

BTI 2008 | Estonia Country Report

Status Index	1-10	9.42	# 3 of 125	
Democracy	1-10	9.55	# 3 of 125	➔
Market Economy	1-10	9.29	# 3 of 125	➔
Management Index	1-10	7.37	# 2 of 125	

scale: 1 (lowest) to 10 (highest) score rank trend

This report is part of the Bertelsmann Transformation Index (BTI) 2008. The BTI is a global ranking of transition processes in which the state of democracy and market economic systems as well as the quality of political management in 125 transformation and developing countries are evaluated.

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Key Indicators

Population	mn.	1.3	HDI	0.86	GDP p.c.	\$	13,770
Pop. growth ¹	% p.a.	-0.2	HDI rank of 177	40	Gini Index		35.8
Life expectancy	years	73	UN Education Index	0.97	Poverty ³	%	7.5
Urban population	%	69.1	Gender equality ²	0.61	Aid per capita	\$..

Sources: UNDP, Human Development Report 2006 | The World Bank, World Development Indicators 2007 | OECD Development Assistance Committee 2006. Footnotes: (1) Average annual growth rate 1990-2005. (2) Gender Empowerment Measure (GEM). (3) Percentage of population living on less than \$2 a day.

Executive Summary

Since EU accession in 2004, Estonia has entered a new development and transformation phase in which democracy has been fully consolidated, but there is a sense of public alienation from politics and diminished responsiveness among the political elite. Economic transition has brought tremendous growth and improved living standards to Estonia, but a new development model is needed to ensure that progress continues. For Estonia, the period under review has represented a respite from the intense period of change prior to accession. During this period of relative calm, political and economic divisions have solidified as five major political parties consolidated a relatively secure grip over the electorate and interest groups. The ability among political actors to compromise has grown considerably, but short-term expediency in terms of political decision-making still arises. As parties bid to build their own fiefdoms within administrative structures, the civil service has become increasingly politicized. Public outcry over such trends, however, has rarely evoked any response.

Estonia's initial phase of post-communist market transition has come to an end during the review period. The rapid growth associated with privatization, foreign investment and low production costs may not be sustainable as new challenges have emerged, such as the need to shift toward a knowledge-based economy and develop value-added industries. Individual sectors such as biotechnology and computer programming have taken the lead here while the country grapples with the question of whether the state should influence these processes more noticeably or continue a policy of free market liberalism. EU membership has not changed dramatically Estonians' view of themselves or of the world. Although discussed a great deal before accession, euroskepticism actually proved to be indifference rather than opposition to the European Union. In geopolitical terms, the European Union was primarily seen as an

effective bulwark against Russian influence. Relations with Moscow have remained poor, which limits Estonia's ability to serve as a European bridge to Russia. These problems have run parallel to the challenge of improving social integration between Estonians and Russophones in the country. In 2007, the Estonian government completed an expensive seven-year minority integration program aimed at Estonian language training and educational reform. However, very little progress was made in reducing socioeconomic and political disparities between the two ethnic groups.

History and Characteristics of Transformation

The beginning of Estonia's economic and political transformation coincided with Gorbachev's perestroika and glasnost policies. Whereas the Communist Party of Estonia and the government resisted Moscow's reform tendencies, local leaders used perestroika and glasnost policies to mobilize the population on a range of issues, including Russification, industrial pollution, the constant influx of Russian workers and economic degradation. Overall, although economic and democratic considerations did play a role, transformation actually started as a movement for Estonian state and nation-building. Some steps were taken toward democratization and economic liberalization in the late 1980s, but transformation began in earnest with the declaration to initiate a process of independence (30 March 1990) and the actual restoration of Estonian independence (20 August 1991).

Democratic transformation was characterized by an ideology known as legal restoration, which declared the independence process not as the beginning of a new era of statehood, but rather as a restoration of the same statehood and legal continuity of the pre-1940 republic. Since this legitimized the new institutional setup as a return to the well-functioning pre-war parliamentary system that had existed prior to the shift to authoritarianism in 1934, the country benefited from quickly establishing institutions and procedures with a high degree of legitimacy and consolidation. At the same time, because of this restorationist approach, all post-1940 immigrants (mostly Russophones) were excluded from citizenship and democratic participation unless they were naturalized. Likewise, economic transformation policies referred to the liberal market economy of the interwar period. However, restorationist policies were never implemented against the logic of the market, with the exception of some property restitutions. Whereas Soviet-era heavy industry was largely abandoned (with the exception of oil shale), export-oriented service industries, biotechnology and IT industries were strongly promoted. As a result, the small country soon reached a critical mass of economic development, though it was concentrated in certain sectors, and regions or cities. In hindsight, there have been two related key assets in Estonia's transition management, namely a unique sense of determination and purpose, and the political courage and readiness to take innovative approaches. The national consensus

on transition to some extent excluded the Russian minority and was partly a reaction to Russian obstruction (locally and internationally). Despite the perceived restoration of a pre-Soviet Estonia, most policies have been remarkably innovative and forward-looking. Estonia began tackling “post-modern” developments and phenomena such as democratic apathy, European Union skepticism, de-industrialization, globalization and an aging population earlier than most other post-communist countries. At the same time, civic participation, regional policy and ethno-politics have lagged behind.

Transformation Status

I. Democracy

1 | Stateness

Estonia is a stable country with full state control over the entire national territory. The country's main regional cleavage concerns the northeast of the country, where a majority of the Russian-speaking minority population lives. The main city on the border with Russia, Narva, has a population of 70,000 and is 95% Russian. The surrounding Ida-Viru county has a population of some 175,000, of which 71% are Russian. During the early 1990s, when tensions were high over such questions as citizenship and minority rights, a number of ex-communist Russian leaders attempted to raise the prospect of possible secession to Russia. These efforts dissipated, however, after a dubiously organized referendum on the issue was declared unconstitutional by the Estonian Supreme Court.

