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Promoting Sustainable Market Institutions in the Transition Economies: the Role of International Assistance

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the lessons learned."

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PROMOTING SUSTAINABLE MARKET INSTITUTIONS IN THE TRANSITION ECONOMIES: THE ROLE OF INTERNATIONAL ASSISTANCE

Nancy J. Cochrane[1]

ABSTRACT

This paper examines the role of international technical assistance in building the institutions critical to the success of market reform in the Transition Economies. While there have been many successful grass roots projects aimed at helping individual firms or associations compete in the market, projects aimed at institution building (credit markets, market information, agricultural extension, food safety and animal health regulations, etc.) are not always so successful. These projects succeed only when the recipient Government truly buys into the project and is willing to commit its own resources. These services tend to be public goods, so attempts on the part of donors to bypass Government institutions and privatize these activities are usually not sustainable.

Keywords: Institution building, technical assistance, market information, Armenia, Serbia, Montenegro, Bosnia and Hercegovina

I INTRODUCTION

Sixteen years after the beginning of the transition, a consensus has emerged that while price and trade liberalization may be necessary for successful agrarian reform, they aren't sufficient. Nearly all the countries of Eastern Europe and the Former Soviet Union liberalized trade and eliminated price controls, and many have made significant progress in land and enterprise privatization. But not all can be considered successful reformers. The more successful countries not only liberalized prices and trade, but also built the institutions critical to productivity growth—land markets, rural credit, market infrastructure, agricultural extension, and regulations governing food safety, plant and animal health standards. Institutional reform outside agriculture is also critical—reform of the judiciary to ensure contract enforcement, banking reform, and growth of non-agricultural employment.

In recognition of this need, international donors have implemented some wide-ranging technical assistance programs aimed at addressing these institutional needs. The primary players in the agricultural sector were USAID, USDA, the European Union (EU), the World Bank, the United Nations Food and Agricultural Organization (FAO), and a number of bilateral programs sponsored by individual EU countries, as well as Japan. Many projects addressed the issue of rural credit; others were aimed at agricultural extension, market information systems, development of grades and standards, construction of wholesale markets, assistance to plant health and veterinary services, and the capacity to carry out agricultural policy analysis.

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[1] The author is an economist with the U.S. Department of Agriculture. The discussion in this paper is mainly drawn from the author's experiences implementing technical assistance programs in Eastern Europe. Any opinions, findings, or recommendations expressed in this paper are those of the author and do not reflect the view of the U.S. Department of Agriculture.

But success has been mixed, and many of the transition countries still have weak and underdeveloped market institutions. The strongest institutions can be found in the eight countries that joined the European Union (EU) in 2004. But the New Member States (NMS) were strongly influenced by the accession process—the EU required them to develop the administrative capacity to implement the *acqui* and provided considerable technical and financial assistance to that end. Outside the NMS, success stories are harder to find. There have been many successful grass roots efforts to help producers invest in modern technology, organize producers associations, or provide financing to small processing plants. But efforts to build the institutions to support those new entrepreneurs often meet with less success. The landscape is littered with failed projects--market information systems that withered away, seriously underfunded extension systems, livestock auction houses that stand empty. Would-be exporters are thwarted by the lack of a nationally recognized system of grades and standards and lack of credible veterinary or food safety inspections.

This paper will present examples of successful and unsuccessful attempts to build market institutions in the transition economies and attempt to draw out some lessons from those examples. The examples will be chosen from the subset of transition economies where the agricultural sector is dominated by small private farms. Some such as the former Yugoslav republics were always dominated by private farms. Others such as Armenia, Azerbaijan, Georgia, and Kirghizstan were previously dominated by large socialized farms but privatized nearly all their land very early in the transition period. Small farmers in these countries have typically been ill equipped to adapt to the market. They lack access to capital or inputs, they don't have any information about what is demanded by the market, and these face serious obstacles as they try to reach those markets.

