The Post-Communist State and Capitalism in Transition: Towards a Complementary Relationship

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ABSTRACT:

This paper claims that the post-communist state has been constantly assailed by the dominant liberal paradigm of the post-communist transition. It is rather questionable whether the administered advice of deregulation, liberalization, and 'down-sizing' the state has had a positive effect on the macroeconomic performance of post-communist countries. For both theoretical and policy-related practical purposes, the post-communist state and transition capitalism ought to be considered complementary. Further post-communist reforms have to take into account the existence of complementarity between major institutional domains of modern capitalism to avoid derailment and considerable growth-reducing impact. The theoretical discussion in the paper is supported by the comparison of Polish and Ukrainian transformation experiences.

In my view, some, and perhaps much of the advice now being offered the Central and Eastern European states, proceeds from a view of the so-called capitalist or free-enterprise economies that bears no relation to their reality. Nor would these economies have survived if it had. What is offered is an ideological construct that exists all but entirely in the minds and notably in the hopes of the donor

John Kenneth Galbraith (1990: 8).

The basic premise of this paper is that the state as a research problem has been abandoned during the first decade of post-communist studies, whereas the state as a form of political association and a distinct set of political institutions has been regularly assailed by the vast majority of commentators and scholars of the post-communist transformation. It is contended that the reason why the state has not had a good press recently is that the dominant paradigm of the post-communist studies – the perspective from which most observers and practitioners view post-communism – has been constructed in terms of discourses of liberalization, practices of the New Right, and policies of neo-liberalism. Drawing its ideological inspiration from the classical liberal theory of *laissez-faire* that postulates that the government of a state should have no control at all over economic matters, and especially from the writings of the twentieth century conservative and libertarian theorists, the dominant transition paradigm has been primarily focused on the design and implementation of various liberalization policies broadly aimed at assuring minimal government interference. The problem of the post-communist state has been largely removed from the academic research agenda, since the 'policy-relevance' of the issue is widely considered of secondary importance. It has often been explicitly alleged that by dismantling or, at least, by limiting and 'down-sizing' the post-communist state, one would greatly expand and enhance the mechanisms of the self-regulating free market and, thus, could encourage economic growth and boost the overall macroeconomic performance of the post-communist countries. Thus, in most of the conventional writings, the clearest dichotomy is between the (post-communist) state and the (post-communist) market. The less you have of the former, the more you have of the latter. That, in turn, is assumed to generate (more) prosperity and (better) social welfare.

This paper questions the orthodox dichotomy and critically examines the relationship between the post-communist state, market, and capitalism in transition. By considering and comparing the divergent post-communist pathways of Poland and Ukraine, I argue that the conventional transition story cannot provide an adequate explanation for different outcomes of transformation: there appears to be no systemic relationship between changes in government size and economic growth. Moreover, the entire view of the post-communist transformation as a transition 'from plan to market' is particularly simplistic and reductionist.

Consequently, I outline an alternative concept of the post-communist transformation which is aimed at exploring a potential complementarity between the state and central institutional forms of modern capitalism. I claim that by conceptualizing the post-communist political economy in terms of a comparative 'varieties of capitalism' approach, one will be able to develop a satisfactory explanation for the divergent post-communist outcomes and to provide a more realistic interpretation of the political-economic dynamics of this historical period. It is contended that an alternative approach towards the post-communist state and capitalism in transition would be more socially applicable and policy-relevant than the dominant liberal transition paradigm.

THE DOMINANT TRANSITION PARADIGM

The start of the post-communist transformation, the collapse of Soviet power, and the end of the Cold War in 1989-1991 led a number of observers, most notably Francis Fukuyama, then Professor of Political Science at George Mason University (Virginia, U.S.), to declare that the history, as it had been known before, ended by an unabashed victory of economic and political liberalism and the total exhaustion of viable systemic alternatives to Western liberalism (1989). Given the prevalence of liberal ideas and ideational constructs at the time of its conception, the dominant transition approach has been based from the very beginning on the principle of individual freedom, the pursuit of which is considered to be the ultimate goal of a society according to the liberal doctrine. The dominant transition theory has been inspired by the classical liberal theory of the nineteenth century and by the school of neo-classical economics based upon it. Furthermore, the conventional post-communist transition paradigm draws most of its assumptions from a range of twentieth-century conservative and libertarian theorists. It is especially indebted to the writings of Ludwig von Mises, Friedrich von Hayek and the Austrian school of political economy, to the free market ideas of Milton Friedman and the Chicago school, as well as to the Virginia school of public choice theory founded in the 1960s by J. M. Buchanan and Gordon Tullock, two libertarian right-wing academics deeply suspicious of the state and 'over-supplied' government bureaucracy. Thus, mainstream post-communist theorists stress the efficacy of the free market for economic and political freedom and the significance of competitive polyarchy (or liberal/pluralistic/parliamentary democracy) for protecting the rights and liberties of individuals (see, for example, Kornai 1990, 1998; Lipton and Sachs 1990; Gelb and Gray 1991; Fischer and Gelb 1991; Sachs 1993; Balcerowicz 1995; Åslund 1995, 2001; Crawford 1995; World Bank 1996, 2002; Klaus 1997; Rose, Mishler, and Haerpfer 1998; Bunce 1999; EBRD 1999, 2003).

At its core, neoclassical economics sees the market as an institution allowing maximum scope for voluntary exchange between utility-maximizing individuals and hence for the efficient allocation of scarce resources. It emphasizes the role of rational expectations (i.e. competitive maximizing behaviour) in decision-making and the natural rate of unemployment in equilibrium growth. Neoclassical economic theory postulates that no state demand-management intervention is effective, whilst other types of the state intervention into economy should be strictly limited. The limits of the market inhibit the range of choice which enhances social welfare (i.e. the sum of individual preferences). According to the monetarist and supply-side supplements to neoclassical economics, growth can only be enhanced by influencing supply and removing market restrictions of all sorts, for example, by restricting the growth of money supply to control inflation and improve economic stability, cutting taxes and welfare benefits to boost incentives, or diminishing the ability of trade unions to obstruct the workings of a free labour market. In a detailed survey of neoclassical political economy, Caporaso and Levine (1992: Chapter 4) have demonstrated that in the neoclassical idea politics is subsidiary to the efficient exchange within markets, as it becomes an alternative instrument to achieve what the market fails to efficiently achieve. The state enters the stage only to fix market failures. It is allowed to correct market deficiencies (i.e. non-priced 'externalities'), provide public goods (e.g. roads, primary education, property rights, and courts of justice), and guarantee competition (e.g. break up monopolies).

The central thesis of the dominant liberal post-communist transition theory argues that, in order to approach the Western level of prosperity, post-communist countries must adopt the economic model of the free enterprise economy epitomized in the Anglo-American system of competitive capitalism and limited government intervention.[1] Assuming that all the deficiencies of state socialism as well as of any other non-Western economy stem out of pervasive government involvement and control over all important aspects of economic activity, prices, and international trade, and of extensive government ownership of productive assets, the fundamental solution prescribed by mainstream theorists is two combined policy reforms, such as macroeconomic stabilization and structural adjustment. The first reform that post-communist countries are set to introduce in order to achieve macroeconomic stability include cutting public spending and reducing excessive money growth. The second policy reform involves changes in the basic structure of the economy to be achieved by providing stronger incentives for productive economic activities and international trade based on comparative advantage. The most important element in the structural adjustment stage is a reduction of the extent of government involvement in the economy and an increase in the role of markets. Both policy reforms are regarded as integral in fostering the self-organizing system of the market: macroeconomic instability is believed to be caused by excessive fiscal spending and money growth, which follows directly from the state ownership and control over the economy; and to reduce the state involvement into the economy one has to engage in structural reforms (for this textbook example of the orthodox transition package, see Yarbrough and Yarbrough 1997: Chapter 21).

The combination of macroeconomic stabilization and structural adjustment are said to result in the unleashing of markets – 'the basic enabling reform from which all the potential benefits of transition follow' (World Bank 1996: 7). In the words of Milton Friedman, whose dreams of a 'night watchman state' have been taken into account by new post-communist elites:

> The transition to freedom in Eastern Europe cannot be accomplished overnight. The formerly totalitarian societies have developed institutions, public attitudes and vested interests that are wholly antithetical to the rapid creation of the basic

[1] Here I focus primarily on the economic branch of the dominant liberal transition paradigm. Political and societal branches of the conventional transition model (i.e. democratization and civil society-building) are beyond this paper's scope.

> economic requisites for freedom and prosperity. These requisites are easy to state, but far from easy to achieve … The one thing that is common to all of them is a drastic reduction in the size and role of the government … Government must be narrowly limited to its essential functions of maintaining law and order, including enforcing private contracts; of providing a judicial system to adjudicate differences in the interpretation of contracts, and to assure that laws against theft, murder, and the like are applied justly; of establishing the rules of the game, including the definition of private property. Such a reduction threatens almost every powerful vested interest in the current society … However, the talk about 'the enormous costs of moving to a free-market economy' is much too gloomy. There is no reason why total output cannot start expanding rapidly almost immediately after the totalitarian restrictions on people's activities are removed (1990: 6-7).

