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Independence and Macroeconomic Stabilization in ex-Yugoslav and Former Soviet Republics

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The breakup of the Soviet Union and the former Yugoslavia raises the question of the economic viability of the new post-Communist states. It is distinctly possible that separation was economically irrational exante, for at least some of the new states.[1] This, however, will be eternally debatable, while expost results can at least be studied empirically. The useful studies undertaken by Uvalic and von Selm, discussing the costs and benefits of the breakup of the former Yugoslavia and the Soviet Union respectively, rely more on theoretical argument and prediction than on analysis of postindependence outcomes.[2] This essay attempts a more modest task: to see whether separation has facilitated the new states' efforts to handle the urgent tasks of bringing down inflation rates and creating a macroeconomic environment conducive to economic growth.

The nub of my argument is that, while stabilization is always technically possible, it may be prevented by distributional conflicts and political barriers. National independence affects this by altering the political and social space in a once-and-for-all-manner. The breakup of a larger state into smaller components may disrupt old distributional coalitions and create a more homogeneous society in which consensus is easier to arrive at. However, it may also elevate the relative importance of distributional coalitions; what once was a relatively small fish in a large pond may now become a relatively large fish in a small pond. And these relatively large fish may be in a position to block social consensus on stabilization policy.

In short, the new countries are not automatically less polarized by distributional conflict than the larger entities they came out of. The evidence I introduce below shows that only certain new countries–those with strong independence movements and lower levels of regime continuity–achieve the most coherent stabilization results. Those with close external alliances with Western market democracies, and the smaller nations, also tend to stabilize more rapidly and more successfully. Factors such as ethnic homogeneity, political system design, income level, and the magnitude of initial separation and transition shocks play less important roles in explaining stabilization success.

In this article I consider developments through the end of 1996 in Slovenia, Croatia, and Macedonia from the former Yugoslavia; and in Estonia, Latvia, Lithuania, Moldova, Russia, Belarus, Ukraine, Turkmenistan, Uzbekistan, Kazakstan, and the Kyrgyz Republic from the former Soviet Union. (I exclude other new states because armed conflict pushed stabilization off the agenda, or at least clouded the decision about stabilization timing to a great extent: Bosnia-Herzegovina, Federal Yugoslavia, Georgia, Armenia, Azerbaijan, Tajikstan).[3] At the start, I justify the choice of stabilization as a focus by showing the connection between successful stabilization and the resumption of economic growth. In the next section, I develop ten hypotheses about the effects of separation on stabilization. In the third section, these hypotheses are compared with evidence from the fourteen countries. Some comments on long-term issues and conclusions follow.

Stabilization and Growth

Economists continue to debate whether there is a tradeoff between inflation and growth.[4] The cases of Brazil and Argentina, in which high inflation coincided with rapid economic growth in the 1970s and to a lesser extent in the 1980s, suggest that even 20 percent monthly inflation can be lived with in certain circumstances. However, significantly higher inflation seems incompatible with growth, and 20 percent monthly inflation usually precludes growth.

Table 1. Real GDP Growth in
Early and Late Stabilizers, 1994–1996

	1994	1995	1996
Stabilized by 1994			
Slovenia	5.3	3.9	3.5
Croatia	0.8	1.5	5.0
Macedonia	-8.4	-4.0	1.1
Estonia	-0.1	3.2	3.1
Latvia	2.2	0.4	2.5
Lithuania	1.0	3.1	3.5
Kyrgyz Republic	-20.1	1.3	5.6
Moldova	-31.2	-3.0	-8.0
Did not stabilize by 1994			
Belarus	-12.2	-10.2	2.0
Ukraine	-23.0	-12.0	-10.0
Russia	-12.6	-4.0	-2.8
Kazakstan	-25.0	-8.9	1.0
Turkmenistan	-18.8	-8.2	-3.0
Uzbekistan	-4.2	-0.9	1.6

Source: Data from IMF, World Economic Outlook, May 1997, 141.

Fischer, Satay, and Vegh provide a careful analysis of the inflation-growth tradeoff for all the transition countries. They argue that successful stabilization has led to the resumption of economic growth.[5] Within the group of countries studied in this paper, real GDP growth resumed within a year to a year and a half *after stabilization* in Slovenia, Estonia, Latvia, Lithuania, Croatia, Macedonia, and the Kyrgyz Republic. Among the early stabilizers, real GDP has continued to fall only in Moldova. At the same time, those nations not stabilizing by the end of 1994 had not shown signs of growth by the end of 1995, and only three of these six showed growth in 1996. Table 1 contrasts the behavior of output in those countries that had stabilized inflation by 1994 with those that had not.

Table 2. Sectoral Shifts and Output Fall

	Change of GDP Share of Industry (1989-1994, current prices)	Maximum Contraction	GDP 1996 1989=100
Stabilizers			
Slovenia	-5.8	17	97
Croatia	2.1	37	67
Macedonia	0.2	45	55
Estonia	-8.4	37	67
Latvia	-13.1	49	55
Lithuania	-3.4	58	55
Kyrgyz Republic	-11.9	40	68
Moldova	-0.3	54	46
AVERAGE	-4.2	42	62
Non-stabilizers			
Belarus	6.2	39	61
Ukraine	-12.2	64	36
Russia	-7.8	52	48
Kazakstan	12.3	54	46
Turkmenistan	23.4	39	61
Uzbekistan	-5.8	20	89
AVERAGE	2.7	45	55

Sources: Data on industry share from Martha de Melo, Cedevet Denizer and Alan Gelb, "From Plan to Market: Patterns of Transition," in *Macroeconomic Stabilization in Transition Economies*, ed. Mario Blejer and Marko Škreb, (Cambridge: Cambridge University Press, 1997). Data on maximum output fall and cumulative GDP from IMF, *World Outlook*, and Robert Mundell, "The Great Contractions in Transition Economies" in Blejer and Škreb. Averages are unweighted.+

Furthermore, the argument that stabilization and resumption of growth are connected is strengthened by the fact that the return to growth in 1996 in Kazakstan, Belarus, and Uzbekistan followed on the heels of stabilization in late 1994 and early 1995 in these countries.[6]

A further question about output decline is whether those nations engaging in stabilization programs suffered worse cumulative output declines than the others. Table 2 provides some data on the matter, but they should be examined with caution. Much of the variance in output decline must be attributed to factors other than stabilization policy. Of special importance are trade-related shocks: demand-side effects such as loss of traditional markets due to the collapse of the federations and the Council for Mutual Economic Assistance (CMEA), increased protection in former republics, and the pace of domestic trade liberalization as well as supply-side effects such as unavailability or increased cost of imported inputs and terms of trade shocks. These effects, of course, were felt in very differing degrees by different countries.[7]

Nevertheless, the data point to three observations. First, there is little evidence that stabilizers experienced sharper output drops than nonstabilizers. The maximum output contractions were very similar on average. However, because of the more rapid recovery of growth in the successful stabilizers, 1996 output in relation to 1989 was noticeably higher among successful stabilizers (62 percent to 55 percent). Given the small sample size it is not possible to draw strong conclusions, but when the specific embargo and war-related problems of Croatia, Macedonia, and Moldova, are taken into account the difference between the average output fall of successful stabilizers and of unsuccessful stabilizers suggests that stabilizers may have indeed fared better, when other variables are controlled for.

Second, the share of industry in output seems to have shrunk slightly in stabilizers and increased slightly in nonstabilizers, which suggests that after stabilization, economies may be better able to repair the excessive emphasis on industry characteristic of the communist period. Stabilization provides a less uncertain and less noisy economic environment which is conducive to the entry of new businesses into the tertiary sector.[8]

Third, stabilization of inflation does not mean its complete elimination. The experiences of the countries studied here, as well as countries in Eastern Europe, suggest that annual inflation even as high as 80–90 percent is quite compatible with growth. Such a rate of price increase can hardly be called "low inflation." Indeed, it seems logical to expect that significant inflation will be necessary to facilitate the large and frequent relative price shifts associated with large-scale restructuring.[9] Thus, the conclusion of this section may not satisfy antiinflation hawks: stabilization appears to be an important precondition for economic growth in transition countries, but stabilization to levels of 3–5 percent monthly inflation may be adequate, at least initially.

Factors Affecting Stabilization Adoption and Success

Distributional Conflict in the New States: More or Less?

Distributional conflict underlies the macroeconomic imbalances that create the need for stabilization. And distributional conflict often prevents stabilization. Hence, to understand the adoption and effectiveness of stabilization programs, it is necessary to see how structural and institutional factors contribute to distributional conflict.

When a country faces high inflation, difficulty servicing external debt, or balance of payments difficulties, stabilization becomes a necessity, since it is a necessary condition for the resumption of economic growth. Although there are short-term costs, the resumption of growth benefits the overwhelming majority of the population. Yet, observation shows that governments may fail to act for long periods of time. Why?

