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Hans-Jürgen Wagener (Ed.)

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Contents

Part III
Policy Aspects of Transformation

Part IV
The Alternative or the Odd Man Out?

Chapter 6

On the Normative Theory of Transformation

LÁSZLÓ CSABA *

1. Introduction

An overall feeling of hangover seems to have taken the place of euphoria of 1989/90. Politicians who used to be the heroes of opposition and the fighters for thorough changes seem to have been worn down by the political processes following the *annus mirabilis*, and with legendary figures/movements the fatigue is unmistakeable, from Solidarity to Civic Forum, from the one-time heroes of East German opposition to the Alliance of Democratic Forces in Bulgaria, from the Gaidar team to the Hungarian Democratic Forum. A large segment of the economics profession, especially those involved in policy advising seem to be still incredulous of the overwhelming side-effects and rather limited directly intended effects of their recipes. The public is increasingly fed up, an the following of protest parties of various sorts is on the increase. Losses in terms of consumption are often coupled with losses of perspective. Wondering whether or not the entire exercise of transformation was worth the price is increasingly fashionable in more than one country, and not only on the extreme left.

Mistakes in system design, in macroeconomic policies, in sequencing reform measures as well as in selling the idea of tranformation are fairly obvious and are being increasingly admitted in public by those involved (Dabrowski 1992, Kádár1993). Criticism of observers of course also abounds. What seems to be a general view is that it could have been done better. But how? Leaving clearly and exclusively politically motivated opinions aside even leading IMF opinion-molders concede (Bruno 1992) that applying the conventional macroeconomic therapies has fallen short of addressing many of the specificities of transition economies. Thus the answer to the questions what should have been done and why have the first legitimate governments so much underperformed is anything but trivial. Comparative and general economics will have a lot to say if they look deeper than the customary reference to vested interests and ignorant politicians. All the more so, since modern theory is able to endogenize the effects and working of the political cycle. Therefore the rather mixed results should certainly be fed back into the theories applied, in order to get a better understanding and better proposals.

* Kopint-Datorg Institute, Budapest.

In this vein of thought there is a significant body of recent literature which attempts to produce a general theory of transformation, with cross-country validity. These analyses attempt to generalize, standardize and predict developments, and—with a varying degree of resoluteness—attempt at a standard or even optimal strategy, against which actual policies and, of course, errors could be measured (cf. Kornai 1992; Apolte 1992: esp. 187–197; Lösch 1992; Dewatripont and Roland 1992). In other words, a general normative theory of transformation is already in the making.

2. On the feasibility of a normative theory

Against this background it might be just as well to ask the heretical question whether or not it is possible to elaborate a general normative theory of transformation? If yes, it could serve as a base for optimizing reform measures in future cases as well as identifying the nature of suboptimality of past deeds. It would be of cross-country validity and could serve as a base for forecasts, i.e. it could be predictive. And conversely, if the task proves unfeasible, it will be difficult to delineate what went wrong in reality. If the answer is affirmative, a "planned" introduction of the market order could easily be declared superior to evolutionary developments, at least on the level of theorizing. Conversely, if the answer is negative, it will be hard to indentify against which background the analyst evaluates actual outcomes, and the door will be open for widely varying subjective judgements. For instance, in terms of immediate wealth effects it is difficult not to see transformation as a desaster. Meanwhile, in a dynamic perspective few analysts would venture to advance the thesis that Central and East European brands of real socialism were anywhere close to any concept of an equilibrium, and/or continuation of reform socialist policies with more technocratic competence could well have yielded better results. Thus, in terms of perspectives, there could have been nothing inferior than these countries remaining in the developmental dead end, thereby more or less any cost might be justified. Likewise, considerations of human freedom in general and the individual quest for protection do not quite go hand in hand, to put it mildly.

