

LESSONS FROM TRANSITION IN EASTERN EUROPE.  
A PROPERTY-RIGHT INTERPRETATION

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Abstract

This paper questions the neo-classical and gradualist views to transition in Eastern Europe, and suggests a property-right approach based on the economics of institutions and the public-choice literature. This allows us to make a clear and most important distinction between reform and transition: only the latter is a serious attempt to change the existing property rights system. It is argued that the chances for successful transition depend critically on the public-choice equilibria prevailing at the beginning of the transition process, and on the sources of legitimacy for the ruling coalition(s). This conceptual framework is then applied to analyze the case of the former Soviet Union and of three different categories of East-European countries.

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**LESSONS FROM TRANSITION IN EASTERN EUROPE.  
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(Enrico Colombatto and Jonathan R. Macey)

1. A critical view of transition economics

Attempts to transform the command economies of the former Soviet bloc into more or less free market systems have not always met unmitigated success. In fact, the opposite seems to be a closer representation of reality. Although it is not difficult to perceive that some economies perform relatively well (as in the case of the Czech Republic, for instance), while others are in a rather chaotic situation (as Belarus), it is not at all clear why some countries did well and others very poorly. Even the future of Russia presents plenty of ambiguities.

The traditional approaches to the economics of transition are well known. According to the neo-classical tenet, transition means privatization, price liberalization and a balanced budget, plus free trade and a fully convertible currency. The virtues of this stereotype in a frictionless, zero-transaction-cost world are beyond dispute. Nirvana economies always work, by definition. It is indeed acknowledged that the adjustment process on the way to Nirvana involves some costs and that, as a consequence, national income may drop in the short run. But this is usually considered an affordable price to pay in order to achieve "optimality". In other words, transaction costs are not looked upon as part of the transition problems, but rather as an unpleasant temporary by-product. In that perspective, neo-classical economists therefore maintain that transition should be fast (shock therapy was the catchword fashionable until recently), so that the "painful" period - i.e. the time during which living standards would fall - stays short, and the desirable consequences of a successful transition process remain visible to everybody almost from the start.

In this light, intervention by international agencies such as the World Bank and the IMF is most welcome. Aid (support for transition programmes) would provide compensation during the period of hardship, and thus credibility to both the transition process and the transition leaders<sup>1</sup>. In this light,

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<sup>1</sup> The fact that most programmes offered by the Western World and by international agencies go to governments, rather than private agents, may be

failure in transition originates from the technical inability or political unwillingness (on the part of totalitarian leaders) to carry out these policies in full, that is with adequate speed and determination.

In partial contrast with the neo-classical stand, gradualists take the view that fast transition towards a free-market framework is too painful to be acceptable in one single blow. Put differently, transaction costs do enter the inter-temporal social utility function of the policy maker. Thus, although their long-run objectives are in many respects similar to the neo-classical prescription, gradualists favour a much more diluted passage from planning to market, to be supervised by government intervention (soft planning) in the pursuit of the public interest, which implies - among other things - low unemployment and "equitable" distribution of income. Once again, the outside world - and international agencies in particular - may play a useful role. The hardship of transition can be softened by foreign resources, and thus policy makers can proceed at a faster pace than it would have been the case otherwise.

The fundamental shortcoming of these traditional approaches is that they are not really concerned with transition, but rather with the methodology of transition<sup>2</sup>. As such, the traditional approaches can clarify the positive economics of success and failure. But are at pains in explaining why in certain countries transition has been easier than in others, why it has led to a wide variety of different results, or why in some instances the collapse of the communist regimes has had virtually no consequence on transition and economic performance<sup>3</sup>.

From another point of view, one may observe that in a traditional perspective the agents who lead the transition process are supposed to behave

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explained by the fact that the attempt to strengthen the incumbent political leadership ranks very high in the donors' priority agendas.

The notion that transition had to be fast, so that the interest groups opposing transition could not become strong enough to stop or even reverse the process has been a later development of the neo-classical literature on transition. Although it was raised by a number of orthodox economists, it does not fit the orthodox idea whereby policy makers pursue the public interest, and there is nothing coalitions can do in order to persuade politicians and policy makers not do so.

