

ESTONIA



Polity: Parliamentary democracy

Economy: Mixed capitalist

Population: 1,400,000

GNP per capita at PPP \$ (1999): 7,826

Capital: Tallin

Ethnic Groups: Estonian (65.1 percent), Russian (28.1 percent), Ukrainian (3 percent), other (4 percent)

Size of private sector as % of GDP (mid-2000): 75

NATIONS IN TRANSIT SCORES

	1997	1998	1999-2000	2001
Democratization	2.10	↑ 2.05	↓ 2.06	↑ 2.00
Rule of Law	na	na	2.63	↑↑ 2.38
Economic Liberalization	2.13	↑ 2.00	↑ 1.92	1.92

KEY ANNUAL INDICATORS

	1994	1995	1996	1997	1998	1999	2000
GDP per capita (\$)	1,530.0	2,405.0	2,982.0	3,187.0	3,607.0	3,563.0	3,409.0
Real GDP growth (% change)	-2.0	4.3	3.9	10.6	4.7	-1.1	6.4
Inflation rate	47.7	29.0	23.1	11.2	8.2	3.3	4.0
Exports (\$ millions)	1,226.0	1,697.0	1,813.0	2,294.0	2,690.0	2,452.0	3,289.0
Imports (\$ millions)	1,583.0	2,363.0	2,832.0	3,419.0	3,805.0	3,329.0	4,077.0
Foreign Direct Investment (\$ millions)	212.0	199.0	111.0	130.0	574.0	222.0	241.0
Unemployment rate	7.6	9.8	10.0	9.7	9.9	12.3	13.7
Life Expectancy (years)	67.0	67.8	69.8	70.1	68.8	70.6	70.0

INTRODUCTION

Since the reestablishment of its independence in 1991, Estonia has implemented some of the most extensive political and economic reforms among the former Soviet states. Estonia's successful progress toward a democratic system of government and a market economy owes much to the stability of the country's political institutions and to the presence of a broad consensus among successive governments throughout the last decade. Most of Estonia's government and business leaders have supported the ongoing drive to European Union (EU) membership as a means of achieving political and economic reintegration into Western Europe. They also have advocated entry into NATO as a possible guarantor of national security. Estonia has enjoyed free and fair national and local elections, and it respects basic civil liberties, including freedom of the press, religion, and the judiciary. While corruption remains a less serious problem than in most other countries in the region, Estonia's government continues to work with the nonprofit sector to publicize and enact anticorruption initiatives. The status of the large noncitizen, mostly ethnic Russian, population remains a source of tension between Estonia and Russia, although various legislative and policy initiatives continue to address this issue.

Estonia's ongoing commitment to fiscal discipline and structural reforms has led to remarkable progress in the establishment of a market-oriented economy. During the last decade, Estonia privatized most state-owned enterprises, enacted very liberal trade policies, welcomed foreign investment, and pursued generally prudent monetary and budgetary policies. At the same time, the country has struggled with a large current account deficit, high unemployment, and relatively slow progress in social sector reforms during these often difficult years of transition.

Estonia's political situation at both the national and local levels remained largely stable between mid-1999 and late 2000. The October 1999 municipal elections produced a victory for the three-party national ruling coalition in two-thirds of the country's municipal councils, including the capital, Tallinn. Since entrance into the EU and other Western institutions remains a cornerstone of Estonia's economic and foreign policy, the necessity of meeting often strict EU membership criteria drives much of the country's current reform efforts. Estonia continues to proceed rapidly in its membership talks, having closed nearly half of its negotiation chapters by the middle of 2000. Following an economic recession caused by the August 1998 Russian financial crisis, the economy began to recover in late 1999 and exhibited increasing growth throughout the year 2000. The last phase of privatization, which involves large infrastructure and energy enterprises, slowly moved forward amid political and financial controversies.

DEMOCRATIZATION

Political Process

1997	1998	1999-2000	2001
2.00	1.75	1.75	1.75

After three and a half years of fragile minority coalitions and left-right partnerships, the March 1999 parliamentary elections saw a center-right coalition form a majority government with greater prospects for stability. In contrast to the previous minority government of Prime Minister Mart Siiman's, which had faced increasing difficulties in carrying out his political programs, the new leadership of Prime Minister Mart Laar was able to use its majority in parliament to pass various legislative measures in 1999 and 2000. Among the government's initiatives were emergency spending cuts in August 1999 and radical tax code changes in December of that year, both of which were part of the coalition's broader economic liberalization program.

Following the restoration of Estonia's independence in 1991, the country's first post-independence national legislative elections in September 1992 brought the right-of-center Pro Patria Union to power. Two years later, Prime Minister Mart Laar was ousted in a no-confidence vote over alleged financial improprieties and was replaced by Environment Minister Andres Tarand. The victory of the center-left Coalition Party/Rural Union alliance in Estonia's second parliamentary vote, held in March 1995, marked a political shift in the legislature. The results reflected popular dissatisfaction among elderly and rural voters, who were hardest hit by the Pro Patria-led government's market reforms. Tiit Vahi, a moderate who was chosen prime minister, formed a center-left coalition with the left-wing Center Party, while promising to continue the previous government's reform policies.

In October 1995, the government collapsed amid an illegal wiretapping scandal that implicated Interior Minister Edgar Savisaar, who was dismissed and whose Center Party left the ruling coalition. Vahi subsequently formed a new coalition in which the right-of-center Reform Party joined the Coalition Party and Rural Union. This fragile left-right minority coalition held until February 1997, when Vahi resigned over allegations that he had illegally obtained luxury apartments during the privatization process between 1993 and 1995. In March, President Lennart Meri approved Mart Siiman of the Coalition Party as the new prime minister. Throughout 1998, the ruling left-of-center minority coalition, composed of the Coalition Party, Rural Union, the Country People's Party, and the Party of Pensioners and Families, failed to increase its membership and its support in parliament. Consequently, Prime Minister Siiman was unable to carry out many of his political programs, including difficult legislative reforms necessary for EU membership.

The most recent national legislative election, which observers called free and fair, took place on March 7, 1999. More than 1,800 candidates representing 12 parties, as well

as 19 independent candidates, competed for the 101 seats in parliament. The Center Party of Edgar Savisaar won the largest share of votes, 23.4 percent, and captured 28 seats. The other six parties that met the five percent threshold needed to enter parliament were Pro Patria, which gained 18 seats; the Estonian Reform Party, 18 seats; the center-left Moderates, 17 seats; the centrist Coalition Party, 7 seats; the left-of-center Country People's Party, 7 seats; and the left-wing United People's Party, representing some of the country's large ethnic Russian population, 6 seats. Although the Center Party received the most votes of any single party, the Reform Party, Pro Patria, and the Moderates, who together captured 53 seats, formed a majority coalition government and evenly divided the 15 cabinet seats among them. Despite differences between the right-wing Reform Party and Pro Patria and the more left-leaning Moderates, the new coalition, which had signed a cooperation agreement the previous December, promised to be more stable than previous governments. On March 22, 1999, parliament approved Pro Patria's Mart Laar, who had served as prime minister from 1992 to 1994, as the new premier.

On September 20, 1992, Estonia held its first direct post-independence presidential election. According to the constitution, any citizen by birth who has reached the age of 40 may be nominated as a presidential candidate by at least one-fifth of the membership of the Riigikogu. When none of the four candidates received an absolute majority of the popular vote in the 1992 election, parliament held the deciding round of voting and elected former Foreign Minister Lennart Meri. After the 1992 poll, the procedure reverted to the election of a president by parliament.