2 THE PROBLEM: SMALL PRODUCERS ISOLATED FROM THE MARKET

At the beginning of the transition, many countries saw the sudden emergence of a large number of small private farmers who had never previously been in business for themselves. In the former Soviet Union many of the new farmers were former state and collective farm workers. They had typically been very specialized—they were tractor drivers, veterinarians, etc. They were unprepared to manage an entire farm business. Others had never engaged in farming but lost their jobs in industry, acquired a piece of land and began subsistence farming. Private farmers in Poland and the former Yugoslavia had longer experience managing their own farms, but they had grown accustomed to guaranteed prices and guaranteed markets. They were unprepared to deal with the risks of volatile market prices or take responsibility for their own production and marketing decisions

What resulted was a large subsistence agriculture sector. Very little domestic production reached the markets, and urban markets tended to be flooded with imported food. Even though farmers were receiving prices well below world market levels, they could not compete with imports. A number of critical market institutions that would enable farmers to sell more of their production were missing. For example:

- Lack of credit: Farmers who would have liked to expand their operations or make investments to raise productivity or product quality were unable to find the capital.

Interest rates were prohibitive and banks regarded agriculture as too risky to lend to. Farmers were often further stymied because they lacked clear title to their land and could not offer it as collateral.

- Lack of clear property rights and functioning land markets: Many farmers lacked clear title to their land, governments often imposed restrictions on land sales, and credit was difficult to obtain. All these issues slowed down the rate of farm consolidation.
- Inadequate market infrastructure—small producers lacked access to wholesale markets, cold storage, or efficient transportation; these deficiencies raised the transactions costs for farmers seeking to market their output, ultimately forcing them to accept lower prices.
- Lack of market information: timely and accurate market information helps producers make better production and marketing decisions. Lack of information leads to large regional price disparities and leaves farmers at the mercy of oligopolistic buyers who have better information.
- Lack of nationally recognized food quality and safety standards: lack of such standards makes it difficult to compare prices between different markets
- Lack of contract enforcement

3 TECHNICAL ASSISTANCE AIMS TO ADDRESS INSTITUTIONAL SHORTCOMINGS

Technical assistance from western institutions aimed to address all these institutional needs. The primary players in the agricultural sector were USAID, USDA, the European Union (EU), the World Bank, the United Nations Food and Agricultural Organization (FAO), and a number of bilateral programs sponsored by individual EU countries, as well as Japan. Many addressed the issue of rural credit, others were aimed at developing land cadastres and facilitating the development of land markets, others were aimed at building wholesale markets, systems of grades and standards, commodity exchanges, and trade capacity building. Another goal of technical assistance was to promote agribusiness investment and help countries put policies in place to attract investment. Still other projects aimed to improve the flow of market information.

In general assistance falls into two categories: what could be called grass roots efforts aimed at individual farmers, entrepreneurs or associations, and institution building projects aimed at helping national governments build the institutions critical to a functioning market economy. Grass roots projects are focused at the community or province level; they aim to help individual farmers or groups of farmers raise their productivity and improve the marketability of their products. Their goal is generally not to influence policy making at the national level. These projects might help finance the start-up costs of a small processing firm or the purchase of a cooling tank for a dairy farmer, facilitate the organization of a producers association or cooperative, provide training to farmers and other agribusiness entrepreneurs, or provide seed funds for local credit clubs. Typical institution building projects aim at reforming the banking system, creating a land cadastre, strengthening agencies regulating food safety and animal or plant health, organizing agricultural extension and market information systems.

3.1 Grass roots projects are often successful...

The grass roots projects have achieved some notable successes throughout the transition economies. The LAMP (Linking Agriculture to Producers) project in Bosnia and Hercegovina

(funded by USAID), for example, provided a grant to a mushroom producer, allowing the owners to expand their premises, install drying equipment, and ultimately increase their sales by over 50 percent.[2] LAMP has also provided training to dairy farmers in technologies to improve the safety and quality of their milk and more cost effective techniques for cutting and baling hay. Similarly, USDA programs in Armenia have helped Armenian farmers organize producer associations and cooperatives, helped equip small dairy plants with modern cooling equipment, provided seed capital to organize credit clubs in local communities, provided workshops in product quality, packaging and branding, and organized export promotion campaigns for Armenian products (Cocks, Gow, and Dunn, 2003; Aines and Gosser, 2004.)

