PUBLICATIONS DE L'INSTITUT EUROPÉEN DE L'UNIVERSITÉ DE GENÉVE

25 Years after The Wall

HOW DID THE FALL OF THE BERLIN WALL CHANGE OUR LIFES?

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FORUMCAROLUS

UNIVERSITÉ DE GENÈVE

ISBN: 978-3-00-049639-4

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Lech Wałęsa Former President of Poland, Nobel Peace Prize Laureate

In August 1980 Wałęsa was instrumental in political negotiations that led to the ground-breaking Gdańsk Agreement between striking workers and the government. He became a co-founder of the Solidarity trade-union movement. Arrested again after martial law was imposed in Poland and Solidarity was outlawed, upon release he continued his activism and was prominent in the establishment of the 1989 Round Table Agreement that led to semi-free parliamentary elections in June 1989 and to a Solidarity-led government. In the Polish election of 1990, he successfully ran for the newly re-established office of President of Poland. He presided over Poland's transformation from a communist to a post-communist state, but his popularity waned. After he narrowly lost the 1995 presidential election, his role in Polish politics diminished. However, his international fame remains. Wałęsa continues to speak and lecture in Poland and abroad on history and politics.

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Professor at the Faculty of Law of the University of Geneva since 2001, Nicolas Levrat has also taught at the Université Libre de Bruxelles. Since 2007, he has been Director at the European Institute of the University of Geneva and is the Director of the newly launched Global Studies Institute at the University of Geneva. Professor Levrat specializes in the fields of European law, federalism and democracy in Europe, and relations between Switzerland and Europe. His publications include L'Europe et ses collectivités territoriales. Réflexions sur l'organisation et l'exercice du pouvoir territorial dans un monde globalisé (2005), Les conséquences des accords bilatéraux entre la Suisse et l'Union européenne pour les cantons frontaliers de la France (with René Schwok and Stéphane Bloetzer, 2000) and Le droit applicable aux accords de coopération transfrontière entre collectivités publiques infra-étatiques (1994). Nicolas Levrat holds a Doctorate in Law from the University of Geneva and was an Agent du Conseil d'Europe (Strasbourg).

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Czech economist and politician who served as the second President of the Czech Republic from 2003 to 2013. He also served as the second and last Prime Minister of the Czech Republic, federal subject of the Czech and Slovak Federal Republic, from July 1992 until the dissolution of Czechoslovakia in January 1993, and as the first Prime Minister of an independent Czech Republic from 1993 to 1998. Klaus was the principal co-founder of the Civic Democratic Party, the Czech Republic‘s largest center-right political party. His presidency was marked by numerous controversies over his strong views on a number of issues, from global climate change to euroscepticism, and a wide-ranging amnesty declared in his last months of office.

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René Schwok is the Co-Director of the Master of Advanced Studies in European and International Security Studies jointly run by the European Institute of the University of Geneva and the GCSP. René's research interests also include the European Union, theories of International Relations, external relations of Switzerland and the foreign policy of Nazi Germany. René was born in Geneva and is Swiss. He received his PhD from the Graduate Institute of International Studies. He has been a consultant for various Swiss and European agencies and governments, comments frequently on European issues for the media and speaks regularly at conferences. Author "Switzerland - European Union. An Impossible Membership? Peter Lang, 2010.

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Petr Bystron is the President of the German section of the european think-thank Forum Carolus. He studied Economics and International relationships at the Ludwig-Maximilian-University as well as the Hochschule für Politik in Munich. He is publishing political and economical analysis in numerous german speaking magazines and newspapers as well as in the leading czech media. He is often commenting German political issues for foreign radio and TV stations. Bystron works as political advisor with specialisation for Eastern and Middle Europe. For his achievements he recieved nummerous awards and prizes.

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Pola Cebulak completed her PhD within the framework of the GEM PhD School, Erasmus Mundus Joint Doctorate on Globalization, the EU and Multilateralism. Her mobility action included a double degree at the universities in Brussels and Geneva as well as a research stay at Boston University. She received her legal degree from Humboldt University Berlin, where she also followed the School of Polish Law. During her exchange year at King's College London she specialized in European and Human Rights Law. Her experience includes a traineeship at the Court of Justice of the EU and summer internships at the Polish Embassy in Berlin and Clifford Chance LLP.

25 Years of Freedom

▸ Lech Wałęsa

In 1989 we reached an important milestone in regaining our freedom, and in creating democracy and the free market. We did not lack enthusiasm, joy and especially pride in this Polish peaceful victory. However, some anxieties concerning our immediate and more distant future still flickered somewhere at the back of our minds.

These were fuelled by political uncertainties, problems associated with the destroyed economy and unstable society. After we had our highs and victorious battles, we needed to realise the length and difficulty of the road which we still had to walk to achieve the full victory – the construction of the country we dreamed about in August 1980.

After all, daily hard work is more difficult and less attractive than fine and romantic historic swings or breakthroughs that change the course of history. We took responsibility for an subtle and grey country whose riches had been stolen away. It required not only refurbishment, but also systemic and profound redevelopment – starting from a change in thinking and ways of acting, to the creation of new programmes and structures. This redevelopment has been going on for 25 years, and though we can be proud of it, it still requires much effort, responsibility and wisdom.

At the beginning of the transformation, I knew that we could not do this alone. When faced with such problems, I would always evoke the principle of solidarity: "if you can't cope with something alone, ask somebody to help you, and together you will succeed." Everyone benefits from this. I knew that we had to open ourselves to the world, and that we needed a breath of western dynamism from the other side of the Iron Curtain, which, luckily, was becoming a thing of the past. I was convinced that we needed good programmes, proven examples of success in all walks of life, and the support of wise people.

The many years of the communist regime had distorted our view of the West, so we had no idea how to create it in Poland. Therefore, we had to do everything to make sure it came to us in the form of direct investments. I knew how important it was that serious and reliable global players – from Germany, France, Italy, the United Kingdom and the United States – believed in this new Poland.

Today, we can tell foreign investors from the 1990s: "Look, it was worth it! Thank you!"

We did not want charity, but good cooperation. We had to convince the world that we were not only demolishers, but also skilled builders. We tried to show that Poland wanted to develop on the basis of solid foundations, that it was a good country to do business in, that we had ambitious personnel and good areas for investment, and that we were ready to cooperate. Many global enterprises took their risks as early as at the beginning of the Polish transformation, and decided to back Poland.

Today, we can tell foreign investors from the 1990s: "Look, it was worth it! Thank you! Thank you for your courage and belief in Poles, and for your contribution in the redeveloping of Poland."

In the past I appealed for a new generation Marshall Plan. I hoped for great international planned investments that would kick-start capitalism in the falling socialist economies, and create jobs and new infrastructures. However, political decision-makers lacked courage to implement such visions – courage that private investors had. These were theme who have largely implemented this Plan. They invested their capital and wisdom in Poland. The largest and most serious investors were not oriented merely towards a quick-and-easy profit, but towards long-term investments.

They have been transforming Poland, and have changed our way of thinking about the economy and the West, with which we have caught up a distance of several dozen years at blazing speed.

Of course there are still many areas that need improvement. These include the whole capitalist system.

I have been telling people for years that capitalism is not a perfect system, and that it will not last to see the next century in its current shape. It needs more solidarity, more openness to fellow human beings, respect for their rights and dignity.

In this regard, not only entrepreneurs, the Government and trade unions, but also each and every one of us, play an extremely important role in eliminating the imperfections, and perceiving every institution as one's own place that is worth changing. I dream of capitalism that is a community of economic communities based on solidarity, cooperation, equal opportunities and mutual respect. I can observe that in many places more and more attention is given to the essential social aspect of the economy. I believe that others will also follow the path of solidarity.

For the last 25 years we have made incredible developmental progress. Nowadays Poland looks way different than anyone could imagine 30 or 40 years ago. We have become an important member of the great European family, and our country now stands on solid democratic foundations. The Polish economy is presented as an example of wise economic policy, and many forecasts include Poland among the most attractive countries for foreign investments.

Of course there are still many areas that need improvement: These include the whole capitalist system.

Foreign investments aiming at the creation of new jobs, longlasting production and the establishment of new economic space, have changed Poland. Without them we would have easily toppled under the economic problems of a fallen economy, we would have crashed against even greater public discontent.

It is time to continue the smart building process together with our foreign partners, without whom we would not have achieved so much in terms of development. I can tell you now that the Polish economic transformation has been a tremendous success, also thanks to all our partners.

The quarter-centennial of the Polish transformation has been a success story. For external observers, what has been most spectacular is our economic success: Polish GDP in real terms has grown more than twofold since 1989. This is the best result from among all countries which underwent a transformation process. For twenty five years, we have invariably been a growth leader in the region. We have all won!

How should Academics evaluate the Triple Revolution of 1989, 25 years after the fall of the Berlin Wall?

▸ Prof. Nicolas Levrat

In 2014 were held, in many European Countries, loud commemorations of the Century lapsed since the beginning of the Great War, the 1st World War. And only very few concerning the quarter Century lived since the fall of the Berlin Wall. Why are there so few academic events to commemorate the "collapse" of the Berlin Wall, which took place a quarter of a century ago?

Naturally, societies like to focus their celebrations on a defined, specific date. The 9th of November 1989, the breach into the Berlin Wall was chosen as the symbolic focal point to commemorate the events of 1989. It is nevertheless the whole year of 1989 that was pivotal, for the XXth century, for our continent, actually for the world. It was already in February 1989 that were signed, in Warsaw, the "round-table agreements", between the Communist government and *Solidarnosc*, leading to "partially free" elections in Poland a few months later. Mobilizing against and overcoming the communist authorities in a deep-rooted long-lasting series of protests, across Eastern Germany every Monday after the Summer, or in Czechoslovakia from mid-November onwards, was as important and relevant in this year 1989, than the symbolic events of early November in Berlin.

However, this potential debate between relevant dates for commemoration of the event of 1989 was totally overshadowed by the 1914 celebration. This issue on competing dates of commemoration in Europe illustrates the complexity and richness of the European historical build-up, which conglomerates layers of events, on which we stand to try understanding our present. Is therefore 1989 less relevant in 2014 than 1914? Is Europe still based on the situation that led to the first World War (or maybe the architecture that emerged afterwards, between 1918 and 1920) more than of the post 1989 situation? Is 1989 too close for historians, too far for political scientists, economists and lawyers?

It could also be that the perceptions of the Chain of events, their importance and causality in the build-up and history of Europe is substantially different, when you look at them from Praha or Paris, Budapest or Brussels, Berlin or Warsaw, Strasbourg or Geneva. That is certainly one of the underlying issue that needs to be addressed through the different contributions to this volume.

1989 still remains fundamentally relevant and influential today, because it is the starting point, not just of a single, but of a triple "revolution".

As hinted above, a quarter century may also be an odd period for academics to consider. Still very recent; too close maybe for historians to properly analyze; many documents are not yet openly accessible. On the other hand, 1989 is still close enough to us, so that we can ask witnesses, or even better, major actors, to share their memories, understanding and visions of these events; we thus are very pleased to have the contributions of two major actors, as promoters and actors of 1989 changes, and then Presidents in their respective countries, Mr. Václav Klaus and Mr. Lech Wałęsa.

But at the same time, 1989 is probably too far past for political scientists; too many successive events since have changed both their framework of analysis and their analytical tools. Also likely to be already buried for lawyers, under new Constitutions, thousands of pages of legislations (representing for a large part "*l'acquis communautaire*"), reforms upon reforms that have blurred the perspective. And also a difficult focus for economists, as so many of the fundamentals of economic science have been dramatically altered in 1989, … and since.

Theses methodological difficulties explain why an interdisciplinary approach proves specifically relevant for such a hard-case for academics to analyze. Maybe the different and complementary approaches of various specialists will help us, to get a better description and understanding of what did really happen, why, and how much it still affects us today.

That being said, 1989 still remains fundamentally relevant and influential today, because it is the starting point, not just of a single, but of a triple "revolution".

First, for Central and Eastern Europe, and soon for the rest of the world – let us remember that 1989 also was the year, in May and June, where we witnessed large pro-democracy students' manifestations on Tien-an-men square, much further East that is... – 1989 materializes the fall of the Communist (single-party) political system, for the benefit of the liberal-democratic political values and system, to the point that a US-based scholar figured out he was witnessing the end of history! For better or for worse, history certainly did not end in 1989, and the vitality of Nations – as Hegel used to phrase it – had numerous occasions since to show its relevance and potential nuisances. Notwithstanding, the 25 years of liberal-democratic practice in Central and Eastern Europe have produced diversified results in different national political systems, and the relevance, successes or shortcomings of these developments definitely deserve scrutiny and evaluation after a quarter-century.

Second and simultaneously, 1989 materializes the change of paradigm for the economic governance of Central and Eastern Europe. System change appears even more rapid and radical that in the political realm, and planned economies suddenly and immediately gave way to market economies. With solid economic growth for most of these countries – which did not exclude some periods of downturns, sometimes violent – and a whole series of economic transitional mechanisms, that had to be invented. How to fairly privatize a government-run economy? How to guarantee social welfare in both a transitional economic period and in a new liberal market economy? Twenty-five years of this succession of transitions first, and then market economy in Central and Eastern Europe seems a long-enough period for examining the merits – or flaws – of economic experiments and practices that have been implemented in these Countries. And as we shall see below, leads to diverging appreciations on the validity of the process.

Third, with slightly less simultaneity since it will take until 1991 to fully materialize, 1989-1991 initiates a geo-political shake-up whose aftershocks are still being strongly felt, in Eastern Europe... and everywhere else. The bipolar world that had structured, since the Second World War, both the World and the European stages was suddenly gone. With incommensurate repercussions on the world governance; for example, for the first time since the UN creation in 1945, the Security Council was able, in 1990, to adopt a Resolution authorizing sanctions against a State (Irak) which had invaded a neighboring State (Koweit), up to authorizing – for better or for worse – a military intervention. It led to amazing an unthinkable developments of international law (responsibility to protect) and potentialities for global governance. As another international consequence of 1989, the World Trade Organization – which had failed to materialize following World War II – could finally be created in 1994, as a by-product of 1989 events, constituting such a breakthrough in International relations that a non-irrelevant number of scholars, consider that WTO could be the appropriate place for the emergence of global governance mechanisms.

However important the impact of 1989 on the world geo-politics, it was even more dramatic on the European scale. The division of Europe, and not only Berlin, by a wall, or an iron-curtain, was no-more. European Geo-politics was to be fully rethought. But where to start from? Scratch? 1920's? 1945? Also an apparently obvious question, but still difficult to answer today is open by the fall of the Berlin wall: what do we mean by Europe? Are there geographical or new geo-political borders to Europe? Could European horizon be the European Union? If yes, what to do of Ukraine (as we know it is a currently very hot issue), but also of Norway or Switzerland? If EU is not to be the horizon, then how should Europe be organized? Or not organized at all?

As regard intra-EU geo-politics, the equilibriums between large West-European States (France, Germany, Italy and United Kingdom which all had more or less the same population) has been shattered by German reunification. Also, the relatively rapid enlargement of the EU to Eastern Europe imposes to find new equilibriums inside EU, and maybe even a "raison-d'être" to a renewed European project. Especially since 1989 also opened the way for a change of the balance of power on the global level; whereas Western Europe was strongly and safely seated in the driver-seat of the World (not alone, naturally, but think that the G-7 included 4 European States out of 7) until 2008; despite its reunification or enlargement (the choice of wording is matter of perspective) and the ensuing increase in population and capacities, enlarged Europe is sliding to a less dominant position (to say the least) on the world stage. To follow-up on the G-governance mechanisms example, the G-7 was transformed to a G-20 in 2008; the new G-20 still only comprises 4 European States, no more… Comparing four out of seven States to four out of twenty hurts hard. So Europe, Central, Eastern, Western, Southern, Northern, or maybe together, has to think its future under a new global pressure, which may alter the conditions for analyzing, both the current situation and the future prospects.

But in the real world, these three dimensions of the 1989 revolution may not be disentangled.

Naturally, we academics, tend to divide and categorize issues, to have them fitting within the boundaries of our disciplinary approaches. Thus, these three dimensions of the post-1989 revolution might, in classical academic governance, have led to three different research efforts and books. But in the real world, these three dimensions of the 1989 revolution may not be disentangled. They not only happened and developed simultaneously, but they have been feeding each other, and one is also the result, or the pre-condition, of the other. This is why we try here to grasp them together.

This is why we have chosen to gather very heterogeneous expertise to discuss this 25 year landmark of the 1989 revolutions: actors of 1989 and post-1989 and academics from various disciplines and perspective. Were invited to contribute to this evaluation assessment: Václav Klaus, former President of the Czech Republic; Lech Wałęsa, former President of Poland; Andreas Gross, member of the Parliamentary Assembly of the Council of Europe; Dusan Sidjanski, Former Special adviser to the President of the European Commission, and Professor emeritus from the University of Geneva; Richard Sulik, former President of the Parliament of Slovakia and currently MEP; Prof. Thilo Bodenstein, Central European University; Mr Rudolf Hermann, Journalist at NZZ; Prof. Miroslav Jovanovic, University of Geneva; Prof Zdzislaw Kedzia, University of Poznan; Mr. Tomáš Munzi, Head of the Czech Entreprise Institute; Prof Gerald Schneider, University of Konstanz; Prof. René Schwok, University of Geneva; Prof. Dusan Triska, University of Economics, Prague. So what does such gathering produce as an evaluation of the current relevance and significance of these past events?

First, there seems to be an agreement that democracy, as resulted from the 1989 events, is and remain a central and fundamental value in Europe, as was notably underlined by

Gross and Wałęsa. However, twenty-five years after the 1989 events, Sidjanski points out that democratic values may be at risk, due to the current wild economic crisis that hits Europe since 2008. Actually, according to him, both democracy and European integration may be in danger in 2014. Less pessimistic, Klaus and Sulik consider that a liberal economy, with as little constrains as possible by social norms but sufficiently democratic support a stable and secure legal and political environment authorizing economic growth is a sufficient achievement; according to them, the 1989 events did allow to reach such stage.

Actually, Klaus underlines that the main element of the1989 events is the fall of the planned economy model, or in his words the end of subordination of the economy to a political ideology. In that respects, he expresses worries that only twenty-five years after this achievement of 1989, the current wish of the EU members States to develop and strengthen the European single currency (€), may constitute a renewed example of trying to subordinate the economy to a political project. A strategy that, according to him, the 1989 legacy should prevent. Further, he considers the European social model as an attempt from Western Europeans to preserve the political acquis and priorities of the pre-1989 Western Europe, which as a side effect prevents the Eastern Europeans to continue and complete their economic transformation towards a fully liberal economy. Klaus discourse was strongly opposed by Sidjanski, as outgoing special adviser to the President of the European Commission for the past ten years.

So is this opposition real, or only a matter of diverging perceptions. As Kedzia underlined, perception of facts is as important as facts themselves. However, is the strong criticism of the EU by the former Czech President, 25 years after the fall of the Berlin Wall, 10 years after Czech integration into the EU, justified and relevant or is it grossly exaggerated?

Klaus, supported by Sulik, considers that EU is now largely overstretching its interventionist practices into national economic and political dynamics, and has become rather harmful than helpful for the economic growth of its member States. On the other hand, Gross, Jovanovic, Sidjanski, Schneider and Schwok believe that the 1989 events and their follow-up made the EU, and eventually other European institutions (such as the Council of Europe), more relevant and useful than they were before. So who is right, who is wrong? As Liebich underlined in his intervention, it is widely agreed that the West influenced the East after 1989, but it is largely underestimated how much the integration of Eastern European States into the EU also transformed the West, and naturally the EU.

Actually, a key for providing an understanding of the cause for this difference in perception was quite relevantly proposed by Bodenstein and Triska. They each in their own words, showed that in the transition process, for practical reasons, liberalization and privatization come first, institution building and acquisition by public authorities of a redistributive capacity only being realized later. On that precise issue, and basing their argument on the current situation in Russia, both Gross and Kedzia warn us of the risk of a loss of political trust by citizens in political leaders, if the process is not pursued to its end (in clear, if the process is stopped after the liberalization and privatization phase without building the social framework allowing for a reasonable degree of redistribution). Thus, according to them, an unfinished process may weaken democracy, and consequently endanger peace and macro-economic stability, which are pre-condition for liberal economic reforms.

Both sides reasoning seem largely tautological, making it hard to decide on their respective validity on a purely discursive analysis. However, as was clearly underlined by Triska and Munzi, as long as the rule of law principle remain in application, the organized transition towards a stronger social system of redistribution, or the economic consolidation in a genuinely neo-liberal perspective, may both be led, according to expressed democratic preferences and for the benefit of citizens.

So it seems to me that it is where the diverging understanding of the current impact of 1989 events, twenty-five years later, finds its roots. For some contributors to this book, the transition is not yet over (Bodenstein, Jovanovic and Schneider). For other it is over and was worth it, Kedzia and Wałęsa basing their appreciation on political/moral consideration, Herman and Schwok on economic arguments. However, two contributors, Klaus and Sulik, not only consider the transition over, but also that the process of transformations overstepped the momentum initiated by the 1989 events. So clearly, 1989 may for all be considered as a critical juncture, but the debate about its transformative potential is still open. It leads some authors not only to consider it over, but for that same reason that future change will be more or less impossible (Bodenstein and Triska). To these, Wałęsa replied that a critical juncture is not really needed; based on his own experience and in his own words, he stated that "the battle against communism was so easy to win that nobody noticed there was a battle for years." Thus 1989 was not in his view so much of a critical juncture than one specific stage in a long voluntary process of change, initiated by civil society and social movements active within the system. He thus believe that further change is still very possible, and see in some recent protest movements against the excess of capitalism, some similarities with the social mobilization against communism of the 1970's and 1980's.

A middle of the road approach was towards potential additional changes was proposed by Jovanovic and Gross, both underlying that the relationship between economic liberalization and a social political project has to be kept within a reasonable balance, to the risk of failing to respect the genuine nature of liberal democracy. Failing to maintain that balance would constitute a serious threat, not only to values and principles of democracy and European integration, but also as regard peace and stability, as was pointed out by Schwok. However, as was rightly pointed out by Schneider, external (security) threat to democracy may help strengthen cohesion. In that respect, one has to note that cohesion and stability are antonymic to transition. So whether authors privilege stability or change may strongly influence on the current evaluation of the original 1989 momentum for change. Thus at this stage, 25 years after the fall of the Berlin wall, it seems that we are still unable to agree on to whether the transition process is over. I would actually be tempted, to conclude this introduction, by coming back to Liebich's argument, stressing that the transition did not only concerned central and Eastern Europe, but the whole of Europe and especially EU; in that respect, it appears obvious that the transition of EU as an aftershock of the fall of the Berlin Wall is far from being over. That remark would certainly constitute a perfect starting point for a research leading to the assessment of the same question for the 50th anniversary of the fall of the wall, in 2039. In between, competing narratives of the 1989 events and their importance will most likely continue to co-exist. May the present book be considered as a contribution to this ongoing to this ongoing debate.

25 Years after the Fall of Communism: Liberty Rapidly Reborn but Soon Under New Attack[1]

▸ Václav Klaus

Many thanks for the invitation. I am very glad to be in Geneva after a very long time and to see here many friends and colleagues connected with the historic events which happened 25 years ago. In all countries of Central and Eastern Europe, we are remembering the 25th anniversary of the fall of communism these days.

Communism, one of the most irrational, oppressive, cruel and inefficient systems in history ceased to exist suddenly and relatively quietly 25 years ago. It fell at the same time in all Central and East European countries and with some delay also in the Soviet Union – in spite of all the non-negligible differences among the countries of the former Soviet bloc. This fact proves that the common features – even though we all supposed that we were unique – were stronger.

This radical and far-reaching breakthrough brought us many positive improvements. We were happy, joyful, full of hopes. We were fascinated with ourselves, praised by friends and supporters in the rest of the world. We enjoyed both their appraisal and our rapid acceptance in the community of free countries. The overwhelming majority of citizens of our countries have no doubts that they live in a much better world now.

It is also the appropriate time to say that when we became part of the free world we had mixed feelings. We realized that the world did not quite understand us, our fate, our experience, our dreams and ambitions. The degree of the lack of freedom, of the irrationality of the communist system and of the oppression we had to go through was

[1] Speech at the conference After the Fall of the Berlin Wall: 25 years of Market Economy in Central and Eastern Europe, University of Geneva, Geneva, November 7, 2014.

highly underestimated. On the contrary, the degree of our understanding of the free world, which we were not part of for such a long time, our ability to behave quite normally, our level of education, our knowledge of our common European culture, proved to be higher than most people in the West expected. Despite the long-lasting communist propaganda and indoctrination, we knew more about the capitalist West than the non-communist world knew about us. I am afraid this asymmetry is there even now.

Communism still remains misunderstood. It ceased to be discussed and analysed too early, **especially its later stages,** its gradual weakening, emptying, and softening, as well as its complete resignation on defending itself or, luckily, on fighting back. In the final stages of communism practically nobody believed in the original pillars of its ideology – in Marxism and its derivative, the Communist doctrine. The only books and studies which continued to be published have been about communist earlier, much uglier periods, about the "gulag" era (in the Soviet Union) or about the 1950s in other communist countries when people were killed, not just jailed or fired from their jobs.

Not to correctly interpret the later, in many respects milder stages of communism makes it difficult to understand the rather sudden and bloodless end of communism, to comprehend all the tenets of the post-communist transition, and to be able to sharply look at the present era.

I have to claim that the post-communist transition (or transformation) was a success.

The communist regime was in many respects already an empty shell. **As a result, communism melted down (or passed away), it was not defeated**. There are people and groups of people who don´t like this interpretation of events, who claim that they themselves defeated communism which is, however, not true. I don´t want to diminish anybody´s merits, but communism in 1989 needed just one last straw. The subsequent chain reaction of millions of people happened spontaneously and automatically.

Everyone – especially in the West – expected that the end of communism would bring about a shock, chaos, disorder, if not a civic war. As we know, this did not materialize. Even in the Soviet Union, where communism lasted more than seven long decades, it foundered more or less quietly. All of us who knew the book by Andrei Amalrik "Will the Soviet Union Survive Until 1984?", written at the end of the 1960s, expected much more dramatic events. **This relatively quiet end reveals the weakness and effective defencelessness of communism at the end of the 1980s**.

With all my criticism of various details of subsequent developments in my country and elsewhere – which I experienced both as a citizen and as a politician who had been during these years continuously in leading political positions – **I have to claim that the post-communist transition (or transformation) was a success**. The criticism of its particular aspects is undoubtedly justified and more than welcome but its main positive tendency can´t be disputed.

The decisive part of the transformation process was massive, wholesale privatization.

In my country we – relatively very rapidly – succeeded in establishing an elementary institutional structure of a standard, full-fledged parliamentary democracy. It proved that it was not necessary to constructivistically create a political system – it was sufficient, to use the economic terminology, to open the entry into the political market. That was enough.

This favourable political structure lasted till the end of the last decade, till the outbreak of the 2008-2009 financial and economic crisis. At that moment different political tendencies started to prevail. It led to the shift from standard politics to postpolitical, post-democratic arrangements, from authentic, ideologically well-defined political parties to ad hoc political projects based more on marketing than on ideology or party membership.

It was not a consequence of the economic crisis. The crisis only accelerated it. I am afraid this is a more general European trend. **It is the consequence of the more and**

more destructive nation-state weakening, if not liquidating, EU arrangements and of the strengthening of global governance. **It is also a result of the gradual replacement of traditional European and Western values with politically correct norms based on new isms – such as cultural relativism, human rightism, multiculturalism, NGOism, feminism, homosexualism, environmentalism, juristocracy and mediocracy**. Classical political democracy is, I am afraid, over. I don´t feel the triumph of liberty as it is expressed in the title of this gathering.

On the economic side, we organized a rapid systemic change. We proclaimed very early and quite explicitly that we wanted capitalism. **We resolutely refused all dreams about all kinds of "third ways"** or about a possible or desirable convergence of existing economic and political systems. What we are getting, however, is not the "first way". It is the old, well-known "second way", the European socialism. This is another reason for our frustration.

What we really wanted 25 years ago was **to avoid a non-transformation**. We didn´t want to give a chance to all kinds of rent-seeking groups which sought to preserve the status quo and/or steal the whole transformation process to the benefit of their vested interests. This influenced our position vis-à-vis all versions of **gradualism which we considered a non-reform**. We did not believe that gradualism was a realizable reform strategy (in a politically free society) and we, symmetrically, disagreed with the term "shock therapy" both as a useful reform concept and as a description of reality in our country and elsewhere. We refused to accept the "shock therapy vs. gradualism" dilemma even now discussed in the economic literature as meaningful alternatives. The term "shock therapy" is not an analytical term. It is a political accusation used by socialists like Joseph Stiglitz as a political attack.

We considered both the economic and political reforms interconnected and indivisible. To separate them à la China was in Central and Eastern Europe impossible. **The unrealistic concept of gradualism was (and is) based on the belief in the possibility of a detailed orchestrating of reforms**. It would have been, however, possible only with the absence of political freedom which was not our case.

We knew that the transformation project had to be ours, based on our ideas and on our realities. We did not consider ourselves representatives of international institutions and we did not feel any reason to please them. We tried to find our own "Czech way" and to give the people a chance to be part of the game, not to be just passive observers.