In the last presidential election, which took place in August and September 1996, former Chairman of the Supreme Soviet Arnold Ruutel challenged incumbent President Meri. Following two rounds of voting in which neither candidate received the necessary two-thirds vote by members of parliament, the elections were moved to a vote by the electoral college, which comprises the full parliament plus 273 local government representatives. Both candidates automatically entered this round of voting and were joined by three new candidates who had been nominated by at least 21 members of the electoral college. After two rounds of voting, Meri was reelected to his post by a comfortable margin. The next presidential election is scheduled for 2001.

In late 1999, parliament voted down a bill on direct presidential elections that was sponsored by the opposition Center Party. Public opinion polls taken at the time indicated that almost 75 percent of Estonians support a direct vote for president. However, opponents of the measure, including the ruling coalition, claimed that a direct vote would create confusion about the respective roles of the president and prime minister and concentrate too much power in the executive branch at the expense of parliament.

Estonia's parliamentary electoral law encourages the formation of larger, and therefore fewer, political parties. Specifically, it requires parties running in national legisla-

tive elections to receive at least five percent of the vote in order to enter parliament. Since the early 1990s, many smaller parties have merged in an attempt to gain wider public support. More recently, the number of political parties registered in Estonia has declined by roughly half: from 28 in July 1998 to 18 in mid-1999 to some 13 as of mid-2000. In October 1998, two months before the registration deadline for the March 1999 parliamentary elections, an amendment to the 1994 Law on Parties raised the membership requirement from 200 to 1,000 for a political party to register and run in an election. Smaller parties raised concerns about the late introduction of these changes and claimed that the move was prejudicial against them.

In November 1998, just four months before the March 1999 parliamentary ballot, parliament voted to abolish electoral unions. The law's purpose was to prevent political parties from forming ultimately unstable coalitions prior to elections for the sole purpose of passing the five percent threshold to enter parliament, as occurred during the 1995 vote. The law was further amended in February 1999 to allow parties in parliament to form only one parliamentary faction, ostensibly to lead to a more cohesive legislature. Some analysts speculated that the ban also may lead to the eventual reduction in the total number of parties in Estonia by encouraging additional mergers of existing parties.

Despite the continuing decrease in the number of parties, Estonia's electoral system remains multi-party based at all levels of government. Seven electoral coalitions and nine parties competed in the national legislative elections in March 1995, and 12 parties took part in the March 1999 elections. In September 1998, 13 political parties were represented in parliament. After the 1999 poll, the number decreased to seven, largely as the result of the merging of smaller parties. While 19 parties participated in the 1996 local elections, the number decreased slightly to 14 in 1999.

In December 1998, parliament adopted controversial amendments to the parliamentary election law and the local government council election law. According to the amendments, members of these two bodies must possess sufficient Estonian language skills to be able to participate in their respective assembly's work and to understand legal acts. The amendments, which took effect in May 1999, did not affect candidates in the March 1999 legislative elections. In a report by the Council of Baltic Sea States, the organization's commissioner expressed concern that the amendments would restrict a citizen's right to run for office and the electorate's right to vote for candidates of its choice.

Voter turnout for parliamentary elections increased slightly from 67 percent of eligible voters in September 1992 to approximately 70 percent in March 1995 but fell sharply to around 57 percent in March 1999. Reasons cited for the decline include confusion over the large number of candidates and parties, many of which espoused similar platforms, and the belief that voters are unable to influence the political system. While lower than figures at the national

level, voter turnout for local elections has remained steady. Approximately 52 percent of eligible voters, including non-citizen permanent residents, took part the October 1993 and October 1996 local elections. For the October 1999 local elections, turnout dropped below the 50 percent mark to 49.4 percent. Turnout was 50.9 percent for citizens and only 43 percent for noncitizens.

Apathy has also been expressed in the low levels of party membership in Estonia. In a survey conducted by the domestic Saar polling agency in 1997, only two percent of Estonians and one percent of non-ethnic Estonians stated that they had joined a political party. A June 2000 European Forum provided the following membership figures for some Estonian parties: Center Party, 2,100 members; Pro Patria Union, 1,400 members; Reform Party, more than 800 members; and Coalition Party, more than 500 members. According to figures from October 1998, women accounted for 45.5 percent membership in registered parties. Under the constitution, only citizens of Estonia may be members of political parties. However, noncitizens, the majority of whom are Russian-speaking non-ethnic Estonians, may vote in local elections. Several political parties have been formed to address the concerns of both citizen and noncitizen Russian speakers and to increase their involvement in Estonian politics. Most recently, the Russian Baltic Party of Estonia was established in June 2000.

Civil Society

1997	1998	1999-2000	2001
2.25	2.25	2.50	2.25

Although Estonia's nongovernmental organizations (NGOs) continue to suffer from organizational and financial shortcomings, efforts have been made to improve the state of nonprofit groups through training programs, research and publications, and information exchanges. In late 1999, for example, a number of nonprofit groups and political parties signed an agreement to increase cooperation between the third sector and national and local government officials.

In the years of political upheaval immediately preceding independence, the nonprofit sector in Estonia underwent significant changes. With the disappearance of large Soviet-era organizations in the late 1980s, some voluntary associations active before 1940 were restored and many new independent NGOs were established. Among the first new organizations were mass movements such as the Popular Front and the Cultural Heritage Protection Society, which supported the restoration of Estonia's independence and helped to set the tone for the country's emerging political parties.

In the first several years after the disintegration of the Soviet Union, Estonia's nonprofit sector grew rapidly. Hundreds of educational organizations, sports associations, professional groups, and other groups met the registration

requirements by submitting a founding agreement, articles of association, a bank statement of funds, a list of board members, and a nominal fee. Since 1988, more than 70 cultural societies and associations addressing the interests of ethnic minorities have been established, including the Estonian Union of National Minorities and the Union of Slavic Educational and Charity Organizations. Diverse organizations such as Estonian Women in Film, the Estonian Businesswomen's Association of Rapla, and the Estonian Environmental Women's Union represent women's issues. According to official statistics, Estonian civil society currently includes a remarkably large number of NGOs. As of October 9, 2000, the Estonian Central Registry listed 13,182 nonprofit associations and 357 foundations. However, the majority of these organizations are either very small, with staffs of fewer than ten people, or largely inactive.

Popular participation in NGOs remains constrained partly because the existence of an independent third sector characterized by genuine volunteerism, as opposed to enforced voluntary activities during the Soviet period, is still a relatively new phenomenon. Other factors include larger economic concerns, which limit much of the population's activities with charitable and other groups, and a belief that civic initiatives will not solve the country's problems. While the exact proportion of the population involved in NGOs is difficult to determine, one study found that less than 40 percent belongs to at least one nongovernmental group, broadly defined to include political parties, trade unions, professional and educational associations, and cultural and charitable organizations.

In addition to staff and volunteer shortages, most NGOs continue to suffer from limited institutional and organizational capacities. One of the greatest challenges facing Estonian nonprofit organizations is the need to improve their overall level of professionalism. Senior staff members frequently have insufficient management and administrative experience, while other NGO employees exhibit poor skills in areas such as proposal writing, accounting, budget elaboration, and public relations. Most NGOs are not well-versed in public relations efforts with the media, which favor politics, economics, and entertainment over NGO issues. The boards of directors of nonprofit organizations are frequently inactive or unfamiliar with the responsibilities of board members.