<sup>2</sup> See also Winiecki (1992).

<sup>3</sup> Actually, in some cases where transition did not take place economic performance deteriorated after the collapse of the communist regime.

according to a public-interest hypothesis. In the neo-classical framework the technocrat is allegedly led by the long-term public interest of the country; whereas in a gradualist context politicians care about smoothness and stability, in order to avoid chaos and not to jeopardize the chances for transition. However, as argued in McCormick-Tollison (1981) and, more recently, in Colombatto-Macey (1996), this is in marked contrast with reality. Policy making does not follow a public-interest criterion, but rather a public-choice pattern.

Finally, the traditional views fail to explain why the old system collapsed when it collapsed, and not earlier (or later). The standard answer refers to "poor economic performance", which aroused popular protest and favoured change; but is not fully satisfactory for various reasons. In Eastern Europe public opinion had little opportunities to make its discontent manifest, and even less opportunities to generate a change in the leadership. Indeed, very substantial layers of the population were not intolerably unhappy about their living standards, as the survival of strong former-Communist parties witnesses, all of them with a substantial "popular" basis<sup>4</sup>.

## 2. Property rights, reforms and transition

The property-right approach suggested in this article differs from orthodoxy in that it draws heavily upon the economics of institutions and the public-choice literature. As will be shown in the following pages, it provides a more encompassing set of answers, by focussing on the origins of the agents' behaviour in a dying command economy, and on the role of such agents when the existing property rights system is no longer viable. From this standpoint, in some cases transition turns out to display features typical of a path-dependent process, and can be analyzed through the institutional-economics paradigm. In others, a public-choice approach seems more promising, for it considers transition as a function of the bargaining conditions under which old interest groups manage to maintain power, or new groups come to the surface at the expense of others.

In both cases, however, the property-right approach allows one to draw a

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<sup>4</sup> Actually, in many East-European countries economic performance at the end of the Eighties was not significantly worse than in earlier periods. As matter of fact, people in Eastern Europe often had very confused ideas (and preferences) about the options available (including "capitalism") - see Shiller (1991) and Pejovich (1993, p.74).

distinct line between reform and transition, thereby clearing the ground from some confusion<sup>5</sup>. More generally, the rejection of the public-interest argument on how to create Nirvana economies in the aftermath of central planning makes it possible to provide more acceptable answers to the questions raised above - on the relevance of the timing of transition attempts in Eastern Europe, as well as on their mixed success.

Transition in four groups of Eastern European economies will be discussed in sections 3. and 4.. As regards "reforms", this term usually refers to the rather frequent efforts to change some features of the system. Such attempts have been developed in the Soviet bloc from the mid-Fifties. However, they have always generated poor results, as the post-War economic performance of these countries has witnessed. This is not surprising. In fact, reforms in a command economy never implied a major change in the existing property rights system. Rather, they were designed to alter the set of rewards assigned to each of the interest groups in the ruling coalition. Although the balance of power within the coalition was indeed at stake, the composition and legitimacy of the rulers were never in doubt, so that the rent-seeking strategies and instruments were left unscathed. Put differently, the economics of reform was about which group would benefit most from the rent-seeking activities worth fighting for, given the existing criteria for property rights assignments. The criteria themselves always remained those typical of a command economy. Transactions costs for the economy as a whole therefore stayed high, and information remained very scarce. On these grounds, economic performance could not possibly improve significantly.

Transition is of course different from reform. It refers to what happens in the period during which one country moves from one property rights pattern to another, not to the attempts to improve (reform) the existing property rights system<sup>6</sup>. If successful, transition entails a new and far more effective assignment of property rights; thus, a drastic reduction in transaction and information costs. Production and consumption become more efficient. The

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<sup>5</sup> For instance, reforms in the Soviet bloc during the Seventies had stimulated a fairly important literature on "Convergence", whereby it was believed that repeated rounds of reforms would have brought the working of the typical command economy close to that of a typical West-European mixed economy.