The decisive part of the transformation process was massive, wholesale privatization. In our case, it was based on several ideas which are worth repeating:

- our goal was to privatize practically all the existing state-owned firms, not just to allow the setting up of new firms on "green fields";· fast privatization was considered to be the best contribution to the much needed restructuring of inefficient state-owned firms (we did not believe in the ability of the government to restructure the firms prior to privatization);

- privatization of firms in the real economy couldn´t wait for the completion of the privatization of banks (it had to go parallely);

- because of the lack of domestic capital (which did not exist in the communist era) and because of the very limited number of serious potential foreign investors, firms had to be privatized at a low price. This idea led us to the concept of "voucher privatization". The concept played in our country an important, but not dominant role which is very often misunderstood. Only less than one fourth of the Czech privatization was realized by means of voucher privatization.

From the very beginning, **the Czech reformers knew that they had to privatize the economy they inherited as soon and as fast as possible**. We did not want to leave our to-be-privatized-firms in an unavoidable "pre-privatization limbo" in which they were rapidly losing their value. For that reason, we did not have any great interest in the maximization of the size of privatization proceeds. The fast speed of privatization (not its proceeds) was seen as an asset, not a liability.

At the same time, we liberalized, deregulated and desubsidized the economy quite radically and early. This liberalizing tendency lasted, to our great regret, only part of the previous 25 years. Partly due to the loss of our own reform momentum (for domestic political reasons), but mostly because of our approaching and finally entering the EU, we started a reverse process. That is why, **our economy is more regulated and subsidized (and harmonized and standardized) now than 10-15 years ago**. The final blow came with the recent financial and economic crisis and with the methods of its "treatment" by means of a very extensive government interventionism.

In any case, our economy happens to be more regulated and more subsidized than we imagined in the moment of the fall of communism. We did not believe it could ever happen. It seemed to us that the masterminding of the economy from above was so discredited by the communist experience of ours that it cannot return. We were wrong.

We also assumed that everyone understood that the government failure is inevitably much bigger than any imaginable market failure, that the visible hand is always much more dangerous than the invisible hand of the state, that the vertical relations in society must be less productive (and less democratic) than horizontal relations, etc. Again, we were wrong.

Twenty five years ago, I warned against creating a negative expectations-reality gap because it would have undermined our reform process. I have to accept that **I myself experience a huge expectation-reality gap now**. I expected to live in a much more free, democratic society and economy than it is the case today.

It was partly caused by the victory of social-democratism in our own country, partly by the import of the European economic system – its overregulation, its high taxation and redistribution, its welfare state procedures, its fascination with all kinds of antimarket measures (connected nowadays mostly with environmentalism, with this antidemocratic social ideology and political doctrine which successfully hides its real substance and aims pretending that it cares about nature, environment, our Blue Planet). We may be oversensitive in this respect due to our long-lasting communist experience but we see many similar phenomena, tendencies, ambitions, arguments now around us.

To allow this to happen would mean that we didn´t learn from history, especially from the communist era. It would mean that our celebrating the end of communism is inappropriate. It is coming back in different forms, under different flags and slogans, without our sufficient resistance.

Critical Junctures and Economic Transition after the Fall of the Berlin Wall

▸ Thilo Bodenstein

1. Introduction

The fall of the Berlin Wall and the end of the socialist systems in 1989 brought an unexpected chance to build democracy and free market economies in the former communist countries. During the long run-up to the system collapse the countries of the Soviet bloc had suffered from steadily declining growth rates leading to protracted economic crisis and falling living standards. Economic crises had also eroded political legitimacy of the socialist systems and had undermined trust in governments that proofed to be incapable of reform. The initial period after the fall of the Berlin wall was a period of relief and hope that the socialist societies would finally be able to embark on the route to Western liberal and democratic systems. The political scientist Francis Fukuyama coined the term 'the end of history' to summarize the aspirations of the post-communist world (Fukuyama 1992). However, rebuilding their economic and political system turned out to be an arduous endeavour for many transition countries. The task they took on was formidable, to begin with, akin to 'rebuilding a ship at sea' (Elster/Offe/Preuss 1998). But twenty-five years on, the group of transition countries has become so diverse that observers proclaimed the end of the transition paradigm (Carothers 2002). Some countries are on a good track to fulfil the initial promises and are catching up with the liberal West. Others were on a good track, but are now backsliding. Other countries are stuck between their socialist legacies and partial reform while a few countries in the transition group decided not to try to rebuild their ship in the first place and to freeze their systems as they were.

The enormous diversity of reform trajectories calls for explanation and there is no shortage of narratives accounting for it. These can be grouped into several different lines. A first line of debate centred on whether simultaneous ('big bang') or gradualist economic reforms would have a better prospect of success. The virtues of simultaneous reform – all economic reforms at the same time – were seen in the non-separable nature of reforms. Various economic reforms depend on each other and were bound to fall if introduced gradually (Murphy/Shleifer/Vishny 1992) and the short 'honeymoon period' should not go wasted (Balczerowics 1994). The perils of partial reform were seen in the establishment of rent-seeking coalitions that take advantage of the windows of opportunity created by gradualism (Hellmann 1998). Gradualists, by contrast, argued that economic reforms would be more successful if introduced in a sequenced, logical order minimizing the long-term costs of reform (Przeworski 1991; Dewatripont/Roland 1992, 1995). Gradualism would also give room for policy learning necessary to correct early mistakes (Murrell 1992). Political consensus for reform would be more stable under a gradual approach, since costs of reform would be more equally spread across society (Przeworski 1991).

The initial period after the fall of the Berlin wall was a period of relief and hope .

Another debate focused on the broader picture of transition and wondered whether democratic reforms had to be postponed in order to secure economic reforms. Claus Offe (1996) argued that it might be necessary to postpone democratisation until market reforms succeed. He feared that losers of reform and winners of partial reform might halt the reform process implicitly assuming that non-democratic governments are benevolent and have a vested interest in the public good. This proposition did not go uncontested. Opponents to the 'autocratic advantage' theory argued that democratisation should precede reforms. Regular elections lead to more frequent leadership turnovers putting pressure on governments to perform well and also allow new elites to enter the political stage, disrupting rent-seeking networks.

Changing the perspective from domestic politics to international factors, scholars also looked at the role of international institutions and bilateral support in the reform process. International organisations such as the IMF or the World Bank were expected to help sustaining reform through their conditional lending programmes (Collier 1997). Conditionality, however, was not enough to 'buy reforms'. The enforcement mechanisms of the Bretton Wood institutions were not always credible (Harrigan 1996; Stone 2002) and there were large asymmetries in lending mainly due to the varying strategic importance of post-communist countries (Dabrowski 1998; Lundborg 1998).

The diversity in reform outcomes has also been explained from a historical perspective arguing that long term determinants such as culture and civil society mattered (Bruszt et al. 2009). Related to this is the argument of initial conditions. There is a stunning correlation between a post-communist country's geographical location and the duration of its communist rule on the one hand and the extent of economic reforms on the other hand (Treisman 2014). How some immutable variable like geography impacts on human agency may not very clear, but the legacy of communism hints to the role of deeply rooted institutions in structuring the policy arena for reforms. But if the length of communist rule was the decisive determinant for reform success, there would be something fatalistic about the whole political enterprise of restructuring the economy. Yet this contribution argues that institutional legacies matter, but there are windows of opportunity when legacies can be shifted into a new direction.

The contribution adds a new aspect to these grand debates by arguing that success or failure of economic reforms was partially an unintended consequence of early political decisions that structured the new political systems for years to come. Starting from 1989 all socialist regimes collapsed one after another within a very short period laying the institutional foundations of the post-communist systems. In that sense, the post-communist countries went through a brief period – a critical juncture – that was decisive for developments to follow. Analyzing the effect of critical junctures is not only important for a more detailed understanding of 25 years of reform in the post-communist countries, but also for future reform efforts in other parts of the world. Democratic transitions coupled with economic reforms have taken place in many other regions of the world with similar challenges of dual transition (c.f. Greskovits 1998).

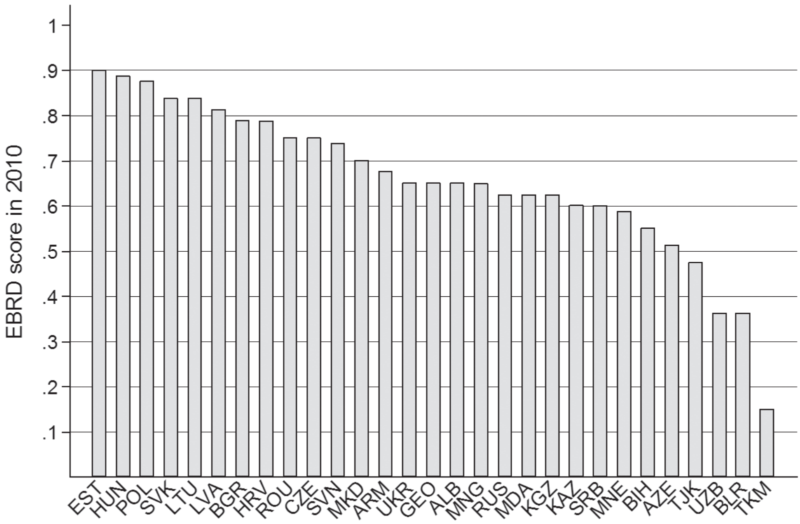
The contribution is structured as follows. The following section discusses the reform indices and summarises the extent of reforms in the post-communist countries over the past 25 years. The third section discusses the logic of critical junctures. Section four analyses the impact of critical junctures on reforms. The last section concludes.

2. Reform patterns

At the beginning of the 1990ies all transition countries started from the same point – they all had the same socialist economic systems. The task was to create market economies on the vestiges of planned economies. The amount of reforms to be done was overwhelming and it is challenging to summarise reform success in a few indicators. A first question to be asked is how to measure market-creating reforms in the first place. The European Bank of Reconstruction and Development (EBRD) started to measure reforms early on and until today it remains the only reform indicator of the post-communist countries we have of. Although there might be legitimate arguments about the validity of some aspects of the indicators (Myant/Drahokoupil 2012) no one has developed alternative indicators of economic reforms in post-communist countries.

The EBRD has been measuring reforms in its yearly Transition Reports since 1990 on various dimensions. The Transition Indicators are judgements of EBRD's Office of the Chief Economist about reform progress in each country and are on an ordinal scale ranging from 1 to 4.3. The exact meaning of each number specifically depends on each reform dimension, but generally speaking 1 depicts little reform progress, 2 is substantial progress, 3 is significant reform, 4 stands for comprehensive reform and 4.3 shows reforms standards and performance typical of advanced industrial economies. The Transition Indicators cover following dimensions of reform: Large-scale privatization, small-scale privatization, governance and enterprise restructuring, price liberalization, trade and foreign exchange system, competition policy, banking reform and interest rate liberalization and securities markets and non-bank financial institutions.[1] How did reforms unfold in the post-communist countries? Figure 1 takes a first look.

[1] The codebook of EBRD's Transition Indicators is available under: http://www.ebrd.com/cs/Satellite?c=Content&cid=1395237866249&d=&pagename=EBRD%2FContent%2FContentLayout (accessed on February 8, 2015).

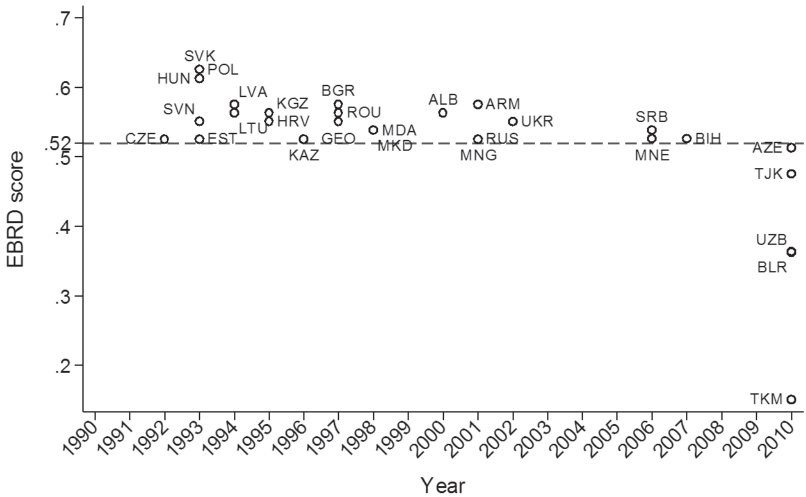


▸ *Figure 1: EBRD Transition Indicator in 2010*

Figure 1 shows the average of all EBRD reform scores in 2010. The original scaling of EBRD's Transition Indicator has been normalised between 0 and 1 to ease interpretation of the data.

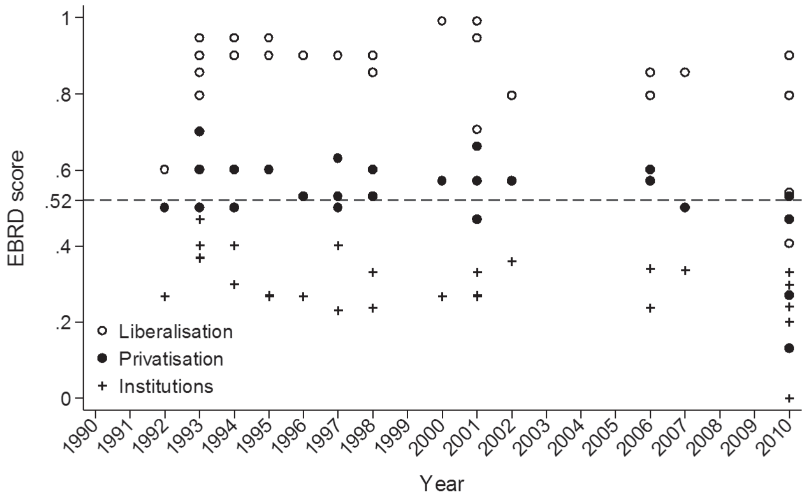
All transition countries started with average reform scores around 0 in 1990.[2] In 2010, Estonia is leading the ranking of reform progress, while Turkmenistan is trailing behind with almost no substantial reforms at all. Also, the leading eleven countries are all EU member states. The mean score in 2010 is 0.65 – the reform level of Albania, Georgia and Ukraine – with a standard deviation of 0.17. The reform scores of Tajikistan, Uzbekistan, Belarus and Turkmenistan are a full standard deviation below the mean and those of Lithuania, Slovakia, Poland, Hungary and Estonia one standard deviation above.

[2] Some countries started reforms already before 1990. Hungary, for instance, had introduced a two-tier banking system in 1987, followed by a modern taxation system includit VAT and secondary trading of corporate and municipal bonds in 1988 (Bokros 2014). Yogoslavia, Poland and Hungary have EBRD scores higher than 0 in 1989.



▸ *Figure 2: Year of reaching the median value of the EBRD Transition Indicator*
Data Source: EBRD (2014)

Figure 2 shows the speed of reform of the transition countries. It depicts the year in which a country has reach the median EBRD reform score (0.52) of all observations from 1990-2010. The 50th percentile may be somehow arbitrary, as some countries never reached it. But it gives an adequate picture of who were the fast reformers and who were the laggards. The Czech Republic was the fastest reformer and reached the median already in 1992, followed by Estonia, Slovenia, Hungary, Poland and Slovakia in 1993. It took more than a decade for Albania, Russia, Mongolia, Armenia and the Ukraine to reach the median. Montenegro, Serbia and Bosnia only reached the median in 2006-7, while Azerbaijan, Tajikistan, Uzbekistan, Belarus and Turkmenistan remain below the sample median even in 2010.



▸ *Figure 3: Subtypes of the EBRD Transition Indicator*
Data Source: EBRD (2014)

Figure 3 gives further inside into the reform patterns. It groups reforms in three different reform types – liberalisation (price liberalisation, trade and foreign exchange liberalisation), privatisation (large-scale privatisation, small-scale privatisation, governance and enterprise restructuring) and institutional reforms (competition policy, banking reform and interest rate liberalization, securities markets and non-bank financial institutions). Figure 3 shows again the years when a country reached the median, but this time disaggregated into the three sub-types of reforms. What we see is that liberalisation reforms were the most advanced in all countries, also for those countries that reformed quickly. The extent of privatisation reforms is somewhere in between, while in most transition countries institution building reforms are clearly lagging behind. Thus, the path of reforms in the transition countries started to diverge already at an early stage and in 2010 the picture of reforms has become very diverse. However, despite of reform success liberalisation reforms have been the most successful, whereas institutional reforms are still lagging behind, even in the most advance transition countries. The next section looks as how critical junctures may account for this diversity.

3. Critical junctures

There are moments in history of countries that decisively shape the course of events for a long time to come. These moments are referred to as 'critical junctures'. The one characteristic that sets the transition of the post-communist countries apart from macro-historical processes in other regions of the world is the almost identical timing of regime change under highly similar conditions. Arguably, the transition countries shared the same communist system. They were similar in terms of political and economic institutions, albeit with small variations. Decisive change towards a new system took place in a very narrow period of time between 1989 and 1992.

Critical junctures is not an uncontested concept. There are competing concepts in the social science literature with a similar, but slightly different meaning. Most prominent is the concept of path-dependency (c.f. Pierson 2000, Collier/Collier 1991, Jones-Luong 2002, Mahoney 2002). The idea of path dependency stipulates that institutional choices made at some point in time may have a lasting effect on the range of choices available to political actors. The idea of a critical junction is logically entailed in path dependency, but often not accounted for explicitly (Capoccia/Kelemen 2007). The focus of the concept of path-dependency is more on the reproduction of institutions over time, rather than on the starting point – the critical juncture – as such.

The neglect of critical junctures in the path-dependency literature may well have to do with the vagueness of the concept itself. For instance, the duration of an event to qualify as critical juncture is loosely defined. In their study on critical junctures and regime dynamics in Latin America Collier and Collier (1991) defined processes that lasted up to 20 years as critical junctures. But such a long duration of critical juncture may easily qualify as institutional change. Moreover, studies based in the tradition of institutional economics conceptualise the role of agency in institutional change in a way that obscures periods of critical junctures. In this vein, critical changes are seen as a series of microscopic choices or a series of small random events that trigger long-lasting effects (c.f. Arthur 1989). In the study of reforms in the transition countries the neglect of critical junctures has similar reasons. The emphasis on long-term conditions refers to the concept of path dependency without further asking how the conditions emerged in the first place. For instance, the argument that civil society developments during communism had a lasting impact on later reforms (Roland 2012) refers to the concept of microscopic, random change rather than critical junctures.

The critical juncture in 1989-1992 created institutional constraints for future reforms.

Capoccia and Kelemen (2007: 348) define critical junctures as "relatively short periods of time during which there is a substantially heightened probability that agents' choices will affect the outcome of interest". Critical junctures, thus, have to be of a short time period. What this means is that the duration of the critical juncture should be significantly shorter than the subsequent period that is constrained by them. How long that is will certainly depend on the specific policy area, but as far as post-communist reforms are concerned the period of 1989-1992 certainly qualifies as a short and decisive juncture for the events of the subsequent 25 years. Also, critical junctures have an identifiable unit of analysis and are consequences of decisions of by agents, not the result of micro or random events. The unit of analysis in case of the transition countries is institutional settings – round tables, party negotiations, and parliaments – where agents had for a short time a much larger choice of institutional outcomes than during 'normal' times. Finally, periods of critical juncture should have a heightened probability that their choices have a long-term impact on subsequent outcomes relative to 'normal' times. All these characteristics of critical junctures are present in the regime changes of the transition countries, which is why the concept may be meaningful for the analysis of economic reforms.

The critical juncture in 1989-1992 created institutional constraints for future reforms. Within a short period of time agents had to negotiate new 'rules of the game' or in some cases decided not to change the rules much. Bodenstein and Schneider (2006) present a game theoretical model that covers the most important features of that critical juncture. The model identifies three types of actors – regime hardliners, who are against democratic reforms and against economic reforms; regime softliners, who are against democratic reforms but who support economic reforms; and the public, which demands democratic reforms, but no economic reforms. Each group of actors can have either credible threat or is lacking credible threat. In addition, hardliners consist of resistant, in-between and 'whimpy' hardliners. Table 1 shows sub-game perfect equilibria of the transition game.

▸ *Table 1: Outcomes of the transition game Source: (Bodenstein/Schneider 2006)*

		'Resistant' hardliners	'In-between' hardliners	'Whimpy' hardliners
Softliners (with credible threat)	Public (with credible threat)	Status quo	Economic reforms only	Double transition
	Public (w/out credible threat)	Status quo	Economic reforms only	Economic reforms only
Softliners (w/out credible threat)	Public (with credible threat)	Status quo	Political change only	Political change only
	Public (w/out credible threat)	Status quo	Status quo	Status quo

▸ *Source: (Bodenstein/Schneider 2006)*

As Table 1 shows only one outcome results in a double transition (democratic and economic reforms). When softliners with a credible threat negotiate with representative from the public who have a credible threat and 'whimpy' hardliners, the result is a double transition. When either the softliners or the public lack credible threat and hardliners are not resistant, than the outcome will be economic reforms or democratic reforms only. Whenever resistant hardliners are involved the final outcome remains the status quo.

Critical junctures should work through two causal channels. On the one hand, they can open the path towards democracy. More democratic transition countries were better able to implement reforms (Treisman 2014). The second channel is the creation of veto players and of rule of law. The introduction of checks and balances gives voice to stakeholders to lobby for reforms. But maybe more importantly, veto players and rule of law raises the cost of arbitrary reform reversal. Once a certain level of reform is reached it will be more difficult to undue reforms. Frye and Mansfield (2003), for instance, show how veto players have spurred foreign economic reforms in the transition countries.

More precisely, the organisation and outcomes of the first founding elections of the transition countries were decisive for subsequent developments. Fish (1998) categorised the transition countries' initial elections according to who won them (victory by old elites or reformers), whether elections results were annulled or not, whether elections were free and open and whether the elections involved all important offices or only part of it. Fish's (1998) index scores from 1 to 5, where higher numbers depict free, fair and open elections. Table 2 shows the index.

▸ *Table 2: Initial elections in transition countries*

0	1	2	3	4	5
Azerbaijan	Kazakhstan	Moldova	Albania	Armenia	Croatia
Belarus	Tajikistan	Ukraine	Bulgaria	Macedonia	Czech Rep
	Turkmenistan		Georgia	Russia	Estonia
	Uzbekistan		Kyrgyz Rep	Slovenia	Hungary
			Mongolia		Latvia
			Romania		Lithuania
					Poland
					Slovak Rep

▸ *Source: Fish (1998)*

The next section explores to what extent these transition modes influenced economic reforms in the transition countries.

4. Empirical assessment

The key dependent variable of the empirical assessment is the EBRD Transition Indicator and the indicators of the three sub-reforms – liberalisation, privatisation and institutional reforms. The key independent variable of interest is the role of critical junctures conceptualised as *Initial elections* (Fish 1998). As critical junctures have shaped the political arena, this section investigates in more detail the pathways of reform. First, in order to assess the effect of overall level of democracy, the variable Democracy is included which is the Polity 2 indicator of the Polity IV database. It ranges from –10 to +10, whereas –10 is a perfect autocracy and +10 a perfect democracy. Moreover, one pathway of democracy may work through checks and balances. Checks and balances are measured by the variable *Executive constraints* from the Polity IV database. It ranges from 1 to 7 (1=unlimited authority of the government, 7=executive parity or subordination). Second, critical junctures may shape the public space and other non-governmental institutions such as rule of law. The measurement of this dimension is *Civil liberties* (Freedom House). The variable covers freedom of expression and beliefs, rule of law, associational rights and personal autonomy. In order to make the coefficients of *Civil liberties* easier to interpret the coding of the variable has been reversed, so that higher values stand for more liberties (1=least free, 7=most free). Finally, *Fractionalisation* depicts the number of parties in parliament. It is different from *Executive constraints*, which measures institutional rules. *Fractionalisation*, by contrast, grasps informal veto players conceptualised as the extent to which finding compromise in parliament may be hampered by partisan considerations. The variable is a Herfindahl index and is based on data from Armingeon et al. (2011).

In a first step the the role of historical legacies is investigated. Treisman (2014) argues that the length of communist rule and the geographical location of transition countries is a good predictor of reform success. To test this assumption the variables *Years under communist rule*, *Longitude* and *Latitude* are used. In addition following covariates are included in the estimations. *GDP per capita* measures a country's level of wealth; *growth* is the yearly GDP growth rate showing a country's increase of wealth; *oil and gas income* controls for natural resource endowment; *economic crisis* is a dummy variable for years in which the GDP growth rate decreased below –5 percent; and finally, *war* is a dummy variable for interstate or civil wars. These control variables a routinely used in studies on post-communist reform (Fish 1998, Bodenstein/Schneider 2006, Treisman 2014).

The summary statistics and sources of the data are listed in Appendix 1. The empirical estimation models are OLS regression with robust standard errors for models 1-10. Models 11-26 are panel data, which is estimated using panel corrected standard errors with a panel-specific AR1 autocorrelation structure (Wooldrige 2009). Table 1 shows the regression results.

▸ *Table 1: The role of critical junctures and initial conditions*

	Dependent variable							
	EBRD score		Liberalisation reforms		Privatisation reforms		Institutional reform	
	1	2	3	4	5	6	7	8
Initial elections	.080*** (.013)		.069** (.021)		.093*** (.015)		.075*** (.012)	
Years under communism		-.010** (.003)		- .009* (.004)		-.011* (.004)		-.016*** (.002)
Longitude	-.001 (.001)	.001 (.001)	.000 (.001)	.002 (.002)	-.000 (.001)	.001 (.002)	-.002* (.001)	.000 (.001)
Latitude	.004 (.004)	.012** (.004)	-.003 (.005)	.004 (.005)	.001 (.004)	.009 (.005)	.012** (.004)	.019*** (.003)
Constant	.265 (.197)	.682** (.199)	.801** (.246)	1.15*** (.223)	.358 (.208)	.793** (.250)	-.204 (.211)	.256 (.190)
N	26	26	26	26	26	26	26	26
R^2	.757	.665	.371	.285	.744	.556	.803	.814
F	16.5***	14.1***	4.2*	2.9	15.0***	9.7***	30.3***	37.8***

▸ *Note: OLS regression; robust standard errors in parentheses; *p<.05, **p<.01, ***p<.001.*

Table 1 shows the estimations for four different dependent variables. The key independent variables of interest are *Initial elections* and *Years under communist rule*. *Initial elections* has a positive coefficient sign showing that moving up in the categories of the variable improves the reform scores, while the negative sign of *Years under communist rule* shows that longer communist rule lowers the reform scores. Both variables are statistically significant. However, the significance level of *Years under communist rule* drops in models 4 and 6. The variables *Longitude* and *Latitude* are not robust, since they change signs and significance levels across the models. The lack of robustness of *Longitude* may be explained by higher correlation with *Initial elections* and *Years under communist rule*, but *Latitude* is only weakly correlated to *Years under communist rule*. If *Latitude* mattered it should at least be robust in models 2, 4, 6 and 8, which is not the case. The conclusion is that geographical location as such is not a convincing predictor of reform. The models which include *Initial elections* have a higher R^2 than those including *Years under communist rule* except of models 7 and 8 where R^2 is about the same level. Both variables struggle in explaining liberalisation reforms – R^2 is low in models 3 and 4 and in model 4 the F-test is insignificant. This confirms arguments that price liberalisation was the default option for all transition countries, independent of their political or economic specificities.

▸ *Table 2: Marginal effects of critical junctures and initial conditions*

	Initial elections		Years under communism	
	min	max	min	max
EBRD score	.417 (.298 .535)	.817 (.775 .859)	.831 (.760 .903)	.499 (.361 .638)
Liberalisation Reforms	.672 (.496 .848)	1.02 (.949 1.08)	1.02 (.936 1.11)	.747 (.579 .916)
Privatisation reforms	.380 (.251 .509)	.845 (.796 .895)	.841 (.747 .935)	.498 (.326 .670)
Institutional reforms	.280 (186 .373)	.655 (.597 .714)	.697 (.621 .774)	.327 (.233 .420)

▸ *Note: Predicted levels of dependent variables show for minimum and maximum values of the independent variables; 95% confidence intervals in brackets.*

Table 2 shows the marginal effects of models 1-8 for the minimum and maximum level of *Initial elections* and *Years under communist rule*. For instance, a change from the minimum to the maximum level of *Initial elections* increases the extent of reforms by .4 on a scale from 0 to 1. A change from maximum to minimum *Years under communist rule* increases the reform only by .33. *Initial elections*, thus, is a stronger predictor of reforms than Years under communism. However, both variables struggle to explain the extent of liberalisation reforms. The effects are still between 35 and 27, but the confidence intervals exceed 1. This is another sign that liberalisation reforms were the default option in the post-communist countries that is only little explained by other independent factors. *Initial elections*' effect is especially strong on privatisation reforms with .47 on the standardised reform scale. The impact of Years of communism on reforms is only about .34. Finally, both variables have about the same impact on institutional reforms, which are generally lower than other reform dimensions (see Figure 3).

