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Subjective and objective factors in post-socialist economic reforms.

The past decade of economic reform generated a great interest in generalizing the transition experiences that occurred over this period. These experiences have been highlighted in a number of recent provocative papers. While the process of post-socialist transformation in its essence appears economic and political, the noted papers and related discussions inevitably appeal to personal motives and beliefs of those who took an active part in shaping economic policies.

Post-socialist economic reforms were nothing but the "learning by doing" process. Consequently, in order to understand the reform policies, one needs to consider what was that the future policy-makers' prevailing vision of the main challenges they would face and ways to tackle these challenges in the transformation process. To analyze this problem, one needs to do two things. First, one needs to understand the political and economic constraints that determined the framework of policies available, and second, one must know what the noted vision was.

Contemporary papers draw a broad picture of the role of subjective factors in the transformation of the post-Soviet territory. In essence, the picture is as follows:

1. The Soviet economy was inefficient, but a steadily functioning institution;
2. Young market romanticists with economic background in the post-Soviet government did not understand the complex structure of modern economics and the role of institutional factors therein. They decided to immediately launch radical reforms, dismantle the old system of management, liberalize prices and economic activity, introduce convertible currency, and implement mass privatization. They assumed that all the above would secure a rapid rise in the economy's efficiency and economic growth.
3. Once deprived of traditional socialist management levers and lacking a mature system of institutions that ensures modern market functioning, the economic system reacted to reformist attempts via a drastic fall in output and living standards[i].

It should be noted, however, that this picture of the post-socialist universe slightly looses its elegance when viewed through the real historical process. For instance, one could recall that the break-up of the USSR led to formation of 15 different states with 15 different governments pursuing substantially different policies. Those aware of the details of these policies would hardly imagine the Prime Minister of an independent Ukraine, Mr. Vitold Fokin, or his colleague from Belarus, Mr. Vyacheslav Kebich, in the role of market "Sturm und Drang" romanticists. However, the tempting simplicity of this construction which allows an easy explanation of one of the most dramatic crisis in economic history is comfortable for many.

Let me draw another, more complex, and in my opinion, closer to reality, picture of the interconnection between objective and subjective factors in the development of situation in the post-Soviet zone.

One can hardly realize socio-economic policy options without understanding the key problem of post-socialist transition-- fundamental contradictions between the integrity of industrial socialism, the revolutionary nature of its collapse, and the need in a specific period of time to build the foundation of an efficient market sector for a post-socialist economy. This foundation would be able to form the basis for the renewal of economic growth.

The developed, industrial socialism forms an integral system of interconnected socio-economic and political institutions. At the same time, such a system is the biggest anomaly in economic development during the past century[ii]. The essential core of this system is a rigid totalitarian power spurring the formation of an integral bureaucracy. The latter substitutes for market forces by ensuring current coordination of economic activity and ensures switching off delicate market and civil society mechanisms. The emergence of such a system allows the elimination of barriers to increase the state's burden of national savings and investment and the limitation of domestic competition in regards to imports. At early stages of industrialization this allows the acceleration of industrial growth rates by an ultimately fierce exploitation of agriculture. Later, the socialist economy begins to suffer from the accumulation of sclerotic elements caused by structural rigidity, the inefficiency of consumption of resources, low quality goods, and inability to compete in the world markets. Consequently, such an economy experiences a growing dependence on imports of food stuffs and new equipment.

Should the noted contradictions manifest themselves relatively early, when industrialization's reserves have not yet been exhausted, the agrarian sector is able to deliver resources to form a new market-oriented sector parallel to the old, socialist one. Following this path, the abandonment of socialism could be relatively smooth (China and Vietnam, for example). However, under a high level of socialist development, with agrarian resources already exhausted and the contradictions of socialist industrialization crystal clear, there is no easy path to a free market. Serious attempts to switch on market mechanisms cause an intense crisis in the structures formed by socialist industrialization[iii]. Although the analysis of problems in socialist economic dynamics is beyond the framework of this paper, one needs to emphasize the fact that in a developed socialist system, elements of socio-economic and political systems appear perfectly fitted to one another. In such a situation, one cannot opt at one's discretion to chose something pleasant. Several factors define this system, including: the ultimately high level of state drain on GDP, overly military production, the respective structure of the industrial sector, and the large-scale output of products with negative value-added in world price equivalent, as well as a relatively egalitarian distribution of monetary income, reasonable funding of education, shortages of qualitative (and oftentimes—complete lack of) consumer goods, party control over staff promotion, closed borders, absence of freedom of press. All the above factors are not isolated positive or negative features of a communist system, but they form an integral system. In such a system the possibility of single elements surviving without the system as a whole is not at all guaranteed.

Several factors played a role in the destabilization of communist regimes, including the intensification of the crisis of a socialist economy, an obvious loss of momentum, defeat in its rivalry with the West, the growing dependence on export of energy sources, dependence on world market movements and Western credit inflows. However, the collapse of the socialist empire per se appears primarily a socio-political rather than an economic phenomenon. The growth in the literate urban population and the industrial growth of society undermine the fundamentals of a totalitarian regime's legitimacy. Plus, one should note a growing uncertainty among the communist elite in their own ideals and institutions, as well as a dangerous expansion to Eastern European countries whose peoples were greatly influenced by Western culture and values. All this combined to break an allegedly unbreakable regime. Glasnost and perestroika, Mr. Gorbachev's policies, just put a torch to an already flammable pile of institutions.

The Poles who voted for the Solidarity movement, the Eastern Germans who broke up the Berlin Wall, the Lithuanians who stood up to protect their Parliament, the Muscovites who supported Yeltsin- they all did so not because they believed in a clearly outlined economic program for building a market economy. They simply did not want to allow non-elected leaders and organizations that did not bear any authority for them to decide their destiny. If they had been told that the collapse of the Communist Party of the USSR and KGB would automatically mean a deep crisis of all public and economic structures that were based on the loss of totalitarian power. A revolution is always a verdict to elites of the old regime that they have been incapable to transfer the status quo toward a path of peaceful reform.

Revolution is a radical change of the earlier formed establishments, socio-economic and political institutions, ideological norms, and elites during a period defined by weak, unstable control[iv]. Some experts highlight an unprecedented fall in output in Russia over past years. This is not true – the fall in output in the country in the wake of the 1917 Revolution was more intense. This well-known phenomenon was also characteristic of the Great French and Mexican revolutions. However, in the latter cases revolutions took place basically in the agrarian economies where the functioning of basic structures only to a limited extent depended on the efficiency of power and monetary authorities. On the other hand, the collapse of a totalitarian regime in the industrial socialist countries automatically generated a sharp crisis in the whole economic structure.

