

## **U.S. AID TO CENTRAL AND EASTERN EUROPE: RESULTS AND RECOMMENDATIONS**

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Most assessments of foreign aid to Central and Eastern Europe have been from the donors' perspective. How do things look from the other side?

The 1989 collapse of the communist Eastern bloc inspired a major shift in the priorities of the Western development and aid community. Western agencies re-oriented resources and diverted personnel en masse from the Third World to Central and Eastern Europe. Although the donors had long-standing foreign aid institutions in place to handle aid to the third world, donors nevertheless added new entities and reorganized the mechanisms of aid management to administer aid to the new recipients.

The European Union (EU) created a wholly separate PHARE (Poland-Hungary Aid for Restructuring the Economy) program to manage assistance to the region. The U.S. Agency for International Development (USAID) created a new entity to manage aid to the new recipients, the Bureau for Europe and the New Independent States. The U.S. effort engaged some thirty-five federal agencies, most of which had no prior foreign aid or overseas experience. To coordinate the effort, the U.S. government created the Assistance Coordination Group, a body chaired by the State Department.

The West offered aid, and the East accepted it. Western politicians came to show support. So how, in a few short years, did this promising cooperation become filled with so much disillusionment? Many recipients wanted to know "where have all these billions gone?" Eastern citizens developed negative impressions of Western advisers, saying, "foreigners don't understand our conditions" or "these bureaucrats can't tell my country from Shangri-La." The disillusionment was often mutual. Donor representatives would grumble in private, "they [the recipients] just can't handle it," "they have no sense of democracy," or "it's a gift--why are they complaining?"

How could there be such a discrepancy between how aid projects look in the field and the "success stories" conveyed in donor reports? To find out, I conducted extensive interviews in Washington, Brussels, Central and Eastern Europe, and Russia; I discovered that aid is a story not just of economics but of political, social, and cultural impact. These concerns may seem tangential, and they are certainly less quantifiable than the study of expenditures and their targets. Yet the technical assistance that makes up much of the Western aid packages is as much about relationships among people as it is about goods and money.

How local people interpret aid affects whether aid can become the object of criticism by nationalist demagogues as examples of foreign influence. A Czech politician launched his career by waging a campaign against an aid program. The slogan, "A Foreign Elite Steals from us while the Polish People are at the Bottom," decorates the main entrance to a Polish factory.

Another reason the political and social aspects of aid to Central and Eastern Europe should be given special consideration is that many of the donors' approaches to aid imply substantial political and social transformation. In fact, changing the very nature of recipient institutions is a goal of aid to Central and Eastern Europe (whether explicitly stated or not). (This is a marked departure from aid policies to the third world: aid to India, for example, tends to be couched in terms of efficiency and economic growth.) Moreover, many in the West argued that they had only a brief "window of opportunity" to effect change and that they had to move quickly to fill the political-economic vacuum created by the collapse of the Soviet bloc. The donors' heightened sense of urgency, however, may have led to overpromising and to frustration on the part of the recipients.

## Aid to Poland, Hungary, and the Former Czechoslovakia

It is worthwhile to examine aid responses and models in Poland, Hungary, and the former Czechoslovakia for two reasons. First, after four years of operation, an analysis of key programs is warranted. Although much attention has been paid to the donor side, aid projects tend to look different from the vantage point of the field. Second, because these countries were considered the most likely to make a successful "transition," it is important to examine how the assistance has worked in these "model" cases.

If the aid process is not understood, problems that arose in these nations might be repeated and even exacerbated further south and east--in Bulgaria, Romania, and Albania, and in Russia and Ukraine, countries that are generally regarded as more economically and politically troubled. They also had less prior exposure to the West. It is also important to understand why and in what areas aid to Central and Eastern Europe has been effective, and the extent to which these productive models might be applicable to the new aid situations. My research, involving extensive interviews with aid principals during 1991-92 and the spring and summer of 1994, has identified the following three phases in recent aid history in Poland, Hungary, and the former Czechoslovakia.

**Euphoria: 1989-90.** East Europeans brought an idealized view of the West and naive understanding of foreign aid to their expectations of what the West could do for them. The late Rita Klimova, who was Czechoslovak ambassador to the United States, characterized her country's expectations at the time: "People imagined the United States to be a kind of rich Soviet Union." What she meant was, "We expected to have a relationship of dependence, as with the Soviet Union, but with a lot more cash coming our way."

