Transition challenges

Original paper
330.342.14/.151

Breakdown of the Transitional Model for the Passage from Socialism to Capitalism

VLATKO MILETA

Faculty of Political Science in Zagreb
Professor of International Economic Relations

Summary

The article deals with transitional countries that, after initial successes, found themselves beset by a plethora of predicaments, among which massive foreign loans are only the tip of the iceberg of the exigencies they have to cope with.

The author argues that due partly to subjective reasons and partly to inapt advice, there has occurred the deliberate devastation of manufacturing capacities and the indiscriminate capital influx that has on the one hand stimulated economic recovery, but on the other created considerable quandaries, so that the professed achievements are increasingly dubious.

The author places the transitional countries' foreign debts into the context of universal excessive borrowing in the world that exceeds 2,000 billion dollars. The author is trying to shed some light on this global problem by means of the theory of the "third way", that has been gaining legitimacy in the debates on the future of world industry and society.

The belief that after the collapse of communism the transitional states were to go through a period of rapid recovery and dynamic growth by a quick transformation of the socialist into the capitalist system, soon proved completely unfounded. Instead of success, the transitional states went through a series of failures; since they are not able to drag themselves out of the early morass of the transitional process, the problems are compounded and their end is nowhere in sight.

The crisis of Russian economy has demonstrated the full weight of the transitional problems and exposed the unfeasibility of official and unofficial advice on a fast recovery by relentless devastation (understandable in ideology and politics, but not in economy).

Just as the nature dislikes leaps, economy does not tolerate them as well. The nationalization of everything under the sun was one such leap and it is well-known where it has brought us. Transition is a similar leap and God knows where it could lead us.

Marshall observed a long time ago that economy does not stand leaps. A hundred years ago, he promoted a natural principle for economy – *Natura non facit saltus* – using it as a motto for his “Principles of Economics” (1890). Although an advocate of *laissez faire* capitalism, he does not have only words of praise for free competition, but also criticises it, which makes him one of the first theoreticians who realised that the free market “philosophy and practice” could not solve (even then) urgent problems of the poverty of big populations nor create prosperity – which has been promised to us, too.

Another major bourgeois economist, W. W. Rostow, in the book with the subtitle *Anticommunist manifesto* (The Stages of Economic Growth, 1960) refutes the Marxist theory of economic development but also lists serious objections to the developments in capitalism.

Particularly under fire have been the conceptual conditions of the transitions from one phase of social development to another, so dear to Marxists, and now to liberalists, particularly those in MMF, who indiscriminately dole out identical advice in completely different situations of transitional states.

By analysing the ascent and development of capitalism, Rostow came to the conclusion that this is not a synchronised process, let alone equivalent and simultaneous. According to him, this is a process that began in different countries at different time, and the whole development has been adjusted to specific circumstances and needs. That is why it is so difficult to talk about capitalism as an integral phenomenon, since there are in fact as many capitalisms as there are contemporary states.

In light of Rostow’s conclusions, one must ask: can the transition from socialism to capitalism for all transitional states be performed according to the same rules and the same recipe?

Judging by the transitional results – it obviously cannot. Instead of the one approach, variety is called for. Had there been variety, then perhaps the transitional outcomes would have been more propitious. But, there has been no such variety. The model supported (still) by the MMF, the World Bank and even the European Bank, has wrought havoc in transitional countries. As things now stand, there is no transitional state that may boast of any notable successes. In some of them the situation is disastrous and Russia, in turmoil and under huge pressure, might easily explode. But that is not solely Russia’s problem. Social tensions due to the operation of the “four transitional levers” (privatisation, liberalisation, marketisation, and globalisation) are more conspicuous by day, and soon it will be clear that they are not endemic for Russia, but are a global contingency.

The difficulties of transitional states are most noticeable in their foreign debts and rampant unemployment. According to the data by *World Economic Outlook – 1997*, transitional countries’ debt has reached the stupendous 300 billion dollars, up from 153 billion dollars at the beginning of the transition. Some transitional countries use up more than half of their national budget just to pay off their foreign debt.

The biggest share of the total foreign debt is Russia’s and it amounts to 41.3%. Without Ukraine and Belorussia, the states of Central and Eastern Europe own more than 159 billion dollars (52% of the total debt). In 1997 these countries had to pay back 33.9 billion dollars and in 1998 35.4 billion.

That is why all the indicators about the more successful or less successful development of transitional countries are very dubious as is the rate of their annual economic growth, since the other side of its coin are their huge foreign debts. In fact, the repayments are bigger than the net income from the export of goods and services i. e. the total debt is almost as big as the total export of goods and services. This means that if the total export of goods and services is 100, then the total debt for 1998 was 98.1%.

