

Working papers



Transition, Transformation, and the Social Sciences: Towards a New Paradigm

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Abstract

This paper reviews the first decade of the postcommunist transition debate. It examines some of the major continuities and changes in the social science and policy literature in light of key events and developments of the 1990s. It introduces a distinction between theoretical, policy, and ideological concerns in order to clarify the fundamental dimensions of the debate. It argues that the ideological dominance of neoliberal discourse has shaped both policy programs and theoretical approaches, though some policy makers and a growing number of social scientists have been challenging the far-reaching consensus with increasing success. We argue that a paradigm change is well on its way in the transformation debate. Scholars from a variety of social science disciplines are contributing towards a comprehensive cross-disciplinary conception of postcommunist transformation that leaves behind the simplistic conceptions of transition to the market and democracy. The paper presents some of the main elements of this new paradigm and discusses its relationship to and implications for policy debates.

In many research areas of social science, the agenda is set by extra-scientific – technological and political – needs and challenges. Postcommunist transformation studies is a recent instance of scientific work driven by practical concerns. The collapse of communist regimes in Eastern Europe formulated the fundamental practical problem in no uncertain terms: what comes after socialism, and how to get there. In this paper, we trace the interactions between theory, policy, and ideology during the first decade of postcommunist transformation. Our analysis thus belongs to the recent literature that asks, what lessons have been learnt (e.g. King 2000; Lavigne 2000; Wyplosz 2000; *East European Politics and Societies* 1999). What is distinctive of our effort is that we make a clear analytical distinction between the dimensions of theory, policy, and ideology in the transformation debate, roughly corresponding to three major groups of participants – social scientists, policy experts or technocrats (especially in the IFIs), and politicians. The distinction helps us to determine why certain views and paradigms have been dominant, and what have been the dynamics of change. Concretely, we account for the early dominance of the neoliberal paradigm and its subsequent fate. We find that in spite of strong theoretical criticisms and apparently serious policy failures, neoliberalism has to date remained the politically most influential view in the debate. However, since the mid-1990s, alternative views have been articulated by some members of the policy and political communities and by a growing number of social scientists. Our interpretation of this finding is that a paradigm change is well on its way. We describe some of the major elements of this new paradigm.

We begin our analysis with the *first generation of theories* applied to the postcommunist region that dominated the field until the mid-1990s. These early approaches had particular methodological and normative characteristics that help to account for their success. They claimed to combine the most advanced theories and methods of social science with superior Western values in formulating clear and unambiguous policy recommendations. This vision of a “self-organizing” and universally applicable democratic market society proved irresistible for postcommunist reformers. “Today liberal democracy *is* the only ‘rightful’ game in town,” as Giovanni Sartori (1991: 443) seconded neoliberal discourse from the perspective of democratic theory.

Admittedly, numerous objections to the simple application of mainstream economic theory and standard IMF recipes to the failed planned economies had already been brought forward in the early 1990s. Political scientists had cautioned that formal institutions alone would be an insufficient focus for reforming political systems, while sociologists had pointed to unintended consequences of narrow economic reforms and the social embeddedness of markets. However, such academic critics could not assert themselves against the hegemony of a neoliberal

reform discourse that was secured in a variety of ways. The ten commandments of the “Washington consensus” were buttressed by combining the institutional power of the international financial institutions and the U.S. administration with the intellectual prestige of economic theory and a faith in the organizational capacity of markets that was not easily shaken by counterevidence. Thus the orthodox stream of transformation theory to this day remains committed to the trinity of rapid stabilization, liberalization and privatization as the essence of reform policy that accounts for reform success or failure, the formation of reform coalitions, and the consolidation of democracy (Aslund et al. 1996; Fischer and Sahay 2000; de Melo et al. 2001; Mussa and Savastano 1999).

Yet the weight of objections to and fundamental criticisms of neoliberal orthodoxy emerging from all social science disciplines, including economics, has steadily increased. They have reached a sufficiently critical mass to speak of a paradigm shift in transformation studies. Before we turn to the emerging new paradigm, the next section will offer some historical and methodological background to the debate by reconstructing the neoliberal discourse of reform that dominated the new field of transformation studies in the early 1990s.

1. The Politics of Marketization and the Neoliberal Discourse of Radical Reform

The research area of “transitology,” organized around a set of well-defined problems, emerged in the space of only a few years in the early 1990s. In the wake of the collapse of Communism and the disintegration of the Soviet Union, a dominant paradigm for the transition to the market and democracy was quickly established. This approach centered around a by now well-known set of fundamental reforms designed to shift stagnating planned economies onto a fundamentally new path of development. The early reform programs called for structural adjustment policies – stabilization, liberalization, and privatization – that international financial institutions had prescribed to Third World countries since the early 1980s. Since postcommunist countries were pursuing a project of systemic change, these were not just conventional economic policies but represented a “politics of transformation” (Bruszt 1992) based on a strong belief in the market as a kind of meta-institution of social change. We refer to this conception as the *neoliberal discourse of radical reform* in order to underscore that we are not simply dealing with an application of neoclassical economic theory to the problem of transformation. Rather, neoliberal discourse contains general conceptions of institutional change and collective action as well as political and normative judgments that are quite independent of specific theoretical justifications. It is for this reason that neoliberal discourse can be justified with reference to such diverse

theoretical perspectives as the evolutionary tradition of the Austrian school, German ordoliberalism, neoclassical theory, monetarist doctrines, or simply common sense – and it may well be consistent with all of them. The Latin American debt crisis of the 1980s gave birth to an economic reform strategy which has become known as the “Washington consensus”¹ because of its strong backing from Western governments under the leadership of the United States and the international financial institutions. It refers to a set of supposedly uncontroversial theoretical and political assumptions about the composition and sequence of market-oriented reforms for economic growth. This discourse was powerful not so much on account of its specific content but because it structured the field of legitimate arguments, suggesting a direct and consistent link between scientific analysis and policy-making, and introducing the politically and morally potent distinction between radical reformers and conservatives (or populists).

In the international development debate, the concept of self-reliance was abandoned in favor of the primacy of international trade and capital, which in turn required far-reaching structural adjustments of policies and institutions to the rules of a globalized economy. In the theoretical debate industrial and trade policies fell out of favor as the whole field of development economics was called into question.² The barriers to development in the different regions of the Third World were diagnosed as a disease caused by state ownership, price controls, tariff walls, established distributional coalitions and rent-seeking behavior. The state lost its traditionally central role for modernization in what amounted to a “universal rediscovery of the market” (Tanzi 1997: 17). At the same time, the end of thirty years of state expansion was hailed as a “watershed in economic history” (De Vries 1986: 157).

It is therefore no accident that after 1989 the transition countries were incorporated into this consensus, even if they were not viewed as classical developing countries. The context for interpreting the failure of communism had thus been prepared. Communism’s collapse appeared as the final confirmation of the inevitable failure of state-centered modernization approaches based on public ownership, planning and protectionism. It was also widely seen as the ultimate

¹ The phrase is credited to John Williamson (1990). It was an attempt at the end of the Cold War battle between capitalism and communism to define a number of rather basic ideas of good economics, initially aimed at the specific conditions of Latin America. In hindsight, Williamson regrets that his concept mutated into a form of market fundamentalism in support of “radical reforms.” “My qualifications about this being an agenda for a specific part of the world at a particular moment of history were quickly forgotten, as the search for a new ideology, to endorse or to hate, was perceived to have succeeded” (Williamson 1999: 5). Williamson, however, is not entirely without blame. In consideration of the political climate in Washington, he had failed to incorporate the social dimensions and distributional consequences into his “one world consensus” (Waelbroeck 1998), even though he recognized their significance. For more recent revisions of his view, see Williamson 1997 and 1999. On the background and the flexible contents of the Washington consensus, see Bresser Pereira 1993: 18-23, 30-36, 65, n. 4 and 5; and especially Naim 2000.

refutation of development economics which had recommended a centrally planned distribution of resources and import substitution as appropriate instruments for combating poverty and inequality.

Yet it cannot be said that the neoliberal discourse was forced upon the postcommunist countries from the outside, even though the international financial institutions very soon assumed the mandate for overseeing the economic reform process in Eastern Europe. The “elective affinity” between East European reformers and Western advisors probably runs deeper than is often assumed. In order to understand the hegemonic position of this discourse, its theoretical implications, and especially its recent revisions, let us examine its major constitutive elements.