The long-term financial viability of most Estonian NGOs remains uncertain because of decreasing foreign aid, inadequate private financial support, and unfavorable provisions in tax laws. Recent legislation governing the operation of nonprofit organizations includes the 1996 Law on Nonprofit Associations and the Law on Foundations, which allow groups to earn income that can be used to achieve statutory objectives. However, all NGOs pay taxes on earnings from business activities related to their work; some groups must pay taxes on funds received from donors. According to the Income Tax Law of 1994, only organizations engaged in activities for the public benefit, including science, culture, education, sports, religion, health care,

social welfare, and environmental protection, may qualify for tax exemptions on financial contributions.

Financial support from the business community, for which the idea of donating to charitable organizations is still a relatively novel concept, remains low. Under existing laws, companies are only exempt from paying income taxes on the first ten percent of their annual profits donated to charities; for individuals this figure is five percent. NGOs in larger cities largely depend on private sector donations and decreasing foreign assistance, while those in smaller towns and rural areas receive most of their funding from state and local administrations and through membership fees. The government supports the nonprofit sector through tax revenues from items like alcohol, tobacco, and gambling, which totaled \$5 million in 1998, and through direct funding from the state budget, which exceeded \$7 million the same year. Sixty-eight percent of respondents to a December 1999 public opinion poll said that the government should be the primary source of financial support for nonprofit groups.

In an effort to help remedy the organizational and financial concerns of NGOs, nonprofit groups have demonstrated an increasing willingness and ability to exchange information and cooperate on joint projects. The Network of Estonian Nonprofit Organizations (NENO), an umbrella group for NGOs, provides training programs on diverse topics such as nonprofit management, strategic planning, fund-raising, attracting and using volunteers effectively, and working with board members. In 1998, NENO helped to organize Estonia's first NGO forum for nonprofit groups to discuss issues of mutual interest and concern. NENO also issues publications on various NGO topics in Estonian, Russian, and English. An online NGO database maintained by the Jaan Tonisson Institute allows local organizations to obtain and share information and to inform the public of their activities.

The government's perception of the NGO sector has continued to improve, as a result of various efforts by some nonprofit groups. In an attempt to strengthen cooperation between the state and the nonprofit sector on shaping public policy and legislation, approximately 20 leaders NGOs and political parties signed a memorandum of cooperation in December 1999. The groups established a chamber of cooperation for maintaining regular contact between the two sides and worked out a blueprint for the continued development of Estonia's civil society.

Membership in Estonia's trade union sector, which operates independently from the government, is in decline. According to the U.S. Department of State, membership in the Central Organization of Estonian Trade Unions (EAKL), the country's principal trade union alliance, has decreased from a reported high of 500,000 in 1992 to 330,000 in 1993, 200,000 in 1994, and only about 65,000 in 1999. This decrease has been attributed largely to the privatization and breakup of large state-owned enterprises and to the subsequent shift of workers into smaller firms and the service sec-

tor. Only about 15 percent of Estonia's 600,000 wage earners currently belong to trade unions. In late 1999, the government finally registered the EAKL under the 1996 Law on Nonprofit Associations, after having threatened to liquidate the group unless it met the strict registration requirements for trade unions. The International Labour Organization assisted in the process by finding a compromise on applying the registration procedures in practice. In June 2000, parliament adopted a long-delayed Trade Unions Act that defines the following: the rights of labor unions to oversee the interests of their members; the relationship of unions to employers and public and local government agencies; and the requirements for the establishment, operation, and dissolution of unions as nonprofit associations. Representatives of trade unions have praised the law for protecting employees' rights, including in cases of collective disputes.

Entrepreneurs' organizations have grown in Estonia since the mid-1990s. The Estonian Chamber of Commerce and Industry has a membership base of more than 26,000 large companies and smaller enterprises, while the Estonian Association of Small and Medium-Sized Businesses encompasses approximately 300 member groups. The Estonian Farmers' Federation, whose membership declined from 10,000 in 1991 to approximately 5,000 in 1999, represents the interests of farmers. The Estonian Chamber of Agriculture and Commerce, which represents Estonian agricultural producers and processors, has about 200 member organizations and companies.

Although the constitution stipulates that only citizens of Estonia may belong to political parties, noncitizens may form nonprofit and social groups. Political parties and associations whose activities promote the violent change of the country's constitutional system or violate criminal law are prohibited. Politically active interest groups focus on education, the environment, minority rights, and social welfare.

Independent Media

1997	1998	1999-2000	2001
1.75	1.75	1.75	1.75

Since the collapse of the Soviet Union, Estonia has witnessed the development of a vibrant media sector characterized by a surprisingly large number of print and broadcast outlets for the country's small population. Partly as a result of this intense competition for limited advertising and subscription revenues, financial difficulties continue to plague newspapers and broadcast media. Despite some legislative shortcomings, particularly regarding the criminalization of libel, Estonia enjoys an independent press that is free from government interference.

The operation of privately-owned media began shortly before the restoration of Estonia's independence in 1991. The first new privately run newspapers were established in

the late 1980s. The first paper to be privatized was the daily *Postimees*, which has consistently been the biggest selling paper in the country. The first private radio station began broadcasting in 1990, and the first licenses for private broadcasters were issued in 1992.

For a country of only 1.4 million people, Estonia boasts three national private television stations: TV3, which enjoys the country's second largest viewership, Kanal 2, and TV1. The state-owned public service channel, Estonian Television (ETV), enjoys the highest ratings in Estonia, despite competition from independent stations. State and private channels broadcast Russian language programs, while cable and satellite networks offer programs from throughout Europe. More than 30 radio stations are privately run, and the state-owned public service Eesti Raadio broadcasts a mix of popular and classical music, news, and Russian-language programs on four channels. The country's two most popular stations are the public non-commercial Vikerradio and the independent Radio Elmar, which plays older Estonian pop music.

All Estonian-language daily newspapers are privately owned and receive no state subsidies. Of the country's seven national daily newspapers, five are printed in Estonian and two in Russian. There are dozens of weekly papers and magazines, as well as local and regional publications. The three most popular daily newspapers continue to be *Postimees* (The Postman), with a circulation of about 60,000, *Eesti Päevaleht* (The Estonian Daily), and *Sonumileht* (The Daily Story). The two main news agencies are the Baltic News Service (BNS), a privately-owned agency headquartered in Tallinn with branches in all three Baltic states, and the previously state-run Estonian News Agency (ETA).

Following the restoration of independence, the government monopoly on printing and distribution facilities was abolished. While the government formally owns the newspaper printing plant in Tallinn, it does not interfere in a private company's management of the facility. The country's various regional printing plants and distribution networks are privately owned and operated.

One of the country's primary media organizations is the Estonian Newspaper Association (EALL), an umbrella group of newspaper publishers, editors, and journalists that was established in 1990. Uniting more than 40 newspapers printed in Estonia, the EALL defends the common interests and rights of newspapers and fights against violations of freedom of the press. In 1991, the EALL established the Estonian Press Council, a self-regulatory body for the media. Of the Estonian Press Council's 15 members, six are women. Other media associations include the Association of Estonian Broadcasters, the Journalists' Union, and the Media Educators Association.