Operationally, the standard model that has stimulated the orthodox transition approach was the structural adjustment package (often called stabilization programme or SAP) of the International Monetary Fund (IMF) and its sister organization – the International Bank for Reconstruction and Development (the World Bank) that had been tried first in underdeveloped Latin American countries in the 1980s.[2] The SAP model has been redesigned in the late 1980s – early 1990s as a set of key policy measures aimed at shifting non-market societies towards liberal capitalism. Dubbed the 'Washington consensus' because of the location of the two international financial institutions in the U.S. capital city (Williamson 1990), the orthodox transition approach has called for ten policy reforms, which stated in a more detailed manner how to achieve macroeconomic stabilization and structural adjustment through deregulation, privatization, sectoral restructuring, price liberalization, fiscal consolidation, and financial and trade integration with the world. The Washington consensus policy measures have become a general prescriptive mechanism to ensure the transition towards what international financial institutions see as a standard free market economy.[3] According to John Williamson, the author of the concept, the orthodox reform package could be considered a generally applicable 'universal convergence programme' that summarized 'the common core of wisdom embraced by all serious economists' (1993: 1334).

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[2] In turn, the structural adjustment programmes themselves go back to the monetarist theory of Milton Friedman and, more specifically, to 'monetarist' economic policies of ruthless cuts in government spending, social security, and real wages, instituted in Chile after the military coup d'etat in 1973 by the dictatorship of General Pinochet. For a review of SAPs, see Killick (1982) and Ghai (1991).

[3] The original 'Washington consensus' has included the following measures: (1) fiscal discipline should be imposed to minimise the overall budget deficit (including, in addition to the central government deficit, also those of the local governments, of the state enterprises, and of the central bank) of about 2 per cent of GDP; (2) priorities in public expenditures should be redirected from politically sensitive areas (i.e. administration, defence and subsidies) towards primary education and health, and basic infrastructure; (3) a tax reform should be implemented, with lowering the tax burden, broadening the tax base and simplifying tax administration; (4) financial liberalisation should be aimed at market-determined but moderately positive interest rates; (5) the exchange rate should be unified and market-determined; (6) trade should be liberalised and outward oriented, and import tariffs should be reduced to a uniform low tariff of no more than 10 per cent; (7) foreign direct investment should not be restricted and foreign firms should be allowed to enter freely and compete with domestic firms on equal terms; (8) state-owned enterprises should be privatised; (9) government regulations of economic activities should be abolished and maintained only to ensure safety and environmental protection; (10) property rights should be secured without excessive costs, and made available to the informal sector (Williamson 1993, 1994).

As the post-communist state liberalizes the economy in transition, it is forced to undergo a radical process of 'slimming down' and 'shrinking'. The World Bank's report *From Plan to Market* published in 1996 is a good example of the orthodox neo-liberal policy advice concerning the role of the state under post-communism:

> The transition from plan to market calls for a whole-sale reinvention of government. The state has to move from doing many things badly to doing its fewer core tasks well. This means government must at once shrink and change its nature … First, the role of government in producing and distributing goods and services must shrink dramatically. Public provision must become the exception rather than the rule. State intervention is justified only where markets fail – in such areas as defense, primary education, rural roads, and some social insurance – and then only to the extent that it improves upon the market. Second, government must stop restricting and directly controlling private commercial activity and extricate itself from intimate involvement in the financial sector, focusing instead on promoting macroeconomic stability and providing a legal and institutional environment that supports private sector development and competition. Finally, instead of providing generous guarantees to secure adequate living standard for all, governments need to foster greater personal responsibility for income and welfare (110).

Following a public choice theory argument that politicians are not less 'rational' or selfish than entrepreneurs and that the polity is, like the economy, is driven by self-interested individual actions (e.g. see Downs 1957; cf. Niskanen 1971; Buchanan and Tollison 1972), the World Bank also called for the restraint of government powers and tight control over public spending and bureaucracy:

> Where markets fail, a case-by-case judgment is needed on whether government provision – or the regulation or funding of private provision – can do better. Governments, too, may fail: interventions may be guided by political objectives, be poorly implemented, create vested interests, or give rise to rents and corruption. Well-intentioned government intervention to correct market failures may prove even worse than suboptimal private provision. In a market economy the burden of proof regarding public intervention lies with the government (World Bank 1996: 111)

Notwithstanding the lack of any evidence to suggest the existence of some systemic relationship between changes in government size and economic reforms, one of the world's most powerful economic organizations alleged that in the post-communist context the smaller the size of government is, the better the transition performance ought to be:

> General empirical studies relating levels of government spending to economic growth yield few robust conclusions. In transition economies, however, there are stronger grounds for thinking that large governments will hurt economic performance: government spending, especially at high levels, tends to be quite

inefficient and, as a result, to contribute less to growth than in market economies; also, financing government programs is costlier and poses a greater risk of inflation (World Bank 1996: 113).

It is very symptomatic in this regard that in most of the post-communist world the Washington consensus project of transition through deregulation, marketization, and privatization was understood and designated from the very beginning as a programme of 'de-statization', i.e. the withdrawal of the state (*rasgosudarstvlenie* in Russian; *rozderzhavlennia* in Ukrainian). In the following section we examine whether there exists the alleged positive systemic relationship between 'de-statization' and macroeconomic performance.

TOWARDS SLIMMER GOVERNMENT AND BETTER PERFORMANCE?

To evaluate how the prescribed neo-liberal policy of 'slimmer and better government' has worked in the post-communist context, we turn towards the empirical examples of Poland and Ukraine. It is contended that despite Ukraine's much more radical liberalization and slimmer government, the country's economic and human development progress in the 1990s has been poorer than that of Poland, a country that retained a large state. However, I also argue that it is impossible to establish some clear systemic relationship between the size and scope of the state and macroeconomic performance. My claim is that the dominant neo-liberal transition approach with its 'de-statization' thesis fails to provide an adequate interpretation of the state-market relationship and of its effect on the outcome of the post-communist transformation.

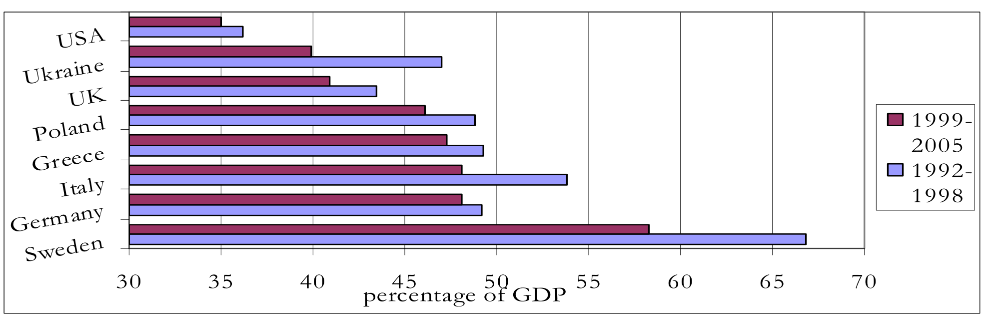

Figure 1. The size of state in Poland and Ukraine: an international comparison, 1992-2005 (general government sector expenditure as share of GDP, annual percentage averages per period)
Source: Author's calculations on the basis of USSC (2000, 2002, 2003, 2004a); NBU (2004); World Bank (1999); PSCO (1996, 2000, 2002, 2003, 2004a); Easterly and Sewadeh (2001); UN (2004); OECD (2004a).

First, we consider the reduction of the size of government under post-communism in the two countries. Figure 1 compares the average sizes of the general government sector expenditures between 1992 and 2005 in Poland and Ukraine, and in a number of representative Western countries (high-income member states of the Organization for Economic Co-operation and Development). Figure 1 indicates that throughout the entire post-communist period the

Ukrainian state has been shrinking in a far more radical manner than its Polish counterpart. Moreover, since the late 1990s, the size of the Ukrainian state has been as small as in some liberal market economies. By contrast, the size of the state in Poland has remained on a par with that of Southern Europe.

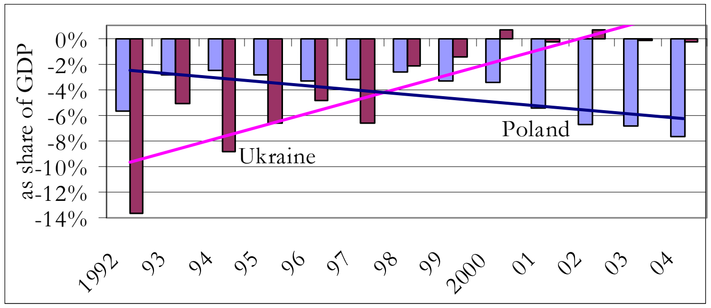

Figure 2. Government budget deficit levels in Poland and Ukraine, 1992-2004 (the general government sector expenditure balance as share of GDP, annual percentages and trends)
Source: Author's calculations on the basis USSC (2000, 2002, 2003, 2004a); PSCO (1996, 2000, 2002, 2003, 2004a); Easterly and Sewadeh (2001); NBU (2004); OECD (2004a).