<sup>6</sup> In fact, attempts to reform the economy appear to be an appealing tool which the incumbent politician makes use of in order to avoid transition.

potential for growth can be exploited and the catch-up process may follow its course.

In this light, the real question therefore relates to the variables which determine success or failure in transition. To a large extent, the property-right approach traces them back to the moment transition is set into motion, and to the public-choice equilibria prevailing at that moment. That is, transition is not only about teaching the technical arrangements required to keep a free- (or mixed-) economy going. Much more relevant is to understand why pressure in favour of institutional change has built up in those countries. And whether such pressure could and can be expected to lead to a new system of property rights, given the existing cultural and historical heritage, which of course includes the informal institutional framework in place. In other words, successful transition does require that some institutional constraints be met<sup>7</sup>. But the crucial question is whether such constraints are acceptable in a country starting the transition process. If not, transition is doomed to failure, and myopic or post-myopic behavior prevails<sup>8</sup>.

The recent experience in the former Soviet-bloc area offers numerous interesting insights in this respect, and also helps explain to what extent transition was carried out from above, i.e. by easy-to-identify interest groups; and to which extent it was driven from below, i.e. by the public at large. As will be analyzed shortly, this is often a critical issue in order to assess the features of a transition process. For transition from above is successful only when the new coalitions draw legitimacy to authority from an explicit commitment to growth and to more efficient property rights assignments<sup>9</sup>. Constitutional law making will then be aimed at increasing the transaction costs of rent-seeking; it will enhance information and at the same time reduce the cost of entry (and exit) into (from) the political arena.

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<sup>7</sup> See Colombatto and Macey (1994).

<sup>8</sup> A myopic behaviour is one where the autocrat tries to maximize rent-seeking at the expense of the public interest within a short period of time. A post-myopic framework is one where the political life of the autocrat extends beyond the expected horizon.

<sup>9</sup> It may be appropriate to observe that this successful linkage between the source of legitimacy - i.e. commitment to growth - and economic performance is not new. Campos and Root (1996) analyze the case for a number of South-East Asian countries.

When coming from below, pressure always originates from a desire for a higher level of income and individual well-being at large. It seldom supports specific and consistent projects for constitutional change. Thus, it may not be enough to solve the contractual problems among interest groups. The existing institutions tend to remain unaffected, and the rules of the game as regards ordinary law making are not altered to a substantial extent. If the desire for better economic performance is accompanied by a generalized inability to abandon the old system, then constitutional law-making becomes fairly similar to ordinary law-making. The cost of rent-seeking is actually lowered, DUP activities and uncertainty increase, while economic activities decline. Chaos tends to be the ultimate outcome, as we have recently explained in another paper (1994). But if pressure for better economic performance goes hand in hand with the widespread and explicit acceptance of new criteria for property rights assignments, then transition stands a good probability of success.

### 3. Transition in the former Soviet Union

The collapse of the former USSR dominates the Eastern-European experience, because that system survived some seventy years; because, after WWII, it became typical of many countries of the world; and because its recent fall ignited dramatic consequences in the rest of the so-called Soviet bloc.

#### *3.1 Why did the Soviet economy collapse?*

There are two explanations for the peaceful disintegration of the Soviet command economy. One is political and one is economic, with a common background.

The common background is provided by the Stalinist "war-economy" model, according to which the autocrat was legitimized by the danger of capitalist aggression, and the economy was aimed at building up enough strength to win an armed conflict. Personal and ideological loyalty were the qualities in demand. Technological requirements were relatively limited, and the task of the bureaucracy was to transmit orders from Stalin's ministers to the firms. The army was the only possible interest group in a position to challenge the autocrat.