▸ *Table 3: Critical junctures, initial conditions and speed of reform*

	Early reforms	
	9	10
Initial elections	– 2.836*** (.512)	
Years under communism		.360** (.091)
Longitude	.010 (.034)	– .050 (.052)
Latitude	– .123 (.129)	– .394* (.145)
Constant	23.261** (6.157)	8.784 (8.029)
N	26	26
R^2	.724	.613
F	19.3***	11.6***

▸ *Note: OLS regression; robust standard errors in brackets; *p<.05, **p<.01, ***p<.001.*

Table 3 shows the impact of initial conditions on the speed of reforms. The dependent variable is the number of years it took from 1990 to reach the median level of all reform scores (see Figure 2). The negative sign of *Initial elections* in model 9 tells that higher categories of the variable shorten the number of years to reach the reform median. Similarly, the more years a country spent under communist rule to more years it needed to reach the median reform score.

▸ *Table 4: Marginal effects of critical junctures and initial conditions on speed of reform*

	Early reforms	
Initial elections	17.9 (14.3 21.5)	3.7 (1.3 6.1)
Years under communism	3.3 (– .1 6.7)	14.9 (11.3 18.4)

▸ *Note: Predicted levels of dependent variables show for minimum and maximum values of the independent variables; 95% confidence intervals in brackets.*

According to table 4 *Initial elections* has a strong impact. A change from the minimum to the maximum value shortens the time to reach the median level of reform from 18 to 3.7 years. A corresponding change of Years of communist rule shortens the time span from 15 to 3.3 years, but the confidence interval falls below 0. The conclusion of this first analysis is that *Initial elections* is a better predictor of long-term reform success and speed than Years of communist rule. The next question is what aspect of institutional development triggered by *Initial elections* fostered reforms. From the discussion of critical junctures in section 3 development of democracy, institutional constraints, informal veto players, rule of law and civil society are consequences of critical junctures. But Table 5 shows first the effects of level of democracy on reforms, before analysing the effects of the components of democracy on reforms.

▸ *Table 5: Democracy and economic reforms*

	Dependent variable			
	EBRD score	Liberalisation reforms	Privatisation reforms	Institutional reforms
	11	12	13	14
Democracy $_{t-1}$	.012*** (.001)	.018*** (.002)	.012*** (.002)	.008*** (.001)
GDP pc (log) $_{t-1}$	.101*** (.012)	.029 (.017)	.091*** (.017)	.140*** (.011)
GDP growth (log) $_{t-1}$	.003 (.005)	.009 (.009)	.003 (.007)	.0005 (.003)
Oil and gas income (log) $_{t-1}$	– .012** (.004)	– .013** (.004)	– .014** (.005)	– .007 (.005)
Economic crisis $_{t-1}$	– .013 (.013)	.013 (.020)	– .022 (.015)	– .024 (.013)
War $_{t-1}$	– .046 (.062)	– .070 (.112)	– .012 (.067)	– .062 (.056)
Constant	– .376** (.114)	.451** (.161)	– .288* (.146)	– .875*** (.093)
N	503	500	500	500
Groups	26	26	26	26
Wald χ^2	400.8***	264.7***	222.4***	357.1***
P	.658	.592	.676	.690

▸ *Note: estimations with panel corrected standard errors panel-specific AR1 autocorrelation structure; standard errors in brackets;* $^{*}p<.05$, $^{**}p<.01$, $^{***}p<.001$.

The effect of *Democracy* is positive and statistically highly significant in models 11-14. This corroborates similar results provided by Treisman (2014). Regarding the control variables *GDP per capita* is positive and statistically significant, but not in case of liberalisation reforms (model 12). Wealthier post-communist countries thus advance more in privatisation and institutional reforms. The growth rate, by contrast, does not have a significant impact on the extent of reforms – *Growth* is statistically insignificant in all models. In a similar vein, *Economic crisis* also has no impact on reforms. This refutes claims by gradualists who argued that the depth of transitional crisis might stall reforms. Likewise, *War* is not statistically significant, although the coefficient of the variable is negative. Finally, countries with higher revenue shares from oil and gas made less progress in overall reforms and liberalisation and privatisation reforms (models 11-13). However, *Oil and gas revenues* has no statistically significant effect on institutional reforms. The following table shows how strong the effects of the significant variables on reforms are.

▸ *Table 6: Marginal effects of democracy and controls on economic reforms*

	Democracy		GDP per capita		Oil and gas income	
	Min	max	min	max	min	max
EBRD score	.374 (.330 .418)	.595 (.550 .640)	.332 (.263 .401)	.681 (.638 .725)	.555 (.514 .596)	.454 (.393 .515)
Liberalisation Reforms	.547 (.493 .600)	.880 (.831 .930)			.807 (.774 .840)	.697 (.624 .771)
Privatisation reforms	.370 (.310 .430)	.590 (.538 .641)	.344 (.263 .425)	.665 (.606 .725)	.556 (.504 .607)	.442 (.373 .511)
Institutional Reforms	.243 (.196 .290)	.405 (.367 .442)	.083 (.033 .132)	.576 (.524 .628)		

▸ *Note: Predicted levels of dependent variables show for minimum and maximum values of the independent variables; 95% confidence intervals in brackets.*

A country's level of wealth (*GDP per capita*) has the strongest impact on overall reforms, followed by the level of democracy. The impact of *Oil and gas revenues* on overall reform is rather week with overlapping confidence intervals in overall reforms, liberalisation reforms and privatisation reforms. Liberal reforms are best explained by *Democracy*, while *GDP per capita* is not statistically significant. The effect of *Democracy* on institutional reforms, however, is modest with an improvement of .16. By contrast, the impact of *GDP per capita* on institutional reforms is very strong with an effect of about .5. Thus, institutional reforms are best explained by a country's level of wealth, while the other reform dimensions more closely follow democratic developments. The following table breaks down the concept of democracy into three subcategories and looks through which cannels democracy has affected reforms.

▸ *Table 7: Subcategories of democracy and economic reforms*

	Dependent variable		
	EBRD score	EBRD score	EBRD score
	15	16	17
Executive const. $_{t-1}$	.043***		
	(.008)		
Civil liberties $_{t-1}$		.050***	
		(.008)	
Fractionalisation $_{t-1}$			.152***
			(.033)
GDP pc (log) $_{t-1}$	.088***	.087***	.143***
	(.018)	(.019)	(.013)
GDP growth (log) $_{t-1}$	.003	.012	.046
	(.008)	(.007)	(.026)
Oil and gas	-.005	-.013*	-.022***
	(.007)	(.006)	(.004)
income (log) $_{t-1}$			
Economic crisis $_{t-1}$	-.018	-.031	.010
	(.021)	(.022)	(.024)
War $_{t-1}$	-.065	-.020	
	(.078)	(.061)	
Constant	-.447**	-.048	-.908***
	(.146)	(.195)	(.148)
N	498	479	423
Groups	26	26	26
Wald χ^2	295.3***	151.6***	270.4***
P	.651	.715	.761

▸ *Note: estimations with panel corrected standard errors panel-specific AR1 autocorrelation structure; standard errors in brackets; *p<.05, **p<.01, ***p<.001*

In Table 7 *Executive constraints*, *Civil liberties* and *Fractionalisation* have positive and statistically highly significant effects on reforms. On first sight it is not straightforward to distinguish the role each variable has played for reforms. But before moving to the analysis of marginal effects Table 8 shows the estimations for the subcategories of economic reforms.

Table 8: Subcategories of democracy and subcategories of reforms

	Dependent variable					
	Liberalisation reforms			Privatisation reforms		
	18	19	20	21	22	23
Executive const. $_{t-1}$	.061** (.012)			.040*** (.009)		
Civil liberties $_{t-1}$		.070*** (.012)			.052*** (.009)	
Frac. $_{t-1}$			.202*** (.047)			.175*** (.037)
GDP pc (log) $_{t-1}$	.011 (.023)	.003 (.027)	.080*** (.020)	.084*** (.022)	.080*** (.021)	.133*** (.016)
GDP growth (log) $_{t-1}$	.006 (.011)	.015 (.009)	.032 (.035)	.002 (.010)	.015 (.009)	.079** (.029)
Oil/gas inc. (log) $_{t-1}$	– .005 (.009)	– .013 (.007)	– .03*** (.006)	– .009 (.008)	– .015* (.006)	– .02*** (.004)
Economic crisis $_{t-1}$	.011 (.029)	.004 (.031)	– .075 (.217)	– .026 (.024)	– .049* (.025)	.011 (.026)
War $_{t-1}$	– .100 (.115)	– .052 (.082)		– .032 (.086)	.025 (.073)	
Constant	.359 (.184)	.985*** (.272)	– .075 (.217)	– .394* (.185)	.013 (.216)	– .96*** (.171)
N	498	479	432	498	479	423
Groups	26	26	26	26	26	26
Wald χ^2	151.1***	74.8***	73.9***	185.8***	131.0***	197.5***
ρ	.622	.674	.718	.669	.701	.769

	Dependent variable		
	Institutional reforms		
	24	25	26
Executive const. $_{t-1}$	.035*** (.007)		
Civil liberties $_{t-1}$		.039*** (.007)	
Frac. $_{t-1}$			.088** (.027)
GDP pc (log) $_{t-1}$	.129*** (.016)	.134*** (.015)	.181*** (.014)
GDP growth (log) $_{t-1}$	.000 (.006)	.008 (.004)	.020 (.024)
Oil/gas inc. (log) $_{t-1}$	– .001 (.006)	– .008 (.006)	– .013** (.004)
Economic crisis $_{t-1}$	– .029 (.018)	– .045* (.019)	– .014 (.020)
War $_{t-1}$	– .075 (.061)	– .036 (.058)	
Constant	– .94*** (.117	– .66*** (.143)	– 1.3*** (.145)
N	498	479	423
Groups	26	26	26
Wald χ^2	225.0***	265.2***	225.8***
ρ	.676	.706	.821

▸ *Note: estimations with panel corrected standard errors panel-specific AR1 autocorrelation structure; standard errors in brackets; the variable War t-1 is omitted in models 20, 23 and 26; *p<.05, ** p<.01, ***p<.001.*

All three sub-dimension of *Democracy* are highly statistically significant in model 18-26, but the significance level of *Executive constraints* drops in model 18 and that of *Fractionalisation* drops in model 26. The control variables have similar signs and significant levels as in models 11-15 (Table 5). The following table shows the marginal effects.

▸ *Table 9: Marginal effects of subcategories of democracy*

	Executive constraints		Civil liberties		Fractionalisation	
	min	max	min	max	min	max
EBRD Score	.308 (.205 .412)	.610 (.546 .674)	.371 (.307 .436)	.670 (.602 .739)	.470 (.414 .526)	.621 (.575 .667)
Liberalisation reforms	.468 (.333 .603)	.892 (.826 .958)	.550 (.453 .647)	.969 (.892 1.05)	.683 (.607 .758)	.884 (.833 .934)
Privatisation reforms	.321 (.202 .440)	.601 (.524 .678)	.366 (.294 .438)	.679 (.604 .753)	.456 (.393 .520)	.631 (.577 .684)
Institutional reforms	.179 (.093 .266)	.423 (.366 .481)	.236 (.189 .283)	.473 (.411 .535)	.336 (.286 .387)	.424 (.379 .469)

▸ *Note: Predicted levels of dependent variables show for minimum and maximum values of the independent variables; 95% confidence intervals in brackets.*

Of the three sub-categories of democracy *Fractionalisation* has the weakest effect and shows overlapping confidence intervals in the estimations for institutional reforms. Thus, the number of informal veto players that *Fractionalisation* is supposed to measure had a statistically significant, but only a weaker role on reforms. *Executive constraints* and *Civil liberties* have about the same effect on overall reforms. However, the effect of Executive constraints is stronger when it comes to liberalisation and institutional reforms, whereas the variable *Civil liberties* has a stronger impact on privatisation reforms.

5. Discussion and conclusion

Initial elections shaped the institutional structures of the emerging democracies in a way that enabled economic reforms.

The contribution's aim is to show the long-term effect of critical junctures on economic reforms in the transition countries. Economic transformation is a complex process contingent on large number of factors. Explaining each transition country's reform trajectory in detail is beyond the scope of this contribution. But as a key result it argues that critical junctures in the form of initial elections had a decisive impact on the long-term reform trajectories in the post-communist countries. Initial elections shaped the institutional structures of the emerging democracies in a way that enabled economic reforms. More precisely, the strictness of institutional constraints that emerged as a consequence of initial elections turned out to be conducive for early liberalisation reforms in the first place. Institutional constraints also had a decisive effect on the extent of institutional reform, which have advanced less than liberalisation reforms.

The extent of civil liberties had the strongest effect on privatisation reforms. The variable *Civil liberties* comprises rule of law, but also freedom of media and associations. Thus, strong civil society combined with rule of law was an important factor to reduce the influence of early winners of reform who often had vested interests in stalled reforms to retain their rent-seeking privileges. Hellmann (1998) advocates democratic elections and government turnover to break rent-seeking networks, but it seems to be the effect of civil society and rule of law that had the strongest long-term effect on privatisation. This is supported by Treisman's (2014) observation that public opinion in democratic transition countries has always been strongly in support of reforms, even in the years of deepest economic crisis. However, Denisova et al. (2012) using survey evidence for 28 transitions countries in 2006 found widespread criticism of privatisation among respondents. But the results do not necessarily contradict positive public opinion towards reforms found in earlier studies. A large majority of respondents is still in favour of privatisation, but is dissatisfied with the way privatisations had been done – a highly critical, but still positive assessment of privatisation. It is reasonable to assume that public opinion is meaningful only when a country's media a free. We do not know public opinion on reforms in non-democratic transition countries at the beginning of the reform process, but state-controlled media may have channelled public opinion into a more reform-sceptical attitude. *Civil liberties* controls for the media effect, as it entails media freedom.

A large majority of respondents is still in favour of privatisation.

Party fractionalisation, by contrast, had the weakest effect on reforms. The variable conceptualises the role of informal veto players and politics in a more general way. The fact that more informal veto players also let to more reforms shows that fears about reform deadlocks caused by the democratic process were premature (i.e. Offe 1996). However, the effect is weaker than the effects of institutional constraints or of civil liberties. This corresponds to results by Treisman (2014). He finds only inconclusive effects of more fine-grained politics variables. For instance, leader change, competitiveness of elections, the proportion of votes for the winner in the first round of presidential elections or the proportion of seats held by communist successor parties do not affect reforms. However, when countries where governed by communist leaders or leaders that belonged to communist parties throughout the transition period they also had lower reform success. This does not contract the initial elections argument, because these countries had flawed initial elections and did not democratise later on. Consequently, politics was less influential on long-term reforms than institutions.

An important question is whether critical junctures or historical legacies led to specific institutional structures. The evidence of a lasting historical impact on reforms is strong, as the results of Table 1 show. Treisman (2014) argues that Islamic cultural traditions combined with the duration of communist rule undermined the free-market orientation of countries. But it is not easy to set apart these effects from potential confounders. Table 2 shows that initial elections have a stronger effect on reforms than years of communist rule and therefore seem to be a better explanatory variable. It could be argued that the result of initial elections were determined by a country's duration of its communist rule, but the Spearman rank correlation between duration communist rule and initial elections is much weaker than this argument would suggest.[3] The outcomes of initial elections for many transition countries are not just a function of their communist past. Initial elections were rather a filter through which historical legacies where channelled into new trajectories.

Critical junctures also affected the speed of reforms. Countries with free initial elections were the first to reach the median level of total reforms. Early reforming countries were also the most successful reformers at the end of the transition period. Treisman (2014) suggests that early reforms enable long-term reform success. If this is true then the argument put forward by gradualists that 'shock reform' could undermine legitimacy

[3] The Spearman rank correlation between Years of communist rule and Initial elecions is –.65 for 26 countries.

of subsequent reforms can be refuted. The number of years it took a transition country to reach the median of all countries' reforms is strongly correlated with the level of total reform in 2010, as well as privatisation and institutional reform. However, the correlation with liberalisation reform is weaker.[4] Speed of reform mattered, but speed of reform was also determined by initial elections (Table 3).

Critical junctures mattered in the economic reform process. The outcomes of the short period of system transformation around 1990 had a lasting impact on the amount of economic reforms more than two decades later. Are critical junctures deterministic? They are certainly not. Critical junctures set the new rules of the game, but within the rules agents are free to act. Agency matters. Even the new rules that emerged after critical junctures will not last forever and can be altered by agents. Contemporary Hungary is a case in point. Throughout the transformation process it was one of the most democratic transition countries with strong executive constraints and civil liberties, as the outcome of its initial elections would have predicted. Yet government under Prime Minister Viktor Orbán starting in 2010 used its two-thirds majority in parliament to revoke institutional checks and balances, curb the free press and started harassing civil society organisation (Kornai 2015). This was not without effect on economic reforms. The Hungarian government also started to reverse key achievements of the economic reforms by first nationalising mandatory private pension funds, followed by nationalisation of key 'strategic' assets of the economy such as utility providers, building artificial monopolies such as licensing national tobacco shops and introducing distortionary taxes aimed at foreign companies, to name a few measures (Bokros 2014). Reform reversal is always a possibility. The outcomes of critical junctures can be changed by agency.

Politics is also an important ingredient of the picture of reform.

But even if the constraints set by critical junctures are binding agents have large room of manoeuvre. This is also true for the economic reform process. For instance, the

[4] The correlations of Number of years with EBRD score is −.89, with Liberalisation reforms −.72, with Privatisation reform −.88 and with Institutional reform −.83. The negative sign indictes that the less number of years it took to reach the median reform score the higher the reform scores in 2010.

personality of leaders mattered. Treisman (2014) shows that within country-specific settings leaders made a difference. He found out that Russia's Yegor Gaidar added an additional .17 EBRD reform scores in 1992 than estimations would have predicted for Russia, Poland's Leszek Balcerowicz added additional .18 scores in 1990-91 and Bulgaria's Dimitar Popov added .06 additional scores in 1991. These were to leading reformers that pushed the reform scores of their countries beyond what would have been predicted. Leonid Kravchuk, by contrast, reduced Ukraine's predicted scores by .08 in 1991-93.

Could successful economic reforms have spurred democratic reforms? The short answer is positive.

Politics is also an important ingredient of the picture of reform. Bulgaria's reform process was characterised by intense vacillation between reform and reversal. Djankov (2014) argues that the former secret police took control of the banking sector and export business at the beginning of the transformation and later on allied with organised crime. The socialist party, thus, had a vested interest in reform reversal, mainly in the area of privatisation, but also with regards to institutional reforms that enhanced transparency. Ukraine's path to reforms was no less tormented. Ukraine's first President Leonid Kravchuk stroke a deal with the independence movement Rukh to focus on state-building rather than on far-reaching economic reforms. These early years gave rise to oligarchs that later in the process turned out to be impossible to be removed and who had a vested interest in protracted reforms. Even the Orange revolution saw only a short-lived defeat of oligarchs, as they bounced back quickly. Interestingly, it was under Viktor Yanukovich's presidency that Ukraine moved forward again on the reform agenda (Havrylyshyn 2014). Another example is Russia. Despite of the early success of the Gaidar reforms the political conflict between President Boris Yeltsin and the Russian Congress negatively affected reforms, because Yeltsin could only rule by Presidential decree (Åslund 2014). These examples do not contradict the logic of critical junctures, as all three countries had a problematic start in terms of outcomes of initial elections. But they highlight the fact that politics shaped the trajectories of reforms, the analysis of which is beyond the scope of this contribution.

Could successful economic reforms have spurred democratic reforms? The question has not been followed in this contribution, but the short answer is positive. Fish and Choudhry (2007) show in their estimations that the causal arrow also runs from economic reforms to democracy. But in the case of the post-communist transition countries the starting point of the complex process of dual reforms was a narrow window of opportunity that decided how the institutional framework of politics and policy making would look like. If there is one overarching lesson to be learned of more than two decades of dual reform than it is that windows of opportunities must be used wisely.

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▸ *Appendix: Summary statistics*

Variable	Obs	Mean	Std. dev.	Min	Max	Source
EBRD score	572	.49	.26	0	0.9	EBRD
Liberalisation reforms	572	.72	.32	0	0.99	EBRD
Privatisation reforms	572	.49	.28	0	0.9	EBRD
Institutional reforms	572	.33	.24	0	0.8	EBRD
Polity 2	566	3.66	6.46	– 9	10	Polity IV
Executive constraints	534	5.2	2.1	1	7	Polity IV
Civil liberties	514	3.5	1.7	1	7	Freedom House
Fractionalisation	457	.62	.26	0	1	Armingeon et al. (2011)
GDP per capita	563	7924	5542	849	27197	World Bank
Growth rate	537	1.5	8.9	– 45.3	33.0	World Bank
Oil and gas income	523	120	381	0	3523	Ross (2011)
Economic crisis (dummy)	537	.1	.2	0	1	World Bank
War (dummy)	572	0	.04	0	1	Correlates of War Intrastate and Interstate Wars dataset

Emerging Market for Ownership Rights and The Rule of Law

▸ Dušan Tříska

INTRODUCTION

Leaving aside the essential importance of the fundamental change in the political system, the economic aspects of the institutional transformation under study generally rests in the following four pillars:

1) macroeconomic stability,

2) price liberalization,

3) privatization,

4) social safety net.

Focusing on item 3), two major topics should be differentiated:

- primary "top-down" transfer of the already existing state-owned means of production to non-state agents (privatization in the narrow sense) and
- secondary restructuring of thus created (newly established) property rights – mergers, acquisitions and from scratch business operations[1].

It is the latter topic that this paper will deal with – abstracting then from all other above mentioned – highly inter-related - aspects of the overall transformation process.

[1] Cf., e.g., Claessens, Djankov, S. (1999), Djankov S., P. Murrell (2002), Coffee (1995).

2. TRANSFERS OF THE STATE-OWNED PROPERTY

2.1 Markets for capital goods

Hence we shall differentiate between W-privatization and E-privatization, according to whether these two seemingly similar processes occur in the context of a market ('western') economy or constitute a fundamental part of a post-communist transformation, respectively.

The transfer under study ("top-down" privatization in the narrow sense) is ina post-communist country (in contrast to that in a market economy), a process of (re)creating a capital good as a fundamental economic category. By ascribing an owner every piece of land and office building, they become tradable by definition and the capital market may emerge. In order to allow for this change, the first (initial) owner has to be created (looked-for and found).

Contrary to the western experience, privatization in a post-communist world is not a process within which property changes hands. Rather, it is the process within which the state becomes an issuer of newly marketable capital goods. Thus the initial owners from a test-tube have been born/created.

Hence we shall differentiate between W-privatization and E-privatization, according to whether these two seemingly similar processes occur in the context of a market ('western') economy or constitute a fundamental part of a post-communist transformation, respectively.[2]

The reason is that privatization is a notion well established both in the West and Central and Eastern Europe. This fact has made many politicians, analysts and advisors believed that the know-how of the former may be transferable to where it seemed to be needed most - to the post-communist countries.

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[2] Klaus (1993).

As a result, quite a number of various myths and misconceptions have been generated from a misunderstanding of the substantial differences between W- and E-privatization. Economically speaking, the objective of E-privatization, as said, amounts to establishing what we may refer to as capital goods markets. Only through these can the optimal allocation of capital resources be obtained and a genuine restructuring of the economy be launched.

In somewhat more general terms it should be stressed that the damage caused by the communist regime to the countries in the Central and Eastern Europe rested primarily in the overwhelming destruction of institutions. Among them a prominent position should be ascribe to a guaranteed system of property rights, namely those towards the means of production. The seemingly natural character of the ownership rights, their routine and everyday presence in developed countries, could make many independent observers forget that the constitution and enforcement of the rights has taken centuries of evolutionary developments.

It is thus one of the main messages of this paper that in the Central and Eastern Europe a new society was to emerge - not only particular business units. Economically speaking: however disabled this or that individual enterprise may appear, it is not the enterprise itself, but the overall economy, which requirs therapy.

The highly unique nature of the task called for unique or non-standard methods of its solution. Not only were our state-owned enterprises privatized without prior restructuring - as going concerns. Moreover, a great portion of the overall state-owned property was transferred for free. Various statistics can be found in data bases and literature. Our own rough estimates 1990 – 1998 of the overall amount of the property, classified according to the major methods of privatization (in billions CZK) are the following[3]:

[3] Zemplinerová et al., 1997, pp. 55-67 write - with the reference to the CSU, 1998, p. 542-543 - that the property released officially from "public ownership" for privatization during 1990-1998 was estimated at US$ 37 billion (at non-market book values), what represented 62% of all Czech productive assets. It comprised nearly all assets in agriculture, industries, construction and trade, and an important part of the assets in banking, healthcare and transport. Out of the total, 5% went to auctions and public tenders, 7% for restitutions, 7% for free transfers to municipalities, 9% for non-competing sales to pre-selected owners, 20% remained under the governance of National Property Fund and 52% were released for privatization by means of equity shares. The latter included voucher give-away privatization (34% of the total), stocks for sale (9%) and other privatization programs (9%).

1) small-scale privatization (20)

2) large-scale, *British-style* privatization (400),

3) voucher privatization (300),

4) transformation of agricultural cooperatives (200),

5) restitution (100)

6) free transfer to municipalities (300).

From these methods, only 1) and 2) were "commercial transfers for cash" and within the other four the voucher concept attracted much interest and criticism. If we deal with it further in more detail then mainly because it best illustrates what we proudly claim to be the Czech way of not only privatization but the country's transformation at large.

2.2 The voucher option

2.2.1 Voucher privatization

It may be of value to recall what we presented in 1990 to our Parliaments and general public as the major arguments supporting the scheme[4]:

1) Every citizen should be given a chance to participate.

2) So-called spontaneous (wild) privatization should be protected against the so-called management buy-outs.

3) The restitution puzzle was greatly resolve by the scheme 97 + 3, e.g. 97 % of the privatization shares for vouchers the rest to the Restitution fund from which the restitution claims were to be compensated.

4) By establishing their own investment privatization funds ("IPFs") the Czech banks were indirectly supported financially – with a strong incentive to bring the privatized shares to the market and continue a standard ways of collective investment.

[4] One of the first treaties on the topic can be found in Tříska (1991).

5) New guardians over abandoned privatized, now privatized property were to be established by investment funds and individual share-holders; if a damage should be caused by the so-called asset stripping (tunneling) it should be caused to the living agents not the anonymous state.

6) General public should get its first lessons about capitalist institutions, collective investment, share-holding companies, etc., even if it were by their "bad experience"; "next time it can be your life-time savings", we ten warned on TV.

7) Every state-owned enterprise should get a clear message that the government has a credible and technologically feasible method how to privatize whatever and whoever may attempt for resistance.

8) As the disintegration of Czechoslovakia was "in the air" the expected division of property between the two states should be eased in this way.

Contrariwise, we never let anybody feel that what is being distributed was of a monetary value. As we will argue repeatedly in this paper, we stressed over and over that no one can pretend to know the genuine (market) value of the state-owned property and that the shares of the privatized enterprise represent their nominal, administratively set book-values. This message was understood very well by the general public as the data showed in already first round of the first wave.

2.2.2 The scheme

Given its key role in the Czech transformation process and the many references to it throughout the paper some more details of the scheme may well serve the purpose.[5]

The scheme was realized in two privatization waves. To illustrate the concept, the first one will be briefly characterized:

[5] From among independent descriptions see, e.g., Shafik (1993, 1994), Katz, Owens (1995, 1996), Stiglitz (1999).

1) Almost fifteen hundred of state-owned enterprises (SOEs)[6] were selected and and formally transformed into joint stock companies (JSCs). The respective number of shares were issued on the basis on the book-value of the company – an entirely unreliable value at that time.

2) Investment vouchers were offered to every adult citizen for a registration fee of CZK 1,000 (some 30 USD or an average weekly salary at that time).

3) The value of vouchers was denominated in investment points; each voucher-holder was entitled to use 1,000 investment points during each of the two privatization waves. No exchange rate between an investment point and the regular currency was suggested officially.

4) Shares of JSCs were repeatedly offered for investment points in consecutive privatization rounds, until the shares were all allocated and investment points spent.

5) In the so-called Round Zero, i.e., before the actual bidding started, voucher-holders could choose to entrust their investment points to one or several Investment Privatization Funds ("IPFs") that would then act on its own, while the voucher holders were to become share-holders of the IPFs. Generally whoever could establish his/her IPF.[7]

It was thus described credible "threat" of privatization often exercised disciplinary pressure upon the then management of state-owned enterprises. Hence it was the very existence of the "voucher plan" that became the main vehicle how to spread the information - in an extremely bold and credible manner - that:

- if there is a trust-worthy standard privatization project, it is highly welcome but has to be presented right now,
- there is no room for endless discussions about what and how should be valuated, restructured, de-monopolized, etc.,

[6] In 1990, the Czechoslovak industrial sector consisted in some four thousand SOEs and only them.

[7] Simoneti, Tříska (1994), Egerer (1995), Coffee (1995).

- should only a part of the enterprise be privatized, the fate of the non-privatized remainder must be explained,
- with only few exceptions every enterprise will be privatized and the nearest voucher privatization wave is how it can be easily done.