Second, the larger Polish state has also been much costlier than the Ukrainian one. Figure 2 shows that between 1992 and 2004, the average general government sector's budget deficit in Poland amounted to 4.4 per cent per year, whereas the corresponding figure for Ukraine was 3.8 per cent. Moreover, the lower level of public spending under post-communism in Ukraine has been increasingly more balanced, reaching around 0 per cent deficit figure in the early 2000s. By contrast, the situation concerning Poland's public finances has been steadily worsening: in 2004 the general government sector budget deficit approached 8 per cent of the country's gross domestic product.

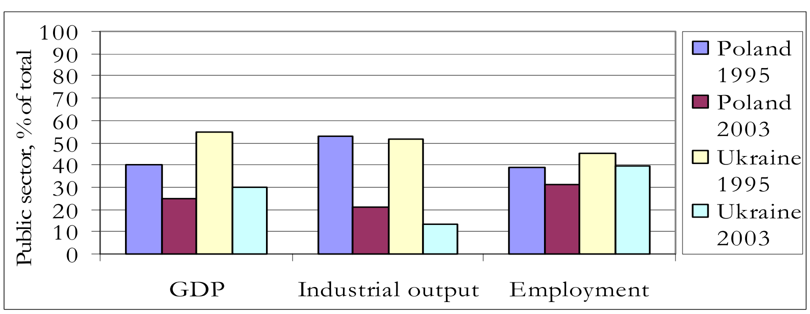

Figure 3. The scope of state in Poland and Ukraine, 1995-2003 (public sector as share of gross domestic product, industrial sector, and workforce)
Source: Author's calculations on the basis of USSC (2000, 2002, 2003, 2004a); PSCO (2000, 2002, 2003, 2004a, 2004b); EBRD (2003).

Third, in the course of transformation the scope of the two public sectors has been substantially reduced as well. One has to mention that at the end of the 1980s, in contrast with other state socialist economies, the Polish economy was already characterized by a substantial share of private commercial activities in agriculture and services. Poland was also the first post-communist country to initiate comprehensive market-oriented reforms at the end of 1989, long time before the start of economic transformation in Ukraine. Figure 3 indicates that under post-communism the direct involvement of the state in the production activities decreased significantly in both countries: to one quarter of the Polish economy and to one third of the Ukrainian economy. Yet given its rather late beginning, the reduction of the public sector appears to be more remarkable in the Ukrainian case, especially as regards large-scale industry. Nonetheless, what effect has the process of 'de-statization' had on macroeconomic performance and the overall outcomes of transformation in the two countries?

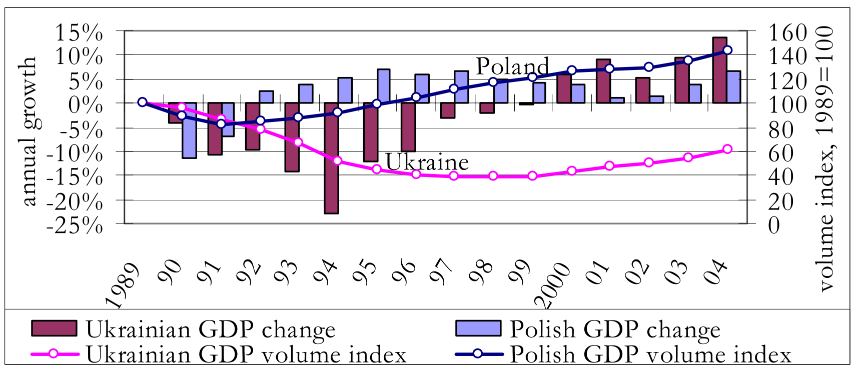

Figure 4. Economic growth in Poland and Ukraine, 1989-2004 (annual percentage growth and GDP volume index, 1989 = 100)
Source: Author's calculations on the basis of EBRD (2000, 2003, 2004); USSC (2000, 2002, 2003, 2004a); PSCO (2000, 2002, 2003, 2004a).

Contrary to the above-mentioned predictions and prescriptions of the orthodox neo-liberal transition approach, the radical shrinking and withdrawal of the state in Ukraine correlated with a long economic depression that the country had experienced in the 1990s. Figure 4 shows that even after five years of robust economic recovery, Ukraine's GDP in 2004 amounted to just 62 per cent of its 1989 level. In turn, since 1992, Poland experienced thirteen consecutive years of sound economic growth, expanding to over 143 per cent of the pre-transitional level. On the other hand, the Polish economy has been growing on average by 4.4 per cent annually since 1992, whereas after its return to growth at the end of the 1990s, Ukraine's GDP figure has been rising on average by 8.7 per cent a year. Why have both post-communist economies returned to growth, despite the divergent characteristics of their governments and public sectors?

It also appears from Figure 4 that the decline of the public sector and the consequent rise of the private sector have had no particular systemic influence on macroeconomic performance. Poland's post-communist recovery had begun when the majority of enterprises were still state-owned, producing over 55 per cent of GDP. By contrast, Ukraine registered its first annual economic growth in 2000, when over 60 per cent of the country's GDP were already produced by private firms and farms (for the expansion of the private sector share in GDP, see EBRD 2003). In addition, the dominant paradigm can hardly explain why total output could not start expanding rapidly almost immediately after the 'totalitarian' restrictions on economic activities were removed.

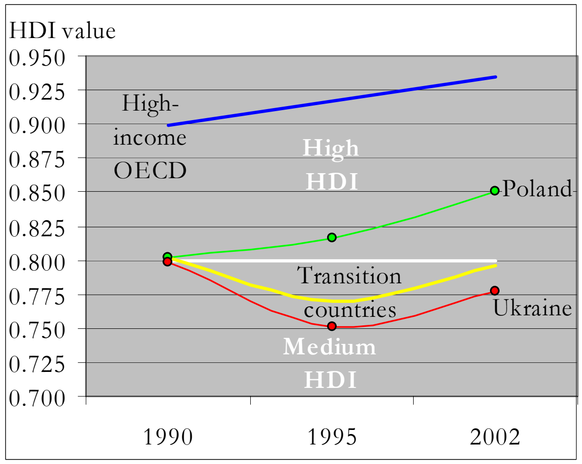

Figure 5. Human development trajectories under post-communism, Poland and Ukraine: regional comparison (scale: 0 – 0.5 = a poor human development country; 0.501 – 0.8 = a medium human development country; 0.801 – 1.0 = a high human development country)
Source: Author's calculations on the basis of UNDP (2004).

The process of 'de-statization' has also had different effect on the degree of human survival and development in Poland and Ukraine. The two post-communist societies have had to endure huge social costs of transformation. To assess them, I first use the Human Development Index (HDI) introduced by the United Nations Development Programme in the 1980s as a synthetic uniform measure that covers three major aspects of human development – a long and healthy life, knowledge, and a decent standard of living – by evaluating (1) life expectancy at birth, (2) adult literacy rate, (3) combined gross primary, secondary and tertiary education enrolment ratio, and (4) gross domestic product per capita in US dollars at the purchasing power parity rate. Figure 5 shows human development trajectories generated by Poland and Ukraine under post-communism. It also summarizes the average human development index results for the industrially advanced countries of the West as well as for the countries of Central and Eastern Europe and the Commonwealth of Independent States. Figure 5 indicates that Ukraine's transformation towards slimmer and smaller government has corresponded with an extraordinary deterioration of the human survival and development standards, leading to poorer income levels, worse education standards, weaker health and lower life expectancy. By contrast, Poland's human development index values have been steadily growing under post-communism, indicating a general improvement in living, health, and education standards of the population.

Thus, the reduction of the role of the state has had a very mixed impact on economic growth and human development in the two post-communist countries. The process of radical 'de-statization' in Ukraine in the 1990s was accompanied with a deep and protracted depression and a sharp decline in human survival and development. By contrast, the maintenance of Poland's large externally financed state correlated with a faster economic recovery and expansion, and a significant degree of human development progress achieved under post-communism. Poland's much larger and more expensive government did not hurt the country's economic performance and human development progress. On the other hand, Ukraine's push for slimmer government did not result in any particular economic or human development improvement.

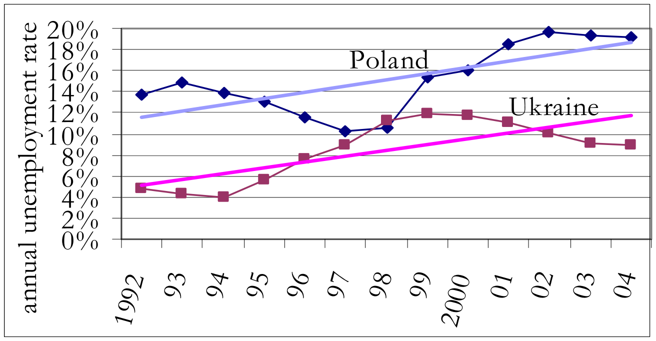

Figure 6. Unemployment in Poland and Ukraine, 1992-2004 (labour force survey-based unemployment rates and trend lines, percentage of unemployed to total active labour force, age 15-70)
Source: Author's calculations on the basis USSC (2000, 2001, 2003, 2004a, 2004b); PSCO (2003, 2004a, 2004b); IMF (2003b).