Monopoly on the use of force

Citizenship has been a highly contested issue in Estonia. When the restorationist doctrine of statehood was applied to citizenship, Estonia was suddenly left with some 400,000 "non-citizens" out of a total population of 1.4 million. Although around 85,000 of these people eventually became citizens of the Russian Federation and received permanent residency permits to live in Estonia, another 170,000 did not choose any citizenship, essentially becoming stateless persons. Only around 100,000 people decided to become naturalized Estonian citizens by passing a modest language and civics test. The remainder left Estonia. Because Estonia was approximately 95% ethnic Estonian in 1945 and the vast majority of postwar settlers were Russian, Estonians now make up only 68% of the population although they constitute 84% of the citizenry. Moreover, only 40% of the Russian minority community in Estonia today are citizens. As a result, the citizenship policy has been widely seen as not only exclusionary, but also ethnically discriminatory. It has had a profound effect on reducing ethnic Russian political representation in Estonia, since only citizens can vote in national elections, although non-citizens with permanent residency are allowed to vote in municipal elections. This has therefore also greatly diminished the sense of legitimacy of the Estonian state among many Russians, even though citizens and

State identity

permanent residents are equally eligible for all social welfare benefits. Since 2000, the Estonian government has undertaken a number of measures to encourage the country's non-citizens to be naturalized as Estonian citizens. This has been part of a broader integration program aimed at building greater inclusiveness. To date, however, the results have been only modest. During 2004 and 2005, the number of naturalizations per year rose to around 7000, but this was still low considering that some 136,000 stateless people were still living in Estonia in 2006.

Although Estonia has two main religious denominations, Lutheranism and Russian Orthodoxy, the state is entirely secular and is not defined by any religious dogmas. No religious parties have ever been represented in parliament. In 1998, a Christian People's Party was founded, however, it has never won more than 2% of the vote in parliamentary elections. In a 2005 public opinion survey conducted by the University of Tartu, 73% of respondents agreed with the statement that church leaders should not influence government decisions. Less than 20% agreed with the notion that a politician who does not believe in God should not be in government service. Despite public outcry over lacking ethics in public administration and corruption, there has been no shift toward greater religiosity in politics.

No interference
of religious
dogmas

Estonia has a differentiated administrative structure throughout the country, including a multi-tiered court system, extensive regional government and effective tax collection.

Basic
administration

2 | Political Participation

Estonia's basic political course is determined by periodic free and fair elections. The parliament is elected every four years using a system of proportional representation. Municipal elections are held every three years. The parliament has seen five election years (1992, 1995, 1999, 2003 and 2007). Municipal elections have also been held five times (1993, 1996, 1999, 2002, 2005). No major controversies have erupted during any of these elections. All citizens 18 years of age and older may vote. However, given Estonia's particular citizenship policy, only 80% of the voting-age population are actually citizens. Thus, the officially eligible voting population amounts to roughly 860,000 people. Non-citizens can, however, vote in municipal elections, raising the number of voters in that case to 1,050,000.

Free and fair
elections

Estonia's elected rulers have the effective power to govern, and this is based on a well-balanced constitution and effective state administration. While the prime minister is nominated by the president, he/she is appointed to office by the parliament and is ultimately accountable to the legislature. There are no veto

Effective power
to govern

players outside the constitutional system. Therefore, the ability of government leaders to rule autonomously is limited only by the influence of key business elites, such as industrialists or transit-trade oligarchs. In recent years and as political parties and a class of business elites in Estonia have consolidated, they have also established tighter links to one other. In 2005 and 2006, the relationship between the Center Party (Estonia's largest) and a key food industry magnate, Oliver Kruuda, received extensive coverage in the press. One report described a scheme in which one of Kruuda's companies, the chocolate maker Kalev, sponsored a series of advertisements right before municipal elections in October 2005. The advertisements were ostensibly for a new milk treat the company was introducing, but bore a suspicious resemblance to the Center Party logo and campaign slogans. The advertisements were controversial, since by law, all outside advertising for political parties was to have ended by then. The move was seen as a sly attempt by the party to circumvent campaigning laws with the help of a major businessman.

Freedom of association and assembly is unrestricted within the basic democratic order. Civil society in Estonia is uninhibited, and laws regulate the creation of NGOs and other free associations.

Association /
assembly rights

Freedom of expression is guaranteed by the Estonian Constitution and is buttressed both by additional legislation and an extensive mass media, including both Estonian- and Russian-language outlets. Since regaining independence in 1991, Estonia's media have undergone a cycle of diversification and consolidation. Whereas in the mid-1990s there were as many as five Estonian-language national dailies, this number has now been reduced to just two mainstream papers and one tabloid. At the same time, foreign ownership of the media has increased, with the Norwegian company Schibsted and the Swedish firm Bonnier holding controlling stakes in the national daily Postimees and the business daily Äripäev respectively. An Estonian company, Ekspress Grupp, controls the daily Eesti Päevaleht and 50% of the tabloid SL-Ohtuleht (alongside Schibsted, which also has 50%). The Russian-language press has undergone even greater consolidation. In December 2006, the most popular Russian-language daily, Vesti Dnja, was bought up by a non-profit foundation linked to the Center Party, which raised questions about increasing party influence over the media. The debate was accentuated by a simultaneous proposal in parliament to reorganize the composition of Estonia's public broadcasting board (which governs state television and radio) to include only members of parliament and exclude independent media experts who had previously been appointed to the board. None of these moves represented a direct restriction of press freedom, but they did point to a narrowing of the media space. In recent years, Internet websites have also become a very popular forum for all kinds of discussions. In the beginning, such forums were open to all computer users and to all opinions.

Freedom of
expression

Gradually, however, many online newspapers and public affairs forums (such as a popular site called “Delfi”) began to require that participants register. In June 2006, moreover, the Estonian parliament passed a law making it a criminal offense to post opinions that incite hatred, violence or discrimination and that threaten the life, health or property of others. The law was seen by some as a restriction of free speech, but was initiated by Justice Minister Rein Lang, a former media operator and member of the liberal Reform Party. To date, no criminal cases have been brought under the new law.

3 | Rule of Law

The Estonian constitutional system established in 1992 represents a careful balance between parliament, the government (headed by a prime minister) and the president. Similar to a classical parliamentary democracy, the prime minister depends on legislative support to remain in office; both the prime minister and individual ministers can be removed by parliament with a vote of no confidence. Alongside these institutions, however, Estonia also has a president who is elected either by parliament or a special electoral college. Although the president’s duties are mostly ceremonial (such as promulgating laws), he can veto legislation if he believes an act is fundamentally unconstitutional. Furthermore, Estonia has a legal chancellor who likewise monitors the constitutionality of all legal acts in Estonia. The legal chancellor has proven to be a very influential institution, often called upon by other branches of government to provide expert opinion in cases of institutional disputes. This has further helped maintain the balance of power. Lastly, in 2002, the Supreme Court was given the formal power (hitherto not foreseen in the constitution or regular law) to rule in disputes over whether to declare a high state official (e.g., the president or the legal chancellor) unable to perform his or her duties. In 2005, a more specific balance-of-power controversy was resolved when the Supreme Court ruled that members of parliament would no longer be able to simultaneously sit on municipal councils. Similar to the question of *cumul de mandats* in France, a number of major political parties defended the policy as a necessary link between national and local politics, while others decried it as enfeebling local government. In June, parliament passed an amendment allowing parliamentarians to occupy seats at both levels. President Arnold Rüütel vetoed the amendment, arguing that such double representation violated the principle of separation of powers. When the parliament overrode Rüütel’s veto, the president appealed the law to the Supreme Court. The court delayed its decision until just two days before local elections took place on 16 October, but eventually ruled in Rüütel’s favor.