Therefore, the search for a general normative theory is a rather legitimate effort in more than one respect. However, there are several grounds for scepticism.

a) The crux of the market order is spontaneity, in other words the dominance of spontaneous, uncoordinated decentral decisions against any central will, over governmental visions of whatever sort. This is the case historically, if one thinks of the genesis of capitalism be that in Northern Italy or in the USA. This is the case philosophically, as demonstrated e.g. by Hayek (1989) and many others. And we do not know about any capitalist economy where the public sector or governmental tutelage would indeed dominate over business considerations, especially in the longer run. Even East Asian dragons, facing the growing maturity of their economies and societies have entered the way of further decreasing governmental involvement in economic affairs.

b) It could be quite handy to possess an optimal strategy against which individual country experiences and governmental improvisations could be evaluated. This need goes without saying for adherents of gradualist designs, but in an inverted manner shock therapists are often rather more than less of a social engineer than planners used to be. The very idea of introducing economic institutions and behavioural norms to societies where there is no historical antecendent, and that in a short period of time, is a fundamental feature of social engineering of its simplest brand. Thus, missing self-set targets in terms of privatization, in terms of passing legislations, or in terms of attaining macroeconomic indicators (normally expressed in quantitative terms) has already neatly backfired to adherents of this approach in more than one country.

From the theoretical perspective the above listed criticism aims only at the top of the iceberg. In order to qualify any given outcome as suboptimal, a—preferably explicit—concept of optimality should be at hand. Optimizing however presupposes at least four prerequisites: a subject, a procedure, means of implementation and availability of an objective function or criteria according to which optimality versus suboptimality is being measured.

Let us consider whether or not there is any empirical evidence supporting the operationality of the four criteria in any real world economy. In a planned economy, in theory—and even more so in ideological legitimation—there should have been such a single optimizing centre. However, both early theories of optimal planning (Petrakov 1966) and descriptive analyses of actual planning prodedures in various Eastern European countries (Bauer 1981) concluded, that not even in theory, let alone in practice such an optimizing subject could ever be identified.

It is next to trivial to argue that in a market economy, even with sizeable state regulation, no such optimizing centre can be identified. Thus, if neither of the model cases possesses such a centre, would it be realistic to expect transition economies to have one?

c) The real theoretical lure of a normative theory of transformation would be its cross-country validity and its serving as a base for forecasts, i.e. predictive nature. This is the area where signs for hope are the scantiest, since theories, expectations and actual outcomes have been so widely divergent all over the transformational period, irrespective of the ideology and target-setting of the given government. Cross-country analyses, of course, remain rather valuable for comparative and international economists. However, by the very nature of the exercise results are available only *retrospectively*, which is precisely the opposite of the very idea of normativity. For the public choice school this might be a non-issue not, however, for optimizers and policy advisors.

3. Conceptual delineation

Many people may find it superfluous to define where transformation starts and when it comes to an end. However, this issue is anything but irrelevant. For one, in the growing number of contributions to the subject several theorists include into "transformation" any sizeable modification of the traditional socialist model. This is misleading both in theoretical and in operational terms. In theory, transformation starts with the abolition of the one-party system and the democratically legitimated choice for capitalism. This is not mere semantics. Reforming a system means changing any element in order to *preserve* the unerlying construct. Transformation starts at the point where substituting one construct for another becomes the issue.

The author would be the last one to deny the relevance of evolutionary heritage for transformation. In countries like Czechoslovakia, Hungary or the ex-GDR there has been nothing to be stabilized. Therefore the entire theoretical literature on stabilization, including the application of Latin American analogies is of academic rather than policymaking interest. Countries where the government is not very credible can only opt for radical steps in order to build up their image. Still, this should not allow for including the years of *perestroika*, or of market socialism in its last, most radical phase into the theories on transformation. Furthermore, the Gaidar programme should not be on the list either, as this policy was a *par excellence* case of enlightened absolutism, implemented by presidential decrees and governmental orders. This is an important, but "pre-revolutionary" step, which should not give ground for inferring far-reaching conclusions on what is—or is not—wrong in transformation.

