2002, p.122). This change has been supported by cheaper and faster transports and developments in telecommunications.

The world trade grew at an annual average rate of 6.2 per cent and outpaced the growth of world output of 3.8 per cent a year between 1948 and 2000. During the same period the share of Africa of World merchandise exports declined from 7.4 to 2.4 per cent and the transition economies from 6.0 to 4.4 per cent The major winners were the Asian countries, that is, China, Japan and the Far East economies increasing their shares from 14 to 27 per cent (UN 2001, pp. 154-156).

The growth of trade has been supported by development of international money and capital markets since the 1970's. Advances in information and computer technologies, globalisation of national economies jad competition among the providers of intermediary services have led to financial globalisation. Both global gross capital flows and cross border flows have experienced fourfold increase in the 1990d, being 7.5 and 1.2 trillion dollars respectively in 2000 (Häusler 2002). However, these flows have taken place mainly between Far East, Western Europe and the United States, whereas they have circumvented the FSUCEE and the SSA countries (Laulajainen 1999)

Table 7 shows the trade marginalisation of SSA and the transition countries. The shares of the SSA and FSUCEE countries of the world trade remain modest in comparison to the shares of the developed countries and 'rest of the world', that is other developing countries. Although the developing countries have been described to be subject of "exploitation" primary products (food, agricultural raw materials and fuels, raw materials), the shares remain modest. The exports of the SSA countries have collapsed from 142 billion to 35 billion dollars between 1985 and 1999, which represents average annual growth of -10%.In fact many of the SSA countries have been forced to import food due to low productivity of their own agriculture and exceptional weather conditions.

Table 7 Composition of Merchandise Trade in 1999, shares in % and growth 1985-1999.

1999					1985-1999	
	Imports		Exports		Annual average growt	
	Primary	Manuf.	Primary	Manuf.	Imports	Exports
FSUCEE	4,3	3,6	6,5	3,4	5,7	6,4
SSA	0,8	0,6	2,6	0,2	3,8	-9,9
Developed	68,6	69,5	49,1	69,1	9,0	9,1
Rest of the	26,3	26,3	41,8	27,3	9,2	9,3
World, %	100	100	100	100		
World, Bn	1022,1	4407,2	1023,3	4406,3	8,8	8,8

Remark: the growth figures are inflated due to the inclusion of trade flows between the states of the FSU, which were considered internal until 1992.
Source: UN 2001, tables A15 and A16, pp. 260-263.

TradeUN02stat.xls, taulu2

As shown in table 8, the EU and other developed countries are the most important trade regions to both the FSUCEE and SSA countries. About 60 per cent of trade of both the SSA and FSUCEE took place with the European Union and other developed countries. The EU is a more important trading partner to the FSUCEE than to the SSA countries. The share of trade *between* the FSUCEE countries was relatively

high, 28 per cent of their total trade, for obvious historical reasons, but the growth of that trade has been modest. The share of trade between the SSA countries was 10 per cent in 2000 and is growing relatively fast. Interestingly, the trade between the SSA and FSU countries has grown rapidly between 1995 and

2000, although their shares of respective regions' total trade have been very modest (only 2.8 per cent of the SSA's exports and only 0.4% of the FSUCEE countries' exports).

Table 8 Direction of Trade: Exports (F.O.B.), year 2000

	Share, %			Average annual growth 1995-200		
Destination (below)	SSA	FSUCEE	World	SSA	FSUCEE	World
EU	39	48	35	4,1	8,5	2,8
Other developed c.	21	11	32	6,0	9,8	7,9
FSUCEE	3	28	4	17,8	0,8	4,5
SSA	10	0	1	7,8	19,7	4,5
Other developing c.	13	13	27	2,5	5,8	3,7
Unkown	14	0	1			
Total, %	100	100	100			
Total, Bn dollars	44	275	6341	7,8	5,8	4,5

Source: UN 2000, table A.14, pp. 258-259.

According to Ajayi (2001), Africa's relatively isolationist policies and closed economies have led to sluggish economic growth and marginalisation (p. 7). During 1960-1969 the Africa's average share of total world imports was 5.0% and exports 5.3. In 1990-98 these figures dropped to 2.2 and 2.3 %, respectively. Restrictive trade regimes of African countries and high transport costs to and from markets are obvious reasons for the low rate of participation in the world trade. Still in the 1990's, in spite of the liberalisation of the trade regimes, they still remained more restrictive than those ones of their trading partners or competitors (Ajayi 2001, p. 7).

Also the foreign direct investments seem to avoid the FSU and SSA regions. As can be seen in Appendix table 1 the restricted access to finance, uncertain property rights, heavy regulation and black markets, and treatment of the FDI (excessive restriction, minority rights) constitute major obstacles for the FDI. The economic freedoms are better but the political risk bigger than in the FSUCEE. In sum, as shown by table 9, these regions do not attract the FDI, main flows of which are concentrated to high income industrial countries.

Table 9 Foreign direct investment, net inflows, BoP based, current USD in 1999

	Net inflows BoP, bln dollars	Share, %	% GDP	Per capita dollars	Av.annual growth 1989-1999
Sub-Saharan Africa	7,9	0,9	2,5	12	11,6
Russian Federation	3,3	0,4	0,8	23	na
NIS	2,8	0,3	2,4	23	na
FSU	6,1	0,7	1,2	23	na
HIPC	8,1	0,9	4,0	13	27,7
High income countries, >= $9,26	699,0	79,0	2,9	780	14,1
World	884,5	100,0	2,9	148	15,2

Source: World Bank CD-ROM 2001 and author's calculations
FDISTAT.xls

The commodity structure of the trade between the East (Russia) and the West (the EU or Western Europe) follows an inter-industry pattern. Russia provides Western Europe with traditional Soviet-era exports of oil, gas and raw materials and receives in exchange manufactured goods and food to be consumed by the most well to do part of Russian consumers. About 50% of exports from Russia consist of fuels (oil and gas), and together with ores, metals and precious stones, these items account for about 80% of Russian exports. Russia is relatively vulnerable for oil price changes: 10% change in oil price would create more than 2 % change in the Russian GDP with two years' time lag (Rautava 2002). Nearly 90% of imports to

Russia consist of fabricated or half-fabricated consumer or investment goods (Goskomstat 2001). About 30-40% he Russian foreign trade is inter-industry trade.

Russia is one-sidedly dependent on its foreign trade, of which about 70% takes place with European and about 35% with the EU member countries. These trade dependencies are asymmetric if looked at from the side of the EU countries: trade with Russia is not very important for them. The share of each EU member country's trade with Russia in terms of its total foreign trade remained at about 1 %, with the exceptions (IMF 2000). Moreover, the role of Russia as Europe's energy supplier has been cemented through the "partnership in energy" between EU-Europe and Russia. It was concluded in the European Union and Russian summit on 15 October 2000 in Paris, proposed "positive interdependence" by way of Russia increasing energy deliveries to Europe in exchange for investment and new technologies form the EU countries. Although this dependence has also been a matter of concern among Russian economists and politicians, one can safely assume that the structure of production is not going to change drastically in the foreseeable future. The structure of foreign trade change slowly.

Similar features can be observed about the trade of the SSA countries with their more developed trade partners. The SSA countries depend often on few export commodities are far more sensitive in the negative change of terms of trade. Virtually all raw material prices are currently in their lowest ebb since 10-15 years. Coffee and copper cost presently about one half and cotton one third of the end-1999 prices. Also the FDI draws back. In Zambia the Anglo-America PLC announced that it will withdraw having sunk €120 million during the last two years. Zambia suffers of drought implying that is bound to import food. The increasing foreign trade deficit implies Zambia, as most of the already highly indebted countries in the sub-Saharan countries, gets even deeper in the external debt problems.

Table 10. Trade dependency of selected African countries

Country	Raw material	Share, % of exports	Change in total exports 1998	1999	2000
Uganda	coffee	56	-11	-23	-28
Zambia	copper	56	-20	-26	-25
Mali	cotton	46	-11	-23	-28
Rwanda	coffee	45	6	-11	-25
Chad	cotton	42	-6	-15	-20
Burkina Faso	cotton	39	-4	-16	-25
Benin	cotton	38	-7	-14	-16
Tanzania	coffee	11	1	-7	-13

Karismo 2002

These features repeat themselves in the trade between SSA and industrial countries. The asymmetric trade dependency implies, that the trade with industrial countries is potentially important for the SSA countries, but - looked from the economic point of view - the industrial countries can do without trade with SSA countries. As a rule, the exports of the SSA countries depend on one or few products, usually from the primary sector with fairly low degree of value added. Trade between SSA and industrial countries is typically inter-industry trade.