It was the collapse of trade within the framework of the Council for Mutual Economic Assistance that became the most characteristic manifestation of the crisis in Eastern Europe. The large-scale mineral exports from the USSR in exchange for Eastern European manufactured products was based upon barter agreements, clearly not market-based. Such an exchange could survive only within the framework of a single military and political empire. The political liberation of Eastern Europe inevitably meant a radical revision of such forms of trade and, consequently, the crisis of the economic structures dependent on it[v].

Under a socialist economy, production and delivery of goods is dictated by superior bodies that penalize agents in case of failure rather than support profitability. Kolchoz or sovkhoz delivers grain to an elevator ("obeying the first testament") not in the hope of receiving funds, but because its director is well aware that his failure to accomplish the task will lead to his ousting from office as well as from the Communist party with no chance to regain his position in either structure. In a worst case scenario, failure can end in jail time. The political collapse of a totalitarian regime also implies the breakup of the whole system of economic ties based on the fear of severe punishment from above. However, it does imply an immediate switch to mechanisms of private and market ties that were broken decades ago.

So, the collapse of a totalitarian regime caused by a political crisis automatically implies the beginning of the crisis of the current coordination of economic institutions and structures created by the socialist system. However, such a collapse does not automatically form institutions and structures needed for the normal operation of market mechanisms. This appears to be the major reason for the post-socialist crisis and recession.

Once the problems of production slump in post-socialist countries began to emerge, researchers began to focus their attention on the disorganization of economic ties caused by their adjustment to market conditions[vi]. The problem, however, is much broader. An efficiently functioning market economy is not just market prices, proclaiming private property, and the establishment of formal institutions. Rather, it is primarily traditions and customs of business turnover and civil society formed by experiences of prior generations and their respective skills and practices.

It is an efficient judicial system and law enforcement that forms the crucial precondition of a well functioning market economy. Under a totalitarian regime, there is no room for an independent court following the law because it appears contradictory to the regime's fundamental powers. The whole tradition of legal proceedings inherited from socialism is the tradition of the court being an element of the repressive system that loyally follows the respective communist party's instructions. One can promptly pass legal statutes on judicial reform and guarantees of courts' independence. This process was accomplished by the overwhelming majority of post-socialist countries. However, an impartial court that follows the letter and spirit of law is not just formal statutes and a disconnected "hot telephone line" with a local communist party boss; it is primarily a long history of emerging professional ethics, behavioral norms adopted among the judicial community, reputation, and above all, a truly functioning civil society always ready to impose social punishment on a judge that breaks accepted norms. At this point, one needs time, the adequate funding of the judicial system, and consistent efforts in order to develop a functioning legal system. However, there are no guarantees for the time frame needed to accomplish this particular mission.

The functioning system of law and legal proceedings forms the backbone of an operating market economy. The latter is immeasurable more difficult to reach than any written law. It is traditions of economic turnover that play a determining role in its everyday operations, and it happens very rarely that conflicts and disagreements arising in this process are brought to the court. In the overwhelming majority of cases, it is well-established customs and the threat to loose one's reputation due to violation of such customs that appear sufficient to resolve a conflict. Had any of the most civilized and mature market economy been left with all its law structures and legal enforcement institutions, but deprived of the noted traditions and civil society on guard, the next day there would be economic jungle and a war of all against all. Naturally, there are certain behavioral norms in a socialist society, including: orientation towards report rather than to result, upward distortions, a highly valued system of personal contacts based upon access to deficit resources, small stealing from one's enterprise, etc. Unfortunately, these factors do not appear useful in the course of the emergence of an efficient market economy.

The realities emerging from the collapse of the communist regime are different. Even if new authorities are very keen to demand an immediate formation of market reputations, the system of public ties that helps shape them, and efficiently functioning law enforcement system, none of these things can simply take shape the next day. This becomes the source of a chronically low level of accomplishment of undertaken obligations ("non-payments"). This becomes the usual norm for years, as well as spurs the formation of private, including criminal, forms of arbitration and enforcement of contracts.

The problems of the banking system emerging after socialism are just a partial manifestation of the general shortage of market traditions. The establishment of an efficient system of banking control demands well trained, non-corrupt staff who must understand how the domestic banking system operates. It is impossible to import such personnel at an adequate scale. However, the problem is more serious. As in any normally functioning banking system the banking control is just the last safeguard. The system's sustainability to a great extent depends on the banking community's professional ethics standards. They do not appear at once after the removal of a monument to the local communist dictator and the return of national symbols. This explains a massive spiraling of "phony" credits disbursed among affiliated structures and private individuals, broad practices of asset transfers, as well as the chronic unreliability of the banking system that does not allow it to become an effective instrument reallocating resources in favor of functioning and growing enterprises.

Notably, the process of emergence of the latter is likely to be one of the most complex challenges facing the post-socialist transition. It was not a secret to anyone that the essence of the post-socialist transitional economy primarily was the reallocation of resources frozen in inefficient production processes and enterprises in favor of efficient, capable entities that can survive market competition. What proved to be unexpected was, first, the magnitude of hardships related to the formation of the sector for enterprises efficiently operating under market conditions, and, second, the time period the sector needed to fully mature before it could compensate through organic growth for the contraction of non-vital production.

Today, after accumulating the respective experience, the reasons for such hardships are evident. These hardships were not caused just by structural anomalies inherited from socialism, or hypertrophied development of military production and its related sectors. As well, is it the fact that a considerable part of production capacities proved to be incapable to adjust themselves to meet consumer demand or their "megalomania" and chronically low quality output. Indeed, enterprises capable to function and develop efficiently under market conditions are not just adequate production facilities. They are primarily an efficient management team that is aware of marketing and financial management practices and is able to adapt flexibly to strict conditions of market competition. Furthermore, such sound management and entrepreneurial skills are needed at thousands of enterprises rather than at a few "leading" ones. As far as the radically changed conditions are concerned, all the managerial traditions and skills formed over decades of socialism (focus on production and supply rather than on sales and finance, behavioral stereotypes of the "economy of shortages", absence of skills in market analysis, a low attention to quality of goods, etc.) were counterproductive. At the same time the idea that a new managerial elite can be supplied on someone's request[vii] proves to be clearly utopian. Even when it starts being influenced by market realities it does not mean that old-time managers that are incapable to set up an effective production process, but are capable to squeeze the last benefits out of a dying socialist enterprise are eager to leave the scene.

As well, one should not overestimate the post-socialist government's capacity to control the process. A proactive stand with training programs for market-oriented personnel is of course useful, but this requires a considerable amount of time, and proves to be modestly efficient. At least over the first years after the collapse of socialism the old elite would retain rather strong position within the government, and this would happen regardless of the government leadership's orientation. In such a situation it would be overly optimistic to hope for a pro-active, positive role from the government that has undergone a broad "reshuffle" of a great part of the elite. This process is at best time consuming and harrowing.