The Chinese experience should be also excluded from this discussion from the very outset. It is of course highly relevant from the developmental perspective and is a subject on its own right because of the size of that country. Even from the point of view of transformation economics it is anything but irrelevant whether or not the outgoing communist régime bequeathes chaos or some of the foundations of a market order, as was the case in Hungary. However, this does not seem to justify the interpretation of those (e.g. Hermann-Pillath 1993b, Brus 1993) who believe in the separability of the political and economic aspects of the issue, and—based on growth statistics as well as on the undisputeable expansion of non-state sectors in China—conclude about the superiority of the Chinese reform socialist approach to "disruptive" Central European practice. China can—indeed should—be compared to Vietnam after 1989, the Gorbachev years, or the Polish, Hungarian and Yugoslav reform socialist practices of the late 80s, and its superiority can be duely acknowledged. However, this country is still under one-party rule, with bureaucratic coordination and public property having the upper hand. Nobody would doubt that the dual track price system is a far cry from free pricing, and that privatization—as different from de-etatisation—is still not an issue. Public firms do not go bankrupt, and

agricultural accumulation of capital as well as freedom to purchase and sell is restrained in many—rather feudel—ways. Nomination of managers is still in the hands of the Party. In sum, due to a number of specificities—from country size to the low level of development—an outgoing socialist model might well be able to show better performance than transition economies amidst their adjustment crisis. But this should not be the proper comparison: China should be measured against Taiwan and Singapore rather than against Bulgaria. And in terms of development economics, it might well be that an enlightened absolutist model might be better suited to a poor country in the first modernization phase, than an unconstrained free market model—this will be no surprise for those working on the problems of the South.

An equally relevant conceptual issue is identifying the final stage of the transformation process. Both from the policy and theory perspectives a clear-cut vision is needed. Most analyses find it sufficient to conclude, that the market-based or price-led allocation predominates all goods and factor markets. This convenient statement however is hard to operationalise even at the level of applied theory, let alone economic policy. Let us leave for the moment the sterile world of perfect competition and approach real world market economies of various sorts:

Looking at Western Europe, one sees one of the factor incomes, wages determined by collective bargaining rather than anything else. In a bargaining society, wage rates depend much more on political and cultural factors and the like than on productivity.

In agriculture it would be rather difficult to find any European country where free market forces would have a decisive say in shaping the size and incomes as well as location of farming. Quantitative targets and *ex ante* set income positions are not seen as perversion.

Social corporatism is fairly widespread a phenomenon all across Europe. Such dissimilar countries as Greece, Finland and Austria have been practising it for decades. The really "frightening" fact about their experience is that their macroeconomic and international trade performance in 1970–90 does not show signs of lagging behind as some might well have expected (Landesmann 1992).

Reference is customarily made to Japan and the NICs, but several European countries and the EC also embrace concepts of industrial and technological policies, and follow trade practices which are a far cry from zero protection. Capital account restrictions are widely practised by many countries especially in times of difficulties (e.g. Spain in the autumn of 1992).

Last but not least, mention should be made of the welfare state, which professes a stubborn resistance to the rhetoric of the need for its rolling back. In this area 40 per cent of GDP is being redistributed on other grounds than efficiency.

To sum up, in real world economies, especially in Europe where transformation of economic system has become an issue, there is nothing close to a model economy, where only utilities and indivisible public goods like justice are provided by the state, and the rest is allocated by market forces. This statement is not meant to justify the *status quo*. Several analysts (e.g. Leipold 1990) have come to the conclusion that West European countries themselves have to face transformational problems quite akin to Eastern countries. However, two conclusions might be immediately inferred.

1) The conventional formula describing the end-state of transformation requires Central and Eastern European economies to be more free market than are the countries of the proponents. This might be seen either as an attempt to act as world improver, or as taking transitional economies as experimental fields for yet untested games. Given the lower level of development, aggravated by the adjustment crisis inherent in the transformation one can see very limited theoretical justification for subscribing to such ideas as policy relevant propositions.
2) The end of the transformation process can not and indeed should not be defined such that a large number of EC countries could not qualify either. And in the end of the day, do we really have to wait until 95 per cent of all assets will have been owned by private persons to be content? Do we really need to wait until those forms of the capital market which exist basically in the US and Britain only evolve in relatively backward countries? Should we expect them to enforce measures instituting these to qualify for being accepted as civilized members of the international community? If not, what is the point of repeating simplistic propositions from prestigous fora?