Exports of fuels, minerals, diamonds, foodstuffs from African and FSU countries benefit the industrial countries and the export earnings tend accumulate to end up to the hands of the commercial and political elite of the exporting FSU or SSA country. In the worst case the export earnings, which optimally should be invested in the development of domestic industries, are spent to luxury consumption. The agricultural failures in the SSA quite often force the government to use a large part of the export earnings to import foodstuffs. The extent the export earnings of returns from direct investments will benefit the poor people, depends on the preferences of the preferences of exporting country's government (Sharer 2001, Smirnov).

On average, the trade regimes of African countries are more protectionist than those of other countries, including Africa's major trading partners. Still the African countries made a substantial progress in their foreign trade liberalisation particularly in 1990s. According to the IMF (IMF, "Trade Liberalisation in IMF-supported Programs) 75% of the countries of the region had trade regimes classified as "restrictive, but presently this percentage is only 14. At the other end of the scale, presently 43% are classified as open whereas ten years earlier there were no open countries for foreign trade in Africa:

Table 11. Trade regimes (number of countries)

	Africa 1990	Africa 2000	Rest of the world 2000
Open	0	43	61
Moderate	23	43	24
Restrictive	77	14	15

Source: Sharer 2001, p. 15

Open trade is expected regimes promote international trade provided that other preconditions exist. Although the sub-Saharan Africa has made impressive progress in trade liberalisation during the past ten years and in structural reforms, it is still more protected than its main trading partners (Europe and North America) and other regions. According to Sharer, Africa's current average tariff of about 19% is still higher than the average of 12% of the rest of the world. In the beginning of the 1990s the un-weighted tariff rates accounted for 25% and non-tariff restriction 47% of trade, which compare to 22% and 24% of al countries (UNCTAD 1999, Cotton & Ramachandran 2001).

The trade restrictions may be one of the impediments for development of *regional integration* of the SSA countries. Sharer points out the benefit of regionalism in stimulating efficiency and reforms should not be underestimated, it is not substitute for broad based liberalisation of trade with Africa's major trade partners (Europe, North America). The intra-regional trade of the SSA countries consists currently 10% of total trade but has been increasing rapidly at an annual average rate of almost 8% in 1995-2000 (table 6). The sceptics state that regional organisation do not necessarily help to solve common problems. Weak states make weak partners. Competition between leaders prevent a co-operative atmosphere to be created and lead to emergence of a regional market is a number of overlapping and internally inconsistent initiatives. The overlapping reduces the gains from regionalism, worsens the investment climate, transparency and leads to costly duplication of administration (Sharer 2001, Olcott 2001). Similar problems, added by the different size of partners, have disturbed also the efforts to harmonise the co-operation between the CIS countries.

Rodriguez & Rodrik (1999) point out that both academic and policy discussions overstate the systematic evidence about positive correlation between trade openness in favour of trade openness as catalyst of economic growth. The openness and growth are related matters, however, not justifying the conclusion, that once the governments only dismantle their barriers of trade, the growth will automatically follow. The trade policy, the actual trade - or export - volumes and the economic growth are related issues but do not have any unambiguous causal links. The ambiguity of the causalities calls for more sophisticated analysis of the issue (Rodriguez & Rodrik 1999, p. 39). Obviously, there are intervening variables between the trade policy and trade, like the geographic and cultural distance, or political and legal environment.

Trade policies and the absence of trade barriers matter between neighbouring countries or trade partners having close trade relations. Geographic and cultural distances matter. CEE is closest to Western Europe, followed by Russia, Belarus and Ukraine, while Caucasus and Central Asia remain last ones. Tastes and traditions matter in generation of trade in consumption goods, training, R&D, industrial standards and traditions in manufacturing. While there is an obvious links between actual development of trade and the economic growth, there are several factors, which may interfere the openness or trade policy of trade and actual trade development, or trade policies and economic growth.

On the other extreme, taking any Central-Asian or sub-Saharan land-locked country, geographically and culturally distant from markets, it hardly makes much relevance to such a country's growth, whether it maintains trade barriers or dismantles them. The Kyrgyz Republic, for instance, having joined to the WTO and most of the international organisations 1993, is victim of it geopolitical location. No matter, how liberal trade policy its government decides to conduct, it has not assisted to Kyrgyz Republic essentially to increase its foreign trade or its economic growth. The same holds for a number of SSA land locked countries like the Central African Republic, Chad, Niger, and Mali (Dollar & Kraay 2002a, p. 132). Contacts of Northern African countries with relatively wealthy Mediterranean countries along with the historical trade routes (North African countries or South Africa) have obviously contributed their higher rate of participation in the word trade and economic growth. For instance, the Arabic North-African countries have 1.2-2 times higher per capita growth of the GDP than the SSA countries (Smirnov 1999, pp. 143-144).

4.4 Population and income distribution

Population: growth and qualities

Each year 83 million people is added to world population; 82 million of them in developing countries. Pressures for migration nationally and globally are increasing. The world’s population growth seems to have passed its peak and the worldwide famines have taken place. Instead, the production of food has tripled in about thirty years. There is no observed correlation between the growth of population and the growth of economy. Easterly makes an interesting point that in the long-run populations growth increases the economic growth potentials, because larger populations carry more innovativeness, human geniality, larger scale markets and improved technology, which in turn enables to feed a larger population (Easterly 2001, pp. 96-97).

The fast population growth has been seen as a burden, because the national income has to be shared by too many and is not enough to anyone if divided evenly (Smirnov). On the other hand, in Russia, the population has declined during the nineties and the income distribution has became more uneven. While in SSA the low rate of economic growth h seen as a reason for low economic growth and skewed income distribution, in Russia the decline of population is regarded as a consequence o the deterioration of social condition after the dissolution of the Soviet Union. The relations between population growth and associated change in the age structure on the one hand, and the economic growth and income distribution in the other remain ambiguous, which leads to conclude that negative economic consequences depend the corroded state structures expected to support the safety nets in Russia, and total absence of these structures in a large part of the SSA.

In contrast to Russia, in Africa the population is growing to fast to be able to take care of welfare and social safety of the rapidly increasing population. Many of the African societies are not organised enough to take any collective measures or social reforms to take care of those in need. Moreover, in countries are hit repeatedly by natural catastrophes or wars, people are forced to think short-term just to survive themselves over the next days or weeks. The short-life expectancies support this short-term thinking. The lives are simply too short to collect experiences and to pass that experience to descendants.

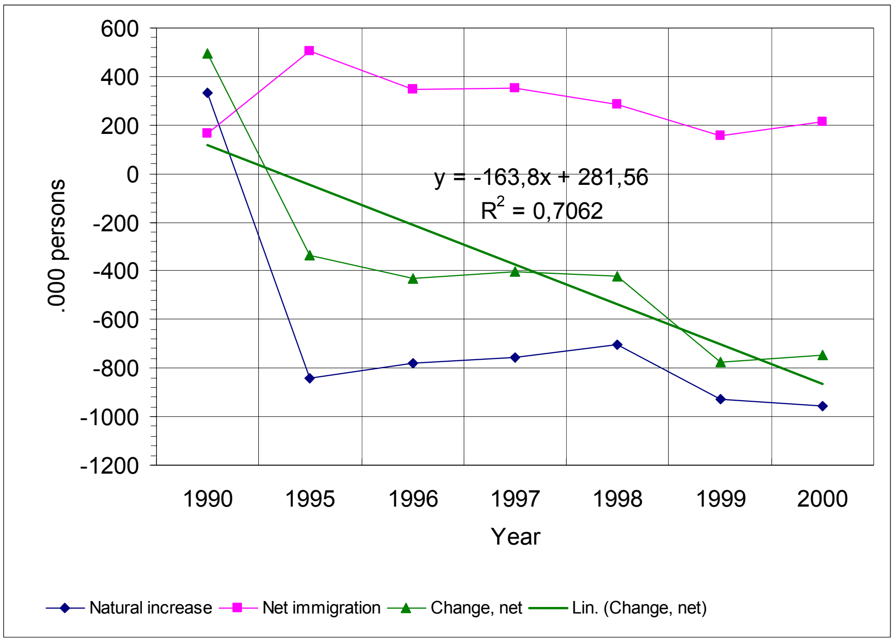
Table 12: Changes in age structure in the SSA, Russia and high-income countries, %.