So, the collapse of a totalitarian political regime automatically launches the self-destructive process of the socialist economic system, for which it was the backbone. One soon arrives to the understanding of the impossibility of retaining a considerable part of prior economic structures and production, while the emergence of institutions and traditions needed for a satisfactory functioning or, specifically, the growth of a market economy requires time. This fuels the inevitable long-lasting post-socialist recession when the availability of resources freed from traditional sectors and productions is not fully compensated by the growth in market sectors.

The absence of historical precedents for the collapse of the socialist economic and political regimes, and the problems created by that excluded any possibility of an *apriori* (proceeding from the set of data available as of its beginning) estimation of the magnitude and duration of the production decline after socialism. Though the Polish reformers who pioneered the reform process realized that structural changes, as well as the policy aimed at securing monetary and financial stabilization, could lead to a temporary fall in the volume of output and growth in unemployment, the magnitude of the production decline and its duration proved to be unexpected both to them and to the overwhelming majority of experts in transitional processes. As at that time the post-communist reformers lacked other post-socialist countries' experiences and a clear picture as to how long the production decline would take, it caused the first wave of professional papers of 1990-91 that directly relate economic dynamics with concrete forms of the Polish reformers' economic policies ("shock therapy" in particular). It was at that time when the large-scale demand for gradualist remedies arose. Such formulae related the scale and length of the Polish production slump with the excessive tightness of monetary and financial policies during the time. This formulae advocated softer and slower transformations[viii].

Several realities undermined the popularity of gradualist explanations and their respective economic and political remedies. Those were, specifically: 1) the start of economic growth in Poland in 1992 (in the fourth year after the price liberalization of 1989 and in the third year after the launch of systematic reforms), 2) the significant size of the production slump, and the length of the slump period noted in all the eastern European countries that began their systematic reforms later than Poland. Later on, the dynamic nature of Polish economic growth in the mid-to-late '90s has made arguing against the Polish "shock therapy" method not fashionable. The advocates of gradualism recently have tended to refer to the gradual nature of the Polish transformation, more specifically to the relatively low rate of privatization of large industrial enterprises. However, at least in some respect the Polish experience laid down an implicit, and substantially constant reality that is always in presence whenever problems of post-socialist transitions are discussed: under an adequate economic policy one needs a 3- to 4- year period to get out of post-socialist recession and renew economic growth. The Eastern European countries underwent similar scenario: the renewal of economic growth (though with different levels of sustainability) occurred, as a rule, over the 3rd or 4th year after the start of systematic economic reforms. These scenarios provided a steady (though not formulated clearly) hypothesis for a preset minimal duration of a post-socialist recession. It was the very standard picture of Eastern European experiences with which the actual picture of economic development in the post-Soviet states was compared. The absence of economic growth after 3 to 4 years of reforms in the largest countries of the region (Russia, Ukraine, and Kazakhstan) formed the grounds for the widespread speculations in 1998-99 that a radical difference between the paths of economic development had occurred. According to some analysts, Eastern Europe and the Baltic countries, on the one hand, realized one path, while the major part of the post-Soviet zone, on the other hand, took a significantly different road[ix].

We have already considered the set of factors that complicate economic growth renewal. The factors are the legacy of socialism, and to a crucial extent their nature is rooted in social history: hardships facing the emerging market sector and reallocation of resources in its favor, formation of an adequate market economy, systems of institutions and behavioral standards. All these forces clearly find themselves directly dependent to what extent market skills were erased from public practice over the socialist era and how radical the suppression of civil society elements was. All these parameters are directly related to the length of time socialism was practiced in the respective country and its intensity.

By the start of reforms in Eastern Europe and the Baltic countries there were millions of people for whom market and private realities (then replaced by socialist influences) had been an element of life during their childhood. These peoples' children formed the backbone of the younger cohorts being most active in politics and business. As in the overwhelming majority of cases, socialist institutions and establishments were imported via Soviet bayonets, a considerable part of the noted countries' societies always conceived them alien and forced. Plus, there clearly were certain civil society elements in eastern European countries (a relatively independent church, small private businesses, etc.).

In contrast to that, there was nothing of the sort throughout the lion's share of USSR territory. The socialist experience was the only available one, while the majority of the population had a picture of market economy borrowed from Western movies, and the number of those who ever visited developed market economies was negligibly small. In these countries socialism was not imported by foreign bayonets (violent means), but it became a result of a tragic development of national history, thus becoming an inseparable element of society. It was over 7 decades that all civil society attempts at public self-organization were suppressed in these countries. This suppression was much more brutal than in the majority of eastern European countries. In addition, the economic structure of the Soviet economy itself to a great extent was deformed by socialism and was much more militarized than the younger eastern European socialist economies.

While abstracting in this particular case from comparing the quality of economic policies pursued in Eastern Europe and the post-Soviet zone, we have strong evidence to assume that even if other conditions were equal, the intensity and duration of the post-socialist recession in the post-Soviet states should be substantially greater than in Eastern Europe. When life compels us to take part in a race to climb out from the trench of the socialist inferno, its results should be judged in accordance to the depth of the trench.

It was in papers published between 1996 to 1997[x] in which experts focused on an evident and strong negative correlation between the duration of the socialist period in a concrete country's history and the outcomes of the post-socialist transition. In the papers of 1998-99[xi] the former parameter traditionally is present among the crucial factors determining the dynamics of post-socialist development. However, in such a case one can hardly accept the concept that dictates that the standard period of post-socialist recession (the picture of which was formed on the basis of Eastern European countries' experiences) should apply to the analysis of the development of the post-Soviet states.

The start of economic growth in the post-Soviet states between 1999 to 2000 has undermined the credibility of the "dispersing development paths" construction. Now it has become evident that the paths and dynamics of output are basically the same, and there are obvious reasons why the duration and intensity of the post-socialist recession in the larger post-Soviet states were substantially greater than in Eastern Europe.

Authors of transition-oriented papers have long adopted the notion of so-called “transition years”. They assume that it is the year of price liberalization that begins the count, and consequently ensures the possibility to compare the development of countries that launched their reforms in different years. As long as a comparative cross-country analysis of the process of getting out of the post-socialist recession is concerned, it is worth considering the year of the beginning of economic growth as the starting point. However, if this is the case than the Russian economy of 2000-01 should be compared with the Polish economy of 1993-94, rather than the Polish economy of 2000-01. Even a quick glance at the statistics is enough to realize that the two economies have a lot in common in terms of key economic indices (inflation rate, the share of credits to private sector in GDP, foreign direct capital investment per capita, etc.).

Thus, post-socialist recession is an inevitable phase of transitional process after the collapse of developed socialism. The recession’s minimal magnitude and duration are preset by indigenous socialist features, as well as the time needed for the emergence of a market sector capable of compensating for the contraction in inefficient production. The duration of the post-socialist recession is related to the duration of the socialist period itself.