As suggested in Naishul (1991), the beginning of *détente* and the technological advancement led to a change in the sources of legitimacy and in

the balance of power within the coalition of interest groups ruling the country. In order to keep the economy going, in the early Sixties the Communist-Party oligarchy had to yield authority to the bureaucrats, who were however still obliged to comply with the nomenklatura system, i.e. *the right of the Communist party apparatus [...] to 'recommend' and 'approve' appointments for all managerial positions in the economic (and public) administration, and managerial positions in enterprises*<sup>10</sup>. The ultimate goal of this wave of reforms was apparent at the end of the Brezhnev period, when it became clear that the top-down planning procedure had been replaced by an iterative planning process within the bureaucracy. But of course, the command-economy pattern introduced by Stalin was still well alive.

Given this situation, according to the "politics first" viewpoint, crisis in the late Eighties broke out when President Gorbachev questioned the rent-seeking power of the bureaucrats and of the top managers of the large firms. Gorbachev's attack was successful. The underlying reform raised the costs of rent-seeking for the bureaucrats, the power of which was greatly reduced. But since the iterative-planning procedures and the opportunities to bypass the deadlocks were based on the bureaucracy, the delegitimation of this interest group led to an enormous increase in the transaction costs for economic activity as a whole. Production was disrupted and economic performance worsened considerably.

The economic explanation differs in that it belittles the role of the fight between the coalition led by Gorbachev and the bureaucracy; and traces the origin of the Soviet crisis back to the ways to compensate for the deficient performance of the economy, especially in the past couple of decades. As a matter of fact, the Soviet potential for growth had always been frustrated by the inherent weaknesses of the command-economy pattern. At the end of the Stalinist period, however, information, the international climate, and the new role played by the bureaucracy created a situation where (a) the number of rent-seekers to be satisfied increased, and (b) the Soviet population would no longer accept sacrifices for the sake of security and ideology. This created potential tensions, between the rent-seeking goals of the major interest groups on the one hand, and - on the other - the need to reduce transaction costs and deadweight losses.

In the Fifties and in the Sixties such tension was partially solved by

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<sup>10</sup> See Winiecki (1991, p.4).

extensive growth and informal institutional arrangements, which made the inefficiencies of command planning less problematic. But by the Eighties extensive-growth opportunities had been exhausted. The ruling *élite*, or part of it, was thus forced to take a leading role in abandoning the command-economy pattern and advocating institutional change, so as to be a plausible candidate for the post-communist period. In other words, by supporting economic transition the incumbent leaders took their chance to distance themselves from the past and try to outlive poor economic performance.

### 3.2 *Features of transition in Russia*

It is clear that the two explanations outlined above have a great deal in common. In both cases economic performance is acknowledged to have been inadequate, and in both cases transition started as a result of a political breakdown. The difference between the political and the economic versions concerns the ultimate cause which led to the collapse of the command economy - either a struggle within the ruling coalition (Party against bureaucracy and top managers), or economic failure, which in turn delegitimized the Party as traditionally understood.

The two theories also differ sharply as regards the predicted results of the transition phase. If the command-economy pattern collapsed just as the unintentional by-product of an internal struggle among interest groups within the coalition, then it is clear that transition in Russia is heading nowhere. On the other hand, if the centralized property rights pattern lost its appeal because the ideological motivation was no longer enough to compensate for low living standards, then it is plain the "new" politicians are acceptable as long as they are committed to growth-enhancing constitutional change. Selecting credible and committed politicians may be a difficult, time-consuming process; and then, that may not be enough to make promises and expectations real. But the economy would still be heading towards an identified target, with some chances of success.

In fact, the abruptness with which the Soviet economic system broke down seems to indicate that at the beginning there existed some rather wide popular support for the new wave of reforms<sup>11</sup>, whereby the bureaucracy was to be

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<sup>11</sup> It is worth emphasizing that Gorbachev's scenario never considered the transformation of the Soviet bloc into a free-market area. The recurrent concepts were "enhanced efficiency", "reduced waste", with a lot of ambiguity about the role of private property and private initiative. Of course, all that was quite similar to many previous rounds of reforms.

singled out as the scapegoat for the economic failures. It seems fair to say that at the beginning hardly anybody was really thinking about transition, that is about changing the criterion to assign property rights. As a consequence, the reform programme did go through, but led to chaos, for the reform programme hit one of the pillars of the system. Attempts to get transition started began in earnest much later (mid-Nineties), when the weakness of the property rights assignments generated by the institutional vacuum induced politicians to claim power by promising the median voter neither ideological purity, nor military might; but economic growth and the end of chaos. The credibility of such a claim is crucial to assess whether transition is really under way, or whether the institutional vacuum left by economic crisis and ill-designed reforms is going to be the arena where old and new interest groups act to galvanize into effective, possibly long-lived coalitions, ultimately fighting for power, rather than to promote growth.