The national transformation outcomes in other social spheres have been less conclusive comparatively. Real unemployment rate under post-communism has been twice as high on average in Poland as in Ukraine. Figure 6 shows that besides a short period in the late 1990s, the two post-communist countries have produced rather divergent trajectories of labour utilization, as calculated in accordance with the International Labour Organization methodology (i.e. labour force survey-based unemployment rate). The two unemployment trend lines presented in Figure 6 also indicate that, in the field of employment stability, the general process of the state's withdrawal in both Poland and Ukraine has been positively related to higher unemployment. Yet, there appears to be no systemic relationship between a faster pace of 'de-statization' and higher unemployment.

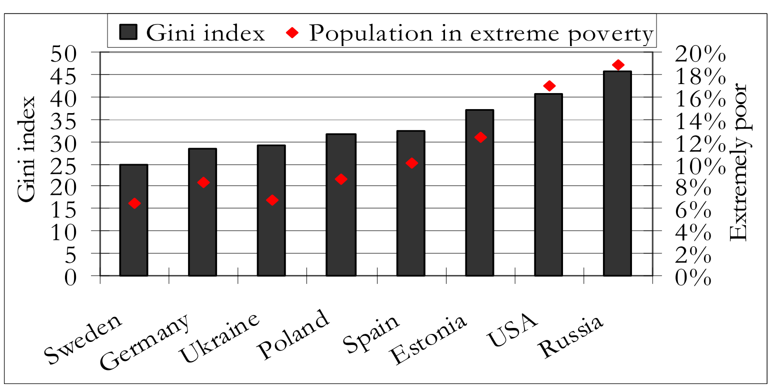

Figure 7. Income inequality and poverty in Poland and Ukraine, international comparison, 1999-2000 (Gini coefficient index: 0 = perfect equality, 100 = perfect inequality; Extreme poverty rate: population below 50% of median income)

Note: Gini coefficient indices of Ukraine, Poland, and Russia are for per capita consumption; the remainder are for per capita income.
Source: World Bank (2000b); UNDP (2004).

The final set of indicators concerns changes in income and wealth distribution, and poverty in Poland and Ukraine. In the 1990s, all the post-communist countries experienced a rise in income, wealth, and consumption disparities. In both Poland and Ukraine, inequality increased substantially, but the distribution of income and household consumption patterns remained fairly egalitarian. The Gini coefficient (which is the most often-used inequality index) for per capita consumption rose in Poland from 25.8 in 1987 to 31.6 in 1999, whereas in Ukraine the increase was similarly moderate, from 24.0 to 29.0 respectively (Deininger and Squire 1996; World Bank 2000a, 2000b; UNDP 2004). Figure 7 shows that the increase in inequality in Poland and Ukraine has been far below the one experienced by other post-communist countries, where consumption Gini coefficients almost doubled (for a detailed discussion of inequality under post-communism, see World Bank 2000a). Moreover, notwithstanding substantial differences in the size and scope of their state structures, the process of transformation in both Poland and Ukraine have been characterized by similarly modest rises in relative impoverishment. There are a number of ways of defining income poverty lines. According to one of the standard household survey methodologies used in this paper, a relative poverty line of 75 per cent of the median adjusted disposable household expenditures (or income) is usually chosen as a criterion for poor households, 60 per cent of median expenditures (or income) is used as a criterion for very poor households, and 50 per cent of median expenditures as a criterion for extremely poor households (see World Bank 2000b). On its right scale, Figure 7 shows the percentages of the population living in extreme poverty in a number of post-communist countries and in some high-income OECD member states. Figure 7 indicates that the shares of the Ukrainian and Polish population living in relative extreme poverty in 1999-2000 (6.7 and 8.6 per cent respectively) were on par with those registered in some of the most egalitarian societies of Western Europe, and far below the extreme poverty levels observed elsewhere.

To conclude, this comparative study has been unable to identify the existence of any meaningful systemic relationship between, on the one hand, the size of government, level of public spending, and the degree of state involvement in the economy, and, on the other hand, macroeconomic performance and social outcomes of the post-communist economic transformation. A more radical and profound reduction of the state's role can be well related to a long, deep economic depression and a considerable deterioration of human development standards, whilst the maintenance of a large state and 'costly' government can be beneficial for economic growth and human development. On the other hand, in the spheres of employment, income distribution, and poverty, the two country's post-communist outcomes point into the opposite direction, i.e. slimmer government should not be necessarily accompanied with relatively higher unemployment, more inequality and widespread poverty. The inconclusiveness of the evidence presented illustrates the apparently contradictory nature of the (neo)classical dichotomy between the state and the market, on which most of the post-communist policy advice and technical assistance has been based. By analyzing the phenomena of the post-communist economic transformation within the dominant paradigm of 'de-statization' one is unable to interpret the political economic dynamics of the process.

It is contended that an alternative conceptual approach is necessary, if one is to provide an explanation for post-communism's varied outcomes.

THE 'VARIETIES OF CAPITALISM' APPROACH

A number of theories recently developed within Western comparative political economy are believed to be especially useful and appropriate for the study of the post-communist transformation. What is common to all of them is the concept that various state and market institutions are not totally autonomous and that they function in certain interdependent and hierarchical fashion. Masahiko Aoki (1994) was the first to argue that, similarly to the concept of 'complementary goods', there can exist complementarity between the institutions of the political economy. In the basic case of complementary goods, pairs of goods for which consumption is interdependent, for example motor-cars and petrol or bacon and eggs are known as complements; and changes in the demand for one will have a complementary effect upon the demand for the other. In the case of *institutional complementarity*:

> Two institutions can be said to be complementary if the presence (or efficiency) of one increases the returns from (or efficiency of) the other. Conversely, two institutions can be said to be 'substitutable' if the absence or inefficiency of one increases the returns to using the other […] This point about institutional complementarities has special relevance for the study of comparative capitalism. It suggests that nations with a particular type of coordination in one sphere of the economy should tend to develop complementary practices in other spheres as well … If this is correct, institutional practices of various types should not be distributed randomly across nations. Instead, we should see some clustering along the dimensions that divide liberal from coordinated market economies (Hall and Soskice 2001b: 17-18).

The second common feature amongst several conceptual approaches within the comparative political economy of modern capitalism is the idea of *institutional hierarchy*. As recently argued by Bruno Amable, institutional hierarchy means that institutional design in one area depends on or takes into account the constraints and incentives associated with the institutions prevailing in other areas. While the notion of complementarity links different institutions between the different elements conditioning the coherence of the whole system, the notion of a hierarchy insists that one institution or a few institutions somehow impose the conditions to which complementary institutions are going to supplement them and those few institutions dictate the dynamics of the whole architecture as such. Yet, the true source of hierarchy is not anteriority: the institutional hierarchy is defined according to which set of rules dictate the design and possibilities of other rules (Amable 2003: Chapter 2).

In a pioneering study of the institutional foundations of comparative advantage, Peter A. Hall and David Soskice (2001a) have elaborated a 'varieties of capitalism' approach based on the analysis of strategic interactions between major institutional spheres of modern capitalism: industrial relations, vocational training and education, corporate governance, inter-firm competition, and the intra-firm employee co-ordination arrangements. The major contribution of this perspective has been the idea that, due to the discovered existence of institutional complementarity and hierarchy, national political economies can and ought to be compared by reference to the way in which firms resolve the co-ordination problems they are faced with in all these five spheres. Following Michel Albert's delineation between the 'neo-American' and the 'Rhine' models of capitalism (1993), the 'varieties of capitalism' approach draws the core distinction between presumably the two most opposite ideal types of capitalist political economies: *liberal market economies* and *co-ordinated market economies*, with the USA and Germany playing the symbolic poles of a spectrum along which capitalist nations can be displayed.

According to the 'varieties of capitalism' approach, in liberal market economies, firms co-ordinate their activities primarily via hierarchies and competitive market arrangements: (i) several features of the financial systems or markets for corporate governance of liberal market economies push firms to pay special attention to current earnings and the price of their shares on equity markets; regulatory regimes are tolerant of mergers and acquisitions, including hostile takeovers that happen when the stock-market evaluation of a firm ultimately declines; the terms on which large firms can secure finance (bonds, shares issues, and bank lending) are heavily dependent on their short-term valuation in equity markets, dominated by dispersed investors; (ii) the industrial relations arena is characterized by the market relationship between individual worker and employer, who has unilateral control over the firm, including freedom to hire and fire; the presence of highly fluid labour markets provides firms with the ability to release or hire labour relatively easy in order to avert immediate threats to profitability or to take full advantage of new opportunities; in turn, with no promises of long-term employment, individuals are encouraged to invest in general skills, easily transferable across firms, and to pursue changeable and movable career trajectories; (iii) companies are loath to invest in apprenticeship schemes that instruct industry-specific skills, as there are no guarantees that other firms will not simply 'poach' their apprentices without investing in training themselves; therefore, the education and training systems of liberal market economies are focused on providing general skills that can be used in many different firms and sectors; (iv) inter-firm relations are based on standard market relationships and enforceable formal contracts; the legal system of liberal market economies prevents companies from engaging in relational contracts with other firms; (v) technology transfer is ensured through the movement of scientists and engineers from one company to another, or from research institutions to the private sector (Hall and Soskice 2001b: 27-33).