Against such a background, during the past decade almost three dozen post-socialist countries have been trying to set a course for their economic policies. They underwent hundreds of government reshuffles and tasted various economic models and initiatives. All this could not help but impact the characteristics of a transitional period and the emerging market economies. Given that until this point in the paper we abstracted from the impact of economic policy on transition dynamics, it should now form the object for our analysis.

By the moment the Solidarity’s triumph in the elections opened a “window of opportunity” for the Polish reformers, there were no adequate experiences which could form a basis for forecasting the future development of post-socialist countries. The unprecedented nature of the mission did not allow one to estimate the scope of the challenges ahead and the future hardships of societies and economies adjusting to market conditions. It was the ‘emergency policy’ situation, the unique moment which could not be missed that formed the crucial factor substantially influencing the decisions made at that time. The USSR still firmly existed at the genesis of the Polish reforms, and no one could reliably forecast what the outcome of the internal political struggle would be, and whether democracy and independence would prove stable in such conditions. This is why the Polish reformers were so keen on fully exploiting the chance to form a viable market economy. The “emergency policy” environment per se extended the freedom of maneuverability and allowed a maximal concentration of the necessary transformation efforts.

In such a situation, the Polish reformers opted for a simultaneous price liberalization, economic liberalization, introduction of convertible national currency, termination of inflation on the basis of a set of monetary and budget policy measures as well as wages policy instruments, and the launch of structural reforms, primarily privatization. Even looking back from today, it is hard to rebuke the Polish reformers for underestimating the value of establishing the institutional fundamentals of a market economy. On the contrary, from the very beginning they vigorously worked in this direction, promoted respect for the law, and created agencies and structures needed for market conditions to take root. However, such work, of course, required time[xii].

I believe a real deficiency at that time was the underestimation of the role played by several forces, including: traditions and behavioral standards, time needed to change them, the role of the emerging market sector, excessive expectations with regard to privatization, a poor understanding of the duration of the process necessary for the emergence of efficient private owners in the large industrial sector, and simplified concepts of the interrelation between financial and monetary stabilization[xiii].

Now, let me focus on the latter factor. Today we have a far better idea of the magnitude of the mission to form the mechanism for sustainable growth than in the early '90s. Plus, the standards of decent behavior in the monetary and budget spheres have become common knowledge. For this reason it is hard to understand the roots of the debate and the struggle of that time that clearly concentrated on the financial and monetary policy issues and on curbing inflation. It appears evident that inflation forms just one of numerous sources of uncertainty in the post-socialist reality. So, its suppression per se does not at all guarantee a renewal of post-socialist growth.

I think the fact that reformers focused their attention to this particular element of economic policy was determined by several factors.

First, high inflation (and the threat of hyperinflation) formed a sharp and evident problem undermining the efficiency of market mechanisms. In the eyes of the general public, curbing inflation, along with the elimination of shortages, formed a clear criterion by which, at the beginning of the transition towards a market economy, society could evaluate the effectiveness of the reform course.

Second, in contrast to the complex problem of post-socialist transition that suggests no simple solutions, high inflation is a well-known, fairly standard economic phenomenon that can be subject to more or less standard treatment. The only and - as it became clear later on- correct hypothesis reformers should have adopted in such a case was to handle it by standard monetary methods-- in post-socialist conditions high inflation is primarily a monetary phenomenon.

Third, the most developed market economies failed to establish original political-economic mechanisms that were analogous to "The Marshall Plan" after the Second World War in order to help the nations abandoning socialism. As a result, they laid responsibility for the provision of the process on the International Monetary Fund. For the IMF, the mission to ensure financial and monetary stabilization was standard and well developed, though one can hardly argue the same with regard to the post-socialist transition on the whole.

It was this happy coincidence that made the Polish reformers right from the beginning to focus on the political-economic challenges of disinflation facing them. The prompt solution to it proved to pave the way for an efficient post-socialist transition, though thanks to substantially different microeconomic reasons that those originally believed in the early '90s.

In the conditions of the post-socialist transition, the reformist governments' consistent focus on suppression of inflation and the respective tightening of budgetary and monetary policies formed both prerequisites for the stabilization of a national currency and, not less importantly, the strengthening of strict budget constraints at a micro-level.

In the course of time it became clear that the reaction of a socialist economy to price liberalization, introduction of convertible national currency, stabilization measures, and the start of structural reform that manifested themselves in Poland was fairly general and appeared everywhere, where similar sets of political-economic measures were implemented.

The late phase of socialist economic development is characterized by the existence of a monetary overhang, ie. the excessive volume of the money supply compared with the demand for money on the part of economic agents. Such an overhang takes the form of shortages of goods. A socialist economy is in essence the economy of suppressed inflation. Once prices are fixed, the government enjoys broad possibilities to increase the money supply. While having no chance to end up in a higher price level, an excessive money supply caused by the funding of a budget deficit or the granting of credits to enterprises operating in the public sector is accumulated in the form of compulsory savings and non-satisfied demand for goods and services.

Liberalization of prices and economic ties radically changes conditions for exercising monetary policy. Now an excessive money supply leads to acceleration of prices rather than to intensification of shortages of goods. Given that under socialism customers had no choice but compulsory savings or purchasing of a good at a higher price, with price liberalization in place, such a choice becomes reality. It is at this point where an actual level of demand for money is revealed. It is the preceding monetary history, the level of confidence in the national currency and the government's stabilization efforts that are crucial factors determining the noted level of demand for money.

So, there are two large-scale macroeconomic processes facing post-socialist countries: a sharp production decline and a sharp downfall in the real money supply. As a rule, these processes are of a greater magnitude than pro-reform governments originally expected. For this reason right after the start of reforms their opponents advocated constructions that related production slumps to an excessive compression of credit and the money supply as well as to proposals to increase money supply growth rates in order to stabilize production[xiv].

Wherever pro-reform governments managed to resist such proposals and continued a tight monetary policy, the inflationary tide generated by liquidation of the monetary overhang disappears rapidly and inflation rates drop, while the demand for national currency and real money supply begin to grow. Should the monetary policy become loose and a government attempts to support production by increasing the money supply, the disinflation process proves to be longer.

The key role played by structural transformations, such as the formation of a broad range of production units being able to efficiently compete on the market for the sake of market reform, compels us to pay special attention to the microeconomic mechanisms that secure these factors. The main cause of economic stagnation and the intensifying crisis of socialism that eventually lead to its collapse is that the socialist economy lacks a set of institutions fostering efficient innovations and an automatic reallocation of resources in favor of economic entities that could efficiently utilize them.