2.2.3 The speed

The following time table is to pin point that – regardless of the kind of the institutional change - the speed is what has matters:

<u>November 1989</u>
the *Velvet revolution* (the collapse of communism)

<u>January 1990</u>
the complete re-design of the state budget

<u>July 1990</u>
elimination of a negative turnover tax

<u>October 1990</u>
the strategy of the economic transformation is approved by the Parliaments
(Slovak, Czech and Federal)

<u>September 1990</u>
small-scale privatization and restitutions adopted

<u>February 1991</u>
an extremely simplistic institutional frame is established for price liberalization, foreign trade liberalization, privatization and social safety net (prices increased by 25.8 % in the first month, 7 % in the second, 4.5 % in the third, and then between 1-2 % in the next 60 months – when we exclude the month of the tax reform)

<u>February 1992</u>
large-scale privatization and restitutions adopted

May 18, 1992
the first privatization round (of the First Privatization Wave for almost 1 500 state-owned enterprise – "SOEs") started; within six months one third or so of the economy ended up in the hands of those of the citizens who showed interest.

January, 1993
Czechoslovakia disintegrated into CR and Slovakia

2.3 Technical comment

The techniques elaborated throughout in the West were labeled in the CR 'standard' – in the sense that :

· an enterprise entering privatization is restructured (the so-called *privatized property* is established),

· the *privatized property* is valued and then offered for sale to more or less constrained group of purchasers.

Both restructuring and valuation of enterprises are well known for being extremely time consuming and costly. Put otherwise, the Wprivatization strategy strongly depends on the following preconditions:

· the government is to privatize maybe tens but certainly not thousands of enterprises,

· the domestic supply of financial services is sufficient to cope with the restructuring tasks,

the government, its personnel and agencies are stable, well organized and qualified.

To assume all this is, of course, a far cry from what could be observed in the CR in the early 1990s (or even today) and, we expect, the same applies to the other transforming countries.

3. RESTRUCTURING OF THE INITIAL OWNERSHIP[8]

As said the paper focuses on – *de-facto* – post-privatization problems of "secondary trading" with capital goods or means of production – mergers, acquisitions and from scratch business operations.

3.1 Prerequisites of privatization

3.1.1 Debates with Pejovich

The key question is what, if any prerequisites of privatization are needed for the post-privatization process concerned. Our plain answer is "none" – contrary to the common wisdom.

A nice opportunity how to dwell on the topic may be to refer to our polemic with Svetozar Pejovich namely because he is one of the founders of the New Institutional Economics and namely Property Rights School[9].

To begin with, Pejovich, needed to stress that (p. 215 of the op. cit.):

"[...] Russian president Vladimir Putin inadvertently provided the best evidence that the rule of law, the credibility of private-property rights, and the enforcement of contracts in the region should have come before the privatization of state-owned firms was initiated."

Similarly on p. 222 he writes:

"[...] Credible private-property rights are the basic prerequisite for successful privatization. Government regulations distort the terms of exchange that individuals prefer. Hence, the incentive effects of the attenuation of private-property rights and of growing government regulation raise the transaction costs of moving privatized assets to their most valuable uses."

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[8] From early contributions of the author on this issue, see, e.g., Tříska (1994, 1996).

[9] See Pejovich (2005), Klaus; Tříska (2006). We extend here upon the presentation of the polemic to the workshop "Korea and East Asia: Transformation of Socialist Systems" in Tříska (2009).

Contrary to this, let us repeat, our concept is that:

a) the new institutional frame, including Pejovich's credible private-property rights is the objective (not a prerequisite) of the transformation process,

b) even if a) did not hold, the post-communist government does not have a choice how to sequence these or those transformation steps.

3.1.2 Legal frame and ex ante regulation

Statements like 'rule of law first!' bring irresistible temptations for all who would rather block the transformation.

The public good provided by an efficient enforcement of law is only too obvious and no serious discussant would ever attempt to think otherwise. At the same time it should not be difficult to understand that if a post-communist government were able to introduce directly, right from the start, *rule of law* which would reasonably well award whatever is *good* and punish every *evil*, one could easily ask why transform this magnificent system, what improvements may privatization produce.

Moreover, statements like 'rule of law first!' bring irresistible temptations for all who would rather block the transformation. They are those who understand immediately that the requirement can never be fulfilled during their lifetime, that there is no such thing as a legal frame apt for the process concerned. Still today (spring 2009, 25 years on) the institutional frame is certainly not in the position to deal with problems of the scope and scale that the transformation brings forward. Put differently, if ever today less *casualties* are observed, this can hardly be ascribed to a better developed regulatory frame and higher efficiency of law enforcement agencies. The improvements should rather be conceived of as a consolidation of the markets and a society as a whole – the above discussed final separation of wheat from shed.

Also in the CR the attacks upon privatization were disguised by the seemingly serious proposals for legislative developments, without which, as Pejovich also believes, the society will not absorb the incredibly rapid growth of the private entrepreneurship and thus prevent massive occurrences of – you name them - money laundering, inside trading etc.

Even if for nothing else, it is the *self interest* of the 'carriers of change' what makes them consider every way of how to improve the legal frame. They are well aware of the threat brought up upon them personally by the institutional inadequacy of the society in transition.

Put differently, a politician understands instinctually and thus almost instantly that they will have to defend themselves in the first place should there occur a genuine transformation *casualty* and that the defense, against the charges (criminal ones in particular), will be processed by agencies (police units in particular) who never before heard of a *collective investment*, *enterprise valuation*, *call/put options*, *short sales*, *debt equity swaps* etc.

External observers from international organizations often call for courage of the governments in transition countries. Only rarely they understand the true contents of what they ask for. What we stress here thus is that very often personal security of the 'carriers of change' may be at stake.

The owners emerging directly from privatization ('initial owners') need not (and most probably will not) be the final, not to mention 'optimal' rescuers of the ailing companies.

3.1.3 Ex post regulation

Still today, it is almost impossible to indicate (in a 'real time') which *casualty* is of a really *systemic* nature and thus legitimizes a corresponding institutional adaptation – amendments to legislation, new government agency formation, reorganization of the police etc. Put differently, already now it is not always easy to recognize whether a *casualty* is not only a failure of concrete people or companies, not to mention mere accidents that will most probably never repeat. Any mistaken interpretation is than immediately taken as a misbehavior of the Government and-or its respective official.

Very close to impossibility seem to be attempts to explain that:

- *casualties* may be reasonably dealt with only *ex post*, or – said more precisely – with the help of agencies established only on the basis of the damages observed in reality and their proper interpretation,
- often it is so that only the real-world *casualties* provide reliable arguments why and which new agencies are to be formed and properly staffed,
- the looked-for institutional frame, its contents and legal forms can only evolve – can never be installed, not to mention imported.

3.2 Initial owners

As one of the principles suggests, the objective of privatization should never consist in increasing efficiency of privatized companies, that it is the economy as a whole what requires improvement. Put alternatively:

a) many companies will not (and should not) survive their privatization and, at the same time, it is beyond anybody's capacity to indicate ex ante which of them these will be[10],

b) the owners emerging directly from privatization ('initial owners') need not (and most probably will not) be the final, not to mention 'optimal' rescuers of the ailing companies.

As to a) we may only repeat that it is not within the capacity of the government to make the appropriate 'ranking' of companies and that it has to be left to the new owners (initial or secondary) to differentiate 'wheat from shed'; organize investors for the 'good' enterprises and hopefully close the 'bad' ones.

[10] Apparently, the Schumpeterian concept of 'creative destruction' suggests itself here. Some estimates of that time suggested that up to 80% of the economy has no future, i.e., only 20% of the 4,000 or so enterprises will survive and the rest of the newly emerged economy will be of the green-field businesses.

As to b) governments should create an environment so that the 'secondary restructuring of the ownership' may proceed smoothly and efficiently.

The above policy of the Czech government materialized in its liberalism – for example the easiness with which securities exchanges could be established, as well as markets with real estate and labor.

In sum, amongst the post-privatization processes the major importance was attached to what we refer to as a secondary restructuring of ownership, its speed and efficiency. Consequently, massive transfers have been observed - of business units, blocks of shares, buildings, machinery, claims, obligations, inventories.

In voucher privatization, the initial structure of owners was to a great degree determined by the initial distribution of investment points among individuals and IPFs. As noted already, initially ten largest IPFs seemed to dominate the corporate control in the country.

The initial owner, if incapable of resolving the restructuring problem, must be motivated to sell fast. In some cases, of course, the (secondary) sale has been his/her obligation.

3.3 Foreign investors' involvement

In the CR the presence of foreign investors has always been considered beneficial and, therefore, most welcome. However, it has never been accepted that, in the reality of E-privatization, they will play a pivotal role.

W- and E-privatization also substantially differ with respect to the way they deal with foreign investors.

In the CR the presence of foreign investors has always been considered beneficial and, therefore, most welcome. However, it has never been accepted that, in the reality of E-privatization, they will play a pivotal role. It has become one of the fundamental theses of the Czech privatization program that foreign capital will ultimately enter the country in appropriate magnitudes only after privatization because the desired influx of foreign capital must ultimately rely on private initiative rather than on the capacity of government bureaucrats.

Following this philosophy, the Czech government resisted strong temptations to implement a *foreign investment law*, according to which a foreign capitalist should receive better treatment than (an investor) of domestic origin. Still worse, with respect to the foreign advice, the government 'dared' to remove the preferential taxation of foreign companies which had been granted by the communist parliament!

In E-privatization, foreign capital involvement can never play a crucial role.

The wisdom of this strategy is now tested, among other things, on securities exchanges which emerged as a direct outcome of privatization. By licensing these exchanges the government was keen to insure that there would be no constraints imposed upon foreign participants. Foreign buyers and sellers are offered to use the exchanges facilities on the same basis as domestic ones. They are thus in a position to take full advantage of the initial price level which is for the time being relatively low due to a large supply and only limited demand.

Summarizing, then, in E-privatization foreign capital involvement can never play a crucial role. Only after the post-communist economy is privatized, foreign investors will enter in substantial numbers and magnitudes. The role of foreign advisors and consultants, in this respect, must not be exaggerated.

3.4 Green-field entrepreneurs

If there is good news for post-communist countries, it is that the 'rule of communism' left behind enormous vacancies in the market. Many goods and especially services have been (and often still are) in 'short supply'. Not always these can be filled, in the short run, by imports. This situation makes it somewhat easier to open new business undertaking and make it profitable. As a rule, if you hit the vacancy, the profit margin is much higher than that in a stable Westernstyle (market) economy.

It is little understood that the objective of privatization should rests in opening space for all newly emerging entrepreneurial agents (domestic or foreign).

The post-privatization economy should be a battle field for a competition between two types of agents: the 'transformed old structures' (i.e. privatized companies) and the green-field undertakings (including such as McDonalds and Sony Music).

Given the topic of this paper, and recalling that IPFs have been mainly active in the realm of the 'old structures', it may be of interest to give some comparisons of the 'old' and 'new'.

4. LESSONS TO BE TAKEN?

The methods used in Central and Eastern Europe and the outcomes – for good or bad - may be of value to countries that now consider transformation (not only "reform") their owns system of institutions.[11]

Despite we hardly believe that there is an universal know-how that can be exported, the following few points may be worth mentioning[12]:

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[11] Tříska (2009).

[12] Klaus (2014).

The transformation of society - if genuine - amounts to the entirely new distribution of power and wealth. As such, it creates its fortunate winners and frustrated losers. The latter ones will be more willing to bear the unavoidable hardship of transformation should they have the clear notion that the 'windows of opportunity' have been fairly opened to the nation as a whole. A 'direct access' and 'free entry' to the new chances should thus be kept open to the public, i.e., protected against the merciless attempts by namely the first winners, mostly under the disguise of regulation, customer protection and alike.

Even if the previous did not hold, it goes by definition that the institutional change, if fundamental, necessarily brings up new agendas and-or their executors to the government. Its agencies may thus hardly have the competences to efficiently enforce regulation as known from already emerged economies. Hence, the emerging society cannot be other than much more liberal than the already developed systems – regardless of the ideological background of the politicians in charge. If so, this kind of liberalism only increases the already existing (unavoidable) level of spontaneity, i.e. the share of phenomena outside the government's highly limited powers – including criminal activities. It is then of no surprise that the respective governments easily become the first victims of their own transformation policy.

The transformation of society
creates its fortunate winners and frustrated losers.

It must not be forgotten that it is the society and economy as a whole, not individual institutions and enterprises that need transformation. And that the existing economy may be un-transformable *vis a vis* the entirely transformed political and economic environment. The *creative destruction* may amount to 60-70% of the existing institutions and business units. The objective of the transformation must thus rest in establishing conditions for the so-called green-field (from scratch) entrepreneurs – domestic or foreign. The former ones must be assisted by the state given the necessary lack of capital. As governments are short of financial resources themselves, the free distribution of production factors to their citizens suggests itself as an obvious solution.

Reform enthusiasm decays incredibly fast – contrary to the increasing, as already noted, strength and appetite of the first winners – the newly born lobbyists (interest groups). The speed of the transformation is thus of the highest importance. Among the counter-arguments the key role is played by the seemingly obvious and politically correct requirement to establish "rule of law" first. In other words, a "correct" legal frame and its enforcement is to be installed as a prerequisite of transformation. However, it is obvious to claim that in the CR, even now - 25 years on -, this, otherwise indisputable, condition cannot be taken as fulfilled.

Architects of change need a lot of courage. Trivial as it may sound the core of the statement is that the first government must forget its dreams about future respect for its work – both from future domestic politicians and international organizations including conceited noble universities.[13] Their courage and energy must be based on something entirely different – on the fact that there is nothing as rewarding as the participation in a process that is to bring your country from the state that has definitely over lived itself to the point from which new opportunities open to the nation as a whole.

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[13] At least since 1995 the economic literature has been enriched by sharp exchanges between the team of Václav Klaus (including the author) and, e.g., Joseph Stiglitz, the US prominent university professor, then the Chief Economist of the World Bank and, after all, the Winner of the Nobel Prize in Economics. See Stiglitz (1999). Still harsher, however, have been later attacks on the Russian way of "doing things". The initial concepts can be read from, e.g., Blanchard et al. (1993).

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Emerging Markets and Institutional Change 25 years after the fall of the Berlin Wall[1]

▸ Tomáš Munzi

A quarter of a century is relatively long period for evaluating the economic, political and social transformation in Central and Eastern Europe. The fall of the Berlin Wall was certainly the unique moment of enthusiasm, hope and expectations. A better and safer world was seen on the horizon. Therefore, it was also a golden opportunity for fundamental and radical changes of the whole post-communist world in the broadest possible sense. In hindsight, it was a challenging situation, as well as one of the most critical moments in the human history, as Central and Eastern Europe expected a very difficult and hardly imaginable transformation from a nuclear weapons armed enemy of Western civilization to a faithful partner. As we see today, fortunately, after a quarter-century, this complete transformation in the fundamental sense succeeded. Today's strained relations with Russia cannot be compared with the period of the Cold War. In retrospect, we can maybe only wittily regret that Lenin during his long stay in Geneva did not fall in love with this beautiful city enough to live here peacefully and forget his theoretical dream about the Bolshevik revolution in a country where the blue-collar proletariat had still not been developed enough to be allegedly exploited.

My contribution will proceed as follows: first, I will describe basic theoretical approaches to the institutional change in the emerging markets; second, I will apply this framework to the transformation in Central and Eastern Europe; third, I will evaluate this process from the institutional and law & economics perspectives; forth, I will analyze in more detail the case of the Czech Republic; and finally, I will conclude.

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[1] Presentation given at the conference "After the Fall of the Berlin Wall: 25 years of Market Economy in Central and Eastern Europe" ,November 7, 2014, Global Studies Institute - Université de Genève.

Theoretical approaches to the institutional change

From a broad perspective, there are two main approaches to the institutional change. Both approaches are necessarily based on understanding of institutions as such. First one treats institutions as rules in a hierarchical order which are more exogenously pre-determined outside the world of economic and societal life, such as legal rules and social norms. Organizations, legal contracts and other economic and social arrangements are then perceived as transaction-costs-saving responses within those constraints. This is the stance typical of the tradition of Nobel laureates – North[2] and Williamson[3]. Second one treats institutions more as endogenously shaped institutionalized rules within a dynamic and inter-temporal reality of our world. This second view is very typical for instance of Nobel laureate – Friedrich von Hayek[4]. Many academic papers tried to examine both attitudes and related issues. The question is which framework is more appropriate for understanding complex and dynamic phenomena within the societal reality, and whether these two approaches can be complementary to each other or even reconcilable. It is of course contentious in academia. Many works tried to incorporate to this analysis for example aspects of bounded rationality, or, they applied the methods of the game theory. In a game theoretical view, we can conceptualize institutions essentially more endogenously, but within the exogenous constraints to the individual agents. However, we still see the dichotomy between the rule-making game and the operational game. Therefore, there are still many obstacles that would allow more integrative and coherent view for understanding the dynamic interactions between individual agents. Very popular is also the so called "equilibrium view" of institutions that emphasizes a role of both formal and informal rules and institutions are identified with equilibrium patterns rather than the rules shaping behavior[5].

[2] Institutions, Institutional Change and Economic Performance, Cambridge University Press, 1990.

[3] The Economic Institutions of Capitalism: Firms, Markets, Relational Contracting, Free Press, 1985.

[4] Law, Legislation and Liberty, 1973.

[5] E.g. Aoki, Masahiko. Comparative Institutional Analysis: Theory, Corporations and East Asia, Edward Elgar Publishing, Nov 29, 2013.

A certain integrating approach naturally arises from the fact that both more evolutionary theories and theories treating institutional change as more centralized, collective-choice processes, have been developed to study different phenomena under certain circumstances and time horizons. In this regard, we cannot rank these theories but we have to put them into a proper context of the real-world processes of institutional change. For instance, we can mention the common law legal families that have emerged as formal rules based on the underlying evolutionary processes. Institutional change is also the path-dependent process of learning in the context of interactions between the formal and informal rules. It is very important to note this especially when we analyze the complex societal transformation, as in Central and Eastern Europe. However, this is true for virtually all emerging markets economies in our world with respect to the causes, process and outcomes of institutional change. This naturally requires a great dynamic complexity in understanding economic history, transition, development and transaction costs economics, as well as behavioral economics.

Transformation in Central and Eastern Europe

Even today's advanced capitalist economies had to undergo significant institutional change during the Industrial Revolution.

As the role of institutions in economic development has received more and more attention from policy makers and academicians, the linkages and causalities between the institutional set-up and development outcomes are perceived as fundamental. And, of course, it must especially apply to developing countries that lack a long period of stable institutional environment. Countries in Central and Eastern Europe experienced a very painful Communist past that irreversibly disrupted political, economic a social structures. Development outcomes are not influenced only by institutional dynamics, but also by local settings and socio-cultural aspects of the human actors. It means that we have to take into account the extent to which these individual natures of human behavior were also distorted by the totalitarian past. This applies especially to entrepreneurial skills and certain moral attitudes that were suppressed systematically by Communist regimes. Or, in more rigorous way, we should analyze how interactions between exogenous shocks and endogenous parameters changes influence societal development over time and place.

Above mentioned aspects play a key role in learning what are the real drivers of institutional change in emerging markets economies. It means that in developing countries, there are logically different sources of inertia that make institutions stable over time and place than in the developed Western countries. Therefore, theories of institutional change have to be applied accordingly. The role of informal institutions is then necessarily shifted, since it must to some extent substitute for underdeveloped formal institutions during the transition period. However, it can still fit into a broader conceptual framework for understanding the dynamics of institutional change. Even today's advanced capitalist economies had to undergo significant institutional change during the Industrial Revolution to respond to complex changes in political, economic and social structures. The question remains whether it is possible to speed up the development by some institutional imitation of time-tested formal rules of the most developed countries. In this regard, we usually talk about the potential effectiveness of so-called legal transplants that allow faster implementation of the rule of law according to the standards of advanced economies.

Transformation from the institutional and law & economics perspectives

Legal transplantation has had a long history since the time of the military expansion of the Roman Empire. Legal standards developed in a completely different civilizational environment were also imposed on indigenous populations during the colonization. The case of Japan that imported its original Commercial Code from Germany in 1898 is also very often mentioned[6]. The Soviet Union used Communist law as its imperial and oppressive tool. In East Asia developing countries were pushed to copy the institutional features of Western countries, especially the commercial law. It was mainly influenced by law and development scholars. Following reunification, extensive legal transplantation took place also between West and East Germany, including legal personnel that were delegated to

[6] Kanda, H., Milhaupt, C.J.: Re-Examinging Legal Transplants: The Director's Fiduciary Duty in Japanese Corporate Law, Columbia Law and Economics Working Paper No. 219, March 24, 2003.

implement the Western system. Today's pressures on the legal evolution to Western standards arise, in particular, from the international involvement of the developing countries in global value chains. Global transactions are then a very strong catalyst for development of the international commercial standards and dispute resolution centers.

We can hardly claim that the sudden copies of Western law would be a panacea for successful institutional change.

But in the case of legal development in the countries of Central and Eastern Europe after the fall of the Berlin Wall, we have to treat the possibility of legal transplants from the Western systems in a different mode. Legal families of Western and Eastern Europe are much closer in comparison to Asia. Soviet bloc disrupted the long-term development that was especially in Central Europe significantly linked to the institutional evolution in Western Europe and America. Therefore, we can hardly claim that the sudden copies of Western law would be a panacea for successful institutional change. Legal evolution is a much more complex process which is conditioned by many cultural, economic and social aspects of a particular time and place. Furthermore, objective linguistic and translation difficulties do not allow mere translation of laws and concepts that are often even in the Western legal tradition perceived very differently across countries. Legal transplant solution can be applied between countries in particular time, but also applied with substantial time delay across historical periods in the form of court action (e.g. as in case of "Mostecka uhelna mines" case which is treated by the Swiss justice some ten years after the Czech transition ended). Of course, the time delay does not help to make the legal transplant more suitable nor desirable approach. Implementation of legal reforms can never be an imitative process regardless of the circumstances of the complex economic and social development. For instance, if the insolvency law of the Western style were artificially implemented at the very beginning of the transformation and privatization, economy in the process of price liberalization and macroeconomic stabilization would immediately collapse. Socialist enterprises had past burdens from centrally planned management of production chains and prices, suffering from inefficient production structures. Also, there could hardly be any realistic valuation of companies, their assets and liabilities, when there was no functional price mechanism.

If we take into account all of the above, how can we actually evaluate development since the fall of the Berlin Wall to the present? If we look at the success of transformation in CEE after a quarter-century, it is clear that some countries have been more successful and some less. Entry into the European Union ten years ago was definitely an important moment for some countries within CEE. On the one hand, free trade within the EU accelerated economic and institutional development; on the other hand, European regulations and subsidies impose additional burdens and inefficiencies on the structure of the CEE emerging economies.

The main goal was to find new owners that would have started immediately with the restructuring of enterprises. It was the only way to increase competitiveness and encourage entrepreneurship.

The speed of transformation and privatization was absolutely crucial for successful institutional change toward the Western standards. The restoration of rule of law and property rights was not possible without fast and widely acceptable privatization that would distribute an important share in the national wealth equally among the population. Therefore, multiple methods of privatization were appropriate to use for risk diversification, because it was not a classic Western-style privatization after some period of socialist nationalization of certain sectors. It had to be a massive transfer of property rights to restore the link between ownership and management of companies. In this respect, the privatization process cannot be definitely assessed according to yield for state, but according to the efficiency and fairness in a large-scale transfer of state assets to all citizens. It was a total change of the system and large-scale privatization could therefore not be equivalent in terms of revenues for the state. The main goal was to find new owners that would have started immediately with the restructuring of enterprises. It was the only way to increase competitiveness and encourage entrepreneurship.

Transformation in the Czech Republic

Taking into account all of the above, in this regard, the Czech Republic is today one of the most successful countries in the CEE from the perspective of the institutional change and gradually converges to Western standards. There were used all the diverse methods of privatization - voucher privatization, restitution, small privatization and direct sales to foreign investors and Czech managers. Macroeconomic stabilization and liberalization of prices during the transition was successful and the Czech Republic did not experience a greater rate of inflation as in other countries. The banking sector is one of the most stable in Europe, which has been demonstrated even during the financial crisis. The Czech Republic has a very low poverty rate, low living costs, a massive middle class and high rate of home ownership that is the most effective tool of the social protection. Problems remain, however, especially in the case of the inefficient and bloated welfare state, which is a constant subject of the political populism, however, it does not match the maturity of the economy. PAYG system destroys inter-generational solidarity and discourages private savings over the life. Also, the education and transport infrastructures desperately need the entry of private capital.

Conclusion

To summarize and conclude, theories of institutional change are very helpful to structure the complex problem of social transformation of emerging markets economies towards Western standards. The linkages and causalities between the institutional set-up and development outcomes are perceived as fundamental, especially for developing countries that lack a long period of stable institutional environment and experienced a very painful Communist past that irreversibly disrupted political, economic a social structures. The main goal of the transformation in the process of institutional change must be a systemic correction of structural deficiencies in the political, economic and social trends and restore the rule of law. In this regard, rapid and large-scale privatization is absolutely necessary for the reestablishment of property rights, and, therefore, the real owners and entrepreneurs who could start with business restructuring to dramatically improve the quality of investment allocation, increase competitiveness and encourage entrepreneurship. Large-scale privatization process during the complex societal transformation is completely different from standard individual privatizations of state enterprises. Therefore, this massive restoration of property rights after the Communist past cannot be evaluated by the privatization revenues, but by economic efficiency and fairness in a large-scale transfer of state assets to all citizens. The possibility of accelerating development through an institutional imitation of time-tested formal rules of the most developed countries is very questionable for the emerging markets, especially in Central and Eastern Europe.

The Build-up of a Middle Class as Precondition for Future Prosperity

▸ Rudolf Hermann

In this presentation, I would like to make the point that Central/Eastern European (CEE) transition countries that have managed to build up a middle class in the process of their economic transformation will be better equipped to deal with future economic problems than countries that still have a sharp divide between a class of a few "haves" and a large mass of "have nots".

Let me start with two personal observations:

The first is from the Moldovan capital Chisinau, where you can see a lot of luxury cars and luxury shops on Stefan cel Mare Boulevard, the main town artery.

But right next to the boulevard, the Central market is just one block away. There, people do not arrive in luxury cars but in shabby minibuses, and you can see that they are struggling to make ends meet.

So in Chisinau, there is literally no "middle ground" between the few rich and the many poor.

The second observation is from Warsaw and the transformation of the Rondo Dmowskiego, one of the main crossroads in the central business district, over the last 25 years.

In the early 90ies, there was a luxury mile on one side, and a cheap market on the other, with an array of flimsy stalls also in the pedestrian passage under the streets – just as it is today in Chisinau.

But soon the subway passage started gradually to change, today we find there many nice and tidy shops and eateries, people take lattes and croissants on their way to work, and sushi or smoothies on their way back from work. This indicates that demand patterns and consumer culture have changed and a middle class has emerged.

The shape of subway passages in CEE cities can say a lot about the state and structure of their respective countries' economies and their success in the transition from central planning to a market economy.

Transition countries that have managed to build up a middle class in the process of their economic transformation will be better equipped to deal with future economic problems.

One might even speak of a "subway passage index". Comparing e.g. Kyiv and Warsaw – in the Ukrainian capital we see women standing in passageways selling flowers, whereas in Warsaw there are proper flower shops. In Kyiv we still see makeshift market stalls, in Warsaw nice and modern convenience stores.

Also the shape and function of markets themselves indicate economic shifts: The Central Market in Chisinau is for the low income buyers, but Farmers' markets in Prague, which have become very fashionable in recent times, are for the wealthy new middle class that is eco-conscious and ready to pay a premium price for premium home-grown produce.

Why is the existence, or non-existence of a middle class an important indirect economic indicator?

Because it points to differing patterns of economic transition in 90ies.

First pattern: In the economic sphere, there has been privatization of small and later large business entities, support for the concepts of private ownership and legal security, administrative and social reform,

On the political level we see open competition of political forces, orderly changes of government, a gradual buildup of civil society, drive for integration into western structures on political, economic and security levels, and readiness to undertake corresponding reforms.

Second pattern: Parts of the old communist elite strive to maintain as much as possible of their former influence, which leads to an "oligarchisation" of the economy and the emergence of insider business groups controlling essential parts of the economy. This process takes part in a still largely unstable legal and administrative environment. Once control is achieved by oligarchic groups then their incentive for reform is greatly reduced because the creation of an open society and economy would threaten the position of these leading groups, i.e. their own positions.

Once these oligarchic structures become entrenched over a number of years will be much harder to break them up. The consequence is social unrest, because the "common people" see no perspective of positive change. Recently we have seen protests in Bulgaria, Romania and Ukraine, expressing desperation with a status quo that apparently cannot be changed anymore.

In the CEE region, the pattern of development I mentioned first is represented by Poland, the Czech Republic, Hungary, Slovakia after 98, and the Baltics.

The second pattern is represented by Bulgaria, Romania, Ukraine and Moldova.

To switch from a negative to a positive development pattern is possible, albeit not easy. The best example in this field is Slovakia, which shed a semi-authoritarian regime in 1998 and turned to a vigorous and successful reform path.

Also Romania and Bulgaria have started moving in right direction, but time is not on their side. They lost most of 90ies and so they are at least 10 years behind.

Oligarchisation and a large city-country-divide are still serious problems there.

Ukraine and Moldova are in many respects even further behind and still at the beginning of the process.

Problems of countries with delayed development:

Who missed the transformation in the 90ies had to do it after 2000, and was busy transforming instead of harvesting the first transformation fruit when the European and global economy was humming. Later, the global crisis got in the way just at the moment when things had a chance to finally get better.