By contrast, as Hall and Soskice have maintained, in co-ordinated (or regulated) market economies, firms rely more heavily on non-market relationships to harmonize their endeavours with other actors and to build their core competences: (i) the financial system or market for corporate governance typically provides companies with access to long-term finance that is not entirely dependent on publicly available financial data or current returns; the performance monitoring is secured by the presence of dense networks of reputation linking the managers and technical personnel inside a company to their counterparts in other firms on terms that provide for the sharing of reliable information about the firm's progress; (ii) the internal structure of the firm reinforces these systems of network monitoring by obliging top managers to secure agreement for major decisions from supervisory boards, which include labour representatives as well as major shareholders, and from other firm's managers, suppliers, and customers; (iii) many firms in co-ordinated market economies pursue production strategies that rely on a highly skilled labour force; to prevent highly damaging conflicts with their employees and to stop the enticement of skilled workers by other firms, co-ordinated markets economies have developed a special industrial relations system which settles potential disputes by setting wages through national- or industry-level bargains between trade unions and employers associations and equalizing wages at equivalent skill levels across an industry; (iv) the development of high industry-specific or trade-specific skills and competence of labour, on the extensive usage of which many co-ordinated economies depend, is conducted through an adequate education and vocational training system; (v) the nature of relationships between firms is based on co-operation in product development, collaboration and common knowledge-bases that facilitate technology transfer and diffusion. (Hall and Soskice 2001b: 21-27).

Hall and Soskice have argued that, notwithstanding the inherent differences between liberal and co-ordinated models of capitalism, due to the complementary nature of their institutional designs, both types can deliver sound and sustainable macroeconomic performance. While the broader line of analysis of the 'varieties of capitalism' approach has gained a major acceptance amongst comparative political economists, the central criticism has been focused on the approach's binary classification of the capitalist economies (between liberal and co-ordinated). As some critics of the 'varieties of capitalism' have argued, countries that can neither belong to liberal market economies or be clearly identified with co-ordinated market economies – the 'intermediate cases' – are regarded as somewhat deficient. In the U-shaped relation between performance and institutional features all these transitional cases are thus expected to generate inferior results and are located at the bottom of the U-shape. However, not all the intermediate cases have actually been characterized by poorer performance or lower-value comparative institutional advantage (for this line of criticism, see Amable 2003: 79-85; cf. Schmidt 2002: Chapter 3).

Amable (2003) has critically incorporated the 'varieties of capitalism' approach into his cross-national study of modern capitalist economies and developed a new typology of diverse modern capitalism. In its summary, Amable's theoretical contribution is based on the differences of major institutional forms and different institutional complementarities which are developed among them in five broad spheres such as: the character of competition in product markets, the wage-labour nexus and labour-market institutions, the sector of financial intermediation and corporate governance, the social protection system, and the education sector. The basic postulate of Amable's theory is that there are more than two or three types of capitalism and that each of these types is characterized by specific institutional complementarities. In other words, the mechanisms of institutional complementarity do not follow 'more market versus more state intervention' logic subsequently in each of the institutional spheres but the institutional complementarities evolve in a much more intricate way. As the result of an extensive large-scale comparative analysis of twenty one major capitalist economies (the core OECD member states), Amable has identified five different models of modern capitalism: the market-based Anglo-Saxon model, Asian capitalism, the Continental European model, the social-democratic Scandinavian model, and the South European model.

To conclude, the common theme that unifies Hall and Soskice (2001a), Schmidt (2002), Amable (2003), and other theorists working within the 'varieties of capitalism' approach is that the alleged all-out superiority of market-based economies needs to be qualified. Institutional variables have a significant effect when interacting with each other and should be analyzed in such a way as well. For instance, sound macroeconomic performance is possible either with uncoordinated industrial relations and deregulated product markets, or with coordinated industrial relations and regulated markets. As Amable has summarized: 'there does not seem to be a clear growth advantage unconditionally attached to the specific features of the market-based model. Regulated markets and centralized financial systems can deliver good growth performance too' (2003: 218).

DIVERSE CAPITALISMS IN TRANSITION

It is beside the purpose of this paper to consider particular features of each of the several major types of modern capitalism identified or to provide a comprehensive comparison of the Polish and Ukrainian economic systems with these ideal types. It is within our limits, however, to make an attempt to break away from the (neo)classical dichotomy between the state and the market, and to discover whether the 'varieties of capitalism' framework can provide a more adequate interpretation of the post-communist phenomena. In particular, the following questions warrant further consideration: why the human development and unemployment trajectories generated under post-communism in Poland and Ukraine have been different, whilst the inequality and extreme poverty levels registered in the two countries have shown a very similar change pattern?

In the previous section, we have mentioned five major complementary institutional domains such as product markets, the wage-labour nexus, the finance sector, social protection, and the education sector, which are identified by the theorists of the 'varieties of capitalism' approach for studying different models of modern capitalism. It is contended that by discovering the contours of actually existing East European capitalisms in the spheres of product-market competition, the labour market, and the social protection sector, we will be able to account for the differences and similarities in the observed outcomes of transformation. For a partial comparative analysis of the two post-communist capitalist systems conducted in this section,[4] I have generally adopted the 'diversity of capitalism' methodology, which was developed by Amable (2003) and based mostly on extensive data-bases compiled by the OECD research staff in the late 1990s – early 2000s. The missing institutional indicators for Poland and Ukraine presented here are my own calculations and scorings, constructed from primary sources and national data using the respective OECD techniques. The institutional features of the two post-communist capitalisms in the fields of market competition, industrial relations, and public welfare, will be contrasted with the countries that are found to be the most representative of five different ideal types of modern capitalism, namely the liberal market-based economy (or the Anglo-Saxon model), social-democratic economy (or the Scandinavian model), Asian capitalism, co-ordinated market

[4] A full comparative institutional analysis of post-communist capitalism would cover the finance and education sectors, in addition to product-market competition, industrial relations, and the social protection systems analyzed here.

economy (or the Continental European model), and the South European capitalism (or the Mediterranean model)[5].

Product-market competition

The nature, form, and intensity of competition between firms in the markets of goods and services are determined by public regulation, i.e. specific institutional settings defined by the state to govern the product-markets. This is the first fundamental institutional domain that is believed to differentiate the existing models of capitalism. Nicoletti, Scarpetta and Boylaud (2000) have collected and formatted a database of internationally comparable data on certain economy-wide and industry-specific regulations; and provided a multi-stage estimation of indicators of regulation that summarize (at different level of detail) the extensive information on the regulatory environments characterizing OECD member-states. Overall, they have constructed seventeen detailed indicators of regulation to describe the regulatory environment in the product market. The detailed indicators were classified in the following three broad domains: state control over business enterprises; barriers to entrepreneurship; explicit barriers to international trade and investment.

Without entering into any further detail, one has to mention that according to the ideal type classification of modern capitalism elaborated by Amable (2003: Chapter 3), in the sphere of product-market competition, market-based economies are characterized by the high importance of price competition and the non-involvement of the State in product markets. Economic agents in the Anglo-Saxon model are co-ordinated through market (price) signals, whilst product-markets are open to foreign competition and investment. Social-democratic economies are characterized by the high importance of quality competition, the strong role of the State in product markets, and the high degree of co-ordination through channels other than market signals. Product markets in the social-democratic model are open to foreign competition and investment. The Asian capitalism is characterized by the importance of both price and quality competition, the high involvement of the State, the great degree of non-price co-ordination, and the high level of protection against foreign firms and investment. The role of large corporations in the Asian capitalism is particularly essential. The Continental European capitalism is characterized by the moderate importance of price competition, the relatively high importance of quality competition. Public authorities are involved in regulating product markets and the degree of non-price co-ordination of economic agents is relatively strong. Domestic product markets in Continental European

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[5] These five ideal-typical models of capitalism have been identified and examined by Amable and are said to be most associated with the following OECD countries correspondingly: (1) the UK, USA, Australia, and Canada; (2) Finland, Denmark, and Sweden; (3) South Korea and Japan; (4) Germany, Belgium, France, and Austria; (5) Greece, Italy, Portugal, and Spain. According to Amable's factor and cluster analyses, the United Kingdom is the closest existing example of the ideal market-based model of capitalism; Finland is the nearest country to the ideal social-democratic model; Korea is the country closest towards the 'Asian' ideal type of capitalism; whilst Greece approximates the Mediterranean model. With regard to the paragon of each cluster, i.e. the country that comes closest to the average position of the cluster as a whole, the USA is said to be most average for the market-based cluster. The paragon of the social-democratic cluster is Denmark, that of Continental European countries is Germany, and Spain is the paragon for the Mediterranean cluster. As there are only two countries within the Asian-capitalism cluster, each of them can play the role of the archetype (Amable 2003: Chapter 5).

economies are moderately protected against foreign firms and investment. In the Mediterranean model, product-market competition is characterized by price- rather than quality competition, the involvement of the State, little non-price co-ordination, moderate protection against foreign trade or investment. Product markets in South European economies are dominated by small firms.