Formation of an environment securing such incentives constitutes a strategic task of the post-socialist transition. In a developed market economy, the crucial mechanisms securing solutions to these problems are based on hard budget constraints that enterprises impose on themselves. Enterprises incapable of using their resources efficiently, and those failing to use the most rational production methods turn out to be non-profitable; their managers lose their jobs while their owners lose their property. A strict relation between efficiency and financial insustainability in maintaining control over the respective resources ensures the success of a market economy in its competition with socialism.

In the framework of the traditional socialist enterprises' soft budget constraints and a weak financial responsibility, socialist firms are compensated by the strict responsibility of their managers for accomplishing planned tasks critically important for the superior levels of the hierarchy. Upon the collapse of socialism, the noted soft budget constraints are still there and enterprises find themselves in a unique position: soft administrative responsibility is now combined with a soft financial one. Enterprises do not have to accomplish any planned tasks with their volume of output and can demonstrate a chronic inability to be profitable. They can be insolvent without serious penalties applied to the management. The evolution of the former public enterprises towards promotion of soft budget constraints appears natural, and its logic is determined by the mature traditions of the relationship between the enterprise and the state, managerial skills, and the state of the legal infrastructure.

The factor counteracting the realization of such a scenario in the countries that pursued the accelerated disinflation policy is hard financial constraints initiated for the government itself. The stabilization monetary policy constrains the scope of an acceptable budget deficit and its financing. So, to go beyond the set limits means to acknowledge the defeat of the chosen strategy for transition towards a market economy and the course towards an accelerated convergence with Europe. In the overwhelming majority of cases post-socialist governments are confronted with a transitional fiscal crisis, budget problems caused by the erosion of traditional state revenue sources and by the high level of state obligations inherited from socialism[xv]. In such a situation the refusal to apply effective penalties to indebted enterprises, thus allowing them to accumulate tax arrears appears incompatible with the task of maintaining an adequate revenue base for the state budget. Pro-reformist governments then had to choose between the course of suppression of inflation and, accordingly, hardening of budget constraints for enterprises, or an increase of budget disporportions that lead to the failure of the stabilization policy. It is the impact of its financial needs under which the government becomes hard to its own enterprises, thus making them follow different market behavioral standards.

The hardening of financial constraints for public enterprises both changes the priorities of their own economic activity and, not less importantly, leads to a vigorous reallocation of freed resources to a promptly emerging new private sector. Lacking traditional ties with governing hierarchies, the latter allows the traditions of hard budget constraints to take root right from the beginning. For many years after the launch of market reforms the former public enterprises (especially the largest ones enjoying strong political support) have demonstrated low financial accountability. The concentration of tax arrears in this particular sector has remained a serious political-economic problem. However, the scope of the sector was rapidly shrinking and it has discontinued to play a dominant role in the economy.

The significance of hardening enterprises' financial responsibility goes far beyond the government's budget problems. Enterprises have to take a more pro-active stand with regard to changes in the market and price proportions. Should their management fail to ensure an efficient production of competitive goods, they would loose control over resources. One notes a fast change in the composition of the economic elite and promotion of those able to organize production in accordance to market conditions. Post-socialist enterprises undergo convergence between their business practices and standards and those inherent in developed market economies. It is the enterprises operating under hard budget constraints with no tax arrears that become the main locomotives of economic growth.

It was a consensus among national political elites on the problem of choosing a country's strategic development course that created the specific dynamics for countries that became capable to complete a rapid disinflation and cement the fundamentals for a renewal of economic growth. Their changing governments focused on the most rapid integration of the countries into European structures and future accession to the European Union. All that established a non-articulated veto on attempts of large-scale experiments with the economics of populism. The populist rhetoric and proposals to solve economic problems by means intense money issuance and a rise in budget expenditures were quite regular in the course of electoral campaigns. However, they proved to have a very loose impact on consequent economic policy.

In contrast to the above, the majority of post-Soviet states, as well as Bulgaria and Romania, did not demonstrate such a consensus. In these countries the choice of economic paths underwent a sharp political struggle, while their financial and monetary policies fluctuated sharply. In some of the noted countries, the government initially focused on attempts to pursue "soft", "generous," gradual reforms (Romania, Ukraine, etc.), while in some others the start of radical transformations proved to be politically unsecured and was consequently replaced soon by attempts at implementing soft monetary and budget policies (Russia, Bulgaria). As a result, the countries have experienced a long period of high inflation and delayed financial stabilization. Their further development showed that a long period of high inflation leads to the emergence of a number of micro and macroeconomic factors that proved to be unstable, and that restricted economic growth and reproduced financial instability. This type of high inflation substantially affected the further progress for the national economies in question.

Similar to the nations pursuing a hard stabilization policy, in the post-Soviet zone it also is the fall in the volume of output and in the share of money in GDP that form first visible outcome of post-socialist reforms. However, noting a loose political support for stabilization policy, public enterprises react to the challenge of the changed economic environment through a considerably more intense increase in mutual non-payments compared to the respective indexes of the countries pursuing a rapid disinflation policy. The fall in output along with a sharp contraction of the real money supply and an explosive rise in mutual non-payments between enterprises causes the following relations in an economy: excessively tight monetary policy pursued due to monetarist considerations, shortage of money in the economy, non-payments between enterprises, and a production decline. This also suggests a standard remedy: to increase the money supply ("to saturate the economy with cash"), to solve the problem of non-payments by means of monetary emission and off-sets. This would ensure the basis for economic growth. Plus, all the above usually refers to Keynesian theory and is associated with economic solutions to the Great Depression.

In order to lobby such a political-economic move, one can form a powerful socio-political coalition uniting heads and employees of public enterprises who are eager to retain soft budget constraints and refuse radical restructuring, and lobbyists representing budget sectors keen to increase budget expenditures funded by money emission. As a result, the conflict between a hard budget policy at the macro-level and soft budget constraints at the level of public enterprises is resolved by softening the government's budget and monetary policies.

Such experiments can be renewed repeatedly, and they prolong the period of high inflation and the production slump. Sooner or later the society grows tired of skyrocketing prices, a low demand for the national currency, and a fast contraction in budget revenues due to emission. Consequently, the time comes to form a political coalition capable of implementing monetary stabilization by lowering the scale of monetary financing of the budget deficit and growth rates of money aggregates to the values compatible with a curbing of inflation. However, should all this be implemented, the countries undergo a delayed process of financial stabilization and demonstrate a number of similar and important characteristic features:

A long period of high inflation leads to the undermining of confidence in a national currency, a sharp fall of the monetization of the GDP and a high dollarization rate in the economy. These are steady characteristics that are just slowly overcome during the consequent period of monetary stability. The set of behavioral standards formed in the conditions of a soft budget regime (off-sets, arrears, non-payments, barter) generates a steady fall of the share of budget revenues in GDP to the values being substantially lower than in the countries that survived through the "shock therapy." High inflation causes a greater stratification of society in terms of income levels and increases inequality indices compared to the noted countries of the first group. Once combined with a considerable fall in budget expenditures, this generates a sharp rise in the share of the impoverished in the population.