	SSA		Russia		High Income Countries	
	share of tot.pop.	growth 1992-99	share	growth 1992-99	share	growth 1992-99
Population, age <15	44	2,3	22	-2,9	18	0,3
Population, age >64	3	1,7	11	1,7	14	1,7

Source: World Bank CD-ROM 2001 and author's calculations
FSUsSAcomparisons.xls taulu 3.

According to the World Bank statistics the annual average growth rate of the sub-Saharan Africa's population has been around 2.7 %, whereas the corresponding figure for Europe and Central Asia has been about 1 %. The total population of the sub-Saharan Africa has grown close to 660 million by the year 2000, while the whole world's population hit the 6 billion in that year (Excel file made from WB CD-ROM). The population density of the sub-Saharan Africa remains, despite the strong population growth, fairly low, between 20-30 people per square kilometre. In Euro-Asian region the corresponding figure is about 120 people per square kilometres.

Chart 1. Net changes in Russian population development in the 1990s



Source: Goskomstat
"Russia/tilastokeskus.xls" table 1.

The decrease of the Russian population as a result of natural increase (subject to nativity and mortality developments) and immigration is seen in table above, and shows a downward trend. The population of Russian federation was 139 millions in 1980, 148.5 millions in 1990 and 146.5 millions in 2000. There are two obvious reasons for the decline: in the age-structure of the Russian population it represents the second cycle (1941-1948, 1966-1973, and 1991-1998) of the loss of people at age of 20-30 years in the Second World War.

Another reason for the decrease of the Russian population is the grave socio-economic situation resulting from the developments of dissolution of the FSU. In case of Russia, a diminishing part of population has to support a growing elderly population with fairly weak safety nets. On the other hand, in comparison with the African countries, Russia is better organised to feel responsibilities about the elderly population. In the country side people are living outside the monetised exchange economy, based on self-sufficiency by growing their own food and depending on the safety net provided by the family members and relatives and neighbours in the same village.

However, the level of education and openness and receptivity of the society for new information may matter more than the age structure. At least, this 'perverted' age structure seem to prevail in the most developed industrial countries as a result of slow down of the drop in the fertility rates produced by higher standards of living. The postponement of getting the first child and limiting their number relates to the younger generations' ambitions to gain higher level of education, have a good start in the competitive careers and, finally, to give better possibilities to their children. This seems to have slowed down the population growth in most developed countries (Easterly 2001). Due to the increased productivity based on elevated levels of education and professional skills, the productivity of labour could be expected to increase to a degree, that the economic growth hardly will be hampered due to the added burden of taking care of the expanded older age groups. Also, in the FSU economies the younger generations and part of the older ones seem to be amazingly fast assuming the new ideas.

Easterly (2001) proposes that in countries with ageing population FSU, the older generations try to protect their own positions and vested interests and may, if not suffocate, at least slow down the younger generations' efforts to introduce new ideas and technologies to promote the economic growth (Easterly 2001, pp. 179-185). Easterly makes the point the in Africa the younger generation might make a 'big leap' to starting to take advantage of the internet and reap the benefits of newest technologies in the it-business (for instance, India already has its own 'silicon valley).

On the other hand in the poor African countries having low life expectancies of about 40-50 years, the life may not be long enough to get enough education and to transfer it to the next generation. There again the physical age or the age structure may not be so important than the access to education and professions where the knowledge and skills can be applied, accumulated and be converted into experience. This, in turn, requires that there exists an organised society and state powers to support education and labour market.

In Russia, a diminishing part of population has to support a growing elderly population with fairly weak safety nets. On the other hand, in comparison with the African countries, Russia may be better prepared and organised to assume responsibilities about the elderly population. On the other hand, both in the FSU and the SSA the informal safety nets consisting of family members and relatives and neighbours replace the absence of official arrangements.

The migration may cause high economic and social disadvantages for surrendering countries loosing their resources through emigration as well as for economic and social problems from immigration for receiving countries with large structural unemployment. However, total number of people not living in their country of citizenship is 2 % of world population (World Bank GGP 2001, p. 10). The economic consequences for the giving and receiving countries or regions would call for more economic research particularly, when the political debate and controversies are increasing.

More extensive has been the migration within countries from the rural and less developed regions to the urban and metropolitan areas. In Russia people are migrating from the fringe areas in the northern, eastern and southern regions to the growth centres, where the immigrants meet harsh conditions. The government does not have the resources to improve the deteriorating conditions of living for these immigrants. Both in the FSU and SSA the main problems have been the inability to develop industries to absorb the people moving from agriculture to urban areas, which has led to impoverishment of the migrants and creation of slums and squatter towns in the outskirts of urban areas Russia (Kontorovich 1997, Smirnov 1999).

Income distribution

Income and poverty move together. When the economies decline, also poverty increases. This has been case in Russia and Central Asia, but holds also for the sub-Saharan Africa. There is also causality between the economic growth and income redistribution, which, however, remains ambiguous (Easterly 2001, p. 14).

The UNDP report (1999) emphasises the strong growth of inequality and increased poverty in Russia are caused by the corrosion of the state machinery in charge of health care and social security. In the FSU on of the pillars of human security under the old Soviet system was an extensive network of social protection. The social protection system was corroborated duet to depressed developments of Soviet and post-soviet economies reducing tax revenues, abolition of universal coverage social security and privatisation. The UNDP report describes the dismantling of the former comprehensive system of social security as one of the great tragedies in the transition of the FSU and in much of the Eastern and South-eastern Europe. The WHO estimates, that to normalise the Russian health care, the allocations should account to 5-6% of GGP (UNDP 1999, pp. 52-55). The UNDP report also confirms the prevailing "rule by law" and the deficit of social capital: "People are objects instead of participants in shaping policies that affect their daily lives" (UNDP 1999, p. iii).

In 1989 about 14 million people in the FSUCEE lived on less than $4 a day. By the mid-1990 that number had risen to about 147 million." (UNDP 1999, pp. iii-iv). Table 9 below presents Tikhomirov's (2000) calculations according to which amore than half of the Russian population would have fallen to low-income bracket, while this share was slightly over one tenth in 1990. In the beginning of the decade more than one third qualified as a high-income earners, but eight years later only 4% could boast of being rich, or probably very rich.

Table 13. Percentage of Russian population belonging to low, middle or high income groups in 1990 and 1998

	1990	1998
Low-income-group (less than 0.5% of the average per capita income in 1990)	11	52
Mid-income group (0.5-1.0 of the average income per capita in 1990)	52	44
High-income-group (over 1.0 of the average income per capita in 1990)	37	4
	100	100

Source: Tikhomirov 2000, p. 192
Russia/Tilastokeskusvenäjä.xls, taulu 2

In relative terms, in the sub-Saharan Africa, about 300 million people live by less than 1 dollar a day, which is considered the line for extreme poverty. The SSA countries, being very poor, economic crises seem to increase poverty more than wealthier countries even in the FSUCEE, which are also institutionally better prepared to protect their population. For instance, in case of Ivory Coast, Mali and Zambia, poverty increased rapidly during severe recessions of the economies. As noted above, the relation between the change of GDP and poverty remains empirically ambiguous.

The average annual growth of the GDP/capita at constant 1995 prices has been slowest in the sub-Saharan Africa and slower than even in the low-income countries, which include also virtually all sub-Saharan countries. Given the per capita income growth rates at constant prices, it is not possible to conclude, that the income differences would have been reduced at least between the sub-Saharan Africa and rest of the world. It is obvious from table 5 that the gap in income and wealth between the major regions has widened in the long term and during the last decades.