In sum, there is both a theoretical and policy relevance of delineating the accomplishment of transition fairly realistically. This should be a point where problems and reforms necessary to improve efficiency of the postsocialist economies are similar in quality to those faced by the European welfare states or by the newly industrialising economies. With such a measure, the market maturity of some Central European countries, like Poland, Bohemia, Slovenia und Hungary will certainly have reached the limit by the mid-90s, where the quality of the economic order can no longer be subject to serious doubts. The point of no return is conditioned by the stabilization of the pluralist political system, open trade régime, steady growth and dominance of the private sector as well as currency convertibility and modearate inflation at worst. The above listed criteria are objective and forward looking, rather than emotional.

4. Operationalisation of transformation in functional terms

If the overall decision to introduce a fully fledged market economy was nearly unanimous, there was a lot of controversy over the ways and means it could be operationalised. Since international advice was focusing on stabilization, several issues that are peculiar to transforming a postsocialist economy at a medium level of development received little or no attention or, if they did, then only as subordinate to stabilization policies. This proved to be quite a problem, as stabilization and systemic change are not quite twin sisters, they often have conflicting rationality. To bring a trivial example, positive real rate of interest and tough tax collection procedures are not known to be particularly helpful in fostering and accelerating capital accumulation by luring people to spend their savings on productive investments.

In the following pages I shall abstract from all issues that are related to stabilization only. Rather than following the customary deductive procedures, I shall attempt to adopt an inductive approach. Drawing on concrete paradoxes in operationsalising the idea of introducing a spontaneous order by governmental policies, I hope to be able to contribute to an empirically better founded general theory. As will be seen at the end, there are only a few encouraging signs in terms of normativity.

4.1. The system of taxation

It has become quite clear by now that reforming the system of taxation is one of the fundamental tasks of any transformation strategy. Having received much less attention than the alternative technologies of privatization, this issue has proved to be a matter of survival for many transforming economies. Whereas the speed and methods of ownership change has come to the limelights, the underlying bread and butter issue of taxation seems to have received little if any attention.

This has produced a host of problems. For one, the tax apparatus in most postsocialist countries was equipped to deal with a few hundred large companies with elaborate bookkeeping departments and very extensive accounting controls. These tend to be closed down, chopped up, corporatized etc. By and large, they constitute the ailing part of the economy. Meanwhile hundreds of thousands, in Russia millions of private small ventures emerged. These—for obvious reasons—do not follow the elaborate taxation rules. For one, self-employed can not afford the luxury of employing the administrators needed for this system. Secondly, these rules are fairly restrictive, especially for non-state activities. If these were observed, they could not harvest their returns, not to speak of accumulation of capital. Last but not least, a grey zone between the legal and informal sectors has widened rather than narrowed in the course of overall liberalisation and erosion of central powers.

In sum, the tax administration remained understaffed, underqualified and in more than one way ill-equipped for coping with the new realities. Governments with a limited if any credibility cannot afford the luxury of tough collection rules and implementing them, because that would be rightly seen as an onslaught of the emergent private business, as an open contradiction to their devotion to privatization and as the continuation of Soviet-type practices of the past. This implies a quite unhealthy situation in which tough laws and accounting rules remain in force, but are hardly implemented, which is not a step forward on the road towards the rule of law or towards civilized market behaviour. Any attempt at enforcing regulation is therefore rightly seen as bureaucratic arbitrariness by economic agents, whereas non-enforcement undermines both the credibility and the fiscal base of the authorities.

In other words, the healthy part of the economy is less and less controlled by the state at a time, when pressures for contercyclical activities are strong. Socially motivated expenditures are quite difficult to trim at a time when GDP, as in 1990–92, has dropped by about 30 per cent in Eastern Europe, and that with radically increasing income differentiation. Meanwhile the healthy part of the economy does not share the burdens of the public which, of course, undermines its legitimacy.