Many private media outlets continue to face financial difficulties. This is due, in part, to diminishing advertising revenues and to the large number of competing media organizations relative to the small size of the country's population. In 1999, the total volume of media advertising was

639 million *kroons*, or ten percent less than the previous year. Nearly half of all advertising revenues were spent on newspapers, followed by television, with 20 percent, and magazines and radio with about 12 percent each. However, according to the media research company Baltic Media Facts, the advertising market is expected to grow by five to ten percent in the year 2000.

Despite receiving government funding, the state-run ETV faced numerous financial problems in 1999 and 2000 that resulted in deep funding cuts, staff dismissals, and reductions in programming. The station's budgetary problems peaked in early 1999 after the country's three main private television stations agreed to pay ETV a fixed sum to stop running advertisements from January 1998 through August 1999. ETV, which previously had drawn its revenues from both the state budget and advertising, would be financially compensated by the three private stations. The director general of ETV, Toomas Lepp, explained that the decision was motivated by a desire to stop commercial considerations from interfering with public service programming decisions. In May 1999, however, ETV began airing commercials again after the private channels, particularly TV1, had been consistently late with their payments and thereby had violated the agreement. The government subsequently intervened and declared that ETV should not show advertisements. In June, ETV's board of directors resigned in protest over what they called Lepp's autocratic leadership style and decisions that were harmful to ETV. By the end of 1999, citing management failures and financial irregularities, the Estonian Broadcasting Council had dismissed Lepp.

The Estonian constitution prohibits censorship and guarantees the right to freedom of expression. The government respects these provisions in practice. According to article 45, "everyone shall have the right to freely circulate ideas, opinions, persuasions and other information by work, print, picture and other means," and "there shall be no censorship." While there is no specific press law, print media are regulated through various other pieces of legislation, including the copyright, competition, language, and state secrets acts. Electronic media are governed by the May 1994 Broadcasting Law, which enshrines the right of television and radio stations to make independent decisions about the content of their transmissions. In its annual *Survey of Press Freedom*, Freedom House rated Estonia Partly Free in 1992 and Free from 1993 to 2000.

Although Estonia's overall legal framework adequately protects press freedom and does not contain legal penalties for "irresponsible journalism," cases regarding libel continue to be punishable under criminal law. The ENA has lobbied the government to make defamation and libel civil offenses. In 1997, in a high profile case, the Estonian supreme court upheld a lower court's conviction of investigative reporter Enno Tammer on criminal charges of insulting the wife of Estonian politician Edgar Savisaar during an interview. Tammer was ordered to pay a fine of 220 kroons

(approximately \$15) and court costs. PEN and the Estonian Newspaper Association (ENA) condemned the decision—the first of its kind in post-Soviet Estonia—as an attempt to limit freedom of speech. In 1998, the case was brought before the European Court of Human Rights. In late 1999, the court ruled that it would continue with its investigation, a decision that does not guarantee that the case will go to trial.

Estonia’s press, which is now entirely privately owned, enjoys editorial independence from the government. Likewise, public service radio and television, which receive financing from the state budget, do not face government interference in their editorial decisions. While the country’s major newspapers have particular political leanings, not all of them openly endorse individual parties or candidates. Nevertheless, much of the press demonstrated a bias against the Center Party of Edgar Savisaar during the 1999 parliamentary election campaign, and some newspapers have published paid political advertisements as part of their editorial content. Although much of the media frequently conduct probing investigative reports, some journalists tend to publish rumors and allegations as facts; “yellow journalism” is not uncommon. The Estonian Press Council, a group composed of various broadcast and print-related organizations, hears cases involving journalistic improprieties or problems with the authorities. Although its decisions are not legally enforceable, the Estonian News Agency can publish the results and thereby exert pressure on the government to recognize the editorial independence of the country’s media.

Estonia continues to have one of the highest levels of Internet penetration in the former Soviet Union and Eastern Europe and more Internet users than some European Union member states. According to a BMF Gallup Media survey, approximately 28 percent of persons aged 15 to 74 used the Internet as of spring 2000, compared to 16 percent a year earlier. A national campaign (code-named “Tiger Leap”) launched in 1997 and sponsored by the United Nations Development Programme has helped to extend Web access throughout the country and to establish more than 80 public access sites where Estonians can use the Internet for free. The only restriction that private citizens face regarding Internet access remains the high cost of Internet connections and computers.

Governance and Public Administration

1997	1998	1999-2000	2001
2.25	2.25	2.25	2.25

The October 1999 local elections largely mirrored the parliamentary poll held earlier that year, as the center-right grouping of Pro Patria Union, the Reform Party, and the Moderates secured victories in two-thirds of Estonia’s local councils. Their most important win also proved particularly difficult: this “triple alliance” secured a slim majority

in Tallinn’s City Council by forming a coalition with other parties, including those representing Russian speakers.

Under Estonia’s constitution, which was adopted in 1992, a clear division of power exists between the executive and legislative branches of government. Among the main responsibilities of the country’s 101-member parliament are the adoption of laws and regulations, the passage of a state budget, the election of the president, and the authorization of the prime ministerial candidate to form a government. The executive branch, which is represented by the prime minister and his cabinet, executes domestic and foreign policy, prepares draft laws, administers the implementation of acts adopted by parliament, and directs the work of government institutions. Estonia’s president, who serves as the country’s head of state, commands a largely ceremonial position. The legal chancellor, an independent official who examines the conformity of legislation from the legislative and executive branches and local governments with the constitution, enforces a system of checks and balances. If a conflict is found and appropriate changes are not made within 20 days, the legal chancellor appeals to the supreme court (the court of constitutional review) for the law’s repeal.

The constitution guarantees transparency in the work of the executive and legislative branches of government. Article 44 requires all state and local governments to provide information about their activities to Estonian citizens at their request. This requirement does not include information that is intended for internal use only or that is prohibited by law to be revealed. However, it has been reported that government officials, particularly at the local level, arbitrarily deny citizens and journalists access to information that they have requested. Most sessions of parliament are open to the public, and all laws adopted by the legislature are published in the official State Gazette. The government press office, along with each ministry’s press secretary, disseminates official information to the news media.

Despite pressure from various local and international organizations, Estonia has not adopted a freedom of information act. In July 1999, a working group composed of media, government, and academic representatives presented a draft public information law to the Interior Ministry. The law was intended to ensure the right to gain access to documents produced by state and local authorities. In March 2000, parliament passed the Digital Signatures Act, an important precursor to an eventual public information law. The Digital Signatures Act, which will go into effect in January 2001, requires the government to digitally code every online document it prepares in order to ensure its authenticity, facilitate the placement of government documents on the Internet, and provide the public with easier access to such information.

During the period of political upheaval in the Soviet Union in the late 1980s, the local council elections of 1989 restored Estonia’s system of local self-government system. From 1989 to 1992, Estonia had a two-level local government system formed by 15 counties with self-governments

at the regional level and six larger cities at the municipal level. The Local Government Organization Law of 1993 abolished elected county governments and reorganized the county system into regional units of the central state administration. The one remaining level of local government consisted of more than 200 towns and rural municipalities, all of which enjoy the same legal status. While the 1992 constitution provided the general legal basis for local power, subsequent laws addressing specific issues of subnational government included the Territory of Estonia Administrative Division Act, the Municipal and Town Budget Law (June 1993), the Law on the Correlation between Municipal and Town Budgets and the State Budget (August 1993), and the Local Taxation Law (September 1994).