On the basis of factor analysis matrices and other techniques developed by Nicoletti *et al.* (2000), and using the relevant Ukrainian regulatory policy documents and other legislation (e.g. the Commercial Code, the Law on Enterprises, etc.), I have compiled the detailed and summary indicators of the product-market regulation in Ukraine and made the necessary comparative scorings. Table 1 presents the summary indicators of the product-market regulatory framework in the three main fields of state control, barriers to entrepreneurship, and barriers to trade and investment, for Ukraine and Poland, as well as for five countries that are believed to be most representative of the modern capitalism's ideal types, i.e. the United Kingdom (market-based capitalism), Finland (social-democratic capitalism), South Korea (Asian capitalism), Germany (Continental European capitalism), and Greece (Mediterranean capitalism).

Table 1. A synopsis of summary indicators of product market regulation by domain, point estimates, late 1990s – early 2000s

	Summary indicators			
	Overall indicator	Domains		
	Product market regulation	State control	Barriers to entrepreneurship	Barriers to trade and investment
UK	0.5	0.6	0.5	0.4
Germany	1.4	1.8	2.1	0.5
Finland	1.7	2.7	1.9	0.6
Greece	2.2	3.9	1.7	1.3
Korea	2.4	2.3	3.1	1.7
Poland	3.3	4.2	1.8	3.7
Ukraine	1.5	2.9	1.4	1.1

Note: The comparative scale range is 0 – 6 (from least to most restrictive product-market regulation).
Source: Nicoletti, Scarpetta, and Boylaud (2000); VRU (1991a, 1991b, 1992, 1996, 2000a, 2000b, 2003b); USSC (2003); and author's own calculations and scorings on the basis of the methodology of Nicoletti *et al.*

Table 1 shows that the Polish capitalism has been characterized by heavily regulated product markets, extensive government involvement in the economy and the large scope of the public sector, the high level of co-ordination of economic agents through non-market signals, the moderate level of administrative burdens for entrepreneurship, and intense protectionism. On average, the product-markets regulation in Poland appears to approximate the Mediterranean and Asian-capitalism clusters: it is very close to the former with regard to the level of state control and barriers to entrepreneurship, and to the latter in the field of outward-oriented protectionist policies. In turn, the Ukrainian capitalism has been characterized by competitive to mildly regulated product markets; the involvement of the State is high; the protection of the domestic product markets is moderate; and the administrative burdens and barriers to entrepreneurship are relatively low. On average, the Ukrainian product-markets regulatory framework approximates the Continental European model cluster as exemplified by Germany.

The wage-labour nexus and labour market institutions

The second institutional arena that we examine is concerned with the industrial and employment relations, as well as with capital, labour, and state institutions, which govern these relations. According to the 'diversity of capitalism' theory, the market-based model is characterized by weak employment protection and extensive labour flexibility: easy recourse to temporary work and easy hire and fire. In Anglo-Saxon economies there is no active employment policy, wage-bargaining is decentralized, whilst trade-unions pursue defensive strategies. The social-democratic model is characterized by moderate employment protection, co-ordinated or centralized wage bargaining, active employment policy, strong labour unions, and co-operative industrial relations. In the Asian capitalist economies employment protection is provided within the large corporation. This model is characterized by limited external labour flexibility, labour-market dualism, seniority-based wage policy, accommodating industrial relations, and strong firms' unions. There is no active employment policy, and wage bargaining is decentralized. The Continental European model is characterized by high employment protection, limited external labour flexibility, conflicting industrial relation, active employment policy, moderately strong unions, and the co-ordination of wage bargaining. Industrial relations in the South European economies are said to be characterized by high employment protection within large firms but also by labour-market dualism (i.e. a 'flexible' fringe of employment in temporary and part-time work). The industrial relations are potentially contentious. There is no active employment policy, but wage bargaining is centralized.

To assess and compare the differences in labour market institutions in the two post-communist regions with the advanced capitalist economies, I use an OECD-developed comprehensive technique to analyze the employment protection legislation – the first specific aspect of labour market regulations. Nicoletti *et al.* (2000) has compiled and review fifteen detailed indicators of the strictness of employment protection legislation, which they have grouped into two broad domains, one referring to provisions for workers with regular contracts and the other referring to provisions affecting workers with fixed-term or contracts with the temporary work agencies. The examined regulations on permanent employment cover *procedural requirements* that refer to the process that has to be followed from the decision to lay off a worker to the actual termination of the contract; (b) *notice and severance pay* that refers to three tenure periods[6] beyond any trial period, dismissed on grounds of poor performance or individual dismissal, without fault; and (c) *prevailing standards of and penalties for 'unfair' dismissals* that include the conditions that identify an unfair dismissal, when employers cannot demonstrate appropriate efforts to avoid the dismissal, or when social, age or job tenure have not been considered; it also includes the length of the trial

[6] The tenure periods are nine months; four years; and twenty years.

period and account is taken of the fact that, in some cases, labour courts may require employers to reinstate a worker affected by an unfair dismissal, or award high compensation payments in excess of regular severance pay. Indicators on the stringency of employment protection legislation for temporary and part-time contracts focus on regulations for fixed-term contracts and for contracts under temporary work agencies, including the following elements: (a) 'objective' reasons under which a fixed-term or temporary contracts could be offered; (b) the maximum number of successive renewals; and (c) the maximum cumulated duration of the contract (for a full description of the labour market regulation analysis technique used, see Nicoletti *at al*. 2000).

Table 2. A synopsis of summary indicators of employment protection legislation by domain, point estimates

	Summary indicators		
	Overall indicator	Domains	
	Employment protection legislation	EPL Regular contracts	EPL Temporary contracts
UK	0.5	0.7	0.3
Denmark	1.5	1.7	1.2
Japan	2.6	3.0	2.3
Germany	2.8	3.0	2.5
Greece	3.5	2.6	4.5
Poland	1.9	2.3	1.4
Ukraine	1.3	2.3	0.3

Note: The comparative scale range is 0 – 6 (from least to most restrictive labour market regulation).
Source: Nicoletti, Scarpetta, and Boylaud (2000); OECD (2004c); VRU (1971); and author's own calculations and scorings on the basis of the methodology of Nicoletti *et al.*

Table 2 presents the results of the factor analysis for regulation affecting regular and temporary contracts in Poland, Ukraine, and five representative countries of major models of modern capitalism. It shows that, in general, the two post-communist countries are characterized by moderate levels of employment protection. Ukraine appears to have a more flexible labour-market regulation, yet both countries appear to be close to the level of employment protection attributed to the social-democratic model.

The second specific aspect of this institutional domain is the type of industrial relations. The major variables considered here concern wage-bargaining co-ordination (e.g. inter-organizational co-ordination through national agreements; intra-organizational by trade unions, by employers' federations; or through pattern bargaining); centralization and corporatism (national, industry, or company, weighted levels of wage-bargaining), the role of governments in bargaining (direct intervention, statutory minimum wage), trade union density, industrial disputes, practices of national social dialogue and relations between managers and employees evaluated through the collective agreement coverage.

Table 3. Summary indicators of industrial relations, point estimates, late 1990s - early 2000s

		GBR	*DNK*	*KOR*	*DEU*	*ITA*	*POL*	*UKR*
Levels of bargaining	Inter-sectoral		x					x
	Sectoral	x	xx	x	xxxx	xxx	x	xxx
	Company	xxxx	xx	xxxx	x	xx	xxxx	x
Coordination	National agreement		1		1	2		1
	Intra: unions		1		1			1
	Intra: employers		1		1			1
	Pattern bargaining		2		2			2
Government role	Pay indexation mechanism							
	Statutory minimum wage	1						
Capital-labour relations	Union density, %	31.2	74.4	11.4	25.0	34.9	14.7	73.0
	Industrial disputes,	22.4	49.6	97.4	2.6	76.4	4.7	28.4
	Direct collective bargaining coverage, %	32.5	82.5	12.5	68.0	82.5	42.5	80.0

Notes: Levels of bargaining: maximum score is 5 ('xxxxx') divided over three levels. Co-ordination mechanisms:'2' is major / strong; '1' is minor / weak. Else: absent.
Industrial disputes are evaluated as the average number of days lost to strikes per 1000 salaried employees in the last five years for which data are available (principally 1998-2002).
Source: Authors calculations and scorings on the basis of Elmeskov, Martin, and Scarpetta (1998); Visser (2000); Carley (2002); ITUFR (2004); ILO (2004); OECD (2002a, 2004c); USSC (2003); MLSPU (2004a, 2004b, 2004c); Seniv (2004).