Transformation success was much easier to achieve for those who were ready to take advantage of the growth-environment of the first years of the new millennium, than in the crisis that set in after 2008. Or, as a Bulgarian sociologist put it to me recently: in 2009 it was difficult to explain to the Bulgarian people that the good times were gone already, because they hadn't experienced much of the benefit of the "good times" before.

A last point I would like to make is the correlation of the value of education to a society and the economic outlook education generates for individuals:

The notion that "education pays" was non-existent in socialism, as manual labour was officially held in higher regard than academic work, and that for ideological reasons.

An early transition to an education-focused society facilitated the groundwork for an emerging knowledge economy. A knowledge economy in turn facilitated faster economic growth. Again, this happened in countries like Poland and the Czech Republic much more than in Romania or Ukraine.

It is now crucial for CEE economies to retain their intellectual capacity and workforce at home and to prevent a brain drain, if their ambition is to change their profile from the low-wage "workshop-and-assembly"-economies they represented in the 90ies, to a more sophisticated knowledge economy they need to be in order to successfully compete on European and World markets with high-value products.

Does economic transition have an end?[1]

▸ Miroslav N. Jovanović
▸ Jelena Damnjanović

And Moses did look upon all the work, and, behold, they had done it as the Lord had commanded, even so had they done it: and Moses blessed them. Exodus 39:43

There were no theoretical foundations and experiences for the process of economic transition.

1. Introduction

Economic transition is a process of change from a centrally planned system to a market-based economy. The problem of economic coordination among actors is handled in its pure theoretical form in the market system by prices, rather than by the government's central plan as was the case in the centrally planned economies.

The fall of the Berlin Wall in 1989 is taken to be the start of the transition process even though there were earlier signs of changes in the socialist countries of Central and Eastern Europe. Western-type liberal democracy won over other social systems (Nazism, communism, feudalism, autocracy) and some announced 'the end of history' (Fukuyama, 1992). Regular free and fair multi-party elections are accepted as the norm. However, one forgot or neglected a tremendous direct influence of huge corporations and banks on the political process and lives of people. Resistance to such a corporate-led social system

[1] The views expressed are our own and do not necessarily reflect the position of the organisations for which we work. We are solely responsible for all errors and mistakes. Correspondence address: Miroslav Jovanović (corresponding author), Global Studies Institute, University of Geneva, 20 rue de l'Ecole de Médecine, 1205 Geneva, Switzerland, (e-mail) miroslav.jovanovic@unige.ch; Jelena Damnjanović, Novi Sad School of Business, Vladimira Perica Valtera 4, 21000 Novi Sad, Serbia (e-mail) jelenaschoolofbusiness@gmail.com.

continues to provoke various global and local types of resistance and protests. The end of history has not arrived. Social and political (r)evolution continues under different names and sometimes unsavoury ideas.

The transition process of transfer of state ownership to a predominantly private one and a market management of the economy is taken here in this order. After this introduction, (section 2) considers theoretical background for economic transition. Social environment is briefly tackled in section 3. Section 4 sheds light on various strands of economic transition from a planned to a market-based economy. A selection of economic effects on Central and East European countries is given in section 5. Concerns about the speed of transition are outlined in section 6. The final section 7 concludes discussion.

2. Economic theory

If put in rather simple terms, special features of the socialist economic system in Central and Eastern Europe was state ownership, central planning and the rule of the Communist Party which handled directly or indirectly almost all aspects of economic life. Average size of firms was huge; there were relatively few firms (it is easier to control them); firms were overstaffed; there were few new enterprises; financial, housing or land markets were absent;[2] there was no bankruptcy; innovation was generally weak;[3] while market-related institutions such as competition policy, accounting standards, protection of minority shareholders, property rights or banking regulations were absent or operating badly according to the market criteria.

The classical Marxist theory gave little guidance on how to run a socialist economy. This theory analysed (wild) capitalist system. Concentration and planning (as opposed to the 'anarchy of the market') were seen as the appropriate economic strategy for relatively poor economies. And so it was during the initial phases of development a century ago in the region. An early development of heavy industries and electrification, as bases for the

[2] Banks were checking the fulfilment of plan targets, they were not taking risks or inspecting business decisions. A soft budget constraint made firms worry little about possible losses as the government was always there to bail them out.

[3] Creativity existed. However, the system was not apt to absorb it fully. For instance, Otto Wichterle, a Czech chemist, invented at home soft contact lenses in 1961. This new gadget was not in the production plan in Czechoslovak firms. Therefore, he sold the licence to an American firm.

establishment and growth of other industries, contributed to relatively high growth rates. However, later on, planning converted from a means to achieve change to a tool that prevents transformations.

The principal theoretical working horse was the general neoclassical economic thought until the early 1990s. Development economics was a rather advanced theoretical field, but with little consensus.[4]

There was no theory of economic transition before the fall of the Berlin Wall. There were no theoretical advices on how to convert the middle income industrialised countries with educated population and underdeveloped services into market economies. Many of these countries were developed, but developed in the wrong way according to the market criteria. New institutions had to be built. They had to establish, apply, monitor and enforce market rules of the game for both private enterprises and the government. Since 1990, there was a huge amount of research in the field of economic transition, a lot of arguments, but little consensus. Economics of transition is still not a well understood novelty.

Assistance and advice was necessary in this transition 'works in progress'. This came from the developed market economies and international institutions such as the World Bank, the International Monetary Fund (IMF) and the European Bank for Reconstruction and Development (EBRD).

There was no theory of economic transition before the fall of the Berlin Wall.

Choices offered by the economic discipline to policymakers were rather limited. They were between liberal market fundamentalism as advocated by the Washington Consensus

[4] Development is in many cases a self- and home-grown matter. Britain, the US, China, India and others grew without much advice from the outside. Britain also, for instance, slumped later even though there were many policy advices. This should not be taken to mean that development assistance was a mistake or that it should be withdrawn. Assistance was provided on moral basis to help the poor. Whether taxpayers' money from the developed countries ended up where it was intended (or with the corrupt officials) is another matter. 'In sum, we don't know what actions achieve development' (Easterly, 2007, p. 331). Even after two long generations of research, economic development is still an intellectual enigma.

and the omnipresent bureaucratic planning. However, one may find huge complexity of the economic system between these two extremes. Evolutionary economics deals with issues such as path dependence, non-ergodic systems, government intervention, strategic behaviour or imperfect information. As a result, not 'one size fits all' (as urged by the Washington Consensus), but rather context specific policies are necessary. This is because in a highly complex and changing world what works in one place and one time, does not necessarily work in other places and another time. Blindly pushing 'one size fits all' policies may easily have harmful effects.

3. Social background

Most of the transition countries of Central and Eastern Europe did not have a truly 'market system' even before they became centrally planned socialist economies. Hence, even the kernel market institutions were largely absent and had to be built from scratch. These countries had deep roots in the Hapsburg, Prussian, Ottoman, Russian or Soviet Empires. However, relatively more educated citizens were more likely to embrace change, as well as democratic checks and balances.

Transition countries rich in resources such as energy (Azerbaijan, Kazakhstan, Russia and Turkmenistan) rely on taxes on resources. The government feels less pressure to be accountable to the citizens and taxpayers through democratic institutions. This creates grounds for corruption and authoritarian regimes. However, once the 'democratic threshold' is crossed, chances to slip back to autocrats diminish.

Another feature in the transition region is that there were some rather old countries such as Russia, Poland, Romania or Bulgaria and totally new countries such as the Former Yugoslav Republic of Macedonia and Bosnia and Herzegovina which had to run their states on their own for the first time.

4. Economic transition

Seed sources of pressure for change existed even during the centrally planned system. There were inabilities to fulfil promises about economic performance superior to the one in the 'capitalist countries'. Internal pressures asked for an improvement in the effectiveness in business, while strikes and protests were not reported in the media. Shortages, queues and the black market spread.

There were conflicting advices on how to translate centrally planned economies towards predominantly market ones. Two ideas were principal: convert aggressively fast (shock therapy) and do that gradually, to build first institutional framework.[5] The World Bank and the IMF offered and pushed their 'Washington Consensus' ideas.

The term, Washington Consensus was coined to express the extreme form of neo-liberal policy advice given (or imposed) by the Washington-based international financial institutions (principally the World Bank and the IMF) to unlucky Latin American countries from 1989 (and even before).

These policies include fiscal discipline; channelling of public expenditure priorities towards health care, primary education and infrastructure rather than investment in production (for this loans need to come from Washington and Wall Street); tax reform (to lower marginal rates and broaden the tax base); interest rate liberalisation; a competitive exchange rate; trade and FDI liberalisation (the more, the better); privatisation; deregulation of the economy (to reduce and eliminate barriers to entry and exit); corporate governance; and protection of property rights.

Neo-liberalism and globalisation were terms often used synonymously in debates on trade and development. In any case, this type of globalisation and Washington-style policy advice (*i*) never changed Latin American countries from being vulnerable exporters of commodities to exporters of higher-technology products and (*ii*) led them into crisis and misery because they were driven to follow advice that paid little attention to distribution and fairness. In addition, loans and their reprogramming were such that the debtor countries would 'never stop repaying them'.

[5] Institutions are relatively stable social arrangements in a given society that govern how people behave in a variety of circumstances (rules, norms, conventions). These can be formal, informal, government led and private. Institutions, customs, habits and attitudes in a society develop gradually and over a long time. Trust develops with time and experience (banks, insurance companies)(Hare 2013, p. 35). The World Bank and IMF did not pay an adequate attention to an 'institutional infrastructure' in Central and Eastern Europe.

> To this day, there is remarkably little good evidence that countries which adopted the Washington Consensus more have enjoyed better growth and poverty-reduction performance than those which adopted it less, at least if one excludes states which are barely able to do anything. Haiti over the past decade scores well by Washington Consensus criteria, Vietnam scores badly; but Vietnam has by far the better performance...
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> ...the prescriptions are couched as valid for countries at all stages of development. They ignore the "late development effect", the idea that countries which begin to industrialise when other countries are already highly developed have to use different policies and institutional arrangements to those used by earlier developers, in order to compensate for the disadvantages and capture the advantages of coming late - advantages such as the potential to use more advanced technologies already used elsewhere.[6]

The simple vision of the real world and a naïve policy advice is that a free-market economy is self-organising. Lipsey (2013, p. 37) criticised such a view with an observation that:

This led many students to draw the inference that the 'miracle of the market' could do the whole job without any human assistance. That such an inference was wrong was forcibly illustrated by the disastrous consequences of the marketisation of the former Soviet Union's economy in the absence of many of the needed institutions.

The Washington Consensus, a neo-classical policy-mix advice and its development-related ideology: privatise, liberalise and stabilise failed. Advice was given (imposed) on governments that were not prepared for such harsh ivory-tower cabinet-crafted old-textbook policies. The one-size-fits-all policy advice suggested and forced by the Washington Consensus was: increase welfare by removing (or reducing) every distortion. The General Theory of Second Best (Lipsey and Lancaster, 1956-57) demonstrated that this was not a valid conclusion. Sustained public investment in infrastructure, education, training (teachers should not be underpaid) and health are the proven development policy tools in the hands of a competent and non-corrupt government. Without those ingredients, no country maintained a fast growth. The task to sustain a high rate of growth is tough, but not impossible. Growth (an abstract accounting exercise?!) is not everything, but everything else depends on growth.

[6] K. Lee, J. Mathews and R. Wade, 'Rethinking development policy: A new consensus', Financial Times, 19 October 07.

Price signals in a liberal market economy carry on an enormous amount of information. However, price signals alone are inappropriate for the modern economy which is characterised by big global corporations (including banks) which manipulate markets on a large scale and create global financial alchemy:

Twelve global banks that have been publicly linked to the Libor rate-rigging scandal face as much as $22bn in combined regulatory penalties and damages to investors and counterparties, according to Morgan Stanley estimates.[7]

This asks for a careful and continuous government intervention in the creation and enforcement of rules.

The two biggest IMF debtors, Brazil and Argentina, decided in 2005 to repay their loans ahead of schedule. Hungary did the same in 2013. They wanted to get rid of loan conditions and policies that caused poverty and pain among the people. China and other East Asian countries did not follow the Washington Consensus advice to remove tariffs fast and to liberalise their capital accounts. These countries used industrial and trade policies against the advice from Washington. However, a new lease of life for the IMF came with the global credit crunch (2007-09) when the IMF was asked to step in with its funds and usual policies. None the less, Hungary decided to pay the IMF all its debt in advance and gladly closed its Budapest office in July 2013.[8]

The common outcome of the Washington Consensus policies in Central and Eastern Europe was a sharp fall in output and employment, as well as high inflation for

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[7] B. Masters and A. Barker, 'Banks face $22bn Libor bill', Financial Times, 13 July 2012.
A new set of heavy fines by regulators in Britain, United States and Switzerland hit global banks (UBS, Citigroup, JPMorgan Chase, HSBC, Royal Bank of Scotland and Bank of America) in 2014 for exchange rate rigging (D. Schafer, C. Binham and K. Scannell, 'Six banks hit with fines of $4.3bn over global forex rigging scandal; •First results from regulators' rates inquiry •Most expensive year for banks since 2007', Financial Times, 13 November 2014).

[8] Greece, a country in a deep economic 'black hole', decided to try to escape from IMF's claws:
'Samaras denies that Greece wants an acrimonious break from the IMF. The organisation, perhaps more than the EU, has insisted on tough reforms and austerity measures in return for the rescue funds. These have exacerbated a six-year recession, the worst on record, left a quarter of the workforce unemployed, and seen support for Samaras's fragile coalition plummet' (H. Smith, 'Greece tells IMF it wants early exit from rescue programme', The Guardian, 12 October 2014).

some years after 1989. It took most of these countries about two decades to return just to the pre-transition level of manufacturing output.

Stiglitz (2002, p.139), chief economist at the World Bank (1997-2000), criticised the arrogant Washington-based financial institutions because of their dangerously simple policy agenda based on old-fashioned textbooks which overlook the need and importance to have well operating market-related institutions in place:

> In the nations with mature market economies, the legal and regulatory frameworks had been built up over a century and a half, in response to problems encountered in unfettered market capitalism. ... They tried to take a shortcut to capitalism, creating a market economy without the underlying institutions, and institutions without the underlying institutional infrastructure. Before you set up a stock market, you have to make sure there are real regulations in place.

In the new market-style circumstances, local administrations got new responsibilities, for instance, in infrastructure. They had no experience in this area and had no adequate finance at the local level.

Some may dispute the large post 1989 fall in output in the transition countries. They may argue that the real depression was far less serious than was reported by statistics. Doubts come first from dubious, i.e. inflated production figures during the centrally planned period. Firms wanted to claim rewards for the fulfilment of planned targets, so there was a degree of false reporting. Next, in a transition (and market) economy firms may underreport output to reduce tax obligations. Finally, there was a rapid growth of the new private sector in services and informal economy that may not be fully captured by the official statistics.

Prospects for the joining of the European Union (EU) strongly assisted in the transition process. Trade, financial aid, investment, competition, improvements in environmental affairs and education exchanges helped a lot in the transition process. However, the 2007-09 crises had a negative impact on developments. Populist measures such as subsidies for pensions, energy and transport, as well as state control were featuring rather high. This was unfriendly both with economic transition and democracy.

Growth picked up during the transition period, but it was on average slow. The European Bank for Reconstruction and Development (EBRD) was concerned about the continued economic vigour in the transition region. EBRD questioned in 2013 if 'convergence can continue at a sufficient pace to push average per capita income in most of these countries above 60 per cent of the EU-15 average (and above 80 per cent in a few cases) by about 2035. ... the transition region does indeed face a serious long-term growth problem and that, given the current policies, convergence with Western living standards as defined above will not be achieved in most countries. Even if convergence is eventually achieved, progress will be very slow' (EBRD, 2013, p.11). Only the Czech Republic and Slovakia are projected to have incomes per capita of 80 per cent of the average in the old EU(15) by 2035 (EBRD, 2013, p.17).

Volkswagen-Škoda is an example of a successful FDI story. Elsewhere, in Hungary, Nuovometal GmbH acquired DAM Miskolc foundry just to close it down in order to reduce competition on the EU market.

Transition opened opportunities for integration with the world economy. Openness gave a chance to foreigners to invest in the transition region. Principal drivers for foreign direct investment (FDI) were low wages and potentially expanding local markets. Volkswagen-Škoda is an example of a successful FDI story. Elsewhere, in Hungary, Nuovometal GmbH acquired DAM Miskolc foundry just to close it down in order to reduce competition on the EU market. Once the Eastern or Central European firm is acquired, the usual practice was to close down first the local research and development department. In spite of that 'local research brain closure', linkages with foreign companies provided the local firm with new technologies in production, management and marketing. It included local firms into a huge global supply and marketing chain that was previously missing.

Belarus was one of the transition countries that reformed least. The country abolished central planning, liberalised trade, but kept strong state control of the economy. The population saw the transition-related chaos in the neighbouring countries. There was little bottom up pressure for a change from the population. Living standards was relatively high, there was social stability, population was subsidised, while energy prices were low because of the heavy discount received from Russia. The Belarus social contract was that the government provides stability, order, certain modernity and low level of income inequality in return for votes. The population valued order over political freedom. One ought to keep in mind that 'Belarus has the highest proportion of Schengen visas per capita of any country in the world and Belarusians routinely travel to neighbouring Lithuania and Poland (both of which are EU Member States with democratic political orders)' (EBRD, 2013, p.31). The Belarus population was informed about and exposed to alternative social and economic choices and consequences. While Belarus economic performance was superior to the performance of other ex-Soviet states (bar the Baltics), the country's performance was comparable to the average performance of central European states.

Russian oligarchs built their business empires on close links with state officials in a lawless business environment.

Russian oligarchs built their business empires on close links with state officials in a lawless business environment. These 30 or so persons had a privileged access to foreign exchange, subsidies, allocation of export quotas, preferential import tariffs and privatisation of state property.[9] If they wanted to add political power to their significant economic might, they run into trouble with the Russian President Putin.

5. European Union entry effects on Central and Eastern European countries: economic dimension during 2000-2013

Let us start first with basic data on GDP in the 'new' EU eastern member countries (Table 1). A striking feature is that all of these countries demonstrated economic growth both before and after EU entry. This is a positive sign which shows strength in the expansion of the economy. Even a strong possibility of EU entry provides grounds for vigour

[9] Oligarch Khodorkovsky was able to stop the 2002 law in the Russian Duma that would raise excise tax on oil.

in growth. Another issue is that the rates of growth in the 'new' EU countries before the financial crises (2007-09) were significantly faster than the average in the 'old' EU countries. This is, of course, the consequence of their lower economic starting point, but the fact remains that these countries were expanding fast. The crises hit hard in the east, hence the fall in GDP in 2009 was on average deeper in this group than in the western part of the EU.

Table 2 presents GDP data per capita in euros. There is an obvious gap between the 'poor' east and 'rich' west/north of the EU. An encouraging fact is that most of the eastern countries almost doubled their GDP per capita in the period 2000-13. The lower the staring base, the faster the improvement. Still, there is a huge gap between the average EU GDP per capita and the same indicator in most of the eastern EU member countries.

Manufacturing production is a good indicator of the health of an economy, especially those that rely more on this economic sector than on services, agriculture, mining and fisheries (Table 3). Manufacturing production experienced a constant rise following 2000. However, the crisis year 2009 was especially hard for the entire EU. Some recovery was noted in the subsequent period.

The rate of unemployment indicates in part the irreversible loss of potential contribution to GDP (Table 4). Many eastern countries started the period of observation with a rather high rate of unemployment. In spite of obvious emigration (in certain cases quite massive) towards the 'old' EU countries, EU entry did not bring about a clear and noticeable change in the rate of unemployment (2009 was a tough year for the entire EU, even for this indicator).

The rate of inflation during the period 2000-2013 was largely under control throughout the region (Table 5). This rate had a slight deceleration tendency which shows that the monetary authorities were able to handle this important economic indicator. The budget deficit indicator is covered in Table 6. Apart from 2009 as an exceptional year, most of the eastern EU members were very close to the Maastricht Treaty prescribed limit of 3 per cent of GDP. In fact, the eastern countries that were outside of the eurozone were following the eurozone's basic rules in a superior way to the full eurozone members. The same is true for the government debt level prescribed by the eurozone (60 per cent of GDP)(Table 7). The eastern non-eurozone countries exhibited an excellent performance regarding this indicator. However, the troubling sign is that while the average eurozone government debt increased from 70 per cent in 2004 to 91 per cent in 2013, the same debt in the eastern EU countries usually doubled if not tripled (Bulgaria is an exception as its debt remained largely undisturbed in the period 2007-13).

Tables 8 and 9, respectively, confirm that trade was an engine of growth for the 'new' EU member countries in the east. There was a strong and continuous expansion of exports and imports following EU entry. This reconfirms the expectation that integration increases trade. However, apart from Estonia, Latvia and Malta, all eastern countries had a deficit in trade (Table 10).

The EU trade war with Russia provoked by crisis in Ukraine in 2014 introduced reciprocal sanctions in commerce. EU farmers, especially in Central and Eastern Europe (but also in France, Spain and Greece) suffered a lot as they could not export their traditional goods to Russia. It was rather hard to be tough on farmers in Poland (or Greece) for selling perishable fruits to Russia at the same time when France was selling Russia state of the art offensive warships.

Integration and EU entry also stimulated inflow of FDI in the east of the EU (Table 11). Even a serious prospect of EU entry gave investors the incentive to enter the 'new' EU countries. The biggest beneficiary of FDI inflows was Poland (the size of the domestic market also played a role in the attraction of FDI).

The troubling sign is that the fragile and indebted eastern economies may not have access to the capital market.

Our final set of tables is devoted to foreign debt (Tables 12 and 13, respectively). In general, the foreign debt of the eastern EU countries almost doubled vis-à-vis GDP since their EU entry. The current economic success is heavily financed by people borrowing from their children and grandchildren (inter-generational transfer where those that are supposed to foot the bill in the future are not asked now about expenditure). The exception is Bulgaria, which kept the same level of foreign debt. Certain indebted countries such as Hungary had to call the IMF for a rescue, but after the IMF imposed harsh austerity policies Hungary decided to rescind all assistance from the institution and closed the IMF's office in 2013 (one may observe a decrease in debt burden since 2011 in Table 13). The troubling sign is that the fragile and indebted eastern economies may not have access to the capital market and obtain loans at favourable rates to finance obligations in the future. Belt tightening would be necessary, but it will have a negative impact on employment, trade and especially on growth in the future. If there are moves towards a more federal structure of the EU, including the banking union and direct federal transfers of resources to the disadvantaged countries, a number of eastern EU member countries may be on the side of consumption of these benefits. If one compares debt and GDP growth rates one may conclude that in almost all countries debt acceleration is much faster than the rate of GDP growth. Hence, these countries (just like most of the world's other countries) were living on a 'credit card'.

6. Questions

Has transition been worth it? Let us put aside obvious political and social gains such as democracy and greater openness and access to the outside world. In economic terms (the topic of this article) overall economic performance in terms of growth since the late 1980s for most transition countries averages out at a very low rate. The national economies did not become more vigorous and confident even after a generation-long transition. The exception may be perhaps Poland and a few other countries.

Regarding one 'verdict' about the end of economic transition, let us paraphrase Kolodko (2013, pp. 465-466):

- Could it have been better?
- Yes, if the objectives had been more carefully determined.
- Will it be better?
- Yes.
- When it will be better?
- 'It has already happened...'

There is no magic bullet in the transition process. If one compares economic development of England from the Elizabethan Era (1558-1603) with the country's current level of progress, Lipsey (1985, p. 455) observed that

It took 400 years for England to develop from that stage to its present one. To do the same elsewhere in half time of 200 years would be a tremendous achievement; to aspire to do it in 25 or 50 years may be to court disaster.

This may be to a large extent so. However, there is a (shining) example of China which under the communist regime, somehow opened up its economy, achieved a tremendous economic transformation since 1980s. In fact, China became the biggest single economy in the world in 2014. This has an important psychological effect globally. Positive growth-related economic changes and strong improvements are possible within a generation.

Hare and Turley (2013, p. 14) ask a question 'Would people have opted to abandon communism and embark on transition to a market-type economy had they realised how rocky and difficult the subsequent two decades would prove to be? We leave the final judgement about this to our readers.' Our comment is that in spite of casualties and costs,[10] the transition was worth it in spite of risks that come from openness to the influences from the global economy (as was the case in 2008). The centrally planned system was unsustainable in the long term compared to the market based economy which provides a certain degree of flexibility. However, the market system is not firmly embedded and shall need additional time to bring solid fruits to the fledgling economies in transition.

7. Conclusion

The principal mistake regarding transition in Central and Eastern Europe was an excessive faith in free markets and the Washington Consensus. Where free markets had a

[10] The world has recognised victims of holocaust, Nazism, communism and Stalinism. They all got monuments. The brutal economic policy of transition brought misery to tens of millions of people. However, nobody considers them as victims. Women suffered disproportionately from transition in terms of job security and a loss of non-wage services and benefits.

free hand, the outcome was an enrichment of few individuals without much accompanying economic development. Belarus and Uzbekistan reformed least, but they avoided the cost of extreme liberalisation and state breakdown. They did better than the most obvious comparator countries (immediate neighbours).

The process of transition brought enormous political gains to the population in terms of potentials for economic and political liberties; openness to new opportunities (often abroad); reduced pollution and brought cleaner environment (in the countries that joined the EU); travel, studies and work abroad. On the economic side, gains may be attained on a larger scale only over a long period of time as the fragile national economies need time to become robust and secure in the market-type environment. The most successful parts of the national economies became the ones that are linked with inward FDI. In fact, foreign subsidiaries are most often the principal national exporters. Still, few high-technology activities developed under domestic ownership, while FDI brought few of their high-value activities. The local manufacturing industry in Central and Eastern Europe performed badly compared with the rest of the EU. The future economic success depends in the transition region to a large extent on developments in the wealthy foreign partners, especially in Germany and even in Russia.

The process of transition brought enormous political gains to the population.

The EU membership offered chances, assistance and funds to accelerate transition, but this has happened at a price. External debt in Central and Eastern European countries went through the roof. There was also strong emigration by the young from Bulgaria, Romania and the Baltics states. The best workers also often left Poland. These countries remained with both shrinking and ageing (consumers) population which does not provide solid grounds for the future when the economy picks up (in a decade or so). Developments in demography create important challenges which have implications for pensions and public finances. Youth unemployment is worryingly high and persistent.

Eastern economies are modernising, but there is a cost: it has been a fast acceleration in government and foreign debt (danger of debt slavery) that has financed those successes. The risk is that this debt burden may partly suffocate economic vigour, enthusiasm and initial optimism in the eastern part of the EU, especially when interest rates increase. To sustain the payment of interest, transition countries would need to cut other spending. The former communist EU countries have been living on a 'credit card' debt that will have to be settled by future generations.

Uncertainty about the eurozone's future; no prospects for any significant growth in the eurozone for many years to come; the division between the EU's north and south; continuous riots in the south of the EU; the possibility that some countries may leave the EU; and apprehension about migration within and into the EU have all ensured that the general mood in the EU will be sombre for the coming decade. To some, the EU may no longer be the fuel from which one can get significant political mileage. The economic side of EU enlargement is a mixed bag of effects for the EU's eastern countries. Membership in the EU and economic transition is not a tide that lifts all boats.

Transition will not be complete until functioning institutions and reasonable public expenditure (education, health, pensions) are in place without excessive burden on the private sector. After a quarter of century of economic 'transition', the process brought many failures and certain successes, enthusiasm for it may evaporate, at least a bit. In fact, 'economic reform has stagnated in the transition region since the mid-2000s even in countries that are still far from reaching the transition frontier' (EBRD, 2013, p.4).

The future of Central and East European countries is uncertain. It largely depends on choices and preferences decided outside most of the transition countries, especially in Berlin, Brussels and Moscow. The end of transition is not yet in sight.