The Political Context for Neoliberal Discourse

The origins of fundamental market reforms in Eastern Europe date back to reform attempts in the late Soviet period and the reform program of the first postcommunist government in Poland.³ In the Soviet Union, radical reformers promoted by Gorbachev were able to gain the upper hand in the Communist Party after 1987. They had drawn their own lessons from the long history of failed attempts to make the planned economy more dynamic by introducing market incentives. The economic disintegration in the course of perestroika appeared to them as the final proof that the old system could not be reformed. “The time for gradual transformation has been missed, and the ineffectiveness of partial reforms has been proved by the experiences of Hungary, Yugoslavia, and China” (Yavlinski et al. 1990, quoted in Aslund 1995: 37).

The dismantling of the economics ministry, the paralysis of the party apparatus and finally the establishment of a sovereign Russian state seemed to create the political preconditions for the implementation of a “shock therapy” designed to effect the transition to the market in 400 or 500 days. The plan called “Transition to the Market” presented by the Shatalin group did not even contain the word socialism. A return to the methods of a command economy was improbable since there was no longer a functioning executive, while the legislature was immobilized, ultimately dissolving the unity of the Soviet state. It is no accident that programs like the Shatalin plan failed to mention the legal, administrative and institutional prerequisites for a market economy or to acknowledge the relationship between economic and constitutional reform. The politics of marketization and privatization was an attempt to use the institutional disintegration of the state and the weakness of politics as a means of eliminating those interest groups that still occupied the institutions of the old regime.

² See Hirschman 1981, the polemical diagnosis by Krugman 1995: 15-29, 81-84, and Waterbury 1999.

³ On what follows, see Aslund 1995: 27ff., Hough 1997: 103-139 and Nuti 1990.

In this respect, the Russian radical reformers were inspired by the strategies that had been developed in Poland since the summer of 1989. The Polish “big bang” was designed under the specific political conditions confronting the newly elected Solidarnosc government: how to translate electoral success into a decisive break with the past without having their own experienced personnel staffing the ministries. The new government turned to Western experts for help in designing a program of rapid and comprehensive market reform. In a short period of time, several plans for a shock therapy were drawn up, inspired by the now famous metaphor that an abyss can only be crossed in one leap. Jeffrey Sachs, one of the most prominent advisors of the Polish government and later the Russian government, saw shock therapy less as an economic strategy but rather as a political strategy for the dismantling of old structures. The initiative for the transition to a new society was entrusted to the beneficial effects of self-organizing markets. As Sachs reassured reformers, “[m]any of the economic problems solve themselves: markets spring up as soon as central planning bureaucrats vacate the field.”⁴

The strategy proposed by Sachs and Lipton and adopted by Poland’s liberal finance minister, Leszek Balcerowicz, initiated the new transition economics that brought together neoliberal political advisors and East European reform politicians. From a Western perspective this might not have been surprising. However, for East European economists it marked the final departure not only from Communist views, but also from the idea of market socialism. After the defeat of the Prague Spring the political intelligentsia of Central and Eastern Europe had abandoned reform socialist alternatives since “totalitarian communism” seemed unreformable. It had been proven beyond doubt that this order was incompatible with the introduction of market mechanisms and the institutionalization of even limited pluralism.

Against this background, it is understandable that the freedoms gained in 1989 were not risked in a new experiment in pursuit of a “Third Way.” “In the course of the anti-communist revolution in Eastern Europe public opinion turned against any form of socialism, market socialism included.” (Brus and Laski 1991: ii)⁵ In this light, the attractiveness of the works of Friedrich Hayek, Milton Friedman and Ludwig Erhard⁶ for Eastern European reformers is not

⁴ Sachs 1994: xiii; cf. Lipton and Sachs 1990. A similarly optimistic prognosis was issued by Aslund (1992: 90) at the start of the Russian reforms: “No doubt, a few million enterprises will be created in Russia alone during the first year of freedom of enterprise and free prices.”

⁵ This statement is especially significant since in past decades Brus had rehearsed all the arguments in favor of the compatibility of a socialist economy, market elements, and political liberalization (cf. Brus 1992). Now, however, he had come to the conclusion that the old debate between Oskar Lange and Friedrich Hayek had been decided both in theoretical and practical terms in favor of the Austrian School (Brus and Laski 1991: Chap. 5). On the dissolution of East European reform socialism during the 1980s, see Chavance 1993: 119-131.

⁶ Erhard is considered the architect of West Germany’s post-World War II “economic miracle.”

difficult to understand. The enthusiasm once devoted to socialist ideals was transferred to the market which promised to be more than merely a mechanism for efficient distribution but also the model of a “constitution of liberty” (Hayek) in which economic freedom is the precondition for all other freedoms.

Why it was market liberalism that came to fulfil East European needs for orientation can perhaps be best explained by identifying the different levels on which the neoliberal reform discourse has worked. Even before any theory of transformation was available, neoliberal doctrines offered a political strategy for the radical separation of political power and economic decision-making that would make the transition to the market irreversible. And even before this strategy could actually be implemented, it had a powerful normative message. “The moral attractiveness of the market as a foundation for freedom and prosperity [formed] a crucial part of its appeal in Eastern Europe.” (Glasman 1994: 200)⁷ In this sense, liberalism had conquered the normative and intellectual terrain in Eastern Europe before the international financial institutions brought to bear their institutional power in support of a specific reform strategy.

The new field of transformation studies emerging in the 1990s, however, took off only when IMF and World Bank stepped in and became involved in the liberalization and stabilization of the Polish and Russian economies. The model for the new research field was a comprehensive analysis of the Soviet planned economy commissioned by the Group of Seven in the summer of 1990. One year later, IMF, World Bank, OECD, and the newly created European Bank for Reconstruction and Development (EBRD) presented a final report on the Communist economic system that advocated a program of radical market transition (IMF et al. 1991). *A Study of the Soviet Economy* became the paradigm for the type of research that in the following years was applied to all societies intent on leaving behind their Communist past. At the same time, the study formulated the standard package of rapid and comprehensive reforms whose implementation more or less determined access to international loans. Price liberalization was designed to make production more responsive to scarcity and actual demand. Elimination of subsidies, privatization of state enterprises and the competitive pressure from a newly emerging private sector were expected to provide the impetus for the reorganization of enterprises. Liberalization of foreign trade was to undermine the position of domestic monopolists, while liberalization of capital flows was to attract foreign investors and know-how. The state’s task was to consolidate budgets, to depoliticize monetary policy, and to establish a legal order for the protection of private property.

⁷ The different criteria of success for neoliberal doctrines at scientific, policy and ideological levels are discussed in Pickel 1997a.

The political influence of this paradigm is powerfully illustrated by the fact that between January 1990 and April 1995, 24 transition countries followed a stabilization program along those lines. The attractiveness of the reform package was in part due to the promise that in principle all societies were capable of establishing the basic institutions of a modern market economy regardless of their specific history, the state of their economy, or the structure of their political system.

Neoliberal Discourse and the Break with Area Studies

What have been the implications of the dominance of neoliberal discourse for the *theoretical debate* about the dynamics of postcommunist transformation? Most noticeable was the break with area studies which since the late 1940s had provided the bulk of professional analysis of the region. It marked the end of one of the most significant academic innovations after World War II. Area studies were conceived as the interdisciplinary study of linguistically, geographically and culturally relatively coherent regions which had been all but ignored in university curricula. Their task was to inject foreign policy, and subsequently development policy, with politically relevant insights into non-Western countries and societies that were beyond the intuitive grasp of an Anglo-American or European observer. The research focus on cultural and historical particularities of a region was clearly at odds with the formal models of analytical social science and the abstract universalism of orthodox modernization theory. On the other hand, area studies provided the impetus for comparative modernization studies linking general developmental processes with the characteristics of a specific region. Soviet studies, comparative communist studies, as well as the comparative study of economic systems emerged in this context in the 1950s.⁸

The fields of Communist studies and Sovietology are too broad to pass any simple judgment on their achievements. In the early 1990s, however, their reputation suffered a serious blow which had far-reaching consequences for the emerging field of transformation studies. The “strange death of Soviet Communism”⁹ was followed by the demise of the sciences devoted to its study. The surprising end of the Soviet Union was interpreted as evidence for the meager analytical capacity of Communist studies. The most advanced analysis of the late Soviet economy had examined perestroika along the lines of earlier reform cycles, even if a

⁸ On the tensions between the institutionalization of area studies and modernization theory, see Wood 1968 and Wallerstein et al. 1996: 36. For the history of communist studies and its relationship to modernization approaches see Mueller 1998.

breakthrough to “comprehensive reforms” appeared more probable in the late 1980s. The scope for successful reforms appeared to be defined by the institutional legacy of the old system, the balance between reformers and conservatives, and the informal bargaining between the most important interest groups. The influence of the West and of international organizations was considered to be low (Hewett 1988: 373-91).¹⁰ In the political science literature as well, the dominant view was that the evolution of the Soviet system would be driven and constrained by the system’s well-known contradictions (Smith 1988: 335). In hindsight, diagnoses of this sort rested on weak foundations. As a result of an excessive preoccupation with the internal logic of power preservation and leadership politics, the critics charged, global pressures for change bound to break up the so-called socialist world system had been overlooked. Misplaced faith in the reformability of socialism had made a radical systemic break inconceivable.

