openloc
working papers series

Analysis, interpretation, and the local dimension of economic transformation: What went wrong and why?

Bruno Dallago

WP 13/2009

This research was funded by the Autonomous Province of Trento, as the sponsor of the OPENLOC research project under the call for proposals "Major Projects 2006". Partners of the project are: the E. Mach Foundation, the Manchester Institute of Innovation Research, the Trento Museum of Natural Sciences, the University of Bologna and the University of Trento

PROVINCIA AUTONOMA
DI TRENTO

EAEPE

SYMPOSIUM

THE TRANSFORMATION OF POST-SOVIET ECONOMIES TWENTY YEARS ON

9-10 October 2009

Offley Place Country House, Great Offley , Hitchin SG5 3D

Draft
August 2009

Analysis, interpretation, and the local dimension of economic transformation: What went wrong and why?[1]

by Bruno Dallago
University of Trento
bruno.dallago@unitn.it

Abstract

Transformation has been put in motion by a variety of both endogenous and exogenous forces. Although not any process was under the control of those countries, their choice of goals and instruments was anyway particularly great, at least theoretically. However, transformation was implemented as a rather narrowly defined and technically circumscribed problem-solving process aiming at applying sound general principles of economics and management to reach well-defined goals. It turned out to generate new problems and resulted in different outcomes in different countries and, within individual countries, in different territories.

This paper treats transformation as innovation and considers that it had to deal with different dimensions, including both general principles and local features, opportunities, and constraints, and both analysis based on problem-solving, and interpretation of the new situation. These dimensions should have been managed simultaneously, but failed to do so. The paper provides a general explanation for the failure in managing simultaneously the various components of transformation and considers what the 2008 international crisis has revealed of the implementation of 20 years of transformation.

Keywords: Transformation, Local development, Reform, Analysis, Interpretation, Crisis, Washington Consensus, Innovation

JEL: O43, O57, P20, P26, P27

[1] The author gratefully acknowledges financial support by OPENLOC, a research project funded by the Autonomous Province of Trento, under the call for proposals "Major Projects 2006".

> "Productive societies, to sustain themselves, must be both efficient and creative. The two attributes do not coexist comfortably. The balance between them must in fact be continuously reassessed and recreated, especially in periods of rapid economic change." (Lester and Piore 2004, p. 194)

Transformation has been put in motion by both endogenous and exogenous forces. The former had to do with achievements and failures of the Soviet-type system and the national variants that existed, the latter with international processes such as globalisation and the economic, military and political pressure, threats and opportunities that richer Western countries, their governments, agencies, enterprises, and citizens exerted upon Central and Eastern European countries. Although not any process was under the control of those countries, their choice of goals and instruments was great, at least theoretically.

However, transformation was implemented as a narrowly defined and technically circumscribed problem-solving process aiming primarily, if not exclusively to apply sound general principles of economics and management to reach well-defined goals. Indeed, its most popular definition is that of "transition", that implies knowing the starting point, having clear the goal and a precise idea of the path leading from the former to the latter. The path was largely determined, or anyway strongly influenced by what was defined as the "Holy Trinity" of the Washington Consensus: macroeconomic stabilisation, privatisations, and liberalisation.

By implementing transformation as a problem-solving, transition turned out to cause as many problems as it contributed to solve. Even more important, it resulted in different, sometimes extremely different outcomes in different countries and, within individual countries, in different territories. Although achievements have been important in various cases, the sustainability of successes is far from being guaranteed. The 2008 crisis may have revealed the structural weakness of the situations that came out of transformation. After two decades it is time to ask what happened: was transition the wrong approach, or did countries implement badly a correct recipe, or did they react in the wrong way to political and social pressures? Or was a technically sound strategy implemented in the wrong context? Was anything important disregarded or was a different strategy required?

The paper relies on some recent developments in political economy theory and treats transformation as innovation, as indeed it was. In the next section it presents briefly recent developments in political economy theory that are particularly close methodologically to the issue of transformation. Section 2 deals with the legacies of the old system, that identify starting conditions, and considers choices that countries were confronted with in order to transform their economic systems. In section 3 it is considered what economic performance during the last 20 years reveals about the soundness of the chosen strategy and development path. It turns out that transformation had to deal with different dimensions, that should have been managed simultaneously, but failed to do so. This is the topic of the fourth section. One important, disregarded dimension that could have contributed to such simultaneous management was local development: section 5. highlights why this is so and what are the consequences of its disregard. Section 6. concludes by providing a general explanation for the failure in managing simultaneously and at different (general and local) levels the various components of transformation. It also considers what the 2008 international crisis has revealed about twenty years of transformation and depicts the challenges ahead.

1. Reform theory

Transformation can be interpreted as multilevel radical innovation. Indeed it consists in a set of wide-reaching and deep processes of different nature and at different levels that changed dramatically and permanently the very nature, working and outcome of economic activity, along with many other fields. Among the most important innovative changes have been the institutional setting of former Soviet-type economies; property and other economic rights and relations (e.g. the right to hire and dismiss employees); social relations in the economy (particularly between capital and labour); the role and nature of policies (from administrative to market policies); economic calculation and decision-making (from centrally planned macroeconomic to decentralised microeconomic); motivations and incentives to economic activity (from implementing central plans to competition and profit); the organisational setting of the economy (different types of enterprises and economic organs, representation of different and sometimes conflicting interests, such as entrepreneurial associations and labour trade unions); coordination mechanisms (from plan and central administration to markets); the role of foreign trade and geographical orientation of markets (from close or semi-close economies to open economies, from East to West); change of the main actors of economic activity (from administration to capitalist enterprises, from large bureaucratic companies to different size enterprises); change of technology (from semi-autarchic technology to world technology, introduction of new products and processes, reorganisation of research). After these processes were implemented, and in spite of important path dependence and changes of strategy, the economies, their main agents, and their working were widely and deeply restructured and sometimes thoroughly changed.

Considering transformation a multilevel radical innovation implies that change takes place at different levels and perspectives and that, being radical, uncertainty is pervasive. Being multilevel means that the process of transformation is under the influence of factors of different levels: international, national, and local level; formal and informal institutions and processes; past achievements and future aims and goals; public and private, large and small actors; processes of competition and cooperation. As a consequence, transformation must be in respect of general economic principles of sound management of the economy, but this must be done embedding these principles into local features, capabilities, opportunities, and constraints to guarantee economic, political, and social sustainability and effectiveness of changes.

Being radical means that uncertainty is pervasive, since feasible goals are not clear, in particular if we consider their economic, political, and social sustainability, and the path to be followed is blurred. In fact, reference models and relevant knowledge are missing, being the first time in history that a radical transformation of centrally planned economies into market economies is implemented in a short span of time. Being radical also means that changing the parts (individual institutions and actors) is not sufficient: also the coordination of the constituent parts and the whole (the entire economic system) must change. All this is a daunting aim that requires precise analysis and problem-solving. However, due to the novelty and the far reaching nature of the undertaking this is not sufficient. Transformation also necessitates a broad and socially converging perspective of the problems at stake, far-reaching and imaginative discussion of feasible and sustainable alternatives, debate and interaction among involved parties to collect ideas and streamline goals and action, anticipation of the interrelation among individual changes that are introduced, coordination of expectations. Therefore, it is not sufficient to analyse: it is also necessary to interpret what exists and is changing. Both analytic and interpretative abilities are required.

The problems to be solved in order to understand and manage transformation can be represented in a two by two matrix (table 1). The matrix lines include the double level of reforms that have to be implemented: conjugate the respect of general economic principles of good management with the adaptation to local circumstances (features, capabilities, opportunities, and constraints). In column, we find the double request of innovation: analysis to define the problems and clarify possible solutions, and interpretation to figure out the potential nature and features of the new product or process and build a common language among those who contribute to innovation. The matrix includes some examples of explanations, policies, or situations that have focused primarily (although not exclusively) on one of the four possible locations in the matrix.

Table 1. The two double dimensions of transformation analysis

		Innovation	
		Analysis (problem solving)	*Interpretation*
Reform	*General principles of good economic management*	Washington Consensus Shock therapy and top-down policies	Round tables Gradualism
	Local circumstances (features, capabilities, opportunities, constraints)	SMEs policies "National" and regional ways Actual budget policies	Industrial districts/clusters Paternalism/populism Bottom-up policies

Recent political economy theory offers some interesting perspectives and instruments to analyse the complex nature of transformation and brings the above matrix to unity. Reform policy analysis studies the conditions for identifying the optimal reform and reform procedures to promote growth (Rodrik 2007). Since reviving growth and converging to the level of income of West European countries was the most prominent among the economic goals of transformation, this perspective is central to our analysis.

Reform policy has, nearly by definition, trust in the ability of governments to improve the society and economy they are responsible for. This consideration is realistic in the case of transformation, since the role of governments was dominant, at least in the first stage when the new institutions and structural change were implemented. This governments do by following general principles of good economic management, but also keeping local circumstances in great evidence, since opportunities and constraints differ according to the specific environment in which policies are implemented.[2]

In fact, general principles of good economic management (first-order economic principles in mainstream parlance) – which include protection of property rights, contract enforcement, market-based competition, appropriate incentives, sound money, debt sustainability – are the outcome of institutions which can take on different forms in diverse environments to deliver those functions. Institutions do not map, then, into unique policy packages, thus leaving reformers substantial freedom.[3]

Since "[d]ifferent packages have different costs and benefits depending on prevailing political constraints, levels of administrative competence, and market failures" (Rodrik 2007, p. 29), the skill of reformers will be to find the package of institutions that will minimise the costs and difficulties and maximise the benefits for a particular economy. This is under the constraint of path dependence (the "pre-existing institutional landscape" in Rodik's parlance) and other local circumstances. Successful reforms, then, require "considerable local knowledge" (Rodrik 2007, p. 42). And since local circumstances vary, so do the reforms that work.

This important conclusion stresses the necessity that reforms respect simultaneously the general principles of sound economic management and local embeddedness of policies. This amounts to say that rarely first-best solutions and policies are the most apt for reforming economies, since these are based exclusively on general principles. Effective and sustainable solutions and policies are typically second-best.

Therefore, reforms require deep and detailed practical knowledge of the particular economy under reform. This opens an important space for analysis, but also requires far-reaching interpretation. In fact, reforming governments are constrained by limits on their financial, administrative, human, and political resources and capabilities. To alleviate these constraints, governments must be able to identify reform priorities, based on local realities.