Separation of
powers

Estonia has an independent judiciary with a three-tiered system. The first tier involves county courts and administrative courts. The former hear all civil,

Independent
judiciary

criminal and misdemeanor matters, the latter all administrative disputes. At the second level, circuit courts hear all appeals lodged against county and administrative courts. At the third level, the Supreme Court hears all final appeals, but also serves as Estonia's Constitutional Court. Specifically, the Court has a nine-member subdivision called the Constitutional Review Chamber, which reviews all appeals filed on constitutional grounds. Appeals can be brought by the lower courts, the legal chancellor or the president. This judicial review process has been highly effective, producing over 150 rulings since 1993. After 2002, the Chamber was also given the task of adjudicating electoral disputes (usually protests from individual candidates). This has caused a near doubling of the Chamber's workload. It has also made electoral politics more fair, however. In particular, the Chamber was called on in September 2006 to review the decisions of Estonia's National Electoral Commission to refuse the registration of two delegates elected to the presidential electoral college. Because President Toomas Hendrik Ilves won that election by just one vote, the Chamber's ruling appeared crucial. In the event, the Chamber reinstated only one of the disputed delegates, thereby sustaining the electoral outcome indirectly. In no instance has the Chamber's decision been seen as illegitimate or been challenged by any political party or institution.

Estonia has generally been free of large-scale corruption and has consistently scored very well on Transparency International's Corruption Perceptions Index. In 2006, it ranked 24th in the world and was the best-placed country in all of Central and Eastern Europe. The country has an Anti-Corruption Act as well as numerous other laws regulating public transactions, public property administration and civil service ethics. At the same time, few corrupt high-level officeholders have been prosecuted despite extensive media coverage. Following the disclosure in August 2005 that the prominent food industry magnate, Oliver Kruuda, had sold a seaside summer home to the Center Party leader Edgar Savisaar for less than a quarter of its market value, Prime Minister Andrus Ansip came under heavy public pressure to force Savisaar to resign. Ansip refused, however, claiming that any accusations of buying favors would first have to be proven by criminal investigators. A year later, the Estonian State Prosecutor's Office issued a report confirming that Savisaar had obtained the property at a significant discount, but that because Kruuda had not suffered a loss as part of his overall development of that resort area, neither party could be accused of wrongdoing. Eventually, such controversies led to the coining of a new buzzword in Estonian, "jokk," representing the first letters of the Estonian-language sentence "legally everything is correct" ("juriidiliselt on kõik korrektne"). This was the kind of defensive answer given by many officials and politicians when questionable dealings, such as those of Savisaar, were revealed. In legal terms, the transactions were all above board. In ethical terms, however, they generated much controversy. In December 2006, the Social Democratic Party opted to make

Prosecution of
office abuse

the buzzword one of its campaign slogans for the March 2007 parliamentary elections. The party promised to end “jokk” if elected. But the success of this appeal was rather mixed; the party placed fourth in the election.

Civil rights are well protected in Estonia. Paragraphs 13-16 of the Estonian Constitution enshrine the right to life and oblige the state to enforce this right as well as offer all individuals recourse to the courts. All essential civil rights are also protected explicitly and equally for citizens and non-citizens. In March 2005, a new State Legal Aid Act came into force, offering free legal advice and court representation for those who do not have the financial means. The act also offers monetary support to NGOs that provide free legal services to the public. At the same time, human rights groups have criticized the law for allowing the state to demand reimbursement of these aid costs if the plaintiff loses the case.

Civil rights

4 | Stability of Democratic Institutions

As a rule, political decisions in Estonia are prepared, implemented and reviewed in legitimate procedures by the appropriate authorities. Accession to the European Union represented a major test in this respect, as the country studied, debated, adopted and began to implement the European Union’s *acquis communautaire*. One issue that raised considerable institutional friction, however, concerned the enforcement of an EU rule regarding the amount of sugar that could be stocked in a country at the time of accession. In May 2004, when Estonia joined the European Union, it had exceeded its allotted quota by 90,000 tons. As a result, the European Union levied a fine of more than €45 million on Estonia in November 2006. The incident quickly became a political scandal, as different ministers responsible for this domain (agriculture, economics, finance) attempted to assign blame to others. An investigation by the national auditor revealed that a lack of effective coordination among different government agencies was the prime cause for the debacle.

Performance of democratic institutions

The legitimacy of democratic institutions in Estonia is not contested. Controversial presidential vetoes or Supreme Court decisions have all been accepted by the relevant political and social players.

Commitment to democratic institutions

5 | Political and Social Integration

Estonia’s party system can be considered stable, moderate and socially rooted. If during the mid-1990s the number of effective parties in parliament was 8.3, by 2007 this figure had dropped to 4.4. The party system has consolidated to near five major parties, each more or less propagating a different political-ideological orientation. Occupying the conservative-nationalist wing were the Pro Patria and