Whether or not one agrees with this view, area studies in any event proved unable to influence the general approach adopted by the mainstream of transformation theory. “The competition between theory and area studies has come to an end – with the virtual defeat of the latter.” (Johnson and Keehn 1994: 18)¹¹ Since Eastern Europe was returning to a state of “normalcy,” there was little reason why in this context other laws should apply than in the West. Thus, as Peter Rutland (2001) suggests, Communist studies was replaced by a *theoretical conception of transition* that emphasized the universal logic of market economies. The point of departure for this conception was the logic of break and reconstitution, the simultaneous economic, political, and sociological dimensions of which Martin Malia has succinctly summarized as follows: “the Soviets’ total system ended in total collapse, which meant that at the exit from communism society was confronted with a total problem. Nothing could be salvaged from the old order; everything had to be replaced and rebuilt; the economy, the polity, the society itself.” (Malia 1992: 69)¹²

⁹ Thus the title of the special issue of *The National Interest*, No. 31 (1993), which in addition to a post mortem of Communism exposed the “sins of the scholars.” For self-criticism by Soviet and Communist studies scholars, see Fleron and Hoffman 1993, Solomon 1993, and Bence and Lipset 1994.

¹⁰ See also Hewett 1989: “Is Soviet socialism reformable? Yes, it is reformable, and is already reformed at a pace far greater than the conventional wisdom would suggest.”

¹¹ As Johnson and Keehn (1994: 20) have put it with reference to the new theoretical approach, “if the rest of the world is evolving to look like the democratic capitalism of the United States, then there is no longer any transcendent strategic reason for Americans to know anything about ‘the rest.’ American scholars need only continue to perfect mathematical proofs and the inevitability of the American ‘rules of the game’.”

¹² Strictly speaking, the concept of transformation in this view would be inappropriate, since it presupposes some kind of coherence as a starting point. “Governments were faced not so much with the task of

Neoliberal Discourse as an Interdisciplinary Framework

These themes were analyzed in an interdisciplinary framework in which the organizing potential of markets was assigned a central role. A revived theory of totalitarianism found in the ruins of Communism little more than disorganized masses, a moralistic civil society of dissidents incapable of serious political action, civilizational incompetence, and nationalist demagogues. Radical liberalization appeared as the only effective way of “detotalizing” the regime: “in the postcommunist situation it is the process of economic reform that governs the prospects for democracy” (ibid. 70). For much the same reasons, the political sociology of systemic change initially focused on the strategic conditions under which market reformers would be able to outflank the conservatives of the old regime and macroeconomic populists. Under postcommunist conditions economic liberalism and political liberalism became two sides of the same coin.

In the political, theoretical, and empirical context sketched above, neoliberal discourse established itself “as a basic paradigm for successful transition” (Fischer and Sahay 2000: 18) - a kind of metatheory of transformation that, in addition to a general theory of the market, supplied basic concepts for a political sociology of transformation. It also provided a basis for the explanation of diverging transformation paths and reform outcomes with operationalizable criteria of success and a quasi-experimental research design.

Atomized postcommunist societies appeared like a clean slate on which the economy could be restructured according to the model of general equilibrium theory, whose abstract axiomatics was converted into an axiology of political action. According to the assumptions of this theory, the coherent coordination of the decentralized activities of rational actors is assured. Given initial endowments, preferences, technologies and prices, such a model economy results in an optimal allocation of resources at equilibrium prices in which supply and demand are balanced. In addition, such an equilibrium fulfils certain criteria of welfare economics: in particular, no individual or collective actor could further improve their own position without negatively affecting the position of others. The academic reputation of this approach is based on its universalism and its mathematical precision, which reinforces the popular view “that there is a ‘scientific’ theory which demonstrates the efficiency of market economies” (Hahn 1992: 101).

The political economy of postcommunist reforms could thus be seen to imply that political actors create the preconditions of a “private ownership economy” (Debreu 1959) by creating private owners and by decentralizing price formation to the level of actors whose

transforming existing socialistic norms into new capitalist ones, but rather with a state of *anomie* (Dabrowski et al. 2000: 13).

interaction would create an optimal equilibrium in all markets. It is in this sense that one should interpret Jeffrey Sachs's statement quoted above that "shock therapy" is not so much an economic theory as a political concept for the establishment of self-organizing markets. In order to achieve an optimal allocation of resources corresponding to actual scarcities, it is necessary to establish incentives and sanctions anchored in individual interests. This political theory of the market required hard budget constraints for entrepreneurs and the determination of wages and employment regulated through labor markets. Perhaps even more important than this basic assumption was its correlate that required the elimination of all institutional, sociostructural, and normative barriers to the postulated individualism of social actors. To this extent, shock therapy was aimed not only at the devaluation of obsolete physical assets, but also at the devaluation of old "social capital" and collectivist expectations of subsidies and welfare state patronage.¹³ Systems theorists in sociology have interpreted this process as a delayed functional differentiation of a self-regulated economy from political power. In this sense, we can speak of a strategy of disembedding the economy and of individualizing social actors.

A further important element of the neoliberal discourse was a particular way of interpreting the political process of economic reform. Institutions and the strategies of actors were interpreted in functional terms with respect to their conformity to a generalized market model, which once again plays the role of a meta-norm. Politics was assigned the task of generating credibility and intertemporal consistency, thus providing the appropriate institutional framework for achieving a new equilibrium of expectations and routine behavior. The institutional configuration of transition countries appeared predetermined by a universal path of transition that implies the transfer of the basic institutions of Western capitalism. Not only economic institutions, but also institutions of social integration are assessed according to their market conformity. Policy making was viewed in terms of its contribution to liberalization and growth, requiring a technocratic policy style summed up in Margaret Thatcher's famous phrase, "There Is No Alternative" (TINA). The political process was seen not in terms of parliamentary procedure, consultations with stakeholders, and the art of compromise, but in terms of a technology of implementation. The ideal institutional setting for unpopular policies would thus be an executive largely insulated from parliamentary controls and interest group "pressures."¹⁴ A low level of institutionalization of collective interests seemed to provide ideal conditions for rationally designing the structure of the new system. Diverging views on the proper speed of liberalization were turned into a sharp division between two political camps, i.e. progressive reformers vs the

¹³ This was to be the central function of privatization (Sachs and Lipton 1990: 308; Sachs 1991).

¹⁴ For a survey of the burgeoning literature on the political preconditions for the initiation and consolidation

reactionary conservatives, which made it possible to present every political election as a choice between the new and the old system.

Neoliberalism as a Quasi-experimental Research Design

The dominance of the orthodox approach was also due to the empirical evidence and the quasi-experimental research design that demonstrated the scientific character of its doctrines. Since the beginning of the transformation process, the international financial institutions had been involved in modernizing the statistical systems of postcommunist countries, especially their shift to international standards. Transparent national statistics are “Articles of Agreement” for membership in the IMF and the OECD. Not surprisingly, the institutions representing the Washington Consensus used their privileged access to the relevant data and their reorganization to draw an authoritative empirical picture of transformation that by and large confirmed the fundamental assumptions of the orthodox approach.

To claim that the IMF manufactured a favorable empirical description would clearly be an exaggeration. The reconstruction of the communist-era data by the IMF and other IFI has revealed grave distortions of the net material product, especially the undervaluing of services in favor of material measures and an inflated productivity of investment. In addition to the already well-known informal economy, a sector of “value-subtracting production” was identified in which raw materials, energy, capital, and labor were used for the production of goods for which there was no demand. Finally, it must be granted that the introduction of international statistical standards has made it possible in the first place to make intra and inter-regional comparisons of postcommunist reforms.

The theoretical claims of the neoliberal discourse, however, went well beyond a mere systematization of the data. Already in the studies of the early 1990s before consolidated time series were available, firm causal relations were postulated between the initial conditions, particular policy measures, and the outcomes of transformation.¹⁵ Initially, studies were limited to more narrow monetary and fiscal variables that were analyzed using standard econometric methods. Subsequently, increasingly complex indices were constructed, including the degree of liberalization and other institutional variables. Finally, political and social indicators were incorporated into the quasi-experimental design, creating the impression of an empirically corroborated theory of transformation in which a relatively small group of structural and

of economic reforms, see Bönker 2001: Chap. 2.