Although blue-prints, best practices, international codes and standards, harmonisation can provide important solutions for some of the narrowly 'technical' issues, their importance and role should not be overemphasised within a strategy of institution building at the expense of experimentation. What is fundamental in a general institutional reform is in fact "…a process of discovery about local needs and capabilities." (Rodrik 2007, p. 166) However, the necessity for a detailed and broad process of discovery should not be confused with the necessity for a gradual approach, although this latter method is in a sense familiar to the former.[4] Still the two are two distinct processes.

---

[2] "…appropriate growth policies are almost always context specific. This is not because economics works differently in different settings, but because the *environments* in which households, firms, and investors operate differ in terms of the opportunities and constraints they present. … Learning from other countries is always useful – indeed, it is indispensable. But straightforward borrowing (or rejection) of policies without a full understanding of the context that enabled them to be successful (or led them to be failures) is a recipe for disaster." (Rodrik 2007, pp. 4-5)

[3] "There is no unique correspondence between the *functions* that good institutions performs and the *form* that such institutions take. Reformers have substantial room for creatively packaging these principles into institutional designs that are sensitive to local constraints and take advantage of local opportunities." (Rodrik 2007, pp. 15-16)

[4] "… there is typically a large amount of uncertainty about what those institutional arrangements are , and therefore that the process required is more one of 'search and discovery' than one of gradualism. …

In evaluating reform policies, the focus cannot be on the outcome of reform policies – which is inherently unknowable ex ante – but on getting the reform process right. This can only result from a deep and broadly-based interpretive process that involves both technical expertise, but also genuinely social and political participation. The experience shows that "… participatory political systems are the most effective mechanism for processing and aggregating local knowledge." (Rodrik 2007, p. 8 – see also chapter 5, pp. 153-183)

The relation between analysis and interpretation at microeconomic level and in a competitive context is the main issue of a second important line of thought and research deriving from the analysis of what actually happens in large firms that implement successful innovation of radical type, such as in the case of the introduction of a new product, and the role that the ability to find new sustainable solutions plays.[5] Innovation requires both analysis and interpretation (Lester and Piore 2007). Analysis is essentially a rational decision-making approach organised around projects, that works best when alternative outcomes are well understood and can be clearly defined and distinguished from one another. Analysis requires that communication among the parties consists of the precise exchange of pieces of information. Interpretation can be best defined as a process ongoing in time making use of fluid, context-dependent, undetermined communication. Interpretation is not directed toward the solution of well-defined problems: it is without clear end-points, but setting directions of innovation in order to make people with very different interests and perspectives come to share a common vision and understanding. These kinds of interpretative processes are more appropriate when the possible outcomes are unknown, and in particular when the task is to create those outcomes and determine what their properties actually are. Indeed, interpretation uses ambiguity as a resource out of which new discoveries and insights emerge.

Analysis and interpretation are rooted in different perspectives over the economy and involve very different and in general opposite kinds of skills and different ways of working together with other economic and social actors. It may be actually difficult for the same people to consider both of them simultaneously. However, the ability to manage these two approaches simultaneously and finding a balance between them is the key to sustaining the innovativeness and the competitiveness of economies.

The simultaneous management of analysis and interpretation is important in all fields that require the management and use of innovation. For instance, the development of colour photography by the chemical industry and its use by photographers required the simultaneous management of analysis (developing and using a means that was technically capable of registering reality with sufficient reliability, improve quality, analyse the reproducibility of individual colours, analyse the correspondence of different greys to individual colours) and interpretation (produce films with specialised feature - more faithful or bright - experiment which kinds of subjects are better photographed in colours than in black and white, how to go from a black and white vision and interpretation to a colour one, how to transmit visual messages by means of colours, discover new subjects that in black and white were inconspicuous such as the classical orange) (Dyker 2005, particularly pp. 186-188).

---

what stands out in the cases of real success, …, is not gradualism per se but an unconventional mix of standard and nonstandard policies well attuned to the reality on the ground." (Rodrik 2007, p. 35)

[5] "We tend to think of economic progress as being driven by the uniquely human capacity for rational analysis. But an equally important component of economic progress is creativity, and creativity is a social process." (Lester and Piore 2007, p. 193)

When the interpretive process is missing, the range among which choices are done is too narrow. In these cases, strong analytical processes may lead to choose the best alternative within that range, but this is the right alternative of a bad lot. In fact, and although the analytical dimension must take precedence over the interpretive one in order to clarify the issues that can be clarified analytically, it is the interpretive process that determines the range of possible alternatives.

This way of putting the problem has some correspondence in Amartya Sen's (1999) analysis of development. Development is in fact the fundamental dimension of transformation, even if analysts and policy makers interprete it too often, if not exclusively, as growth of production. According to Sen, "[d]evelopment can be seen, …, as a process of expanding the real freedoms that people enjoy." (p. 3). Freedoms depend certainly upon GDP, but many other factors are equally important. These include social and economic arrangements, such as facilities for education and health care; political and civil rights; and the removal of major sources of unfreedom, such as poverty, tyranny, poor economic opportunities, systematic social deprivation.

According to Sen, freedom is essential to development for two distinct reasons: the evaluative and the effectiveness reasons. The former has to do with the assessment of progress, that has to be done primarily in terms of whether the freedoms that people have are enhanced. The latter reason sees the achievement of development as thoroughly dependent upon the free agency of people. This concept of the relation between freedom and development has much to do with the above distinction between analysis and interpretation. Although Sen's distinction is not the same as between analysis and interpretation, much of this distinction is involved in the concept of development as freedom.

Effectiveness reasons are akin to problem solving, hence analysis: these in fact highlight the relevant empirical connections, in particular the mutually reinforcing connections between freedoms of different kinds that are admittedly a major analytic issue. It seems obvious, though, that these mutually reinforcing connections have also much to do with interpretation, i.e. finding a common language and understanding among the members of society. In fact, empirical connections depend also upon social interaction, that in turn depends upon interpretation.

As to evaluative reasons, seeing development as a process of expanding real freedoms for everybody is clearly the fundamental interpretative dimension and its very foundation. However, at the same time one should consider that "…these freedoms and rights are *also* very effective in contributing to economic progress" (Sen 1999, p. 5), which adds an analytical perspective of assessing how this is so and how to go from freedoms to progress.

There are two sets of problems with interpretation and the need to manage it simultaneously with analysis. One has to do with the inherent fragility of interpretation. Indeed, it requires cooperation, transparency, disclosure, and a great deal of trust among the parties. This may be at odds with a competitive environment, that gives wide room to opportunism and secrecy. This problem, however, can be solved by building public spaces for interpretation. There are "…four critical types of public space" (Lester and Piore 2007, p. 122): the interior of the firm itself, industrial districts, the regulatory process, and the university. In the case of transformation countries, these public spaces should be complemented with political organisations, the media and civic organisations, and international agencies that have supported the process of transformation. However, what actually happened in transformation countries was strikingly similar to what Lester and Piore observe in the case of enterprises, i.e. competition dramatically decreased the scope for and role of interpretation and created a need for public spaces.[6] However, in transformation countries alternatives were missing, since those spaces could only (mostly) be external to enterprises. Their destructuring through transition policies left no room for interpretation.

Convinced that what mattered was to streamline as fast as possible Eastern European economies to the successful Western economies – after a short period of harsh adjustment to take the "fundamentals" to acceptable values - governments and international agencies made away with anything which resembled interpretation and went straight and exclusively to analysis and problem solving. The radical novelty of the process did not discourage this brave approach and was not even perceived as such. One important reason for this was ignorance of the issue. In fact, a new generation of economists and specialised agencies took over the duty who never dealt with Soviet-type economies and did not consider the stickiness of institutions, particularly informal one, and the consequences that this could have in delaying and diverting problem solving. Big ready-made plans resulting from purely analytical processes based almost exclusively on general principles replaced interpretation and due concern for local features.

When the damage of this approach became evident and social and economic tensions grew substantially and economic performance was less than acceptable, transformation countries and also international agencies moved to a more interpretive phase, trying to find solutions more apt to the local features, capabilities, opportunities and constraints.[7] However, at that time these economies were changed in an irreversible way and the room for interpretative reasoning and interaction was greatly constrained (e.g. by unbalanced macroeconomic situation, falling performance, foreign debt, international agreements).

The second problem descends from the potential dangers of interpretive reasoning and interaction in an institutionally de-structured situation.[8] It is hard to imagine a fully cooperative and transparent interaction when institutions do not exist that keep ambiguity within manageable limits. Indeed, Lester and Piore have in mind a situation where fundamental ambiguity is reduced thanks to well working formal institutions and settled informal institutions. They refer to technological and market ambiguity, while transformation consists primarily of institutional ambiguity. As a consequence, and since there is much value at stake that uncooperative and secretive actors can capture, interpretation can easily end up in a strategic game to defend privileges and capture

[6] "The competition unleashed by globalization, technological change, and deregulation has reduced the scope for conversation and interpretation in private industry. This in turn has created a need to expand such spaces outside industry itself, in sectors of society where competitive pressures do not naturally reach. The trouble is that exactly the opposite lesson has been drawn. Convinced that it was competitive pressures *themselves* that were ultimately responsible for the boom of the 1990s, policymakers and business lobbyists have sought to reproduce in public spaces unconstrained by market precisely the kinds of competitive mechanisms that are imposed on private business by market forces." (Lester and Piore 2007, p. 177)

[7] An important step in this process was the "World Bank's "discovery" of the need for urgent reforms of the welfare state. See WB 1998.

[8] This case is different from the one that has been found in some Central European countries, particularly after their accession to the European Union and that took the form of populist economic policies based on the softening of the budget constraint. On Hungary see Lengyel 2008 and Mihályi 2008. When institutions are blurred and ineffective, foot dragging and opportunism serving powerful interest groups is a real danger that can easily derail interpretation and consequently effective reforms.

value. However, this is not an argument for limiting interaction to analysis, but instead to give priority to create the conditions for interpretation to play its irreplaceable role. This requires priority to institutional reform. However, as stressed above, this does not necessarily coincide with the superiority of gradualism against shock therapy.