Table 3 presents a synopsis of major industrial relations indicators for Poland, Ukraine, and five advanced capitalist countries: the UK, Denmark, Korea, Germany and Italy. It appears that the major features of the Polish industrial relations have been decentralized wage-bargaining, the low level of co-ordination, extremely sparse labour unionization, and narrow collective agreement coverage. Relations between managers and employers in Poland are non-confrontational, as the small number of strikes indicates. Generally, little co-ordination and centralization of wage bargaining in Poland resembles very closely labour-market flexibility of liberal market-based economies. By contrast, Ukraine's industrial relations are characterized by the high degree of wage-bargaining centralization, extensive co-ordination, the very high level of trade union density, and very broad collective agreement coverage. As regards the degree of wage-bargaining centralization and co-ordination, Ukraine's industrial relations have clearly become neo-corporatist and the country's wage-labour nexus approximates the social-democratic model.

The third aspect of the wage-labour nexus and labour-market regulation is employment policy. To evaluate the level of state intervention in labour markets, we examine public expenditure on labour markets programmes that is usually analyzed through active and passive measures. Active labour market measures involve spending on public employment services and administration, labour market training, youth measures, subsidized employment, and measures for the disabled. Passive labour market intervention activities cover unemployment compensation and support for early retirement for labour market reasons.

Table 4. Public expenditure on labour market programmes, as a percentage of GDP, 1999-2001, period average

	Korea	*UK*	*Italy*	*Germany*	*Denmark*	*Poland*	*Ukraine*
Active measures	0.50	0.35	0.59	1.25	1.67	0.33	1.01
Passive measures	0.15	0.66	0.69	1.98	3.18	0.76	1.58
Total	***0.64***	***1.01***	***1.28***	***3.24***	***4.85***	***1.09***	***2.59***

Source: Author's calculations on the basis of OECD (2002); CMU (2003); IMF (2003a).

Table 4 summarizes the data concerning public expenditure on active and passive labour market programmes in five representative capitalist countries as well as in Poland and Ukraine. It shows that the level of the Polish state intervention into labour markets in the late1990s – early 2000s has been low and close to the market-based model countries. There are no direct data available on the amount of public spending on labour market programmes in Ukraine. I have assessed the level of the Ukrainian state intervention as the sum of direct state budgetary allocations for active labour market measures and the average annual expenditures by Ukraine's three public financial institutions: Temporary Employment Disability Social Insurance Fund, State Obligatory Unemployment Social Insurance Fund, and Job Accident and Occupational Disease Social Insurance Fund. The figure obtained suggests the level of public intervention in Ukraine's labour market to be close to the Continental European level. Since 2001, the Ukrainian government has been gradually increasing the annual budgetary allocations envisaged for active labour market measures that have significantly boosted public spending on government employment policy measures from the level shown in Table 4 (see *Uriadovyi Kur'er*, 17 April 2002; cf. VRU 2002, 2003a).

Thus, the wage-labour nexus and labour market institutions in Poland have been characterized by the moderate level of employment protection, decentralized and un-coordinated wage-bargaining, low trade union density, narrow collective agreement coverage, defensive union strategies, the low degree of the state intervention in labour markets, and very high wage flexibility. The overwhelming majority of these features indicate a gradual shift of the Polish capitalism towards the market-based model of the wage-labour nexus. By contrast, the Ukrainian labour market has been shifting towards neo-corporatism based on long-term and positive-sum conceptions of common interest between organized powerful agents (for an analysis of different types of industrial-relations system, see Crouch 1993). Since the late 1990s, the wage-labour nexus in Ukraine has been increasingly characterized by a large number of neo-corporatist features common to the social-democratic as well as Continental European models of capitalism such as moderate employment protection, highly centralized and co-ordinated wage-bargaining, strong trade unions, more cooperative industrial relations, declining wage differentials, and the initiation of active employment policies.

Social protection and the welfare system

According to the 'varieties of capitalism' literature, social protection does not always mean 'the state against the market'. On the contrary, the welfare system is believed to rescue the market from itself by preventing market failures. As analyzed by Estevez-Abe, Iversen, and Soskice (2001), social protection complements and aids the market by helping economic actors overcome market failures in skill formation. They have argued that the shape of social protection has bearings on national competitive advantage in international markets and choice of product market strategies. As the availability of specific skills requires appropriate forms and levels of social protection, institutional differences that safeguard returns on specific skills explain why workers and employers invest more in specific skills. On the other hand, the absence of such institutions, in countries such as the USA and UK, gives workers a strong incentive to invest in transferable, generally-applicable skills. In such an environment, it then also seems to be more productive for firms to pursue product market strategies that use these transferable skills intensely.

As to the individual features of social protection in different ideal types of advanced capitalist societies, the 'varieties of capitalism' approach postulates that weak social protection and the low involvement of the State are the major features of the market-based economies. The welfare system's emphasis in the Anglo-Saxon model is on poverty relief ('social safety net'), means-tested benefits, and private-funded pension system. The social-democratic economies are characterized by an extremely high degree of social protection, the prominent role of the State, the great importance of the Welfare State in public policy and society. The Asian capitalist model is characterized by a very low level of social protection and a small share of public expenditures in general welfare. Social expenditures are directed towards poverty alleviation, whilst the overall share of welfare expenditures in GDP is minimal. The Continental European economies are characterized by a high degree of social protection, employment-based social benefits, the involvement of the State, the eminent role of the welfare sector in society, contribution-financed social insurance, and pay-as-you-go pension systems. The Mediterranean model is characterized by a moderate level of social protection and the deep involvement of the State; the expenditures structure is oriented towards poverty alleviation and pensions. Some South European countries have particularly generous family- and elderly-oriented welfare systems (Amable 2003: Chapter 3.4).

Different typologies of welfare systems have been developed (for a comparison of major typologies of welfare systems found in the literature, see Amable 2003: 154-60). According to the prevailing opinion, the USA, Australia, Ireland, Canada, Japan and Korea (i.e. most of the countries of the Anglo-Saxon and Asian capitalism models, except for the UK) belong to the liberal, 'residual-welfare' model (or the weak, non-welfare, 'zero-level' model of social protection). The United Kingdom, Netherlands, Spain and Portugal are considered 'minimal-universalist' welfare systems. The welfare systems of the other two remaining Mediterranean European countries are regarded as much more generous 'subsidiarist' or 'Latin particularist-clientelist' models.[7] The Nordic countries are said to belong to the 'maximal-universalist',

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[7] Subsidiarity is one of the major concepts of the Roman Catholic Social Theory that rests upon an understanding of society as an organism characterised by a hierarchy of mutually supportive organs. In this view, nothing should be delegated to higher organs that can be accomplished by individuals or lesser or subordinate bodies. Thus, according to the European Roman Catholic welfare philosophy, informal care should, whenever possible, take precedence over state intervention in social welfare service (see Cross and Livingstone 1997). However, neither 'Latin' nor 'subsidiarist' adjectives can be used with regard to the Eastern Orthodox Greece and its social protection sector.

social-democratic model of the Integral Welfare State. France, Germany, Austria, and Belgium are characterized by the Continental conservative-corporatist welfare systems.

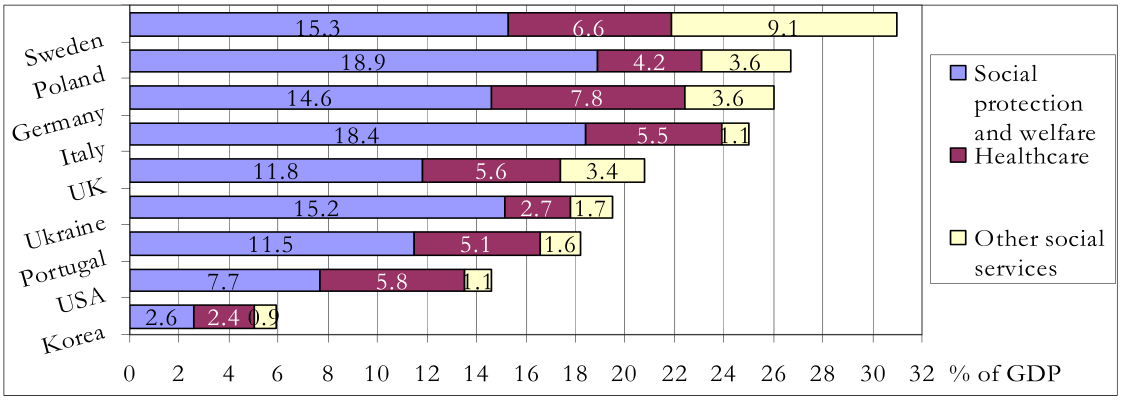

Figure 8. Public social spending by major allocations, as percentage of GDP, Poland and Ukraine, international comparison, average shares in 1998-2002
Source: Author's calculations on the basis of USSC (2000, 2002, 2003); IMF (2003a); PCSO (2000, 2001, 2002, 2003); OECD (2004b, 2004c).