Party system

Res Publica Union. The two parties were separate until May 2006, when they announced a merger. Res Publica had been the major victor of elections in 2003 because it was a new party that had grown out of a conservative political club with the same name. It became the lead party in government with its leader, Juhan Parts, serving as prime minister from 2003 to 2005. However, after the party's popularity plummeted from 25% to just 5%, Parts resigned and the party decided to merge with its closest ally, the Pro Patria Union. Next on the right-left scale is the pro-market liberal Reform Party, which consistently propagates low taxes and minimal government intervention. Its election performance has been one of the most consistent, traditionally winning 15-18% of the vote, though it rose to 28% in 2007. In the political center are the Social Democrats, known for many years as the Moderates. The name change came in 2004 in an effort to project a stronger center-left image. However, the party continued to attract roughly 10% in the polls. Among rural and agrarian voters the People's Union is the strongest, with a consistent vote share of around 13%, although this fell to 7% in 2007. The Center Party is the most popular among lower-class voters and pensioners. The Center Party has long been considered Estonia's strongest party, with a vote share in 2007 of 26% and the largest number of members. In this respect, the socioeconomic profiles of each party are generally known, and a 2005 survey conducted by the University of Tartu also showed that voters rank the parties on a right-left scale roughly in the same order. The parties' linkages with civil society are mixed in the sense that proportionally, a very large number of Estonians (over 5% of the eligible voters) belong to political parties. In large part this is due to Estonian party law that requires parties to have at least 1000 members in order to be registered. Indeed, the biggest parties, such as the Center Party or the People's Union, boast over 10,000 members, while other major parties total around 5000. In addition, a generous system of state financing for parliamentary parties (roughly €4 million a year distributed proportionally according to electoral strength) allows parties to create extensive local networks and support youth and women's committees. In an effort to stem the influence of big business in politics, parliament also banned corporate donations to political parties in 2004. Parties are required to submit quarterly financial reports detailing all of their income. In practice, however, these measures still leave many questions unresolved, since huge contributions are often made by single individuals whose regular income could not possibly support such large donations. In 2004, the Center Party also came under scrutiny for having issued €640,000 in promissory notes to unknown supporters. The suspicion was that this loan would never be paid back and was just a veiled contribution.

Estonia's network of interest groups and cooperative associations is relatively well organized with a number of umbrella organizations covering different civil society sectors or fields. The Roundtable of Estonian Non-Profit Organizations was created in 2000 as a central forum for discussing major issues relating to the

Interest groups

non-profit sector. In addition to having a regular general assembly, the Roundtable has six different chambers, which group similar organizations such as foundations, informal societies, minority associations or youth organizations. The Roundtable was active not only in the adoption of the Estonian Civil Society Development Concept in 2002, but also in its implementation by organizing the joint state-NGO commission that reviews progress in the field. The Network of Estonian Non-Profit Organizations works specifically for its roughly 80 member organizations, including major grant-giving foundations and regional societies. There are therefore strong networks between organizations and between the non-profit sector and the state. However, third-sector groups regularly complain that, in reality, cooperation with actual government officials is often difficult. Some consultative mechanisms have been created whereby ministries can disseminate policy proposals to interested groups for comment and discussion. However, such comments are not always taken into consideration and decisions are often still made without consultation.

Estonia also has a tradition of tripartite negotiations between the state, trade unions and employers. The talks, however, are not institutionalized by law, and have therefore broken down at different points in time. In recent years, the trade unions (represented by the Confederation of Estonian Trade Unions) and employers (represented by the Estonian Employers' Confederation) have reached their own bilateral wage agreements, which the state has then enacted into law. In November 2006, the Estonian media profiled an American white supremacist, Craig Cobb, who had moved to Estonia to start a new movement. Few details were given of any organized activity, but the Estonian Security Police Board estimated that the number of right-wing skinheads was less than 100 in 2004 and that no European right-wing organization had been able to establish any firm connections in Estonia. The board expressed much greater concern about the activities of numerous Russian minority organizations, which it alleged were actively tied to the Russian Federation Embassy in Estonia and therefore tools of Russian foreign policy used to discredit Estonia and to maintain a degree of influence over Russian "co-nationals" in Estonia. Few cross-ethnic, explicitly Estonian-Russian civil society organizations exist.

Popular consent to democracy is high, although satisfaction with how Estonian democracy is performing is mixed. Surveys in 2004 and 2005 conducted by the University of Tartu showed that when people were asked whether they thought things would be better if the country had one strong leader who did not need to reckon with a parliament or political parties, a strong majority of 60% disagreed. Still, 35% agreed with the statement and only 5% were undecided. Likewise, only 35% of respondents were satisfied or very satisfied with the performance of democracy in Estonia, while nearly 60% were dissatisfied. Admittedly, these numbers have not changed very much since the mid-1990s. In addition, no

Consent to
democratic
norms

political protests have ever called Estonia's democratic constitutional framework into question. However, a certain degree of political alienation is reflected in the relatively low electoral turnouts. In 2003, only 58% of eligible voters participated in parliamentary elections. In 2007, this number rose only slightly to 61%.

As in many post-communist countries, social self-organization in Estonia has been greatly weakened by five decades of totalitarian rule. In addition, Estonians generally have an image of themselves as very individualistic and averse to collectivist undertakings. Thus, while roughly 50% of respondents in a 2005 University of Tartu survey said that most people can be trusted, a much larger majority of 65% agreed with the statement that people cooperate only when they stand to gain personally, and 81% believed that if person does not stand up for himself, others are likely to take advantage of him for their own gain. On a very practical level, however, post-communism also had a positive effect on self-organization in that the total privatization of state-controlled housing during the mid-1990s actually spurred the creation of over 8,000 independent apartment cooperatives across the country. A hallmark of Soviet rule in Estonia had been the construction of hundreds of gray, pre-fabricated concrete apartment buildings. Yet when Estonia embarked on its ambitious housing privatization program, part of the plan was that the new apartment owners in each building would be forced to come together and form a cooperative to manage their common affairs. Since 75% of Estonians lived in such apartments at the time, some three-quarters of the population were suddenly involved in building a cooperative organization from the bottom up. For the most part, these cooperatives were successful, with several hundred applying for commercial bank loans in order to carry out structural renovations and other improvements on their buildings. Although obviously not all apartment owners were active in their cooperative (especially since apartments were also bought and sold very often), it was an early lesson in democracy and cooperation for many people.

Associational
activities

II. Market Economy

6 | Level of Socioeconomic Development

Thanks to economic growth rates averaging around 6% over the last 10 years, Estonia has risen considerably in terms of socioeconomic development. From a Human Development Index score of 0.793 in 1995, the country rose to 0.858 in 2004 and was ranked 40th in the world. The percentage of individuals living in

Socioeconomic
barriers

absolute poverty (as measured by statisticians at the University of Tartu) also declined dramatically from 37.3% in 1997 to 17% in 2004. The percentage of people living on \$1 a day between 1990 and 2004 was just 2%. At the same time, Estonia's Gini index, 37.2 in 2004, was high compared to the rest of the region. Latvia and Lithuania had scores of 33.6 and 31.9 respectively, while Finland's score was just 26.9. In particular, economic development in Estonia varies according to region and ethnicity. Average personal incomes in the capital Tallinn and surrounding Harju county are generally twice what they were in southeastern and northeastern Estonia. Russians consistently make up a higher than proportional share of the unemployed and generally have lower average incomes given similar education levels. In part, these disparities are due to structural changes in the economy. During the Soviet era, Russians were mostly employed in industry or in the transport sectors, which were transformed radically following privatization and market transition. Poor Estonian-language skills among Russians have also disadvantaged them on the labor market. In this respect, their privation has been relative, not absolute.

