The IMF in Central and Eastern Europe: Looking back at the past thirty years (by Jiří Jonáš)

***Jiří Jonáš**, former advisor at the Czechoslovak Ministry of Finance in Prague, joined the IMF in 1991 when the IMF was heavily involved in the transformation process of Central and Eastern European countries from centrally planned to market economies. Quoting Ján Toth, the Deputy-Governor of the NBS, the IMF employees involved in the assistance were among the "smartest people in the country who provided feedback to us, often smart enough to catch any fiscal gimmicks, we were playing". Still with the IMF, Mr Jonáš is currently Senior Economist at the Asia Pacific Department.*

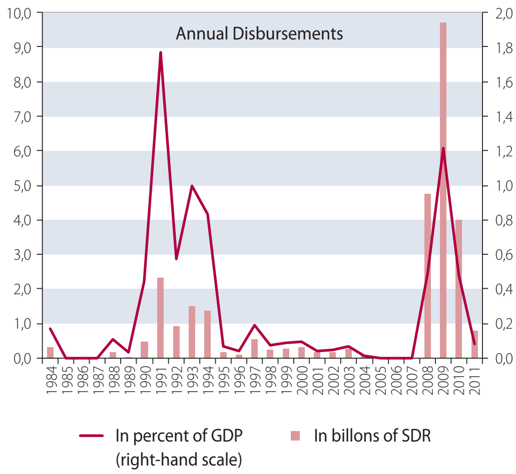
In his presentation, Mr Jonáš provided a complex overview of the IMF's involvement in the Transformation process, not only in Slovakia, but also in the rest of the transition economies in this region. For the purposes of his presentation, the term encompasses all former centrally planned economies that are currently members of the EU, plus Croatia, which will join the EU on 1 July this year.

Starting with the history of the IMF and transition economies Mr Jonáš pointed out the main milestones for Czechoslovakia (Slovakia) and the rest of the Central and Eastern European transition economies with regard to their IMF membership. Czechoslovakia was the first one of this group to become a member of the Fund in 1945, followed by Poland in 1946. In 1954 it was the only country expelled in the whole history of the Fund, which was due to political reasons and its failure to provide required data, unlike Poland, which withdrew its membership under pressure from the Soviet Union in 1950.

The presentation continued with an overview of the history of the IMF's help to the transition economies, which was provided in the form of both lending and technical assistance. As shown in Figure 1, illustrating the lending to transition economies in both SDR (left axis) and percentage of GDP (right axis), two peaks in financial assistance occurred. One in the early 1990s, in the early stages of transition, followed by a winding down until 2007, when there was no credit outstanding to the transition economies. With the financial crisis there was a substantial increase in the volume of loans to transition economies, reaching the second peak in 2009, as a consequence of the global crisis.

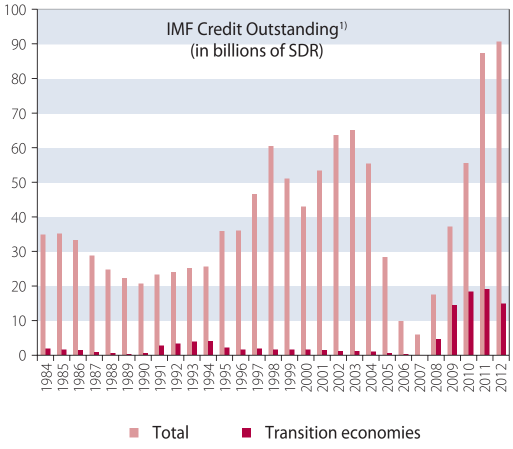
In Figure 2 Mr Jonáš showed the total help provided by the International Monetary Fund, in the period 1984 to 2007. As can be seen, the spikes in total assistance provided by IMF were connected with the Mexican (1995), Asian (1997-1998), Brazilian and Argentinian (2000-2001) crises and the amount of financial assistance to transition economies was not significant, since these economies were still detached from the global environment. However, starting in 2008 lending to transition economies rose as significantly as the rest of the global economy and reached almost half of the total financial assistance provided by IMF in 2009 (even though only three countries were involved in the financial assistance: Hungary, Romania, and Latvia). As Mr Jonáš explained, the fact, that the cri-

Fig. 1 IMF lending to the transition economies



Source: IMF data.