To be successful as a multilevel radical innovation, then, transformation requires the simultaneous management of analysis and interpretation and the consideration of both general principles and local features. Transition as it was implemented in Central and Eastern European countries appeared initially confined to the upper left square of our matrix, i.e. was one-sided. Predictably its outcome is unsatisfactory.

2. Legacies and choices

As any general process of innovation, transformation was set in motion by both endogenous and exogenous factors and the interaction among them. Endogenous factors had to do with both the achievements and the failures of the Soviet-type system and the national variants that existed. These included, among others, the success in implementing the industrialisation of backward countries with the inability to promote technical change and efficiency; the promotion of mass production with the inability to foster innovation and competitiveness; the eradication of unemployment with the inability to use effectively incentives and promote productivity; mass development of public services with their low effectiveness and financial sustainability. These processes ended in progressively falling growth rates after remarkable performance in the Fifties, to near stagnation in the Eighties.

Exogenous factors included mainly the direct and indirect consequences of globalisation and the economic, military, social, and political pressure and opportunities that Western countries, their governments, agencies, enterprises, and citizens exerted upon and opened to Central and Eastern European countries and their citizens. Globalisation opened new opportunities, but also new challenges and constraints for countries. International trade and flows of capital offered new opportunities that Soviet-type economies were unable to capture also for the very inefficiencies of their economic system together with different forms of open and hidden embargo. With globalisation and swift growth of many economies the price of raw materials increased: raw material producers had to afford increasing opportunity costs to continue to export to other socialist countries at the fixed prices (or the delayed mobile averages adopted later on) envisaged by the Comecon agreements. The little integration of Soviet-type economies in the globalisation process through trade, tourism and information and communication revealed the disadvantage in level of consumption and life styles, thus activating a demonstration effect by citizens and consumers that the economy and polity were unable to satisfy.

Pressure by Western countries had both military, commercial, and financial components and both put heavy burdens upon relatively backward and inefficient economies and offered stimulating and favourable opportunities for economies hungry of both capital and imports. This led these countries to deplete their resources to keep pace in the arms race and unbalanced chronically their balance of payments. This happened particularly in the Eighties, but in some cases (in particular Poland, but also Romania and Hungary) also earlier, in the Seventies.

The interaction among endogenous and exogenous factors made the economic situation of those countries nearly untenable during the Eighties. Economic factors interacted with political and social factors and the stick and carrot that Western countries used to make transformation inevitable. Or, better, alternatives (such as police and military repression) appeared unviable to the political leadership of those countries, although a minor part of those leaderships considered it and even tried to implement it, without success (e.g. the August 1991 coup in the Soviet Union). Alternatively, it was used as a minor evil, as in Poland in 1980, to control the society and pursue economic reform.

In the economic domain the main goal of transformation was to revive the performance of the economy. According to the standard explanation and given resource endowment, the performance of an economy depends upon the environment, the economic system, and policies. The environment was changed by the same political decision to open fully and become an integral part of the world economy. The economic system was changed by the decision to implement transformation: eliminate the Communist Party or at least its supreme role in the economy, close down the central planning office, start liberalisation and privatisation. Policies changed by both transforming the economic system (direct administrative intervention became impossible, since the agencies in charge of implementing it either disappeared – like the Central Planning Office – or dramatically changed their nature – branch ministries, the Central Bank and the state budget in particular), pursuing macroeconomic stabilisation, and putting them under the guidance of international organisations.

Which was the role of the four critical dimensions for sustainable reform in the events and achievements that led to transformation and its first steps? The Eighties in Central and Eastern Europe were an important period of systemic analysis and interpretation with great concern for local circumstances. Analysis and experience proved that the old system was not viable and tried to define the problems and clarify possible solutions for reforming the economic system. In this period critical analyses of the Soviet-type economic system and its reform flourished, with quite appreciable results. Many of these analyses criticised the system for disregarding, by its very nature, the most important fundamentals of sound economic management (including hard budget constraint, clarity and enforcement of property rights, effective markets). However, in particular after the Soviet Union, with the 1988 Gorbachev's speech in Berlin, made clear it they did not intend to interfere in the other countries' domestic affairs any more, attempts were also made to strengthen further the local content of the economic (and political) system.

Due to the blurred institutional and political situation, most of the effort was of interpretive nature and tried to figure out the potential nature and features of a new system more akin to the free choice of economic and political actors, and supposedly the citizenry and consumers. The most important economic moments in this interpretation were debates on how to improve the performance of the economy (with positions ranging from plain capitalism to market socialism via self-management), experimentation with new quasi-private organisational forms (particularly in Hungary and Poland), setting up of reform committees (e.g. in Hungary), government-opposition round tables in various countries, opposition circles with informal contact with government and Party circles in most countries.

It is important to stress that this interpretation took place within the limits and the constraints of the (fading) reformed Soviet-type system. This was a period when basic institutions were in a flurry and could hardly constrain the parties, including individuals, to play a plain innovative interpretation. Indeed, under those conditions new valuable positions could be captured that could be used later on to appropriate valuable assets. This situation jeopardised the very existence of public spaces for interpretation, leading so to speak to their privatisation. Interpretation thus became primarily a strategic game whereby each active party tried to figure out and implement those features of the new system which could give them the greatest advantage. This is a situation in which strategies tend to diverge to the damage of socially desirable and shared outcomes. Power relations, strategic alliances and foreign parties decide the outcome. In a sense, the strategy is primarily distributive in nature, while in standard innovative situations interpretation has a socially productive nature thanks to effective institutional constraints.

3. A digression on outcomes: do they prove the correctness of the chosen path?

Although processes are what matters for the success of transformation, after twenty years there was abundant time for those processes to bear the fruits that they were suppose to deliver. Therefore the correctness of processes, in such time lapse, can also be assessed on the basis of outcomes. Along with what can be learned from specialised literature, one could look at the 20 years of post transformation performance of those economies to see whether performance validates the particular changes that were adopted. This is obviously a very indicative exercise, perhaps one methodologically risky in that it must suppose processes that cannot be verified. Yet it can give an idea of the strength of the choices and implementation since 1989.

Following Janossy (1969) and considering transformation as a post-war reconstruction period, we may suppose that transformation is over when economic performance (the level of national income) reaches the level that it would have reached without transformation. Although controversial[9], this perspective has the merit to put the accent on the long-run variables that determine growth. Indeed, keeping its costs into consideration, transformation is economically and socially justified only if long-term growth rates are superior to those brought by the old system.

[9] Jánossy's interpretation intends to demonstrate that any economy has the tendency to return to its long run trend after for whatever reason (e.g. a war) this trend was interrupted and that reconstruction periods are over when the economy reaches this trend again. This long-run growth rate is determined by the number and skill of the labour force which is complementary to the capital stock and its technological composition, and that may not be fully exploited (e.g. because of the lack or destruction of capital). Therefore "economic miracles" are simply the result of the increasing exploitation of this potential made possible by the progressive availability of the missing conditions (capital). In the case of transformation economies we can suppose that, similarly to post-war reconstruction periods, a large gap between actual and potential output opens up due to a discrepancy between the workplace structure of the economy and the qualification structure of the labour force. This 'structural incongruence' is likely to result from the depletion of physical capital, due to the nearly immediate obsolescence of much existing capital during the early stage of transformation. Accelerated investment, made possible also by large Western support, should progressively diminish such structural incongruence, allowing the economy to approach its long-run potential growth path. However, the openness to the more developed countries of the West should improve rapidly the skills of the labour force and accelerate technical progress, thus increasing labour productivity. Critically important, systemic change should give these countries an economic system that guarantees better performance and more effective policies (although it should be noted that post-war years are usually distinct by some level of systemic change). This should result in higher long-run growth rates, i.e. in a new, superior long-run growth path. For an econometric test of Jánossy's model explanatory power see Vonyó (2008).

If we take transformation countries as a whole, the outcome was overall disappointing compared to expectations and still insufficient to convince many constituencies in those countries that it was worth doing (Chart 1a).[10] (Un)satisfaction is obviously a psychological perception that, although it has a real basis, is not necessarily objective. Moreover, it may change when looking at the future instead at the present or the past (Chart 1b). However, it is a fact that there were great expectations (illusions?) in 1989 that transformation would bring clearly improved economic performance and consumption levels soon. Another aspect to consider is that poor performance may depend upon non-economic reasons, as it has been indeed the case in various countries. Therefore, the exercise that follows is simply indicative, a kind of suggestion of a research perspective that should be further explored.

Chart 1a – The perception of changes of wealth of families since 1989

Source: EBRD-World Bank, Life in Transition Survey, 2006. (http://www.ebrd.com/pubs/econo/tr07p.pdf, 29 August 2009)

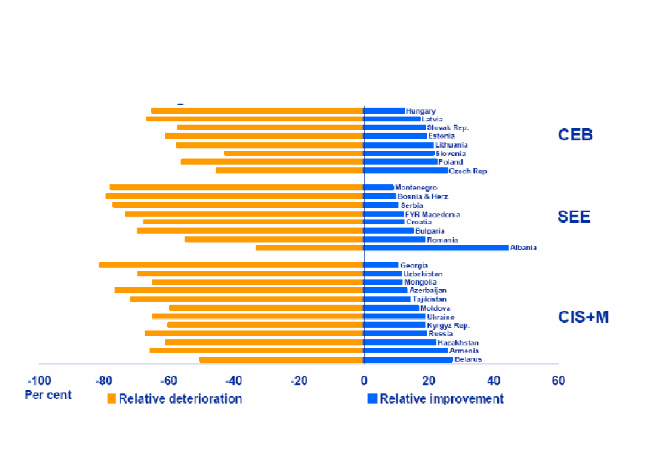
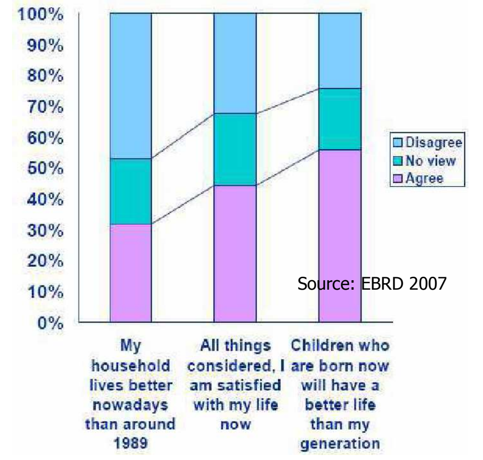


Chart 1b – Different perspectives of (un)satisfaction

Source: EBRD-World Bank, Life in Transition Survey, 2006, p. 9.



