

*The Political Economy of Asian Transition from Communism*

edited by Sujian Guo

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reviewed by Michael Hatziprokopiou\*

The process of transition from a centrally planned to a market oriented economy, undergone since the late 1980s by former communist states all over the world, is characterized by two distinct approaches. First, the radical or “big bang” or “shock therapy” approach, under which a comprehensive set of reforms is introduced simultaneously and in the shortest possible time: large scale privatization, lifting state control over major factors of production and exchange; decline of the communist party power; building of democratic institutions – these are its main distinctive characteristics. Accordingly, the transition from plan to market, as coordinating and resource-allocating mechanisms of the economy, has an overall character and is coupled with transition from a one-party authoritarian state model to a model based on the principles of the multi-party representative democracy. The underlying idea is a complete break with the past and the vision of a new non-communist world. This is the path followed by the communist countries of central and eastern Europe.

Second, the gradualist and multi-stage reform approach, in which reforms have a partial, gradualist and experimental nature. Accordingly, the reforms to be introduced are selective and applied on ‘a trial and error’ basis, in small doses and in sectors that are not very significant and for which pay-offs are expected to be quick; they are strictly restricted to the economic sphere and the existing political system remains unchanged with the hegemonic role of the communist party not being questioned in any way. The underlying idea in this case is improvement of the production and allocation mechanisms, there is no break with the existing ideological and political principles and the vision of a communist world remains unchanged. This path was adopted by the communist countries of the Far East (China, North Korea, Vietnam, Laos, Cambodia). It is this second path that Sujian Guo’s book addresses. What makes this book interesting is the attempt by the author to go beyond mere description of what is currently happening there and his attempt to theorize and draw general conclusions.

\* Universities of Macedonia in Thessaloniki, Greece and New York in Skopje, FYROM

The difference in the paths of transition is often attributed to differences in initial conditions or economic structures existing before the initiation of reform. Asian economic structures - in comparison with Europe - were characterized by a large agricultural instead of an industrial sector, huge instead of limited supplies of labor and a rise instead of a decline in the power of the Communist Party. In addition, the five Asian communist countries under study - despite national differences and local particularities - share a common set of developmental and historical experiences, giving sense to a discussion of general causes and dynamics. Thus:

- All Asian communist countries passed through an initial stage of communist power consolidation and establishment of a soviet type economic planning system. During this stage the State strove to achieve industrialization, develop heavy industry, implement collectivization in agriculture, nationalize industry, banking and trade and abolish private economic activity. At the same time, in the political sphere, party and government administration were increasingly centralized and party-state power was gradually institutionalized. (China up to 1956, North Korea 1946-1967, North Vietnam up to 1975, South Vietnam 1975-1979, Laos 1975-1979, Cambodia 1979-1989).
- A second stage, marked by the effort to accelerate economic development, is observed in almost all communist countries of the Far East with the possible exception of Vietnam. The effort was based on the principles of self-sufficiency and full utilization of domestic resources through ideological appeals and mobilization of the masses. Communes were established in the agricultural sector with authority, control and responsibility over the means of production but also over various activities connected with administration, security, education, small-scale industry, provision of meals, major public projects, etc. The targets set were unrealistically ambitious and the result was economic failure, famine and hardships for the people. (Chinese "Great Leap Forward": 1957-1960, North Korean "Flying Horse March": 1958).
- A period of readjustment followed with reorganization of the communes, decentralization of the decision-making process and adoption of pragmatic approaches to the solution of economic problems (China: 1961-1965).
- The readjustment period was followed by the Cultural Revolution in China and similar policies in other countries of the region (Vietnam and Laos seem to constitute the exception). The ultra-leftist outlook adopted stressed self-sufficiency, emphasis on moral and political incentives, ideological purity, "class struggle" and denunciation of pragmatic policies for production and industrialization as "capitalist" and "revisionist". The economic disorganization, which followed, was much more extensive and the results much more disastrous than those of the Great Leap Forward. (China: 1966-1976, North Korea: The Three-Revolution Team Movement till late 1960s, Cambodia: The Khmer Rouge regime 1975-1979).