Total Foreign Debt of Transitional Countries of Central and Eastern Europe
(in billions of US dollars)

	1996	%	1998	%
Czech Republic	28.6	11.02	23.0	7.71
Hungary	27.6	10.64	23.6	7.91
Poland	42.8	16.50	44.8	15.02
Slovakia	7.8	3.00	11.5	3.86
Slovenia	4.0	1.50	4.3	1.40
Russia	123.1	47.47	170.7	57.22
Bulgaria	9.7	3.70	9.9	3.30
Romania	8.5	3.20	10.5	3.50
CROATIA	4.8	1.85	7.9	2.60
Total:	**259.3**	**100.00**	**298.3**	**100.00**

Calculated according to: Business Central Europe, The Annual Report, 1997/98. For Croatia (1998) according to the data from journals.

The unsatisfactory state of economy is reflected in unemployment as well. The process of transformation is accompanied by privatisation and lay-offs of in the former system ostensibly necessary workers. Workers have also been laid off because of the privatisation, since industrial plants have been shut down or have changed their line of production. Local and foreign entrepreneurs have behaved in the same manner. Frequently, the method of devastation has been used in order to purchase certain property for ridiculously small amounts.

It might be said that the increase of the foreign debt of transitional states has been accompanied by increased unemployment and extreme pauperisation of the populations. According to the *World Development Indicator* estimates, the transitional part of Europe has been swept by a wave of people who spend less than one dollar a day, an estimated 4 million people. Compared to other parts of the world it is an insignificant number (there are more than one billion and 227 million of such people in the world); nevertheless, it is worth mentioning because such statistical data are remarkable (p. 31, 1997).

As we have shown, Russia's debt accounts for the largest part of the foreign debt of transitional countries. All major systems in that country are collapsing. We might say that nothing works, with the exception of the system of capital-drain by the newlycomposed owner class; it is estimated that they have illegally siphoned more than 40 billion dollars off to their secret bank accounts in various foreign banks.

Some international institutions and their administrative/professional apparatus have joined this merciless privatisation. This is true above all for the MMF and the European Bank. The World Bank and its affiliated banks have distanced itself from such behaviour. The analysis of the European Bank's investments shows absolute domination of the financial sector. This is so even for those transitional states whose top priority lies in other sectors e. g. in food production, so badly needed by the local populations (Albania, Bulgaria, Romania).

According to an analysis of the Bank's policy of financing transitional countries, more than 40% of the investments have been funnelled into the financial sectors, a completely different picture than the one advertised through the media. If one were to believe their pitch, the European Bank for Reconstruction and Development is an unstinting source of financial aid for the recovery of transitional countries. However, the reality is something completely different; in it, other interests are much more crucial.

One among them, perhaps the most important, is supporting the process of an all-out privatisation, which is just a disguise for a new pillage, and has turned out to be the counterpart to total nationalisation. In the former case everyone is robbed for the benefit of some, while in the latter some have been robbed to the benefit of, say, everyone. In this way the government's decisions have created a new class of owners, whose prior concern is how to amass the biggest possible wealth in the shortest possible time and transfer it to a safe haven abroad.

The awareness that ownership obliges, so pervasive in the Rhinish model of capitalism is alien to the *noveau* owners; they advocate capitalism that does not oblige and in which somebody else should solve the problems they cause with their actions. Thus major Croatian banks have unashamedly demanded that the state subsidises their dubious claims, though they were the ones who loaned huge amounts of money to "shady" clients without any collateral. Paradoxically, but the state has been doing just this, justifying it with the stability of the economic system.

The scandalous process of transformation has been unravelling in full sight of international public without any protestations. As if the right to a dignified life were not one of the basic human rights. Human rights without economic rights are but a deception or even worse – undisguised ideology. And the populations of transitional countries have had enough ideology.

Open ideology means explaining that market is the almighty factor that balances all and sundry. In its international aspect, the market has never functioned like that and never will. If one is to believe to Schumpeter, we can speak of the global liberal market up to the beginning of World War I. The war, the crisis and the later war moved the global market away from liberalism and it is uncertain whether the World Trade Organisation and the bombastically announced American globalisation will ever reverse the trend.

As we have shown, the major theoretician of the internal liberal market, A. Marshall doubted the omnipotence of liberalism at the level of domestic markets. He had demanded government intervention, just like it was demanded a century later by the leading states gathered in the G-7 (+1) group, by numerous leaders of the global system and the big international associations, such as the MMF and the World Bank.

It is obvious that the model recommended to transitional states is no longer efficient, so its replacement is demanded by many different people and by many different approaches. Even Americans have tried to change it in relation to Latin America by the innovative concept of NAFTA, though on the surface it may not seem so.

At present, the key factors of the international space are preoccupied with the idea of the third way. The third way concept was recently discussed at the seminar on democracy at the School of Law at the University of New York (September 29, 1998, as reported by the American Week Review).