### *3.3 Pre-conditions for successful transition*

The basic lesson from the Soviet experience is that widespread dislike of centralized preferences and decision-making is enough to destroy the property rights system of a command economy, but not necessarily enough to enhance new property rights assignments.

Two major problems stand on the way to successful transition. On the one hand, bureaucratic planning in Russia has been beaten, but the bureaucracy is still there, and it remains an extremely powerful interest group. Bureaucrats or former bureaucrats remain in control of industry, have fairly easy access to various forms of subsidy, can avoid paying taxes. Of course, since they are afraid to be a net loser from a new property rights pattern, they are unwilling to lend support to constitutional bills which reduce their rent-seeking opportunities significantly. If this attitude prevails, property rights assignments in Russia are going to remain weak and uncertain. Initially, transition is bound to give way to fairly primitive and informal economic organizations (local markets, barter, extra-judiciary enforcement of contracts, etc.); at a later stage, the bureaucracy would inevitable take power again, to enforce some kind of spontaneous, informally-agreed-upon order.

In addition, there is a time-inconsistency problem. Even if pressure in favour of transition does build up, it takes time for the new set of incentives to produce results, for the new formal and informal institutional

arrangements to establish their reliability, for agents to adjust their behaviour accordingly. Yet, a ruler who claims legitimacy based on his ability to achieve long-run goals is going to be evaluated on the basis of his short-run results. The inconsistency between the timing of the proposed goals and of monitoring might thus encourage myopic behaviour by the leader(s). Frequent political turnover - or instability - becomes more than just a remote possibility. This would entail undesirable repercussions on institutional reliance, and thus on the chances to reduce uncertainty and transaction costs. Once again, transition would stop short of success.

#### 4. The former Eastern-European satellites

The situation in the European countries of the former Soviet bloc was different. The ruling interest groups were indeed committed to rent-seeking by means of physical planning and bureaucratic bargaining. However, contrary to the USSR, in these cases legitimacy for the ruling *élites* came from the very credible threat of Soviet military occupation, should the command-economy property rights allocation be altered. In short, the alternative to central planning and a totalitarian regime was Soviet invasion, not free market and democracy. In fact, as soon as President Gorbachev announced that Russian troops would no longer interfere with domestic politics and policy making in the satellite countries, the whole area went through bloodless attempts to change the system.

Of course, this does not mean that the practical possibility of dropping central planning implied *per se* a common desire to carry out transition, let alone successful transition. As a matter of fact, three different patterns of institutional change can be identified, following the attitude of the various interest groups towards the transition process.

##### 4.1 *Transition in earnest*

As is known, today only three countries exhibit a more or less successful transition record. Although state intervention is still substantial in all of them, the Czech Republic, Poland and Slovenia have managed to make significant progress towards the property rights system typical of a mixed economy. Hungary and Slovakia are not very far behind.

North (1979) pointed out that there are basically two theories of the state - the contract theory and the predatory theory.

Although some elements of prey cannot be ruled out, it is fairly clear that in these relatively successful countries the contract approach prevailed.

The new situation did not offer other options, anyway. Contrary to what happened in the former Soviet Union, these countries experienced pressure for (bloodless) revolution from below, not from above. The new rulers thus needed legitimacy from the median voter. This was obtained by agreeing on a contract whereby the new policy makers were committed to political independence (away from the Soviet bloc) and fast economic growth. Other issues, such as minimizing the cost of transition, apparently had a lower priority. Proximity to Germany, better trade relations with the OECD area, hope to attract foreign direct investments, familiarity with Western consumption patterns and culture surely played an important role in defining this ranking<sup>12</sup>.