Fig. 2 Peaks in total IMF lending ≠ peaks in lending to transition economies



Source: IMF data.
1) End December, GRA credit

sis affected the post-Soviet countries together with the rest of Europe was actually a result of their successful integration into the global system in 1990s.

Mr Jonáš also mentioned various periods with outstanding IMF credit to particular countries where different time periods were noticeable, ranging from one year (Czech Republic) to twenty-five years (Romania).

The second part of his presentation was dedicated to particular programmes in this region. The main policy challenges focused on three separate stages:

- pre-transition period,
- early days of transition – 1990s,
- late 2000s.

Even though it was not widely known, the Fund was providing **assistance to the Central and Eastern Europe economies even before 1990s**. Particularly, programmes for Hungary in 1982, 1984 and 1988 were designed to deal with external shocks in the form of the debt crisis and liquidity problems, as banks did not roll over loans. Hungary always had a strong commitment to service its debts. A fact in Hungary's favour was that it has already adopted some reforms (unification of the exchange rate, devaluation of the currency, balance of payments adjustment). The second country assisted by IMF in the 1970s and early 1980s was Romania in 1975, 1977 and 1981. Romania encountered balance of payments problems caused predominantly by natural disasters (floods in 1975, earthquake in 1977 and oil shocks in 1981).

The programmes in the early 1990s were designed to assist and guide the integration of isolated transition economies into the global economy. As the countries had to deal with the collapse of central planning and the Soviet Bloc trade system, as well as to ensure macroeconomic stability after price liberalisation, a viable balance of payments position and building the institutional framework of a market economy; the support in the form of policy advice, lending and technical assistance was a unique challenge for the Fund. The programmes in the early days of transition had common features such as strict demand management to prevent one-off price jumps becoming embedded in underlying inflation, reduction in the size of government (privatisation, public expenditures – some programmes had targets to reduce total spending by 15-20% of GDP in one or two years) to bolster the private sector and move to liberalised prices, market-driven exchange and interest rates, but also each had its own particular specifications, such as different exchange rate policies (some countries had pegs, some had a flexible exchange rate), the approach to systemic reforms such as privatisation and debt relief (debt restructuring in Poland, Bulgaria and debt servicing in Hungary). In this period a new tool, the Systemic Transformation Facility.[1] Necessary technical assistance was also provided to the transition economies, with Bulgaria and Poland using the most, with 17.3 staff years (in other words, equivalent to nine people providing technical assistance for almost two years) and 13.7 staff years respectively.

Programmes in the late 2000s focused on very different challenges to those in the early 1990s. Unlike the latter, which were focused on integrating the still isolated countries of Central and Eastern Europe into the global economy, the programmes in the late 2000s addressed some of the problems that arose from the successful integration in the 1990s, as the countries were open to capital flows, had a large presence of foreign investors and strong trade and financial linkages with EU. This resulted in a gradual build-up of vulnerabilities during the "roaring" 2000s, such as rapid credit growth, increasing currency mismatch (for instance borrowing in Swiss francs in Hungary) and rising current account deficits stemming from currency appreciation. All of this created the underbrush ready for the spark to start the fire, which of course came in 2007-2008 when the global financial crisis took hold. Just like the earlier programmes, these had certain common features, such as an effort to restore investor confidence and to avoid a run on debt and currency markets, tightening of fiscal policy, ensuring adequate capitalisation of banks and significant external financing. In this period the Fund introduced a new financial instrument, the Flexible Credit Line[2], so far used only by Poland.

Mr Jonáš concluded that the International Monetary Fund played a key role in assisting the transition from a centrally planned to market economy both by lending and providing technical assistance. It was always able to adjust flexibly to the new challenges and circumstances and, afterwards, help in managing the challenges stemming from the successful economic and financial integration of individual transition economies into the global economy.

(Compiled by Jakub Obst)

1 Systemic Transformation Facility was introduced in order to help countries in transition, as they didn't have yet the ability to implement standard stand-by arrangements. This facility featured less demanding conditionality than the traditional stand-by arrangement and was supposed to buy some time to develop more comprehensive reforms plans. The facility was commonly used by most of the transition economies (with the exception of SK, CZ, HU and PL) until it expired in April 1995.

2 The main feature of this tool is its precautionary character, as it doesn't imply actual drawing of loans, but provides insurance. The Flexible Credit Line is available to countries with strong policies and fundamentals and is mostly used in the case of adverse external shocks or a loss of confidence in order to prevent investors from making rash decisions.