There have been many similar projects in the other transition economies, funded by EU projects as well as U.S. Many of these endeavors have shown positive results in that a significant number of farmers and agribusiness entrepreneurs have established successful enterprises, which have managed to thrive and grow even after the termination of foreign assistance.

3.2 But institution building is more problematic

But the enterprises benefitting from such grass roots assistance often find themselves stymied by the lack of supporting government institutions. In Armenia, for example:

- For all the assistance given to Armenia's dairy industry, it remains impossible to buy fresh milk in Yerevan, because many of the small farms still lack the means to invest adequate cooling facilities and transport.
- There are still no nationally recognized quality and safety standards. One small dairy farmer in Armenia, who had benefited from USDA support, was selling his yogurt to some Yerevan supermarkets, but when asked about quality standards, he shrugged and said there were none, but his buyers knew he supplied a high quality product.
- There are many well known varieties of Armenian cheese. But the World Bank (World Bank, 2005) notes a general lack of harmonized quality standards for different types of cheese.
- Some of the credit clubs organized by USDA have failed because of a high number of non-performing loans and the lack of an effective mechanism on the part of the Government for enforcing repayment.

Most Albanians believe that they produce some high quality beef. However, virtually all the meat sold in urban markets is processed from imported live animals or carcasses, since Albania's processing plants import their raw material rather than buy from domestic producers. Domestic livestock producers either produce only for home consumption or sell their live animals in the local peasant markets. The dairy industry is the only sector that buys all its raw product from domestic producers. But even there, only 20 percent of the milk produced in Albania is processed. The remainder is sold directly by farmers along the roads.

What is missing in many of the transition economies are the fundamental institutions that support a functioning market economy. In many of the countries land markets are still not fully functioning—even though the land is nearly 100 percent privately owned, land sales are hampered by lack of credit, lack of papers proving ownership, and restriction on sales that, for

[2] See http://www.usaid.gov/locations/europe_eurasia/countries/ba/index.html for more detailed description of LAMP projects.

example, give neighbors first right of refusal. Market information is lacking or inadequate, so producers who want to enter the market find it difficult to find out what the market is demanding. A lack of nationally recognized grades and standards thwart many would-be exporters and even hinder domestic sales—supermarkets entering the countries will often import the goods they sell because that is the lowest cost way to ensure consistent quality. Agricultural extension, or advisory services are absent in many countries, and where they exist, they tend to be underfunded and overly focused on technology to boost output rather than marketing advice.

Enforcement of contracts is inadequate in most countries. Without third-party contract enforcement, business relationships are generally restricted to a closed group of acquaintances—often family and long time personal friends--with whom they expect repeat business in the future. In these cases, even without a developed court system, the threat of losing future business is enough to ensure a contract will be carried out. Non-acquaintances have no such threat, and appealing to the court system can be a long and costly process. This can lead to allocative inefficiencies. There could be lower cost suppliers or buyers offering better prices, but their trustworthiness is unknown, and farmers and processors prefer to deal with people they know.

International donor organizations are fully aware of such shortcomings, and many projects have been implemented to address these. But success has been uneven. Success stories include a wide range of institution building projects implemented in Poland, Hungary Czech Republic, and Slovakia during the 1990s. There were a number of successes in Bulgaria—market information, economic analysis, agricultural statistics, warehouse receipts to name a few. There were also a number of failures—market information systems created during the 1990s in Romania and Russia, which subsequently disappeared, policy analysis units attached to ministries, which withered away with the end of donor support.

More common, perhaps, are the indeterminate outcomes—extension systems in Romania and Bulgaria, which proved to be sustainable, but not very effective, or market information systems in Albania, Macedonia, and Armenia, which, while sustainable, suffer from a lack of quality control, inadequate dissemination, and methodological problems. Warehouse receipt systems have been put in place in many of the transition economies. Many are considered successes in that the necessary legislation was passed, a grain grading system was developed, inspectors were trained, and warehouses were licensed. However, without a number of supporting institutions, the systems do not serve their intended purpose. If contract enforcement is weak, producers and banks who might accept the receipts as collateral have no guarantee that the grain they withdraw will have the same specifications that are listed on the receipt. If there is no reliable market information, banks won’t know how to value the receipts, and producers will be unable to make informed decisions about when and how much to store or when to withdraw from storage. If the warehouses are controlled by a small number of oligopolistic companies, storage fees might be too high for small producers to be able to benefit. These have been problems in Ukraine, Kazakhstan, Romania, and other countries.