Under these conditions the idea of shortcutting slow evolutionary change has proved to be counterproductive. The Gaidar government, for instance, introduced—against the advice of World Bank—modern personal income tax and value added tax legislations. With due respect for such institutional options, these are fairly complicated arrangements. In Hungary, it took about 3 years until companies, authorities and the public learned to live with them. Under Russian conditions, implementing them implied a loss of sizeable budget revenue: less than half of the planned amounts could be collected. The lesson of the story is, of course, that no ideal pattern of systemic choice can be elaborated without taking into account the concrete environment of its implementation. A second, relevant finding is that theoretically less original problems might become politically more so. Moreover, no obvious answer can be given to these problems. If one follows the logic of stabilization, tough collection can, of course, be organised (at least in theory). But this will certainly run counter to promoting privatization in times of insecurity, inflation and political conflict, when more than one legal tender is in the hands of the population. The example and its implications clearly exemplify the general problem emphasized in more theoretical writings (Kádár 1984, Schwarz 1992) that strengthening the logic of the market and that of democracy may not be supplementary. They may become directly contradictory just at the times of transition. The room for a general normative approach is thus limited.

4.2. The one-sided emphasis on privatization

Contrary to the mainstream of writings on the subject, privatization can not be taken as a substitute for the package of measures creating all constituents of a liberal market order. A change in ownership *per se* not only might, but actually has triggered effects which many of its proponents would find as perverse.

Experiences of many developing countries indicate that a rent seeking behaviour is anything but specific to public firms. Foreign investors—especially under a protectionist trade régime—are more than eager to collect monopoly profits available on an uncontestable market. In the case of Hungary, first natural monopolies were bought up. In some cases previously competitive subsectors were cartellized by their new foreign owners. The deputy head of the Competition Office proudly noted, that it is not their business to be involved in privatization, since they are focused on competition only, which might run counter to other, "more important" concerns (Stadler 1993).

Meanwhile foreign business has proved to be more ingenious than Hungarian public firms when it came to lobbying, to protective measures of various sorts, to get tax holidays etc. These are prime cases of promoting rather than limiting particular vested interest, which should traditionally be a main concern of overall economic policy—naturally against the given private interest. The propensity of major parties and MPs to get involved in business might get a truly Japanese flavour unless legislation and the press interfere quickly. Disregard of externalities and of civilizing norms is also not exceptional. Thus, the thesis that no market economy can be based on public property should be supplemented by the thesis that functions of government macroeconomic regulation will not be automatically taken over by private agents or, if they do, it is bound to be severely disfunctional. The weakness of Hungarian courts to enforce contracts, to collect collaterals, or force debtors to pay have given rise to private armed units who take care of this business. Thus, the simplistic belief of the best state being the minimal state has already backfired. The Russian mafia-economy may only add further evidence to this proposition.

Ensuring law enforcement, observance of contracts as well as contestability of markets and fair business practices ar more important tasks for government activity during transition than shaping the ownership structure. These macro-functions need to work for privatization to make sense an become efficieny enhancing. This applies *a fortiori* for the transformation period, when old rules and values are already eroded whereas new values and behavioural norms have not yet taken hold. This is the way by which a government may accelerate the process, whereas direct involvement in shaping either the organizational or the property structure of companies will probably be counterproductive.

One wonders how, after decades of socialist experience, anyone can seriously believe in the bureaucracy's ability to restructure and modernize companies, moreover to determine their proprietary structure and values as well. The attempt to shortcut the comprehensive issues of modernization and strategic ownership by means of a voucher scheme is not only theoretically contestable, but has practically backfired. For one, popular capitalism neglects the need to modernize capital assets all across the economy, which is the base for any improvement of income generation, which later may well be redistributed. For the other, this option smacks of cheating. In the Russian version, it was a simple way how *mafiosi* and the military-industrial complex could become a legitimate owner of assets quickly. In the Czech case, direct and controllable public ownership has been exchanged for an indirect and hardly controllable public ownerschip via investment funds. In both cases the equity and the management aspects seem to have been pushed to the background. Many of the underlying ills of the economy remained unresolved, even uncovered, while hopes for quick improvement have been raised. Both is bound to backfire politically and economically alike.

In sum, the one-sided emphasis on ownership change is not an innocent error in devising policy relevant concepts for transforming European economies. Neither is the simplistic antistatist approach.

4.3. Legal reform

It follows from the above that legal reform is a crucial ingredient in changing the behaviour of millions of agents. The above listed and other perversities indicate that state desertion alone is an insufficient condition for civilized market behaviour to take over. Although Western legal systems have been evolving over centuries, social engineers are only glad to propose quick fixes in this area as well. As under Soviet socialism, legal nihilism and a blind faith in legislation can comfortably coexist. Given the need to be integrated into the world economy, propositions to copy institutional and legal arrangements of most advanced nations proliferate in the literature and have found their way into practice as well.