These expectations were fed by the flood of visitors from the West conveying their interest in the region and their willingness to help. The misleading information that circulated in the press in 1990-91 also fueled these expectations. In Poland, news circulated that the West was sending billions of dollars in aid to Poland without qualifying that this included export credits and loans that would have to be repaid. And many people in the region did not understand that much of the grant aid allocated was for technical, not capital, assistance and that advisers, not money, would be sent. All this paved the way for the difficult second phase.

**Frustration and Resentment: Beginning in 1991-92.** Aid outcomes suffered not only from the recipients' unrealistically high expectations and misunderstandings about the type of aid that would be sent but also from the donors' often unfulfilled promises.

Many people in the region began to wonder where the money had gone. As Poland's chief coordinator of foreign assistance, Minister Jacek Saryusz-Wolski, lamented: "When people in Poland hear that billions of dollars come to Eastern Europe, they expect that Poland gets one-half or one-third of that money. . . . Very often people ask us what happened to it." In February 1992, Polish president Lech Walesa articulated the growing resentment when he spoke at the European Parliamentary Forum in Strasbourg, charging, "It is you, the West, who have made good business on the Polish revolution. . . . The West was supposed to help us in arranging the economy on new principles, but in fact it largely confined its efforts to draining our domestic markets."

Similarly, Hungary's chief aid coordinator, Minister Bela Kadar, stated: "The public learns from official statements that the Western world has transferred resources on the order of \$40 billion to \$70 billion so far, to promote transition in the post-communist countries. One has to ask, where have all these billions gone?" In fact, there was a considerable gap between donors' allocations and actual disbursements in the region. In 1992 only an estimated 11 percent of the committed monies actually had been disbursed.

The hundreds of "first meetings" with Westerners also led many Polish, Hungarian, and Czechoslovak officials to conclude that the West was delivering far less than promised. The pendulum swung from an initial open-arms welcome to foreigners to the opposite reaction: "Foreigners don't understand our conditions." Officials in Warsaw, Budapest, and Prague complained that their concerns were ignored despite the presence of American government aid bureaus in these cities and numerous fact-finding missions from the West. Polish officials responsible for aid coordination were unable to obtain reliable information about how much U.S. assistance was being spent on particular projects, although the local USAID office was just a few blocks away. At about the same time the U.S. General Accounting Office (GAO) reported that in Hungary many assistance transactions, including those of the United States, occurred without the knowledge of the Hungarian government's assistance coordination unit.

Indeed, some consultants who came to the region stirred up resentment both among people without any direct experience with aid consultants and among officials with much direct experience. As Czech aid coordinator Pavel Rozsypal expressed in a letter to me dated August 2, 1994: "The salaries paid to foreign assistance contractors advising government ministries are widely known by Czech officials to be stratospheric in local economic terms--it is known, for example, that European Union PHARE advisers are paid six times more (and upwards) than the Ministers they are paid to assist. This of course causes a certain level of cynicism on the part of the local beneficiaries regarding just who is the intended beneficiary of foreign assistance; criticisms in this regard are widely circulated in Czech government offices."

Early on, Poles dubbed the consultants the "Marriott Brigade" because they tended to stay at Warsaw's pricey new five-star Marriott hotel. Polish aid coordination official Marek Kozak went so far as to suggest that the main benefit derived from the Marriott Brigade was not the expertise they provided, but the hard currency they contributed to the local economy. Perceptions of Western acquisitiveness and arrogance may have been exacerbated by the fact that major donors, notably the United States, the EU, and Great Britain, primarily have used for-profit accounting firms to carry out their agendas in priority areas such as privatization. Especially in the early stages of aid delivery, these consultants seemed more likely to cause resentment than the less conspicuous Western professors or city managers. The disillusionment was often mutual. Although few U.S. officials expressed frustration in public, they sometimes denigrated the recipients in private. When recipients perceived such attitudes, the cultural divide widened and led to the third phase of the relationship.