Economic indicators		2002	2003	2004	2005
GDP	\$ mn.	7,041	9,190	11,239	13,101
Growth of GDP	%	7.2	6.7	7.8	9.8
Inflation (CPI)	%	3.6	1.3	3	4.1
Unemployment	%	10.3	10.0	9.6	-
Foreign direct investment	% of GDP	4.0	10.0	8.7	22.9
Export growth	%	0.8	5.8	16	21.3
Import growth	%	3.8	10.6	14.6	17.4
Current account balance	\$ mn.	-779.3	-1115.4	-1457.6	-1444.9
Public debt	\$ mn.	481.7	560.1	561.8	434.7
External debt	\$ mn.	4,740.7	6,972.4	10,008.2	11,255.0
External debt service	% of GNI	11.7	14.1	13.7	12.8
Cash surplus or deficit	% of GDP	1.0	2.5	2.7	-
Tax Revenue	% of GDP	16.8	17.3	17	-
Government consumption	% of GDP	19.2	19.4	19.0	18.3
Public expnd. on edu.	% of GDP	5.7	5.7	-	-

		2002	2003	2004	2005
Public expnd. on health	% of GDP	3.8	3.9	4.0	-
R&D expenditure	% of GDP	0.8	0.8	0.9	-
Military expenditure	% of GDP	1.7	1.9	1.8	1.5

Sources: The World Bank, World Development Indicators 2007 | UNESCO Institute for Statistics | Stockholm International Peace Research Institute (SIPRI), Yearbook: Armaments, Disarmament and International Security

7 | Organization of the Market and Competition

Since its enactment of wide-ranging economic reforms in the early 1990s, Estonia has gained a reputation of being a market-driven economy with high levels of economic freedom. Trade and prices were among the first things to be liberalized. Foreign investment was also opened up rapidly in tandem with a large-scale privatization program carried out in the 1990s. There are equal opportunities for all market participants, and profits may be used and transferred freely. The currency, the kroon, was introduced in June 1992 and was first pegged to the German mark, later to the euro. As a result, Estonia has enjoyed a stable currency throughout its economic transformation.

Market-based competition

Estonia has a competition board, whose central function is to enforce the Competition Act as amended in 2006. The board has three departments that are tasked with monitoring different sectors of the economy, and there is also a department that examines company mergers. The Competition Act lays out the criteria for establishing whether a company occupies a “dominant position” on the market or is involved in a market concentration, thus bringing it under particular board scrutiny. The board can summon individuals, request relevant information as well as conduct on-site inspections. Following European Union accession, the competition board expanded its activities to assess competition issues in a European context. In 2006, together with its Finnish and Swedish colleagues, the board reviewed the purchase of the Swedish cruise ship company Silja Line by the Estonian company Tallink to determine whether the deal constituted a concentration of cruise ship services in the hands of one company.

Anti-monopoly policy

Estonia’s foreign trade regulation complies with both European Union and WTO requirements. Liberalization of foreign trade was one of the first reform measures adopted after market transition began in 1992. Export and import tariffs were abolished and the Estonian market was immediately subjected to open foreign competition.

Liberalization of foreign trade

Estonia's banking system and capital markets have been thoroughly internationalized, thus ensuring both international standards and sufficient resilience to cope with speculative investment. The country's two main banks, Ühispank and Hansapank, are owned by the Swedish giants SEB and Swedbank respectively. The Finnish bank Nordea also has a strong presence. The Bank of Estonia maintains oversight over commercial banks, setting minimum capital requirements and other regulations. In 1995, the Tallinn Stock Exchange was established with its own index, TALSE. In 2001-2002 the company was integrated with the Helsinki Stock Exchange, and in 2004, the exchange became part of the OMX group covering all of the Nordic and Baltic states.

Banking system

8 | Currency and Price Stability

Following a period of rampant inflation that accompanied market transition in the early 1990s, by 1999, the consumer price index was just 3.3% as Estonia settled into moderate rates of price growth. Since then, inflation has averaged 3.8% according to the Bank of Estonia. However, these numbers have still been too high to qualify Estonia for euro zone membership. Indeed, citing continuing future strong economic growth and the likelihood that this will keep inflation above the EU minimum, the Estonian government and Bank of Estonia announced in late 2006 that they do not expect the country to be able to introduce the euro until 2010 at the earliest. This is in line with a majority of other Central and Eastern European countries, but it was a blow for Estonia, which had hoped to be among the first new euro users. On a practical level, the delayed introduction of the currency is not such a problem. Since 1992, the Estonian kroon has been pegged, first to the deutsche mark, later to the euro. The exchange rate has remained the same, at 15.6466 kroon to the euro.

Anti-inflation /
forex policy

Estonia's fiscal policy since independence has been very solid, consistently operating balanced budgets and, in recent years, considerable surpluses. A constitutional provision mandates that all amendments made to the state budget must be offset by revenue calculations ensuring that the changes do not generate extra expenditure. In addition, balanced budgets have become a hallmark of both the parliament and the Ministry of Finance, which is charged with drafting the document.

Macrostability

9 | Private Property

At a very early stage in its transition, Estonia established the framework conditions for private property in a market economy. State intervention in private property is not only regulated by law; Estonia has also developed a strong culture of property rights. This culture has also been fostered by an extensive program of

Property rights

property restitution, returning or compensating for property nationalized by the Soviets in 1940. For many, this was an issue of honoring the sanctity of private property.

Large-scale privatization was carried out during the 1990s in Estonia. By the time Estonia entered the European Union in 2004, only small portions of the country's infrastructure, such as the electricity plants and water companies, were still in government hands. The EBRD's rating for large- and small-scale privatization for Estonia was 4 and 4.3 respectively. In 2006, the Estonian government decided to buy back Estonian Railways from the consortium of investors who had privatized it in 2001. However, this was primarily due to disputes over how the investors had allegedly managed the enterprise. In 2006, the EBRD reported that the private-sector share of GDP in Estonia was 75%.