Alesina and Drazen suggest that the reason is often that social groups hope to be able to shift the costs of stabilization onto others. This can only be done, they suggest, by fighting a "war of attrition": preventing stabilization until other groups agree to bear the burden. Their examples include France in the 1920s, Argentina in the 1970s and 1980s, and Belgium, Ireland, and Italy in the 1980s.[10]

In general, a key factor determining whether stabilization policy will succeed is the degree of polarization of the voting population. Tabellini and Alesina provide a model in which a more polarized society chooses a larger national debt. Their model focuses on the possibility of shifts in the composition of the voting population, so that the preferences of today's majority do not coincide with the preferences of future majorities. In this case, current majorities may choose debt to maximize public spending on their preferred programs or goods, since they are not sure that future majorities will have the same outlook.[11]

At first blush, it seems reasonable to expect that the new, postseparation states will be less polarized. Regional differences should be less strong; common national identity should bind people together. However, several doubts can be raised. First, while smaller political units may be more ethnically homogeneous in most cases, the political significance of ethnic differences may become even more acute in smaller states. This is especially true where ethnic minorities are geographically concentrated, as in Chechnya, the Vojna Krajina region of Croatia, or the Crimea.

Second, in a smaller entity the relative importance of large firms or interest groups may actually increase. An example of this would be a large firm like the Croatian oil company INA. On a Yugoslav scale, INA was big; on a Croatian scale, INA is enormous, and its influence on government policy is correspondingly large.[12] Similar remarks could be made about Russian energy firms such as Gazprom or Lukoil.

Third, the greater ethnic or cultural homogeneity of smaller states may lead to more cohesive and effective labor movements. If this eventually resulted in comprehensive bargaining, it might be conducive to a stable macroeconomic environment.[13] But if it merely resulted in heightened industrial conflict, it would be destabilizing. In addition, where labor conflicts coincide with ethnic conflicts, the creation of smaller entities may intensify the problem.

Fourth, in a small state, it may be easier to form cohesive groupings that can function as effective distributional coalitions. A "mafia" joined by bonds of mutual interest and loyalty, using old-boy networks and nontransparent means, may find it easier to influence policies and distribution in a small state.[14]

Therefore, while it would be tempting to conclude that the new states will be more homogeneous and therefore less subject to distributional conflict, this may not be the case. A smaller entity may be more heterogeneous in important ways, or more subject to the domination of particularistic interests. In other words, it cannot be assumed that the new states are more homogeneous; this is a matter to be investigated empirically.[15]

Political Factors: Strength of the Independence Movement and Regime Continuity

I begin the search for determinants of the degree of distributional conflict in the political system. In the new states, stabilization required a determined effort to change economic institutions and policies to bring emerging hyperinflation under control and lay the basis for future economic growth. Stabilization went hand in hand with reform of the economic system. But what factors explain whether a regime will undertake such sweeping reforms?

Mosley, Harrigan, and Toye list four classes of explanations of why economic reform programs are undertaken.[16] The first view argues that reform occurs mainly under authoritarian rule. Since reform measures often have sharp negative consequences for important groups in the short run, only authoritarian regimes have the degree of insulation from popular pressure to undertake thoroughgoing reform. Perhaps the best examples of reforming authoritarian regimes are Turkey and Chile in the 1980s.

The second view argues that any kind of regime can accomplish reform, but that it is only new governments, in their "honeymoon" period, that can muster the political will do so. Mosley, Harrigan, and Toye call this the "new broom" phenomenon.

The third view sees reform as a learning process. Decisive reform occurs when key actors become convinced that not reforming has led to disastrous economic consequences. Convinced that there is no way out, former opponents of reform may take up the cause of change. A key example would be Jamaica in the second half of the 1980s, when both Prime Ministers Seaga and Manley adopted International Monetary Fund (IMF) reform programs they had previously opposed.

The fourth and last view explains the occurrence of reform by the relative power and influence of interest groups. This view may overlap with the others. As Olson suggests, a new regime may be able to make a clean break with old "distributional coalitions" that have distorted resource allocation and opposed needed reforms.[17] A new broom can sweep away entrenched distributional coalitions.

How do these considerations relate to the newly independent states in our sample? Two hypotheses may be advanced: (1) Strong independence movements facilitate the new broom phenomenon and the breakup of distributional coalitions; therefore strong independence movements tend to produce successful stabilization. (2) Governments that are substantially new in their personnel and philosophy will be more likely to initiate reform programs.

The reasoning behind the first hypothesis is relatively straightforward. A strong desire for independence necessarily involves a desire to change power relations between the new state and the old federation, and this affects power relations within the new state as well. The resulting changes, particularly if they involve large-scale public protest, may allow a fundamental reconfiguration of political relations and distributional coalitions.[18]

In addition, it seems that a strong desire for independence strengthens the hand of those who would pursue decisive reforms quickly. As Przeworski argues, radical reform takes advantage of a moment of political opening to "get the pain over with." That is, radical reform front-loads the costs of transition, making transition irreversible. Any subsequent attempts to slow down the pace of reform have less effect if decisive measures were taken at the start. Strong independence movements are inclined to radical reform, since they wish to establish the foundations of the new state as rapidly and decisively as possible.[19]

On the other hand, countries without strong independence movements, that achieved sovereignty almost by default, are less likely to make rapid, fundamental changes. They may have been relatively satisfied with the old order; or they may wish to keep the option of transnational cooperation open, as in the Commonwealth of Independent States (CIS), and therefore avoid creating major differences between themselves and potential partners.

The second hypothesis emphasizes the transition, as opposed to the independence, aspect. Regimes with less continuity–more widespread personnel changes in both political and economic leaderships–are more likely to make fundamental changes in economic policy and structure, including the initiation and consistent implementation of stabilization programs. This hypothesis is a straightforward expression of the new broom and distributional coalition frameworks.

In relation to regime continuity, it is important to emphasize that the main distributional struggle during the transition period primarily pits socialist enterprises and their supporters in the bureaucracy against reforming governments and proreform social sectors. It is a struggle over subsidies, concessionary credits, and taxes–in short a struggle to keep the main elements of the soft-budget constraint. Regimes with high levels of continuity are badly equipped–or simply unwilling–to oppose the old, soft-budget practices.[20] Such regimes include the very forces who stand to lose from change: the old managers, the nomenklatura, and the bureaucracy of the old system.

This section has sketched how the strength of the independence movement and the degree of regime continuity affect the prospects for stabilization. These elements, in turn, have bases in political and social structures, and, in particular, in distributional coalitions. I now examine how these structures and coalitions affect the adoption and implementation of stabilization programs.

Political Structures: Coalition versus Single Party Governments and Democracy versus Authoritarianism

Alesina and Drazen, in their work on "wars of attrition" over stabilization, and Roubini and Sachs conclude that weak coalition governments find it difficult to enact decisive stabilization measures and especially to reduce government budget deficits. Alesina and Drazen argue that political consolidation is often a necessary precondition for ending the war of attrition and beginning stabilization.[21]

This suggests a third hypothesis for investigation: (3) Multiparty coalition governments are less successful at implementing stabilization than single-party governments.

A similar theme in the literature on stabilization regards the supposed advantages of authoritarian regimes in implementing stabilization. Recent experience with the transition to democracy, however, suggests that authoritarian regimes may often be too beholden to entrenched social interests or too committed to populist economic strategies to stabilize.[22]

Furthermore, new democratic regimes have shown an ability to use the political capital available in the early period of transition to democracy to support stabilization efforts. As Whitehead stresses, both the form of stabilization (whether it involves social dialogue and partnership) and the outcome of stabilization have great impact on the consolidation of democracy.[23] Such reasoning is likely to apply to the countries in transition from Communism as well; democracy need not impede stabilization, and successful stabilization–successful in both the political and the economic sense–can facilitate the consolidation of democracy.

In the cases of the former Yugoslav and Soviet republics, there are added arguments about the compatibility of democracy and stabilization. Those countries seeking to "rejoin Europe" are precisely those most interested in rapid transition to a market economy and the observance of democratic procedures. Also, democracy represents a break with the past; achieving democracy was a major element in the legitimation of the struggle against Communism.[24] Finally, although the emergence of new authoritarian forces cannot be excluded, those most able and interested in maintaining authoritarianism are generally the Communists themselves. Only they have the connections with the repressive apparatus, at least initially, to implement authoritarianism.

For these reasons, I advance two more hypotheses: (4) External alliances play an important role in determining whether a country will choose stabilization. (5) Democratic regimes will be more likely to pursue stabilization than authoritarian ones in the specific circumstances of national independence and transition.

Ethnic and Regional Divisions and Social Homogeneity

Ethnic differences within the new states have proved to be hardly less politically difficult than in the old multinational states. This could be seen as the legacy of the old country that will eventually be resolved, even if by force (war and ethnic cleansing). However, in the first years of the new states, there seems to be little indication that increased ethnic homogeneity, as measured by the fraction of the state belonging to the majority ethnic groups, facilitates more coherent economic policy outcomes.

This can be formulated as a hypothesis: (6) Ethnic homogeneity, as measured by the proportion of total population belonging to the dominant ethnic group, will not be a good predictor of distributional conflicts and stabilization success.

Size and Openness

The new countries of the former Yugoslavia and some of the successors to the Soviet Union are fairly small. In particular, Slovenia, Macedonia, and Estonia each have populations of 2 million or less, and Croatia, Latvia, Lithuania, the Kyrgyz Republic and Turkmenistan have between 3 and 5 million. This raises important long-term questions, such as whether the domestic market of such a small country can create an adequate platform for economic development. For this reason, the new countries have a stronger incentive to join in regional free trade agreements and eventually into the European Union (EU) than the multinational states from which they came.

These long-term viability issues, however, are not my present focus. Instead I ask: how does the smaller size and greater openness of the new states affect stabilization and short-term dynamics?