Table 14. Level, growth, and comparison of the GDP by countries in different income groups, and the SSA

	GDP/capita, dollars at 1995 prices			Average annual growth, %		GDP/cap in comparison with the SSA GDP/cap		
	1960	1980	1999	1960-99	1980-99	1960	1980	1999
Low income, <=$755	248	340	461	1,6	1,6	1	1	1
Middle income $756-9,265	746	1507	2064	2,6	1,7	2	2	4
High income $9,266=>	10037	19748	28892	2,7	2,0	21	29	52
World	2587	4335	5439	1,9	1,2	5	6	10
Sub-Saharan Africa	477	670	561	0,4	-0,9	1	1	1

Source: World Bank CD-ROM 2001
"GDPgrowthtables.xls"

If the per capita income in the high-income-countries was 21 times higher than in the sub-Saharan Africa in 1960, and almost 30 times higher in 1980, and 52 times higher in 1999, it is difficult to conclude that the gab between sub-Saharan poor countries and the high-income-countries would not have been widening in 30 years. The same holds for the low-income-countries, including in addition to sub-Saharan Africa also India, Pakistan, Indonesia and a number of smaller countries. The high and middle-income countries experienced slightly slower rate of growth between 1980-1999, but it has not narrowed the per capita income gap; in contrast, the negative growth in sub-Saharan Africa has strongly widened it.

4.5 Foreign debt and poverty

Debt and debt forgiveness

Reason for the deterioration of the economic situation in the 1980s: in the SSA the production of goods and services decreased by 2.5% in 1981-1985 and their per capita production in 1985 was 15% below the level of the one in 1980. The failure to develop their own economies deepened on the inability to establish external foreign trade relations, which only served imports of food, raw materials and processed goods but not investment goods, modern production technologies and know – how. Subsequently, external debt started to grow from the 1975, although they had been received on concessionary conditions, because it was used to finance the consumption (Smirnov 1999).

Poverty and high foreign indebtedness go hand in hand. The about 600 million citizens earning less than 1 dollar a day in the HIPC countries that owe about 170 billion dollars to foreign creditors. Almost all HIPC countries have very low GDPs (325 dollars per capita in 1999) and do earn enough from exports (in net terms) to be able to service their foreign debts. The HIPC governments would loose their ability to fight against poverty if foreign debt servicing would eat up major part of the budget revenues (Thomas 2001).

Out of the total of 42 heavily indebted poor countries (HIPC) 34 were amongst the 47 sub-Saharan African countries (see summary table 3 in Appendix) in March 2002 [13]. Almost half or 39 of 79 countries eligible for of the international development aid financing is located in the sub-Saharan Africa. The operational cut-off for IDA eligibility for the fiscal year 2002 is 885 dollars expressed in gross national in come per capita in 2000). [14] The external debt of the SSA accounted 67% of GDP in 1999, while the corresponding figure for FSUCEE was 40% and the middle-income countries 36%. While the Russian Federation, the Baltic countries and the CEE's have been able to cope with their foreign trade problems (Cottrell & Ostrovsky 2002), the some FSU countries (Kyrgyz Republic with foreign debt of 200% of the GDP) will face problems in their foreign debt service.

[13] (http://www.worldbank.org/hipc/country-cases/country-cases.html)
[14] (http://www.worldbank.org/ida/eligible.htm)

The share of foreign aid has bee 4% of their GDP, but only 0,7% to the FSUCEE countries. According to critics, the assistance has indiscriminately been granted to SSA government without regard, how corrupted or efficient they are. The assistance has continued although the bad governments have not corrected their governance. Also the debt relief would similarly support the corruption and bad administrative practices, unless the international organisation agrees to enforce the conditionalitites. The problem is bad, because often the poorest countries tend to have most corrupted once.

Thomas makes a strong point that the debt relief will hardly reach the poor, but will benefit to corrupted leaders and government officials. Poverty reduction is the reason to forgive the HIPC debt. Assistance and debt relief should be used to reduce poverty, but many countries having received development assistance did not even have programmes or plan, how to use these funds. In the worst case the money saved through debt relief could be used to buy weapons, or illegally divert to government officials to protect their privileges.[15]

Speeding up the debt relief programmes may lead bad design of poverty reduction strategies. Tight timetables may draw all attention to the compliance with formal conditions. In the longer run higher accountability requirements have to be established to governments managing aid money (Thomas 2001, pp. 44-45). Governments should be given enough time make a credible spending plan and the creditors should then see that the poor people actually benefit from it (Thomas 2001, 45). Effective antipoverty actions are difficult to design, because the poverty problems are complex and location specific. Healey and Killick (2002) think that donors should not withdraw from the poverty reduction activities, although the modest successes may justify the conclusion, that the international donor organisations do not have any specific comparative advantage in that area.

Poverty includes low income and consumption levels, low food and nutritional status clothing and housing, sub-standard access to health care and schooling, inability to make provision against emergencies. Poverty may lead to social exclusion as inferior access to social services, labour market, collective social decision-making and social life. It often includes unequal relationships between landlord and tenant, debtor and creditor, worker and employer, man and woman. Therefore poverty problems should be approached in its societal context. State structures are necessary to finance and run the social safety nets. State is also expected to protect individuals from the major natural catastrophes and assure their safety. The fundamental problem here is how to create enough social capita to enable the state to bring together all different social groups and create incentives enough to trigger necessary actions. The democratic principles and good public governance are necessary to create necessary incentives and cooperation. The question of solving the poverty problem is therefore not only economic, but also political problem (Healey & Killick 2002),.

Globalisation, competition and redistribution of income

Although the discussion about pros and cons falls outside of the scope of this study, links to international trade, income distribution and poverty reduction and large bulk of research (Dollar & Kraay 2001 a-c and 2002 a-b, White Paper 2000, number of World Bank and IMF publications) necessitate some comments. Globalisation is characterised, in particular, by increases in flows of cross-border trade, capital and information, and increased mobility of individuals. It has been promoted by technological development, fol-

[15] A long list could be compiled about mismanagement budgetary resources in general and the development funds in particular. Most of the governments are impregnated by high-level corruption and the funds are used to purchase weaponry and maintain police force and army to support the luxurious life of the governing political elite. Thomas names as examples the state heads of Zaire (president Sese Seko Mobutu, about 5 billion dollars taken aside for personal use), Central Bank and Treasury of Kenya lost 1.1 billion dollars for government officials, and Côte d'Ivoire's president Félix Houphouet-Boigny used 0.3 billion his 'own money' to build a basilica. In Kenya the government officials siphoned 1.1 billion dollars form the national treasury and central bank (38). Lately, Nigerian leaders announced that they plan to use substantial amounts of the IMF financing to construct a football stadium to Lagos and finance the Nigerian space programme (Thomas 2001, pp. 38-45).

lowed by reduction of costs in transports and communications and computers (Douas 2001, p. 4). A global world economy could be also defined " - as one in which neither distance nor national borders impede economic transactions" (Wolf 2001, p. 78).

According to anti-globalisers, globalisation is bad. The antidote seems to be, that the international trade and increased freedoms in movement of all production factors, including information, increases the income gap and deepens the poverty between and with countries. The transitional corporations are singled out as carriers of the poverty and global misery, promoted by reducing the barriers for international trade (WTO) supported by international organisations.

The free movement of capital and other factors of production have also their downsides: substantial brain drain and outflow of funds from African and FSU countries to the United States and Europe. In FSU and SSA countries the low level of institutions and lack of opportunities the financial capital and the highly qualified labour tend to leave the countries. More than 30.000 Africans with doctoral decrees work outside the continent (Ajayi 2001). For the financial capital reliable banking services are not available in the FSU and SSA, higher quality banking services are sought in developed countries, where reliable banking services and attractive investment opportunities were available. This led to substantial capital flight to industrial countries. By 1990 about 40% of Africa's private wealth was held outside of the continent (World Bank GGP 2001, p. 10).Estimates about capital flight from African countries range from 24 to 143 % of their GDP (Collier 1998) and from Russia range from 100-200 billion dollars according to various sources 1993-2000 (IMF statistics, Fitch IBC, Duff & Phelps).[16]

For the market economy the poor people do no represent any kind of market, because they have no money, no purchasing power. the question is, however, how to attract foreign trade and FDI to cover the FSU and Africa rather than closing the gates by raising tariffs and quantitative barriers in the name of anti-globalisation and belief in autarkic isolation. The latter would deprive the opportunities from the FSU and African countries' economic and social development. Bhagwati (2002) admits that the multinational and international aid is there to mend these problems while waiting the recovery of the poor regions to solve the problems (p. 6).