Private
enterprise

10 | Welfare Regime

In line with a neoliberal approach to economic transition, reform of the social security net in Estonia was not a priority in the early stages. Unemployment and pension reforms were enacted as late as 1998. In recent years, however, Estonia has bolstered its welfare regime by implementing a pension reform plan in 2001 and 2002 and enacting a generous system of parental leave benefits in 2004. The latter allows a parent to stay at home with a newborn child for up to 15 months and continue to receive his/her full salary.

Social safety nets

Compared to other European countries, Estonian traditions and the country's substantial progress toward a market economy have meant that gender and social background are not significant barriers to equality opportunity. In 2001, for instance, the mean school life expectancy for females was 14.6 years, one year more than the male average. Instead, regional disparities are substantial; the capital, the harbor cities on the Baltic Sea coast and the university city of Tartu have higher indicators than the rural and industrial periphery in the northeast and southeast. Access to higher education and high-quality employment is more limited in these regions.

Equal opportunity

11 | Economic Performance

Estonia's economic performance has been very strong, not only following its immediate market transition in the mid-1990s, but also in recent years as the country continues to benefit from high levels of foreign investment and relative export growth. Unemployment has declined so much that in many areas of the country, there is now talk of a labor shortage. Inflation has been commensurate with a growing economy. The current account deficit has remained high,

Output strength

constituting a worry for the future. In 2006, the IMF concluded that Estonia's external competitiveness was "adequate." Within Estonia, however, policymakers and analysts have begun to stress that the country needs to work harder to shift to a more knowledge-based and value-added economy in order to maintain its growth rates and expectations for the future.

12 | Sustainability

As the Estonian economy is increasingly service oriented and has a low population density, environmental concerns are of limited importance. Nonetheless, pollution is a serious problem in the restructuring of the old industrial Soviet-era industrial plants, predominantly located in the northeastern part of the country. The levels of environmental pollution and health risks are high, but some industrial activities are considered vital to the national economy, such as energy production from oil shale, which provides 90% of electricity and serves to reduce dependency on Russian energy resources. In addition, some of these industrial activities are considered vital to the socioeconomic survival of the northeast of Estonia, which has a large Russian minority population. However, air-borne sulfur dioxide pollution from oil-shale burning power plants has fallen steadily. Overall, the environment has profited from the significant decline of heavy industry production following transition as well as from improvements in agriculture and waste disposal. In many respects, the structural conflict between economic growth and environmental costs is not a major one in Estonia.

Environmental
policy

Estonia has a solid system of basic, secondary and tertiary education. The percentage of GDP spent on education has ranged between 6-7%, generally above the European Union average. As part of the European Union's goal to raise R&D spending to 3% of GDP by 2010, Estonia has also raised its figure from year to year. In 2006, however, Estonia had barely broken 1%.

Education policy
/ R&D

Transformation Management

I. Level of Difficulty

Constraints on governance capacity in Estonia are moderate to low, since strong economic growth has helped to reduce the threat from structural deficiencies such as poverty or severe infrastructural problems. Instead, one of the most talked about constraints for the future concerns a mounting labor shortage in Estonia and the possibility of importing foreign labor in a few years' time. Rising wage levels have reduced Estonia's competitiveness and are already prompting some foreign investors to shift their production to cheaper sites. Without continued investment based on a competitive labor market, Estonia faces the danger of a market slowdown in its economy and the concomitant political governance problems this would bring.

Structural
constraints

Estonia has a moderate tradition of civil society, which was weakened during the Soviet era, but has strengthened considerably over the last several years thanks to the adoption of the Estonian Civil Society Development Concept and other partnership programs. Outside of politics, growing numbers of organized hobby groups are also helping to build social capital and organizational skills. Generalized social trust remains comparatively low, and trust in political institutions also varies. However, none of these shortcomings constitutes a real constraint on state management.

Civil society
traditions

Ethnic cleavage in Estonian society probably constitutes the most serious challenge to political management. Although confrontation over issues such as citizenship or language rights has never turned violent, these questions continue to cause great apprehension among members of the Russian minority community. Russian political representation has been severely undercut by Estonia's restrictive citizenship policy. This has, in turn, reduced the degree to which Russian interests have been mobilized via political parties or pressure groups. It has even led a number of Russian politicians to join Estonian political parties instead and attempt to influence policy in this manner, but any real success has been limited.

Conflict intensity

II. Management Performance

14 | Steering Capability

The commitment of Estonia's political leadership to constitutional democracy and a socially responsible market economy has been steadfast throughout the period since independence. In large part, this has been driven by a strong desire among Estonian political elites to integrate the country securely into Western structures in order to reduce the risk of Estonia falling under Russian influence ever again. This geopolitical-cultural dimension of Estonia's development has been significant. Financially, Estonia's political leadership has also maintained a balanced budget, even undertaking severe austerity measures in 1999, when an economic slowdown threatened to cause deficits. Business policies, including investment and tax policies, have been consistently open.

Prioritization

Given the success of Estonia's early reforms in the 1990s, subsequent reform policy has been aimed at fine-tuning and deepening this progress. Large-scale pension reform was carried out in 2001 and 2002, creating a three-pillared system of state pensions, mandatory funded pension accounts and private supplementary pension accounts. The new system quickly proved very popular with the public. By the end of 2006, more than 500,000 had joined the second pillar of mandatory accounts, helping to set aside over €400 million in savings. Equally successful was the implementation of a new parental benefit system guaranteeing a parent who decides to stay home with a newborn child his or her previous salary for up to 15 months after the child's birth. Although the reform did not immediately reverse Estonia's negative population growth, it did produce an initial increase in births in 2006. One unsuccessful reform involved an attempt to carry out local government reform under Mart Laar's second government (1999 – 2001). The prime minister appointed a special minister to draft the reform, and long discussions were held about how best to scale down the existing number of roughly 250 local governments to a more reasonable 100 or even less. While the debates did yield many ideas on how to streamline bureaucracy between the state and municipalities, the actual impetus for reform petered out when members of the governing coalition shifted their interests and began to neglect the issue.

