

The post-communist transition should not be misinterpreted

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I read with great interest Dalibor Roháč's article (Roháč 2013) in the February 2013 issue of *Economic Affairs*. This topic is worth discussing.

Economists behave rationally when they look for major economic events because for them they are an alternative to controlled experiments in natural sciences. However, I am afraid that the fall of communism, the collapse of such a large-scale experiment with central planning and abolition of private property,[1] has not been used by economists in this way, or at least not sufficiently. It deserves more attention.

The debate was evidently biased from the very beginning. Old exponents of the 'comparative economic systems' theory came with their old preconceptions and vested interests; adherents of the 'neo-institutional' school used the debate for the presentation of their – very doubtful – views; mainstream economists did not pay attention. The reformers, most of them economists, suddenly turned politicians, were not believed – they were considered defenders of, if not apologists for, their reform projects and were not taken seriously.[2]

As a result, new myths were created, new (or not so new) battles were fought, but the transition from communism to capitalism is still not understood. The comparisons with similar events in the West do not help very much. Unlike us, Margaret Thatcher, Britain's former Prime Minister (1979–90), did not try to shatter the constitutional foundations of her country. She tried to reform the country in order to strengthen the kind of capitalism that Britain has always represented. Our privatisation programme was to liquidate the entire old system for which state ownership was the major vehicle of power.

It would be positive to use Dalibor Roháč's article as a starting point for a new round of discussion. I feel obliged to announce that I have a stake in this debate. I was Minister of Finance and then Prime Minister of one of the transforming countries, the Czech Republic. I was neither an uninvolved observer nor an economic agent participating in the transition process and searching for windfall profits, unlike many Western 'advisers' who had such an ambition.

I was surprised to see that even such a sophisticated young economist (who because of his age could not have participated in the old disputes) uses the terms 'shock therapy' and 'gradualism'. All of us who were involved in the process of transition have been arguing for years that such a choice did not exist in this process – in my case probably most recently in a speech for the 2012 IIASA conference in Vienna. Let me quote from it extensively:

- The overall systemic change is not an exercise in applied economics. It shouldn't be forgotten that the changes started whether we wanted them or not, whether we had the feeling that all relevant, highly needed preconditions had been met or not. It was not possible to stop the spontaneous behavior of millions of people, even if we wanted it, which certainly was not the case. In addition to it, we knew that it was necessary to fill in the vacuum created by the collapse of institutions of the old regime as soon as possible...

- Our critics did not see that there were *transformation measures with objectively different time requirements* and that their introduction and implementation couldn't coincide in time. *The institutional framework and the rule of law have to evolve, they can't be 'introduced'*. Completing them takes years or decades, not days or weeks. Patronizing us in this respect was a very insensitive and thoughtless behavior on the side of some of our Western colleagues and of some of our domestic ones...

- The crucial factor in transition was time. This issue has been discussed – at least at the beginning – under the totally misleading heading: gradualism vs. shock therapy. It should be stressed that both concepts are wrong – neither one has any meaning and any relation to reality. Something else was important. It was necessary to put forward at one moment *a critical mass of reform measures* in order to send a strong signal to the citizens of our countries that we were serious and fully determined to transform the country. After that, the rule was – whenever there was an opportunity – to implement any measure which was prepared. (Klaus 2012; emphasis in original)

This is a fair summary of my position. Dalibor Roháč mentions – partly positively, partly critically – Joseph Stiglitz, which is probably appropriate. This very productive and innovative economic theoretician has a special gift for misunderstanding economic reality. It is a wrong procedure to create a straw man – the shock therapy – and to accuse almost all authentic reformers of being agents of the shock therapy concept and to herald a – never explained or defined – strategy of gradualism. *In the reality of transition, so-called gradualism was considered a non-transition.*

Instead of defining it, Stiglitz repeatedly gives the example of China, but China has never been and could have never been a model for anyone in Central and Eastern Europe. In our part of the world, the political transition – parliamentary democracy, competing political parties, political freedom – was done immediately after the fall of communism. In such a situation no sophisticated sequencing, or gradualism of economic reform measures, was possible. The millions of finally free people, fascinated by the arrival of freedom, wanted to live without being 'planned' or controlled by anyone. In the case of Central Europe, there was no way to separate the economic and political systems. Postponing the revolutionary abolition of the one-party system was impossible and nobody wanted it.

We were also aware that gradualism creates new distortions and were particularly afraid of the so-called spontaneous privatisation (into the hands of old communist directors of state-owned enterprises). Such a result would have been, at least in my country, politically unimaginable.

Dalibor Roháč discusses also the role of the 'Washington Consensus', which 'focused policymakers' attention on variables that they could directly control' (Roháč 2013, p. 66). This never came to our mind. When we prepared our reform programme in the first months of 1990, the term 'Washington Consensus' did not exist. It was, however, implicitly or automatically evident to us that

- we had to be in control of the macroeconomic situation by means of very cautious monetary and fiscal policies;
- we had to liberalise prices and foreign trade as soon as possible;

- we had to fully deregulate and de-subsidise the economy; and
- we had to privatise the economy and set up all kinds of institutions necessary for the rational functioning of a market economy.

Roháč's article unfortunately repeats many myths about shock therapy; and what is – perhaps paradoxically – even worse, he defends it against so-called gradualism. He says that the gradualists did not present any tangible proposal. But I have to repeat that neither of the two options – shock therapy and gradualism – existed or exists in reality. I have been arguing for years that nothing like such a choice existed. It is useless to continue such a dispute. And it would be wrong to confuse newly transforming countries with a false dilemma.

References

Klaus, V. (2012) 'The Political Economy of Introducing Free Markets: Notes for IIASA Conference.' 14 January, Vienna. Available at <https://www.klaus.cz/clanky/3022>

Roháč, D. (2013) 'What Are the Lessons from Post-Communist Transitions?', *Economic Affairs* 33(1), 65–77.

Notes

[1] I accept that we use the terms 'communism' and 'central planning' very loosely these days. In the 1980s we devoted a lot of time to the analysis of the real-world 'Economy of the Socialist Type', which was very different from the hypothetical 'Centrally Planned Economy' discussed in the economics textbooks. The power of central planners was in reality rather limited; in contrast, the power of 'planned' enterprises was much stronger. Being fully absorbed by our new challenges, we ceased to continue this type of reasoning. The role of horizontal – as opposed to vertical – relations was in communist reality much bigger than is usually assumed.

[2] We would have accepted a serious question: who is the particular agent (designer, architect, politician) behind such a fundamental systemic, institutional change? It is fair to ask: what did the politicians (architects of reforms) maximise? The Public Choice School should tell us something about it. Personal ambitions undoubtedly existed, political success was a goal, but the first steps were done 'altruistically'. Yet scholars have demonstrated heavy vested interests in this process – they also wanted to be well-paid advisers.

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