These services to varying extent are public goods, and some level of involvement and financing by the transition governments is critical to the sustainability of these assistance projects. But donors have frequently found it difficult to convince host governments to put their own resources

into projects to strengthen these institutions. National budgets are always tight, and there are many competing demands on those limited resources. Many transition governments don't see the value of such things as market information or agricultural extension—some have very close ties with large agribusiness and are unsympathetic to the needs of small farmers. The transition economies have also been subject to frequent changes in government, so even when a donor finds a group of officials willing to put resources into the project, those officials could be replaced after a new election by a new group of officials with other priorities. Another problem is that government salaries tend to be very low, and experts trained under foreign assistance programs often depart for private sector jobs.

4 THE URGE TO PRIVATIZE—THE CASE OF MARKET INFORMATION

As a result, some international donors decide that it is better to avoid working with the Government and work instead with private sector organizations. This sentiment has led some donors to focus their efforts on grass roots projects. Other donors have chosen to set up a private firm or NGO to deliver services such as market information, agricultural extension, or policy analysis. These entities may be very successful at delivering the services, but the question is how they can be sustained once donor support ends.

A decade of attempts to build market information systems illustrates the pitfalls of this approach. The goal of a market information system (MIS) is the collection, compilation, and dissemination of agricultural prices from different markets around the country. If the information is accurate, timely, and broadly disseminated, it can be an important tool for farmers as they make their production and marketing decisions. But it is also expensive to collect such information--it is necessary to collect a large volume of data through surveys of producers, from spot transactions, and from commodity exchanges, in order to ensure that a market information system contains truly representative prices from all participants in the market.

4.1 Many governments are reluctant to make the necessary investment…

The result has often been an under-funded system that doesn't meet the needs of its users. A case in point is Armenia. Armenia's MIS is the responsibility of a network Agricultural Support Centers (ASC). These were founded by the Ministry of Agriculture, with substantial support from USDA, and their basic mission is farmer training and technology transfer. But the Ministry spun them off into independent, joint stock companies. They now receive some support from the World Bank. There are 10 marz support centers and a Republic Agricultural Support Center in Yerevan. However, the marz centers are not subordinated to the Republic center. There is a Department of Research, Education and Extension in the Ministry of Agriculture that supervises the activities of all 11 centers.

Collecting prices is coordinated for each marz by the marz ASC. This is carried out once every ten days. Each marz has within it a certain number of regions, and their agents in each region collect prices from the major markets in their regions. They send those prices to the marz center, and one staff member there computes simple averages of all the prices and sends those average marz prices to the Republic Center. But:

- Dissemination is weak. The only form of dissemination is a newspaper published by the Republic ASC. This newspaper is published three times a month, and 4500 copies are printed. The subscription fee isn't large—around $6 a year—but it does restrict the availability of the information. Moreover, price reports in these newspapers are not comprehensive; they report only a selection of the prices that are collected.

- There is no system for electronic transmittal of information. The extension agents in the regions use the telephone to report their prices to the marz center, and the marz center sends the information to Yerevan by fax. Both the Ministry of Agriculture and the Republic ASC have websites, but the price information isn't available on either site.

- Wholesale prices are not collected. But in fact, there are no true wholesale markets in Armenia. Instead, the same market functions as a wholesale market early in the morning when farmers bring their products and sell them to traders and then becomes a retail market in the afternoon when the traders sell to the general public. The "wholesale" prices are closer to what the farmers actually receive and would be more useful to them. But, what is reported are the retail prices received by the traders.

- Funding shortfalls. The ASCs do not receive any funds to support price collection, and other funds are increasingly scarce. Without additional funds, the centers will be reluctant to increase the frequency of price collection or devote resources to quality control. But the centers are losing funds and have already laid off staff. The World Bank program currently requires the marz centers to raise 10 percent of their funds from local financing, and this share is to rise to 30 percent. The idea is that the centers should charge farmers for certain services. But the staff working in the centers have serious doubts that farmers would be willing to pay.