A number of general counter remarks can be easily made. First, poverty and misery would exist anyhow, and particularly without economic growth and international trade. Second, closing the economy from the international trade is likely to only harm economy, whereas opening may support, although not warrant, the economic growth. Third, the anti-globalists may be barking at a wrong tree: it is hard to name any organisation, private or public, which would have done more than the United Nations in general, and the IMF and the World Bank in particular, to fight the poverty and assist the least developed countries to build the material and institutional infrastructures, and promote the health, education and social conditions in the SSA and other developing countries.

Wolf points out that the economic liberalisation combined with Internet trade and increased mobility of the production factors make the taxation more challenging for the local governments. He rightly points out that even heavy taxation does not expel the citizens preferring to enjoy the high quality education and public transport etc. The governments are not benevolent welfare maximisers, but instead the competition between governments in the integrated regions increases the incentives to serve best those who pay most taxes.

Globalisation makes national states even more important. As Wolf formulates it " -- the bedrock of international order is the territorial state with its monopoly on coercive power within its jurisdiction (Wolf 2001, 190). Good institutional base with high quality public goods and personal security for individuals

[16] Calculating capital flight as a percentage of private wealth (defined as private capital stock per private sector worker), Collier found that the wealth per worker in Africa, slightly over 1069 dollars, is lower than the private capital stock per worker in any other region in the world, but they have placed 39 % of their wealth outside of Africa. Only in the war-troubled Middle East has the same percentage, but still the wealth of worker is more than three times that one of African worker or 3678 dollars. In Russia the percentage is 2.9 of the 10463 dollars (Collier 1998 p. 93 and on Russia author's calculations based on Goskomstat statistics, pp. 140 and 305)..

offers the best starting point also for integration and globalisation. Subsequently, globalisation does not make the states unnecessary, but on the contrary, any kind of global governance will lay on the depend of the quality of governance of the national states.

Competition and rent seeking are driving forces of the market economy to create economic growth. According to western values and economic discipline the legitimisation of the ownership rights have to be legally earned by one's own work, skills and ingenuity. Altruistic handouts and subsidies to those, who do not work (sick, handicapped or unemployed) seem to be pervert because they violate culturally deeply seated legitimacy of work-related ownership rights. Subsequently, the free market system based on rent seeking, competition and property rights includes disincentives to voluntary distribution of profits to those not contributed in their accumulation. Thus not all institutional changes arising *from competition increase the well being of all members of the society* (Daouas, p. 133).

Thus, the redistribution of the results of the economic growth is a counter-stream operation, which is possible only to the extent it does not discourage incentives for economic competition. The quality of tax regime leads to the question of institutional capacities with a notion, that a well working tax regime calls for a well developed and healthy state capacities supported with adequate social capital to create adequate consensus about the tax rate and the use of the revenues to protect those in need. The consensus in based also on the acknowledgement of entrepreneurs that they also increase in the long-run profits and the sustainability of economic growth for the benefit of rent seeking corporate sector.

An agreement and understanding must be created that the basic network consisting health and medical care, unemployment insurance, public pension etc. is a compromise, which benefits also the corporate sector and economic competition. Distribution of purchasing power benefit also markets and economic growth- poor people do not constitute a market. Creation of these understandings is possible only based on adequate social capital and implemented through democratic procedures. Violent outbursts to try to correct the situation tend to kill the economic growth leaving even less to be redistributed. One of the latest examples in the SSA is the violent take-over the farms of white landowners in Zimbabwe. The manifestation of disregard of the existing ownership rights, even if they are perceived as correction of social unjust, zeroes the markets and economic growth.

A specific line of dicussions, following the traditions of debates in the 1970's, has emerged, whether the gap between the poor countries is increasing or decreasing, or whether the differences of income and wealth have been increasing. The discussion refer to reliability and adequacy of the GDP statistics and the problems related to GINI and T-factors in measuring the income distribution. Paticularly Dollar & Kraay from the World Bank's Development Research Group have defended the view, that the global trend toward greater inequality would have peaked around 1975 and since then stabilised or possibly reversed by virtue of the accelerated growth by China and India (Dollar & Kraay 2002a).

Globalisation leads to faster growth and reduction of poverty in poor countries. The growth rates of rich countries have slowed down during the last 30 years, whereas the growth rates of globalisers have accelerated. This means, the globalisers are catching up the rich industrial countries. The non-globalisers are falling behind. For instance, in the 1990s rich industrial countries grew at a rate of 2.2% per capita, the globalising developing countries at 5.0% per capita and the non-globalising developing countries only at 1.4% per capita. Considering the development within countries, growth rates following the growth of trade increased proportionally the incomes of the poor, and the absolute poverty has been sharply reduced in the globalising economies. Moreover, in the 1990s the growth of the GDP per capita has been 5% for the globalisers, 1% for the non-globalisers and 2% for the rich countries. Restrictions of trade would impose only further hardship on poor people in the developing countries. The authors conclude that open trade regimes tend to boost growth and reduce poverty in poor countries (Dollar & Kraay 2001b).

Dollar & Kraay's views have been challenged by a bulk anti-global research maintaining that globalisation has dramatically increased inequality between and within nations and that the policies of the international trade organisation and international donors only exacerbate the situation (Mazur 2000, Weisbrot & alia, 2000).

4.6 Development hazards

Economic development has bee unpredictably interrupted by random events, either man-made catastrophes like wars or epidemics (AIDS and tuberculosis), or natural disasters like earthquakes., floods, drought followed by famines and general deterioration of the living conditions. Particularly in the sub-Saharan Africa disasters are an obvious reason for the instability of the economic growth. The Ivory Coast, Namibia were previously hit with natural disasters (Easterly2001). Currently bad crops in Malawi, Zimbabwe, Swaziland, Lesotho and Mosambique led to shortage of food threatening a large part of population in these countries.

According to insurance statistic, number and economical losses have monotonically increased since the 1950s. The number of extreme weather events per decade from the 1950s through the 1990s 20-27-47-63-89 incidents and the economic losses 41-73-132-204-629 billion dollars respectively (Munich Reinsurance Company, Annual Review: Natural Catastrophes 2000 (Munich: Munich Re Group) from (Heller & Muthukumara 2002 p. 30). Particularly rural poor in the tropics and subtropics are extremely vulnerable and unable to cope with natural catastrophes and their consequences such as diseases or malnutrition due to losses of crop and arable land.

Wars have dumped the economic growth particularly in Ethiopia, Sudan, Liberia and Somalia. Ethnic controversies (Rwanda in 1994) and religion (Sudan) are usually considered as mayor reasons for African wars. There is no intrinsic hate between ethnic groups or intrinsic hostility in religions itself. Political leaders, supported by corrupted administration, police and army, fuel rivalries between ethnic and religious groups ultimately to gain personal power and wealth for themselves. By referring to current or historical unjust and promising better material future to manipulate they are able to provoke people against each other. Often economic interests and nationalism are included to the texture, like oil in Sudan (Martin 2002). Also diamonds in Liberia or land properties in Zimbabwe serve as examples.

Wars tend to follow their own logic, a vicious circle nourished by hatred and revenge: they continue until the population has been impoverished and fatigued or the leader has escaped or been expelled (like Idi Amin from Uganda or Mobutu from the Democratic Republic of Congo) or killed (like the UNITA leader Jonas Savimbi in Angola). The war in Sudan has raged 11 years of its 45 years of independence has resulted in two million fatalities and made 4 million homeless out of the Sudanese population of about 29 million. The Muslim northerners contempt for the Christian southern culture and feel that it is their right, if not duty, to subjugate the southerners and take over the oil resources for their own benefit. The war is not likely to end before this goal has been achieved (Martin 2002).