Implementation

While Estonia became known as an enthusiastic privatizer of state assets in the 1990s, it also came to learn the limits of privatization, particularly in the area of

Policy learning

large-scale infrastructure. During the second half of the 1990s, the government carried out a long series of negotiations with an American energy corporation, NRG Energy, about the possible sale of Estonia's two major electricity plants located in the northeastern city of Narva. The deal would have been Estonia's largest ever privatization venture and would have involved long-term consequences for Estonia's electricity market. In addition, the sale would have had major geopolitical implications, placing the United States at the top of the list of foreign investors in Estonia. When a preliminary contract was signed in August 2000, however, opposition parties began to campaign against the agreement, eventually collecting over 160,000 signatures in protest. Although there were several reasons for the government's subsequent fall in January 2002, one of its last decisions was to renounce the NRG deal, thus keeping the power plants in state hands. Similarly corrective in nature was a 2005 government decision to begin negotiations concerning the buyback of Estonian Railways, privatized in 2001 to a group of Estonian and American investors. The Estonian railway inspectorate had long raised suspicions that the private owners had not lived up to investment commitments made as part of the final deal. In addition, the inspectorate had safety concerns following the introduction of two dozen extra-heavy American model engines on the rails. When Economics Minister Edgar Savisaar threatened to use these charges to abrogate the privatization agreement and forcibly seek return of the railways, the owners agreed to enter into talks about selling back the company. The final sale price of over €150 million was more than twice what the investors had paid in 2001, and in this respect, it was a major loss for the Estonian state. However, the re-establishment of government control over the railways would hopefully lead to better use of European Union structural funds to modernize the tracks and improve train services.

15 | Resource Efficiency

Estonia's small population obliges the country to make maximum use of the available economic and human resources. The fact that Estonia was able to cope with the full process of European Union accession was a testament to its capacity to organize personnel, budget resources and administrative hierarchies. While much of this practice has remained in place, there is an increasing danger of politically motivated dismissals and an undermining of long-term efficiency. Whereas in the mid-1990s there was an agreement that the top civil servant or secretary general in each ministry would be an apolitical post and that each minister would respect the secretary general in office, new ministers taking office since 2003 have often brought their own staffs and forced the resignation of their secretaries general. More broadly, parties have begun to pressure ministerial officials to join their party and have increasingly hired new staff only

Efficient use of
assets

from their own party. The term "participation" has become widespread in Estonian political terminology. During Estonia's accession to the European Union, an oft-cited critique of the country concerned a lack of administrative capacity to implement and enforce all aspects of the *acquis communautaire*. Although this did not ultimately affect Estonia's entry, it did highlight the fact that as a small country, Estonia often lacks all of the specialists and administrators it would need to manage all aspects of governance. More recently, this deficiency began affecting the police, border administration and emergency services. Low salaries have discouraged young people from entering these fields. From the administrative point of view, Estonia has been one of the pioneers in e-government, offering a range of innovative services and resources for citizens, which have greatly improved efficiency and human capacity. A number of registry functions for both businesses and individuals are available online, reducing the need for standing in long lines and hiring extra personnel. Over three-quarters of Estonians file their annual tax declarations via the Internet. In 2007, Estonia became the first country in the world to allow people to vote in parliamentary elections via the Internet.

Like all parliamentary democracies, Estonia must reckon with coalition governments, which often complicate the ability to coordinate conflicting interests and objectives into coherent policy. Party politics in Estonia often follows a cycle in which winning coalitions take office after an election and then break down after 2-3 years, when the strains of governing take their toll. Thereafter, a new coalition is formed, which is often a second-best combination of policy platforms. In April 2003, a coalition driven by the two center-right parties, Res Publica and the Reform Party, along with the agrarian People's Union, took office. When that coalition fell apart two years later, the pro-market Reform Party turned to the left-leaning populist Center Party to form a government, which would last until the March 2007 elections. The two sides had to compromise on a number of key policy issues, but at the expense of an integrated vision. Politics became more about making deals between different party interests, rather than charting a single way forward.

Policy coordination

Estonia has all the basic integrity mechanisms in place to monitor and deter corruption. The National Audit Office is strong and independent. It has conducted a number of high-profile evaluations, including investigating the reasons for Estonia's vastly excessive sugar stocks prior to European Union accession. Public procurement systems are generally transparent, although small transactions at the municipal level are occasionally manipulated. While Estonia has a rather permissive system of party financing, the rules have recently become more restrictive. In late 2006, the parliament began debating the creation of an independent board that would have the right to monitor and audit all financial activity by political parties. Although parties were obliged to submit quarterly

Anti-corruption
policy

financial reports, there was no authority that could verify the veracity of this information or punish financing violations. High-level ethical scandals bordering on corruption also remain a problem, especially when they involve key members of a governing coalition (such as the leader of the Center Party, Edgar Savisaar) and other coalition partners pass over the controversies. At a lower level, corruption has been dealt with more vigorously, including high-profile cases in the police and customs and tax authority.

16 | Consensus-Building

Estonia is one of the most consistently pro-market, reform-orientated countries in post-communist East-Central Europe. While debates have raged over such things as whether to shift from a flat-rate to a progressive income tax, no political actors have ever questioned the need for a market economy or democracy as strategic, long-term aims.

Consensus on goals

Estonia has never had any direct or indirect challenges to its democratization or transition to a market economy. There are no embedded social classes who might resist reform, since the communist era leveled society's social structure. The military has also been firmly under civilian control and well integrated into NATO structures. Although Estonia's ethnic cleavages remain serious, the restrictive citizenship policy has meant that Russians have much less political power, which otherwise might have enabled them to slow the pace of reform.

Anti-democratic veto actors

The main social cleavage to be managed in Estonia is the challenge of ethnic integration. After having ignored the issue for most of the 1990s, the Estonian government undertook an extensive minority integration program in 2000 with the help of several foreign donors, but also considerable state funds. The program focused predominantly on Estonian-language training for Russian speakers, which was seen as the key to improving this minority's ability to participate fully in Estonian society. While many Russians benefited from these efforts, the policy has yet to address long-term issues such as how to reduce the number of non-citizens in the country or how to reduce socioeconomic disparities between the two main ethnic groups. There is little danger of direct escalation of the cleavage in the short term. However, given the country's labor shortage as well as the desire to shift to a more knowledge-based economy, the need to better use the human potential of the Russian community is evident.