Even leaving aside polarised social stratification (see below) and problems with data comparability and concentrating on aggregate performance, although in some countries performance has been apparently quite successful particularly since mid-Nineties, in other countries transformation resulted so far in substantial destruction with very little or no construction. We can easily see this by considering the growth of GDP after 1989 (Chart 2) and comparing it to the pre-1989 period (table 1).

Table 1. GDP Growth Rates in Central and Eastern Europe

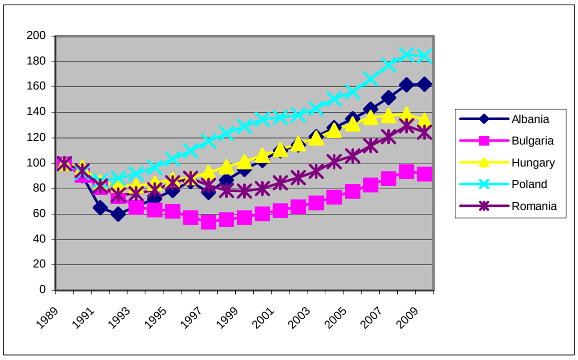
	1950-60	1960-65	1965-70	1970-75	1975-80	1980-85	1985-90
Bulgaria	6,7	6,7	5,1	4,6	0,9	1,2	0,4
Czechoslovakia	4,8	2,3	3,4	3,4	2,2	1,5	1,2
East Germany	5,7	2,7	3,0	3,4	2,3	1,8	1,6
Hungary	4,6	4,2	3,0	3,4	2,0	1,7	0,7
Poland	4,6	4,4	4,1	6,4	0,7	0,7	0,2
Romania	5,8	6,0	4,9	6,7	3,9	1,0	0,6
Soviet Union	5,7	5,0	5,2	3,7	2,7	2,0	1,8

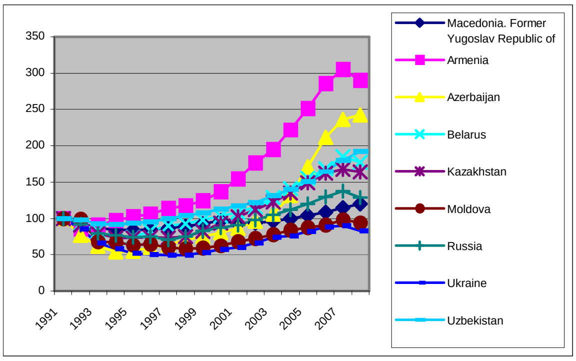
[10] A recent article by Guriev and Zhuravskaya (2009) concludes that transformation made indeed people unhappy and that this is associated with income, i.e. growth but also "depreciation of human capital stock accumulated under central planning, deteriorating public goods, and rising income inequality… Our results imply that life satisfaction in transition countries will continue to rise conditional on continued economic growth" (p. 166).

Unweigh. average	**5,4**	**4,5**	**4,1**	**4,5**	**2,1**	**1,4**	**0,9**

Source: Gregory and Stuart 2004

Chart 2. GDP Dynamics in Central and Eastern Europe (constant prices, national currencies)





Source: International Monetary Fund: *World Economic Outlook Database*, April 2009

As it can be seen (Table 1), annual GDP growth rates were above 3 per cent in nearly all countries and the unweighted average growth rate was above 4 per cent until mid-Seventies. Since then growth rates have dramatically decelerated. Many explanations have been given of this fact that cannot be discussed here. The critical question would be to explain whether the deceleration was due to contingent or extra-economic circumstances or instead they have been caused by structural factors of an irremediably doomed economic system.

To solve this dilemma we consider that transformation was moved by the desire of governments and the population to return to the high growth rates of the first three post-war decades, a growth rate that would allow to converge to Western European countries. It is safe to suppose that this growth rate would be at least 3 per cent. This rate seems quite prudential if one considers the favourable environmental factors that transformation opened up (inflow of financial resources, openness to foreign trade, Western support, technical progress), factors that would have probably revived somewhat growth even in the old system.

With 3 per cent yearly growth rate of GDP income roughly doubles every 24 years. After the 20 years elapsed since 1989, the level of income should have reached approximately 175, putting 1989=100. Few countries have reached this level by 2008. Their number still decreases if we exclude successful performance due primarily to exogenous factors, such as booming oil prices (that had nearly irrelevant effects within Comecon) or massive Western support.

The six countries for which there are continuous comparable data on yearly GDP growth (IMF, *World Economic Outlook Database*, April 2009) have reached the value of 149 (unweighted average) by the end of 2008. Of these, Poland reached 186, but Bulgaria was at a bare 94, below the starting point. These countries are Albania, Bulgaria, Hungary, Mongolia, Poland, Romania. This group includes some of the best performer countries, and even they are clearly below the theoretical level they could have reached. We should not forget, in fact, that in the best performer, Poland, 1989 performance was at an absolute low level due to a decade of political and economic turmoil and therefore had a greater reserve of "unexpressed" natural growth already in 1989.

For another group of countries (including Armenia, Azerbaijan, Belarus, FYR Macedonia, Kazakhstan, Moldova, Russia, Ukraine, Uzbekistan, Kyrgyz Republic, Tajikistan, Turkmenistan) we have complete comparable series since 1991. In this period these countries reached as an average a value of 168, roughly in line with what one could expect. However, this group includes quite distinct performances, spanning from remarkable performance in Central Asia by Turkmenistan (260) and Uzbekistan (192) and the Caucasus by Armenia and Azerbaijan (290 and 242 respectively) and the very difficult situation of Moldova and Ukraina (94 and 93 respectively). The most important country in this group, Russia reached barely an index of 129.

Finally, there is another group of countries, including Bosnia and Herzegovina, Croatia, Estonia, Georgia, Latvia, and Lithuania, whose performance has been generally remarkable and clearly superior to the pre-transformation performance. However, information for these countries starts between 1992 and 1996, at the trough of transitional depression. BiH and Georgia also enjoyed a period of post-war reconstruction strongly supported by foreign countries and international organisations. Foreign support was important also in other countries, from the Baltics to the Balkans.

Various other factors influenced performance along with the change of the economic system: booming world demand (positive), change in population (generally shrinking due to migration and decreasing life expectancy in various countries, hence a negative factor), remittances from migrant citizens (positive), inflow of resources from abroad and the international organisations (positive) and illegal export of capital and resources (negative), post-war reconstruction (positive), natural resources endowment and their access to the world market (positive), international smuggling, laundering, and trafficking (positive). The overall verdict is still pending and the inability to guarantee all other conditions being equal prevents the possibility to reach a clearcut overall picture. It is anyway a fact that some countries – including members of the European Union – are still below the absolute income level in 1989 (or 1991 in the case of post-Soviet countries). Only for few countries convincing evidence exists that in the twenty or so years of transformation economic growth accelerated. However, a more detailed analysis is still pending for attributing the outcome to the different factors at work.

The above data show that, along with some spectacular successes (whose solidity and sustainability are presently at the test of the international crisis), for various countries transformation has been so far overall a doubtful undertaking – although it was certainly a great opportunity for particular individuals and social groups even in the worst cases. The verdict is, anyway, radically different for diverse countries, so that an aggregate explanation would be in an uneasy situation.

Is there a parallel between high growth and transformation policies that had success in managing simultaneously analysis and interpretation and that were respectful of both general principles and local circumstances? An exhaustive answer to this question would require a systematic and deep discussion of the starting conditions and the post-1989 developments. As a hint, limited to some of the new EU member countries, one can observe that the countries that went through far reaching round tables and spent much social time in discussing critical issues such as privatisation strategy, such as Poland, or that relied on a variety of solutions (e.g. in the ownership of firms) so to avoid the polarisation of societies and favour social dialogue, such as Slovenia and to a more limited extent Hungary (all countries have relatively low income differences – see Table 2) were better off in the first decade of transformation than countries, such as Bulgaria, the Baltic states or even the Czech Republic, which relied initially on straightforward solutions (such as mass privatisation) which on (analytic) paper were superior. Particularly noteworthy has been the case of Slovenia, which is probably the country which went closer to the model presented in section 1.

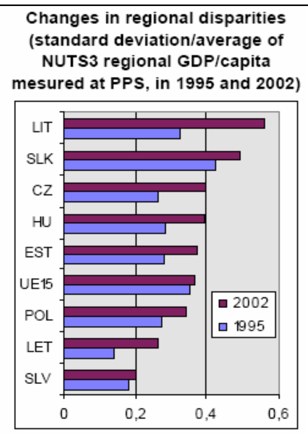
Table 2 – Income inequality in countries in transformation

Country	UN Richest 10% to poorest 10%	UN Richest 20% to poorest 20%	UN Gini index	UN Survey year	CIA Gini index	Eurostat	Eurostat
Albania	5.9	4.1	28.2	(2002)	28.2 (2002)		
Armenia	8	5	33.8	(2003)	41.3 (2004)		
Azerbaijan	3.3	2.6	36.5	(2001)	36.5 (2001)		
Belarus	6.9	4.5	29.7	(2002)	30.4 (2000)		
Bosnia and Herzegovina	5.4	3.8	26.2	(2001)	26.2 (2001)		
Bulgaria	7	4.4	29.2	(2003)	31.9 (2001)	26 (1998)	26 (2004)
Croatia	7.3	4.8	29	(2001)	29 (2001)		29 (2003)
Czech Republic	5.2	3.5	25.4	(1996)	27.3 (2003)	24 (1996)	26 (2005)
Estonia	10.8	6.4	35.8	(2003)	33 (2003)	37 (1996)	34 (2005)
Georgia	15.4	8.3	40.4	(2003)	38 (2003)		
Hungary	5.5	3.8	26.9	(2002)	24.96 (2002)	23 (2000)	8 (2005)
Kazakhstan	8.5	5.6	33.9	(2003)	31.5 (2003)		
Kyrgyzstan	6.4	4.4	30.3	(2003)	29 (2001)		
Latvia	11.6	6.8	37.7	(2003)	35 (2003)	31 (1996)	36 (2005)
Lithuania	10.4	6.3	36	(2003)	32.5 (2003)	31 (1999)	36 (2005)
Moldova	8.2	5.3	33.2	(2003)	36.2 (2001)		
Mongolia	17.8	9.1	30.3	(1998)	44 (1998)		
Poland	8.8	5.6	34.5	(2002)	34.1 (2002)	28 (1999)	36 (2005)
Romania	7.5	4.9	31	(2003)	28.8 (2003)	28 (1998)	31 (2005)
Russia	12.7	7.6	39.9	(2002)	40 (2002)		
Slovakia	6.7	4	25.8	(1996)	25.8 (1996)		26 (2005)
Slovenia	5.9	3.9	28.4	(1998–99)	28.4 (1998)	22 (1999)	22 (2003)
Tajikistan	7.8	5.2	32.6	(2003)	34.7 (1998)		
Turkmenistan	12.3	7.7	40.8	(1998)	40.8 (1998)		
Ukraine	5.9	4.1	28.1	(2003)	29 (1999)		
Uzbekistan	6.1	4	26.8	(2000)	26.8 (2000)		
EU-15						30 (2005)	30 (2005)
EU-25						29 (2005)	31 (2005)

Source: EarthTrends (http://earthtrends.wri.org) Searchable Database Results provided by the World Resources Institute (http://www.wri.org); Eurostat.