Quite often no wars and needed for mass starvation: drought, flood, erosion, epidemics, excessive corruption, or any combination of these. Civil wars lead by corrupted dictatorships and governments still continue and have their effects in Angola, Democratic Republic of Congo, Burundi, Rwanda, Eritrea, Ethiopia, Sudan, Somalia, Liberia, Sierra Leone and Western Sahara. Nigeria, having also suffered from Civil Wars, continues to have chaotic politics, Malawi suffers from hunger. Nigeria, which succeeded to get rid of its military government three years ago, has been able to improve its image as a serious trading partner. Still, members of the corrupt government and administration are busy in grabbing themselves larger shares of the country's oil wealth. Also in Ghana, start for transition in took place in 1983. Economically, the economy had experienced a disaster with cut of the international financing due to arrears. The situation was aggravated further by draught and forced remigration of large number of Ghanaians expelled from Nigeria. Lately Ghana has taken steps to diversify its production and exports, and promote the entrepreneurship. Uganda, after its terror regime 10 years ago and Mozambique, having experienced war and extensive floods in the 1990s, have been lately singled out as particularly successful countries (The Economist, 6 April 2002, "Middle East and Africa", pp.38-40, Chand 1993, p. 353).

Although wars, conflicts and social disorder continue in Caucasus and affect also the Central Asian Republics, particularly the vulnerability SSA continuous problems demonstrates the inability the weak states and institutions to protect the people against madmen and warmongers taking lead as dictators, against consequences of natural catastrophes, drought, floods and diseases; or against alleged or real exploitation from the side trans-national corporations or double standard trade policies of the developed countries.

5. Summary and conclusions

5.1 Summary

Current development literature provides wide support to the primacy of institutional development supported by property rights based economic freedoms. Institutions generating social capital contribute the sustainability of economic growth. Countries, with high quality institutions conducive for economic freedoms, have also experienced high economic growth.

Institutions generating social capital (government, parliament, political parties, NGOs) warrant sustainability of growth. The social capital consists of incentives to citizens and companies to support the aims of the political leadership. Insufficient social capital with economic growth tends to lead to dual economy, where income and wealth are unevenly distributed between social groups and regions. The societies with weak institutional capacities in generating social capita tend to be politically unstable and involve major financial risks to investors in the longer run.

The redistribution of income and wealth runs against the idea of property rights and economic freedoms. Legitimisation can be derived from the redistribution of income and wealth can be effected for reduction of poverty and to support those not able to participate in production process (children, disabled, old people and unemployed) provided, that it is based on adequate social capital generated to democratic procedures including also acceptance of the corporate sector. The optimality is probably country specific, depending on the level and growth of the GDP. Probably also larger inequalities can be accepted in large economies with big factor mobility, than in small economies or in large economies with low factor mobility.

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The state consists of institutions, vested with the task to protect its members comprising both physical and juridical persons against external and internal threats. The administrative traditions associated with the principle of ruling by law in the FSU countries; the state powers are necessarily parallel with those of individuals and firms. The rule of law in the developed industrial countries puts the citizens (individuals and firms) to a more equal position versus state. This implies, in practice, that the burden of proof of the compliance with rules is on officials so that everyone is presumed to act in a good faith if and until otherwise is proved.

The administrative practices, that is, the behaviour and attitudes of the state officialdom, change slowly. Reform oriented governments may gradually catalyse change in the government. Still, the change has to be based on introduction and enforcement of economic freedoms based on clear and enforceable property and contract rights and taking into account the redistribution requirement based on social capital.

The macroeconomic reforms – liberalisation, stabilisation through fiscal and financial austerity, privatisation – can all be reduced back to the private property rights based economic freedoms. Although most of the governments both of the FSUCEE and SSA have already assumed and accepted the principles of the macroeconomic reforms, the enforcement and sustainability can be achieved only, if they are understood and supported by the state officialdom.

In the FSU countries this is necessarily the case. Despite the reform oriented government under president Vladimir Putin, the enforceability suffers from the Soviet minded state officialdom, not understanding or accepting the rule of law. This is not only, because the rule of law runs across the personal rent seeking but also, because the existing institutions do not provide them with standardised procedures, transparency and incentives to do the right things. The absence of the technical standards and arrangements necessary to make the administration operational is to be blamed. On the other hand, the very task of create the institutional capacities and right attitudes is a slow process.

In the SSA countries the state structures are often simply too weak to protect their citizens against climatic or national disasters or – against their own rent seeking leaders. Only in very few cases (Botswana), the pre-colonial experience assisted in balancing property rights between rulers and the ruled ones. Long geographic and cultural distances of most of the SSA, Central Asian and Southern Caucasus economies from the developed markets, or geographic and cultural affinity of the CEE and the Baltics with their European neighbours contrasted to the distance of the explain, why the states' institutional capacities in the SSA and FSUCEE failed, or in some cases succeeded in developing economic growth.

During the second part of the twentieth century, the growth of the international trade exceeded the economic growth. However, the FSUCEE and the SSA remained isolated (tables 7 and 8), and the tiny trade flows consisted mainly of exports of fuels and raw materials in the case of the FSU or other specific export items like cocoa, coffee, copper, diamonds etc (table10). During the 1990s the CEE and Baltic countries rapidly redirected their trade away from the Russia to Western European countries and simultaneously moved from inter-industry to intra-industry trade. As confirmed by substantial empirical evidence, the growth of the international trade has been a major factor contributing the economic growth. However, simultaneously also the income and wealth gaps between the developing and developed world have been widening.

5.2. Conclusions

The most profitable markets and investment opportunities are found in rich countries. Poor people do not constitute a market. Politically and financially risky society lacking proper property rights does not attract FDI. Trade and FDI are not development instruments in the hands of donors, and therefore discussions and efforts should be focussed to these factors, development of which attract the trade and FDI. The CEE and Baltics received more than 80% of the capital inflows to the FSUCEE region in from start of transition to 1997. [17] The Share of the FSUCEE was larger than the share of the SSA (Garibaldi & alia, 1999). Still, these the major capital flows avoided these regions (Laulajainen 1998).

As for the FDI, the joint share of the FSUCEE and the SSA was only 1.6% of the world's total FDI net inflows in 1999. The share of the merchandise imports of FSUCEE and the SSA accounted for 4.4%, and

[17] Russia being net exporter of capital.

exports for 4.7% of the world's total merchandise trade. While more than 95% of the FDI, trade and capital flows keep passing by these regions, their alleged blessing for the economic growth seem to benefit only the rich or middle income countries. A corollary from trade concentration to the rich countries is that the trade policy is important only to the rich countries, but matter less for poor countries. The connection of trade policy and economic growth is bound to remain ambiguous, as observed by Rodriguez and Rodrik (1999), simply because the poor or poorly growing countries do not involve in the international trade for other than trade policy reasons.

The growth international trade and the FDI indicators of development and they correlate with economic growth, but they are not decision-making variables of the international donors. In free markets the decisions to invest, or to export or import, are made by private entrepreneurs, not by donors. What is left for donors is the improvement of state structures and institutions in the SSA and FSU regions by means of technical assistance and funding the training of officialdom to increase the administrative capacities. The priority of the development assistance work should be of quality of state institutions adequate to sustain free markets and democracy.

In the development work the macroeconomic reforms should be included to the conditionalities, first, because they serve as a road map in creation the institutional capacities and defining the role and behavior of the state officialdom. Second, stabilisation of the internal and external values of domestic currency is important, because the failure in doing that would lead to distribution effects violating the property rights. The lack of property rights based standardisation explains excessive bureaucracy and corruption, and slow growth of the financial and capital markets (de Soto 2000). The technicalities in the reform design are often put aside in the development agendas; there is no reason to belittle the significance of the technical side of reforms and the importance of competent technical assistance extended to the governments to improve the state structures. Minute technicalities matter, because the devil lives in small things.

Focussing on public sector should also to be extended to private institution building, development of democratic controls, transparency and party system relevant in generation of adequate social capital so as to determine the optimal degree of income redistribution. The optimality is determined by the level of the GDP, the size of economy, factor mobility and needs to avoid disincentives for competition and rent seeking by too high allowances on the one hand and political and economic risks and disorder by too low allowances.

Discussion and research on development issues is necessary. Donors are also faced with rapidly increased complexity of problems. The learning process is not always gratifying, because often, as soon as the mistakes have been observed and corrective policies and measures assumed, a number of quite new problems emerge leaden to new mistakes (Smirnov 1999). The donors deserve the credit for the work they have accomplish by collecting a astounding amount of data and analysed information, in assisting the developing countries to construct basic infrastructures and later in efforts on extending technical assistance and financing to improve the health, education and training and social conditions of the poor in developing countries (Einhorn 2001, Wolfensohn 2001).