It would have been possible to improve the MIS in Armenia without a large amount of new funding from the Government. However, the Ministry of Agriculture has been unwilling to devote even small amounts of funding to this effort. Instead, officials seemed to be hoping that foreign donors would return with additional funds.

4.2 …spurring efforts to privatize

Because many transition Governments are reluctant to devote the necessary resources to MIS, donors in other countries decided to privatize the effort: either working with an existing commercial firm to do the work or creating a new entity from scratch. In either case, the donor institution would pay the expenses for a fixed amount of time (perhaps the first year); after that start-up period, the agency set up to collect the market information was expected to cover its own costs through government financing, subscription fees, or a combination.

There are some successful examples of partially privatized systems. One is the Bulgarian MIS (known as SAPI in Bulgarian). It has been collecting and disseminating market information for over ten years with no foreign support. But it continues because the Bulgarian Government provides about 40 percent of its funding—it earns the rest through specialized marketing studies and consulting services. In Estonia, responsibility for collecting and analyzing market prices lies with the Estonian Institute for Economic Research, a privatized institute. However, this activity

is done under a contact with the Ministry of Agriculture and is thus publicly funded. The Hungarian institute responsible for market information is partially privatized, but again this part of its activity is funded by the government.

These examples succeed because they remain partially funded by the Governments. Efforts to create a fully privatized market information system have not been successful. In 1996, the EU PHARE Program initiated a project in market information, designed as a public-private partnership between the Ministry of Agriculture and a commercial company called New System—selected through a tender. While the system was functioning, they collected prices from all the counties three times a week. The EU provided computers and installed a special network for data transmission. Prices were collected from all the so-called peasant markets and the weekly "fairs" held in the counties. In turn electronic bulletin boards were installed in the markets and at the town halls displaying prices in the local markets and those in other localities.

The PHARE project ended in March 1997. The program continued for a year and a half after that but then stopped. The fundamental problem was the cost. The data transmission network was extremely expensive to operate. The Ministry declined to allocate any funds to the program. For a time New System attempted to operate the system without Ministry support. New System published the price information in a magazine called *Agrinet*. Initially, these were distributed free of charge, but after 6 months, New System began to charge subscription fees, targeting mainly food processors. But the food processors were not interested in paying for the information, and the whole project eventually folded. The company New System still exists, but it offers various IT services rather than collect market information.

A more indeterminate outcome occurred in Moldova. CAMIB (Central Agricultural Market Information Bureau) in Moldova was established in 1996 by an EU TACIS project. It was converted to an NGO in 1999 as part of a sustainability plan—it was to cover its own costs through sales of products and services. Its mission was three-fold: market research and information, business promotion, and consulting. CAMIB still exists and still collects market information—for now the information can be found at no charge on the website of a Dutch project, known as Alliance for Support to Agricultural Markets, but information on the CAMIB website is available only to subscribers. In the meantime, CAMIB is taking on new foreign projects which stray farther and farther afield from its original MIS mission—the latest is a USAID food safety project.

A similar situation exists in Ukraine. An early USDA-financed program that attempted to work with Government institutions failed because of a lack of commitment from the Ukrainian Government. In 2003, Land O' Lakes, with USAID funding, initiated a new MIS project, with a private firm—APK Inform—as the implementing agency. As of now, one can find very detailed price information and informative commentary on the LOL website. But when U.S. funding ends, APK Inform is expected to begin charging users for the information.

For now, market information systems in Moldova and Ukraine are thriving because the agencies are still receiving large amounts of foreign assistance. But prospects for the sustainability of a 100 percent privately financed MIS are not good. The costs of collecting information are very high, and a private firm needs to charge very high subscription fees in order to cover those costs.

In many cases, particularly in less wealthy economies, potential users are unwilling or unable to pay such high fees.

Market information is viewed by many as a public good. The two basic characteristics of a public good are:

- Indivisibility. Each member of society gains satisfaction from the total output of the good, and use of the good by others does not diminish the satisfaction gained by any individual.
- Difficulty of excluding nonpayers. There are strong incentives for so-called "free riders," and the high cost of preventing free riders inhibits private production of the good.