The delayed financial stabilization taking place after a few years of high inflation and against the backdrop of soft budget constraints on the micro-level displays its own specifics. At the moment of launching stabilization efforts, the confidence in the national currency has been ruined, and the share of money in GDP is low. In such a situation even limited emissions to finance a budget deficit leads to growth rates in the money supply that become incompatible with a successful stabilization. The path towards softer disinflation, with a gradual diminishing of the scope of monetary financing of the deficit (like in Poland between 1990 to 1993), proves to be blocked. That is why the need arises to cut down government expenditure substantially sharper than in the states that pursued the accelerated disinflation policy right from the beginning of reforms[xvi].

In connection with the above, I add just a few comments on the specifics of development of the situation in the post-Soviet zone:

Once it became clear that the demoralized Soviet elite was incapable of undertaking a strict and immediate suppression of any signs of dissatisfaction, the destiny of the socialist system was decided. It is enough to compare the bloody and strong suppression of protest during the empire's maturity period (Novocherkassk massacre of 1962) with the picture of the government's literally trembling hands whenever any violent action was tried (in 1989 - inTbilisi and in 1991 – in Viulnus, etc.) to realize that the most important process at that time in the USSR was the dissipation of the fear of coercion cultivated over decades[xvii].

Every bright man who ever lived in the USSR did not have any doubt that the absolute reign of the Communist Party of the Soviet Union constituted the essence of the whole Soviet government system. That is why when the fear of the Party and secret police began to weaken, it became quite naturally that deprived of its core, the whole state machinery began to disintegrate. Notably, at that time neither the formal law nor traditions contained any answers to basic questions: how one should correlate the Union's powers to those of the Soviet Republics, the Soviet Republics enjoying powers of Autonomous republics, Oblasts and Republics, cities and rayons? What one should do if authorities of different tiers make contradictory decisions on the same matter? One must note that all this was taking place in the country whose whole system of economic ties could function only under the strictest control and compliance to rigidly fixed plans.

While reading the Soviet press of 1989-91 now, one can see the picture of broken discipline, failures to accomplish directives, broken obligations on supplies of goods, barriers built on the way of interregional commodity flows, vanishing consumer markets, and growing shortages. All the above was happening under the control of experienced Soviet-style managers - N. Ryzhkov, V. Pavlov, and I. Silayev. They knew what needed to have been done in the framework of the old system to regain control over the situation. However, to do that, one needed a fundamental prerequisite - to reassert the fear of a brutal unlimited power. This was absolutely impossible to do in the conditions of the growing political destabilization and the ruling elite's lost confidence in their infallibility[xviii]. It was the events of August 19-21, 1991 that highlighted this phenomenon very clearly.

Given that before the August 1991 coup d'etat attempt, when the socialist system was disintegrating gradually, some elements of the communist elite cherished the hope to stop the process by using violence. Since then the process spun out of control: the prohibition of the CPSU, the proclamation of the priority of Republican law over the Union's one throughout the former USSR, Ukraine's declaration of independence, and the USSR Central Bank's lost control over monetary circulation. All the above testified to the fact that the former state no longer existed. However, this did not mean at all that the former 15 Republics automatically were becoming real states, as they lacked such crucial features as borders, customs, control over monetary circulation, armies, etc. It was not a surprise then, that in such a situation kolkhozes and sovkhozes flatly refused to deliver grain, and the whole system of inter-regional supplies began to disintegrate. It was during these real conditions when one needed a blueprint for an action plan for the new Russian leadership.

At that time the situation did not allow any theoretic debate on comparative advantages of monetarism, neokeyenseanism or neoinstitutionalism - the area of actual available alternative solutions was simply different.

The fundamental difference between the development of the post-Soviet zone and that of Eastern European countries was that the latter nations underwent a simultaneous collapse of their socialist systems and their states[xix]. The Eastern European countries thus inherited from socialism functioning government institutions. Naturally, these institutions had to be rebuilt according to new democratic and market conditions, however, the mere fact of their existence, an unambiguous law, the possibility to provide clear answers to fundamental questions as to who was to take control over borders, to enjoy monopoly on legal enforcement, levying taxes, regulation of money circulation broaden the range of possible alternative programs for the implementation of post-socialist reforms and the transition to a market economy. The noted countries enjoyed a real opportunity to choose between more radical and resolute transformations, like in Poland, or attempts to retain a broad circle of institutions inherited from the socialist era, as in Romania.

In the post-Soviet zone, the breakup of the union state and the consequent institutional vacuum substantially narrows the freedom of maneuver and objectively puts into focus another set of alternatives. In autumn 1991 the Russian authorities were confronted with three key challenges:

1. The union state de-facto was no longer in existence. The Russian state de-jure was not independent and had no basic government institutions. The events of autumn 1991 showed that nobody had any idea as to what would happen if

troops located in Russia had received contradictory orders from the Russian and USSR authorities. The Russian authorities then had to formalize the de-facto breakup of the USSR by legal means, and to form government institutions.

2. The RF Constitution and the system of government agencies were inherited from the Soviet period and were hardly compatible to the radically changed conditions. The Constitution did not provide unambiguous answers to the question of division of powers between the branches of power, and the Federation and its Subjects. The Congress of the People's Deputies elected in the Soviet era could not adequately respond to the new political realities that arose after the August events. It was necessary then to pass a new constitution and hold new elections.

3. The socialist administrative economic system practically discontinued to operate. The system of supplies was paralyzed, grain procurements fell to zero, and consumer markets fully collapsed. The overwhelming majority of regions introduced food coupons, though failed to back them up with consumer goods and foodstuffs. It was necessary either to immediately renew the functioning of the old government system, with its brutal repressions and compulsory grain procurements, or to launch market mechanisms capable of overcoming the crisis with supplies to big cities.

As a matter of fact, the existence of the first and second fundamental problems that obviously could not be resolved within several weeks excluded a possibility of opting for the former of the two above mentioned plans. That is why at that time the problem of an immediate launch of economic reforms and price liberalization discontinued to be the core of economic and political debate.

The essence of the alternatives facing the nation was different and included two components:

First, whether it had been possible to unite in time solutions of all three fundamental problems: the legal deconstruction of the USSR, passing a new Constitution, and the start of economic reforms; and

Second, given the conditions of a clearly incomplete process of institutional and legal formation in the new economic state, how one should launch market mechanisms, overcome the crisis with supplies to big cities, if he had both no crucial traditions and institutions for a market economy and even minimally necessary prerequisites for its functioning (a functioning monetary system)?