**Reality Check: 1993-94.** During trips to Poland, Hungary, and the Czech Republic in 1994, I followed up on previous interviews with aid coordination officials in those countries. I observed an evolution of knowledge, experience, and expertise. Officials are more skilled at working with the donor community and more realistic about what aid can and cannot do for them. In some cases they have concluded that the costs of working with a program in terms of timing and meeting donor requirements do not justify the benefits, and they have decided not to participate in the program.

A related development is the blurring of donor and recipient personnel. Whereas previously it was possible to detect "who is who" by nationality, language, and style, now consulting groups, including accounting firms, are hiring more local citizens and expatriates who speak Polish, Hungarian, Czech, and Slovak. Donors also have recruited some formerly high-level East European officials: The Polish-American Enterprise Fund hired a former deputy minister of privatization and a former undersecretary in the Ministry of Industry and Trade to be vice presidents. A Polish aid coordination official who two years earlier had criticized Western aid efforts now heads a new initiative for the EU.

Recipient officials now seem better at identifying their needs and more selective about foreign (and local) advisers. As Salvatore Pappalardo, an American consultant in Poland, observed: There were "a lot of carpetbaggers early on. . . . At this stage of the process Poles are more aware of the things they know and, most importantly, of the things they don't know. They've learned to clarify their needs."

One result is that the Czech government has decided to use a minimum of foreign assistance and has even refrained from relations with the World Bank. In a speech at the World Bank, Prime Minister Vaclav Klaus explained, "After three years of relatively successful fundamental systemic transformation of the Czech economy and society my experience tells me that the role of external factors in this process is relatively small. . . ." Zdenek Drabek, formerly chief aid coordinator of Czechoslovakia, further elaborated: "Many Czechs now proudly believe that Westerners have little to teach us. . . . The attitude has been essentially that we don't need the money." Poles and Hungarians have requested more capital assistance and less technical assistance. While the EU has moved toward more capital assistance, bilateral donors generally have not. (Indeed, the limited funds of the bilateral donors may not go very far in capital assistance projects.)

Although Poland, Hungary, and the Czech Republic appear to be adapting, it is by no means certain that this experience will be duplicated in countries whose aid experiences are just getting under way or being stepped up. In these countries, Phase 2--frustration and resentment--may last years longer and have even greater political and social repercussions. Or they may not develop adaptations favorable to the West.

### U.S. Assistance Agendas in Perspective

Since 1989, the "Group of Seven" industrialized democracies have committed nearly \$35 billion in aid to help Central and East European nations; some 42 percent of this is grant aid. All programs have emphasized, to a greater or lesser degree, the privatization and economic restructuring of state-owned enterprises and private-sector development. Although the programs have many similarities, individual donor nations differ in several areas and reflect the donors' different political and strategic agendas, levels of experience with Eastern Europe, and cultural strengths. The EU's PHARE program is the largest in size.

**Strategy and Duration of Advisors.** The Support for East European Democracy (SEED) Act, which has authorized U.S. aid to Eastern Europe since 1989, established some twenty-five priority areas and called upon the expertise of up to thirty-five federal agencies. This encouraged the compartmentalization of aid into many isolated areas. Moreover, while U.S. assistance was designed to be short term, a long-term commitment was called for if the United States was to have a real impact on the region.

With regard to consulting, East European officials often see "fly-in, fly-out" advisors as redundant, a burden, and sometimes even as engaging in industrial espionage. On the other hand, the dispatching of long-term resident advisers to work in the host country for several years on specific topics requested by the recipients--and mutually agreed on in advance--generally has been well received by recipients.

**Location of Decision-making.** The extent to which input from field representatives is integrated into critical decisions at donor headquarters may affect the allocation of resources and the coordination and integration of programs. Washington has been the center of assistance decision-making, creating many coordination, implementation, and political problems. Initially USAID field representatives had no signature authority in disbursing funds and served only as advisers to the U.S. ambassador of the recipient country and providers of information to the Washington home office of the USAID. Because USAID representatives in Eastern Europe generally had little authority, decision-making often was delayed and the flow of information impaired.