Experience of the one-time GDR might caution us from being much too forthcoming towards this idea. Even with a fair amount of common culture, history and civilization with no language barriers and a massive "import" of professionals, internalizing the arrangements taken over has a long way to go in that country. In countries which are different in more than one dimension, difficulties are bound to multiply.

Legal reform has much too often and in much too many countries been identified with writing or importing new laws without caring much about their implementation. the decretal rule of Boris Yeltsin can only be compared to the practices of the Ceausescu period in Romania, when 3–4 decrees or more were issued daily. Therefore repeated issuance or contradictory decrees are anything but exceptional. It is even physically next to impossible to follow and digest the flood of decrees. Whereas under Ceausescu there were organizational means—like monthly meetings at the municipal Party committee, or weekly meetings of editors-in-chief at the agitation and propaganda department—to filter "informational noise" and explain what should be taken seriously, in Russia nothing like that happened. In March 1993 the 9th Congress of the People's Deputies abolished the institution of presidential nominees (*prefekty*) which could have filled this gap. This state of art, of course, is a breeding ground for lawlessness rather than for universal observance of contracts.

Likewise if institutions have time to be integrated and their workings internalized, they may be of great help in transformation. The Constitutional Court of Hungary is an excellent example by its continuous controlling and cutting back extremes and deliberations incompatible with the idea of rule of law (like retroactive legislation to punish crimes committed decades ago under different laws). On the other hand, cooperation of major actors need to

be secured—by tradition or by internalization—if new institutions are to make sense. Under Russian conditions e.g., independence of courts and their overruling administrative decisions is a rather abstract idea. Likewise the very narrow capital market in Hungary or Slovakia makes little sense of this institution as a base for evaluating companies, thus any obligation to sell large firms via this way remains an empty shell. Last but not least, the cultural aspect must be involved, which is customarily neglected by the monoeconomics vision which dominates international policy advice. Similar arrangements—even the totalitarian régime—have always functioned differently in a different environment. Thus it is extremely naive to expect copying to be the shortest way to heaven. This points to a truly comprehensive set of problems, but I feel relieved from their elaboration as the truly illuminating analysis of Carsten Hermann-Pillath (1993a) has been published in the previous volume of the same series on transformation.

Therefore, unless we expect the rather simplistic vision of a uniform cultural conditioning across the globe and disregard experience, there is very little hope for either a general or a normative vision of how legal reforms should proceed. Beyond the skeleton and the spirit of legislation, concrete options as well as ways of expedient implementation are culturally conditioned and thus are, by definition, dissimilar accross the transforming countries.

4.4. Monetary and fiscal policy

But isn't there in monetary and fiscal policy a large degree of common sense which could be relied upon in the course of transformation? The answer is in many ways affirmative especially at a general level of argumentation. Fiscal laxity or the inefficiency of monetary regulation has not produced any good to any economy. Moreover, the core of transition is precisely to change from bureaucratic to market and monetary coordination.

However, as we all know, the devil is in the petty detail. Under given circumstances, neither a retrospective nor a predictive normative analytical frame could be successfully elaborated, and not because of intellectual laziness. General models distilled mostly from the Polish experience, or more recently—and mistakenly—from the Russian experience, have little if any relevance for Czech Republic, Slovenia or Hungary. Problems of the Romanian implosion in the post-1989 period have little common with East German problems, thus theory and evidence are inescapably incongruous.

Let us look into some of the more elaborate theories to illustrate this point. In their comprehensive and well-argued model Herr and Westphal (1991) pledge for a monetary reform as well as for a virtual renationalization of firms to a state holding company. This might well have been a justified option given their empirical material drawn from Polish and Soviet sources and the works of Kornai on the classical planned economy.