According to the constitution, local authorities autonomously manage and resolve all local issues. The basic functions of local government include the provision of public services, the organization of social services, and the maintenance of local public transportation and roads. Local authorities also share certain responsibilities with the central government, including in the field of education. Although currently there is no regional level of self-government, county governments are responsible for organizing and coordinating the work of national institutions at the local level.

During the last several years, considerable debate has been focused on reducing and consolidating the number of local authorities. Since 70 percent of Estonian municipalities have less than 2,500 residents, establishing fewer but larger local governments would help the authorities improve their financial and administrative capacities. By the end of 1999, 18 municipalities had decided to merge on their own initiative; this decreased the number of local governments from 256 to 247. One of the primary objectives of current local administrative reform is to oversee the eventual reduction of municipalities to between 60 and 80 by October 2002. Under the plan, municipalities would need to have at least 3,500 inhabitants. In order to fulfill joint tasks more efficiently and protect regional interests, local governments continue to work together through national and regional associations, including the Association of Estonian Cities and the Association of Estonian Rural Municipalities.

Since the restoration of its independence, Estonia has held local elections three times: in October 1993, October 1996, and October 1999. International election observers described all three elections as free and fair. While only Estonian citizens may stand as candidates, noncitizen permanent residents who have lived in their respective municipality for at least five years may vote in local elections. In the 1999 elections, the Pro Patria Union, the Reform Party, and the Moderates—nicknamed the triple alliance—took power in two-thirds of Estonia's major cities and towns. In the race for the Tallinn City Council, considered by many to be second in importance only to the national legislature, the Center Party won the most votes and secured 21 of 64 seats. The triple alliance, which also formed the ruling coalition in parliament, received 28 seats altogether. Though

neither side had won an absolute majority, the triple alliance cobbled together a bare majority coalition of 33 seats. The coalition included the four members of the People's Trust and one of the nine members of the People's Choice, both electoral alliances of Russian speakers' parties. The Coalition Party subsequently added its two seats to the ruling coalition. Interior Minister Juri Mois of Pro Patria became Tallinn's mayor. In September 2000, the Coalition Party withdrew from the ruling coalition when Mois called for the removal of two prominent Coalition Party city officials based on allegations of corruption. Nevertheless, the coalition retained its absolute majority in the city council.

Municipal governments receive funding from the state budget through both direct budgetary appropriations and shared taxes; they also raise revenues autonomously. Money is allocated from the state budget to local budgets for purposes which may include supplementing budget revenues and helping to finance teacher salaries and capital expenditures. At the same time, the constitution calls for local governments to keep independent budgets and grants them the right to levy and collect taxes and to impose fees. The Local Taxation Law stipulates the kinds of taxes that local authorities may levy, including a local sales tax, an entertainment tax, and a motor vehicle tax.

Local governments continue to face financial difficulties and to operate at a deficit. According to Estonian Ministry of Finance statistics for the first nine months of 2000, total revenues and grants of local governments equaled 4.846 million kroons, while total expenditures totaled 4.866 million kroons. During the same period, the revenue from personal income tax (a shared tax that is centrally imposed and collected) constituted 56 percent of the total income of local budgets, while grants from the national government accounted for 25 percent of total income. The financial independence of local governments is effectively limited by the fact that the vast majority of their revenues comes from the central government. To address this problem, recommendations have been made to increase the number of local taxes and improve the efficiency of local tax collection measures.

Although Estonia's public administration underwent six reorganizations between 1987 and 1995, substantial reform of the civil service system began in 1996 when three key pieces of legislation came into effect. The Public Service Act, the Government of the Republic Act, and the State Public Servant Official Title and Salary Scale Act, which together established a legal framework for public service, address issues such as the rights and duties of public servants, their recruitment and evaluation, and the salary scales for 35 different levels of employment. According to the Public Service Act, local civil servants are considered local government employees. A recent reform effort was the establishment in 1999 of the Office of Public Administration Reform (OPAR) within the State Chancellery. However, a comprehensive strategy for public administration reform has not been developed, and the

tasks of OPAR remain unclear.

Most of Estonia’s civil servants conduct their work in an impartial and politically neutral manner. At the same time, the public service administration continues to suffer from a lack of qualified candidates because of competition from higher paying jobs in the private sector. Some of the specific problems that have been identified are difficulties in recruiting and retaining higher level officials (turnover rates are estimated at 15 percent), a skewed distribution of staff toward senior positions, and inequality in the remuneration of salaries. At the same time, recent positive developments include the launch of a new civil servants evaluation system that was adopted in 1999.

RULE OF LAW

Constitutional, legislative, and judicial framework

1997	1998	1999-2000	2001
2.25	2.25	2.00	2.00

Estonia’s judicial and legal systems, which operate free from state political control, have continued to undergo various reforms during the last decade. Prison reform efforts gained additional momentum in 2000 with the announcement of plans to build a new facility in southern Estonia. Recent salary increases for police officers should help to attract more qualified and professional candidates. Nevertheless, delays in the criminal justice system, reports of abuse of suspects by law enforcement officials, and poor prison conditions remain serious problems.

One of the first legislative priorities following the restoration of independence was the reestablishment of Estonia’s constitution, which was adopted by public referendum on June 28, 1992, with 93 percent of the vote. The constitution includes a chapter on the rights and obligations of citizens and noncitizens; establishes the separation of authority of the executive, legislative, and judicial branches of government; and contains sections on the national budget, foreign relations, national defense, and local government.

There is no separate court for addressing constitutional matters in Estonia. Rather, the Supreme Court serves as the court of constitutional review through its five-member Constitutional Review Chamber. On the proposal of the chief justice, who also serves as the Chamber’s chairman, the supreme court elects members of the Chamber for no more than two five-year terms. During the first five months of 2000, the Chamber issued six rulings. One important ruling involved an austerity budget law of June 1999 that cut funding to individuals who had been forced out of resituated homes according to a 1994 housing law. The legal chancellor submitted an appeal to the Chamber in January, arguing that the move violated article 116.2 of the constitution, which states that parliament cannot reduce or elimi-

nate budget expenditures prescribed by other laws. Unable to reach a consensus, the Chamber submitted the case to the full 17-member supreme court. In its final ruling in March, the court argued that the housing law did not specify the amount needed to implement the law. Therefore, the court could not declare the budget amendments null and void because it could not assess whether the cuts would effectively halt implementation of the housing law and, thus, constitute a violation of the constitution.

Chapter two of the constitution guarantees fundamental human rights, including freedom of conscience, religion, thought, and assembly. Article 12 prohibits discrimination on the basis of nationality, race, color, sex, language, origin, creed, political or other persuasions, or financial or social status. Estonian citizens have the right to engage in commercial activities and to form profit-making associations. Foreign citizens and stateless persons residing in Estonia also enjoy this right unless otherwise determined by law. Under the constitution, property may not be expropriated without the owner’s consent, except in cases of the public interest and in exchange for appropriate compensation. In practice, the government generally respects these political, social, and economic rights.