Size has an effect in one respect: it is easier for foreign creditors to provide adequate balance of payments support to a small country than to a large one.[25] For example, when the IMF released its first tranche of support for the Kyrgyz Republic, the hardly enormous $25 million disbursement was larger than the country's hard-currency earnings in 1991![26]

Be that as it may, the main factor at play here is greater openness. Since all the trade that used to occur between regions of the old entity have now become international trade, these economies have become, by definition, more open. This, in turn, reduces the options available for managing domestic demand.

This observation may imply a greater willingness to consider institutional arrangements that precommit macro policy, most of all, central bank independence. With less room for discretionary policy manoeuver, and greater vulnerability to international trade and capital flows, the new countries may find the balance of arguments tipped in favor of precommitment. This, of course, has important implications for stabilization.

Also, since the new states will be less self-sufficient, the impulse to meet external standards of behavior (those of the IMF or the EU especially) should be stronger. This, too, militates in the direction of stronger antiinflationary policy and less use of discretionary policy to achieve economic growth. Therefore, another hypothesis: (7) The smaller new states will be forced to stabilize rapidly, while larger states will have more room to manoeuver.

Income Level

Stabilization programs, and transition programs as well, involve a short-run fall in consumption levels. Przeworski asks what the impact of a society's income level will be on its willingness to endure a fall in consumption. He argues that neither the poor in Latin American societies nor the poor in the former USSR are in a position to easily accept decreased living standards; both begin the adjustment/transition process close to the minimum.[27]

However, Przeworski's argument that the poor may oppose stabilization assumes that it is possible to maintain the status quo income level. In the former Yugoslav and Soviet cases, income was already falling before independence. Hence, the real question facing agents is: do we risk exacerbating the downward trend through a stabilization package, with the hope that incomes will start to recover thereafter, or do we allow the declining trend to continue? The alternative of restoring the old system in full is not an option.

In such a situation, even a low-income country may choose to stabilize. But there is a further factor: in a wealthier country, or a country with more income inequality, it may be easier to collect tax revenues and balance the government budget. This creates greater possibilities for successful stabilization, with the assumption that the government is politically able to tax the wealthy–a condition often not fulfilled in Latin America, for example.

With all this in mind, the following hypothesis may be advanced: (8) Income level is not a main determinant of the initiation of stabilization; poorer countries may choose stabilization as well, although richer countries should find stabilization easier.

Separation Shocks and Transition Shocks: The Short-run Problems of Separation

In addition to these structural considerations, we must examine a host of special short-run circumstances facing the new countries that have important implications for stabilization. In essence, the new countries face a separation shock at the same time as they attempt to transform their economic systems from centrally planned or market socialism to market capitalism.

Consider the separation shock first. A common feature thus far seems to be the loss of traditional markets within the old state. At the minimum, trade barriers arise due to the introduction of separate currencies with limited convertibility. More frequently, overt trade restrictions come into play. Hence separation seems to require a reorientation of foreign trade.[28]

Indeed, desire for trade reorientation may partly drive separation, especially in more productive regions which feel that they can succeed more readily on Western markets on their own. Separation allows them to introduce their own currency, allowing them to set an appropriate exchange rate, and it allows the new state to adjust its tariff policies to the needs of its own economy. These two extra ingredients can facilitate the reorientation of trade.

Trade restrictions are particularly important when producers are dependent upon suppliers that are, after separation, in other countries. In these cases–more common in the former Soviet than the former Yugoslav republics–the loss of traditional markets has supply-side implications.

It could be argued that loss of markets, while frequently observed, is not a necessary consequence of separation. In the context of a regionwide movement to freer trade, it might turn out that trade flows are freer even after separation. The case of the Czech-Slovak breakup will probably be the best test of this contention.[29]

Ironically, the fact that income fell dramatically after separation in many states also meant that newlyarisen barriers to trade were less important. Trade was already spiraling downward due to falling income, so additional barriers played only a marginal role in the overall decrease in exchange of goods.

An important element that can be either positive or negative is loss of transfers from the old state. Such transfers were substantial in former Yugoslavia and the Soviet Union. For net donors like Slovenia, this unburdens fiscal policy, but for net recipients like Macedonia, this can be an important negative shock.[30]

Another fact of life is delay in international recognition and interruption in international aid flows. In combination with the frequent lack of foreign currency reserves, this delay sharply constrains possibilities for supporting a fixed exchange-rate regime, a major weapon for stabilization.[31] Furthermore, it creates the requirement for substantial initial trade surpluses to build up reserves, even if the external debt position of the new state is not in itself a problem. Delay in international recognition can also affect trade flows. Export support via established agencies such as the U.S. Exim Bank, or the German Hermes, can be disrupted. Disruption in payments and inconvertibility of currency can also impede trade.

Complicating matters further is the fact that the states in question are in the midst of an unprecedented transition from centrally planned or market socialism to market capitalism. This creates important short-run problems[32] First, transition usually implies adjustment to world market prices. For most new states, this implies a price shock, since crucial prices such as housing, energy, and food were held below world market levels. (For energy producers like Russia, however, the energy price shock would have a positive impact on export earnings.)

Second, transition has caused a supply shock as producers unable to produce goods at world market quality and/or price have been driven from the market. The supply shock has been magnified by import liberalization, which has for the first time put competitive pressure on these producers.

Third, the dissolution of CMEA has to be considered part and parcel of the transition. CMEA was an institution guaranteeing non-market trade arrangements; it was not compatible with opening to the capitalist world-market. The dissolution of CMEA dramatically changed trade flows, and, in the short-run, significantly decreased demand for the products of the former Soviet Republics. This demand shock greatly complicated the short-run problems of macroeconomic management.

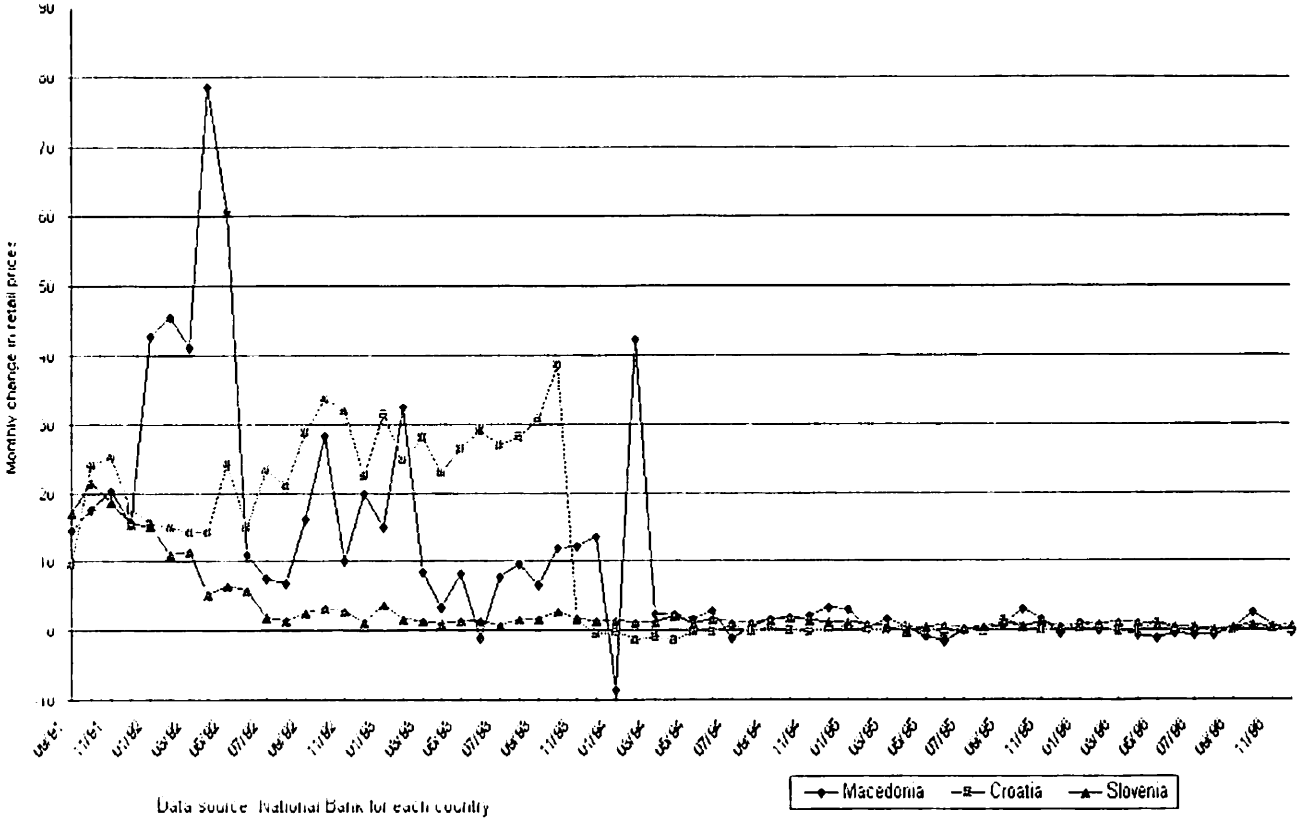
What hypotheses can be advanced about these short-run shocks? (9) Fiscal separation shocks either facilitate fiscal consolidation or make it more difficult. Since fiscal consolidation is crucial to stabilization, fiscal separation shocks can potentially have dramatic effects on the costs of stabilization and therefore on the nature and timing of stabilization programs. (10) Terms-of-trade shocks work the opposite way: an unfavorable terms-of-trade shock forces adjustment, while a favorable shock may in fact render adjustment, and even stabilization, less urgent in policymakers' eyes.