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ANNEX – TABLES

▸ *Table 1. GDP in the EU and eastern member countries, percentage change on previous period (2000-2013)*

GEO/TIME	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
EU (28 countries)	3.9	2.0	1.3	1.5	2.6	2.2	3.4	3.2	0.4	-4.5	2.0	1.6	-0.4	0.1
Euro area (17 countries)	3.8	2.0	0.9	0.7	2.2	1.7	3.2	3.0	0.4	-4.4	2.0	1.5	-0.6	-0.4
Bulgaria	5.7	4.2	4.7	5.5	6.7	6.4	6.5	6.4	6.2	-5.5	0.4	1.8	0.8	0.9
Croatia	3.8	3.7	4.9	5.4	4.1	4.3	4.9	5.1	2.1	-6.9	-2.3	0.0	-2.0	-0.9
Cyprus	5.0	4.0	2.1	1.9	4.2	3.9	4.1	5.1	3.6	-1.9	1.3	0.5	-2.4	-5.4
Czech Republic	4.2	3.1	2.1	3.8	4.7	6.8	7.0	5.7	3.1	-4.5	2.5	1.8	-1.2	-0.9
Estonia	9.7	6.3	6.6	7.8	6.3	8.9	10.1	7.5	-4.2	-14.1	2.6	9.6	3.9	2.2
Hungary	4.2	3.7	4.5	3.9	4.8	4.0	3.9	0.1	0.9	-6.8	1.3	1.6	-1.7	1.1
Latvia	5.7	7.3	7.2	7.6	8.9	10.1	11.2	9.6	-3.3	-17.7	-0.9	5.5	5.5	4.1
Lithuania	3.6	6.7	6.8	10.3	7.4	7.8	7.8	9.8	2.9	-14.8	1.5	5.9	3.7	3.3
Malta	:	0.0	2.4	0.7	-0.3	3.6	2.6	4.1	3.9	-2.8	4.0	1.6	0.8	2.9
Poland	4.3	1.2	1.4	3.9	5.3	3.6	6.2	6.8	5.1	1.6	3.9	4.5	1.9	1.6
Romania	2.4	5.7	5.1	5.2	8.5	4.2	7.9	6.3	7.3	-6.6	-1.1	2.2	0.7	3.5
Slovakia	1.4	3.5	4.6	4.8	5.1	6.7	8.3	10.5	5.8	-4.9	4.4	3.2	2.0	0.9
Slovenia	4.3	2.9	3.8	2.9	4.4	4.0	5.8	7.0	3.4	-7.9	1.3	0.7	-2.5	-1.1

▸ *Source: Eurostat(2014), http://epp.eurostat.ec.europa.eu/tgm/table.do?tab=table&init=1&plugin=1&language=en&pcode=tec00115 (accessed on 26.10.2014)*

▸ *Table 2. GDP per capita in the EU and eastern member countries member countries, annual data in euros, 2000-2013*

GEO/TIME	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
European Union (28 countries)	20.800	21.100	21.400	21.600	22.000	22.400	23.100	23.700	23.700	22.600	22.900	23.300	23.100	23.200
Euro area (17 countries)	24.000	24.400	24.500	24.500	24.900	25.200	25.800	26.400	26.400	25.100	25.600	25.900	25.700	25.500
Bulgaria	2.200	2.300	2.500	2.600	2.800	3.000	3.200	3.400	3.700	3.500	3.500	3.700	3.700	3.800
Croatia	6.500	6.800	7.100	7.500	7.800	8.100	8.500	8.900	9.100	8.500	8.300	8.600	8.400	8.400
Cyprus	16.700	17.200	17.400	17.500	18.000	18.400	18.900	19.400	19.600	18.700	18.500	18.100	17.400	16.400
Czech Republic	8.300	8.600	8.800	9.200	9.600	10.200	10.900	11.500	11.700	11.100	11.400	11.600	11.500	11.300
Estonia	5.800	6.200	6.600	7.100	7.600	8.300	9.200	9.900	9.500	8.100	8.300	9.100	9.500	9.800
Hungary	7.100	7.400	7.700	8.000	8.400	8.800	9.200	9.200	9.300	8.700	8.800	8.900	8.800	9.000
Latvia	3.700	4.000	4.300	4.700	5.200	5.800	6.500	7.200	7.000	5.900	5.900	6.400	6.800	7.100
Lithuania	4.100	4.400	4.800	5.300	5.800	6.300	6.900	7.700	8.000	6.900	7.100	7.700	8.100	8.500
Malta	11.900	11.800	12.000	12.000	11.900	12.200	12.500	12.900	13.300	12.800	13.400	13.500	13.500	13.800
Poland	5.500	5.600	5.600	5.900	6.200	6.400	6.800	7.300	7.600	7.800	8.000	8.300	8.500	8.700
Romania	2.700	2.900	3.100	3.200	3.500	3.700	4.000	4.200	4.600	4.300	4.200	4.300	4.700	4.800
Slovakia	5.600	5.800	6.100	6.400	6.700	7.100	7.700	8.500	9.000	8.600	8.900	9.200	9.400	9.500
Slovenia	12.100	12.400	12.900	13.300	13.800	14.400	15.100	16.100	16.600	15.200	15.300	15.400	15.000	14.800

▸ *Source: Eurostat (2014) http://appsso.eurostat.ec.europa.eu/nui/show.do?dataset=nama_aux_gph&lang=en (accessed on 26.10.2014)*

▸ *Table 3. Production in industry in the EU and eastern member countries, annual data, percentage change (2000-2013)*

GEO/TIME	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
European Union (28 countries)	4.9	0.2	-0.4	0.5	2.3	1.5	4.1	3.6	-1.8	-14.0	6.8	3.0	-2.2	-0.4
Euro area (17 countries)	5.2	0.2	-0.5	0.2	2.1	1.4	4.2	3.8	-1.8	-15.1	7.3	3.1	-2.4	-0.7
Bulgaria	:	2.2	4.7	12.8	12.7	7.0	6.1	9.7	0.3	-18.2	2.3	5.7	-0.2	0.0
Croatia	1.4	6.4	4.9	3.3	2.5	5.0	4.3	5.1	0.7	-8.9	-1.5	-1.2	-5.4	-1.9
Cyprus	:	4.5	1.6	-0.1	1.8	0.9	0.4	4.7	4.2	-9.3	-1.7	-7.8	-9.7	-12.2
Czech Republic	7.4	7.6	1.9	3.7	9.7	4.3	8.7	10.6	-2.4	-13.1	8.2	5.9	-0.8	0.2
Estonia	15.8	8.5	8.7	11.4	9.6	11.1	10.1	6.4	-4.8	-23.9	23.0	19.7	1.4	3.0
Hungary	17.5	4.0	3.3	6.5	6.9	7.2	10.6	8.0	-0.9	-17.4	10.3	5.6	-1.4	1.5
Latvia	-4.5	10.8	7.3	8.0	6.3	7.6	6.5	1.5	-3.2	-18.0	14.5	8.8	6.1	-0.3
Lithuania	-1.2	14.0	4.6	14.5	11.1	7.8	4.9	2.0	4.7	-13.8	6.1	6.7	3.6	3.5
Malta	:	-6.5	0.5	4.6	-0.8	-5.5	7.2	7.3	-4.4	-14.2	8.7	1.5	3.0	-5.2
Poland	7.8	0.9	1.6	8.4	12.3	4.1	12.3	9.2	2.3	-3.7	10.8	7.1	1.4	2.4
Romania	:	4.2	0.2	-0.8	1.5	-2.9	9.9	10.0	2.6	-5.4	4.8	7.6	2.4	7.8
Slovakia	5.7	3.6	7.0	15.5	3.5	-0.7	15.8	16.8	14.5	-15.6	8.2	5.4	7.7	5.3
Slovenia	7.2	3.5	2.1	0.9	3.8	4.6	6.3	7.3	1.4	-17.6	7.0	1.9	-0.5	-1.4

▸ *Source: Eurostat (2014), http://epp.eurostat.ec.europa.eu/tgm/table.do?tab=table&init=1&language=en&pcode=teiis090&plugin=0 (accessed on 26.10.2014)*

▸ *Table 4. Unemployment rate in the EU and eastern member countries, annual data (%), 2000-2013*

GEO/TIME	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
European Union (28 countries)	8.9	8.6	9.0	9.2	9.3	9.1	8.3	7.2	7.1	9.0	9.7	9.7	10.4	10.8
Euro area (17 countries)	8.7	8.1	8.5	9.0	9.3	9.2	8.5	7.6	7.6	9.6	10.1	10.1	11.3	12.0
Bulgaria	16.4	19.5	18.2	13.7	12.1	10.1	9.0	6.9	5.6	6.8	10.3	11.3	12.3	13.0
Croatia	15.8	15.9	15.1	14.1	13.8	12.8	11.4	9.6	8.4	9.1	11.8	13.5	16.1	17.3
Cyprus	4.8	3.9	3.5	4.1	4.6	5.3	4.6	3.9	3.7	5.4	6.3	7.9	11.9	15.9
Czech Republic	8.8	8.1	7.3	7.8	8.3	7.9	7.1	5.3	4.4	6.7	7.3	6.7	7.0	7.0
Estonia	13.6	12.6	10.3	10.1	9.7	7.9	5.9	4.6	5.5	13.8	16.9	12.5	10.0	8.6
Hungary	6.3	5.6	5.6	5.8	6.1	7.2	7.5	7.4	7.8	10.0	11.2	10.9	10.9	10.2
Latvia	13.7	12.9	12.8	11.3	11.2	9.6	7.3	6.5	8.0	18.2	19.8	16.2	15.0	11.9
Lithuania	16.4	17.4	13.8	12.4	11.3	8.0	5.2	3.8	5.3	13.6	18.0	15.4	13.4	11.8
Malta	6.7	7.6	7.4	7.7	7.2	7.3	6.9	6.5	6.0	6.9	6.9	6.5	6.3	6.4
Poland	16.1	18.3	20.0	19.8	19.1	17.9	13.9	9.6	7.1	8.1	9.7	9.7	10.1	10.3
Romania	6.8	6.6	7.5	6.8	8.0	7.2	7.3	6.4	5.8	6.9	7.3	7.4	6.8	7.1
Slovakia	18.9	19.5	18.8	17.7	18.4	16.4	13.5	11.2	9.6	12.1	14.5	13.7	14.0	14.2
Slovenia	6.7	6.2	6.3	6.7	6.3	6.5	6.0	4.9	4.4	5.9	7.3	8.2	8.9	10.1

▸ *Source: Eurostat (2014) http://epp.eurostat.ec.europa.eu/tgm/table.do?tab=table&init=1&language=en&pcode=tipsun20&plugin=0 (accessed on 26.10.2014)*

▸ Table 5. Inflation rate in the EU and eastern member countries, annual average rate of change (%), 2000-2013

GEO/TIME	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
European Union (28 countries)	3.5	3.2	2.5	2.1	2.3	2.3	2.3	2.4	3.7	1.0	2.1	3.1	2.6	1.5
Euro area (17 countries)	2.2	2.4	2.3	2.1	2.2	2.2	2.2	2.1	3.3	0.3	1.6	2.7	2.5	1.4
Bulgaria	10.3	7.4	5.8	2.3	6.1	6.0	7.4	7.6	12.0	2.5	3.0	3.4	2.4	0.4
Croatia	4.5	4.3	2.5	2.4	2.1	3.0	3.3	2.7	5.8	2.2	1.1	2.2	3.4	2.3
Cyprus	4.9	2.0	2.8	4.0	1.9	2.0	2.2	2.2	4.4	0.2	2.6	3.5	3.1	0.4
Czech Republic	3.9	4.5	1.4	-0.1	2.6	1.6	2.1	3.0	6.3	0.6	1.2	2.1	3.5	1.4
Estonia	3.9	5.6	3.6	1.4	3.0	4.1	4.4	6.7	10.6	0.2	2.7	5.1	4.2	3.2
Hungary	10.0	9.1	5.2	4.7	6.8	3.5	4.0	7.9	6.0	4.0	4.7	3.9	5.7	1.7
Latvia	2.6	2.5	2.0	2.9	6.2	6.9	6.6	10.1	15.3	3.3	-1.2	4.2	2.3	0.0
Lithuania	1.1	1.6	0.3	-1.1	1.2	2.7	3.8	5.8	11.1	4.2	1.2	4.1	3.2	1.2
Malta	3.0	2.5	2.6	1.9	2.7	2.5	2.6	0.7	4.7	1.8	2.0	2.5	3.2	1.0
Poland	10.1	5.3	1.9	0.7	3.6	2.2	1.3	2.6	4.2	4.0	2.7	3.9	3.7	0.8
Romania	45.7	34.5	22.5	15.3	11.9	9.1	6.6	4.9	7.9	5.6	6.1	5.8	3.4	3.2
Slovakia	12.2	7.2	3.5	8.4	7.5	2.8	4.3	1.9	3.9	0.9	0.7	4.1	3.7	1.5
Slovenia	8.9	8.6	7.5	5.7	3.7	2.5	2.5	3.8	5.5	0.9	2.1	2.1	2.8	1.9

▸ Source: Eurostat (2014) http://epp.eurostat.ec.europa.eu/tgm/table.do?tab=table&init=1&language=en&pcode=tec00118&plugin=0 (accessed on 26.10.2014)

▸ *Table 6. Government deficit/surplus in the EU and eastern member countries, percentage of GDP, 2000-2013*

GEO/TIME	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
European Union (27 countries)	0.6	-1.5	-2.6	-3.2	-2.9	-2.5	-1.5	-0.9	-2.4	-6.9	-6.5	-4.4	-4.2	-3.2
Euro area (17 countries)	-0.1	-1.9	-2.6	-3.1	-2.9	-2.5	-1.3	-0.7	-2.1	-6.4	-6.2	-4.2	-3.6	-2.9
Bulgaria	-0.5	1.1	-1.2	-0.4	1.9	1.0	1.9	1.2	1.7	-4.3	-3.1	-2.0	-0.5	-1.2
Croatia	:	:	-4.1	-4.5	-4.3	-4.0	-3.0	-2.5	-1.4	-4.1	:	:	-5.6	-5.2
Cyprus	-2.3	-2.2	-4.4	-6.6	-4.1	-2.4	-1.2	3.5	0.9	-6.1	-5.3	-6.3	-5.8	-4.9
Czech Republic	-3.6	-5.6	-6.5	-6.7	-2.8	-3.2	-2.4	-0.7	-2.2	-5.8	-4.8	-3.3	-4.0	-1.3
Estonia	-0.2	-0.1	0.3	1.7	1.6	1.6	2.5	2.4	-2.9	-2.0	0.2	1.2	-0.3	-0.5
Hungary	-3.0	-4.1	-9.0	-7.3	-6.5	-7.9	-9.4	-5.1	-3.7	-4.6	-4.3	4.3	-2.3	-2.4
Latvia	-2.8	-2.0	-2.3	-1.6	-1.0	-0.4	-0.5	-0.4	-4.2	-9.8	-8.1	-3.6	-0.8	-0.9
Lithuania	-3.2	-3.5	-1.9	-1.3	-1.5	-0.5	-0.4	-1.0	-3.3	-9.4	-7.2	-5.5	-3.2	-2.6
Malta	-5.7	-6.3	-5.7	-9.0	-4.6	-2.9	-2.7	-2.3	-4.6	-3.7	-3.6	-2.8	-3.7	-2.7
Poland	-3.0	-5.3	-5.0	-6.2	-5.4	-4.1	-3.6	-1.9	-3.7	-7.4	-7.9	-5.0	-3.7	-4.0
Romania	-4.7	-3.5	-2.0	-1.5	-1.2	-1.2	-2.2	-2.9	-5.7	-9.0	-6.8	-5.6	-3.0	-2.2
Slovakia	-12.3	-6.5	-8.2	-2.8	-2.4	-2.8	-3.2	-1.8	-2.1	-8.0	-7.7	-5.1	-4.2	-2.6
Slovenia	-3.7	-4.0	-2.4	-2.7	-2.3	-1.5	-1.4	0.0	-1.9	-6.2	-5.9	-6.4	-3.7	-14.6

▸ *Source: Eurostat (2014) http://epp.eurostat.ec.europa.eu/tgm/table.do?tab=table&init=1&language=en&pcode=teina200&plugin=0 (accessed on 26.10.2014)*

▸ *Table 7. General government gross debt ('Maastricht debt') % of GDP in the EU, eastern member economies and select other countries, annual data, 2000-2013*

GEO/TIME	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
European Union (27 countries)	61.9	61.1	60.5	62.0	62.4	62.8	61.6	59.0	62.3	74.6	80.0	82.5	83.6	85.4
Euro area (17 countries)	69.2	68.2	68.0	69.2	69.6	70.3	68.6	66.4	70.2	80.0	85.4	87.3	89.1	91.1
Bulgaria	72.5	66.0	52.4	44.4	37.0	27.5	21.6	17.2	13.7	14.6	16.2	16.3	18.0	18.3
Croatia	:	:	40.0	40.9	43.2	43.7	35.5	32.9	28.9	35.3	:	:	64.4	75.7
Cyprus	59.6	61.2	65.1	69.7	70.9	69.4	64.7	58.8	48.9	58.5	61.3	71.1	79.5	102.2
Czech Republic	17.8	23.9	27.1	28.6	28.9	28.4	28.3	27.9	28.7	34.2	37.8	40.8	45.5	45.7
Estonia	5.1	4.8	5.7	5.6	5.0	4.6	4.4	3.7	4.5	7.1	6.7	6.1	9.7	10.1
Hungary	56.1	52.7	55.9	58.6	59.5	61.7	65.9	67.0	73.0	79.8	81.8	81.4	78.5	77.3
Latvia	12.4	14.1	13.6	14.7	15.0	12.5	10.7	9.0	19.8	36.9	44.4	41.9	40.9	38.2
Lithuania	23.6	23.0	22.2	21.0	19.3	18.3	17.9	16.8	15.5	29.3	37.9	38.5	39.9	39.0
Malta	53.9	58.9	57.9	66.0	69.8	68.0	62.5	60.7	60.9	66.4	67.4	70.3	67.9	69.8
Poland	36.8	37.6	42.2	47.1	45.7	47.1	47.7	45.0	47.1	50.9	54.8	56.2	54.4	55.7
Romania	22.5	25.7	24.9	21.5	18.7	15.8	12.4	12.8	13.4	23.6	30.5	34.7	37.3	37.9
Slovakia	50.3	48.9	43.4	42.4	41.5	34.2	30.5	29.6	27.9	35.6	41.0	43.3	52.1	54.6
Slovenia	26.3	26.5	27.8	27.2	27.3	26.7	26.4	23.1	22.0	35.0	38.6	46.9	53.4	70.4
Japan	-	-	-	-	166.3	169.5	166.8	162.4	171.1	188.7	193.3	210.6	216.5	224.6
Switzerland	-	-	-	-	59.4	56.2	50.0	50.0	45.5	44.5	43.2	42.3	46.5	46.2
United Kingdom	-	-	-	-	43.9	45.5	45.3	46.4	56.7	71.3	84.5	99.0	101.6	99.3
United States					67.5	64.6	63.4	63.8	72.6	85.8	94.6	98.8	102.1	104.3

▸ *Source: Eurostat (2014) http://epp.eurostat.ec.europa.eu/tgm/table.do?tab=table&init=1&language=en&pcode=teina225&plugin=0. (accessed on 26.10.2014) OECD Economic Outlook. Vol. 2014/1 © OECD 2014, p. 311.*

▸ *Table 8. EXPORTS - EU trade: Total and by the eastern member states, exports in million euros, 2000-2013*

GEO/TIME	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
EU (28 countries)	849.740	884.707	891.899	869.237	952.951	1.057.627	1.161.776	1.244.005	1.319.819	1.101.746	1.360.059	1.561.890	1.683.088	1.737.022
Bulgaria	2.302	2.247	2.301	2.456	3.015	3.686	4.619	5.292	.6086	4.104	6.092	7.660	8.533	8.873
Cyprus	174	217	191	163	249	316	316	287	341	298	357	419	532	640
Czech Republic	4.438	5.024	5.813	5.465	7.130	9.082	10.815	13.149	15.041	12.340	16.046	19.836	22.850	23.037
Estonia	411	690	667	703	936	1.355	2.656	2.391	2.536	1.978	2.749	4.053	4.254	3.562
Hungary	4.997	5.522	5.672	6.032	7.560	9.665	12.462	14.646	16.100	12.666	16.435	19.426	18.214	17.966
Latvia	390	479	538	526	730	973	1.348	1.668	2.167	1.786	2.356	3.208	4.003	3.657
Lithuania	973	1.275	1.699	2.291	2.455	3.260	4.097	4.409	6.383	4.213	6.107	7.796	9.092	10.457
Malta	1.754	966	1.127	1.020	1.024	924	1.071	1.399	1.413	1.229	1.592	1.858	2.016	1.509
Poland	6.460	7.563	8.199	8.595	11.867	15.369	18.555	21.602	25.717	19.950	25.169	29.862	34.320	38.355
Romania	3.136	3.151	3.841	3.861	4.796	6.657	7.683	8.277	9.921	7.496	10.390	13.112	13.315	15.068
Slovakia	1.312	1.323	1.606	2.719	2.967	386	4.393	5.625	7.085	5.686	7.633	8.742	9.953	11.017
Slovenia	2.648	3.038	3.439	3.591	4.276	4.927	5.848	6.740	7.405	5.770	6.370	7.251	6.258	6.446

▸ *Source: Eurostat (2014) http://appsso.eurostat.ec.europa.eu/nui/show.do?dataset=ext_lt_intratrd&lang=en (accessed on 26.10.2014).*

▸ *Table 9. IMPORTS - EU trade: Total and by the eastern member states, imports in million euros, 2000-2013*

GEO/TIME	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013.
EU (28 countries)	992.695	979.143	936.967	935.265	1.027.522	1.183.213	1.363.882	1.445.155	1.582.932	1.234.317	1.531.043	1.726.514	1.798.576	1.682.390
Bulgaria	3.337	3.489	3.560	4.063	4.996	4.677	5.994	9.082	10.866	6.757	7..989	9.508	10.499	10.428
Cyprus	1.405	1.539	1.660	1.421	1.357	1.566	1.730	1.955	2.322	1.563	1.939	1.931	1.749	1.404
Czech Republic	8.597	1.303	11.805	13.070	11.090	11.433	14.482	17.155	22.311	16.525	23.983	27.828	27.072	25.278
Estonia	1.357	1.613	1.581	2.003	1.760	1.951	2.738	2.445	2.203	1.427	1.875	2.728	3.123	2.497
Hungary	11.806	12.793	13.987	15.007	15.325	16.108	18.564	21.285	2.3547	17.486	21.506	22.554	21.707	21.314
Latvia	891	938	964	1.131	1.388	1.728	2.157	2.522	2.691	1.729	2.110	2.621	2.926	2.690
Lithuania	2.569	3.066	3.438	3.745	3.635	5.065	5.746	5.640	8.975	5.369	7.664	9.877	10.538	10.799
Malta	1.455	998	891	909	784	723	1.005	913	850	806	1.139	1.194	1.178	1.340
Poland	16.483	16.990	17.720	18.344	17.790	20.157	27.306	32.301	39.961	29.405	39.242	45.443	50.008	48.512
Romania	4.941	5.719	6.005	6.749	8.955	12.056	14.931	14.726	17.321	10.491	12.878	14.995	14.478	13.416
Slovakia	4.15	4.613	4.722	5.101	5.078	6.183	8.903	11.214	13.529	10.020	13.745	15.368	15.829	15.820
Slovenia	2.538	2.576	2.602	2.874	2.562	3.368	4.279	6.048	7.238	5.529	7.297	8.255	6.975	7.525

▸ *Source: Eurostat (2014) http://appsso.eurostat.ec.europa.eu/nui/show.do?dataset=ext_lt_intratrd&lang=en (accessed on 26.10.2014)*

▸ *Table 10. EU trade balance: Total and in the eastern member states, in million of euros, 2000-2013*

GEO/TIME	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
EU (28 countries)	-142.956	-94.436	-45.068	-66.028	-74.571	-125.586	-202.106	-201.150	-265.424	-132.571	-170.984	-164.624	-105.323	54.362
Bulgaria	-1.034	-1.242	-1.260	-1.607	-1.981	-991	-1.375	-3.790	-4.780	-2.653	-1.897	-1.848	-1.966	-1.555
Cyprus	-1.231	-1.322	-1.469	-1.258	-1.108	-1.250	-1.414	-1.668	-1.981	-1.265	-1.581	-1.511	-1.217	-764
Czech Republic	-4.159	-5.279	-5.992	-7.605	-3.960	-2.351	-3.667	-4.005	-7.271	-4.185	-7.937	-7.993	-4.222	-2.241
Estonia	-946	-923	-914	-1.300	-824	-596	-81	-54	333	551	874	1.326	1.131	1.066
Hungary	-6.809	-7.271	-8.315	-8.974	-7.765	-6.444	-6.102	-6.638	-7.448	-4.821	-5.071	-3.128	-3.493	-3.348
Latvia	-501	-459	-426	-605	-659	-755	-808	-854	-524	57	246	588	1.077	967
Lithuania	-1.596	-1.791	-1.739	-1.454	-1.181	-1.805	-1.649	-1.231	-2.593	-1.156	-1.557	-2.081	-1.445	-342
Malta	299	-32	237	111	240	201	66	487	563	424	453	664	838	169
Poland	-10.023	-9.426	-9.520	-9.749	-5.923	-4.788	-8.751	-10.699	-14.244	-9.455	-14.073	-15.580	-15.388	-10.158
Romania	-1.805	-2.569	-2.164	-2.887	-4.159	-5.399	-7.248	-6.448	-7.400	-2.996	-2.488	-1.884	-1.089	1.652
Slovakia	-2.803	-3.290	-3.116	-2.382	-2.111	-2.896	-4.510	-5.589	-6.444	-4.334	-6.112	-6.625	-5.652	-4.803
Slovenia	110	461	838	716	1.713	1.559	1.569	692	167	241	-926	-1.004	-717	-1.078

▸ *Source: Eurostat (2014) http://appsso.eurostat.ec.europa.eu/nui/show.do?dataset=ext_lt_intratrd&lang=en (accessed on 26.10.2014)*

▸ *Table 11. FDI inflows in the EU and eastern member countries, 2000-2013 in millions of dollars*

Country/Year	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
EU (17)	671.417	357.441	374.000	295.154	-	-	-	-	-	-	-	-	-	
EU (27)	-	-	-	-	204.245	496.075	581.719	850.528	487.968	346.531	304.689	441.557	216.012	246.207
Bulgaria	1.002	813	905	1.419	3.452	3.920	7.805	12.389	9.855	3.351	2.170	1.827	1.849	1.450
Croatia	1.089	1.561	1.124	1.713	1.227	1.825	3.473	5.035	6.179	2.911	583	1.502	1.356	580
Cyprus	804	652	614	830	1.090	1.186	1.864	2.234	4.050	5.725	4.860	1.372	1.257	533
Czech Republic	4.954	5.639	8.483	2.583	4.974	11.653	5.463	10.444	6.451	2.927	6.781	2.318	7.984	4.990
Estonia	387	542	284	891	971	2.869	1.797	2.725	1.731	1.838	1.539	257	1.517	950
Hungary	2.764	3.936	2.845	2.470	4.506	7.709	6.818	3.951	7.384	2.045	2.377	5.757	13.983	3.091
Latvia	411	163	384	360	637	707	1.663	2.322	1.261	94	349	1.466	1.109	808
Lithuania	379	446	732	179	773	1.028	1.817	2.015	2.045	172	629	1.448	700	531
Malta	622	281	-428	380	403	676	1.840	1.006	845	760	1.041	413	4	-2.100
Poland	9.341	5.713	4.131	4.225	12.890	10.293	19.603	23.561	14.839	13.698	9.681	18.911	6.059	-6.038
Romania	1.037	1.157	1.144	1.566	6.517	6.483	11.367	9.921	13.910	4.847	3.573	2.523	2.748	3.617
Slovakia	1.925	1.584	4.123	571	3.031	2.429	4.693	3.581	4.687	-50	526	2.143	2.826	591
Slovenia	137	369	1.606	181	827	588	644	1.514	1.947	-582	834	999	-59	-679

▸ *Source: WIR (2004, 2006, 2011, 2014).United Nations Conference on Trade and Development (UNCTAD)*

▸ *Table 12. Gross external debt as a % GDP, EU eastern member states, at the end of fourth quarter of the year, 2000-2013*

GEO/TIME	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Bulgaria	-	-	-	58.07	61.69	66.68	78.15	94.30	105.13	108.26	102.70	94.26	94.88	94.54
Cyprus	-	-	-	-	-	-	279.54	326.56	447.40	544.14	491.89	468.24	448.46	348.04
Czech Republic	-	-	-	-	-	40.14	39.91	43.05	48.52	51.35	56.30	59.65	60.48	64.64
Estonia	-	-	-	64.27	77.01	86.50	96.67	108.32	117.18	123.16	114.26	94.04	95.20	86.28
Hungary	65.93	60.97	53.13	64.43	71.15	82.38	92.37	105.42	123.15	144.92	144.93	147.99	129.65	120.34
Latvia	68.85	68.85	73.37	79.83	93.52	100.01	114.51	128.11	130.05	156.46	164.81	145.03	136.37	134.56
Lithuania	43.11	43.11	39.21	40.24	42.13	50.49	59.91	71.50	70.98	83.90	82.92	77.45	75.38	67.14
Malta	195.97	178.35	191.26	218.94	259.51	356.60	405.22	497.20	540.80	500.83	515.28	500.89	504.90	493.91
Poland	38.66	36.80	40.30	47.59	42.04	44.09	46.58	48.43	56.83	59.40	66.36	72.30	71.07	70.17
Romania	-	-	37.32	37.21	34.53	39.38	40.45	50.90	56.05	68.55	75.67	77.17	75.16	68.94
Slovakia	-	-	-	-	-	-	-	-	--	74.09	75.77	77.89	76.05	82.81
Slovenia	-	-	-	-	56.36	71.34	77.51	100.55	105.34	113.83	114.76	110.93	115.66	113.20

▸ *Source: European Central Bank (2014) http://sdw.ecb.europa.eu/browseSelection.do?type=series&q=gross+external+debt&node (accessed on 26.10.2014)*

▸ *Table 13. Gross external debt (millions of euro), EU eastern member states, at the end of fourth quarter of the year, 2000-2013*

GEO/TIME	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Bulgaria	-	-	-	10.634	12.561	15.504	20.691	29.017	37.247	37.817	37.027	36.295	37.636	37.758
Cyprus	-	-	-	-	-	-	41.008	51.919	76.760	91.705	85.618	83.711	79.469	57.440
Czech Republic	-	-	-	-	-	43.132	48.684	59.219	69.474	72.907	85.167	88.436	94.785	100.601
Estonia	-	-	-	5.604	7.459	9.672	12.945	17.406	19.025	17.205	16.420	15.250	16.622	16.059
Hungary	32.564	37.562	38.496	45.994	59.775	71.730	86.864	103.833	122.566	137.332	138.741	131.184	124.406	117.806
Lithuania	5.218	5.982	5 945	6.671	7.687	10.586	14.442	20.547	23.009	22.363	22.976	23.976	24.830	23.252
Latvia	5.061	6.389	6.814	7.561	9.943	12.929	18.275	27.081	29.533	28.831	29.700	29.598	30.334	30.437
Malta	8.586	8.019	8.899	10.157	12.120	17.585	21.123	27.785	32.066	29.956	33.005	33.648	35.189	35.871
Poland	74.757	82.081	81.029	85.339	95.167	112.312	128.875	158.599	174.527	194.570	236.478	247.826	278.269	276.288
Romania	-	-	16.146	17.851	21.682	30.920	41.198	58.696	71.713	81.089	92.980	99.376	99.356	96.923
Slovenia	-	-	-	-	15.343	20.497	24.068	34.783	39.234	40.318	40.723	40.100	41.264	39.930
Slovakia	-	-	-	-	-	-	-	-	-	46.527	49.910	53.828	54.067	59.735

▸ *Source: European Central Bank (2014) http://sdw.ecb.europa.eu/browseSelection.do?type=series&q=gross+external+debt&node (accessed on 26.10.2014)*

Did EU Membership of the Central and Eeastern European Countries Contribute to Peace?