- A new stage of readjustment started with the end of the Cultural Revolution. A careful, gradualist and experimental open-door policy initiating a sustained effort to introduce economic reforms was adopted. The role of market mechanisms was gradually increased at the expense of state planning and administrative control and material incentives and partial decentralization were encouraged. In China economic liberalization started with replacing the communes with 'the household responsibility system', promoting foreign trade and forming farmer markets and free economic zones. Similarly, in North Korea economic reforms concentrated on the creation of free economic trade zones, free farmers' markets and private enterprises; light industry, partial trade decentralization and private farming were developed. In Vietnam readjustment and liberalization came after the withdrawal of the U. S. and the unsuccessful attempt to collectivize agriculture in the South. Similarly, the failures of central planning seem to be the main reason for the introduction of market mechanisms in Laos and Cambodia. (China: 'the Four Modernizations': 1978-1992, N. Korea: especially after the early 1980s-2002, Vietnam: 1978-1986, Laos: 1970-1986, Cambodia: 1979-1986).
- The last stage, currently experienced by all countries of the region, is that of establishing market socialism. According to the author market socialism (state ownership without state control) is a socio-economic system, applied in the past in Yugoslavia and Hungary, clearly different from the system of the planned command economy (state ownership combined with state control) developed in the Soviet Union or from the system of state capitalism (private ownership with state control) adopted in Taiwan and South Korea. Market socialism, however, is very far from the free market economy (private ownership without state control), such as 19th century U. K. or pre-New Deal U. S. (China: 1992, N. Korea: 2002, Vietnam: 1991, Laos: 1986, Cambodia: 1993).

Sujian Guo, however, argues that initial conditions alone can only explain the necessity of the reform process. They do not have the power to explain the particular path the reforms will follow. It is elite strategic interactions and policy choices that play a direct role in shaping the particular pattern of transition. This means that factors such as conflict of political ideologies, struggle, splits, interaction and compromises among the various leadership groups, political resistance and support, uncertainty regarding the outcome of the reforms, distribution of gains and losses, etc. are very important in shaping the particular transition pattern. In the case of the Asian countries under study, it seems that the transition path was determined not so much by the initial conditions but by the interplay between economics, e.g. the necessity for economic growth on the one hand and politics, e. g. the preservation of party-state interests and power on the other.

According to the author reforms do not come out of the blue. They are the outcome of a series of domestic and international factors, generated in the social, economic,

ideological and political sphere. Thus, the transition process is initiated by a crisis on the economic level, which is followed by a crisis in the ideological sphere. It is true that after a period of initial success and high growth rates the limits of the soviet-type centrally planned economy became apparent. Low productivity, inefficiency, developmental stagnation caused a crisis of the central planning system. The crisis was intensified by the disastrous economic results of leftist policies in China and in other countries. Economic stagnation and comparisons with the western world adversely influenced ideology and shattered the faith of the masses, the cadres and the leadership in the future of central planning. The people and political elite then started questioning the superiority of the command economy and were gradually persuaded that the introduction of market mechanisms was absolutely necessary to get out of the crisis. This was a point of general agreement among the various elite political groups in the Asian communist world. Similarly, there was a more or less general understanding among the leaders, radicals and conservatives as well, about the ultimate objective of the changes sought. The objective of Asian communism was to make the system more productive and efficient under the existing social order and without questioning the basic ideological principles and visions of communism. Therefore the disagreement over strategic choices and the conflicts and debates related to it had to do not with the idea of reforms as such but with the extent, the content and the sequence of the reforms. The conservatives recognized the necessity of reform, but at a slow pace and only in the agricultural sector and other non-strategic industries and with maintenance of control over investment and foreign exchange. On the other hand reformers had a broader vision of the necessary changes and advocated a faster pace in the introduction of new policies.

At this stage elite strategic choices and the interplay of politics and economics became important. Since the old elite was withdrawing from the scene and a new leadership, fundamentally different from the old one, was taking its place the balance of power was turning in favor of the reformers. Approximately half a century after the end of the Second World War, the old guard of revolutionaries was withdrawing from the scene. A new generation of technocrats, better educated and open-minded, dominated the key decision-making bodies. This new leadership had in the history of socialism examples of successful and non-successful attempts to introduce market oriented reforms. Such examples were Lenin's NEP, the Yugoslav Workers Participation Model, the Hungarian Gulash Market Socialism, the Czechoslovakian Socialism with a Human Face, Kosygin's reform effort, Gorbachev's Glasnost and Perestroika.