In particular, the post-Soviet ruling *élites* could not insist on rent-seeking for two reasons. On the one hand, their legitimacy came from their commitment to a new, fairly decentralized property rights pattern. This was the essence of the implicit contract mentioned earlier.

On the other hand, before transition this group of economies was relatively open to trade with the "free world", although firms were not responsive to the international terms of trade, but to the domestic bureaucracy in charge of the foreign-trade plan. In the aftermath of central planning and Comecon, the greater exposure to the new trade patterns and to the world relative-price system would have necessarily brought about a drastic change in the balance of power of the interest groups; and shape new groups altogether. The foreign-trade bureaucrats were doomed, and the rules of the rent-seeking game with the exporting/importing firms would have changed drastically. Of course, the outcome of such a change was hardly predictable, for the rules were not obvious, nor were the actors. But it was fairly clear that any politician anchored to property rights assignments designed to create rents for - and/or to extract rents from - pre-transition interest-group distribution would have made the policy maker very weak as soon as transition took off. It is plausible to assume that in this framework the safest course for the new political *élite* was to restrain from rent-seeking with the old coalitions,

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<sup>12</sup> This surely applied to the early Nineties, when the new politicians were aiming at obtaining power, rather than maintaining it. As time went by, however, the ranking changed, and the politicians turned out to be reluctant to face the political cost of hardship. Even in the perhaps most committed free-market country - the Czech Republic - much of the banking/financial sector is still controlled by the state.

accumulate credibility to spend in the post-transition period, and put off rent-seeking issues with the private sector at a later stage.

As a result, trade openness in such countries contributed to lessening the scope for tensions between the need to allocate property rights so as to reduce transaction costs, and the wish to allocate such rights so as to increase rent-seeking opportunities. Uncertainty was too high to make this potential trade-off a serious issue.

#### 4.2 *The illusion of transition*

At the other extreme, there are countries like Belarus, the Ukraine, Bulgaria, Rumania, where transition never took off. In all but one case (Rumania), these are situations where the command system collapsed because its inefficiencies could no longer be compensated by the Soviet Union, unable to transfer enough resources to allow people to survive. Politics played a relevant role, too. In one situation the autocrat suddenly lost legitimacy (in Ceausescu's case, his political survival was guaranteed by the threat of Soviet invasion). In general, incumbent policy makers found themselves without the only major interest group supporting them - Moscow's ruling *élite*. The struggle for power which followed destroyed the command-economy pattern which by the end of the Eighties had become the result of an elaborate and delicate system of balances, of formal and informal links involving the various layers of the Party and of the bureaucracy.

Surely, in all these cases pressure for change came from above, not from below. For the fight for power was among short-sighted "roving bandits", who were aiming at taking power, and at keeping it long enough to maximize their revenues from rent-seeking. Of course, since the lack of legitimacy would reduce the chances of staying on top for a long time, and would expose the new rulers to the realistic possibility of being turned out of power any moment by other equally-short-sighted bandits, rent-seeking revenues were maximized over a relatively short time interval<sup>13</sup>. In a nutshell, the bases of the predatory

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<sup>13</sup> International support for the ruling coalition and the free-rider problem contribute to explain why short-sighted rulers may stay in power for relative long periods, and thus become long-lived myopic rulers. But that does not change their optimal strategy. The long-lived myopic ruler is unable to play the rent-seeker game, for there is little left to extract. The bandit looks very much like his subject, except for the wealth accumulated in previous periods.

See also Colombatto and Macey (1996) for a more detailed discussion of the rent-seeking attitudes of a totalitarian leader in countries characterized by low information and - more generally - high transaction costs.

state were never seriously questioned. In such countries revolution was much more similar to a palace insurrection than to a quest for institutional change. In particular, the end of the command economy was little more than an accidental casualty, so that the very clear property rights assignments derived from the command economy did not give way to a new property rights structure, or to a consistent drive towards it; but rather to a vacuum. These countries were doomed to be prey of institutional chaos.