Empirical Evidence

Classification of Stabilization Success

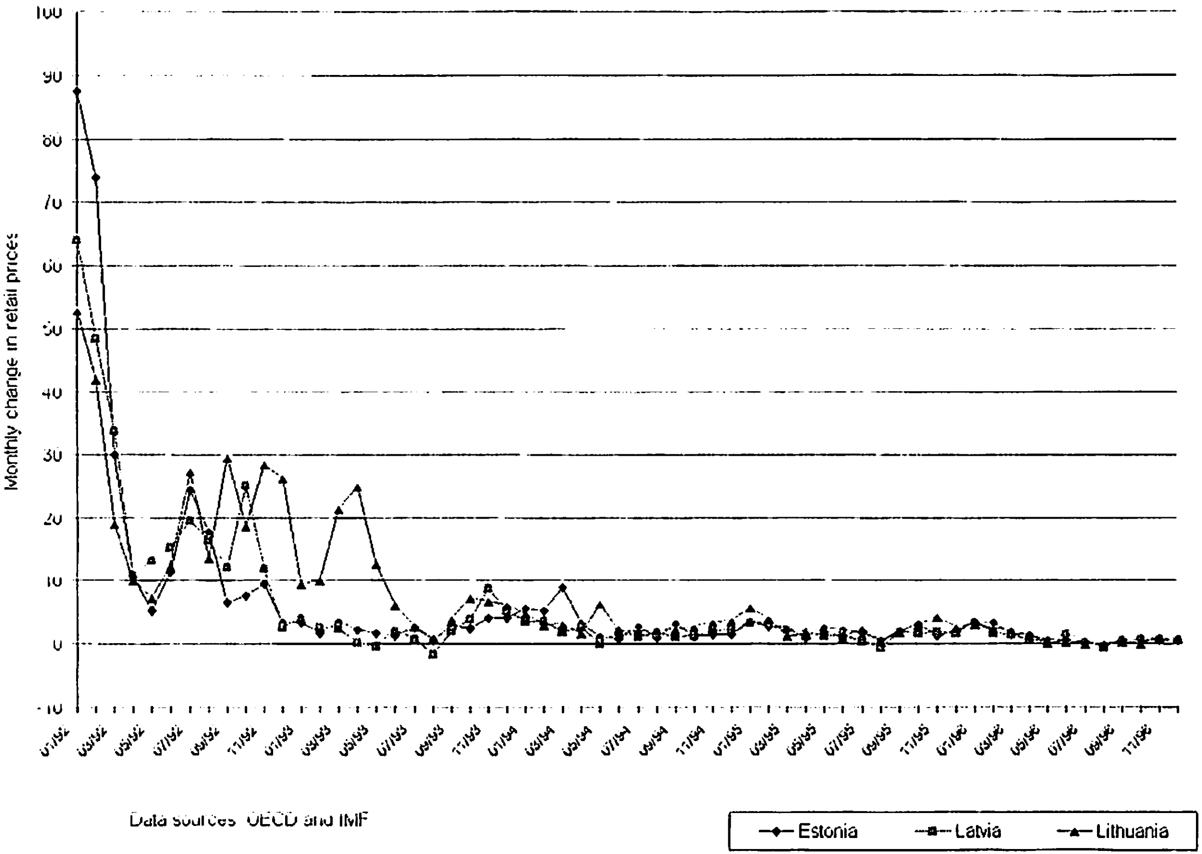
By the end of 1996, all the countries in the sample except Turkmenistan had achieved average monthly inflation rates below the benchmark level of 5 percent; the main difference has been in the speed with which inflation has been brought down. For this reason, I measure success in dealing with inflation in terms of the length of time required to achieve low levels of inflation. As table 3 shows, this measure of stabilization delay was also closely correlated with the level of inflation in 1995.[33]

GRAPH 1 INFLATION IN MACEDONIA, CROATIA AND SLOVENIA, 1991-1996



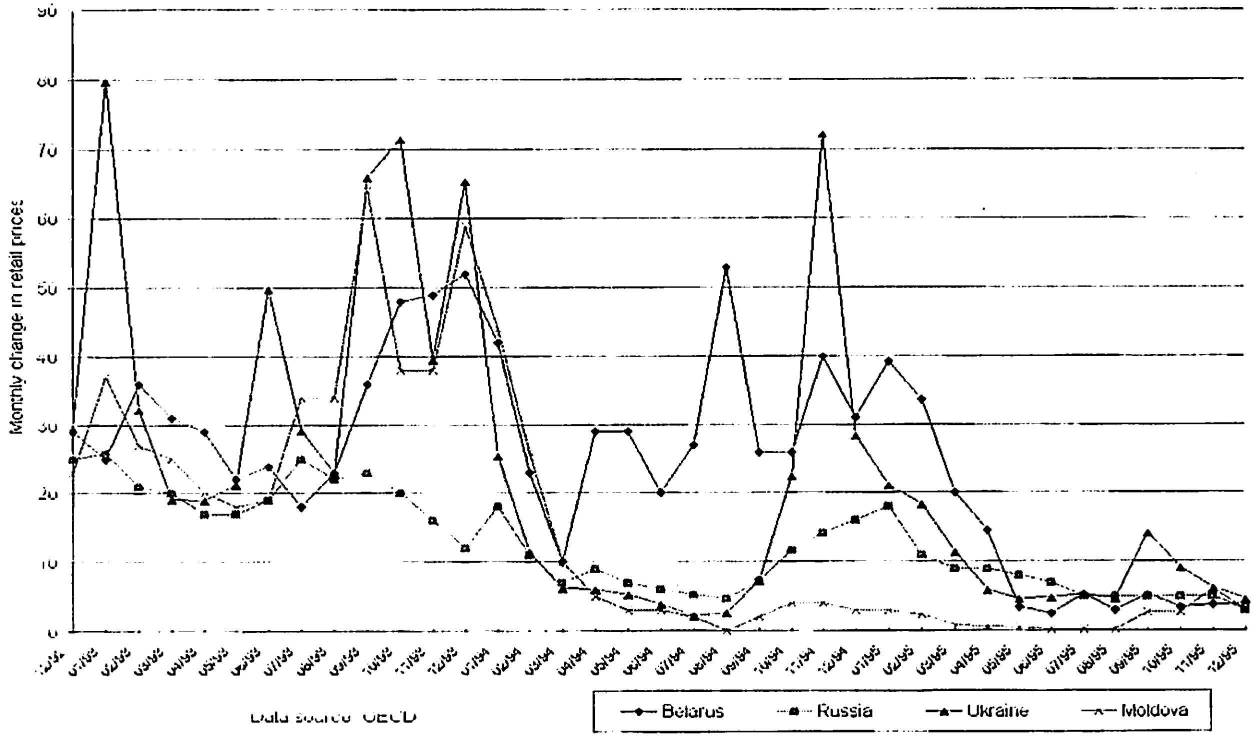
Data source: National Bank for each country