Information clearly meets the first criterion for a public good. The second may be less clear cut. There are private information sources that charge subscription fees and successfully exclude nonpayers. But they tend to provide very specialized information and their customers are the more advanced, commercially oriented farmers. For basic market information, once the large fixed cost of collecting the information is covered, the marginal cost of disseminating the information over the internet is virtually zero. Therefore, the collection of price information exhibits classic characteristics of a natural monopoly. Private companies who collect information for a fee will likely collect and distribute less than the socially optimal amount of information. A government-sponsored agency that collects data and distributes it for free can bring the amount of market information available closer to the socially optimal one.

4.3 Technical assistance succeeds in Serbia and Montenegro.

In contrast USDA efforts to build market information systems in Serbia and Montenegro have been largely successful. After three years of work in Serbia and just two in Montenegro, As a result of these efforts weekly reports of fruit, vegetable, and live animal prices can now be found on the Ministry of Agriculture websites of both Serbia (www.stips.minpolj.sr.gov.yu) and Montenegro (www.amis.cg). Serbia also reports prices of grains and oilseeds. These reports list prices from multiple markets in the respective countries both wholesale and retail. They report prices from the neighboring countries, where available, as well as the EU, and they present a brief commentary describing the supply and demand factors that are affecting prices. In both countries, these projects have proved sustainable, in that the Serbian and Montenegrin Ministries are fully financing the systems. Media coverage is slowly expanding, and farmers are becoming more aware of the program. There is already evidence that some farmers are changing their behavior in response to improved access to information.

5 WHAT EXPLAINS THE DIFFERENCE?

Serbia and Montenegro are also fairly poor countries, also with many competing demands on the State budgets. But officials in both countries recognized the value to the program and were willing to commit their own funds and staff to the project. These two governments are also seriously committed to strengthening their extension systems and overhauling their regulatory systems for food safety and plant and animal health. Their experience shows that a small national budget need not be a barrier to serious institutional reform. Serbia continues to move forward in these areas despite a considerable amount of political instability.

5.1 The lure of the EU

Both Serbia and Montenegro aspire to eventual EU membership; neither has official candidate status, but both are making concrete progress towards that goal. As EU members, the countries will be required to implement stringent food safety and animal health regulations, and they will also have to report comprehensive market information to Brussels. The accession process has also been an important factor behind the relatively advance state of reforms in the 10 East European countries that have already joined the EU. Armenia and most of the rest of the Former Soviet Republics are unlikely to become serious candidates for EU accession.

But the EU isn't the whole story: there are other lessons to be learned. The USDA experience in Serbia and Montenegro has reinforced the validity of the lessons learned during our work in Bulgaria and Poland during the 1990s, described in some detail in Cochrane and Osborne (2004) and summarized below.

5.2 Flexibility and collaborative design of projects

The process of technical assistance needs to be flexible enough to allow programs to evolve to fit the conditions in each country. While many of the basic methodological tools being transferred are standard, countries develop their own mix of commodities, style of reporting, methods of dissemination and use of information. Counterparts will develop their own ways of working together, based on the structure of their institutions and their cultural traditions. This process can proceed efficiently when the approaches are locally generated. Governments will be more likely to buy into the projects if they have a role in designing the programs. If the program truly meets to most urgent needs of the recipient country, local institutions will be more willing to devote their own resources to it. This means listening to counterparts and understanding their priorities.

5.3 Flexibility also means patience

Many international assistance projects are designed to last just one or two years. USDA's experience has demonstrated that it often takes much longer to leave a sustainable program in place. Successful USDA programs in Poland and Bulgaria during the 1990s also took five to seven years to establish. USDA has been working in Serbia since 2002, and it took nearly two years of discussions with various officials before the training could really get started. But those extended discussions allowed time for Serbian officials to decide exactly what they wanted the program to look like, and in the end, they were more ready to take ownership.

5.4 Start small

We began with only a small number of commodities—fruit and vegetables to start—expanding only gradually to cover live animals, slaughterhouses, and finally grains and oilseeds. The list of commodities expanded only as the counterparts developed the capacity to absorb the additional work.