Monetary reform started by a currency reform is obviously an option in any economy after a war or similar cataclysm. In the case of Hungary, former Czechoslovakia, Slovenia and China (if they opt for transformation) no such situation has been around. Even in Poland, 1989 inflation of 244 per cent was half of what is conventionally termed hyperinflation. Moreover, in the last quarter of 1989 monthly rates showed a steady deceleration of 55, 22 and 17 per cent (Kolodko 1991: 22). In other words, there was no earthquake, and nothing made it imperative to go that way. Equally in Russia, though currency reform might have been an option at the time when there still used to be a functioning central authority, say till mid-1990. But inflation rates—even corrected for repressed inflation—did not call for it, as hyperinflation has been a product of the Yeltsin era. Furthermore, when the power to implement currency reform was still around in Russia, this step did not fit into the populist rhetoric and mildly reformist policies of that period. In the Polish case, the government which has finally opted for schock therapy was one without a parliamentary majority, which often seems to be forgotten. In Romania, following the citizens' rebellion of December 1989 for about two years the idea was out of question as nobody was really in charge of macroeconomic policy.

Arguments in favour of a currency reform are technical, with a certain disregard for policy. The Pavlov episode of January 1991 has clearly indicated the long-term repercussions of a not fully successful attempt in this field. Meanwhile most of the purposes of such an act can well be attained with much less pain through a temporary hyperinflation which later calms down as it did in Poland and, to some extent, also in Bulgaria. Thus it is no surprise that in cases where this option was available it was rejected for less painful variants, whereas in other cases the need for such a drastic step could not be substantiated.

The other proposition of virtual renationalisation also may cause more problems than it solves. True, it would clarify proprietary rights and ease the fiscal crisis resulting from the earlier explained problems of taxcollection. Further it could limit malpractices common in spontaneous privatization. However, there are serious counter-arguments in cases where transformation starts not from nowhere, but follows a reformist period, when several market institutions and a fair degree of managerial autonomy have been created. This implies real rather than formal decisionmaking autonomy which can be empirically verified in the behaviour of enterprises. Since all theoretical and empirical evidence is indicative of quick privatization being a clearly utopian aim, a large segment of the economy willy-nilly remains in state hands for a protracted period of time. In this context one cannot but subscribe to the view of Dabrowski (1993) noting that the above listed arguments in favour of renationalization are obviously inferior to the consideration and imminent need of improving management and efficiency of public firms. Moreover, stateowned firms can and will be privatized in a variety of ways, and time periods. In all these cases the use of decentral knowledge is indispensable for any successful modernization project. Thus scarce managerial capacities would caution against creating one—or even

several—superbureaucracy which sooner or later will be converted into a new version of planning agency or, what is worse, sectoral ministries of the Soviet type.

Doing away with fiscal deficits is of course a proposition few people with economic education would oppose. The problem lies in the specificity of the transformation period. As eloquently elaborated by Bruno (1992), an overdose of orthodoxy is—and indeed has been—in open conflict with the peculiar tasks and conditions of economic transformation. In countries where the adjustment crisis is severe and the earlier described fiscal trap is more or less inevitable, simple minded efforts to equilibrate the general government budget might seriously derail the entire process. One has to be realistic enough to avoid openly and immediately contractionary policies in countries which have been in an depression, and where illusions for quick improvement have been fuelled by more than one political force.

Hungarian experience might well be illustrative to this point. In 1992–93 direct subsidies to production, consumption and productive investment constitute about 2 per cent of governmental spending each. In other words, there is no room for the conventional cuts. 70 per cent of public spending is related to the social security system, pensions, health care and transfers of various sorts. From the late 1970s on non-economic, i.e. social transfers have been expanding, further administration and outlays for law and order grew heavily. Despite several projects and attempts, 1990 was not a starting year of transformation in terms of fiscal policy and coordination (Muraközy 1992: 1062). Therefore thorough cuts of whatever sort have become a directly political issue, with skyrocketting crime rates and the war at the Southern frontier of the country.

Turning to social transfers nobody would doubt that a Swedish style welfare state is incongruous both with the productivity level of the country and with the need of primary capital accumulation. The question is how to institute cuts without causing more harm than good in a country with stable double digit rates of unemployment and after four consecutive years of contraction.