In these cases the outlook for the future therefore remains gloomy, unless a major shock occurs, and a new *élite* legitimized from below or with enough power to expect long-term rule emerges. That would be the beginning of a state based on some elements of contract.

#### 4.3 *Slow transition*

The third group of countries identifies a set of situations where the source of legitimacy for the ruling *élite* is not entirely free from ambiguity.

The collapse of the command economy may have come from above, as in some Asiatic Republics of the former Soviet Union. Or from below, following the pattern of the satellite countries, as in the Baltic states. However, under both sets of circumstances the sources of legitimacy for the ruling class were to some extent vague. Pressure for growth was not as high as in other parts of the former communist bloc; whereas the identity of the median voter was still uncertain. It was clear enough that the command-economy pattern could be abandoned without risking an invasion. Similarly, everybody would share the desire for decentralized preferences, as opposed to state priorities. Yet, the desire to decentralize decision making in production remained relatively weak, while it was apparent that the median voter feared that transition towards a free-market pattern might affect the existing informal institutional setting. In fact such informal frameworks has probably fared much better in these countries - where distance from the center (Moscow) and ethnic bounds played a major role - than in other areas of the Soviet bloc.

As a result, these economies have been featuring a very slow transition process. In their own way, they follow the Popperian process of piecemeal engineering, starting from an obviously undesirable situation. Constitutional law-making has been looked upon with skepticism; utopian social engineering has been set aside. Caution prevails. Little by little, change in the formal property rights system will reflect adaptation to the informal institutional framework, lagging behind rather than leading.

The resulting evolution need not be monotonic, though; for mistakes can be made and even encouraged. Indeed, in a broader perspective one could expect (piecemeal) transition for the worse, too. The ruling coalitions may take advantage of the persisting ambiguities to become stronger, increase the degree of government intervention, extract rents and keep growth low<sup>14</sup>. Or they may try to keep rents low and adopt a long-run survival strategy by following and incorporating spontaneous informal institutions into the legislation.

In these cases the outcome is unpredictable, but evolution controlled by selection is taking place, although at a relatively slow pace. Myopic behavior by the policy makers is unlikely, for short-term bandits hardly have the possibility of seizing power. However, fast-growth policies are constrained by a median voter who is unlikely to take chances and see his political and economic situation change drastically. Committed efforts to achieve fast transition towards a radically new property rights system would spell decline for any politician.

##### 5. Concluding remarks

The collapse of the command economies of the former Soviet bloc has offered an almost unique opportunity to observe and compare the implications of mainstream economics as opposed to the property rights approach.

According to the latter, it is critical to focus on the origins of the Communist collapse, so as to understand the sources of legitimacy of the new rulers, their goals, and thus their ability to keep rent-seeking at bay, and reduce transaction costs through appropriate constitutional change. As explained in Pejovich (1995), spontaneous institutional change becomes the very essence of the transition process. Thus, the analysis of how to run or how to reach the utopian economy is of less interest. Instead, the ability to create a suitable - not necessarily the optimal, whatever this term may designate - institutional framework produces the real challenge. Hence, from this standpoint, and from this standpoint only, it makes sense to put forward and discuss informed scenarios about future developments.

As for policy making, its purpose is to single out the barriers which do not allow the most efficient organizations to arise, and to remove them. This is of course even more important during transition. When this process is

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<sup>14</sup> See North (1990, ch.11).

successful, then transition will be realized, although the timing and sequencing patterns will necessarily follow, not lead, informal changes. Whereas if weak property rights assignments and deliberate short-sightedness allow policy makers to behave differently, either in order to please the median voter and preserve power over a long-term horizon, or to maximize rent-seeking over a limited time interval, then economic performance is going to be disappointing, to say the least<sup>15</sup>.

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<sup>15</sup> One may note that these conclusions are fully consistent with Alchian (1950) and Winiecki (1991), where the role of policy making is analyzed in greater depth.

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