Over the last decade, Estonia has overhauled its system of criminal legislation. An interim criminal code, which went into effect in June 1992, revised the Soviet-era law and eliminated political and economic crimes. A code of criminal procedure was adopted in 1994, and amendments to the criminal code in 1996 provided police and prosecutors with more tools to combat organized crime. Under Estonian law, a warrant is required for the search and seizure of property. During the investigative stage, the prosecutor issues warrants after probable cause has been shown. Once a case has gone to trial, the court is responsible for issuing warrants. According to the constitution, detainees must be informed promptly of the reasons for their arrest and given the immediate opportunity to choose an attorney. If a defendant cannot afford legal counsel, the state must provide it.

In late 1999 and early 2000, several hundred police officers were dismissed as part of an effort to cut expenses from the Interior Ministry while providing salary increases for the remaining law enforcement officials. Since some police officers reportedly have used excessive physical force and verbal abuse during the arrest and questioning of suspects, the controversial move was designed to help attract and retain qualified individuals. In April 2000, parliament announced plans to construct a new prison near the southern town of Tartu. The decision represents part of the government’s multiyear plan to improve conditions in Estonia’s prisons, which continue to suffer from a lack of resources, inadequately trained staff, and overcrowding.

Estonia’s constitution establishes an independent judiciary, which in practice is generally free from interference from other branches of government. The Status of Judges Act, which regulates various aspects of the judiciary, also includes basic guarantees for the independence of judges.

Although most judges are politically impartial in their rulings, some judges continue to show uncertainty in their application of the law. The quality of court decisions varies considerably, but it remains particularly unsatisfactory in the lowest-level courts. To address this problem, training programs have been conducted for judges and prosecutors, with some 60 percent having undergone 112 hours of training each. Many qualified lawyers still regard a career in the judiciary as unappealing, particularly since judges' wages lag behind those in the private sector. In August 2000, a Ministry of Justice bill proposed increasing the salaries of judges by 20 percent as of 2001. Most judges would receive around 18,000 kroons per month. The fact that 14 of 238 judges' posts remained vacant during the first half of 2000 contributed to the persistent backlog of cases, that is, criminal cases pending for more than one year and civil cases pending longer than two years. In 1999, the number of pending cases in Estonia's courts equaled 42.4 cases per judge per month.

The judiciary operates under a three-tier system of lower-level rural and city courts, district courts, and higher courts, including the supreme court. All judges are appointed for life and may be removed only by a court decision. To help ensure transparency, the constitution calls for public court proceedings; closed sessions may be held only for specific reasons such as the protection of state or business secrets or in cases involving minors. The lower levels of the court system are linked financially to the Ministry of Justice, while at the highest levels judges are paid from the state budget independently of the ministry. The enforcement departments of county and city courts generally implement judicial decisions effectively in both criminal and civil cases.

The status of Estonia's large ethnic Russian population has continued to strain relations with Russia, which has accused Estonia of violating the rights of its Russian-speaking population. However, according to a recent EU report on Estonia, the rights of the Russian-speaking minority, both citizens and noncitizens, are largely observed and safeguarded. All residents—citizens or not—can file complaints directly with the supreme court about alleged violations of human or constitutional rights. In some cases, the court has decided in favor of complainants. In predominantly Russian-speaking regions of the country, the Russian language continues to be used extensively in the court system and administration. While the 1993 Law on Cultural Autonomy of National Minorities provides for the preservation of the languages and cultures of national minorities, some noncitizens have termed the law discriminatory since it only applies to citizens.

During the Soviet era, large numbers of non-Estonians (mostly Russians) migrated to Estonia. They and their descendants now account for approximately one-third of the country's total population of 1.4 million. Under the 1992 Citizenship Law, which readopted legislation from 1938, anyone born after 1940 to a citizen parent of pre-World War II Estonia is a citizen by birth. Those who arrived

during the Soviet period are regarded as immigrants and must apply for citizenship. A new Citizenship Law adopted in 1995 toughened certain requirements for naturalization, including lengthening the residency period. The Russian government, Russian-speakers in Estonia, and some international organizations criticized elements of the law as discriminatory. In December 1998, the government adopted amendments that allow stateless children who are born in Estonia after February 26, 1992, to legally resident yet stateless parents to acquire Estonian citizenship. They can do so at the request of their parents and without having to pass a language test. As of August 2000, more than 1 million residents of Estonia are citizens, of which more than 112,000 have been naturalized since 1992. Bureaucratic delays and the language requirement continue to be cited as among the primary disincentives for securing citizenship. There is a dearth of qualified teachers to provide Estonian language training, and the growing demand to take the national language test has left the state exam center with insufficient funding to administer the test to all who are interested.

The issue of knowledge of the Estonian language remains important not only with regard to citizenship, but also in terms of education, employment, and political participation. In February 1999, parliament adopted amendments to the Language Law that require private sector workers, public servants, and local government officials to use Estonian when providing goods and services to the public. The law attracted considerable criticism from many Russian speakers. Some international organizations believed the law was in conflict with EU criteria by violating the principle of free movement of labor and services.

In June 2000, the Language Law was amended further. It no longer requires the unconditional use of Estonian in the private sector—only in cases where it is in the public interest such as security or safety. The 1998 Parliamentary and Local Elections Law, which requires candidates for public office to have a sufficient command of Estonian for participating in debates and understanding legal acts, has been criticized for restricting the rights of non-Estonian speakers to choose their candidates at the local level. In the area of education, the Law on Basic and Upper Secondary Schools was amended in April 2000 to allow 40 percent of teaching in upper secondary schools to be in a language other than Estonian after 2007. Initially, all such instruction was to be provided exclusively in Estonian.

During the last decade, the government has taken a number of steps to further the integration of nonethnic Estonians into society. In 1993, President Meri established a Roundtable of National Minorities to participate in the state's national minorities' policy. Its members are representatives of ethnic minorities, stateless persons, and political parties. The post of minister without portfolio, responsible for population and integration issues, was created in 1997. The following year, a state Integration Foundation was also established. In 2000, the government approved the State Integration Program for 2000 to 2007. Implemented by the Estonian Integration

Foundation, the program focuses on education, language training, public awareness campaigns, and the preservation of cultural identity.

Corruption

1999-2000	2001
3.25	2.75

Despite its reputation as one of the least corrupt Eastern European or former Soviet countries, Estonia continued its efforts in 1999 and 2000 to address corruption through legislative reforms and accession to international treaties. One of the most publicized and long-lasting corruption cases, that of former Bank of Estonia president Siim Kallas, drew to an apparent close in late 2000 when Kallas was cleared of all charges against him. However, the authorities continue to pursue other cases against officials. NGOs engage in anticorruption public education and research projects.

In Transparency International's 2000 Corruption Perceptions Index, Estonia received a score of 5.7 on a 10-point scale, where 10 represents the lowest possible level of corruption. With a ranking of 27 out of the 90 countries Transparency International surveyed, Estonia's placement was better than any Eastern European or former Soviet country. A Business Environment and Enterprise Performance Survey (BEEPS), which the European Bank for Reconstruction and Development (EBRD) and the World Bank conducted from June to August 1999, included questions to more than 3,000 firms in 22 transition countries on their impressions of various forms of corruption. Of the 132 Estonian companies surveyed, approximately 65 percent admitted to having paid bribes at least once. Most of the payments were for government contracts (34.5 percent), licenses (26.5 percent), and customs (15.2 percent). However, when asked how often bribes are demanded of them, only about 12 percent of respondents answered "mostly" or "frequently." This was the second lowest number among the countries surveyed.