Cleavage / conflict management

The Estonian parliament adopted the Civil Society Development Concept in 2002, which is aimed at better structuring the relationship between NGOs and the public sector. The concept committed both sides to promoting citizen initiative, encouraging social cooperation, reducing social exclusion and increasing participatory democracy. The concept also created a joint

Civil society participation

parliamentary-NGO commission charged with implementing the program. Every two years, the parliament is required to have a debate concerning progress on implementing the concept. Given the framework provided by the Estonian Civil Society Development Concept, the Estonian political leadership could encourage civil society's participation in the political process much more. So far, however, these mechanisms have led to only some generalized participation mechanisms, such as an online portal where individuals can post policy recommendations or where forums are created for NGOs to debate policy proposals pertaining to their area. A 2004 study conducted by PRAXIS, an independent Estonian think tank, found that government authorities often see input from civil society groups as purely recommendatory in nature, rather than as a starting point for dialogue and cooperative decision-making. At the same time, many civil society groups are weak and lack the analytical capacity to fully comprehend all the levels and details of policy-making. The above-mentioned PRAXIS Center for Policy Analysis has become a major player in terms of independently evaluating government policies in the areas of labor policy, innovation, economic competitiveness and housing policy. Government ministries are also turning to independent analysts for policy analyses and evaluations increasingly.

The issue of historical and moral justice has operated on two levels in Estonia. In contrast to some other post-communist countries, Estonia never pursued an extensive policy of lustration or prosecution of communist-era officials. The names of some former KGB officials have been made public, and individuals generally have access to secret service files pertaining to themselves. However, no meaningful restrictions have been placed on the activities of former regime officials or agents. The state has attempted to prosecute some individuals directly linked to mass arrests and deportations in the 1940s. Yet as a rule, these defendants have been elderly men who are no longer politically active. In 1998, President Lennart Meri formed an international commission to investigate Nazi and Soviet crimes against humanity carried out in Estonia. This was seen as a way to balance reconciliation in relation to both the Holocaust and the Soviet era. Apart from producing some detailed analyses of archival data, however, the commission has done little to promote public discussion of the past. On a second level, the question of historical injustice has also been concerned with reconciling the different views of the past held by Estonia's two main ethnic communities. In 2006, these divisions flared up when Estonians and Russians debated whether to remove a Soviet-built World War II memorial in the center of Tallinn. The monument, known as the "Bronze Soldier," had traditionally been the gathering place for mostly Russian Soviet war veterans on May 9, the day of the end of the war for the Soviet Union. In 2005, their gathering was disrupted by some Estonian counter-demonstrators, who demanded the monument be removed as a symbol of the Soviet occupation of Estonia. Following some scuffles, the monument was blocked off by the police for some

Reconciliation

three months while the government debated what to do. The governing coalition, however, soon split over the issue, with Prime Minister Andrus Ansip and his Reform Party firmly in favor of relocating the monument, while his coalition partners, the Center Party and People's Union, were opposed. Sensing that they were losing credibility among Estonian voters due to this indecision, the Reform Party joined the opposition parties in parliament to pass a law giving the government the prerogative to remove monuments on local government territory if they were a source of public controversy. The new procedure would still require the cabinet to adopt a unanimous decision, which meant that any move against the Bronze Soldier would have to wait until after the 2007 elections. However, the controversy revealed deep divisions concerning the interpretation of World War II. One group sees it as a heroic victory over fascism, while the other considers it a tragic period in which Estonia was caught in the struggle between two totalitarian regimes.

17 | International Cooperation

Estonia's rapid transformation to a democracy and market economy could not have been possible without the favorable conditions and means offered by the European Union. Estonian elites saw this as the key to rebuilding the country after communism and in particular distancing it from any possible Russian influence. Such staunch pro-Western attitudes and reform policies were often at variance with Estonian public opinion, which would have preferred a more gradual transition. While Estonian leaders never used EU rules or IMF prescriptions to justify the urgency of certain reforms, there was always an implication that shock therapy, large-scale privatization, foreign investment and free trade were essential to secure the ultimate goal of integrating the country firmly into the West. Any technical expertise or advice that could be obtained to implement these policies was readily accepted and applied.

Effective use of support

Estonia's accession to the European Union and NATO in 2004 was the strongest endorsement the country could receive in terms of its reliability as a partner in the international community. High levels of foreign direct investment (including over €2 billion in 2005 and a stock value of €7682 per capita) could also be taken as a sign of external confidence. Commercial risk assessors such as Moody's, Standard and Poor's and Fitch all gave Estonia A-level ratings. The long-standing flat-rate income tax as well as the institution of the currency board have also served as foundations for foreign confidence.

Credibility

While Estonia's relations with its Baltic and Nordic neighbors have been extremely fruitful, relations with the country's eastern neighbor, Russia, have long been frosty. In 2005, there was hope of a breakthrough when the two sides finally signed a border treaty in which Estonia agreed to the existing borders,

Regional cooperation

resolving years of debate over some 2000 square kilometers of territory annexed by Stalin to the Russian Federation in 1945. When the accord reached the Estonian parliament for ratification, however, conservative deputies secured the adoption of an additional statement, re-affirming Estonia's legal restorationism. Since Russia has always rejected that principle, the move immediately drew objections from Moscow. President Putin withdrew his country's signature from the treaty, and the entire border issue went back into a deep freeze. In 2006, controversy over the "Bronze Soldier" war memorial also strained relations. But because the monument remained in place, Russia did not undertake any direct retaliatory moves.

Strategic Outlook

Estonia's need to find a new development strategy for its post-transition challenges goes hand in hand with many new opportunities presented by EU membership. Chief among these is taking full advantage of the structural funds the European Union would make available to the country beginning in 2008. If the projects for these funds are chosen carefully, the country could take a major step forward in terms of preparing its infrastructure for a new kind of knowledge-based economic model. While government and economic leaders need to take measures to stem mounting wage pressures, such increases could be better justified if economic activity were shifted into more value-added areas. This would also improve Estonia's current account balance and reduce its dependence on foreign investment.

Estonia's political system is strong, providing ample steering capability and resource efficiency to manage further development. However, political parties need to engage with citizens more and avoid reducing politics to vague slogans or one-off promises of more money or higher salaries. Ethical scandals are starting to negatively affect satisfaction with democracy and political participation. Instead of overlooking such incidents in the name of coalition politics, more accountability is needed. The ethnic cleavage between Estonians and Russians left by 50 years of Soviet rule and compounded by a restrictive post-independence citizenship policy remains an area in which political courage and action are essential. Although Estonia's first integration program was a pioneering effort at raising political awareness and implementing some innovative policy measures, the next stage needs to involve the reform of Estonia's 100 Russian-language primary and secondary schools. Estonia also needs to create an education system capable of ensuring that younger Russians do not grow up alienated from the Estonian state and society. Greater social harmony would serve to improve Estonia's human resource potential, alleviate tensions with Russia and help overcome many of the psychological legacies still leftover from the Soviet rule.