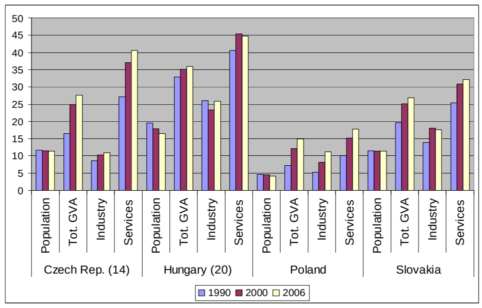
In spite of their geographical extension and unfavourable initial conditions (e.g. regional concentration of heavy industry with high territorial disparities, particularly in Slovakia) both Poland and Slovakia, let alone Slovenia, have increased territorial differences less than the other countries, including Hungary (Chart 3a). The same can be said to a certain extent of concentration of production in capital cities (Chart 3b). One can attempt to state that the former were more successful in managing simultaneously analytical and interpretive processes and this management gave greater room to local circumstances, along with strong(er) respect of general principles. This fact is obviously in strict relation to pre-transformation experimentation and reforms.

Chart 3a – Changes in regional disparities



Source : Eurostat

Cart 3b - Concentration of production in capital cities



Source: OECD

A further aspect that the simultaneous management of analysis and interpretation has guaranteed is the change in the composition of elites. Elite structure, in fact, differs remarkably between countries: "The more limited the ideological and power monopoly of the cadre elite and the more balanced it is by counter-elites [i.e. the more important is social interpretation on the eve of transformation], the greater the chances of a regime and peaceful constitutional-political transformation." (Lane et al. 2007, pp. 13-14)

It is easy to see how this aspect is linked to the burden and length of transitional depression. In fact, where there was a profound and far reaching regime change, also before transformation formally started, and privatisation was relatively orderly with less opportunities for illicit or illegal asset appropriation, the degree to which elites also changed was high. Also the quality of the elites mattered: pre-transformation reforms in Central Europe had a far reaching effect on the capabilities of both economic and political elites, in particular by opening the way to managerial positions to better educated and skilled people, less linked to the party structure (Rus 2007, Lengyel 2007). In such countries as Poland and Hungary "…there was a far smaller chance for the respective members of the cadre elite to remain in party or state position… [while] the winners of the Russian nomenclature of 1988 had a greater chance to be still in party and state positions in 1993, and a smaller number switched to managerial or professional positions." (Lane et al. 2007, p. 14) In Poland and Hungary two-thirds of the former cadre elite shifted mainly towards business, managerial or professional roles. One important reason for this is that in some countries (e.g. Hungary) there was a substantial change of managerial personnel, particularly during the Eighties, whereby younger, better educated, technically skilled and less politicised managers replaced older and more politically faithful managers.

Being the new economic elites more technical and less political in their origin and formation thanks to pre-transformation reforms, Central European countries had better managed enterprises, transitional depression was milder and shorter, and economic growth started sooner (even without relying on rich endowments with natural resources). Having the elite circulation been greater, it was easier to find a common language between the new economic and political elites. Clearly this situation was more favourable not only for professional problem-solving, but also for interpretation, since it caused less social tensions and less strains within enterprises. Systemic openness to competence at enterprise level also means that local features were better evaluated and considered. However, this development was accompanied by lower regard for general principles of sound management, including softer budget constraint for both the state and enterprises (Kornai 1986).

One could ask whether the real difference among different cases lies in the time that was left to actors and processes to change and adapt. The debate on shock therapy versus gradualism highlighted some important aspects of the issue, yet it missed the essence of the problems at stake. In fact, shock therapy – as any other kind of stress situation (Dallago 2007) - is likely to push actors to which the therapy is addressed to adopt conservative behaviour and answers and prevent experimentation, while gradualism can also give time to block change and to entrench positions.

What really matters is the quality of processes (respect of general principles and consideration of local features) and finding a common, socially shared view of the changes, based on a good analysis of the problems at stake and the technical processes that can be used to solve those problems and the consequences deriving from their use. It is only on this basis that the selection between fast action and lengthier processes becomes a technical issue devoid of strategic behaviour and an issue of implementing the society's vision and choices, placing the accent on production in place of distribution of the ownership and control over existing assets. This solution would also give actors the necessary incentives to acquire the knowledge and capabilities necessary in the new system.

4. What prevented the different dimensions from being managed simultaneously

Why was the necessity for the simultaneous multilevel management of transformational issues difficult to recognise ex ante by most analysts and policy makers, both domestically and internationally? First, one could maintain that the necessity for a simultaneous management of analysis and interpretation in due respect of both economic principles and local conditions may be true in "normal" conditions and not in the exceptional transformation of a market-averse system, which paid no attention to those principles, into a market system. Here, one could maintain, interpretation was solved once and for all by the democratic decision of those countries to change the economic system in a market sense. In some countries round tables between social and political forces were organised ex ante to deal with the hottest interpretative issues.

The simplifying view of the exceptional circumstances is mistaken for two sets of reasons. On the one side, the old system managed both analysis (in the form of central planning) and interpretation (through socialist ideology) and took general principles (idiosyncratic to Soviet-type socialism) and local features (national variants and reforms) in some accounts, but this happened in a limited, incomplete and often non sustainable way. However, this approach to the four issues was embedded in social relations, economic standards and psychological attitudes that were some of the basic legacies of the old system and survived through time.

On the other side, the transformation strategy that prevailed put economies under stress, which often caused conservative adaptation to the new four issues, thus slowing down or diverting their entry into effect. For the success of transformation is was necessary to get rid of the old approach and the prevailing transition strategy implicitly considered, wrongly, that this could be done with a clearcut and hard vision of the four issues, in the sense that only general principles and the deriving analysis matter. The exceptionality thesis, thus, contradicts itself, along with being out of tune with the rapidly evolving situation.

Indeed, while central planning was analytic, most interpretation was left to ideology and, to a limited extent, to the central political level (Grossman 1983, Kornai 1992). Public spaces for interpretation were rare and, except in a limited number of cases (particularly Hungary and Poland), under the influence of ideology and politics. Firms were executors of central orders, with the partial exception of reformed economies. However, even in the latter case analysis and interpretation had often as a goal more to manage shortage (and get private advantages), then to innovate for improving performance and wellbeing. These features could not disappear overnight, missing an interpretive dimension to give the necessary reference to economic actors. The starting point was, therefore, unfavourable, while the size and range of the aims and goals were enormously demanding and evolving.

Second, the Washington Consensus – which constituted the core of the transformation strategy at least in the first years - had a vision of the four issues that was incomplete and at odds with the situation of those countries. In fact, the Washington Consensus is intrinsically analytic and based on general principles, implying a set of effective and enforced market institutions and well working markets. Consequently it can suppose that the path of transformation is known (i.e. it is a process of transition) and that local circumstances and discovery are irrelevant, except perhaps in quantitative terms. Interpretation was missing, and the essence of the Washington Consensus and its basic components (macroeconomic stabilisation, liberalisation and privatisation) was one of ready-made recipe fitting all situations. Also the implementation of this strategy left little space to interpretation and limited the possibility of experimentation.

Liberalisation pushed firms to adapt rapidly and so it supported analysis. Moreover, the role of competition may be disruptive of interpretation. For economic actors who were at best used to compete on the input side even mild competition may be disruptive of interpretation. Foreign competition, while providing a ground for imitation, is particularly damaging for interpretation adapted to local circumstances in a period of transformation, since imitation may easily have foreign circumstances as a reference.

As to privatisation, large firms received generally harsh priority. This focused attention at country level on analytical problems, such as establishing the value of the firm and finding new owners, and away from interpretation, such as considering whether and in which circumstances it was preferable to proceed with the privatisation of large enterprises or give priority and related resources to the establishment of new enterprises.[11] Not much energy and time remained to the new owners for understanding what actually matters in an economy, finding a common language (internalising the new institutions) and experimenting solutions, such as finding market opportunities, pursuing technical progress, deciding the products range, achieving strategic alliances. The outcome were booming numbers of enterprises, most of them vary small, uncompetitive and striving for survival (Scase 2003). Since the latter fate also regarded many companies in domestic ownership, the economy became often segmented between a competitive, open sector and an uncompetitive domestic sector which do not communicate or make much mutual business. Interpretation then was missing at both national and firm level.