¹⁵ See, for example, Lipton and Sachs 1992. The quasi-experimental design of transition economics subsequently also became a model for political science analyses, which however employed different explanatory variables.

macroeconomic variables were assigned the status of explanatory variables (Fischer and Sahay 2000: 15). On this basis, transition countries were divided into groups whose varying degrees of success could be explained in terms of the dominant causal influence of political commitment to the neoliberal reform strategy.

2. Anomalies and Alternatives

In spite of the hegemony of neoliberal discourse, political and theoretical alternatives to “market-induced modernization” were formulated right from the beginning of the transformation. Arguments from a Keynesian perspective in the early 1990s emphasized the “error of spontaneity” and “uncreative destruction” as dangers for postcommunist countries that might reduce their output, employment, and standard of living (Kregel et al. 1992). The systematic preference given to monetary variables at the expense of other economic indicators was in later years blamed for an unnecessarily long and deep recession (Laski and Bhaduri 1997). Others criticized the fatal effect of “do-nothing microeconomic policies” on restructuring (Amsden et al. 1994). An abstract, ideologically motivated separation between market and state, it was argued, ignored the constructive role of public policy or simply assumed the existence of a strong executive.

Alternatively, gradualist approaches advocated an extended and sequenced reform model in order to minimize the destabilizing effects of unemployment, asset stripping, and revenue losses and to achieve a fairer distribution of reform costs. Different variants of evolutionism from the start considered constructivist reforms as misdirected for ignoring historically and culturally evolved institutions. Institutional change, according to these perspectives, depends on decentralized information and trial and error at the local level rooted in existing institutions. Rapid privatization was viewed skeptically for two reasons. First, the formal transfer of property rights might not penetrate to the much more complex informal structures and processes in the enterprise. Second, the initial task was to establish an adequate institutional framework, unambiguous property rights, rational price systems and capital markets (Clague and Rauser 1992; Eatwell et al. 1995).

In light of these criticisms, political scientists suggested a different weighting for the central variables. The anti-state bias of the neoliberal discourse as well as its exaggerated fear of rent-seeking coalitions and interest groups of any kind was identified as the reason for the failure to recognize essential preconditions for successful reform policy. The consolidation of the state

was emphasized as a necessary precondition for stabilizing the new democracies. The representativeness of democratic political institutions is determined by electoral laws, the party system, and their openness for the articulation of social interests. A political strategy that is presented as being without any alternatives alienates political elites from social movements, associations, and trade unions which constitute the space for public debate (Przeworski et al. 1995; Linz and Stepan 1996).

Systems of interest representation and party systems, as well as general elite consensus and civil society activity, however, are closely connected with a country's history. A third area of transformation studies was thus devoted to the question whether the considerable differences between transition countries can be reduced simply to different initial conditions on an otherwise universal transformation path, or whether they point to fundamentally different values, systems of authority, institutional legacies, and organizational cultures that can only be understood in their particular sociocultural context. The study of such sociocultural constellations would then require the methods and approaches of historical sociology.

Some of these debates may well be outdated in the second decade of postcommunist transformation. However, major criticisms of the neoliberal discourse have been confirmed by the course of events. Moreover, it is important to note that even within the international financial institutions there has been a gradual shift towards an alternative position that calls into question the core of the neoliberal paradigm – a position more recently referred to as the “post-Washington consensus” (Stiglitz 1998a, 1999; Kolodko 1999). Three defining events prepared the ground for the emergence of the new paradigm since the mid-1990s: the extent and persistence of postcommunist economic and social crises; the Russian crisis of August 1998; and the outcomes of privatization.¹⁶

The Postcommunist Crisis

Following the start of reforms, almost all postcommunist countries experienced a drastic drop in output, production and employment. Even “the transformation ‘successes’ suffered output declines as deep of those of the Great Depression and recovered more slowly than the U.S. in the 1930s” (Gregory 1999: 2). Ten years later, it is hardly possible to call the group of “countries in transition” a growth region. At the turn of the century, their average growth continues to lag

¹⁶ A more comprehensive reconstruction of the debate would have to pay more attention to the Chinese experience. The “Sino-Soviet divergence” (Brus) has represented a major challenge to the neoliberal discourse and has featured also prominently in Stiglitz's critique of the orthodox approach (Stiglitz 2000). For neoliberal interpretations of the Chinese case, which emphasize its peculiarities, see Sachs and Woo 1994; Dabrowski et al. 2000: 6f.

significantly behind that of developing countries, and even more behind the newly industrialized countries, as well as behind the G7 states (IMF 2000a: 2, 26-30). Poland succeeded after seven years of reforms to surpass its 1989 GDP, followed only recently by Slovenia and Slovakia. Even the more successful countries needed almost a decade to reemerge from a surprisingly deep “transformational recession.” János Kornai, who introduced this phrase for characterizing the unavoidable losses of the initial years of reform, confesses his surprise at the duration and depth of these recessions (Kornai 2000: 21, 1994). It seems that a sustainable recovery actually may well take two decades.¹⁷

Interregional comparisons of per-capita GDP are similarly sobering. The Czech Republic and Hungary now rank alongside Gabon and Trinidad/Tobago, Bulgaria is at the level of Papua New Guinea, Russia ranks with Namibia, and Poland, first among radical reformers, with Botswana (World Bank 1997: 245ff). This is why postcommunist Eastern Europe and Central Asia are among those regions in the world which have experienced the sharpest increase in poverty. Between 1990 and 1998, the number of people living on less than one dollar per day increased from 7.1 million to 24 million (World Bank 2000: Tab. 1.1).¹⁸ If this is to be “the end of the transition,” one might ask whether it was worth the trouble.

A number of specific country developments were also at odds with the neoliberal view. Until 1995, Albania was considered a star pupil of the international financial institutions with annual growth rates between 8 and 10 per cent, a private sector share of 75 percent, and an apparently adequate degree of political stability.¹⁹ After the collapse of speculative pyramid schemes, however, the country quickly descended into anarchy. With Yeltsin’s reelection in 1996 Russia seemed to have successfully completed its transition to democracy and market economy, and thanks to IMF-bestowed credentials was able to return to international financial

¹⁷ To note the universal character of the output decline and the common problems is not to deny national differences. While all countries of Eastern Europe and the former Soviet Union experienced a severe transformational recession, some have recovered earlier and have performed better than others. Neoliberals have reacted to this differentiation, which clearly contradicts earlier universalistic claims, by attributing differences in performance to differences in the implementation of neoliberal prescriptions (Aslund et al. 1996; Dabrowski et al. 2000; Fischer and Sahay 2000). However, the evidence is thin. Quite aside from the methodologically questionable causal explanatory claims made by Fischer and Sahay as well as many other authors of the IMF and World Bank, it should be noted that even they are not able to show a clear relationship between balanced budgets and economic growth (Fischer and Sahay 2000: 9f.). The same is true for the relationship between privatization and economic growth (Gregory 1999: 7f.). What is more important, however, is a general point: In their quest for demonstrating the beneficial effects of particular reform measures, neoliberals tend to ignore “deeper” factors such as differences in initial conditions, state capabilities or the pull of the European Union. Yet such factors ultimately decide what reform measures can be implemented and how they operate.

¹⁸ On the methodological problems of measuring poverty in postcommunist countries and on the relationship between poverty and neoliberal policies, see Clarke and Holmes 2000.

¹⁹ See *Transition*, Vol. 8, No. 4, 29. Cf. Fischer, Sahay and Vegh 1996: 64.

markets: “The Russian economy appeared stronger than at any previous time during the transition period.” (OECD 2000: 34). Shortly thereafter the August crisis of 1998 hit, marking a major setback in the recovery process. But not only the problem cases among transition countries saw their economic recovery interrupted. The Czech Republic, for example, in the late 1990s had a stagnating economy and a simultaneously deteriorating political situation. Following the 1997 currency crisis, the rate of the registered unemployed tripled between 1995 and 2000.

These episodes not only document the unjustified optimism of reform advisors. They also indicate how fragile the postcommunist economies and societies still are. Data on growth rates, balanced budgets, and the size of the private sector may be valuable indicators, but they are not sufficient to assess the state of the transformation process. The numerous surprises of the last several years illustrate that economic indicators are too short term to furnish a basis for theoretically tenable conjectures about the trajectory of Eastern European transformation. The hopes they inspire are ominously reminiscent of the one-dimensional focus on the growth rates of planned economies and the resulting overestimation of their stability.