Washington-based management changed somewhat in early 1993 following congressional direction that authority be delegated to the field "in order to avoid planning and contracting in Washington for specific activities without the concurrence of the people in the field who have more intimate knowledge of the particular country." Although the number of USAID field representatives has since grown and they appear to have more input into approving and designing projects than in the past, they still are not charged with the authority of field "missions" established for Third World aid. An

evaluation of USAID privatization projects in Central and Eastern Europe commissioned by USAID independently concluded that: "The AID field office should have the ability to authorize funding of policy/program assistance, and/or at a minimum the flexibility to amend authorized funding. The lack of this local authority has, at times, held up host country-requested assistance, especially in Poland."

By contrast, the British and the German resident representative in Poland say they have significant input into aid decisions and veto authority. It may help that each program has only one official who handles aid in the recipient country. While this system makes decision-making more efficient, it can also lead to a loss of control and reduced accountability. In any event, it is an inefficient use of human resources to have many representatives in the field acquiring knowledge and experience and then to give them few decision-making responsibilities.

**Contracting Procedures.** Contracting procedures for hiring consultants greatly affect the delivery of assistance and recipients' responses to it. Reflecting its political and administrative constraints, USAID's contracting procedures make it difficult for recipients to select consultants, except from a very limited pool. However, the expertise provided by federal agencies under inter-agency agreements (e.g., the Treasury Department's Financial Sector Technical Assistance Program) provides more flexibility because the agencies are not subject to these contracting constraints.

The EU's PHARE program has a similar problem because PHARE requires geographical balance among its member states, which may work against hiring the consultants with the most expertise. On the other hand, under PHARE it is now possible to select consulting firms not only from the EU but also from Eastern Europe. Recipient officials say this offers an advantage over U.S. assistance. However, a host of Central and East European officials report that USAID acts faster than PHARE. Because of this, some recipient officials say they prefer USAID when time is an important consideration, but select PHARE when flexibility and input are vital.

By contrast, the British Know How Fund, although small in comparison to these donors, has had a more favorable reputation among many of the region's officials because of its flexibility and relative speed. With few strings attached, recipient officials could choose long-term advisers of their choice to be paid by the Fund. Zdenek Drabek, formerly chief aid coordinator of Czechoslovakia, said that the British Know How Fund had made decisions "very quickly" and "without much bureaucratic procedure."

**Recipient Input.** Two issues are involved here. The first is the recipient's ability to influence and guide the development of aid programs. The second is the extent to which the donors exchange information with recipient parties before and during the assistance. U.S. programs that come under USAID contracting mechanisms are seen by some officials in the region as less effective than EU programs because the U.S. programs allow recipients less leverage to set terms or select experts. However, in the case of expertise provided through inter-agency agreements, the predominance of evidence seems to indicate that, in many cases, recipients can have more input.

**Donor Relationships with Recipient Governments.** Under USAID, publicly financed private groups have unusual access to East European institutions. The United States in particular has exhibited strong support for "private" solutions; the target of assistance is almost exclusively the private sector, and private firms are also the primary delivery mechanisms. USAID works more with non-governmental organizations (NGOs) than do most other donors, and NGOs constitute a large part of the range of assistance providers.

The way some programs are structured implies that it is better to bypass government bureaucracies and work directly with the private sector. Although direct aid to the private sector makes sense when the goal is to promote private business, in some program areas (e.g., privatization and environmental improvement) this has led to a situation in which relevant governmental bodies can be virtually ignored. For example, the U.S. preference for bypassing governments almost entirely is counter-productive when the goal is to privatize state-owned enterprises.

The emphasis on the private sector has intentionally created a situation in which government-to-government links are weak. A 1992 Department of State letter to the GAO printed in a GAO report states, "We have also designed our programs to deliver assistance primarily to the private sector rather than to the government. Indeed, we have intentionally avoided government-to-government aid agreements, which contrasts with the EC PHARE program approach." This approach appears to have changed very little and was recently reiterated by the State Department Coordinator of U.S. Assistance to the New Independent States.

However, the fundamental drawback of this approach is, as GAO concluded in the same report, that the U.S. assistance program "has lacked coordination in working with the host governments." First, U.S. assistance is not set up for optimal access to recipient governments or to local contacts. Second, the weakness of government-to-government links has sometimes resulted in a lack of mechanisms to establish aid priorities and instruments. This has made it difficult for aid coordinators in the recipient countries to anticipate and coordinate aid projects. In this regard, the EU's PHARE program is better organized because it is administered through Program Management Units directed by recipients, who naturally have access to local contacts.