The mission to improve the institutional capacities of national state structures and institutions, both in the SSA and FSUCEE, is also in harmony in globalisation. Strong and institutionally well developed national states would be able to protect their citizens against the alleged or real drawbacks of globalisation. Therefore, the national state in a globalised and integrated world is not likely to became abundant. Failed, disorderly, weak or corrupt states are difficult to be integrated with the strong ones. Disciplined and non-corrupted states composed by high quality institutions - not national isolation and autarky - is precondition for globalisation. Increased competition due to globalisation makes the participating national states stronger. (Wolf 2001).

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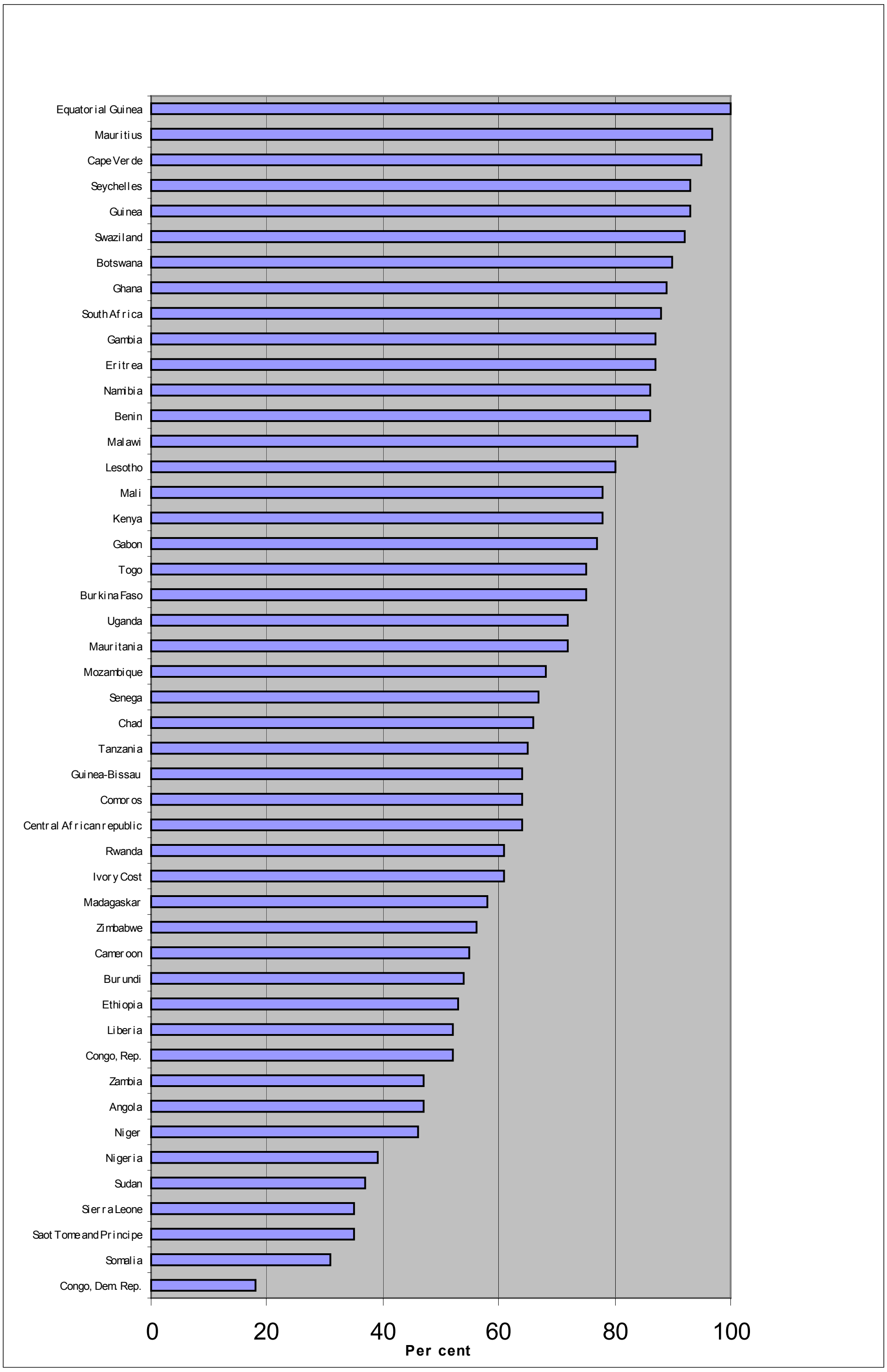
STATISTICAL APPENDIX

Appendix Chart. Sub-Saharan countries: level of 1998 GDP per capita as a share of maximum achieved



Source: UN 2001, Table 1, pp. 6-7.

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Appendix table 1. Economic freedom and financial risks. Average scores for the FSUEEC and SSA according to Weder's typology related to level of institutional quality and economic growth

Heritage Foundation & Wall Street Journal 2002

Free <2.0, mostly free 2.0<3.0, mostly unfree 3.0<4.0, repressed 4.0-5.0

	Total score 2002	Total score 1997	Change since -97 negat. = improved	Trade	Tax burden	Gov. interven	Monetary policy	FDI	Banking & finance	Wage & prices	Property rights	Regulation	Black market	Number pf countries	GDP 2000 current prices million $	share of grand tot
FSUCEE1	2,5	2,8	-2,6	2,2	4,3	2,0	2,6	2,0	1,8	2,2	2,2	2,6	2,9	5	277208	31
FSUCEE2	2,6	3,0	-3,2	3,3	7,7	4,7	4,0	4,0	4,7	4,7	6,0	6,0	6,7	3	37493	4
FSUCEE3, Russia	3,5	3,7	-1,3	3,0	3,3	2,8	4,3	3,0	3,4	3,0	3,7	4,0	4,1	7	309081	35
FSUCEE4	4,1	4,3	-0,9	3,8	3,6	3,4	4,4	4,0	4,4	4,2	4,0	4,4	4,7	5	59752	7
FSUCEE5	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0	0,0	0
FSUCEETOTAL	3,2	3,5	-1,7	3,1	4,3	3,0	3,9	3,2	3,5	3,4	3,8	4,1	4,3	20	683534	78
Russian Federation	3,7	3,6	0,8	4,0	3,5	2,5	5,0	3,0	4,0	3,0	4,0	4,0	4,0	1	251092	29
SSA1	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0		
SSA2	3,1	3,3	-1,0	3,8	3,3	3,1	2,7	2,7	2,8	2,3	3,0	3,7	3,6	6	33211	4
SSA3	3,2	3,3	-0,6	3,9	3,5	2,5	2,3	2,8	3,2	3,0	3,5	3,7	4,1	14	54426	6
SSA4, Nigeria	2,8	3,0	-1,2	3,3	2,7	2,2	1,3	2,9	3,1	2,1	3,1	3,3	3,8	9	73185	8
SSA5	2,0	2,0	0,5	2,1	1,5	1,3	1,1	1,4	1,6	1,5	1,7	1,8	1,9	15	36371	4
SSATOTAL	2,7	2,8	-0,5	3,2	2,6	2,1	1,7	2,3	2,6	2,2	2,7	3,0	3,2	44	197193	22
SSA5 all*	4,0			1,7	1,3	1,1	0,9	1,2	1,3	1,3	1,4	1,5	1,6	14	36371,0	0
SSA5 less islands	4,3													11	18560	0
Nigeria	3,6	3,3	1,7	4,0	3,0	3,0	1,0	4,0	4,0	3,0	4,0	4,0	5,0	1	41248	5
Geand total	2,9	3,0	-0,9	3,1	3,1	2,4	2,4	2,6	2,9	2,6	3,0	3,3	3,6	64	880727	100

Remarks: SSA5 includes only countries, scores of which have been indicated in the source statistics
*SSA5 all includes war countries, which have been assigned score of 5
**SSA5 all incl. war countries, which have been assigned score of 5 less small island states

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Persentages, total max, 100 indicates zero-risk, different riskes weighted as indicated in columns.
The smaller the score, the bigger are the financial risks.