5.5 Leadership matters

Our programs succeeded when we were able to find a small group of strong, committed counterparts who can mobilize their colleagues to work on the projects without any immediate or guaranteed reward for it. Initial efforts to establish a market information system in Serbia floundered because the Government in power had no interest in the project. But the new Government that took power in 2004 immediately understood the value of the project and committed its own funds to pay 18 extension stations to collect the information. It was thanks to

the determination of a handful of officials at the Ministry of Agriculture that the project has been successful. In Montenegro, Ministry officials saw the success in Serbia and approached USDA to ask for similar assistance. The Montenegrins too have committed their own resources to the project.

5.6 The salary issue

While USDA consistently refused to cover the salaries of counterparts working on our projects, many other donors have directly hired the local staff working on the projects. The typical argument is that low salaries paid by public institutions in the recipient countries make it impossible to attract and retain qualified workers. This was the approach typically taken by the EU when setting up policy analysis units at the agricultural ministries. The EU implementers determined for the ministries did not have enough qualified staff. So they hired a group of economists from local universities and research institutes and trained them to do policy analysis. The theory was that after three years or so, the ministry would see how valuable these units were and would take them over paying the analysts' salaries out of their own budgets.

The problem was that the ministries are unable to pay the relatively high salaries that the foreign donor had been paying. Once the foreign assistance ended, most of the trained analysts departed for the private sector. The policy analysis unit in Romania no longer exists, and the analysts trained under that project are now migrating from one foreign project to another. Likewise the analysts hired for the Bulgarian policy analysis unit returned to their institutes and began supplementing their pay through consulting contracts, mainly with foreign organizations.

The danger is that when a program is fully funded in this way by a foreign project, it is easy for the program to be too ambitious, growing far beyond the scope that can be easily sustained by the recipient government. The USDA programs in Serbia and Montenegro avoided this pitfall by training staff already employed by the Ministry and the regional extension centers and expanding commodity coverage and report frequency only as counterparts were able to absorb the extra burden.

6 REMAINING CHALLENGES

The situations in Serbia and Montenegro are not perfect. The future of the MIS programs is clouded by continuing shortages of funds and political instability. The Extension Service in Serbia, which is responsible for price collection, has other duties and is short of funds. The Ministry, which oversees the system, is also understaffed and unable to exercise the quality control that would be optimal.

One of the biggest challenges is reaching the very smallest farmers. Market information in both Serbia and Montenegro is available on the internet, allowing for timelier and lower cost dissemination. Throughout the region, more and more users within the governments and the agribusiness community now have access to the internet. But internet access in rural areas lags considerably behind that in urban area, and only a small number of farmers have access. Many farmers still rely heavily on the media. Furthermore, even when farmers do have access to the information, they often need help interpreting it and using it to make their production and marketing decisions.

There is an obvious role for extension services in disseminating information and helping farmers make use of it. But of all the transition economies, only Poland and the former Yugoslav republic have well-developed extension systems, and these countries had an extension system during the Communist period. Efforts to create extension systems from scratch in the other transition economies have faltered. It is extremely expensive to organize and maintain an extension system, and local governments have found it difficult to provide enough funds to sustain the system after the end of western assistance. Even in Poland, where the extension centers continue to play a pivotal role in disseminating information to farmers, the number and staffing levels of these centers have declined since the end of USDA assistance. The Serbian extension system is uneven in quality—some stations are excellent, and others barely function--and under increasing pressure to privatize.

There are broader issues to address as well. Capacity building projects such as MIS, agricultural extension, or policy analysis can be challenging in an environment of tight budgets and political instability. But reforming the judiciary and ensuring prompt enforcement of contracts and property rights are even bigger challenges that cannot be addressed by agricultural experts alone, and these problems must be solved if institutions like MIS or extension are to have their optimal impact on markets. The New Member States of the EU have made substantial progress in overcoming these deficiencies, but only under immense pressure from the EU and the promise of eventual membership. It is an open question how long it will take to achieve progress in transition economies not in line to join the EU. And in countries, such as many in the Former Soviet Union, where Governments have proved unwilling to provide basic public goods, it is not clear just what Western assistance can do to help build the institutions that are so critical to successful market reform.

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