The Russian Crisis and the Dangers of Globalization

Growing doubts about the feasibility of the neoliberal program were evoked by the new dimension of the Russian crisis of August 1998 that demonstrated the vulnerability of postcommunist transitions to the changing fortunes of a globalized economy. The postcommunist states have pursued a relatively uncharted road of modernization through radical external liberalization, ignoring the lessons of West European post-war reconstruction and the East Asian developmental state.²⁰ They adopted a development strategy that was first introduced in the Latin American debt crisis of the 1980s – though they did so evidently with the goal of catching up with the West rather than the South. The loss of confidence in Russia as well as Eastern European financial markets sparked by the Asian crisis has raised the question whether the hasty liberalization of capital and currency movements contributed to further deepening the postcommunist crises.

The general rationale for world market-oriented modernization was based on a reassessment of the role of foreign direct investment and capital flows. Rather than viewing these in terms of dependence and unequal exchange, they were perceived as an opportunity to import technological and organizational know-how and to make up for insufficient domestic savings.

²⁰ Eatwell (1996) refers to the liberalization of financial markets and the corresponding development strategies as “the most important systemic transformation of the world economy since the establishment of the new world order at the end of World War II.” In this context, he emphasizes the new approach of the IMF.

The rapid growth of private direct and portfolio investments in developing countries and emerging markets in the early 1990s seemed to confirm this view. Thus the activities of international financial institutions were to be reduced to providing services and expertise to facilitate private capital flows. However, the positive relationship between inflowing capital and domestic growth goes hand in hand with the well-known risk of abrupt outflows. The investment behavior of short-term investors and creditors is not shaped by real economic trends but by diffuse general perceptions that are prone to wild fluctuations. The rapid outflow of capital may produce not only dramatic economic consequences but also enormous social costs and political instability. The Asian crisis was surprising and unsettling in so far as the countries affected, unlike Latin America in the 1980s, did not suffer from notorious balance-of-payment deficits, high inflation and excessive public spending. The lesson of this crisis, which resulted from general imperfections of capital and currency markets, was that in the face of systemic contagion, sound fundamentals may be a positive, but hardly a sufficient condition to be spared the effects of external crises.²¹ In liberalized financial markets, changed risk assessments can easily spread from one region to another.

If even comparatively stable economies can fall victim to such a crisis, how much greater are the risks for the countries in transition?²² In the case of the latter, the general problems associated with free capital markets are compounded by the specific problems of fragile banking systems and the inadequate regulatory capacity of weak states. In this context, one needs to ask whether the international financial institutions did not contribute to this situation with their inconsistent and ill-sequenced policy recommendations (Stiglitz 1998b: 12-16). As Peter Rutland (2001) explains in his analysis of the Russian situation, the IMF advised the Russian government to establish a market for government bonds in order to achieve a non-inflationary financing of the state budget and the depoliticization of monetary policy. This artificial construction could appear successful only as long as the high interest rates for Russian bonds attracted significant foreign capital. However, it was illusory to think that this was a way of closing the gap between public spending and tax revenues, “on the assumption that some mystical reform package would

²¹ “History suggests that a *laissez-faire* international regime may well hinder rather than help the process of transformation in Central and Eastern Europe,” as Eatwell (1996: 53) had warned. The criterion for successful reforms defined by Fischer (1998: 321), in contrast, redefines the problem as the solution: “sustainability also entails ability to withstand shocks.” See also Bhagwati 1998; Rodrik 1998, Eatwell and Taylor 1999. For an early careful assessment of the effects of the Asia crisis on the Eastern European countries, see Fries et al. 1998.

²² This is the crucial point that Slay (2000) ignores in his polemic against Stiglitz, where he follows the apologetic IMF on the Asian crisis. The IMF’s usually belated policy revisions referred to by Slay were always a response to earlier faulty diagnoses that however never were treated as such in order not to weaken the institution’s authority.

generate economic recovery before they fell due for repayment” (Rutland in this volume). The cooperation of Russian banks with foreign investors created a speculative pyramid in the market for government bonds and a bubble on the Russian stock market which exploded as a result of the Asian crisis (OECD 2000: 35-45).²³

The abstract liberalism of Western policy advice, even if unwittingly, thus contributed to the emergence of this situation. A view restricted to a handful of economic variables, false priorities and narrow goals failed to recognize the deeper causes of the Russian crisis. Due to a lack of interest in regional specificities, insufficient attention was paid to clientelistic politics and the informalization of the economy. Since the institutional environment, particularly in the financial sector, and the peculiarities of policy formulation were ignored, it was impossible to assess the potential effects of the standard reform program in the Russian context (Gould-Davis and Woods 1999: 18f.; Thornhill 2000). Finally, the Yeltsin government’s carefully nurtured image as the only true reformers and committed democrats was never seriously questioned.

Other countries in transition suffered somewhat less from the effects of this crisis. They too are forced, however, to adjust their reform policies to the portfolio strategies of international financial markets, even if those policies are not related to domestic needs. Unlike other countries with developed capital markets, transition countries do not possess the means to fend off speculative attacks. As a result, they may be forced to adopt the “perverse economic policy of raising interest rates, increasing taxes, and reducing government spending in the face of recession” (Krugman 1999: 65)²⁴

The Unfulfilled Promise of Privatization

A range of unanticipated consequences have emerged in a key area of transformation, that of privatization (Havrylyshyn and Odlin-Smee 2000; Nellis 1999; Rosenbaum et al. (eds.) 2000). The postcommunist privatization process is no doubt of a highly complex nature and does not lend itself to simple conclusions. The appeal of privatization policy, however, was precisely its apparent simplicity. The rapid introduction of private property rights was intended to separate the economy from the state and thus eliminate opportunities for rent-seeking, as well as create an entrepreneurial class interested in advancing market reforms and enterprise restructuring.

²³ The opening of the financial sector on the advice of the IMF is now also criticized by Aslund (1999: 22f.) as a sequencing error. “Ironically, Russia was flooded with foreign financing – primarily private but also intergovernmental – after serious attempts at economic reform had faded.”

²⁴ A notable exception was China, which on account of still existing capital currency regulations, was able to resist the devaluation pressure coming from other countries in the region. Despite their high external indebtedness, Poland and Hungary were less vulnerable to speculative capital flows since both countries

It became evident very soon that privatizing a planned economy was not simply a technical problem but a process in which there were different approaches and competing goals generating controversial results. There are widely differing views on the effects of privatization on employment, income distribution, and state finances. In the light of early experiences with privatization, Western advisors were soon forced to admit that their original assumptions had been somewhat naïve.²⁵ Western privatization methods, such as the British one, proved to be unworkable given the scope of the task, the amount of information they required, and the bureaucratic processes involved. The speed of privatization had to be balanced with considerations of efficiency and justice. Above all, it became clear that "the state" did not actually own the means of production. Different actors made competing de facto ownership claims on "collectively owned assets." The influence of ministers, local administrators, managers and employees turned out to be one of the major conditions determining to what extent governments were able to implement their goals.

The initial view of privatization as an act of redefining property rights has been superseded by a more differentiated conception that takes into account the institutional, political, and structural dimensions of privatization. This is significant in several respects. Privatization can obviously not be part of a shock therapy. None of the transition countries has successfully accomplished the rapid privatization of the state sector. A general survey of postcommunist privatization in the 1990s concludes that at best results have been mixed (EBRD 1999: 32-34, 119-121). There are very few tenable generalizations about the relationship between methods, speed, and sequencing of privatization policy, on the one hand, and the performance of privatized enterprises, on the other. The single most important factor determining the quality of governance in privatized enterprises was the regulative capacity of the state and its active role in restructuring and the creation of competitive markets.

The extended duration of the privatization process, which allowed for prior restructuring, is credited with the relatively successful outcomes in Poland and Hungary. In countries pursuing rapid destatization, on the other hand, the problems of an unreconstructed enterprise sector were concealed by fuzzy ownership structures in which inadequately supervised investment funds and state-owned banks were involved. Thus the Czech Republic had initially moved far ahead of its neighbors with the development of a formally privatized sector when in 1997 it was caught in a structural crisis that is seen largely as the result of a hasty privatization policy (Nellis 1999: 10-12).

had preserved capital controls and financed their current account deficits more through FDI than portfolio investments (*The Economist*, February 13th., 1999, 84).