GRAPH 2: INFLATION IN ESTONIA, LATVIA AND LITHUANIA, 1992-1996



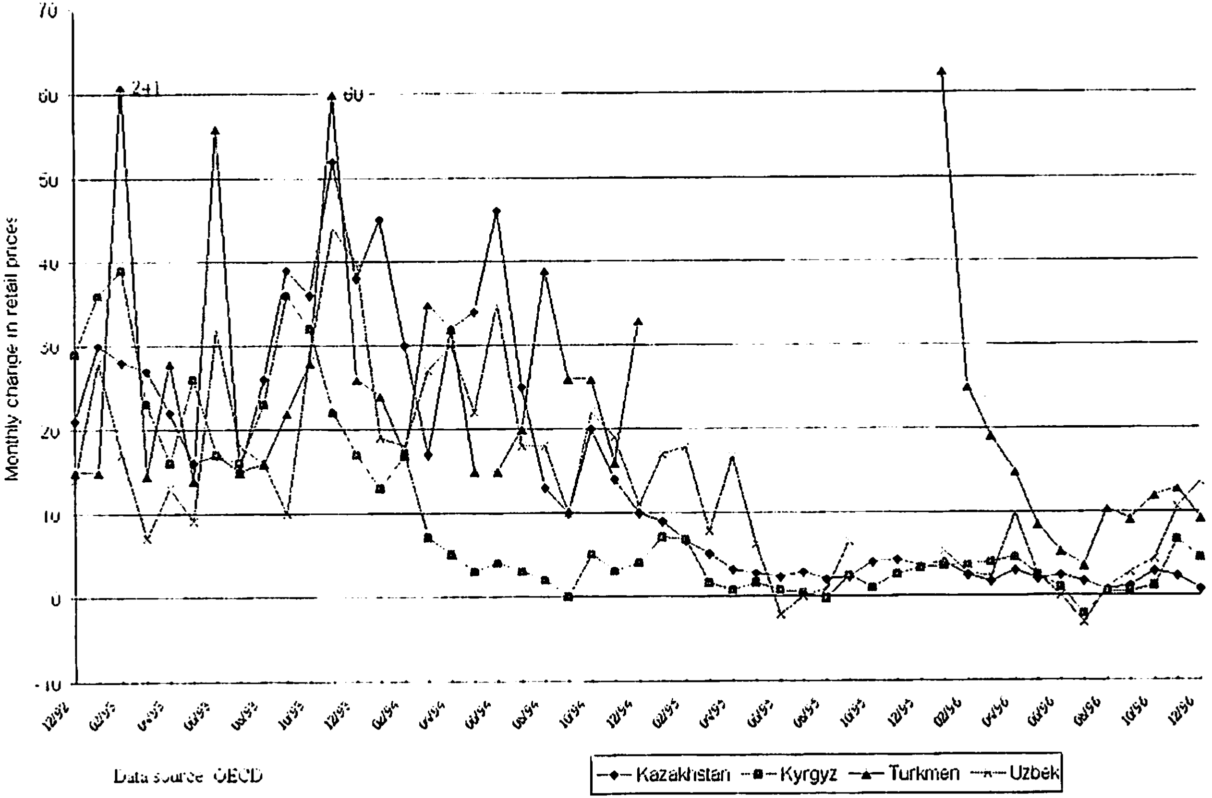
Data sources OECD and IMF

GRAPH 3: INFLATION IN BELARUS, RUSSIA, UKRAINE AND MOLDOVA, 1993-1995



Data source: OECD

GRAPH 4: INFLATION IN KAZAKHSTAN, KYRGYZ REPUBLIC, TURKMENISTAN AND UZBEKISTAN, 1993-1996



Data source: OECD

Table 3: Classifying Stabilization Success

	Months from Independence to Stabilization	1995 Average Monthly Inflation
Very successful		
Slovenia	10	0.7
Estonia	14	2.1
Latvia	14	1.8
Successful		
Croatia	25	0.3
Macedonia	28	0.7
Lithuania	20	2.6
Kyrgyz Republic	29	2.4
Moldova	32	1.8
Somewhat unsuccessful		
Kazakstan	39	4.0
Belarus	42	11.5
Uzbekistan	43	7.9
Russia	44	7.5
Unsuccessful		
Ukraine	51	9.2
Turkmenistan	N/A	22.1

Sources: Various issues of the bulletins of the Bank of Slovenia, Ljubljana; The National Bank of Croatia, Zagreb; and the National Bank of Macedonia, Skopje; International Monetary Fund, *International Financial Statistics*; and Organization for Economic Co-operation and Development: *Short-Term Economic Indicators*: *Transition Economies* (Paris, OECD).

The measure used to quantify stabilization success is the number of months between independence and the achievement of monthly inflation rates below 5 percent. The very successful category is reserved for countries that took less than sixteen months; successful stabilizers took between sixteen and thirty-two months, somewhat unsuccessful stabilizers took between three and four years (thirty-six to forty-eight months); and unsuccessful stabilizers took more than forty-eight months, or did not even achieve inflation below 5 percent monthly in 1996.

As table 3 and graphs 1–4 show, the most rapid stabilizers were Slovenia, Estonia, and Latvia. After independence, Slovenia and Estonia quickly introduced comprehensive stabilization packages, including new currencies. Latvia followed a different order, introducing its new currency first in parallel to the ruble, then proceeding relatively quickly to stabilize and make the lat the sole currency.[34]

The successful stabilizers were Croatia, Lithuania, Macedonia, the Kyrgyz Republic, and Moldova. In each case there was some delay between independence and successful stabilization. Croatia's stabilization effort of October 1993 (in some ways a continuation of reforms begun in December 1992) proved extremely successful, reducing inflation to negative monthly rates; but its previous effort at stabilization in mid-1991 had achieved only gradual decreases in inflation and had been abandoned.[35]

Lithuania also experienced some delay in stabilization, introducing its new currency nearly a year after Estonia had unveiled the kroon. Although inflation fell to below 5 percent monthly by July 1993, it rose again in the autumn, and only definitively went below 5 percent after January 1994.

Similarly, although Macedonia avoided falling into the hyperinflation engulfing much of the former Yugoslavia in 1992 and 1993, it was unable to keep inflation below 5 percent consistently during this period. Only with the introduction of the country's third stabilization package at the end of 1994 was high inflation in Macedonia tamed.[36]

The Kyrgyz Republic was faced with even higher inflation than Russia in the aftermath of price liberalization in January 1992, massive negative fiscal shock, and expansive Russian monetary policy in the second half of 1992. In April 1993, the government responded with the introduction of a new currency, the som, and a standby agreement was reached with the IMF in May 1993. By March 1994, inflation had been reduced to single figures.[37]

Finally, Moldova, which liberalized most prices along with Russia in January 1992, reached an agreement with the IMF in September 1993 and implemented a stabilization program. In April 1994, monthly inflation fell below 10 percent, where it stayed for the rest of the period under consideration. Somewhat like Croatia, Moldova stabilized despite a limited military conflict over the Transdniester region. The open military conflict was ended by the cease-fire agreement of July 1992, but the issues regarding autonomy or separation for Transdniester have not yet been resolved in a permanent way.[38]

Somewhat unsuccessful are Russia, Belarus, Kazakstan, and Uzbekistan. The Russian case is distinct in that decisive reform measures were taken immediately, but did not bear the expected results, in part because of political resistance. The initial tight monetary and fiscal stance advocated by Prime Minister Yegor Gaidar was reversed when pressures to subsidize industry, agriculture, and exporters led to massive subsidized credits and fiscal handouts from June 1992 on. Antiinflation policy was initially put on the back burner by

Gaidar's successor, Viktor Chernomyrdin. Inflation remained at about the 20 percent per month for most of 1993, but was gradually reduced in early 1994. There were more bumps in the road, as inflation rose in late 1994 and was finally contained only in the second half of 1995 and 1996.[39]

The reluctance of the post-October 1993 parliament to approve stabilization-oriented policies and to contain the fiscal deficit was a key factor holding up successful stabilization, along with the continuation of subsidized credits by the National Bank of Russia. The distributional struggles underlying these battles over monetary and fiscal policy were fierce, and the idea that fiscal and monetary restraint would be needed to contain inflation was not definitively accepted by many political actors until very late in the game.[40]

Despite this, Russia was a pathbreaker whose actions had crucial effects on its neighbors. The Russian "big bang" of 1992 forced most of the other ex-Soviet states to liberalize prices. And the stabilization effort of 1992, even though not a full success, had great influence on the other republics.[41]

Belarus, especially after the election of Andrei Lukashenko to the presidency, was very wary of market economics. The IMF, while working with the Belarussian government, was openly critical of what it considered excessive credit given to enterprises by the National Bank of Belarus and its resistance to privatization. Inflation rates remained in the hyperinflation range through early 1995. At that point, a stabilization program was implemented. Inflation came down sharply in May and stayed in control thereafter.[42]

In the Central Asian states of Kazakstan and Uzbekistan, there may have been a demonstration effect from the Kyrgyz Republic's stabilization efforts. Kazakstan, which had not tried stabilization initially, tried to restrain its fiscal deficit in 1994 and took stronger steps toward stabilization in the middle of the year. It also made great efforts to welcome foreign investment.[43] But large-scale enterprise arrears appeared, and the government deemed it necessary to intervene with subsidies. This distributional struggle prevented the consolidation of stabilization in 1994. Only in 1995 did the authorities tighten the fiscal stance along with monetary policy and achieve a lasting stabilization.

Uzbekistan, which was very slow to implement reforms in general and stabilization in particular, also achieved some progress toward stabilization in 1994. But liberalization of important prices resulted in a series of inflationary outbursts in the last months of the year. Had Uzbekistan liberalized prices earlier, like the more reform-minded CIS countries such as Russia, Moldova, and the Kyrgyz Republic, this late outburst would not have happened. Only in mid-1995 were price increases again brought under control.

The "fundamentals" in Uzbekistan seemed favorable by 1996: the fiscal deficit, of about 4 percent of GDP, was manageable, the exchange rate had stabilized, and the foreign exchange market had been liberalized. Nonetheless, inflation rates were quite variable in 1996, exceeding 5 percent in four months and exceeding 10 percent in the last two months of the year. For this reason, there is still reason to be reserved about the success of stabilization in Uzbekistan.[44]

The most unsuccessful are Ukraine and Turkmenistan. Ukraine moved reluctantly toward stabilization, with many reversals. It was dragged into limited price liberalization by the Gaidar reforms in early 1992 and the government of Leonid Kuchma, formed in October 1992, brought partial liberalization and a degree of stabilization.[45] However, when the mandate for emergency rule was not renewed in May 1993, the new government reintroduced many administrative measures and allowed the emergence of hyperinflation. A considerable degree of stabilization was achieved in early 1994 mainly thanks to strong credit restriction. But high inflation returned in September 1994, when a more systematic reform led to a new inflationary wave.[46] By April 1995, inflation once again seemed to be under control, but economic reformers were still under sharp political pressure. The tremendous struggles over the third tranche of the IMF standby loan in October and November 1995 indicated the continuing political problems over stabilization.[47] Inflation again soared above 5 percent from September 1995 to February 1996 (with the exception of December, when inflation was 4.6 percent). Finally, in March 1996 inflation fell to 3 percent and stayed at low levels for the rest of the year.

In Turkmenistan, quite simply, there was little interest in stabilization. This attitude was bolstered by a belief that the country's natural resources put it in a good position for the future. Price liberalization did not occur until 1995 and early 1996, and even then, a few important prices remained controlled (bread, meat, baby food, sugar, milk, heating, and housing) and gas, electricity, and water were still distributed free to the population.[48] Extremely high inflation rates continued into 1996. A strong credit contraction in the first half of 1996 brought inflation rates down to a low of 3.6 percent in July, but inflation picked up again in the rest of the year, as the regime still did not achieve a decisive victory over inflation.