The possibility of a simultaneous implementation of political and economic reforms formed a hot issue in autumn 1991, and it is still debated in numerous papers highlighting Russian history in the past decades. In his provocative and thoughtful book on the Russian revolution of the late 20th century[xx], M. McFaul argues that the refusal to immediately dissolve the Congress of People's Deputies, to pass a new Constitution and hold new elections, was a grave error at the time. I cannot agree with this conclusion. Mr. Yeltsin had no constitutional powers to dissolve Congress, and such an idea was extremely unpopular among the Deputies, thus making chances of passing this decision equal to zero. It should also be noted that the Russian authorities lacked any power agencies to dissolve the Congress by force. It was also impossible to explain to the nation why right after suppressing the August coup together with the Deputies, the RF President then clashes with the majority of Congress. At the same time, the suspension of Congress's and the Supreme Council's operations and powers, along with new elections, would have made it impossible to formally dissolve the Soviet Union. These institutions were necessary for the process to be legitimized by the effective Parliaments of its Republics. In addition, it was to risky to sustain a paralyzed state in a country full of nuclear weapons.

All that dictated the choice of priorities - an immediate formation of the Russian government, the start of building viable government structures, and the launch of economic reforms. All this needed to occur while the political reconstruction of the Russian state itself went on. The adoption of a new constitution was to be postponed. Such a compulsory decision practically predetermined the inevitability of a growing crisis of dual power sharing (*alias dvoyevlastie*), and the consequent limited possibilities to pursue a consistent economic policy in such a situation. Finally, a dangerous political conflict of September-October 1993 ensued. Such a background excluded any possibility of a successful implementation of accelerated disinflation. So, it was at that time when a long period of high inflation, soft monetary and budget policies and the roots of soft budget constraints took firm hold as economic and political reality.

There was another serious challenge: how, lacking control of a single central bank over money circulation throughout the former USSR and any possibility for its former Republics to immediately introduce their national monetary systems, can one preclude that hyperinflation could have reproduced the crisis with supplies in big cities even under free prices. However, this is another story[xxi].

All the above does not at all mean that the inaccurate ideas regarding the main problems of post-Soviet transformation that had dominated at the start did not have a serious impact on the actual development of the situation. One should just acknowledge the fact that the reality appeared substantially different from the capricious picture that currently prevails in papers on the history of reforms.

As far as key challenges that determined the economic dynamics throughout the post-Soviet zone are concerned, which of them were not adequately realized at the moment the Soviet Union collapsed?

1. The duration of the post-Soviet recession.

As noted above, in the late ‘80s the existence of the post-Soviet recession was not evident. The events in Eastern Europe set a certain standard that became a focus for those who developed programs for the post-Soviet zone. The start of economic growth in Poland in 1992 and the consequent beginning of economic growth in Hungary and the Czech Republic caused the illusion of pre-set time frame (3 to 4 years) for the post-Soviet recession. Excessive expectations with regard to the term of renewal of economic growth generated dangerous illusions that encouraged experiments in the monetary and finance sphere as well as attempts at an early acceleration of the scope of economic activity. These attempts, as a rule, ended up in an acceleration of inflation and fall in demand for money.

2. Time lags in structural reforms.

Property does matter - the fairness of this thesis was also proven by the past decade of transformations in the post-Soviet zone. As some research works, including studies done by the Institute for the Economy in Transition[xxii] that I have a honor to head, show the enterprises that find themselves under control of outside owners not related to management have performed far better than average enterprises in the given sample. These studies also show that public enterprises have proven to be substantially worse in this respect. The basic hypothesis underpinning decisions made in this particular field - should property rights be set clearly and rules of the game on the market be equal would the quality of property management improve gradually as a result of privatization - has proven to be correct. However, there was a serious underestimation of the time period needed for the projected outcome to occur.

3. The danger of copying institutional decisions that have worked perfectly in developed market economies.

In the developed market society the system of institutions is a product of its complex and long historical evolution, including: survival through European feudalism, a long experience with taxpayer democracy, reactions to social challenges of the early industrialization, and crises caused by a rapid acceleration of economic growth between the 19th to the 20th centuries. The young democratic states emerging on the ruins of the Soviet Empire did not experience substantial elements of such a history. This caused confusing ideas regarding the import of set of Western European or United States institutions to the post-Soviet zone. To the greatest extent this should be attributed to the tax system. The tax establishments formed in the noted zone in the early '90s in many aspects copied the European examples from that time period. From the formal perspectives, they were not worse or better than the majority of European tax systems: those were systems with high marginal tax rates and a broad spectrum of tax benefits implanted onto the post-Soviet economic life. However, they objectively encouraged the large-scale emergence of a shadow economy and excluded enterprises unwilling to adopt "tax planning" schemes. It was after the accumulation of some experience several years after the start of reforms that the we arrived at the realization of the fact that with our background and quality of our bureaucracy, we could not afford having as bad a tax system as the one the Europeans enjoyed.

4. The danger of disinflation strategies, including fixing the exchange rate.

The past decade, more specifically, the Asian crisis of 1997-98 and the fresh Argentinean experiences have provided a convincing demonstration of risks inherent in pursuing disinflation programs that use an exchange rate as a "nominal anchor". However, as early as the beginning of the '90s there were no such experiences related to currency crises of the 2nd and 3rd generations. As a matter of fact, the emergence of this new type of crisis was absolutely unexpected for the major participants in decision-making processes of the world economy[xxiii]. In 1992, however, it was the trivial fact of lacking foreign exchange reserves needed to implement an exchange rate-based disinflation policy rather than the understanding of the respective risks that formed a major obstacle to pursuing such a policy. It was later - in the course of implementation of the stabilization program of 1995-97 and the crisis of 1997-98- when the dangers of a rigid exchange rate policy showed themselves clearly.

5. The interrelation between financial stabilization and hard budget constraints that take root at the enterprise level.

In the late '80s, it was J. Kornai's Economics of Shortage[xxiv] that was likely to be the most popular monograph regarding socialist economic systems among future Russian reformers. The book specifically addressed the role played by soft budget constraints in a socialist economy. In light of this book, it was just impossible to ignore the key role the hardening of budget constraints played for the formation of a functioning market economy. As well, one could not ignore the importance of anti-inflationary policy during the conditions of a severe inflationary crisis. What was not really understood during the periods preceding the reforms and during the early stages of reform was the strict interrelation between micro and macro-economic aspects of a stabilization policy, and the impossibility of ensuring the hardening of budget constraints at the enterprise level without the framework of a consistently implemented disinflation policy.

Now, some words in conclusion.

The tremendous socio-economic turmoil during the collapse of the socialist system, the Soviet Union, and the Soviet Empire in Eastern Europe ushered in dramatic challenges for many weak governments. As it happened during the time of other turmoils, their weakness is not determined by the concrete personalities representing them,. Vladimir Lenin was a rather strong, brutal and committed personality. However, the Bolshevik government he headed proved to be unable to efficiently collect taxes or to ensure normal functioning of state machinery between 1917 to 1922. The reasons for such a failure was the absence of the traditional legitimization of new power institutions that substituted for the old ones, a lack of consensus among the elites and the society on the rules of the game, and the readiness of participants in the political process to change the rules at any moment. Hence, one notes an ultimately narrow frame for freedom of maneuver, a pre-set choice in favor of political pragmatism, and a limited role for ideology.