These findings appear to be largely supported by an October 1998 public opinion survey of perceptions of and experience with corruption conducted by the Jaan Tonisson Institute and the Saar polling organization. When asked whether a government or private enterprise official had ever requested a bribe in exchange for favorable treatment, 69.4 percent of the 1,002 people surveyed answered "not at all," 17.4 percent said "rarely," 7.4 percent replied "hard to say," 4.4 percent responded "often," and only 1.2 percent said "very often." Among the persons or groups perceived to be the most corrupt were state officials (33.5 percent), followed by politicians (19.2 percent), police (13.3 percent), businessmen (11.4 percent), members of the court system (7.8 percent), and other persons (4.5 percent); 10.2 percent of respondents provided no response. Not surprisingly, the majority of those polled demonstrated a greater tolerance for corrupt practices involving smaller sums of

money, less expensive gifts, or more common personal activities. The following activities were described as not qualifying as corruption: a teacher or a doctor accepting gifts from a pupil or a patient in exchange for preferential treatment, 56 percent; using a company car for personal errands, 46.9 percent; favoring an official's relative or friend in a real estate deal, 26.7 percent; and a government or business official accepting money or gifts in exchange for special favors, only 6.9 percent.

Most personal services such as telephone installation and hospital admission do not require bribes. However, the generally low salaries of public servants (relative to the private sector) and certain wage discrepancies within the civil service have raised concerns about the potential for corruption. According to a recent World Bank study, although the pay system is relatively straightforward, it is not particularly transparent or fair because most of an employee's remuneration does not relate directly to job performance. The State Public Servants' Official Titles and Salary Scales Act established a uniform scale of 35 salary grades supplemented by a system of bonuses based on length of service (up to 15 percent), language and education qualifications (up to 10 and 20 percent, respectively), and performance (based on the supervisor's discretion). Anecdotal evidence suggests, though, that higher level officials can receive bonuses of up to 30 percent and enjoy perks such as cars and housing that are not available to lower level staff. In addition, some officials at the same salary grade reportedly have earned significantly different amounts. A new civil servants evaluation system adopted in 1999 should help to address this problem.

The primary anticorruption initiative in Estonia was the 1995 Anticorruption Act, a new version of which was passed in January 1999. The law contains provisions for amending legislation such as the Criminal Code and the Public Service Act that address corruption issues. It also introduced a legally enforceable Code of Ethics that sets standards for the behavior of civil servants. Estonia signed the Council of Europe Civil Law Convention on Corruption in January 2000 and the Criminal Law Convention on Corruption in June 2000.

To help combat corruption and prevent conflicts of interest, public officials must declare their financial assets and adhere to restrictions on private sector employment. Under the Anticorruption Act, government officials must submit yearly declarations of economic interests—real estate holdings, vehicles, income sources, shares or interests in businesses, and expensive gifts—to their respective agency heads. In May 2000, parliament adopted amendments to a law on wages that allow the release of information about the salaries of top state officials and heads of state enterprises without their consent.

Government officials may not belong to directory bodies of commercial enterprises, unless the enterprises are partly state-owned. They may engage in enterprises if they receive permission from their government agency; however, the enterprise must not hinder their work as public servants.

A public servant who is a member of a state enterprise directorship may not receive financial compensation, but this rule is not always followed in practice. The amendments to the law on wages are intended to improve the transparency of top officials' salaries, particularly with regard to illegal financial compensation from private sector activity.

Various government institutions implement anticorruption legislation. The State Audit Office, which is the country's supreme independent audit institution, conducts external audits of the entire public sector and reports directly to parliament. The Security Police, the Select Committee of the Parliament on the Application of the Anticorruption Act, and the Procuracy are involved in detecting and investigating corruption, while regular court systems conduct trials for alleged corruption. In 1999, the number of registered corruption cases was 51, compared to 45 in 1998, 38 in 1997, 78 in 1996, 45 in 1995, 42 in 1994, and 45 in 1993.

Estonian authorities have pursued several corruption cases involving both senior and lower-level officials during the period covered by this report. In December 1999, a customs inspector from the town of Valga received a two-year suspended sentence and was fined 1,250 kroons (\$80) for having accepted a bribe of nearly 30,000 kroons (\$1,900). In October 2000, a former finance ministry chancellor and a former deputy chancellor received a one-year suspended sentence and a fine of 24,000 kroons (\$1,343), respectively, when they were convicted on corruption charges stemming from a questionable auto sale deal. In May 2000, the former manager of the now-bankrupt Maapank was convicted of misusing deposited funds. The Tallinn District Court overturned the ruling in September; the state has 30 days to appeal the decision.

One of the highest profile corruption cases in recent years involved Siim Kallas, former president of the Bank of Estonia. The case centered on a 1993 loan of \$10 million by the Bank of Estonia to the now-defunct North Estonian Bank for investment in a Swiss fuel company. While the firm repaid \$2 million worth of interest, the rest of the money was never recovered. In June 1998, Kallas' immunity as a member of parliament was lifted to allow charges to be brought against him. Accused of submitting false information and abusing his power, Kallas was acquitted on March 5, just two days before parliamentary elections. After subsequent appeals by the prosecutor and the return of some indictments to the Tallinn city court, Kallas was finally cleared of all charges in October 2000.

In an effort to further publicize and combat corruption, the Jaan Tonisson Institute (JTI) has conducted educational programs and research projects on corruption-related issues, often in cooperation with state agencies, other nonprofit organizations, and private enterprises. JTI directed a program from 1998 to 1999 that consisted of conferences, studies, and training programs for journalists. The Estonian Law Center initiated a two-year

project in December 1999 to analyze current anticorruption legislation.

ECONOMIC LIBERALIZATION & SOCIAL INDICATORS

Privatization			
1997	1998	1999-2000	2001
2.25	2.00	1.75	1.75
Macroeconomic Policy			
1998	1999-2000	2001	
2.00	2.00	2.00	
Microeconomic Policy			
1998	1999-2000	2001	
2.00	2.00	2.00	

Having experienced a recession after Russia's August 1998 financial crisis, Estonia's economy began to recover during the last quarter of 1999. A return to growth in late 1999 and 2000 helped ongoing government efforts aimed at harmonizing Estonian legislation and practices with EU membership requirements. However, political and financial concerns continued to delay the last phase of privatization of large infrastructure and energy firms; reforms in the social sector struggled to catch up with those in the economy.

Since regaining its independence in 1991, Estonia has experienced significant changes in its political sphere and, perhaps even more dramatically, in its economic sector. Beginning with major monetary reforms launched in 1992, the country drew upon a broad political consensus for the successful implementation of a wide range of stabilization and structural reform policies. Among the country's most notable achievements are the introduction of a fully convertible currency under a currency board system, extremely liberal trade practices, a rapid and extensive privatization program, comprehensive price liberalization, and highly favorable policies towards foreign investment. After a banking crisis in the early 1990s, Estonia's surviving banks consolidated and adopted more prudent financial and administrative practices. Sound economic management led to a drop in inflation rates from triple to single digits between 1992 and 1998, and real growth in gross domestic product (GDP) ranged between four to ten percent between 1995 and 1998. While two speculative runs were attempted against the currency in 1997 and 1998, both were thwarted by the currency board's strict requirements for revaluation. The government has a limited direct role over most of the economy because of the currency board arrangement and a

balanced budget requirement in the constitution. As a result, Estonia now has one of the most free and competitive market systems in the former Soviet Union and Eastern Europe.