Looking at all the cases, it is apparent that some countries moved quite decisively, while others experienced many delays and reversals. With this in mind, I now examine the hypotheses about the determinants of stabilization success. Table 4 contains a summary of the hypotheses, and table 5 presents a summary of the variables used to explain stabilization success.

Table 4. The Hypotheses

(1) Strong independence movements facilitate the new broom phenomenon and the breakup of distributional coalitions, thereby encouraging successful stabilization.

(2) Regimes that are substantially new in their personnel and philosophy will be more likely to initiate reform programs.

(3) Multi-party coalition governments are less successful at implementing stabilization than single-party governments.

(4) External alliances play an important role in influencing the decision to stabilize.

(5) Democratic regimes will stabilize more effectively than authoritarian ones in the specific circumstances of national independence and transition.

(6) Ethnic homogeneity is not a good predictor of stablization success.

(7) Smaller size implies greater openness, which forces stabilization policies upon small states. Larger states have more room to manoeuver.

(8) Income level is a much less useful predictor of stabilization success than openness.

(9) Fiscal separation shocks either facilitate fiscal consolidation or make it more difficult. Since fiscal consolidation is crucial to stabilization, fiscal separation shocks can potentially have dramatic effects on the costs of stabilization and therefore on the nature and timing of stabilization programs.

(10) Terms-of-trade shocks work the opposite way: an unfavorable terms-of-trade shock forces adjustment, while a favorable shock may in fact render adjustment, and even stabilization, less urgent in policymakers' eyes.

Table 5. Explanatory Variables of Stabilization Success

	Independence Movement	Regime Continuity	External Alliances	Political Freedom	Population (million)	GDP/Capita ($,1992)
Most successful						
Slovenia	Strong	Medium	Europe	6.5	2.0	6330
Estonia	Strong	Low	Eur., Scand.	5.5	1.6	2750
Latvia	Strong	Low	Eur., Scand.	5.5	2.6	1930
Successful						
Lithuania	Strong	Medium	Eur., Scand.	6.0	3.8	1310
Croatia	Strong	Low	Europe	4.0	4.8	1600
Macedonia	Weak	Medium	Europe (?)	4.5	2.2	852
Kyrgyz Rep.	Weak	Medium	West (?)	4.5	4.5	810
Moldova	Strong	High	West	4.0	4.4	1260
Somewhat unsuccessful						
Kazakhstan	Weak	High	Russia	2.5	17.0	1680
Russia	N/A	Medium	Reg. power	4.5	148.9	2680
Ukraine	Medium	High	West (?)	4.5	52.1	1670
Uzbekistan	Weak	High	Russia, Turkey	1.0	21.3	860
Unsuccessful						
Belarus	Weak	High	Russia	4.0	10.4	2910
Turkmenistan	Weak	High	Russia, Turkey	1.0	3.9	1270

	Ethnic split (%)	Central Bank Independence	New Currency	Trade Union Competition	Fiscal	Shock, Terms of Trade
Most successful						
Slovenia	88.3	Yes	Oct. 1991	Yes	+	?
Estonia	62.30	Yes	May 1992	No	+	-
Latvia	52.34	No	July 1992	No	+	-
Successful						
Lithuania	80.9	No[1]	Oct. 1992	Yes	+	-
Croatia	75.12	Yes	Dec. 1991	Yes	+	?
Macedonia	67.20	Yes	July 1992	No	-	?
Kyrgyz Rep.	52.21	No	May 1993	No	-	-
Moldova	65.14	No	Aug. 1993	No	-	?
Somewhat successful						
Kazakhstan	40.38	No	Nov. 1993	Yes	-	-
Russia	82.4	No	N/A	Yes	+	-
Ukraine	73.22	No	Nov. 1992	Yes	0	-
Uzbekistan	71.8	No	Nov. 1993	No	-	-
Unsuccessful						
Belarus	78.13	No	Jan. 1993	Yes	0	-
Turkmenistan	72.10	No	Oct. 1993	No	-	-

Sources and Definitions:

Strength of independence movement: strength of preindependence mass movements. Data from Philip Roeder, "Soviet Federalism and Ethnic Mobilization," World Politics, 43, (January 1991.): 196-232; Lieven The Baltic Revolution, Benderly and Kraft, Independent Slovenia; and press accounts.

Regime continuity: Degree to which Communist Party officials remain in government after independence.

External alliances: Main external allies or alliances joined.

Population. From Wallich (1995)

GDP/Capital, ibid.; World Bank estimates for 1992

Ethnic split: Percentage of population of two largest ethnic groups; Data from former Soviet republics from Europa World Yearbook 1993 (London: Europa Publishers, 1993), and Brian Hunter, ed. The Statesman's Yearbook, 1993-4 (New York: St. Martin's, 1994); for former Yugoslav republics from Savezni Zavod Za Statistiku. Statisticki Godisnjak Jugoslavije 1990 (Belgrade, 1991).

Central Bank independence: Central bank legally independent of government. Specifically, bank governors not subject to parliamentary recall; bank policy decisions not subject to parliamentary or presidential veto; central bank not obligated to float loans to government. Data in the table reflect situation as of 1993; many countries increased central bank independence during or just after stabilization. Data from IMF, IMF Reviews for ex-Soviet republics; Kraft, "Does Separation Facilitate Macroeconomic Policy Making" for ex-Yugoslav republics.

Political freedom: Index of political freedom constructed by Karatnycky. Scaling of de MElo et al. is used: higher numbers indicate greater freedom.

New currency: Date of removal of old currency from circulation. This date may precede the introduction of a new permanent currency. Data from Russian EconomicTrends, 3, 2 (1994).

Trade union competition: Do independent unions exist in competition to old official unions? Data from Free Trade Union Institute

Separation shock, Fiscal: Net gain in fiscal transfers after independence. Data for former Soviet republics from Europa Worldbook, IMF, IMF Reviews; for Yugoslavia, Kraft "Evaluating Regional Policy."

Separation shock, terms of trade: Initial effect of moving to world-market prices for ex-Soviet republics. Data from David G Tarr, "The Terms of Trade Effects of Moving to World Prices on Countries of the Former Soviet Union," Journal of Comparative Economics, 18, 1 (February 1994): 1-24.

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Note:
1. Lithuania adopted a currency board arrangement in 1994. At the time of stabilization in 1993, the Bank of Lithuania was not independent.

Hypothesis 1: A Strong Independence Movement Facilitates Stabilization

Table 6 shows how the strength of independence movements correlates with stabilization:

Table 6. Stabilization by Strength of Independence Movements

	Most Successful or Successful	Somewhat Unsuccessful or Unsuccessful
Strong	6	0
Medium	1	1
Weak	1	4

In accordance with the theories of the new broom and distributional coalitions outlined above, independence provided an opportunity for new regimes to redesign institutions and to break with distributional coalitions established across the old country. For Slovenia, independence meant the opportunity to escape the domination of the soft-money coalition that controlled the National Bank of Yugoslavia. Local supporters of soft money were weak, and Slovenia immediately implemented a tight-money policy upon independence. A crucial weapon in this fight to change monetary policy was the introduction of a new currency.[49]

The learning theory also has some relevance. During the 1980s, attempts to solve economic decline by reforming the socialist system failed in both former Yugoslavia and the Soviet Union. The new, postindependence leaders in many cases accepted the need for radical reform as a result of their assessment of recent history.

However, learning does not explain why some new leaders embraced radical change and the transition to a market economy more than others. An explanation is provided by the new broom and distributional coalition theories, which emphasize the importance of a new regime and the reconfiguration of distributional coalitions. In this context, the key to the nature of the new regime, and of the distributional coalitions emerging in the new society, is the social basis and strength of the independence movement. In countries like Slovenia and Estonia, where independence was supported by a mass movement, the new regime had great leeway to redesign institutions and reshape distributional coalitions. In countries like Belarus, where there was little proindependence sentiment, a new regime was not in a position to function as a new broom.

Finally, the institutional and cultural legacies of the past are important factors. In the ex-Yugoslav republics, for example, many institutions central to stabilization existed in some form before separation. Republics had administered their own budgets since 1974, republican national banks had existed as branches of the National Bank of Yugoslavia, and a two-tiered banking system had been established in the mid-1960s.

By contrast, in the former Soviet republics, such institutions had to be created nearly from scratch. And, while certain of the republics, such as the Baltics, had recent traditions as independent states, others, particularly Belarus and those in Central Asia, had little past history of independence to draw on.

If we now look at the data in table 5, we see that countries with the strongest independence movements–the Baltic States, Slovenia, Croatia, and Moldova–were the successful stabilizers. Those countries with weak or nonexistent independence movements, such as Belarus and the Central Asian states, have been rather unsuccessful at stabilization.

The cases that do not entirely fit are Macedonia, the Kygyz Republic, and Ukraine. Macedonia had a strong national identity, but its leadership was reluctant to contemplate independence during 1990 and much of 1991 because of the republic's high degree of integration with the rest of Yugoslavia, its dependence on Yugoslavia for substantial transfers, its internal ethnic problems, and its vulnerability to hostile neighbors.[50] When more or less forced to seek independence, Macedonian leaders easily gained popular support, due in part to the people's unwillingness to remain in Serb-dominated Yugoslavia, and in part to Macedonian national identity.[51] This political support has facilitated stabilization measures.