To further complicate aid relations, the United States has had difficulty working out bilateral assistance agreements with many countries in the region. First, many countries, including Poland, Hungary, the Czech Republic, and Slovakia, have refused the U.S. request for diplomatic immunity of its aid workers who do not have diplomatic standing. Officials in these countries indicated that no other donors had made such requests, and that, although such a request might be justified in Third World settings, it is not in Central and Eastern Europe.

**Donor Concentration on "Independent" and "Private" Sectors.** For U.S. assistance, privatization and private sector development have been stated priorities as well as the largest expenditure areas. As of March 31, 1994, more than three-quarters of the aid committed to Central and Eastern Europe was in the area of economic restructuring. By contrast, the EU's PHARE program has included such areas as public administration, in which there has been only a very limited amount of U.S. aid.

The privatization and restructuring of state-owned resources has been determined by donors to be the most critical need and the linchpin of the entire transitional process. The United States in particular has looked to privatization as a way to measure progress in the "transition" from a socialist to a market economy.

Yet other developments, such as the sale or liquidation of smaller state-owned enterprises at the local level and the considerable growth of private sectors, have tended to be the chief engines of restructuring in the region. In addition, the privatization of large companies has been much slower and more politically complex than anticipated. Because the socialist enterprise that provided jobs, housing, and medical and child care symbolized the workers' state, so the breakup of the enterprise has come to symbolize the transition. But it is difficult to give effective and neutral aid in a politicized arena. Privatization aid can be effective only if it is regarded by the recipients as impartial, professional, and able to accomplish something that local businesses cannot. In practice, these conditions are difficult to achieve. In a highly politicized arena with disincentives to quick privatization, convening state-owned enterprises can hardly be accelerated simply by bringing in outside consultants.

## Summing Up

In giving aid to Central and Eastern Europe, the United States presumably has in mind its strategic interest in helping the region to become more democratic, stable, and friendly to the United States. To achieve these goals, American policymakers should keep the following two things in mind: First, the United States might be well advised to have modest aims and make modest claims. Given the level of donor commitment, donors must recognize what limited aid can--and cannot--accomplish. Second, given that the donors' approaches to the region include political and social goals, donors should pay

particular attention to the political and social implications of aid, as well as to the economic ones. How will aid be received in Ukraine or Tajikistan, where the institutional crises and potential for chaos are even greater than in Central and Eastern Europe?

In giving aid, it is important to demonstrate that aid--which entails involvement in a recipient's domestic affairs--is being used to establish new democratic structures so that all can benefit. Aid activities can encourage the development of a more comprehensive market system or inadvertently promote opposition to it. Moreover, recipients' perceptions of assistance and experience with aid-paid consultants may help to form their opinions of donor nations.

If we have learned anything since 1989, it is that assistance should be more recipient-driven with informed and significant oversight from donors. The effectiveness of assistance depends on the active engagement of both donor and recipients, and in particular, the long-term commitment of those who transmit and receive aid.

#### For Further Reading

U.S. government documents detailing aid to Central and Eastern Europe include: USAID, U.S. Assistance for Central and East Europe: FY 90-94 Obligation Summary as of 31 March 1994, May 1994; Department of State, SEED Act Implementation Report: Fiscal Year 1994, January 1995; GAO, Eastern Europe: Status of U.S. Assistance, February 26, 1991; GAO, Poland and Hungary: Economic Transition and U.S. Assistance, May 1, 1992; House of Representatives (Foreign Operation, Export Financing, and Related Programs Appropriations Bill, 1993), report 102-585, June 18, 1992; and GAO, "Eastern Europe: AID's Indefinite Contracts Assist Privatization Efforts But Lack Adequate Oversight," January 1994.

Private assessments of U.S. aid include Raymond Barre, William H. Luers, Anthony Solomon, and Krzysztof J. Ners, *Moving Beyond Assistance* (New York: Institute for East-West Studies, 1992); and "Final Report; Privatization Phase II Program Evaluation" (submitted to USAID, Washington, DC, by Development Economics Group/Louis Berger International, Inc., and Checchi and Company Consulting, Inc., July 30, 1993).

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