Despite impressive structural changes and growth, the Estonian economy suffered considerably from the Asian and Russian financial crises in 1997 and August 1998, respectively. The country's tiny stock market was among the first areas to be negatively affected when what had been only upward movement since its inception ended in October 1997. Estonia felt the impact of the Russian crisis in 1999, when real GDP declined by 1.1 percent and the federal budget deficit reached nearly 5 percent of GDP. The direct effect on most of the country's banks, which had invested less than one percent of their assets in Russia, was more modest; still, Estonia's general economic downturn hurt their profits.

Immediately preceding the Russian crisis, Russia had accounted for about 13 percent of all Estonian exports. This figure dropped to just under 9 percent in 1999. Hardest hit by this decline were Estonia's agricultural producers, for whom Russia was an important market. Consequently, many dairy, fish, and other food industries struggled to find other export destinations, merged, or went bankrupt. The percent of GDP coming from agriculture had already been decreasing, falling from 21.0 percent in 1989 to 6.4 percent in 1998 and 5.8 percent in 1999. But the Russian crisis accelerated the decline, as evidenced by average annual growth rates of -0.8 percent in 1998 and -1.4 percent in 1999. During the same period, the industrial sector also contracted. The share of GDP from industry decreased from 40.6 percent in 1989 to 28.1 percent in 1998 and 25.7 percent in 1999. By contrast, the service sector has grown considerably, with its share of GDP rising from 38.4 percent in 1989 to 65.5 percent in 1998 and 68.5 percent in 1999. Estonia's dramatic shift during the last ten years from a largely industrial and agricultural economy to one increasingly based on the service sector is illustrated by average annual growth rates for the period of 1989-1999 of -5.0 percent in agriculture, -5.7 percent in industry, and 0.3 percent in services.

The Russian crisis served to lessen Estonia's significant current account deficit, which had reached a high of 12.1 percent of GDP in 1997 before declining to 9.2 percent in 1998 and dropping further to 5.8 percent in 1999. Although exports dropped substantially, a general recession caused domestic demand to contract substantially. This, in turn, led imports to decline at an even faster rate. Foreign direct investment (FDI) doubled from \$267 million in 1997 to \$581 million in 1998 because of Swedish investments in Estonia's two largest banks; this severely distorted current account calculations in 1998.

During the second half of 1999, signs of economic recovery were evident. After declines in GDP of 5.6 percent, 3.9 percent, and 2.6 percent in the first, second, and third quarters of 1999, respectively, GDP began to grow in the

fourth quarter of 1999. By the middle of 2000, the economy had resumed much of its previous growth. GDP increased by more than 7 percent in the first six months of 2000 over the same period in 1999. The draft 2001 budget, which assumes GDP growth of 5.5 percent and an inflation rate of 4.1 percent, is 3 percent larger than that of 2000. In the banking sector, the largest of Estonia's six banks achieved positive financial results in 1999 and 2000. Finnish Sampo Finance's June 2000 agreement to purchase the Bank of Estonia's 58 percent shareholdings in Optiva Bank will leave the Bank of Estonia with no ownership interests in the country's commercial banks.

The upturn in the economy has also led to increased imports, a rise in the current account deficit, and a slight acceleration in inflation from 3.9 percent in 1999 to 4.1 percent as of July 2000. Unemployment levels remain high, which official statistics listed as 6.2 percent in September 2000. More accurate labor force surveys put the number at more than 13 percent in the second quarter of 2000.

While grappling with the effects of the Asian and Russian crises, Estonia's government has focused during the last few years on preparations for EU membership. In the economic sector, this has meant ongoing efforts to bring national legislation and practices into harmony with EU directives in areas such as agricultural policy, energy production, customs administration, and the completion of pension, health care, and land reforms. Supporters of EU membership insist that Estonia's entry will produce positive effects on the country's future development, including improved administrative procedures, better quality control through stricter regulations, and even greater attractiveness for foreign investors. Estonia applied for EU membership in 1995 and began accession negotiations in March 1998. By mid-2000, Estonia had closed 13 of the 31 negotiation chapters of EU regulations with which applicant countries must comply to qualify for membership. Compared to the other Central and Eastern European candidates, Estonia has proceeded the most rapidly with its membership talks.

While much has been written about the potential benefits of belonging to the EU, the possible negative consequences of Estonia's membership have received less attention. The need to comply with EU standards in areas such as infrastructure and environmental upgrading will increase government expenditures, at least in the short term. While Estonia's current trade policies are governed by agreements with countries on an individual basis, EU regulations specify which EU member states are allowable export destinations for Estonian goods. While a number of trade concessions have been addressed in the accession negotiations, trade issues will remain relevant because Estonia's main trading partners are EU countries. The country's struggling agricultural sector will face particularly significant repercussions such as greater impediments to sending goods to EU and other markets. Ironically, the Estonian government's earlier tariff-free policy, which international organizations

and Western governments praised, has been amended to meet the EU's strict membership criteria. Specifically, Estonia introduced customs tariffs on agricultural products from non-EU countries and from countries with which Estonia does not have free trade agreements.

During the last several years, Estonia's government has advocated EU membership for economic and political. Many regard entry into the EU as yet another step along the road back to the "community of European nations," as well as a necessary precursor to NATO membership. However, others have argued that Estonia's government has pursued various policy changes necessary for EU accession too rapidly and without sufficiently considering the possible negative effects. While successive governments have continued to push for EU membership, public support declined from 52 percent in January to 43 percent in October 2000. According to one recent poll, 73 percent of those surveyed believe that EU membership will have a negative effect on consumer prices; 41 percent believe that membership will make it more difficult to reduce unemployment.

By 1998, Estonia had largely completed its rapid and comprehensive privatization program, which involved the purchase and sale of vouchers on secondary markets with listed prices. The private sector now generates approximately 70 percent of the country's GDP. Despite such impressive achievements, the last phase of the privatization process, i.e., the sale and subsequent modernization of the few remaining large infrastructure and energy enterprises to conform to EU requirements, has met with considerable difficulties. For example, after negotiations for the sale of the national freight carrier Eesti Raudtee were criticized for having taken several years, the ruling coalition's election promise in March 1999 to privatize the railroad by the end of May renewed what soon became a stalled

process. In April 2000, the government announced plans to sell 66 percent of Eesti Raudtee to a strategic investor who will undertake a much needed modernization program. Likewise, the privatization of the national power utility Eesti Energia has been fraught with political battles. Successive governments have negotiated with the U.S.-based NRG Energy for nearly five years about a partial sell-off of the firm. But Estonia's president, opposition parties, business leaders, and the management of Eesti Energia oppose the plan because they fear, among other things, higher energy prices. Nevertheless, an agreement was signed on August 25, 2000, for the sale of a 49 percent government stake in two Narva power plants that supply more than 90 percent of the country's electricity.

In contrast to the relatively quick progress made in Estonia's economic sector, reforms in the country's social sector generally have proceeded more slowly. However, certain EU requirements combined with the country's declining birth rates and general aging of the population are creating a growing sense of urgency about pension and health care reforms. Estonia has started the gradual implementation of a three-pillar pension system that includes a pay-as-you-go system, a fully-funded contribution program, and a voluntarily funded scheme. Implementation of the second pillar has proven especially problematic because the idea of mandatory employer and employee contributions has not gained widespread acceptance. In the health sector, improvements in overall efficiency and financing policies will supplement earlier reforms in primary care.

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