In the Kyrgyz Republic the leadership was not highly oriented toward independence, but the country's lack of natural resources, small size, and relative isolation forced it to seek external help. This involved pursuing stabilization.

The case of Ukraine is also a bit unusual. While proindependence sentiment was slow-growing in comparison with the Baltics, Ukrainian nationalism has long been formidable. Here the key factor has been a high degree of regime continuity, the factor to which I now turn.

Before doing so, a note should be made on the ambiguous position of Russia in this discussion. Although Russia currently celebrates the anniversary of its independence from the Soviet Union as a national holiday, it is difficult to interpret Russia's reemergence as a country in the same light as, say, Estonia's. As the dominant player in the Soviet Union, Russia was more the country that other republics sought to break away from than a country itself seeking independence. At the same time, Russia's struggle to assert its autonomy from all-Union structures in 1990 and 1991 had many similarities to the independence movements of other republics: Russia sought the right to make political and economic decisions autonomously. The decisiveness of Russia's reform efforts in 1992 in part reflect the strength of this struggle for autonomy.

Hypothesis 2: Regime Continuity Hinders Stabilization

A second aspect of whether the new regimes functioned as new brooms is the degree of continuity within leadership. The variable regime continuity refers to the degree to which executive and parliamentary leadership remained in the hands of Communist officials after independence (See table 7).

Table 7. Stabilization by Regime Continuity

	Most Successful or Successful	Somewhat Unsuccessful or Unsuccessful
High	1	5
Medium	5	1
Low	2	0

Once again, most of the successful stabilizers had moderate levels of regime continuity. Only two states can be said to have low continuity: Croatia and Estonia. In these countries, few former Communists performed key executive or parliamentary functions.[52]

In the other successful stabilizers, a mixture of continuity and change was seen. For example, the president of Macedonia was a well-known Communist reformer, and the reformed Communists were the strongest party; but other parties were involved in the coalition, and the new prime minister was a young person with limited roots in the old system. In Slovenia, the president and the second postindependence prime minister were reform-minded top Communist leaders. However, the parties in power (first the DEMOS coalition, then the Coalition of Christian Democrats, Liberals, and former Communists) were largely non-Communist. In Latvia, as Lieven comments, "the great majority of pro-independence deputies (in the Supreme Council) were either members of the Soviet establishment or people who had achieved a certain official status in society. This was even more true of the Godmanis government" that ruled through June 1993.[53]

In Lithuania, continuity was relatively low from 1990 to 1992, but the reformed Communist Party returned to power in the November 1992 elections. In the Kyrgyz Republic, President Askar Akaev, notably, was not a high party official, but did come to power through the support of reformers in the Communist Party's Central Committee. The biggest exception is Moldova; even though most of its political leaders were holdovers from the old regime, it carried through stabilization.

Among the unsuccessful stabilizers, continuity is generally high. The classic cases are the Central Asian republics (excepting the Kyrgyz Republic), in most of which very little personnel change has occurred at all. Belarus is another excellent example. Ukraine embodied continuity in the person of President Leonid Kravchuk and in an antireform parliament elected under undemocratic rules in 1990. Russia, on the other hand, has only moderate continuity, with President Boris Yeltsin (a Communist Party drop-out) counterbalanced by the prominence of Communists in the post-October 1993 parliament, and the nomenklatura background of Prime Minister Viktor Chernomyrdin.

There is a strong interrelationship between regime continuity and strength of the independence movement. In most cases where the independence movement was strong, regime continuity was moderate or low. This applies to Slovenia, Croatia, Estonia, and Lithuania. Conversely, where there was little proindependence sentiment there was also usually little challenge to the existing regime (Belarus, Kazakstan, Turkmenistan, Uzbekistan). Leaders from the Communist period remained in power in the new state, precluding a sharp break with past economic practices.

There are three cases in which the existing regime survived a strong independence movement. These could be called cases of "if you can't beat 'em, join 'em." In Latvia and Moldova, the Communist Party simply swung over to the cause of independence. The situation in Ukraine was complicated. Bojcun argues that Kravchuk effectively managed to maintain regime continuity by acquiescing in the outlawing of the Communist Party in 1991 and courting proindependence forces. He remained as leader of the "party of power," representing incumbents in the government, military, and economic apparatus without a formal party structure or ideology.[54] So, in this case, regime continuity was preserved in the face of a growing independence movement by skillful political maneuver.

There are also cases in which regime continuity was moderate despite weak independence movements. In Macedonia, the elections of 1990 led to significant changes in the leadership of the Socialist (former Communist) Party and the formation of a coalition goverment. In the Kyrgyz Republic, the turmoil of independence led to the emergence of a new leader and some changes in leading personnel.

The notion of regime continuity advanced here focuses on cases in which there are no substantial changes in top government and economic management personnel. A situation in which the Communist Party loses power and then returns is not a case of regime continuity. In fact, it appears that the return of Communist or neo-Communist parties to power does not necessarily doom reform. The cases of Lithuania, Poland, and Hungary (outside the sample) are indicative here.[55] Once the political economy has been set on a new course, Communist leaders tend to function within the new rules of the game. The crucial point is this: in cases where the same Communist leaders remain in power throughout, little change occurs. High regime continuity precludes decisive reforms and stabilization.

Hypothesis 3: Voting Rules, Parliamentary and Representation System Matter

Despite Roubini and Sachs's results showing that multiparty coalition governments tend to be unable to implement stabilization plans, the presence of one party in the government was not a good predictor of stabilization success (table 8). Indeed, of the successful stabilizers, five had multiparty coalition governments (Slovenia, Estonia, Latvia, Lithuania, Macedonia), while only three had single-party leaderships (Croatia, Moldova, the Kyrgyz Republic). On the other hand, of the unsuccessful stabilizers, four had strong, single-party majorities (three of these being systems of presidential rule with minimal opposition–Kazakstan, Uzbekistan, and Turkmenistan; and the other a system dominated first by former Communists and then by pro-Russian, also Communist forces–

Belarus), and two had political bottlenecks defined mainly by conflict between the president and the parliament (Ukraine and Russia).

Table 8. Stabilization by Type of Government

	Most Successful or Successful	Somewhat Unsuccessful or Unsuccessful
Multiparty	5	2
Single party	3	4

Looking at specific cases, Slovenia is a good example of a successful stabilizer with weak coalition governments–two of them in the stabilization period (the DEMOS government formed in May 1990 and the three-party coalition formed in July 1992). Lithuania's ex-Communists, returning to power in coalition in November 1992, were also successful stabilizers. On the other hand, Croatia's electoral system, structured to produce a one-party majority in parliament, facilitated successful stabilization after October 1993.

Among the nonstabilizers, political paralysis was crucial in both Ukraine and Russia. Ukraine's political atomization has clearly been a factor preventing stabilization, making agreement among presidents, prime ministers, and parliament extremely difficult.[56] Similarly, in Russia, the running battle between President Yeltsin's economic team and parliament tremendously complicated stabilization.[57] Even after the October 1993 conflict and the referendum-based increase in presidential powers, a fractured parliament, often hostile to the government's program, prevented implementation by blocking budget agreements, vetoing the president's candidate for governor of the Central Bank, and so forth. On the other hand, the relatively oppositionless regimes of Belarus, Kazakstan, Uzbekistan, and Turkmenistan were not success stories of stabilization, as noted above.

From studying the actual cases, it is clear that the political will to stabilize must be present; the form of government is only a facilitating variable. Apparently, formation of a single-party, majority government is not even a necessary condition for stabilization. A possible explanation for this phenomenon is that coalition governments allow blame-sharing; it becomes safer to undertake unpopular measures knowing that one's major rivals are also implicated.[58]

In the longerterm it will be interesting to see whether political structures that allow more clear-cut governing majorities to emerge prove more effective at stabilization and economic reform. The data so far, however, do not really support the advantages of clear-cut majorities.

Hypothesis 4: Location and External Alliances Affect Stabilization

The location of the new states plays a key role in determining their external alliances and their foreign policy. This in turn strongly affects domestic policy. The desire of some new states to join the EU[59] or to restore close ties with traditional neighbors (the Baltic states) has certainly been an important factor in policymaking in these states. On the other hand, the aloofness and ambivalence of Belarus, Ukraine, and Russia toward the West has somewhat limited the imitation of Western institutions. Finally, in Central Asia, a number of external influences are important, including Turkey, Iran, the Gulf States, and of course, Russia (table 9).[60] The new states have not accepted any single model from outside. The exception here is the Kyrgyz Republic, which has embraced the IMF model and received IMF support.

Table 9. Stabilization by External Alliances

	Most Successful or Successful	Somewhat Unsuccessful or Unsuccessful
EU	6	0
West	2	1
Russia	0	3
Other	0	2

It is interesting to note in this context that none of the signatories of the draft Treaty on the Union of Soviet Sovereign Republics on July 23, 1991, have been successful stabilizers:

Russia, Belarus, Kazakstan, Uzbekistan, and Tajikistan.