In the worst case, privatization itself has become the major obstacle for the continuation of the reform process. The collapse of transformation in Russia and other Soviet successor states, it is now evident, has been brought about by the pathologies of reform policy. The redistribution of property created interest groups that supported Yeltsin's stabilization course. The new capitalist elites very much favored a tight monetary policy that assured them of large profits on high interest government bonds. They also favored rapid privatization which gave them access to the more profitable sectors of the post-Soviet economy. Contrary to general expectations, the new capitalists have not evolved into a strong pro-reform constituency (Hellman 1998). Rather, they have used their political influence to expand their strong market positions into monopoly positions. Their highest priorities were receiving tax breaks and privileged access to new areas of business. They have little in common with romanticized views of the postcommunist entrepreneur. "Profits rather than competitive markets are what capitalists seek to maximize" (Havrylyshyn and Odlin-Smee 2000: 5).²⁶

All this has led to paradoxical results. Postcommunist privatization has become the potentially most corrupt area of transformation, especially where the state has retreated and left the field to the unregulated struggle of interest groups. In some reform countries, re-nationalization is considered as a way of dealing with the most obvious pathologies of privatization. Jeffrey Sachs, one of the early proponents of the primacy of privatization, now advocates partial re-nationalization in Russia. What is generally missing are not private interests, but a "public service with the public interest in mind" (Nellis 1999: 25).

3. Towards a New Paradigm

The realities of postcommunist crises, unanticipated anomalies and diverging development paths have challenged conventional conceptions of transformation. Since the mid-1990s neoliberal discourse in particular could no longer avoid facing up to these realities,²⁷ without however

²⁵ Thus the self-critical diagnosis of Blanchard et al. 1993: 4-7, 37-80.

²⁶ This represents an empirical confirmation of the theoretical objections to the primacy of privatization formulated by Stiglitz (1994: 180). As Desai and Goldberg (2000: 15) add, "[t]he system of enterprise property rights has preserved firms as, above all, a source of rents." The theory of rent-seeking which is usually presented in this context is inadequate since it is based on a sharp (static) distinction between functioning markets and a self-interested bureaucracy. In the transition economies, on the other hand, there is the genuine dilemma of simultaneous imperfections in both the market and politics. As Poznanski shows in his contribution to this volume, foreign strategic investors are no panacea for this dilemma.

²⁷ "No one foresaw the scale and the collapse in output that occurred in these economies, or the extent of the erosion of fiscal revenues that stemmed partly from it," as Michel Camdessus admitted in 1994, without however acknowledging those authors who had predicted precisely that. Dabrowski et al. (2000, fn. 1)

accepting their theoretical implications. Attempts to account for the depth of postcommunist crises in the framework of neoliberal discourse remained ad hoc or descended into cynical apologies comparing “shock therapy” with chemotherapy administered to a terminally ill patient regardless of the risks involved. However, an international institution could not simply dismiss the anomalies produced by its universalistic policies by pointing out that all its members were entitled to “equality of treatment.”²⁸

The disappointment with neoliberalism in Eastern Europe coincided with similar experiences in other parts of the world. The results of almost two decades of “structural adjustment” in Latin America have been meager. The mishandling of the Asian crisis further undermined the IMF’s reputation. These developments precipitated changes in terminology that hollowed out the Washington Consensus from within. Demands for “good governance” and “second generation reforms” shifted the abstract opposition between state and market towards a more constructive view of the role of public policy in creating an adequate institutional environment for markets. This “more proactive approach [for] improving the management of public resources through reforms covering public sector institutions” was initially presented as the result of a pragmatic learning process – the lessons of which were to be implemented in cooperation with other UN organizations that had broader mandates than the IMF (IMF 1997: vi, 3).

This “pragmatic evolution” had of course more general implications. The concept of second generation reforms amounted to a de facto admission that radical reform policies had largely failed. This sparked heated debates within and between the international organizations, creating in turn a discursive space for the reassessment of postcommunist transformation policies. These ongoing debates clearly also have implications for the field of transformation studies. Theoretical critiques and heterodox approaches that for a long time were confined to the margins of academic debate have moved to the center of broader, interdisciplinary theorizing transcending the narrow conceptual repertoire of neoliberal discourse. Both the policy and academic dimensions of the debate will now be discussed in more detail.

simply adjust in an ad hoc fashion the optimistic goals of the neoliberal program announced at the start of the transition to actual outcomes. “We speak here of the transition *from* communism, not the transition *to* capitalism. It is clearly not the case that all the post-Communist countries have become, or will inevitably become, normal and successful capitalist market economies.” Such a lowering of standards clearly contradicts earlier universalistic claims. See Naim 2000 for an excellent reconstruction of ad-hoc revisions of the Washington Consensus in light of unanticipated outcomes – a classic example of what philosophers of science call immunization strategies.

²⁸ IMF 1999a, 259; Mussa and Sevastano 1999, 27f. However, the treatment, it should be noted, was not determined by all members but by the “Wall Street-Treasury Complex” (Bhagwati), and the flexibility in its application, especially with respect to Russia, by the U.S. administration.

The Washington Dissensus

The debate about “good governance” and “second generation reforms” emerging in the mid-1990s was not primarily a platform for cooperation between the international organizations but signaled a significant shift in discourse that brought to light unresolved disagreements between them (cf. also Murphy 1999). “Good governance” was the phrase employed by the World Bank since 1989 for adopting broader political conditionality in response to the disappointing results of structural adjustment. The call for “adjustment with transformation” and “second generation reforms” emerged in the African and Latin American contexts where conventional programs had produced widespread dissatisfaction (Gibbon 1993; Naim 2000).²⁹ This gave rise to concerns in the Eastern European context that the postcommunist crises might replicate the disappointing scenarios played out in other regions.

Indeed, an interregional comparison of the results of world-market oriented modernization seriously calls into question the wisdom of the “political economy of patience.” How much time should the populations of postcommunist countries reserve for the “intertemporal trade-off of macroeconomic reforms,” i.e. for a “short-term” loss of income for the promise of subsequent rewards? In Latin America, the region with the longest experience of world-market oriented reform policy, results have not been encouraging. In the 1980s income distribution became increasingly unequal, while by the end of the 1990s average real wages had fallen below their 1980 level. Reform policies neither provided a major boost to investment or domestic savings, nor did they significantly reduce budget deficits and external debt. The costs of disinflation, austerity, and structural adjustment can still be felt and have provoked a backlash against reforms and democracy (UN/ECLAC 2000; Stalling and Peres 2000; Karl 2000). For postcommunist countries much the same questions arise: how to reconcile the market, democracy, and trust in institutions in increasingly unequal societies; and how to avoid that the experience of postcommunist crises leads to cynicism and alienation from the formally established, but still unconsolidated institutions. These questions take on even more urgency in the postcommunist context since the communist state had established a level of expectations with respect to social infrastructure, employment, and social integration that had become unsustainable.

²⁹ The emergence of the World Bank’s good governance discourse was closely related to the fact that with the collapse of communism the distinction between authoritarian (pro-Western) and totalitarian (communist) regimes had lost the strategic rationale that Jeanne J. Kirkpatrick (1981) had given it for U.S. foreign policy. Political conditionality could now also be imposed on those authoritarian and corrupt regimes that had previously received loans in the context of the anticommunist strategy of containment.

The impetus for the emergence of a “New Development Paradigm” thus resulted from a whole series of negative experiences with structural adjustment policies: “the Washington consensus failed to deliver on its promise” (Rodrik 2000a: 2). None other than John Williamson, who is credited for having coined the phrase “Washington consensus,” identified its crucial weakness: “Policy needs to shift back from cutting a state that had become bloated to strengthening a number of key state institutions whose efficient functioning is important for rapid and/or equitable growth.”³⁰ The IMF’s adoption of concepts developed by the World Bank and other regional organizations did not resolve their more fundamental disagreements. On the one hand, the IMF interpreted “good governance” in a rather narrow fashion and focused almost exclusively on its impact on the development of the private sector. On the other hand, there were legitimate reservations concerning the IMF’s mandate and competence with respect to “modernizing the state” in transition countries. Other lines of conflict emerged with respect to the mandate of the EBRD. The neoliberal strategy favored by the US Treasury aimed primarily at opening up the resource-rich regions of Central Asia and Russia for private investors. By contrast, the European Commission sought to use the resources of the EBRD for a more ambitious strategy of institutional integration aimed at preparing the Central European states for membership in the EU (Robinson 1997).