The Jacobin government was well aware that it was bad to print unsecured money, and the same can be said about the first Russian pro-reformist government. However, the Bolsheviks of 1917-21 did not see any ideological flaws with such policy. Nonetheless, in all three cases inflationary financing was determined by the government's inability to collect taxes or limit public expenditures, rather than any ideological preferences. Given that for the French Termidorians price liberalization and the renewal of free trade were ideologically natural, the same can be attributed to the Russian reformers. Concerning the Bolshevik party, the transition to the New Economic Policy, the renewal of free trade and the abolition of compulsory grain withdrawals led it to an ideological crisis. However in all three cases the respective steps were pre-set by the impossibility of withdrawing material resources in sufficient volumes, reallocating them by means of administrative enforcement, and ensuring proper supplies to big cities.

The collapse of the socialist experiment has decreased the attractiveness of Marxism as a secular religion. However, it does not mean that Karl Marx should be crossed out from the list of the most serious past researchers in the socio-economic arena. I think that today those who analyze the causes of the collapse of socialism and its consequent developments should reread his works.

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[i] This is of course a stylized picture, however it appears fairly close to what is such a serious analyst as J. Stiglitz argues. Stiglitz J. Whither Reform? Ten Years of the Transition. World Bank. Annual Bank Conference on Development Economics, Washington, D.C., April 28-30, 1999.

[ii] The in-depth research into the logic of socialist system functioning is Kornai J. The Socialist System. The Political Economy of Communism. Clarendon Press. Oxford. 1992.

[iii] For more details see: Ye. T. Gaidar " Anomalii ekonomicheskogo rosta" [Anomalies of Economic growth" Moscow., 1997.

[iv] Mau V. Starodubrovskaya I. The Challenge of Revolution. Contemporary Russia in Historical Perspective. Oxford University Press, New York. 2001.

[v] It was not accidental that regardless of the moment of the start of reforms in the major part of eastern European countries, 1990 became the first year of production slumps

[vi] Olivier B. Kremer M. 1997. Disorganization. Quarterly Journal of Economics. November. Vol. 112, No.4. P1091-1126.

[vii] An obvious exception proving general rule was the former German Democratic Republic whose new managerial elite mostly was exported from the former Western Germany.

[viii] Interestingly, one of the most consistent opponents to L. Balzerovizch, G. Kolodko, then Minister of Finance in Poland, in 1991 published a paper with a very characteristic title - “The missed Chance”

[ix] See, for example.: Transition Report 1999. EBRD

[x] See for example. De Melo, Martha, Cevdet Denzier, Alan Geb, and Stoyan Tenev (1997), ‘Circumstance and Choice: The Role of Initial Conditions and Policies in Transition Economies’, World Bank Policy Reserch Working Paper №. 1866, Washington: the World Bank.

[xi] Berg A., Borensztein E., Sahay R. and Zettelmeyer J. The Evolution of Output in Transition Economies: Explaining the Differences. IMF Working Paper. 99/73. May 1999.

[xii] The paper by S. Fischer and A. Gelb publisged in 1991 reflect ideas prevailing among key designers of reforms of that time and shows that they did not at all ignore the need in a serious attention to building institutions.. Fischer S., Gelb A. Issues in Socialist Economy Reform. Journal of Economic Perspective, 1991. Vol.5. No. 4. P. 91-105.

[xiii] The failures of the Russian reformers who started transformations between proved to be of a similar nature

[xiv] For what is likely to be the most qualified articulation of this point of view that enjoyed a great popularity at the beginning of transformational research, see: G.Calvo, F.Coricelli. Output Collapse in Eastern Europe: The Role of Credit - The Macroeconomic Situation in Eastern Europe. World Bank and IMF. 1992.

[xv] Dombrovsky M.. Fiscalny crisis v period transformatsii [The fiscal crisis in the period of transformation]. Warsaw, 1996; Hemmins. R., Cheasry. A., Lahiri. A. The Revenue Decline - Policy Experiences and Issues in The Baltics. Russia and Other Countries of The Former Soviet Union. Wash. 1997; Ye. Gaidar Detskie bolezni postsocialisma. (K voprosy o prirode budzhetnykh processov etapa finansovoy stabilizatsii) [Children’s illnesses of socialism (On the problem of the essence of budget process on the financial stabilization stage)] – Voprosy ekonomiki. 1997. № 4, C.4-25.

[xvi] For more details on the interrelation between slow disinflation and the emergence of soft budget constraints, see:.: Yegor Gaidar. The Legacy of the Socialist Economy: The Macro- and Microeconomic Consequences of Soft Budget Constraints. // Mario I. Blejer and Marko Skreb Transition the First decade. The MIT Press, Cambridge, Massachusetts, London, England. 2001. P. 293-326.

[xvii] The interconnection between the dissipation of the fear and the start of the breakup of the socialist empire is highlighted brilliantly in a book by Amb. John Matlock, at that time the US Ambassador to the USSR J.F. Matlock, Jr. Autopsy on an Empire.

The American Ambassador's Account of the Collapse of the Soviet Union. Random House. New York. 1995.

[xviii] On the interrelation between the political and economic crises in the USSR, see: Leon Aron. Yeltsin A Revolutionary Life. St. Martin's Press New York, 2000. And Anders Aslund. Building Capitalism. The Transformation of the Former Soviet Bloc. Cambridge University Press, 2002.

[xix] The emergence of the situation in the territory of the former USSR could resemble the situation in Yugoslavia. However by that time the latter had long been a market – oriented socialist economy. As far as Czhechoslovakia is concerned, the "divorce" was well organized there, and it was completed in the frame of already functioning market economy.

[xx] Michael McFaul. Russia's Unfinished Revolution. Political Change from Gorbachev to Putin. Cornell University Press. 2001

[xxi] Gaidar Y. Days of Defeat and Victory. University of Washington Press. Seattle and London. 1999.

[xxii] Radygin A., Entov. R.. Corporativnoye upravlenie i zacshita prav sobstvennosti: empirichesky analyz i aktualnye napravlenya reform.[Corporate governance and protection of property rights: empiric analysis and current directions] Institute for the Economy in Transition. Moscow. 2001.

[xxiii] J.Breadford DeLong, Barry Eichengreen, Between Meltdown and Moral Hazard: The International Monetary and Financial Policies of the Clinton Administration. National Bureau of Economic Reseach. August 2001. Working paper 8443.

[xxiv] Kornai J. Economics of Shortage. Amsterdam, 1980.