	Total score	Political risk	Econ. perf.	Debt indicators	Debt in defoult or resched.	Credit ratings	Access to Bank finance	Access to short-t. finance	Access to capital markets	Discount for for-faiting
Max. possible/column	100	25	25	10	10	10	5	5	5	5
FSUCEE1	68	18	10	8	10	6	4	3	4	4
FSUCEE2	58	15	8	9	10	4	3	2	3	4
FSUCEE3, Russia	32	6	5	8	9	1	1	2	1	0
FSUCEE4	29	5	3	9	10	1	0	2	1	0
FSUCEE5	0	0	0	0	0	0	0	0	0	0
FSUCEETOTAL	44	10	6	8	10	3	2	2	2	2
Russian Federation	36	9	7	9	7	2	0	2	0	0
SSA1	0	0	0	0	0	0	0	0	0	0
SSA2	25	6	4	5	6	0	0	2	1	1
SSA3	28	6	4	6	10	0	0	2	0	1
SSA4, Nugeria	24	4	3	5	9	0	0	1	0	1
SSA5	25	3	3	6	10	0	0	2	1	0
SSATOTAL	26	0	0	1	1	0	0	0	0	0
Nigeria	21	5	4	8	0	0	0	2	0	2
Geand total	14	3	2	3	3	1	1	1	1	1

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Appendix table 2. Overlapping of FSUEEC and SSA countries by economic freedom and financial risk

Freedom								Financial risks							
FSUCEE				SSA				FSUCEE				SSA			
Rank	(the smaller score, the better freedoms)	Total score 2002	Group	Rank	(the smaller score, the better freedoms)	Total score 2002	Group	Rank	(the larger score, th lesser risk)	Total score March 2002	Group	Rank	(the larger score, the lesser risk)	Total score March 2002	Group
1	Estonia	1,8	1					1	Slovenia	73,8	1				
2	Lithuania	2,4	2					2	Hungary	70,2	1				
3	Czech Rep.	2,4	1					3	Czech Rep.	68,5	1				
4	Hungary	2,4	1					4	Poland	65,8	1				
5	Latvia	2,5	2					5	Estonia	63,5	1				
6	Poland	2,7	1					6	Slovak Rep.	62,5	2				
7	Armenia	2,7	3					7	Latvia	58,3	2				
8	Slovak Rep.	2,9	2									8	Mauritius	56,7	5
				9	Botswana	2,9	2	9	Lithuania	54,4	2				
				10	Cote d'Ivoire	2,9	2	10	Kazakhstan	47,9	3				
				11	Namibia	2,9	2					11	Seychelles	37,3	5
				12	Mali	2,9	3	12	Azerbaijan	37,0	4				
				13	Swaziland	3,0	3					13	Kenya	36,5	4
				14	Uganda	3,0	3	14	Russian Fed.	35,9	3				
				15	Mauritius	3,0	5					15	Gambia	35,5	2
				16	Mozambique	3,1	3					16	Ghana	35,5	2
				17	Central African Republ	3,1	5					17	Uganda	34,8	3
18	Slovenia	3,1	1									18	Swaziland	34,8	3
				19	Gambia	3,1	2					19	Senegal	34,5	3
				20	Madagaskar	3,1	3	20	Armenia	34,1	3				
				21	Benin	3,2	3					21	Tanzania	32,8	2
				22	Cape Verde	3,2	5	22	Ukraine	29,8	3				
				23	Burkina Faso	3,2	3	23	Turkmenistan	29,7	4				
				24	Senegal	3,2	3					24	Niger	29,6	4
				25	Kenya	3,2	4					25	Burkina Faso	29,6	3
				26	Cameroon	3,3	3					26	Mozambique	28,9	3
				27	Gabon	3,3	3	27	Uzbekistan	28,9	4				
				28	Zambia	3,3	3					28	Madagaskar	28,8	3
				29	Guinea	3,3	3					29	Gabon	28,8	3
				30	Mauritania	3,3	5					30	Lesotho	28,7	3
31	Moldova	3,4	3									31	Cote d'Ivoire	28,6	2
				32	Ghana	3,4	2					32	Equatorial Guinea	28,6	5
				33	Tanzania	3,4	2					33	Cape Verde	28,4	5
34	Georgia	3,4	3									34	Cameroon	28,0	3
				35	Lesotho	3,4	3					35	Mali	27,9	3
				36	Rwanda	3,4	5	36	Moldova	27,8	3				
37	Azerbaijan	3,5	4					37	Georgia	27,6	3				
				38	Niger	3,5	4					38	Sierra Leone	27,1	5
				39	Malawi	3,5	5	39	Belarus	26,9	4				
				40	Ethiopia	3,6	5					40	Togo	26,7	4
41	Kazakhstan	3,6	3									41	Ethiopia	26,3	5
42	Kyrgyz Rep.	3,6	3									42	Benin	25,8	3
				43	Chad	3,6	4					43	Namibia	25,6	2
				44	Nigeria	3,6	4					44	Malawi	24,9	5
				45	Togo	3,6	4					45	Guinea	24,9	3
46	Russian Fed.	3,7	3					46	Tajikistan	23,7	4				
				47	Congo	3,7	4					47	Central African Repul	23,5	5
				48	Congo, Dem. Rep.	3,8	5	48	Kyrgyz Rep.	23,1	3				
49	Ukraine	3,9	3									49	Chad	22,5	4
50	Tajikistan	3,9	4									50	Congo	22,4	4
				51	Equatorial Guinea	3,9	5					51	Eritrea	21,9	5
				52	Guinea-Bissau	4,0	4					52	Rwanda	21,3	5
				53	Zimbabwe	4,3	3					53	Nigeria	21,2	4
54	Belarus	4,4	4									54	Angola	20,8	4
55	Uzbekistan	4,4	4									55	Zambia	20,1	3
56	Turkmenistan	4,4	4									56	Burundi	19,9	5
				57	Angola	na	4					57	Sao Tome and Princi	19,6	5
				58	Liberia	na	4					58	Guinea-Bissau	18,9	4
				59	Sierra Leone	na	5					59	Mauritania	17,8	5
				60	Somalia	na	5					60	Liberia	15,8	4
				61	Sudan	na	5					61	Zimbabwe	15,7	3
				62	Burundi	na	5					62	Congo, Dem. Rep.	14,1	5
				63	Comoros	na	5					63	Somalia	12,1	5
				64	Eritrea	na	5					64	Botswana	na	5
				65	Mayotte	na	5					65	Comoros	na	5
				66	Sao Tome and Princip	na	5					66	Mayotte	na	5
				67	Seychelles	na	5					67	Sudan	na	5

Appendix table 3. General statistics on economic growth, foreign trade, debt, and aid in 1999

	CEE+B	FSU-B	FSUCEE	SSA	LI	MI	HI
Numer of countries in the category	8	12	20	48	64	93	50
Population, million	74	283	357	643	2417	2665	896
GDP (current US$) (bill)	318	517	835	324	1033	5519	24323
GDP per capita, PPP (current international $)	9689	5435	6317	1600	1918	5317	25707
Exports of goods and services (current US$) (bill)	134	238	372	87	214	1600	5323
Imports of goods and services (current US$) (bill)	149	169	318	100	245	1425	5266
Exports of goods and services (% of GDP)	42	46	45	27	21	29	22
Imports of goods and services (% of GDP)	47	33	38	31	24	27	22
External debt, % of GDP	39	41	40	67	55	36	na
External debt, total (DOD, current US$) (bill)	125	210	335	216	572	1991	na
Total external debt service (TDS, current US$) (bill) in 19!	23	18	40	14	47	342	na
DOD/TDS	5,4	11,7	8,4	15,4	12,2	5,8	
External debt, total (DOD, current US$)/capita	1689	742	938	336	237	747	na
Total external debt service (current US$) (mill/capita)	304	62	112	22	20	128	na
Aid per capita (current US$)	30	13	16	20	9	9	2
Aid, % of GDP	0,7	0,7	0,7	4,0	2,1	0,4	0,0

Explanations: CEE+B stands for the Central Eastern European and Baltic countries, FSU-B stands for the Former Soviet Union countries without the Baltics. LI stands for Low income countries with GDP/capita 755 USD or less, MI Middle Income countries with 756-9265 USD, and HI High Income countries with 9266 USD or more.

Source: Author's calculations based on data in World Bank's CD-ROM 2001.

Generaldevelopmentcomparison.xls