The unresolved conflicts between IMF and World Bank³¹ about an adequate conceptualization of postcommunist transformations are illustrated by a revealing inconsistency in the World Bank’s 1996 World Development Report *From Plan to Market*. Whereas Part I explains reform outcomes along the lines of an orthodox IMF study strictly in terms of economic stabilization and different initial conditions, subsequent sections problematize the abstract universalism of privatization policies, emphasize the “differing cultures and traditions” of transition countries, and stress the importance of “long-term institution building” as well as a “competent and strong state.”³² The Report’s introduction already stressed that the postcommunist reform process differed from standard programs in its larger societal scope and in its path dependency from communist modernization achievements, however distorted they may have been. In explicit opposition to a *tabula rasa* approach, the transition to a market economy was to proceed “without throwing away the achievements of the old” (World Bank 1996: 123). Such a (re-)combination of new and old institutions also seemed to make alternative endpoints of

³⁰ Quoted in *The Economist*, November 30, 1996, 26, who with reference to the headquarters of the Inter American Development Bank, speaks about the emergence of a “Santiago consensus.”

³¹ Further on this, see *The Economist*, September 18, 1999 under the headline “Sick Patients, Warring Doctors.”

transition conceivable. “As transition proceeds, policymakers increasingly confront tradeoffs between a somewhat more laissez-faire market economy (as in the United States) and a somewhat more ‘social’ market economy (as in Germany or Sweden)” (ibid. 111).

As is customary in both institutions, inconsistencies and ambiguities of this kind were not publicly discussed and also went unnoticed by their critics on the left. The breakthrough to a new paradigm and a more open political debate is indicated by more recent discussions about a “Post-Washington Consensus” – a phrase adopted by the World Bank’s former chief economist, Joseph Stiglitz (Stiglitz 1998a; Burki and Perry 1998). This turning point is of central importance insofar as it elevates the theoretical reservations emanating from academic social science to the same institutional level from which neoliberal discourse has derived much of its power. The abstract universalism of economic reform programs in fact seems to have contributed to the postcommunist crises. As John Nellis, a coauthor of *From Plan to Market*, puts it: “The international financial institutions must bear some of the responsibility for the poor outcomes, since they often insisted on the primacy of economic policy” (Nellis 1999).

In order to break out of such a narrowly defined reform approach, the so-called “second generation reforms” set different priorities, based on a less technocratic conception of policy and institution transfer than that underlying the “rigid and dogmatic” standard approach. This broader conception was introduced in the late 1990s as the new paradigm of a *comprehensive development framework* (Wolfenson 1999; Pender 2001). This paradigm defines transformation as a problem of social change encompassing the administrative capacity of the state, processes of democratization, market reforms, and the evolution of new norms of social justice. In this view, the social, institutional, and organizational structures of postcommunist societies do not appear external to market processes but are endogenous variables that determine the institutionalization of functioning markets and a sufficient degree of social cohesion. In order to cope with the corresponding problems of interinstitutional integration, the role of local knowledge and actors becomes much more important than in the general application of a particular model of capitalism (Rodrik 2000b). The new paradigm is based on political conditionality, that is, a belief in democracy as the best framework for resolving social conflicts as well as for stimulating long-term equitable growth and the evolution of “good institutions.” Civil society is elevated to the “largest single factor in development” (Wolfenson 1999: 25f.).

The Comprehensive Development Framework has some obvious practical drawbacks since it leaves behind the quasi-mechanical approach of economic conditionality in favor of the

³² World Bank 1996: 87, 93; on the trade-offs of different privatization policies and speeds, see ibid. Chap. 3, 52.

institutional search processes available to a country in a specific situation. This entails a more complex research approach to effective reforms than the above-sketched macroeconomic empiricism of time series and quantitative growth models. Thus, for example, the relationship between policy variables and outcomes, i.e. between political action and economic trends, is extremely difficult to reconstruct without adopting far-reaching *ceteris paribus* clauses. The same is true for the problem of constructing institutional indicators which only rarely match the level of sophistication of the statistical methods applied to them. This is particularly relevant for unconsolidated systems with defective or informal institutions whose latent functions are not well understood. Analogies to nominally equivalent Western institutions are often misleading (as illustrated by the case of Russian banks). Finally, neither economic nor political conditionalities follow simple incentive-response patterns but are filtered through processes of negotiation, communication, and implementation. This also applies to those channels through which external influences affect the policies of reforming countries. The rhetoric of radical reformers as well as the negotiations between international financial institutions and reform governments are to a high degree infected by “cheap talk” and “babbling equilibria,” i.e. non-binding, non-verifiable, inconsistent or uninformative messages.³³ If the considerable complexity of such a situation is acknowledged, a strict methodological distinction between independent variables and dependent variables is no longer possible. The call for participation, empowerment and ownership implies the involvement of a large number of political and social actors who, while drawing on external expertise, will articulate their own goals and ambitions in the design, timing and sequencing of reforms.

Neoliberal critics of the Comprehensive Development Framework have argued that its long-term, holistic approach will achieve too little by aspiring to too much (Bhagwati 1999, 2000; Srinivasan 1999).³⁴ Moreover, they dismiss democratic, equitable, sustainable and comprehensive development as “buzz-words of ageing hippies.” The critics’ skepticism about more sophisticated reform strategies is illustrated by their use of “societal transformation” exclusively in quotation marks.³⁵ The political intention behind these polemics is evidently to defend the traditional intellectual agenda of the international financial institutions and to fend off calls for their cooperation in “UN-style forums.” The charges were directed above all against

³³ These and other methodological problems are discussed in Stallings and Peres 2000: 4-11. The “reform rhetoric-realization relationship” is discussed by Murrell 1995; cf. also Pickel 1997b.

³⁴ For a fundamental critique of the CDF from the left, see Standing 2000.

³⁵ Bhagwati and Srinivasan actually call for a return to the policy advice of 40 years ago – a time when the Soviet Union was seen as a threat on account of its growth rates. On the political background to the resignations of Joseph Stiglitz and Ravi Kanbur, the author of the *World Development Report 2000/2001*, see Beatty 2000.

Stiglitz's unusually open criticism of their failed policies in the postcommunist context. The critics' alternative is a return to the orthodox view according to which rapid growth is the master key to solving problems of development.³⁶

The conflict between institutional and market-induced reform strategies demonstrates that the conceptualization of postcommunist transformation has become the focal point and arena for a struggle over basic political priorities. The sharp tone of the debate is due to the fact that the opposing positions are not so much divided on the question of growth as such, but on the depth of reforms necessary to achieve it. Is it enough to create a general institutional framework for the market? Or is it necessary to place the institutional, social and human prerequisites for "high quality growth" (Rodrik 2000b) in the context of larger societal transformations?

It appears that the debate has so far gone in favor of the second position. Not only representatives of the Inter-American Development Bank assert that "the old reforms clearly need to be reformed" (Iglesias 2000). OECD and ODA as well have, at least on a rhetorical level, endorsed a comprehensive view that clearly suggests an interdisciplinary perspective: "to take more fully into account how markets, societies and governance interact and evolve" (OECD/ODA 2000: Chap. 5).³⁷ It is therefore no mere coincidence that the Global Development Network, established in late 1999 as a worldwide organization of research and policy institutes, is focusing on postcommunist reforms and has devoted its second major conference to the transdisciplinary theme, "Beyond Economics: Multidisciplinary Approaches to Development" (Gizpenc and Squire 2000).

Second Generation Theories: Shifting to Cross-disciplinary Approaches

For obvious reasons, the reorientation in the field of development policy has far-reaching theoretical and methodological implications for the field of transformation studies. Alternative approaches, hitherto confined to academic discussions without posing any serious threat to the hegemonic discourse of neoliberal reform, command increasing attention. Cutting-edge research focuses on the interactions between political, economic, sociostructural and cultural change. Earlier controversies, such as on shock therapy vs gradualism, have dissolved as transformation is

³⁶It goes without saying that this controversy also bears strong implications for EU enlargement. In line with the Comprehensive Development Framework, the EU's accession strategy rests on a multidimensional and institutional strategy of integration. In contrast, the orthodox alternative, which corresponds to the well known polemic of Václav Klaus (1994) against a supposedly over-regulated EU, boils down to a variant of a deregulated free trade zone which the United States favors in its sphere of influence (Dornbusch 2000).