Third, processes were accelerated at the price of their completeness for fear of foot dragging and conservative resistance. It was considered that time mattered a lot, that time should not be lost for interpretation, and results had to be reached rapidly. This was necessary to make transformation irreversible and compensate people for the pains suffered due to the old system and the little transitional depression that was considered inevitable. This led some newly elected governments to accelerate transformation in order to use the "window of opportunity" and consequently get rid of interpretation and adaptation to local circumstances as devices for slowing down and jeopardising the feasibility and success transition.[12] More than for technical reasons, this third point was based on the perceived weakness of new governments and reformers compared to supposedly strong, although covered conservatives and reactionaries and pressure groups. It is not by chance that one of the supporters of this view, Anatoly Chubais, the leading figure in Russian privatisation, spoke of a Bolshevik approach to identify this position.[13]

Fourth, the necessity for the simultaneous multilevel management of transformational issues remained unrecognised also because of the distributive opportunities that a bi-dimensional transformation created. Old managers and politicians and others were interested, on the eve of transformation and during its first period, in positioning

[11] Not all observers would agree with the necessity to give serious priority to the development of strong and competitive new enterprises. Perhaps the best known supporter of this view is Kornai (1990), but many others have shared this view (e.g. McIntyre and Dallago 2003, OECD 2008). As Kornai (2001) put it: "The transition from socialism to capitalism has to be an organic development. It cannot be done otherwise. It is a curious amalgam of revolution and evolution. It is a trial-and-error process, which retains or liquidates old institutions, and tries out, accepts or rejects new ones. Each element in the process might be very rapid, fairly rapid or slow. Each has its own appropriate speed. Some episodes call for a one-stroke intervention. Many other processes advance by incremental changes." A more limited number of analysts maintain that the number of SMEs should be drastically reduced by means of mergers and acquisitions (e.g. Mihályi 2008). The two views are not necessarily incompatible, although the latter overlooks the particular weakness of SMEs in transformation countries. OECD 2008 pays a particular attention to this issue.

[12] Yegor Gaidar, who was minister of stabilisation and privatisation in 1992, stressed that "…the gradualist approach to transforming a communist economy is the strategy of a communist or totalitarian regime trying to adapt to new realities. … But shock treatment is usually the only alternative for a post-communist government coming to power after the strategy of the previous regime (or bad luck) has led to the failure of the gradualist approach." Gaidar and Pöhl (1995), p. 4

[13] Anatoly Chubais is credited to have answered in the following way to a question on his role as privatisation minister between 1992 and 1994: "…Chubais conceded that his privatization efforts could be characterized as *Bolshevik style* – lacking public support and quickly executed. … His strategy was to privatize as quickly as possible, using every minute of the day to privatize: 'I did not speak, I privatized', Chubais proclaimed." From the report issued by the Carnegie Endowment, Washington, D.C. where Chubais gave a lecture on May 17, 1999 (quoted in Kornai, 2001).

themselves in a favourable way, having in mind both the possibility to capture assets and finding valuable positions in the new system. In such a way they themselves disregarded the interpretive dimension. People endowed with superior local knowledge and information could take advantage of the strategy and policies disregard of this dimension. These individuals and groups typically had influence on the strategy and the choice and implementation of policies.[14]

Even if the simultaneous management of the four dimensions failed during transformation, one could maintain that transformation was important in the perspective of Sen's paradigm of development as freedom. If so, the completeness of transformation could be built *ex post* thanks to freedom. Indeed, transformation had this overarching goal as a priority: removing dictatorship or paternalism, opening social and economic opportunities, promote freedom of choice in economic, political and social fields alike. However, as it turned out, too many of these freedoms were lost of sight and abandoned or postponed along the road. As Rus (2007) correctly stresses, what resulted was a transformation process clearly based on agency theory framework even in the case of enterprises, whereby the emphasis on the allocation of property rights to principals neglected the problem of agents. The freedoms of some privileged people (those who had access to assets) were successfully implemented at the expenses of the rest of society and in particular those who had to manage those assets. This led to suboptimal management an sometimes mismanagement of those assets, since social and the agents' control was weak and competitive pressure over their efficient use was also inadequate in the domestic sector.

Transformation that came out of the bi-dimensional approach disregarded important dimensions of the overall problem and gave a sometimes unfavourable role to those components – analysis and general principles – that were privileged. In the debate and policy making during and on transformation, local conditions and their distance from sound general principles were considered under the heading of "starting conditions". However, the analytical dimension dominated even here in that starting conditions were limited to the macroeconomic situation, with nearly complete disregard for the institutional and microeconomic settings. Even when institutions were considered (in particular in privatisation), it was only formal institutions that were the subject of policies, with disregard for informal institutions, their interrelation with formal institutions and their reaction to transformation policies and processes. There was a further dimension missing: by starting conditions was typically meant national conditions, with disregard for sub-national issues (including fostering and nurturing entrepreneurship), while even microeconomic institutions reform followed at a distance.[15] For different reasons that will be clarified below, this dimension was of critical importance.

On the other side, analysis was limited to the technical solutions necessary to solve particular problems: how much of stabilisation, how fast reforms should be, what to privatise and how, how to liberalise and what. The interrelation among different problems and aspects was largely disregarded: e.g. what to do with companies that

[14] The same Gaidar acknowledged in fact that: "In adopting a universal approach [to privatisation], however, we somehow had to take into account the interests of the various social groups that had the power to block the implementation of the privatization procedures: for instance, the managers of the State enterprises, the working collectives, and the regional centres of power." Gaidar and Pöhl (1995), p. 41.

[15] This fact is rather clearly evidenced in the EBRD transition indicators by the delay with which microeconomic transition indicators followed macroeconomic ones (EBRD 2008).

could not be privatised, what happens when prices are liberalised in a context dominated by large monopolistic firms, how would enterprises used to have a soft budget constraint react to restrictive monetary and fiscal policies, what would have happened to supplier networks following the privatisation of large companies. The term traditionally used of "transition" was indeed meant to identify this aspect of problem solving. However, problem-solving requires that the basic coordinates of the issue (the set of problems at stake, their features and interrelation) are known and the goals are defined. This requires that institutions are well defined and effective. This approach overlooked that the undertaking was totally novel (the famous transformation of a fish soup into an aquarium), the actors involved were inexperienced in this undertaking, basic coordinates (institutions) were missing. Under these circumstances experimentation had to play a central role and wide-ranging and deep interpretation was required.[16]

Inexperienced actors in a ill-defined context could hardly solve the problem. The classical solutions are making the actors' boundaries permeable in order to foster cooperation and relying on public spaces (Lester and Piore 2004). The former was hardly a possibility during the first period of transformation, when interpretation was most needed. In fact, boundaries were economically ill-defined in the old system, when they were primarily of administrative nature, and any permeability during transformation could be exploited to grab assets. Privatisation and restructuring made the boundaries change rapidly and radically. Therefore, interpretation had to rely on open spaces. The most important open spaces could be organisations that did not suffer excessive transformational stress, since the latter diverted their energies and focus. This were not enterprises o their associations, but political parties, social organisations, round tables and reform committees, governments (in particular after systemic change), universities and research institutes, and international organisations.

Unfortunately, the social and political context was not conducive to genuine interpretation for both the excessive novelty of the event, the ill-defined issues at stake, and above all the political and social pressure to go ahead with problem solving and implementing solutions and the distributive opportunities that systemic change offered to smart and quick people. Convinced that it was a few critically important formal changes that were ultimately responsible for the improvement of performance that was expected from transformation, domestic policymakers and international agencies tried to get rid of public spaces or sought to reproduce in public spaces the kinds of mainstream and competitive mechanisms that market forces impose upon private business. This approach reduced the space for original elaboration of solutions in line with local circumstances. Being this the dominant game, many individuals and groups owning valuable assets (such as occupying a crucial position, having important interpersonal relations, bargaining power or technical knowledge of particular value in the new context) could use public spaces to strategic ends, namely to capture opportunities to one's or the group's advantage.

The disregard for institutional reform jeopardised the potential outcome that under these circumstances the state could and should act as a public space (Dallago 2009a). The biggest failure was anyway by international economic organisations. These organisations were under pressure to reach success and relied largely on analytical, problem-solving approach and first-best policies that privileged general principles with little regard for local conditions – except perhaps in quantitative macroeconomic terms.

[16] For a partial exception to the dominant approach see also Eatwell et al. (1995)

In the longer run, transformation countries were left to the only approach that works under these conditions: trials and errors. After a first period of experimentation with first-best policies, a period which lasted just a couple of months in some cases or for years,[17] and under political and social pressure and the economic evidence of transitional depression much longer and deeper than envisaged, governments and other parties resumed interpretation and paid greater attention to local circumstances. However, the first period of one-sided transformation and policies had important consequences for both the costs of transformation and their interpersonal and intertemporal allocation. Also the outcome of transformation was different – sometimes quite so – from what was envisaged, with many unforeseen and unwanted consequences, bad and positive surprises (Uvalic and Vaughan-Whitehead 1997). The dominant approach had consequences that are bound to remain in time and that often are a real burden over economic performance and stability. The wave of populist policies that followed in later years in various countries owes probably much to this first approach.

The partial exception was the European Union. This was due to both its nature of a club of member countries with equal rights and duties and the strong role that a more complex economic approach – the social market economy – still has in the EU. Thanks to these features, the EU had to adopt a more differentiated approach that nearly bureaucratised transformation and acted as a long-term external anchor. This was done primarily through the 31 chapters that perspective members have to comply with. However, this kind of friendly yet quasi-rigorous bureaucratisation provided countries with a clear perspective for problem solving, a limited space for interpretation at the margin and a more serious consideration of local conditions through different funds – at least for enjoying asymmetric benefits. The EU was thus the only actor that acted partially as an open space for interpretation and with concern for local conditions. This was due to the fact that, although the EU foresees a clear goal (conforming to the *acquis communautaire*) and set of steps (the 31 chapters), it also requires and allows for progressive adjustment (discussion, bargaining, asymmetries) that in their complex are interpretative in nature.

To summarise, barely any genuine interpretation took place during much part of transformation, while analysis was applied to bring the economies in line with general problems. Local circumstances were largely ignored, except for the quantitative macroeconomic variables. Simultaneous management of the four dimensions was disregarded. It is hard to see how sustainable systemic innovation and strong economic performance could come out of this approach.

5. Transformation and local development: managing analysis and interpretation simultaneously

The process of economic transformation had as a primary step the decentralisation, in a market sense, of previously centrally planned economies together with the need to foster and activate innovation and competitiveness. The Soviet-type system was primarily analytical and based on general ("socialist") principles with little interpretation and adaptation to local circumstances. Interpretation was prevented by ideology (and the Soviet Union control) and was mostly limited to the highest echelons of the

[17] In Poland, e.g., the full liberalisation of imports lasted a few months, while in Russia liberistic policies were inverted only following the 1998 financial crisis.

Communist Party. Some adaptation to local circumstances in the economic domain took place through economic reforms since the Sixties.