▸ René Schwok

Introduction

The formula "Central and Eastern Europe countries" (CEECs) refers to the States that either belonged to the USSR or were under its control before 1989. Seven of them joined the EU in 2004: Estonia, Hungary, Latvia, Lithuania, Poland, the Czech Republic and Slovakia. In 2007, Bulgaria and Romania joined them.

Most experts were then raising doubts about the ability of these countries to reform.

In the early 1990s, all these States were seen as fragile. Many observers were quite pessimistic about their abilities to avoid falling into forms of autocracy that would eventually threaten peace in the region. Most of these countries enjoyed little or no periods of democracy in their history. Their economies were largely controlled by the State and were most of the time in recession. Their bureaucracies were overstaffed and struggling for reform. Some were under strong nationalist impulses at high bellicose potential.

Most experts were then expressing their concern about the future of the CEECs. They were raising doubts about the ability of these countries to reform, to meet the challenges that they were facing and to transform into stable, developed and democratic countries. Every success of an extremist party was then analyzed as a warning sign of the soon to come disasters.

In addition, it was announced that accession of these CEE countries would destabilize the EU because they had not matured enough its values. It was thus anticipated that they were going either to blow up the Union, or to divert it to the wrong direction.

Václav Klaus, a self-proclaimed *Eurosceptic*, often said that accession of Central and Eastern Europe countries (CEECs) to the European Union (EU) did not contribute to their stabilization and to the security of their area. He argues that many other factors have been much more instrumental in bringing peace in Central and Eastern Europe than EU membership. The former Czech prime minister and president also hinted several times that the EU could be a factor of destabilization and chaos.[1]

This chapter deals with those arguments and aims at assessing their relevance. In order to proceed in a balanced way, I tried to reconstitute the two main conflicting conceptions: the one of the *Eurosceptics* and the one of the *Europeists*.

This reconstruction has primarily a didactic purpose, i.e., to allow a better understanding of a ways of articulating an argument. These two conceptualizations are designed as flexible analytical frameworks: "ideal types" in the Weberian sense. In other words, some researchers and politicians who are quoted in the *Europeist* paradigm can, in relation to other topics, belong to the *Eurosceptic* way of thinking and *vice versa*.

My method is dialectical: I will first introduce the *Eurosceptic* approach. Then, I will confront it with the opposite view of the *Europeists* (antithesis). In addition, I will assess the cases of some key countries from Central and Eastern Europe. Finally, I will compare the EU CEECs with the non-EU CEECs.

Euroseptic Approach

The first conception is the one of the *Eurosceptics*[2]. This approach develops a critical analysis of the dialectical link between absence of war in Europe and advent of the Euro-

[1] Vaklav Klaus, Europe: The Shattering of Illusions (Bloomsbury Continuum 2013).

[2] Aleks Szczerbiak & Paul Taggart (eds.), Opposing Europe the Comparative Party Politics of Euroscepticism. Comparative and Theoretical Perspectives (Oxford University Press 2008).

pean Union. *Eurosceptics* such as Václav Klaus dispute the assertion that EU enlargements contributed to security and peace in Europe. First, they challenge the idea that the EU's characteristics, methods and policies have reduced the risks of war. Second, they suggest that there are other factors, beyond the issue of EU membership, which were more effective for stabilizing the Central and Eastern European countries.

Accordingly, any explanation of the pacification of this area has to be related to the own merits of these States and also to their incorporation into NATO. Third, some *Eurosceptics* even claim that EU enlargement can even be a factor of destabilization.

On a conceptual level, the *Eurosceptic* approach uses generally unflattering terms for characterizing EU action such as: naive, pacifist, political dwarf, small power, big Switzerland, Venus (compared to Mars).

European integration has not been a major factor of peace

Eurosceptics do not consider EU legislations as an international kind of law as envisaged by Kantian political liberalism. They see it as mainly economic.[3] Therefore, EU law cannot contribute to the resolution of international conflicts. EU law does not address the issues of war and peace between the Member States. So according to the *Eurosceptics*, it is misleading to convey the message that the significant progress of Community law could be something comparable to the development of international law as envisaged by the cosmopolitist doctrine.

In addition, according to the *Eurosceptics*, the EU does not have a monopoly of legitimate violence in the Weberian sense. It has neither an army nor a police force that could operate on the territory of the Member States. Moreover, when there are problems within the EU that could cause a conflict with military dimensions (Northern Ireland, Cyprus, the Basque country, Catalonia), the Union takes great care not to interfere. And there is clear evidence in the Treaties that the European security and defense policy should only be exercised outside the EU.

[3] Tony Judt, A Grand Illusion. An Essay on Europe (New York University Press 2001).

Researchers belonging to the *Eurosceptic* school of thought have also never missed to express their deepest doubts on the so-called qualities of functionalism. First, they point out that, despite the development of numerous specialized regional and international organizations in the world, the number of conflicts in the world remains just as high as in the past.

The EU does not have a monopoly of legitimate violence.

In addition, *Eurosceptics* point out that technocracy could be itself a factor of conflict because technocrats, such as the so-called *Eurocrats*, are not elected by a popular vote. They have no accountability towards their voters and tend to make decisions with cold rationality in a kind of ivory tower isolated from realities.

Finally, this technostructure is subject to pressure from lobbying groups with which it works closely. In other words, European integration is not driven by the politicians but by a technostructure responding to proposals from private interest groups, as it is practiced in the United States.

Other factors that enlargement explain peace

The *Eurosceptic* approach considers that the relatively good performance of the CEE countries, as well as peace in this region, is the result of multiple components that are distinct from their accession to the EU. *Eurosceptics* point out that it has passed more than a decade between the end of the communist domination and their accession to the EU. During this period, these countries had already consolidated their democracy, established rule of law and liberalized their economies. Thus, the CEECs were on the right track regardless of EU membership.

Concerning the issue of security, realists rather emphasize the positive role played by NATO enlargement than by the EU one. Indeed, all CEE countries have become members of the Atlantic Alliance before joining the European Union. This organization offers much better security protection that the EU because it provides a collective defense mechanism (art. 5), which commits its members to help each other when one of them is attacked. Such solidarity does not exist in the EU, even though a few articles of the Lisbon Treaty can create the illusion (Art. 42 § 7 TEU and art. 222 TFEU).

Added to this is that the most important member of the Atlantic Alliance is the United States. The main army in the world demonstrated in history that it alone has the capacity to assist allies who have difficulties in terms of security. Clearly, the European states do not today possess such capacities of intervention. Finally, NATO has played a substantial role in reforming the armed forces of the CEECs, making them all the more effective and more democratic.

Free trade is neither positive nor a peace factor

The issue of free trade is one of the most controversial one. *Eurosceptics* express all kinds of assessment of free trade from the ultra-liberal side to the Marxist camp.

Numerous British and American economists are claiming that the EU does not promote free trade enough.

For the former, for instance numerous British and American economists, the EU does not promote free trade enough. This is also the view of Václav Klaus. Accordingly, the EU contributes to poor economic health of Europe, to the impoverishment of the population and to dissatisfaction. This fuels political tensions. Basically, the EU remains too protectionist and therefore does not promote peace.

Another criticism of the liberal right is that the EU is limited geographically. Its free trade extends primarily to its Member States. But this creates as a result a sort of protectionism against countries that do not belong to it. For sure, the EU does not raise new barriers towards third countries, but it creates a diversion of trade and services. In addition, *Eurosceptics* accuse the EU of multiplying bilateral free trade agreements at the expense of the World Trade Organization (WTO). This undermines the multilateral system of the post-War, which aims at maintaining a universalist dimension. Once again, this has discriminatory protectionist consequences for those who are not EU members.

Critics expressed by far left people are, in turn, very different. It considers that the EU is too much oriented towards free trade and too favorable to the interests of the big capital. This contributes to increase social inequality. Consequently, this creates frustration and revolts that lead to conflicts. This is the view developed by the Marxist approach, for which trade between capitalist economies derive from the exploitation of the proletariat; this leads to imperialism and ultimately to war.

Far left thinkers challenge the chain of reasoning supporting the positive effects of free trade.[4] First, they consider that free trade does not improve the wellbeing of the population and that it badly damages small and medium enterprises. Accordingly, the international division of labor benefits only the most efficient companies and crushes the weakest ones. Innovation is not always positive and is not determined by international competition. Finally, economies of scale do not contribute to a better quality but to the standardization of consumption patterns.

Having developed such a negative analysis, it is no wonder that Marxists doubt that free trade can contribute to a virtuous spillover towards peace.[5] If populations are impoverished and frustrated, they will be receptive to the calls of the xenophobic parties who look for scapegoats among foreign populations and countries. In addition, the States that are the losers in the free trade competition are the ones who will naturally tend to seek international confrontation.

The Marxist approach always considered that market economy promotes armed confrontation between powers because they are so eager to take ownership of external markets. Therefore interdependence can lead to armed conflict. According to the arguments of the theory of unequal exchange, international trade is a source of conflict. Economic values have become instruments of power, based in particular on, either the monopoly

[4] Chad Damro, 'Market Power Europe' Journal of European Public Policy, 2012, 19, 5, pp. 682-699.

[5] Jacques Fontanel 2014, 'Le commerce international est-il un facteur de paix ?' Politique étrangère, 2014, 1, pp. 55-67.

of natural resources, or on the financial or technological superiority of one country such as Germany. This type of arguments was for a long time the discourse of the communist propaganda relayed by Moscow.

Other factors that the EU was more decisive for bringing peace

For *Eurosceptics*, many geopolitical and economic factors contributed much more to the preservation of peace in Central and Eastern Europe that European integration. There are broadly speaking two types of interpretation. The first approach is rather idealist and the second one is more realist.

An idealist view

For idealists, it is the shock of wars, especially of the Second World War, that led the Europeans to develop a deep aversion of wars. They admit that this has facilitated the acceptance of the ideology of European cooperation, but it does mean that European integration *per se* had any impact of peace.[6]

In other words, even if there had been no European integration, the result in terms of peace would have been the same. Accordingly, the development of democracy, rule of law, human rights and protection of minorities in Europe primarily drove peace but this has nothing to do with European integration.

This political and humanitarian progress was made in parallel with a substantial economic growth, a considerable development of social protection (welfare state) and a substantial societal liberation (decline of parental authoritarianism, secularization, emancipation of women, tolerance of various sexual practice). All these factors have been more

[6] Elie Barnavi, 'L'Europe, ce n'est pas la paix, c'est la conséquence de la paix' Le Monde, 8 October 2013.

decisive than European integration to calm the frustrations of the people and to limit the risks of their exploitation for war purposes. This produced a virtuous spillover that has moved away the minds from warmonger's impulses.

One finds here elements of the so-called *democratic peace theory*[7] that argues that war has become inconceivable in Central and Eastern Europe, not because of the unification of Europe, but because it is now composed of democratic States. According to this view, liberal democracies do not fight one another, although they can go to war.

A realistic view

Another *Eurosceptic* view is, on the contrary, rather realistic. It is particularly developed in the United States, among political scientists of the theory of international relations. According to this interpretation, it is the "American protection + NATO" which primarily explains the improvement of security in Central and Eastern Europe. Expansion of NATO contributed to legitimize the US presence and to formalize the military alliance with the CEECs; this contributed more than EU membership to the diminishing of the risks of war in Europe.[8]

In other words, the *Eurosceptics* reverse the argument put forward by the *Europeists*. The independent variable becomes the dependent variable, and *vice versa*. Because according to their view, peace in Europe should be attributed to factors other than the European project; but they admit that the EU made profit of this security in order to develop itself under its umbrella.[9]

[7] Michael Doyle, 'Kant, Liberal Legacies and Foreign Policy' Philosophy and Public Affairs, 12, 1983, pp. 205–235 and 323–353.

[8] David Green, 'Has Europe Solved the Problem of War ? Explaining the « Long Peace » of the post-1945 era' European Review, 2010, 18, 3, pp. 365-377.

[9] Adrian Hyde-Price, 'Normative power Europe: A Realist Critique' Journal of European Public Policy, 2006, 13, 2, pp. 217-234.

Negative effects of membership

The *Eurosceptic* approach does not miss an opportunity to point out that enlargements have sometimes had negative effects in terms of security. Thus, Václav Klaus has often equated the EU to the Soviet Union. He criticized its so-called colonialist and socialist policies, which challenge the independence of the Member States and impoverish them. All these elements, from his point of view, increase the destabilization of the States in the region and sow the seeds of potential conflicts.

On the far left, on the opposite of the political spectrum, there are recurrent criticism of the EU's actions. There are considered to have been in favor of large multinational companies at the expense of small businesses, workers and retirees. Social inequalities have increased as well as unemployment. This bad situation is a fertile ground for reactionary, nationalist and racist forces.[10] This can be observed in Hungary where fascistic people tend to play the ethnic card in Slovakia and Romania; those policies fuel regional tensions.

***Europeist* Approach**

The conception of the *Europeists* is the view developed by the supporters of the European Union. Theirs arguments are basically the following ones. First of all, they claim that the shock of the two world wars, particularly of the Second, was the main catalyst of the European unification's project.

In other words, the main driver of the European construction was an idealistic commitment to build a lasting peace, through the rejection of past wars.

In a second stage, the *Europeists* attribute the absence of war in Europe to the very existence of the EU. From their perspective, it is the qualities of the European Union that primarily explain the absence of war on the territory of the member States, including the CEECs.

[10] Philippe Marlier, 'L'Europe de la paix, cette grande illusion' Mediapart, 22 October 2012.

On a conceptual level, this school of thought has developed a sophisticated vocabulary for highlighting the EU's original contribution to peace: civil power, normative power, and soft power.

The chain of thought of the *Europeists* can be sum up broadly this way: enlargements enhance security in Europe because EU membership strengthens the following positive elements: interdependence, supranationality, law, cooperation between leaders, professionalism of the experts and economic free trade.

This is why the EU considered that one of the objectives of these enlargements was to strengthen the stability of these States by supporting the moderate and pro-Western forces in order to undermine the nostalgic circles of the communist time as well as the xenophobic nationalists.

This *Europeist* conception of the world is a kind of synthesis between Kantian liberalism, functionalism and free trade.

Kantian liberalism

Cosmopolitan political liberalism has its main origins in Immanuel Kant and his book "Perpetual peace". The German philosopher has influenced numerous thinkers. In broad terms, Kant is convinced that international peace is possible. This is an assumption, which remains disputed by many realists until today. Second, he posits that we can envisage the conditions of its completion.

According to Kant, in order to promote the coming of world peace, at least three conditions are necessary. In the first place, there is international trade (I will consider this point below).

Secondly, it is necessary to base relations between States on law, otherwise the state of war will continue. He considers the development of international law as the main factor of pacification. Because absence of a superior law - applied by a legitimate authority that is holding a monopoly on violence - is considered as one of the main triggers of war. This is why the EU, by being the main regional integration organization to have created a supranational law, is a major contributor to the pacification of the international society.

Thirdly, it is necessary to transform each State into a republic. Only such a system makes it possible the separation of the legislative power from the executive power. If the people are truly involved in the power, the latter cannot initiate a war because it should undergo the consequences. In despotic regimes in which the executive and legislative are amalgamated, the decision to start a war depends only on the goodwill of the ruler, who can disregard the interests of his people. Therefore, peace can only be built on the republicanization of States. Although not all States that compose the EU are *stricto sensu* republics, but they are constitutional monarchies.

Functionalism

Functionalism is a school of thought represented in particular by David Mitrany whose objective is to develop a peaceful international system through functional organs which transcend the nation state.[11] According to Mitrany, the solution to preserve peace is based on the following argument: instead of hoping peace through an unlikely political settlement among all the States, it is better to understand what unites these States and to exploit their relationships as opportunities for tightening interdependencies.

Interstate security arrangements are therefore considered as insufficient: be it military alliances or pacts, they do not solve the fundamental issues. This type of security is not sustainable in the long term. It is rather necessary to move towards a much wider societal security, by taking into account the needs of the people. His conception involves the establishment of cooperative mechanisms based on the organization of a variety of international public services.

[11] David Mitrany, A Working Peace System. An Argument for the Functional Development of International Organization (Quandrangle Books 1966).

This method of action offers at least three benefits. First, it reduces the omnipotence of States, it frames their sovereignty and it slows down their bellicose impulsions by promoting an entanglement of interests.

Second, it facilitates international reconciliation by avoiding political divisions. By focusing on the satisfaction of common economic and social needs, it relativizes the issue of the forms and of the political objectives.

The third advantage of the functionalist method is to initiate a transformation of the international system by betting on the role of experience and learning. The development and the success of international public services do not just strengthen the interdependencies; they also contribute to sow the seeds of a new sense of international responsibility.

Technocracy

There is also inherently to the functionalist approach, a dedication to technocracy. Technocracy is a form of government in which the place of technical experts and their methods is central for making decisions. Rather than politicians, it is intellectuals and technicians who are put in the foreground, i.e. people who are supposed to understand each other because they roughly speak a common language, whatever their origins. The advantage of technocrats compared to politicians is that they are very well trained, that they are selected according to meritocratic criteria and that they have a long-term vision, which is not the one of their next election campaign. They are also supposed to be less dependent on economic and political lobbies.

The question is whether such promotion of technocracy has the slightest effect on the issue of the establishment of peace in Europe. For sure, Jean Monnet agreed with these functionalist conceptions, even if he did not explicitly mentioned them in his written contributions.

The "Monnet method" promotes the idea of shared interest as cement "par excellence" of international cooperation. Integration has to be carried function after function, in proportion to the achievements made on the ground. The wish is that the process is afterward expanded to other areas. What neo-functionalism popularized through the expression of spill over effect.[12]

The Schuman Declaration, inspired by Monnet, was very explicit about the path European integration had to follow: "Europe will not happen all at once, or according to a single plan it will be built through concrete achievements which first create a *de facto* solidarity "(Schuman, 9 May 1950).[13]

A unique level of integration

The European Union is much more integrated and supranational than any **other** regional organization in the world. The *Europeists* emphasize that no other institution has so much called into question the formal sovereignty of States. Certainly, there are dozens of regional organizations in Europe, Africa, America, Asia and the Middle East. But none has gone as far in the direction of supranationality.[14]

Let us also note that the European Union is the organization of regional integration that has the largest number of civil servants (over 60,000), if one includes the numerous specialized agencies and the European Central Bank, (ECB). The EU is also endowed with the largest budget, nearly 140 billion euros per year.

In addition, meetings between representatives of Member States, even at subordinate levels, are daily. They often include representatives of groups of interest who are numerous, nearly 30,000. This demonstrates the extent of European integration. All these characteristics are the main features of the EU when it is compared with other organizations of regional integration.

[12] René Schwok, Théories de l'intégration européenne (Montchrestien, 2005), p. 53.

[13] Marie-Thérèse Bitsch, 'Robert Schuman et la paix' in Matériaux pour l'histoire de notre temps, 108, 2012, pp. 33-38.

[14] René Schwok, 'Peculiarities of the European Union's External Action' in Mario Telo (ed.), Globalisation, Multilateralism, Europe (Ashgate 2013), pp. 91-106.

Such a level of integration fosters peace

The most interesting issue is whether this substantial level of supranationality, this tremendous legal development, this technocracy and this high degree of interdependence have any impact on peace in Europe.

One argument is that supranationality, as its name suggests, is a form of overtaking of the nation state. According to the *Europeists*, nationalism, if excessive, is a factor of war. Therefore, if it is weakened, this reduces the likelihood of international conflicts.

Secondly, interdependence facilitates cooperation, as well as the respect of everyone's interest. Meetings between top leaders boost personal connections that may be useful to mitigate crises. Such integration prevents misunderstandings and promotes a routinization of dialogue. Interdependence creates mutual interests that would be costly to suspend by choosing to resort to strategies of conflict. All these elements reduce the risks of war.

Thirdly, technocracy is seen as a contribution to peace because it gives experts the responsibility for managing European affairs. They are expected to act with more competence, integrity and sense of the general interest than traditional politicians. In addition, they speak a common language despite their different cultural and linguistic backgrounds. This facilitates the search for effective and peaceful solutions by avoiding mutual misunderstandings. Experts often create networks, linking each other's through formal and informal connections. This has the consequence, in the case of crises between States' leaders, to limit damage and to maintain a pacifying stability.

Political integration thus contributes to peace because it creates the conditions for cooperation among States, so that they reconcile their different national goals.[15]

[15] Roger De Weck, 'Neither Reich nor Nation : another Future for the European Union' in Thomas Jansen (ed.) Reflections on European Identity (European Commission – Forward Studies Unit 1999), pp. 107-111.

Free trade is a major factor of peace

For some *Europeists*, one of the EU's merits is to enable an effective fight against protectionism by promoting free trade. According to this view, fighting protectionism is not only a factor of economic growth, but also of peace. Since the EU is the international organization that has the most developed free trade among its members, it is logical to anticipate that its impact on peace would be significant.

Free trade is a theory designed to promote development of trade through the removal of quotas, tariffs and non-tariff barriers. This also requires the dismantling of barriers on the movement of goods, services and capital. In the case of the EU, this also extends to people.

In political and economic theory, the link between peace and development of trade has a long tradition. For example, Montesquieu is known to have coined the term "soft trade".[16] He is also the author of the famous quote that is systematically reproduced by advocates of free trade: "The natural effect of trade is to bring peace."

The first point to establish is the assertion that the EU has actually more fought protectionism than any other organization of regional integration. The *Europeists* underline that no other organization has gone so far in the removal of obstacles to trade. A few other regional organizations have been successful in abolishing customs duties for their member states and some other barriers, but this has never included agricultural and fishery products.

Above all, other regional organizations have so far not included most of the so-called non-tariff barrier, i.e., harmonization of standards, certificates, testing, and access to public procurement. One should also note the importance of the substantial development in European competition law, which, as its name suggests, serves to promote competition by fighting cartel-like agreements, oligopolies or state financial support. All these elements, combined with the introduction of a supranational currency for the countries of the euro area, are the EU's main specificities in international comparison.

[16] Haig Patapan, 'Democratic international relations: Montesquieu and the theoretical foundations of democratic peace theory' Australian Journal of International Affairs, 66, 2012, pp. 313-329.

Such a high level of free trade promotes peace

The second point is whether this development of free trade has had any effect to promote peace. This issue was particularly disputed and raised countless controversies.

Opening of countries to foreign trade forces companies to be more innovative in order to remain competitive on foreign markets.

What is certain is that the EU founding fathers were convinced that protectionism is responsible for economic rivalries and as one of the factors of the beginning of wars. So Jean Monnet equated protectionism to a plague that has to be fought by all means. He saw it as one of the main triggers of war and wanted to avoid a return of Europe to the situation prior to 1939. In his conception, protectionism can be compared to a form of economic nationalism that generates hate that could lead to war. German Chancellor Konrad Adenauer and Dutch Foreign Minister Johan Willem Beyen, as well as numerous other European leaders shared this same view.

Basically, how is articulated the argument that trade development/ reduction of protectionism is a vector of peace? The chain of reasoning is broadly the following:

1. Free trade improves well-being. Its main virtue is to stimulate lower prices of products due to increased competition. The opening to foreign trade also stimulates internal growth through its impact on investment. This provides purchasing power gains for consumers, gains that outweigh the losses of some companies or sectors.

2. To the extent that foreign trade facilitates the diffusion of technology and expands the potential market for domestic enterprises, participation in international trade accelerates gains in productivity thanks to the phenomena of division of labor, learning processes and economies of scale.

3. Opening of countries to foreign trade forces companies to be more innovative in order to remain competitive on foreign markets. This results in an extension of the R & D budgets. Since intra-industry trade between industrialized countries dominates contemporary international trade, product's differentiation appears as a key driver of international trade and, so, of internal growth in innovative societies.

This means that free trade is a vector of peace for the following main reasons:

1. due to the increase in distributable surplus which is generated, it can increase the income of all social groups. If people are wealthier, they are less frustrated and less receptive to the calls by populists and warmongers.

2. Free trade is at the service of the public interest contrary to public interventions defending special interests because the latter create resentment that can be exploited in a confrontational manner.

3. Free trade corrects international inequalities. The distribution of the gains from trade among trading partners would take place spontaneously in favor of the poor as evidenced by the "paradox of Stuart Mill."[17] Compared to small and poor countries, rich countries receive a smaller share of the gains from trade because of the importance of their demand, which increases the price of the products they import. Less frustration from poor countries will cause less revanchist wars.

4. Free trade also influences peace in another way. Free trade of goods, services, capital and people also incorporates ideas and cultures. It transfers ideas, cultures, and technology that manifest themselves through the aspirations among citizens of other countries to gain access to more rights and more freedom.

[17] Alan Charles Kors, 'The Paradox of John Stuart Mill' Social Philosophy and Policy, 28, May 2011, pp. 1-18.

Solidarity

Europeists also point out the importance of the EU solidarity funds devolved mainly to the poorest regions of the new Member States. From an ideological point of view, the concept is rather of social democratic inspiration. The rationale behind this is that the wealthiest EU countries from Western Europe are massively helping the countries of Central ad Eastern Europe, as they are much poorer, unstable and fragile. In other words, even if the principles of market economy are essential to the development of these new members, it must be accompanied by a substantial effort of redistribution.

In the context of the various enlargements, the EU has developed significant financial instruments in order to strengthen economic and internal social cohesion. They help to Member States whose per capita income is less than 90% of the Community average. They place particular emphasis on infrastructure.

Currently, all of these funds represent a very impressive amount of nearly 60 billion euros per year, nearly 35% of the EU budget. These are incomparably higher than those distributed by other international solidarity mechanisms. Note that these funds are gifts and not loans such as the ones from the World Bank and other regional development banks like the European Bank for Reconstruction and Development.

Assessment

In this assessment, I first analyze the German and Russian issues. Then I focus on a few CEECs in order to assess how much EU membership contributed, or not, to their stabilization. Finally, I compare countries of Central and Eastern European who joined the EU with the ones who stayed outside.

The German issue in the context of enlargement

Since the end of communism in Central and Eastern Europe, the Federal Republic of Germany quickly regained its influence in the region. Economic indicators show that it became the main economic partner of the CEECs, as well as its first investor. In addition there are numerous exchanges of populations and a myriad of other relationships.

German economic dominance over Central and Eastern Europe was therefore inevitable. But the populations of some in those States, especially in Poland and in the Czech Republic, were keeping very bad memories of German atrocities committed in the past. It was thus necessary to prevent that Germany, the main economic power, becomes at the same time a political, a militarily as well as a cultural hegemonic power.[18]

This would have been a source of extreme tension. The solution was to decouple those different levels.[19]

In the military sphere, it is the expansion of NATO, which has been the single most substantial element of this decoupling. This organization ensures that the main military power in the region is not Germany or even another European country but a very remote state: the United States, a country that has little economic interests in Central and Eastern Europe.

In cultural matters, English language is prevailing over German, unlike the situation that was dominant at time of the Austro-Hungarian Empire.

At the political level, it is precisely the enlargement of the EU that was decisive. This institution allowed the CEECs to eventually find a place in Europe on an equal basis. By becoming members of the EU, the CEECs gained more opportunities to use communication channels independent from Germany. They could also participate in coalitions with other EU countries that avoided their unilateral and asymmetrical dependence vis-à-vis the Federal Republic.

German leaders were the first to develop this type of thinking.[20] They were aware of the burden of the past and of the risks caused by a possible return of a German colossus

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[18] Frank Schimmelfennig, 'The Community Trap: Liberal Norms, Rhetorical Action, and the Eastern Enlargement of the European Union' International Organization, 2001, 55, 1, Winter, pp. 47-80.

[19] Marcin Zaborowski, 'More than simply Expanding Markets: Germany and EU Enlargement in Helene Sjursen (ed.) Questioning EU Enlargement : Europe in Search of Identity (Routledge 2006), pp. 104-120.