³⁷ Significantly, the concepts of the CDF have also been incorporated into the new Poverty Reduction and Growth Facility (PRGF) that the IMF plans to implement in close cooperation with the World Bank (IMF 1999b). This development clearly contradicts conservative proposals to abolish the IMF or to reduce it to its "core activities" (see Feldstein 1998).

conceived as societal evolution that takes place on many levels and includes processes occurring at different speeds (Kornai 2000). Thus fundamental social science concepts that are not exclusive to any particular discipline have been incorporated into the theoretical vocabulary of transformation studies. These *thematic shifts* broaden the scope of analysis and are creating greater opportunities for cross-disciplinary cooperation. Philosophers of science would speak of a “progressive problem shift” that reintegrates the anomalies and ad hoc stratagems of an outdated paradigm (Lakatos 1978: 31-34).³⁸

With the new perspective comes an increased awareness that there are no global modernization imperatives that automatically would return the countries liberated from the shackles of communism to the “normal world.”³⁹ The postcommunist countries, forced to integrate into the world market from a state of backwardness, are ill-prepared for the forces of globalization. “Normalization” in this context may well imply what Adam Przeworski predicted soon after the fall of the Iron Curtain, i.e. that East European societies “too will confront the all too normal problems of the economics, the politics, and the culture of poor capitalism” (Przeworski 1991: 191). This poses the traditional development problem of how to slow down the trends towards structural heterogeneity, social segmentation, and peripheralization.

As the available empirical evidence shows, postcommunist political transitions also do not follow a universal path to liberal democracy. The much-cited “third wave” of democratization that portrayed the revolutions of 1989 as part of a global trend spanning from South Africa to South East Asia, may well have turned into a reverse wave (Diamond 1996: 20-37). Accordingly, the typology of political orders has been extended to include imperfect, fragile, delegated, etc. democracies. The most fruitful approach employs a comparative perspective paying close attention to the specific prehistories of postcommunist transitions as determined by different degrees of totalitarian sclerosis, the position of the elites in the ancien regime, the mode of political regime change, and other variables. The sterile opposition between area studies and comparative method has been transcended by conceptualizing postcommunist changes as particular versions of the more general problems of development and democratization.⁴⁰

³⁸ The explanatory problems and concepts developed in this problem shift provide the setting for the contributions to Bönker, Müller, Pickel 2001. They demonstrate that the call for cross-disciplinarity is no longer an abstract postulate but has already become a reality shaping the most fruitful approaches in the field.

³⁹ From an orthodox modernization perspective, this is argued by Mouzelis 1993 and Fukuyama 1993; for a neo-modernization perspective see Müller 1995 and Tiryakian 1995.

⁴⁰ The most ambitious attempt in this respect has been undertaken by Linz and Stepan 1996 who combine an interregional comparison of postcommunist transformations with an interregional comparison of transitions from authoritarianism to democracy in Southern Europe and Latin America.

A broader perspective on the functioning of markets has established that markets do not generate an autonomous development dynamic and cannot be reduced to the price mechanism, thus undermining a fundamental assumption of neoliberal discourse. The thesis of market-induced modernization, according to which liberalization and privatization initiate a virtuous circle of social and political self-organization has been replaced by sociological insights into the non-economic preconditions of markets. This means that a number of variables from which the universal model abstracts need to be introduced into a dynamic perspective. It is interesting to note that the theoretical reasons for this were presented not by sociologists, but by eminent proponents of general equilibrium theory who recognized that the strict conditions of the model are even more unrealistic in times of rapidly changing, uncertain, and contradictory expectations. Imperfect markets, asymmetrical information between insiders and outsiders, privatizations under conditions of imperfect competition, and infrastructural problems are instances that typically give rise to pathologies. The most valuable insight that can be derived from general equilibrium theory is the negative point that under conditions of postcommunist transitions markets cannot properly fulfil their coordinating functions. Somewhat ironically, pure economic theory predicted “for purely prudential reasons” the transition to a mixed economy; “that the state will play an important role seems inevitable.”⁴¹

This fundamental theoretical argument concerning the political and institutional embeddedness of transition economies is confirmed by empirical research. In the EBRD’s retrospective of the first ten years of transition, two entire chapters are devoted to the positive functions of the postcommunist state. The conventional wisdom of the political economy of reforms is called into question in several respects, in particular by strongly emphasizing the need for the institutional and political embedding of markets. “The evidence now shows clearly that the central lesson of transitions is that markets will not function well without supporting institutions, a state that carries through its basic responsibilities and a healthy civil society.” (EBRD 1999: 5)⁴²

The rediscovery of markets as institutions converges with the conclusion in the political science literature that pure market economies are not compatible with the formation of sustainable democracies. All modern democratic societies are mixed economies insofar as they establish legal norms for competition and property rights, have a sizable public sector,

⁴¹ Hahn 1992; Arrow 1995: viii; Intriligator 1997. The limited relevance of General Equilibrium Theory discussed by Hahn is consistent with the theoretical objections underlying Stiglitz’s (1994) critique of the Washington Consensus.

⁴² “Liberalization and privatization will not, *per se*, automatically lead to a demand for institutions to support well-functioning markets,” as the report subsequently notes (EBRD 1999: 7).

institutionally regulated class conflicts, and use tax and social policy to modify the distributive outcomes generated by markets (Freeman 1989). Precisely because these are not mere “mechanisms,” Linz and Stepan sum up this “set of socio-politically crafted and accepted norms, institutions and regulations” in the concept of “economic society,” which they assign a central role in the process of democratic consolidation. Successful democratization – in addition to civil society organizations, free elections, rule of law, and a rule-governed state apparatus – also depends on the degree to which such an economic society can be established (Linz and Stepan 1996: Chaps. 1 and 11).

In fact, mixed systems have emerged in all postcommunist societies (EBRD 1999: 121-123). General government expenditure as a share of GDP ranged in 1998 from 46.4 per cent in Hungary and 41.1 per cent in the Czech Republic to 37 per cent in Russia, 29.5 per cent in Ukraine, and below 20 per cent for most Central Asian CIS members. Thus, a high level of state intervention in the economy does not indicate lack of reform commitment. Hungary is near the top of the state intervention index of the EBRD while at the same time being one of the most consolidated transition societies. We would argue that transformation in the Central European countries has been relatively successful and occurred without fundamental policy reversals precisely because institutions for social integration were maintained and the state did not collapse. A high degree of social cohesion and a capacity for political compromise seem to be crucial preconditions for a sustained reform policy and the formation of coherent institutional systems.

We can summarize the problem shifts in transformation research discussed so far as follows. The Hayekian dilemma of simultaneously introducing the market and democracy was transformed into an opportunity: successful reform implementation and the avoidance of policy reversals is dependent upon the inclusion of large sectors of the population and consultation with interest groups (Hellman 1998; EBRD 1999: Chap. 6). For this reason, the renewed attention focused on the role of the state does not augur a return to the old authoritarian developmental state – a state model that is in fact much closer to the neoliberal ideal of an insulated executive capable of implementing radical reforms without having to take into account organized social interests. Recent transformation research therefore has devoted particular attention to the combination of market requirements, state capacity, the democratic openness of the political process, and civil society activity. The interplay of these elements is the common point of reference for more complex explanations of diverging transition paths and for different variants of political capitalism. In this view, “state capture” is a special case, and the concept of “partial reforms” takes on a new meaning. In the absence of an adequate regulatory environment, with underdeveloped representation of political interests, and a non-transparent decision-making

process, privatization and liberalization can be hijacked by old and new interest groups that come to dominate the political process and state institutions. The culture of corruption, clientelism, distrust, and political cynicism so widespread under Communism can therefore survive under new conditions.

Capturing the actual forms of interaction between economic, political, and social reforms requires an appropriate analytical framework. Concepts such as trust, networks, social capital, civil society and national identity that emphasize the problem of social cohesion in the context of political polarization, ethnic divisions, and social exclusion are more suitable for the problem of institutional consolidation. Analyzing the demonstration effects of Western countries on the reform states calls for complex models of institutional transfer as developed in organizational sociology that can show how external models interact with local conditions. Approaches from the area of cultural sociology can shed light on established value systems that provide a source of legitimacy for the development of a complex social order.

Concluding comment

We have argued that a paradigm change is occurring in the field of postcommunist transformation. From our perspective, a transformation paradigm has three distinct dimensions. In a first dimension, it informs social scientific work by demarcating fundamental problems and problem contexts for research. In a second dimension, it informs policy-making, especially in terms of fundamental reform approaches and programs. In a third dimension, it informs ideology and political action by embodying fundamental values and visions of social order. A paradigm change is therefore a cognitive as well as a political process. According to our analysis, the social sciences in the 1990s have produced a redefinition of what are the fundamental problems of transformation and significantly broadened what should be considered the relevant problem context. The leading international policy-making institutions have, to varying degrees, modified and reconceived reform approaches and programs. A paradigm change in ideological terms has at least become conceivable as neoliberal values and visions of global order are called into question or rejected by a growing number of social actors. This is encouraging for social scientists who have contributed to the paradigm change and whose past and future contributions can provide crucial resources for alternative policy approaches and political visions.

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