To make things even more complicated most of the problems faced by Hungary are quite akin to those in advanced European countries. The problem of ageing, cost explosion in medical care, lavish unemployment and minimal wage legislations, the tendency to cut official working hours coexist with a wide variety of services extended on citizens' rights. Looking at the not very impressive results of the Blüm reforms in Germany or at the social reception of the Amato programme in Italy one does not rush at the idea that the pre-Clinton America should really be the only model for Hungary and other transforming economies to emulate. The balance between fiscal musts and social endurance is certainly very delicate, and many answers are yet to be elaborated in other countries as well.

5. Concluding remarks

As we have seen in the preceding sections, transformation of postsocialist economies have already made several countries in Central Europe more akin to "normal" West European patterns than many theories tend to suppose. The problems they face have a lot in common with those in advanced countries, themselves confronted with mixed experiences of privatization and the need to consolidate the welfare state. For these countries the relevance of the command economy model is next to nil, whereas in a large number of countries, from Albania to the Ukraine traditional Sovietological knowledge is anything but antiquated. In yet other countries, like China or Kazakhstan, the reform socialist model has a lot to offer, and this category might well be more relevant to Russia than that of transformational forerunners.

Stabilization was an important issue in Poland and Bulgaria and Slovenia, is still a relevant issue in the CIS states, in Croatia, Romania and the Baltic countries, whereas it is not an issue in Hungary, Bohemia and in the ex-GDR, or in the Asian reform-socialist states. This makes a large portion of the international literature positively irrelevant for understanding what is peculiar about Central European transformation.

Transformation is quite unlike processes in Nature. Thus it cannot be a subject of methods deduced from science. Observable regularities are rather limited. As the public choice is instrumental in bringing about or reverting processes, only a political economy framework seems to fit to the subject.

"Market economy" is just as general a concept as is "command economy". Therefore the theories attempting to visualise transition from one to the other are of limited value at best. It is difficult not to forego the conclusion that an eventual Vietnamese transition will be more akin to Chinese or Korean than to East German or Polish. Subject, object and ways of their interactions differ sufficiently to make generalizations of limited value. Culture, religion, history, and many other factors dating back before the socialist experiment might well have more explanatory power for the given case than the specificities of the last 45 years.

This paper tried to demonstrate some of the more obvious limits to theoretical and policy attempts based on fairly abstract and simplified concepts of how to transform "a" planned economy to "a" market economy. We have found that fairly trivial or common sense propositions will either be hard to operationalize or positively harmful for bringing about a systemic congruence between the two halves of Europe.

Any commonality lies in the specificity of cases. For some subgroups—like Central Europeans, Southeast Europeans, CIS, Asian socialists—commonalities and overlaps may suffice for making tentative generalizations. But the decisive property of a general and normative theory, its predictive capacity, seems to have been ill-founded. One wonders, whether this is so "for the time being", and later a chance for such an exercise will eventually emerge. The nature of the problems we have surveyed may, according to our intuition, suggest, that it is not just a matter of time, data and intellectual effort. The diverse properties of the various issues preclude comparative economists and international agencies to develop such a universal normative theory. This may be inconvenient, but it also makes life and future research more interesting.

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Some Reflections on Privatization as a Means to Transform the Economic System: The Western Experience

Bruno Dallago *

1. Introduction

The transformation of socio-economic systems is the outcome of complex changes in institutions and economic and non-economic variables. Transformation can take place in different ways (cf. Wagener 1993), provided that changes in various areas are mutually compatible, that other elements of the socio-economic system adapt, and that barriers to change are overcome.

One of the most relevant aspects of any economic system and its change lies in two distinct although strictly connected problems: a) the dimension of the state intervention in the economy and its nature and b) the transformation of the economic role of the state through time in both quantitative and qualitative terms. In what follows attention will be put on the latter problem, while the former question—on which the attention of political economy has traditionally been centered—will be disregarded. As will become clear below, we lack well established, reliable theoretical instruments to analize and appraise the rise of the institutions state and market and how the relationship between them should change through time. Even existing evidence is subject to contrasting interpretation. In such circumstances it is not surprising that the debate on the intertemporal relationship between the state and the market—and in particular the policy instruments utilized to change it, namely nationalization and privatization—often remains on a non scientific level and is strongly influenced by political elements and objectives.

To partly overcome such difficulties and given the limited scope of this paper, questions relative to the rise of the institutions state and market will

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