Particular forms of adaptation to local circumstances – and the result of a mixture of problem solving (how to improve performance and go from "extensive" to "intensive" growth within the limits of the existing economic system and political regime) and interpretation – included Khruschev's introduction of *sovnarchozy* or Regional Economic Councils in 1957, that is the failed territorialisation of economic management; the generalisation of personal and family plots in agriculture; self-management outside of Yugoslavia, where it was the outcome of a political decision to contrast Soviet influence; the introduction of semi-private production organisations (such as various labour organisations in Hungary in 1982); tolerance of "residuals" of past systems (small scale private activity) and of the underground economy. While *sovnarchozy* where short lived in Soviet time, other forms of adaptation and limited experimentation were the victims of harsh transition and privatisation.

One reason for the destruction of the little interpretation and adaptation to local circumstances was that these functions were concentrated in the destroyed structures of the Party and central planning. Harsh transition – and certainly also the economic and political weakness of countries in transformation -prevented the possibility for many years to foster those functions in a market perspective. When they started to develop, they were both under the aegis of the need to comply with superior analytical issues (create favourable conditions for foreign capital, decrease deficits and debts, comply with the requirements of international organisations) in full respect of general principles. Interpretation and adaptation to local circumstances remained ancillary.

Local development includes all those conditions that foster performance and transformation of the economy and society located on a given subnational territory. It includes, therefore, both enterprise foundation, growth and restructuring; the production, use, and management of human, social and physical resources (the territory); structural change; and the activity of governments (both local and national). Since any economic activity is localised on the territory and such localisation is determined by the favourable features of a particular location, diffused local development is critical to any economy and is the basis of general economic development. Therefore success with local development means creating favourable conditions for development *tout court*.

To be successful, local development requires both analytical problem solving (e.g. how to decrease costs, which investment should be implemented, where getting financial resources, where building roads and infrastructure, establishing performance friendly taxation) and interpretation (which kind of development and growth strategies are the most apt to a given territory or individual agents; which form of enterprise or kind of relation with partners and competitors should be the most effective; when and how to innovate). It also requires respect for general principles (wages linked to productivity, sound budgets, investing only if there are reasonable expectations to recover costs) and for local circumstances (choose carefully the location of the investment, labour relations in line with local traditions, cooperation between firms and local governments).

In transformation economies, local development is particularly important for another reason. Small and medium size enterprises (SMEs) and local governments are particularly apt to foster interpretation and adaptation to local circumstances. This is so for their very nature linked to the territory, thus feeling less directly the strong external pressure to analyse and follow general principles; and because they are closer to processes and know better local features, capabilities, opportunities, and constraints. Local development is thus particularly important in managing these variables simultaneously with problem solving and general principles under the influence of the central government, provided that the state machine is effective and efficient in a market friendly sense.

This important aspect was largely disregarded during transformation and the little local development that took place was left to the initiative of local governments and social and political movements and spontaneous processes of enterprise foundation, growth, and restructuring. However, the missing reform of the state is at the basis of the lack of coordination among these processes and the possible threat they pose to successful transformation and national performance (the epitome case being Yeltzin's Russia).

During transformation territorial differences increased substantially as much as other forms of inequality. This was due to unleashed "spontaneous" processes that went from agglomeration of economic activities and (foreign) capital to the obstacles that regional governments put to transferring fiscal revenues to the central government. Development programmes (e.g. to attract foreign investments), when sound, where generally analytic/problem-solving in nature and limited to the given locality without discourse and interpretation involving neighbouring localities and central governments and sometimes disregarding sound general principles (e.g. the opportunity cost of granting subsidies to foreign investors). This led to lack of coordination of economic activity and policy making that in the medium run disadvantaged also successful localities. Governments tried to encourage coordination among localities, particularly so in view of EU membership, with uncertain effective success.

Lack of interpretation and experimentation at local level made difficult also to define national strategies, led to uncoordinated actions and waste of resources and, in the long run, waste of opportunities that also depressed the inflow of foreign capital. Indeed foreign capital inflow remained largely linked to privatisation, with much less capital going to greenfield investment. Since much technical innovation is locally based, this led to innovation failure. A proof of this is that SMEs are generally ailing while the analytical devices that were implemented (such as industrial parks, financial support, business incubators) remained largely on paper and were ineffective (on Hungary see Dallago 2009b).

During transformation, socially productive innovation should take place at two levels: at systemic and technical level. At systemic level, institutional innovation often failed to manage successfully the coordination of formal and informal institutions. In fact, it relied nearly exclusively on problem solving approaches both at national and local levels that privileged formal institutions and disregarded informal ones. Even at individual level actors failed to master interpretation and privileged a short-run, formal and narrow approach. What has been missing is the interpretative and integrating component necessary to create language, perception and view common to all the actors involved and pursue a shared development path. The lack of interpretation made also impossible to adapt general principles and best practices to local circumstances. This fostered and increased conflicts between the centre and localities and among the latter, thus increasing the costs of transformation and policy implementation.

At technical level, these countries needed to radically change technology and production organisation, away from the legacy of autarchic technological policies and organisation of production along administrative considerations (central planning, administrative and political control). Once again, the lack of interpretation put these countries in a critical position, although some important results were reached.[18] The analytical approach led to adopt the best practices and solutions that were often alien to the existing technical culture, capabilities, and social organisation and relations. It also failed to pursue adaptation of technology to local circumstances. Technological change succeeded in foreign affiliates, but also there it was often managed by foreign experts (transplantation) and lacked local research basis (that was typically closed down). Organisationally, foreign affiliates themselves remained close to enclaves and also "imported" their suppliers, while most domestic companies interacted among themselves. This generated territorial, organisational, and technical segmentation of the economy.

One important advantage of local development is that it can attenuate foot dragging in transformation, since it lives from and builds up social capital, thus social control and pressure. This is important particularly for the transformation of informal institutions. Formal institutions can be changed through substantial initial investment of human, financial and organisational resources (perhaps financed internationally) to support the take-off of new institutions. Informal institutions, however, are insensitive to this kind of investment since they are sticky, and change incrementally at the margin. Disregarding them was due to the attempt to allocate the cost of the necessary marginal investment to individual actors – or to the confidence that formal institutions would change "automatically", which is the same.

One important reason for fostering local development during transformation lies in the equity and capabilities fostering nature of local development and the effect that this has on stability and diffused entrepreneurship. One of the most striking consequences of transformation was the rapid increase of inequalities and other forms of polarisations of economies and societies (Lane et al. 2007). There is a polarised social and economic stratification, including the rise of a wealthy class and the pauperisation of large strata of the population in most countries. Official statistics and international data show an important increase of distributive disparities since transformation started. However, both the quality of statistics in various countries and the spread of the underground economy, that apparently tends to hide particularly the highest incomes, suggest that official data may underestimate the real disparities existing, particularly in non-EU member countries.

Much of this stratification has its counterpart in territorial stratification, in the sense that the localisation of valuable resources and growth are concentrated in capital cities (in spite of shrinking populations they concentrate an increasing share of the countries' production, income and wealth) and a few relatively wealthy territories (Chart 3a and Chart 3b). Other territories are losing resources and opportunities and ailing. They also concentrate a disproportionate share of the poor and the unemployed (see Eurostat 2009). With the disruption of some countries, in particular former Yugoslavia, territorial disparities may now largely coincide with national borders (see table 3).

This polarisation brings with itself a growing division of interests between different strata of society, and consequently greater difficulty of interpretation and of pursuing simultaneously general principles and appreciation for local circumstances (Chart 1a

[18] For instance, restructuring of production made possible an important restructuring of exports and growing international trade integration. In various countries the share of high-tech and medium-high-tech exports substantially increased. See Fabrizio et al. 2009.

and Chart 1b). Economic, social and territorial polarisation create clashing perceptions, interests and strategies. Congestion on one side and lack of opportunities on the other follow, since losing social groups and regions see their opportunities and capabilities decrease (Sen 1999), while winners may easily waste resources, at least because (particularly so in small transformation countries) they tend to export capital and import luxury goods.

Table 3 – Some indicators of malaise in South-Eastern Europe

	Unemployment rate (2007)	**Gini index (2007)**	**Poverty (%) (2007)**
Albania	12,5	26,7 (2005)	25
BiH	29	56,2	20
Bulgaria	6,3	30,7	14,1
Croatia	14,8	29 (2008)	11 (2003)
Kosovo	40	30 (2006)	37
Macedonia	35 (2008)	39 (2003)	22
Montenegro	14,7	30	7
Romania	3,6 (2008)	32	25 (2005)
Serbia	18,8	30	6,5

Source: World Bank, CIA (The World Factbook), EBRD

Local development has by its very nature diffused character. This supports finding a common language by which to identify innovative solutions which are fundamental in the transformation process. There is an interesting positive relation between the role of interpretation, local development and economic and social stratification. Interpretation requires a commonality of interests and the predisposition to work out jointly a common language. This is possible only if the different stakeholders both within and outside economic organisations share a common view of processes and have common basic interests. The polarisation of distribution of income and wealth, capabilities and opportunities goes hand in hand with the polarisation of economic and social stratification. This prevents finding a common language, hence interpretation and finally innovation. Much of the effort by elites will be addressed to defend their privileges, while that of the destitute will be addressed to survive and perhaps change inequalities to their advantage. This is the old issue of the critical importance of a wide and prosperous middle class and social mobility, which go hand in hand with local development.

6. Conclusion

Along with the pressure from outside, the effect of globalisation and international agencies, and domestic illusions, there are structural factors in the mainstream transition strategy that explain insufficient interpretation and adaptation to local circumstances. The initial disruption of the state (in place of reforming it), the lack of a clear and coordinated relation between different level governments, and the postponement of the institutional reform (or the confidence in the spontaneous implementation through the market) led to a blurred situation ridden with uncertainty (including on property rights, their enforcement, and appropriabiity of returns) that further shortened the time horizon of economic actors and supported rent-seeking strategies. Rapid growing territorial and social polarisation generated clashing perceptions, interests and strategies, which resulted in clear and probably permanent forms of territorial, organisational, and technological segmentation.

