Since the collapse of communism, the countries of Central and Eastern Europe have faced a challenge to transform their economies into market-oriented capitalist systems. This book, a collection of 21 papers, illustrates the progress of financial-system reforms in former centrally-planned economies. The process of building virtually nonexistent market mechanisms and financial institutions provides researchers with a unique opportunity to study and test the theories of modern economics and finance. The book aims to appeal to policymakers interested in the evolution and operation of financial institutions in transitional economies, and to researchers interested in the economics of transition.

The book starts with country profiles. The description of the transition process in 11 countries centers around five common themes: the role of monetary policy in macroeconomic stabilization, the characteristics of the banking systems, the transfer of corporate ownership through privatization, the emergence of capital markets and securities exchanges, and the sources of foreign investments and financial assistance.

The second part of the book presents 10 papers on selected topics: (1) the role of central-bank independence for seigniorage, (2) collusive trade credit and stabilization policies, (3) banks in the Czech Republic, (4) promotional banks, (5) a comparative study of privatization in Poland, the Czech Republic, and Hungary, (6) electronic securities-exchange “RM-System” in Slovakia, (7) managing financial risks, (8) the efficiency of Central European equity markets, (9) modeling stock returns, and (10) foreign debt settlements in Bulgaria, Hungary, and Poland 1989–1996.

Most of the papers included in the book were presented at the conference “Capital Markets in Emerging Economies – Central and Eastern Europe”, held in Vienna, Austria in February 1997.

I was delighted to see a book dealing with the complexity of issues faced by “transition economies”. The country profiles are very informative about the development of financial markets. Since the initial economic conditions of the countries of Central and Eastern Europe differed, the paths taken to create a
completely new set of institutions and mechanisms varied. Although the title “Capital Markets” suggests a somewhat focused theme, the contents deal with a much broader set of topics on financial systems. Substantial parts of the country profiles, as well as papers on selected topics, are devoted to monetary policies, banking, and international trade. I recommend the book to academics interested in the areas of financial-system design and regulation, international economics and finance, bank regulation and monetary economics, and most importantly, privatization and corporate governance.

Each country profile starts with a description of monetary-policy issues. The description of the development of central banking, its legal framework, and the choice of monetary tools and policies provides researchers with additional insights about the debate on the relationship between central-bank independence and inflation. The profiles present extensive accounts of the banking sectors, which still play dominant roles in the economies of Central Europe.

Although the profiles share five common themes and provide a wealth of data, the treatments vary substantially across countries, which often makes it hard to find comparable information. In general, a short article providing a unified overview of the countries of Central/Eastern Europe is missing. Although comparative tables with easy to read figures on GNP growth, inflation, FDIs, and international trade are provided at the end of the book, they are not discussed in the text. Moreover, no such comparative tables are provided about the capital-markets topics – the main subject and title of the publication. In addition, the papers only briefly (if at all) discuss such important components of capital markets as investment funds, investment banks, and security dealers. The questions about viability and extent of alternative corporate-financing choices to bank loans are left unanswered. Do we see any IPOs there? What is the status of the legal environment and law enforcement?

Several minor points may distract a reader. The figures are at times unusual (e.g., the term structure of interest rates depicted in the form of a pie chart, p. 56). Also, the values in tables sometimes are inconsistent (e.g., the mean of weekly returns a negative number while the mean of monthly returns a positive number, p. 405), questioning the quality or preparation of the data or both. Local currencies are used often without any USD equivalent or even a relative measure (e.g., to GDP), which makes interpretations difficult.

An excellent set of papers detailing financial-system developments in Central Europe has recently appeared in the Journal of Banking and Finance. Scholtens (2000), and Hermes and Lensink (2000) give a superb account on the topic and also review the literature on financial-system architecture and regulation. An incorporation of a similar article in this book would have substantially enhanced its quality. Some conclusions of the book such as: “... Central and East European equity markets are similar to the equity markets of far more developed countries” (p. 4), seem to be overstating reality as they contradict findings of Scholtens (2000). Moreover, although the book aims to appeal to policymakers,
no advice or even a discussion is given about the relative success or failure of individual countries’ policies. A discussion along the lines of the reform proposals suggested by Blanchard et al. (1991) would have been helpful. The book stresses at the outset (p. 1) the uniqueness of the transformation process and unavailability of textbook solutions. However, many problems faced by “transition economies” are in fact shared by other developing countries such as Mexico or Chile. Indeed, this point is clearly indicated by the authoritative “International Economics” textbook by Krugman and Obstfield (2000).

The main strength of the book lies in its description of the countries’ institutional structure development, bank regulation, and privatization issues. In addition to privatization overviews in the first part of the book, readers can find an excellent primer on privatization in the selected-topics section of the book. There, Lina Takla highlights a variety of approaches to privatization in Poland, the Czech Republic, and Hungary and offers an extensive discussion of the main issues involved in privatization, examining its preconditions, outcomes and aims. The paper also surveys the theoretical and policy debates surrounding the drafting and subsequent implementation of privatization programs. Readers may also find details on securities-exchange developments and trading. One paper features “RM-System in Slovakia”, which is an electronic securities-exchange system based on a public limit-order book. The book also contains an interesting piece discussing the experience of three countries with the management of foreign debt and debt-service reduction.

Overall, the book provides a valuable description of the financial-system development and often turbulent environment of the countries of Central and Eastern Europe. The text will be certainly appreciated by researchers interested in background information on the institutional structure of transition economies.

References


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