[20] Philip Gordon, 'La normalisation de la politique étrangère de l'Allemagne' Politique étrangère, 1994, 59, 2, pp. 497-516.

in Mitteleuropa. They therefore put the equation that a EU enlargement to the East was a *sine qua non* condition for a peaceful comeback of the CEECs in the international society and therefore for promoting stability in Europe.

The Russian question in the context of enlargement

The relationship with Russia was also one of the motivations of enlargement to the CEECs. EU membership was one of the methods used by the leaders of these States to get rid of the influence of this big neighbor. EU Member States were sharing the same objective: enlargement was seen as an instrument to move away the Russian potential threat hundred kilometers to the East.

In the 1990s and until the beginning of the 2000s, the discourse of the EU and CEECs' leaders focused primarily on the instability and on the decadence of Russia (cf., President Boris Yeltsin, the economic crisis and Russian mafia). In this context, EU membership was presented as constituting a bulwark against the spread of the deliquescence of Russia and therefore as a security for the entire Old Continent.

After President Putin strengthened his power in the Kremlin, it is rather the overtones of Russian imperialism that awakened concerns among the CEECs, particularly among those that have a common border with the Russian Federation.

In the 1990s and until the beginning of the 2000s, the discourse focused primarily on the instability and on the decadence of Russia

The argument became then as follows. Thanks to the enlargement of the EU to the CEECs, imperialist Russia will be deterred from attacking a CEEC because it would run the risk of a confrontation with all Western countries. Moscow would even avoid putting pressure on one country for fear of attracting not only military but also political and economic reprisals from Western Europe.

Poland

Poland is the largest state among the CEE countries in terms of population (38.5 million). Strong nationalist pulses related to its geographical position between Germany and Russia and its tragic history traversed this state.

In the early 1990s, at the end of Communism, per capita income was lower than in the Czech Republic, Slovakia and Hungary. The percentage of farmers in the active population was particularly significant (over 30%). Many people had to emigrate in order to find a job, mainly in Germany and in the UK. In addition, the government administered a "shock therapy" aimed at liberalizing the economy. At that time, it generated a severe recession which enhanced social inequality and increased impoverishment.

Such a situation could have been a fertile ground for the development of extremist political parties, either of nostalgics of communism or of proponents of radical solutions.

Nationalist forces benefited from such favorable circumstances to come to power. This was the case of the twin brothers Lech and Jaroslaw Kaczynski, who were respectively President and Prime Minister of Poland, sometimes at the same time in 2006-2007. During their electoral campaign, they did not hesitate to come closer to anti-European religious parties.

If Poland managed to maintain a moderate policy in such circumstances, it is in part due to its membership of the EU.[21] Indeed, this country had already introduced many reforms in order to adopt the "EU acquis" before its accession in 2004. It would have been very costly to unravel this entire legislative skein. Above all, Poland had become extremely dependent on the Solidarity Fund of the European Union. They currently amount to almost 10 billion euros per year. This gives an idea of their importance. This country is now the largest recipient of EU funds for cohesion, even ahead of Spain. Such aid would have been frozen in case of bad conduct on the part of Poland.

Add to this that Polish farmers, a large reservoir of voters for populist conservatives and nationalists parties like *Law and Justice* of the Kaczyński brothers, had been

[21] Elizabeth Pond, 'Poland: The Success of European Integration' World Policy Blog, 11 October 2011.

converted to the European cause. Thus, from 2004 onwards, Polish farmers began to benefit from substantial EU farm subsidies that were a boon for this generally poor population. In addition, they began to profit from the dismantling of agricultural protectionism in the EU Western European States. This allowed them to export in these countries with high purchasing power. All those elements explain why the nationalist parties have thought twice before engaging in anti-European activities because it could have costed them an important loss of voters.

Slovakia

In Slovakia, the rise of the nationalist movement had already occurred in the 1990s during the period of the government of Vladimír Mečiar. He had been elected prime minister in November 1994. It is during this period that he introduced the most controversial and authoritarian aspects of his policy. They had the effect of isolating Slovakia from the rest of Europe and to delay its integration into NATO until 2004, unlike its Czech neighbor that already joined the Alliance in 1999.

Slovakia was admittedly not a EU member during the Mečiar era, but accession was already its objective. The idea that all other Central European States would soon join the EU, with the exception of Slovakia, convinced Bratislava to avoid the imposition of anti-liberal legislations. In 1998, Mečiar had to leave as head of government and his successors finally set course towards European integration. So much so that Slovakia was in 2009 the first State among the CEE countries to adopt the euro. This was mainly due to political reasons in order to strengthen its European integration and to be placed in the core of the EU.[22]

[22] Milan Nič, Marek Slobodník, and Michal Šimečka, Slovakia in the EU: An Unexpected Success Story? (Deutsche Gesellschaft für Auswärtige Politik 2014).

Hungary

Hungary is another emblematic case. Since 2010, the *Fidesz* party led by Viktor Orbán is leading the government with a very large support. Orbán had already been prime minister between 1998 and 2002 and then appeared as a moderate and pro-European liberal. But in recent years, his discourse was radicalized in a much more nationalist, conservative and anti-liberal direction.

His party and Orbán himself sometimes came close to the radical *Jobbik* party. This political formation obtained more than 20% of the vote in parliamentary elections in 2014. *Jobbik* expresses nostalgia of the period of dictatorship of Miklós Horthy. It makes so-called cosmopolitanism responsible of all the problems and develops a latent anti-Semitism. It is particularly violent in relation to the Roma minority. *Jobbik* would like to return to the borders of Greater Hungary of before the Treaty of Trianon (1920) and is unfavorable to European integration.

It happened that the Orbán government adopted some of *Jobbik*'s views such as the one on the Hungarian diaspora. It passed a constitutional amendment on dual citizenship for Hungarian-speaking minorities living outside the national territory. This obviously created tensions with Slovakia and Romania; needless to say that it is dangerous for international security.

This government also introduced other legislation such as a media control law that was widely criticized by several EU countries and even by the Organization for Security and Co-operation in Europe (OSCE).

Nationalist, authoritarian and xenophobic tendencies in Hungary could have been even worse if the country was not a EU member.[23] They could have caused serious international difficulties with its neighbors. The fact that the Orbán government has moderated his program is to be credited to its membership of the EU and its fear of losing its benefits if he persisted in a way too extreme.

[23] Krisztián Ungváry, Hungary and the European Union 1989-2014 – a Success Story? (Heinrich Böll Stiftung, 2014).

The Russian-speaking minorities in the Baltic States

Improving the lot of Russian-speaking minorities in the Baltic countries is another element that has underpinned the issue of EU enlargement, as it could have been a potentially destabilizing issue. Estonia, Latvia and Lithuania tended to discriminate against people of Russian origin and to deny them access to citizenship because they were sometimes considered as a kind of settlers who are unable to assimilate in the Baltic States. In a context of independence after years of Soviet/Russian occupation, the climate was little inclined to tolerance.

Such Baltic behavior is potentially dangerous because the Kremlin might be tempted to go to war in order to rescue its fellow citizens. Moreover, in the terminology of Moscow, those are Russians and not Russian-speaking minorities; this expression further underlines its self-proclaimed legitimacy to worry about their fate.

Therefore, to avoid a Russian military intervention, the EU has set as a condition for entry of the three Baltic countries in the EU that they waive their discriminatory policies against their minorities.[24] And even after they had become EU members, the European Commission has ensured that those minority populations continue to be well treated in order to avoid conflict with Moscow.[25]

Geographical comparison

Another striking element is the difference of situation between the countries of Eastern European CEECs belonging to the EU and the ones staying outside this organization. The latter are all experiencing bad, if not tragic situations. The most emblematic case is that of Ukraine which embodies all the problems by himself. The *per capita* income in that State has remained very low and is even decreasing. This country works so poorly that one

[24] Michael Johns 'Do As I Say, Not As I Do`: The European Union, Eastern Europe and Minority Rights' East European Politics and Societies, 2003, 17, 4, pp. 682–699.

[25] Jean-Bernard Adrey, 'Minority Language Rights Before and After the 2004 EU Enlargement: The Copenhagen Criteria in the Baltic States' Journal of Multilingual and Multicultural Development, 2005, 26, 5, pp. 453-468.

sometimes uses the term of "failed state" to describe it. The political class is largely corrupt and elections are often held at the limit of legality. More dramatically, this country was carved up of a part of its territory by Russia (Crimea). And separatist rebels supported by the Kremlin are triggering a civil war.

The situation in Georgia is hardly more encouraging and the country has also gone through wars. Separatists also supported by Moscow occupy twenty per cent of its territory (Abkhazia and South Ossetia).

Azerbaijan also lost part of its land following a conflict that has left hundreds of thousands of victims and refugees. Armenia now occupies not only Nagorno-Karabakh but also a large region called the Lachin corridor. Many experts expect a resumption of hostilities in the near future.

Belarus faces a particularly harsh dictatorship and has a low level of development. It is the only country that has not been accepted in the Council of Europe because of the ruthlessness of its political regime and its failure to respect democratic criteria and human rights.

It is also worth mentioning Russia. This country is experiencing an authoritarian drift that challenges some progress made in the 1990s in terms of freedom of expression and respect of human rights. The Kremlin has continued to solve some of its internal and external problems by violence. In the 1990s, a terrible crackdown had befallen on the Chechen separatists and there were hundreds of thousands of deaths. This resulted in massive displacement of population and in the destruction of cities such as the capital Grozny. As already mentioned, in the 2000s, the regime of President Putin was characterized by its aggressive policies vis-à-vis Georgia and Ukraine, not hesitating to take the risk of triggering military conflicts to achieve its objectives.

Finally, another case is emblematic. It is the one of the predominantly Romanian-speaking Republic of Moldova. This State was also cut up a portion of its land (approx. 10%), following a secession organized by Russian-speaking people supported by Moscow (Transnistria).

It is also interesting to compare the economic results of the two Romanian-speaking countries: Moldova and Romania. In 1990, the per capita income of Moldovans was $ 917 and it passed to only $ 2,077 in 2012 (http://fr.kushnirs.org/.[26] For cons, the Romanians stood at $ 1,750 in 1990 and reached $ 7770% in 2012. In the first case, income had doubled, and in the second, it had more than quadrupled over the same period. It is likely that if Moldova had been a EU member such as Romania, its economic results would have been much better, people would have been more satisfied and maybe the Transnistrian rebels would have been more inclined to find a compromise to this conflict.

Conclusion

Europeist and *Eurosceptic* approaches bear some relevance. About the relatively good situation in Central and Eastern Europe, the *Eurosceptics* such as Vaklav Klaus are right to stress that the role of EU membership should not be overemphasized. Other elements were actually at work to achieve this result.

It is also appropriate to mention that the CEECs made their accurate political and economic choices before they joined the EU. It is also likely that many of them would have reached some success without joining the EU.

It is also indubitable that the Soviet withdrawal, the end of communism and the German moderation favored the peaceful climate that actually prevails in Central and Eastern Europe. Added to this is that the American presence and NATO expansion also contributed to the overall stabilization.

The *Europeist* approach nevertheless develops more relevant arguments. Membership in the EU had indeed a beneficial effect in order to prevent excesses with adverse consequences.

Imagine how much German economic hegemony in Central and Eastern European could have triggered instability if the CEECs did not join the European Union (and also NATO) as rebalancing instruments. Imagine also in the context of the annexations of

[26] Ivan Kushnir's research : http://fr.kushnirs.org/macroeconomie/gdp/gdp_romania.html#p1_2

Crimea by Russia and the war in Ukraine what would be today the level of fear in the Baltic States, in Poland and in some other Eastern European countries if they did not have their partnership with other European countries from the Western part of the continent.

Examples of Poland, Slovakia, Hungary and the Baltic countries also demonstrate that their status as a member State allowed them to depart from temptations that could have had negative consequences for the international environment. EU membership alone does not explain the good results of these countries, but it helps to illuminate why they have been consolidated.

EU accession actually offered a direction and a meaning to countries that were just emerging from periods of dictatorship, which were also economically underdeveloped, politically fragile and tempted by populist solutions.

A comparison of the current situation of the Central and Eastern European countries with that of the States that have not been able join the EU is significant.

The European Union has been instrumental in supporting the moderate forces in the CEECs, while making clear to the extremist groups the price to pay for an exit from the European path.

A comparison of the current situation of the Central and Eastern European countries with that of the States that have not been able join the EU is significant. One has only to compare the situation in Poland with the one of Ukraine, or that of Romania with the one of Moldova.

All in all, the unique contribution of the European Union is to confer an exceptional level of quality to the concept of peace in Central and Eastern Europe. This is not just about a cold peace, a kind of cease-fire, but much more about a firm and sustainable peace. It is here that one can claim that the war in Europe is less likely thanks to the EU, although it is still imaginable and unfortunately not impossible.

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Czech Privatisation 25 Years Later

▸ Petr Bystron

The Czechoslovak mass privatisation seems to have been relatively successful, as it quickly taught people to react to market impulses in a way that is typical in a market economy. The political goal of privatisation, creating a large group of shareholders, was successfully fulfilled.

Over the last 25 years, the subject of the transformation has held predominantly negative associations for the public, despite the fact the period has seen an unprecedented growth in living standards as the Czech economy has rapidly moved closer to those of Europe's most advanced countries.

Privatisation did not go smoothly in any country of central and Eastern Europe. Establishing property rights is a complicated process. In Poland the privatisation of state enterprises was not a priority of government policy for a long time. Czech privatisation was part of an entire transformation process. Compared to any privatisation carried out in the West it was unprecedented in extent. However, it differed from standard privatisation in terms of its aim, which was not the immediate success of every individual enterprise.

Was Czech privatisation successful or unsuccessful? In western economies the term "privatisation" generally refers to the market sale of previously nationalised companies following careful analysis of the business's economic value. First of all, the scope of the privatisation issue faced by governments after the fall of communism was much greater. In contrast, in Czechoslovakia there were 4864 state-owned enterprises at the end of the 1980s.

The costs for large-scale privatisation are enormous, ranging around the level of CZK 1 trillion, depending on the model. The higher cost of large-scale privatisation may be a reflection of the lower flexibility of large companies compared to smaller businesses, as well as the overall lower efficiency of management and the associated loss rate of those companies that have not yet been privatised, and to a certain extent also the political layer of large-scale privatisation.

The standard form of privatisation in which the given business benefits from new knowhow, new sales opportunities, new markets, funding or new management "would in reality have taken decades", explains Pavel Rychetský, Chief Justice of the Constitutional Court of the Czech Republic. With this in mind, Czechs opted for a radical and fast privatisation of their economy.

The 3500 poorly managed large firms that belonged to the state, including banks, "had to be put into the hands of people who knew how to manage them as quickly as possible", explains Karel Havlíček, Chairman of the Association of Small to Medium-Sized Enterprises. These businesses were in a catastrophic and outdated condition. The nineties were a very complicated time during which many things needed to be done, not just the remediation of 40 years of socialist economy.

In the case of many enterprises serving as examples of the failures of privatisation, the identification of the first owner did indeed fail. However, in further waves of "creative destruction" assets were allocated to owners that today create value and employ thousands. The great successes of the Czech privatisation – but also the most controversial – comprise PPF (První privatizační fond) and MUS (Mostecká uhelná společnost), among others.

Some Czech businesses were offered for sale to foreign investors, but they did not rush in. The enterprises that promised excellent opportunities for profits were purchased by foreign investors. Companies with average attraction were taken over by domestic strategic investors, on credit.

Because of enterprises were owned by the State, the quasi-entrepreneurial class had only limited capital in the form of own savings. In addition to bank credit, managers could also choose an alternative route: takeovers of companies using loans from the companies themselves. A loan provided by an owner to new buyers is an entirely standard instrument in connection with the sale of companies and cannot be rejected wholeheartedly as an unacceptable approach such a conflict of interest between managers and the owner always has to be assessed on a case-by-case basis and not rejected outright.

Managerial takeovers were a natural manifestation of efforts to create investment capital where it was necessary and where it was also missing. Through their innovation potential and investment capital, domestic entrepreneurs/owners were to create the foundation for new economic growth after the transformation. The role played by entrepreneurs was not limited to the economy; it also had substantial consequences for society as a whole. The creation of an entrepreneurial class was to help stabilise the new social system.

The Czech Privatization: Disappointment Inappropriate

Privatisation

The short-term focus of the initial phase of reforms was on price liberalisation and macroeconomic stabilisation. However, the mid- and long-term goal of the reforms consisted of dismantling the state ownership of the enterprises and banks.

As indicated decades ago by the free market classical writers, Friedrich August von Hayek and Ludwig von Mises, the supremacy of the capitalism over any organised economic system is due to decentralised interests and motivations of multiple economic actors.

	Private sector share of GDP mid-2002 (EBRD estim.)	**Large-scale privat-isation***	**Small-scale privat-isation***	**Gov. & enter-prise restruc-turing***	**Overall per-formance**
Czech Republic	80%	4	4+	3+	85%
Estonia	80%	4	4+	3+	85%
Hungary	80%	4	4+	3+	85%
Slovak Republic	80%	4	4+	3	83%
Lithuania	75%	4-	4+	3	79%
Poland	75%	3+	4+	3+	79%
Latvia	70%	3+	4+	3	75%
Slovenia	65%	3	4+	3	71%
Bulgaria	75%	4-	4-	3-	71%
Croatia	60%	3+	4+	3-	70%
Russia	70%	3+	4	2+	68%
Armenia	70%	3+	4-	2+	65%

	Private sector share of GDP mid-2002 (EBRD estim.)	**Large-scale privat-isation***	**Small-scale privat-isation***	**Gov. & enter-prise restruc-turing***	**Overall per-formance**
Georgia	65%	3+	4	2	64%
FYR Macedonia	60%	3	4	2+	63%
Kazakhstan	65%	3	4	2	61%
Kyrgyz Republic	65%	3	4	2	61%
Ukraine	65%	3	4	2	61%
Romania	65%	3+	4-	2	61%
Albania	75%	2+	4	2	59%
Azerbaijan	60%	2	4-	2+	52%
Moldova	50%	3	3+	2-	50%
Tajikistan	50%	2+	4-	2-	47%
Bosnia and Herz.	50%	2+	3	2	45%
Serbia and Mont.	45%	2+	3	2	44%
Uzbekistan	45%	3-	3	2-	44%
Belarus	25%	1	2+	1	16%
Turkmenistan	25%	1	2	1	14%
Average	63%	3	4-	2+	61%

▸ **max = 4+ / min = 1 / Source: EBRD, 2003*

While the not-so-neat impression of the decentralised economic reality earned labels such as “creative destruction”, in fact it turned out that it enabled to crowdsource the crucial information about scarcities of goods, services and economic opportunities in far most efficient way the human race discovered so far.

In 2003, EBRD evaluated the status quo of the privatisation and enterprise restructuring behind the Iron Curtain. The fastest pace of de-etatisation of economic units was reported by the Central & Eastern European countries, with Czech Republic, Estonia, Hungary and Slovac Republic faring as the best-performing countries.

Not surprisingly, the restructuring of the businesses towards competitiveness and efficiency is closely linked to the extent of the private sphere. In other words, there is no restructuring without privatisation. The restructuring increased the efficiency of the production, the quality of the product and both the profitability and taxation. The speed of the transition mattered – to consumers, businesses, employees and to the state budget.

In the Czech Republic

"The aim of voucher privatization was that the state did not sell their [the citizens'] property for a buck. ... Many companies that we inherited from communism was rusty. About these companies had no great interest." ▸ Václav Klaus, the former prime minister and president of the Czech Republic and the chief architect of the Czech transition

We have in a very short time managed to fulfill the main task of finding the first owner. If you find the first private owner, it's up to him to deal with the assets. Because he is best fit to this responsibility. He says to himself either to sell or alternatively to invest in the asset. But now it's his business. ▸ Vladimir Tomšík, economist and currently the Vice-Governor of the Czech National Bank

Let us jump back in time a couple of decades and recall the mood and expectations of the people living in this region, who opposed to Communist system. At that time, they felt it a hopeless daydream that within the foreseeable future their countries would become democratic market economies. Today however, though this has become a reality, many are disappointed and bitter. ▸ Janos Kornai, the Central and Eastern Europe prominent economist of the central planning and economic transition

As the EBRD privatisation indicators suggest, Czech Republic fared at the top of the transition countries of the former Soviet eastern bloc. However, after the applauded reforms became reality, many Czechs are "disappointed and bitter", as Janos Kornai put it.

There are several qualifications raised against privatization in the Czech Republic: the privatisation revenues were too small, the transformation costs were too high and there were many privatisation scandals and the overall level of privatization corruption and crime was high.

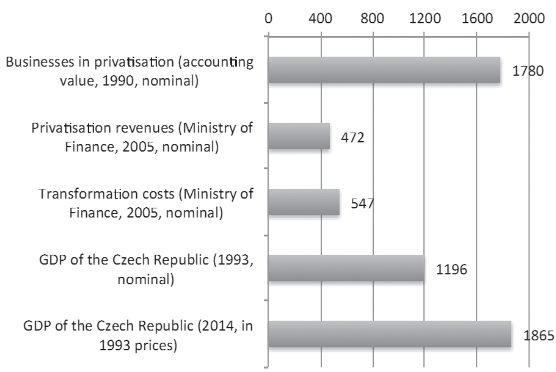
According to the Ministry of Finance of the Czech Republic, the transformation revenues, almost entirely consisting of the privatisation revenues, amounted to less than 500 billion CZK. At the same time, the book value of the businesses in the privatisation as of 1990 was nearly 1.800 billion CZK.

High privatisation revenues were never among the principal goals of the Czech transition. Why? The privatisation revenue is the principal goal of privatising an individual company in a developed market economy – such as was the case in M. Thatcher privatisation of the state owned British coal companies in 1980's.

In transition countries the state was initially the principal owner of the majority of businesses. In this case, the dynamic considerations of the macroeconomic growth track is more important. Privatisation revenues are not the main goal of the privatisation.

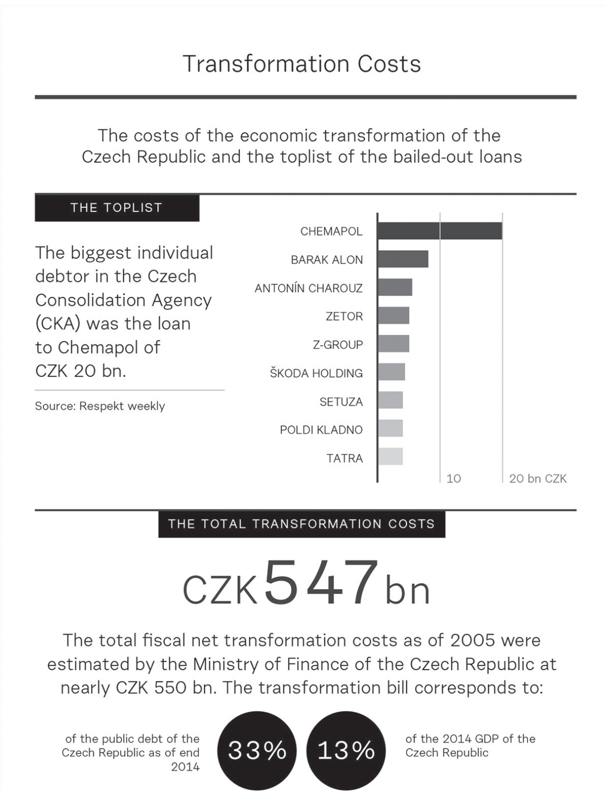
Despite lack of the Czech capital to buy the businesses from the state, the designers of the privatisation decided to transfer part of the the state owned assets to the Czech citizens, instead of selling it to multinational investors "for a buck". That is why about 30 % of the book value was transferred through the voucher privatisation scheme to the Czech citizens without any financial compensation to the state.

The small businesses and some bigger companies were auctioned. It was noted, that in a number of cases the high receipt of the state resulted in the financial difficulties of the new owner. The company's profits were chanelled to repayment of the privatisation loan instead of investment in the technology, and eventually, the company went bankrupt (Mejstrik, 1999).

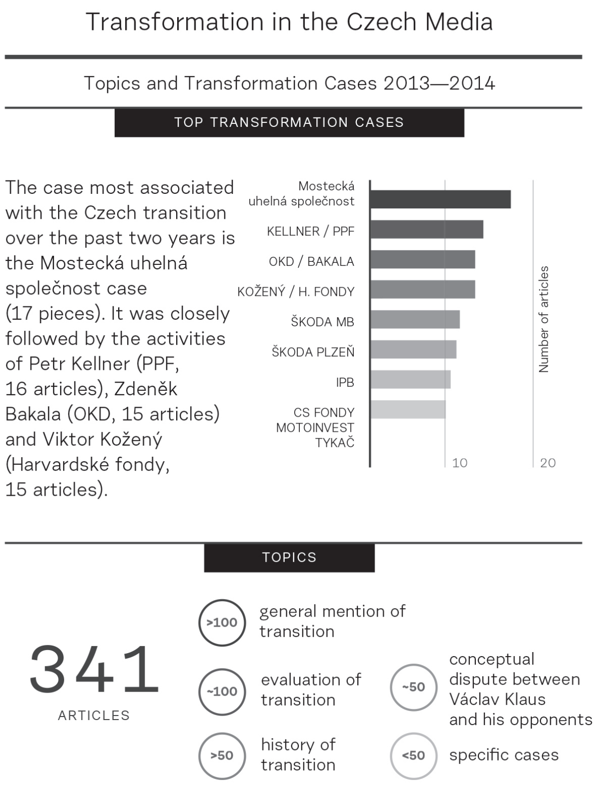


The disappointment from the low level of privatisation revenues is relativized when put into a dynamic perspective. Between 1993 and 2014, the real domestic product of the Czech Republic rose by more than a half. The increase of the GDP would successfully cover the whole transformation costs and would cover the deficiency between the transformation costs and the privatization revenues nine times. The center of gravity of the privatisation "revenues" can be found in the purses of shareholders and employees of the privatised and sucessfully restructured companies.

In the transition country without previous capital accumulation, the one principle source of finance were the banks with forced savings of the Czech citizens. In the Czech republic, the Government decided to retain control over the big banks until the end of the transition decade. The transformation costs reflect to a large extent the so called "qualiffied loans" granted to finance the purchase of privatised companies, the purchase of the new technology or to cover their operation needs.



The bad loans were carved out off the banks balance sheets and transferred to the special Government agency – the Czech Consolidation Agency (CKA). These loans were covered in cash by the state to the banks. The listing of a company in the CKA balance sheet is a principle indicator that the restructuring of the company failed. However, many of these companies' assets continue to be productive until today with the new owner and a new brand, as in the case of the carmaker Tatra, the train producer Skoda or the steelworks Poldi Kladno.



Kursa D., The Czech Transition in the Eyes of Today's Media; IN: Munzi, T., Slaný, M. (eds.) Quarter-Century: Czech Way to the Market Economy. Prague: Czech Enterprise Institute, 2015.

The reflection of the transformation and privatisation is an excellent example of how media picking of negative news bias the public opinion. Kursa 2015 analysed the occurence of "privatisation cases" in the Czech media over 24 months between January 2014 and December 2015. As a matter of fact, a number of the privatisation cases refer to a substantial entry in the CKA ballance sheet or are synonymous to the fraud against the minority shareholders. However, that is not the case for the three “cases” with the highest mention-rate. Neither MUS nor PPF nor OKD left behind any unpaid loans and made any record in the CKA.

Czech Privatisation in the Book Value

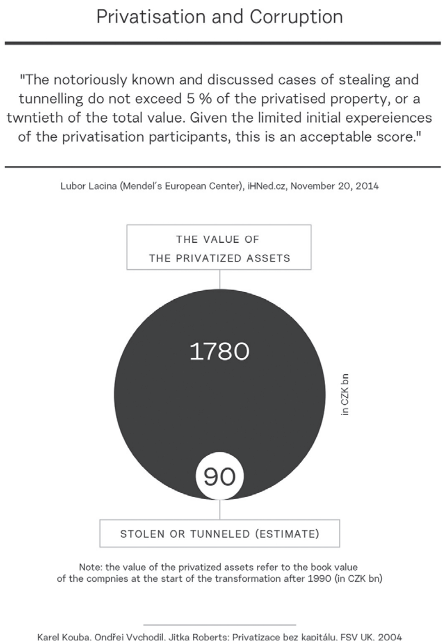
Privatisation phase	**Book value (bil. CZK)**
Small privatisation – small businesses such as shops and restaurants	30
Transfer to municipalities	350
Restitutions – transfers back to the owners (their heirs) as of 1948	200
Large privatisation – companies of tens to several tousands employees	1200
Total	**1780 bil. CZK**

▸ *Source: Kouba, Vychodil, Roberts, 2004*

In the privatisation, about 1.200 big companies along with around 22.000 small business units were transfered to the private owners. According to the sober estimates, the stolen assets and tunelled companies do not account for more than 5 % of the value privatised.

The peaceful, smooth and fast privatisation of the entire Czech economy is the key explanation of the rapid growth of the Czech welfare in the last 25 years. Even the critical voices admit in retrospect that an ideal piecemeal privatisation of the thousands of economic units – from the electric power behemoth to the hairdresser’s around the corner – would take years or decades accompanied by economic stragnation.

The Czech author, Milan Kundera, once put it: “The future is always mightier than the present. It will pass judgement on us, of course. And without any competence.” The disappointment with the Czech privatization and transformation is as understandable and expectable as it is inappropriate.



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