Macroeconomic stabilisation, privatisation, and liberalisation – the key components of the dominant transition strategy - had territorially distinct effects that advantaged some localities, while loser localities tried to resist by slowing down transitional policies. Macroeconomic stabilisation, which implied decreasing state subsidies to enterprises and wages and decreasing state investments, was particularly disadvantageous for the localities that gained most in the past with socialist industrialisation. These were the territories where large investment in heavy industry were concentrated. Macroeconomic stabilisation (and the new environmental policies) led to the destitution of these localities and consequently to unemployment and depression.

Privatisation led further to reallocation of capital away from large firms, children of socialist industrialisation, closure of plants by the new owners and transfer of production processes abroad, but also to massive inflow of foreign capital mainly to acquire existing facilities. These foreign investments went typically to a limited number of areas with favourable conditions, also in the case of greenfield investment. This created opportunities for additional activities (e.g. enterprise foundation or expansion) in the latter areas, but to worsening conditions in the areas of disinvestment.

Liberalisation had similar consequences. Liberalisation of enterprise foundation and investment advantaged territories that were favourably located (could exploit economies of agglomeration, had good infrastructure, enjoyed proximity to large markets), and social groups that had the relevant assets (capital, connections, skills, sometimes reputation). Liberalisation of exports again advantaged the territories and social groups which had advantages in terms of international relations (sometimes pre-transformation contacts and cooperation, those that attracted most foreign investment, proximity to foreign markets, sometimes minority populations with large neighbouring mother countries, typically Germans). Import liberalisation, in turn, disadvantaged particularly economically weaker territories and social groups, where uncompetitive enterprises and lower skills were based. Finally, price liberalisation had similar effects. Territories and social groups that were advantaged by liberalisation tended to coincide, then, in all the three cases.

These events had particularly unfavourable consequences for part of local constituencies and SMEs. Inter-regional differences increased dramatically, different forms of polarisation accumulated (industrial, territorial, social), while most SMEs could not take off in sustainability and competitiveness. Even in countries where their numbers boomed, most of them remained uncompetitive.

These processes were based largely on analytical considerations, but lacked the interpretation necessary for a balanced and long-run development. Not only social discourse was missing: even governments abstained from taking care of the losers. As noted by Rus (2007), the process was dominated by only one side of the agency, that of owners, with little concern for successful management, at least outside the foreign dominated sector. Territorial and industrial polarisation created rich and rapidly growing enclaves, mostly foreign controlled, that - by attracting private capital and public investment and by paying unusually high incomes - have split the economy and the society, and consequently the polity, into segments that hardly communicate. This has obvious negative consequences for the development perspective of large part of the economy, but also for political and social stability.

Socially common understanding based on interpretation and concern for local circumstances was later found in many countries around populist policies, that went to the disadvantage of domestic and external equilibrium. The 2008 international crises has revealed the weak sustainability of transformation strategy and the achievements reached so far. This event further highlights the necessity to unify the four dimensions of transformation, including rebuilding public spaces for interpretation and implementing better policies for local development.

In putting greater weight on interpretation and local conditions there certainly is the danger to open the door to endless bargaining and finally to deadlock. It is not time now to go back to 20 years ago and start from scratch. It is necessary to build upon a sound analysis of achievements (such as young educated and skilled generations, EU membership, dynamic enterprises, improved economic structure, better infrastructure). Interpretation should deal with finding a sustainable development based on these achievements and on improving the place those countries occupy in the international division of labour. Consideration for local circumstances should never go against general principles and should consist primarily in the effort to promote the development of disadvantaged territories and social groups and upgrading SMEs and their competitiveness without disadvantaging or obstructing the most dynamic components of the economy.

For instance, in the case of SMEs such a complex strategy, pursuing simultaneously the four dimensions, could build or rebuild the most important factors that support successful territories and enterprises. Among these, one could remind the necessity to foster investment and technical upgrading, competitiveness, growth of small businesses into medium-sized ones, fluid property structures (with weaker absolute control and attracting external competences) support the development of both horizontal and vertical business networks, promote the aggregation of and cooperation among SMEs, and pursue the progress of dialogue and programmes for fostering cooperation with large businesses. There is also great necessity to motivate and support potential entrepreneurs and improve the skills of employees and to pursue policies supporting a territorially more balanced economic activity.

A particularly important goal should be to develop public spaces serving SMEs, including research centres, universities, and business associations. The role of these institutions remained largely passive as public spaces that should deal with interpretation. This may require different research and educational policy that keeps in greater consideration the cooperation between, e.g., universities and industry.

All this requires a highly professional role for the state in all its dimensions and levels, cooperation between the public hand and the private sector, and a shared interpretation and analysis of the economic future of the country in respect of general fundamental economic principles and local circumstances. Unfortunately, there is not much hope that this perspective will become true soon in the present divided societies of transformation countries. Once again, the international community, and particularly the EU, can play a critical role, this time hopefully in the direction of the simultaneity of the four dimensions. The crisis may perhaps provide a welcome opportunity to put transformation on a more sustainable path, as already happened in part in Russia after the 1998 financial crisis.

Bibliography

1. Dallago, Bruno (2007), 'Corporate Governance in Transformation Economies: A Comparative Perspective', in *Corporate Restructuring and Governance in Transition Economies*, edited by Bruno Dallago and Ichiro Iwasaki, Palgrave Macmillan, Houndmills, Basingstoke, 2007, pp. 15-39
2. Dallago, Bruno (2009a), 'The State and the Transformation of Economic Systems', in *Transition from Socialist to Market Economies*, ed. by Shinichi Ichimura, Tsuneaki Sato and William James, Palgrave Macmillan, Houndmills, Basingstoke, 2009, pp. 164-187 (forthcoming)
3. Dallago, Bruno (2009b), 'From transformation to development: SME policy and competitiveness in Hungary', University of Trento, *mimeo.*
4. Dyker, Geoff (2005), *The Ongoing Moment*, New York: Vintage Books
5. Eatwell, John, Michael Ellman, Mats Karlsson, D. Mario Nuti, and Judith Shapiro (1995), *Transformation and Integration. Shaping the future of central and eastern Europe*, London: Institute for Public Policy Research
6. EBRD (2007), *Transition Report 2007: People in Transition*, London: EBRD
7. EBRD (2008), *Transition Report 2008*, London: EBRD
8. Eurostat (2009), http://epp.eurostat.ec.europa.eu/cache/ITY_OFFPUB/KS-HA-08-001/EN/KS-HA-08-001-EN.PDF
9. Fabrizio, Stefania, Daniel Leigh, and Ashoka Mody (2009), 'The Second Transition: Eastern Europe in Perspective', *IMF Working Paper* WP/09/43, March
10. Gaidar, Yegor and Pöhl, Karl Otto (1995), *Russian Reform/International Money*, Cambridge, Mass.: The MIT Press
11. Gregory and Stuart (2004),
12. Grossman, Gegory (1983), 'The Party as Manager and Entrepreneur', in Gregory Guroff and Fred V. Carstensen (eds.), *Entrepreneurship in Imperial Russia and the Soviet Union*, Princeton: Princeton University Press, 1983, pp. 284-305
13. Guriev, Sergei and Ekaterina Zhuravskaya (2009), '(Un)Happiness in Transition', *Journal of Economic Perspectives*, Volume 23, Number 2, Spring 2009, pp. 143–168
14. Jánossy, Ferenc (1969), *The End of the Economic Miracle: Appearance and Reality in Economic Development*. White Plains, NY: International Arts and Sciences Press. Translation of the German edition (1966), *Das Ende der Wirtschaftswunder: Erscheinung und Wesen der wirtschaftlichen Entwicklung*. Frankfurt: Verlag Neue Kritik
15. Kornai János (1986), 'The Hungarian Reform Process: Visions, Hopes, and Reality', *Journal of Economic Literature*, 4: 1687-1737
16. Kornai, János (1990), *Road to a Free Economy*, New York: W.W. Norton
17. Kornai, János (1992), *The Socialist System*, Princeton: Princeton University Press

18. Kornai, János (2001), 'Ten Years After "The Road to a Free Economy, The Author Self-Evaluation", in Boris Pleskovic and Nicholas Stern, eds. *Annual World Bank Conference on Development Economics 2000*, pp. 49-66. Washington, DC: World Bank
19. Lane, David, György Lengyel and Jochen Tholen (2007), ed., *Restructuring of the Economic Elites after State Socialism. Recruitment, Institutions and Attitudes*, Stuttgart: ibidem Verlag
20. Lengyel, György (2007), 'Hungarian Economic Policy Makers and Businessmen in the 1990s: Similarities and Differences', in David Lane, György Lengyel and Jochen Tholen (2007), pp. 97-114
21. Lengyel, László (2008), *A halál kilovagolt Magyarországról* (Death left Hungary), Budapest: Corvina
22. Lester, Richard K. and Michael J. Piore (2004), *Innovation – The Missing Dimension*, Cambridge, Mass.: Harvard University Press
23. McIntyre, Robert J. and Bruno Dallago (2003) (eds.) , *Small and Medium Enterprises in Transitional Economies*, Houndmills, Basingstoke: Palgrave Macmillan
24. Mihályi, Péter (2008), *Miért begeg a Magyar gazdaság?* (Why is the Hungarian economy sick?), Budapest: HVG Könyvek
25. OECD (2008), *Reforms for Stability and Sustainable Growth: An OECD Perspective on Hungary*, Paris: OECD
26. Rodrik, Dani (2007), *One Economics, Many Recipes*, Princeton and Oxford: Princeton University Press
27. Rus, Andrej (2007), 'Human, Social and Cultural Capital of Slovenian Managerial Elite in Market Transition', in David Lane, György Lengyel and Jochen Tholen (2007), pp. 127-152
28. Scase, Richard (2003), 'Entrepreneurship and Proprietorship in Transition: Policy Implications for the Small- and Medium-Size Enterprise Sector', in Robert J. McIntyre and Bruno Dallago (2003), pp. 64-77
29. Sen, Amartya (1999), *Development as Freedom*, New York: Anchor Books
30. Uvalic, Milica and Daniel Vaughan-Whitehead (1997) (eds.), *Privatization Surprises in Transition Economies – Employee Ownership in Central and Eastern Europe*, Cheltenham: Edward Elgar
31. Vonyó, Tamás (2008), 'Post-War Reconstruction and the Golden Age of Economic Growth', *European Review of Economic History*, Volume 12, Issue 02, Aug 2008, pp 221-241
32. WB (1998), World Development Report 1998, Washington, D.C.: World Bank