Economic developments in communist Europe in the late 1980s accelerated the reform process in Asia. The shock from the collapse of the Council for Mutual Economic Assistance and the resulting damage to inter-communist trade and loss of economic and technical assistance from the Soviet Union greatly influenced the liber-

alization process. Here again the impact was not the same for each country. Internal dynamics had greater weight in large countries such as China and international developments were more important for small countries such as North Korea and Laos. In any case, the reform process in all countries under study usually starts with agriculture and proceeds to prices, trade liberalization, financial policies, enterprise, share-holding reforms, etc. The changes include: increasing application of monetary and fiscal policies, pricing on the basis of cost and international market reality, decentralization of investment decisions, allowing individual household farming, constitutional recognition of user rights, encouragement of light industry, development of land and labor markets, separation of central and commercial banking, legalization of foreign exchange transactions, integration of the economy into the world exchange and production system, introduction of new legislation for contracts, foreign investment and bankruptcy, use of privatization and fees to finance social services, etc.

The study suggests that the step-by-step approach allows the development of non-state sectors without a wholesale privatization of the state sector. It also suggests that this approach encourages high growth rates and socio-economic stability. Thus the more efficient functioning of the public sector, the development of the private sector and the earnings from foreign trade have contributed, with the exception of North Korea, to high growth rates of real GDP, strikingly different from the European transition reality. For 2004 the real GDP growth rate was 8.3 %, 7.3%, 6.5%, 5.4% in China, Vietnam, Laos and Cambodia respectively. This was very important for the transition process because the economic success of the first changes opened the way for a new wave of measures and gave momentum to the reform. It should be stressed, however, that the reform steps were careful and experimental. The transition was achieved step by step and it was not always a march forward. Sometimes there were (and are) second thoughts and steps backward.

One of the fundamental questions extensively discussed in the book is the question of the nature and the limits of the reform process. It is apparent that all the countries of communist Asia are undergoing a process of transition from a centrally planned to a market based economy, although the sequencing of reform and its achievements vary from country to country. After approximately a quarter of a century of reforms these countries have come a long way from the command economy model. On the other hand, almost none of them can be characterized as free market economies since distortions continue to be severe in the sense that there is no sufficient development of factor markets and no substantial reduction in government intervention in the banking system and the exchange rate while public ownership dominates property relations. Using 10 indicators (public/private share of GDP, corporate restructuring, stock/shareholding, prices, factor markets, control of resources, financial institutions, monetary and trade policy) the author estimates that Cambodia has achieved the highest degree of economic liberalization, with Laos, Vietnam and

China in the second, third and fourth position respectively while North Korea is ranked last. The author concludes that with the exception of Cambodia, which seems to have taken the road to a free market economy the other countries are developing towards a “dual structure”, a “hybrid economic system” combining state and market roles or market socialism.

The next fundamental question discussed is that of the future of market socialism. Can market socialism become a competitive, efficient and robust economic system and thus constitute a third way of socioeconomic organization, alongside capitalism or state communism? The transition experience of the Far East has renewed academic interest in this question. Many economists argue that communist party monopoly and market economic laws are mutually exclusive because in a socialist system economics will always be subordinated to politics. The author, however, believes that the fundamental problems of market socialism (soft budget constraint, the principal-agent relations and the lack of free entry and exit of firms) can be overcome if the property rights relations, which shape incentive patterns and resource allocation, are properly restructured. What has happened up to now in the transition process is that administrative decentralization and economic liberalization have allowed the emergence of a multilevel structure of ownership but the usufruct rights –as distinct from the ownership rights- have been entrusted to enterprise managers. In other words usufruct rights are in the hands of people who on the one hand do not take risks and do not have incentives for efficiency and innovation and on the other abuse the power entrusted to them by the state. As a way out of the problem the author introduces the model of the Trustees of State Property. The trustees are not organizations of the governmental bureaucracy or administrative monopolistic corporations and they are not appointed by state officials or politicians. They are competitively selected entrepreneurs, who have imagination, managerial ability, know-how and experience. They take risks by investing personal assets in public bidding and they are bound by legal contracts with the state to maximize profits; failure to do so will entail economic and legal punishment. Their final reward depends on economic results and thus they have a personal interest in enhancing entrusted property value, ensuring efficiency of investment and maximizing profits. Thus, Sujian Guo concludes that the success of the reform process in the Far East depends on restructuring of property rights, in such a way as to drastically improve incentive patterns and lead to production and allocation efficiency. In these circumstances, a bright future for socialism can be foreseen.