I analyze the welfare system of the two East European capitalisms by comparing the level and character of public social expenditure in Poland and Ukraine with the variety of advanced capitalist countries. Figure 8 presents the data broken up by three broad categories of public social expenditure such as: (a) social protection and welfare that covers public expenditure on pensions and old-age cash benefits, disability, occupational injury and unemployment benefits, active labour market programmes, and income support to the working age population; (b) health care; (c) housing benefits, culture, arts, sport and physical exercise activities, and other social services including religious programmes. Figure 8 indicates that with the average share of public social spending in Ukraine's GDP of 19.5 per cent, laying in between UK and Portugal, the country's welfare system clearly belongs to the minimalist-universal system of social protection. The relative level of social protection and welfare support in Ukraine has appeared to be as high as in Scandinavian and Continental European economies, but public expenditure on health and other social services has been much lower. By contrast, Poland's welfare system with the level of public social expenditure amounting to 26.7 per cent of GDP, has been amongst the most generous social protection systems in Europe. Moreover, the level of public spending in Poland on social protection and welfare support alone (18.9 per cent of GDP) has been by far the highest among all the advanced capitalist economies. It is this feature that indicates a strong similarity of the Polish Welfare State with the Mediterranean 'Latin' paternalism, as exemplified by Italy.

Our classification of the two post-communist welfare systems is also supported by the data on the changing role of the State in their economies that have been presented in the second section of this paper (see Figure 1). Figure 1 summarized the average shares of general government sector expenditures to GDP in Poland, Ukraine, and a number of representative capitalist economies for the 1992-2005 period. It indicated the high degree of the Polish state's involvement in the economy throughout the entire period of the post-communist transformation. On average, the government's size in Poland has been comparable with the Mediterranean model of heavily regulated capitalism. By contrast, under post-communism, Ukraine has been experiencing a dramatic change of the role of the State and the withdrawal of the government from the economy to the level far below that of the UK – one of the closest existing examples of the free market economy and the limited welfare state.

COMPLEMENTARITIES AND INCONGRUITIES OF THE POLISH AND UKRAINIAN CAPITALISMS

The two newly emerged forms of post-communist capitalism have been characterized by the possession of a prevailing – albeit incomplete – set of complementary institutions that provides a more coherent and cohesive arrangement of information and co-ordination mechanisms for economic agents. On the basis of our discussion in this paper, Table 5 summarizes the core features of the two transition capitalisms in the spheres of market competition, industrial relations, and public welfare.

Table 5. Characteristics of transition capitalism in the two post-communist regions

Institutional arena	*Poland*	*Ukraine*
Product-market competition	**Heavily regulated product markets; high role of direct state involvement; importance of small firms**	**Competitive to mildly regulated product markets; moderate state involvement; importance of large corporations**
Wage-labour nexus	Moderate employment protection; decentralized labour markets; uncoordinated wage-bargaining; weak trade-unions	**Mild employment protection; co-ordinated labour markets; centralized wage-bargaining; moderately strong unions**
Social protection	**'Latin' Welfare State (particularist-clientilist subsidiarism); high level of social protection and public spending**	Limited (minimal-universalist) welfare system, low level of social protection and public spending

Note: Boldfaced typing indicates institutional complementarity.

Transition capitalism in Poland has been characterized by the great importance of the State and high direct government involvement in the economy, heavy regulation and the moderately high protection of product markets, numerous administrative burdens for large corporations, and by a large public sector. In the sphere of labour markets and industrial relations, the Polish post-communist capitalism has been characterized by a very moderate degree of employment protection, little co-ordination and high decentralization for wage bargaining, increasingly growing wage flexibility, and weak trade-unions. The public welfare system in Poland has been characterized by the high level of social protection; generous public social expenditures are oriented towards poverty alleviation, pensions, and family-oriented benefits, whereas healthcare and additional social services are of less importance.

The Ukrainian variant of post-communist capitalism has been characterized by the moderate level of the public authorities' involvement in the economy, relatively mild non-price 'co-ordination', and low protection against foreign firms and investment in product markets. As regards the wage-labour nexus, the core features of transition capitalism in Ukraine have been moderate employment protection, highly centralized and co-ordinated wage bargaining, moderately strong unions, declining wage flexibility and increasingly active labour market policies. The welfare system has existed in Ukraine in a universal but extremely limited form. It has been characterized by the moderate level of social protection, very low public spending on health, and the low level of government involvement in providing additional social services.

Table 5 demonstrates that two out of three major institutional domains under examination in each of the two forms of transition capitalism are distinguished by the systemic compatibility and complementary. In Poland, heavily regulated product markets and the paternalist social protection system correspond to the basic characteristics of the Mediterranean model of capitalism. In turn, in Ukraine, competitive to mildly regulated product markets, and highly co-ordinated and centralized industrial relations correspond with the Continental European model of capitalism. However, both types of post-communist capitalism possess at least one major institutional incompatibility. According to Amable's 'diversity of modern capitalism' typology and his application of the theory of institutional complementarity, the Mediterranean model of capitalism is based upon high employment protection and employment stability, which is made possible by a relatively low level of product-market competition. As a result of heavily regulated product markets, low competitive pressure allows employment stability (in large firms). On the other hand, formal employment protection prevents fast structural change, whereas de facto employment stability lowers the demand for social protection. In its turn, low welfare expenditures imply lower tax distortions on the domestic market. As our detailed examination of the three institutional domains of transition capitalism has shown, in the case of Poland, the wage-labour nexus that is based on labour market flexibility has not been complementary with the overall logic of the Mediterranean model. Poland's deregulated labour market has significantly increased demand for social protection, which should have been low in the ideal-type Mediterranean capitalism.

In the case of the Continental European model of capitalism, the theory of institutional complementarity postulates that competitive to mildly regulated product markets generate a moderate degree of internal competitive pressure, which enables a relatively high degree of employment protection. Yet, external market pressure demands important productivity gains from economic agents. The quest for productivity gains implies labour-shedding strategies that are politically sustainable only with social protection. The centralization of wage bargaining and corporatism favours 'co-ordination' amongst firms that prevents fast structural change and employment instability, and thus permits a moderately high degree of social protection. Extensive public welfare expenditures imply high taxes and leads to high non-wage labour costs, which is detrimental at the lower end of the skill scale (see Amable 2003: 102-114). Thus, as Table 5 indicates, Ukraine's limited welfare system appears to be incompatible with the Continental European model of capitalism.

It is contented that the puzzling outcomes of the post-communist economic transformation in Poland and Ukraine as regards human survival and development, unemployment, income inequality and poverty have been generated by the identified partly complimentary and partly substitutable institutional factors. Chronically high unemployment in Poland ought to be attributed to the intra-systemic incompatibility of flexible labour markets inserted into a heavily regulated economic system. On the other hand, Poland's generous social protection sector and high levels of public spending have resulted in the country's steadily improving human development indicators, a relatively moderate degree of income inequality, and a low level of extreme poverty. In turn, the dramatic decline in human survival and development indicators, which has been experienced by Ukraine under post-communism, was caused by ever decreasing public expenditure on health and additional social services, and, generally, by the rapid withdrawal of the state from the welfare system. However, the country's moderate internal competitive pressure and a relatively high degree of neo-corporatist wage and employment arrangements have generally resulted in lower levels of unemployment and income inequality than those observed in Poland. In addition, the establishment of a minimal-universalist welfare system, with its strong emphasis on poverty alleviation, has been the primary force behind a very low level of relative extreme poverty in the post-communist Ukraine.

CONCLUSION

This paper has critically assessed the mainstream liberal paradigm of post-communist studies that views post-communism as a transitory stage in the global move from the prevalence of the state power to the dominance of the free market. I have argued that the orthodox transition approach and its prescribed policy advice to liberalize, privatize, and deregulate post-communist economies is built upon the alleged dichotomy between state and market. The practical implications of the process of radical 'de-statization' have not been at all conclusive as to support the neo-liberal policy recommendations that equate slimmer government with better performance. Academically, the liberal transition theory does not possess conceptual tools capable of explaining the divergent social outcomes of the post-communist transformation in different contexts. It has been contended that 'the state against the market' hypothesis that underpins the dominant transition paradigm is unrealistically reductionist.

The paper has illustrated the importance of theorizing in the political economy of post-communism. It has shown that incorporating the perspective of Western comparative political economy into the study of post-communism does indeed provide a better handle on the multiple and complex process involved in the transformations of post-communist countries. I have argued for the vigorous application of the 'varieties of capitalism' approach and conceptual frameworks developed within it to study the post-communist phenomena. This can not only improve our understanding of how markets can be built and how political development proceeds, but it can evidently uncover what *kind* of markets can be built through *which* political mediatory structures. Thus, in contrast with the conventional neo-liberal theory, the 'varieties of capitalism' is believed to be a comprehensive policy-relevant approach. It calls for a comparative institutional analysis of intricate complementary systemic arrangements and mechanisms that provide coherence and enhance the macroeconomic performance of diverse models of modern capitalism. The post-communist state and the market are ought to be considered not as mutually exclusive or contradictory social entities but as complementary institutional forms that can be transformed to interact compatibly and deliver sound and sustainable results.

Yet, at the present stage, this alternative approach is at its very beginning. In order to fully adopt the ‘varieties of capitalism’ theories to the post-communist context and to develop them further, one needs to engage in an extensive cross-national comparative institutional analysis of the post-communist world aimed at developing a typology of actually existing transition capitalisms and discovering what institutional complementarities are present and can be fostered to improve the macroeconomic performance and growth sustainability of the countries concerned.

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