At the seminar, the theoretical rationale of the so called third way was for the first time presented at the government level, as a common denominator for global politics in the economic sphere which would be dominant in the coming years.

The advocacy of the third way modestly surfaced in certain plans about the need for the reconstruction of the MMF and the World Bank in the early eighties, when another global crisis proved that the old methods of financing the development of many countries cannot lead to progress.

This policy only managed to increase the foreign debt (which amounts to 2,000 billion US dollars only for the developing countries) and the wealth of one group of states proportionally to the poverty of another group of states; this condition has prompted experts to design numerous schemes for breaking that vicious circle.

The things got complicated with the appearance of transitional states, since the foreign debt increased for another 300 billion dollars, which makes it more obvious that there is going to be the global collapse unless the "philosophy" of production is changed.

Hence the need for a new approach which was best advanced at the seminar by British Prime Minister Tony Blair. Unlike Blair, American President Clinton still does not believe in the third way policy. He countered with he idea of an "active and disciplined government and community in which everyone contributes" since, in his opinion, it is hard to believe that the third way model is going to bring forth a viable economic policy that would foster growth, lower unemployment and increase savings for social services so that people would believe they live in a just society.

Unlike Clinton who links growth and employment with an "active and disciplined government and community", Tony Blair links the "third way policy" with progress and justice. For him, it is an alliance between progress and justice. That is a policy which is trying to return to essential key values: community, social justice, belief in strong society as a prerequisite of individual fulfilment, the policy which has given up on the old leftist attitudes, with their government and state control over taxes and consumption, but does not incline towards "laissez-faire", either. This is a policy that acknowledges community as an economic factor, because it offers everybody access to education, technology and infrastructure, but does not try to manage firms and burden them with excessive regulation.

According to Blair, the policy of the third way in the economic sphere recognises the role of communities (states), but differently from their traditional role. He sees it as a combination of the public and the private, the voluntary sector as a new "form of government" and solution of social problems.

Blair thinks that the international sphere should be governed along the same lines, because only in that way the political in-fighting going on in the international arena between the internationalists and the isolationists might be alleviated and the dramatic oscillations that are its consequences eliminated. Blair thinks that it is not possible to resolve international problems, particularly those in the economic sphere, if there is no will to restore international institutions and enter a new, different period of international partnership.

That is the bottom-line. Indeed, the question is whether there is enough good will to reinstate international institutions in order to raise international partnership to a higher level. Also, is there enough good will in the third way policy to pull transitional countries out of the crisis which has been precipitated not only by their own fault.

Judging by the gloomy predictions about the perspectives of global industry at the end of the 20th century, voiced ate the annual meeting of the World Bank and the MMF (Washington, October 6-9, 1998), there is going to be less readiness to help transitional countries in that respect, simply because the developed countries will have to address their own internal problems which are already looming.

In such context, it sounds unusual when American President calls for the solidarity of sensible and symphatetic people and offers solidarity instead of momentous changes, by which he in fact raises subjectivism to the level of the universal belief of people that they live in a just society, if they *believe* they really do.

These are the reasons that make the debates on the third way for transitional countries, on the one hand, pure wishful thinking, and on the other, a powerful tool in the battle against those who still advocate the transformation of social ownership as primitive accumulation, in which the concentration of the productive social capital is permitted without any legitimacy whatsoever and with dubious legal background.

So, transitional countries cannot deal with the "philosophical" issues of the third way when preoccupied with the question of how to "survive" in the circumstances of devastated and ravaged economies and how to pay back foreign loans, taken recklessly and under harsh terms.

Instead of the third way, they have to devote themselves to the fundamental issues of putting the destroyed systems back into operation, the task that – obviously – cannot be fulfilled by any sort of private entrepreneurship. No entrepreneurship can link the Russian vast spaces that lie behind the Ural Mountains, except the state, the only one with the necessary strength and obligation to do that.

Croatia definitely needs "the third way". Small states – and by all parameters Croatia is a small state – cannot develop on Clinton's model of strong government and solidarity of "sensible and symphatetic" people. Croatia must reestablish progress and justice, return to the politics that recognises the community as an economic factor, that approaches each activity in a specific way and is not a "slave" to any schemes and "outside" recommendations. The trend by which Croatia has turned into a state of traders must be stopped, since somebody has to employ people.

The new owners obviously have not been doing it. This has been corroborated by a statement by Croatian Prime Minister that he is fed up with those transitional winners who solve their problems by laying off employees. The problem, however, is that this twist in the economic policy will have to occur in much harder circumstances of the impending crisis which has already hit some world regions and is slowly encroaching upon transitional countries.

It is baneful to live believing that water can be drawn from a well indefinitely. It is even more baneful to believe that there is a universal way of the transition from socialism into capitalism and that the same aspirin will universally cure all economic headaches.