The Russian experience deserves special attention, since it is the only country in the sample with an imperial history. Russian stabilization was greatly affected by relations with "the near abroad." Aslund argues that one of the major reasons for the failure of Russian stabilization efforts in 1992–93 was the decision to continue with the ruble zone. Although other members of the zone were not able to print money, they were able to emit credit. This enormously swelled the supply of rubles, stoking inflationary fires not only in the other members of the zone, but also in Russia. In addition, Russia provided enormous subsidies to other members of the zone through cheap credits, cash shipments, and implicit trade subsidies via below-market prices. Aslund, using IMF data, argues that Russia "gave away" 22.5 percent of its GDP in 1992 through such mechanisms. In part, this financing reflected Russia's foreign policy priorities (support for Tajikistan and Armenia in particular).[61]

Furthermore, the role of international financial institutions deserves special mention. The IMF provided important support for the Baltic stabilizations, as well as for stabilization efforts in Moldova, the Kyrgyz Republic, Kazakstan, Ukraine, Russia, Uzbekistan, and Belarus. However, Slovenia and Croatia stabilized without IMF help, and Macedonia implemented two partially successful programs before getting the IMF's help with their third program.[62]

Furthermore, some of the programs that the IMF has supported have not been entirely successful (Ukraine, Russia). Hence, it is not possible to say that IMF support has been a necessary condition for the initiation or the success of stabilization.

The burden of evidence thus supports the importance of geographical location and historical relationships in the choice of new economic and political systems. The breakup of the Communist federations has allowed pre-Communist ties to be renewed in many cases. This external influence, however, should not be taken to exclude internal factors; rather, the two work together. To some extent, independence movements were strong when they advocated joining (or rejoining) an external community that could provide support to the new state. And strong independence movements were then able to make the decisive reforms that achieved stabilization.

Hypothesis 5: Authoritarianism Is Not Necessary for Stabilization

In the cases of the new states, the hypothesis that authoritarian regimes are more likely to implement successful stabilization programs must be rejected (table 10). Several of the strongest stabilizers—Slovenia, Estonia, Latvia, and Lithuania—operated under regimes of parliamentary democracy. In fact, government changes in Slovenia in 1992, and in Latvia in 1993, did not prevent the continuation of stabilization policies.

Table 10. Stabilization by Authoritarianism

	Most Successful or Successful	Somewhat Unsuccessful or Unsuccessful
Permit opposition	8	3
Forbid opposition	0	3

Furthermore, the most authoritarian countries—Kazakstan, Turkmenistan, and Uzbekistan, with strong presidential regimes and little organized opposition—were either very slow stabilizers or did not stabilize successfully at all.

Admittedly, table 10 oversimplifies by making authoritarianism a yes or no question. The Political Freedom Index, a more sensitive measure for tracking the degree of freedom granted to opposition parties, the press, and the citizenry at large, gives a more nuanced view. Most successful or successful stabilizers score 5.06 on average while nonstabilizers score 2.91. (Higher scores reflect greater political liberties.) Excluding the Central Asian states from both sides still leaves a palpable difference: stabilizers score 5.14, while nonstabilizers score 4.33.[63]

The reason for this finding lies in the ability of democratic regimes to use the achievement of national independence and the end of Communism to legitimize bold reforms. The crisis situation created by independence and transition gave democratic governments considerable space to implement policies that required short-term pain. Such policies would have been much more difficult to implement in more normal times; an economic crisis without the accompanying moment of independence would have been much more difficult to handle.[64]

In addition, it seems that democratic governments have greater legitimacy and have less to fear from popular dissatisfaction that might be occasioned by stabilization. The ability of democratic regimes to mobilize popular support and cooperation may in fact be an asset in stabilization.

Finally, democracy may facilitate curbing the power of bureaucrats and managers from the old system who become the object of social disapproval, particularly in connection with spontaneous privatization.

Hypothesis 6: Ethnic Homogeneity Does Not Predict Political Homogeneity Well

The discussion above argued that greater political homogeneity should facilitate successful stabilization, but offered a number of qualifications concerning the relationship between ethnic homogeneity and political homogeneity. The data in table 11 underline these qualifications. While Slovenia, the most ethnically homogeneous state in the sample, is among the most successful stabilizers, several similiar states—Russia, Belarus, Turkmenistan, and Uzbekistan—are among the somewhat unsuccessful or unsuccessful groups.

Table 11. Stabilization by Ethnic Split

	Most Successful or Successful	Somewhat Unsuccessful or Unsuccessful
Majority over 75%	2	2
Majority 65-75%	3	3
Majority under 65%	3	1

At the same time, two of the most heterogeneous states, Estonia and Latvia, are highly successful. It should be noted that citizenship rules in these countries produced electorates that were more ethnically homogeneous than the population as a whole. Also, Russian emigration from the Baltics has occurred since independence.[65]

Another interesting example is the Kyrgyz Republic. Alexander Filonyk argues that, precisely because of the country's highly diverse population, only a tolerant and nonchauvinist approach to ethnic relations is possible.[66] The anti-Uzbek riots in Osh in 1990 showed what could happen if conflicts were not dealt with. Furthermore, relations with the Russian population, which feels its social position endangered, are also quite sensitive. It is very interesting that, in such a delicate situation, stabilization policies have been so successful.

The mere numbers of the ethnic split do not tell the whole story. Relations are far more strained in Ukraine than in Kazakstan, although the numbers would imply that Kazakstan should be more polarized. And despite the sizable 65 percent majority of Moldovans in Moldova, the country was crippled by conflict over Transdniester. Admittedly, this conflict was not simply ethnic; as Kosto et al. point out, Moldovans were on both sides of the conflict.[67] Yet it is incontrovertible that Transdniester is ethnically far different from the rest of Moldova.

Perhaps a key point is that ethnic conflict is not necessarily the same as economic conflict. If stabilization is seen as benefiting everyone, it may be possible to gain support for stabilization policies from both majority and minority groups. On the other hand, if stabilization is seen as exacerbating distributional conflicts that are ethnically defined, then ethnic heterogeneity can be a factor preventing stabilization.

Hypothesis 7: Small Countries Have to Stabilize

One of the initial fears of outside observers following the breakup of both the Yugoslav and Soviet federations was that the new, smaller states would be economically disadvantaged. However, initial evidence is far more optimistic: of the eight new countries with populations under 5 million, only Turkmenistan has thus far failed the stabilization test. Indeed, it is not the smaller states, but the larger ones that have had the most difficulty: of the remaining five states, each of which has a population greater than 10 million, none can be called successful or even somewhat successful at taming inflation (table 12).

Table 12. Stabilization by Population

	Most Successful or Successful	Somewhat Unsuccessful or Unsuccessful
Under 5 million	8	1
5 million to 25 million	0	3
Over 25 million	0	2

Of course, this should not be taken as a call for the further disintegration of the larger states. The long-term economic prospects of Russia and Ukraine, in particular, ought to be good. But their inability to solve the urgent short-run tasks is striking.

Hypothesis 8: Income Level Is Not a Major Factor

We can test this hypothesis by dividing the countries into three income groups: highest (above $2000), middle ($1000–2000) and low (below $1000).[68] The results shown in table 13, suggest that there is no correlation between income level and success of stabilization.

However, there are some anomalies in the classification: Croatia and Latvia are in the middle income group, whereas they could easily be in the high income group. Furthermore, all the income figures are highly sensitive to exchange rates.

Table 13. Stabilization By Income Level

	Most Successful or Successful	Somewhat Unsuccessful or Unsuccessful
High income	2	2
Middle income	4	3
Low income	2	1.

Nonetheless, there is an important story here: richer countries may not stabilize quickly, and poorer countries may. The cases of Macedonia and the Kyrgyz Republic are especially interesting, for they are small, poorer countries with rather good stabilization records. The IMF has supported both countries heavily, in contrast to Slovenia and Croatia, which stabilized without receiving IMF help.

Hypothesis 9: Favorable Fiscal Separation Shocks Facilitate Stabilization

The more successful stabilizers, generally speaking, did gain the most fiscally from separation (table 14). Slovenia, Croatia, and the Baltic Republics all stood to gain from the ending of Federal Yugoslav or all-Union budgetary transfers.

Table 14. Stabilization by Fiscal Separation Shock

	Most Successful or Successful	Somewhat Unsuccessful or Unsuccessful
Positive	5	1
Zero	0	2
Negative	3	3

The clear message here is that a positive fiscal shock makes fiscal consolidation easier and thus greatly reduces a key cost of stabilization. However, a negative fiscal shock can be overcome, as the cases of Macedonia and the Kyrgyz Republic show, even though the costs to the real economy may be more severe. Furthermore, the loss or disruption of markets also created negative demand and tax receipt shocks for all countries in the sample that may offset any positive fiscal separation shocks.

Another unusual case is Russia, with a positive stabilization shock and positive terms-of-trade shock, yet only somewhat successful in stabilizing inflation.

Hypothesis 10: Favorable Terms-of-Trade Shocks Retard Stabilization

Interestingly, matters look different when we consider terms-of-trade shock (table 15):

Table 15. Stabilization by Terms-of-Trade Shock

	Most Successful or Successful	Somewhat Unsuccessful or Unsuccessful
Positive	1	3
Zero	0	0
Negative	3	2

The results seem to suggest that adverse terms-of-trade shocks are correlated with stabilization, while positive terms-of-trade shocks are correlated with lack of stabilization! A reason for this may be that the adverse shocks force countries into contractionary policies for balance-of-payments reasons, reinforcing the stabilization motive. Conversely, a terms-of-trade windfall may make adjustment seem unnecessary. Something like this may be going on in the energy-rich state of Turkmenistan.[69]

Furthermore, the introduction of new currencies has had a positive terms-of-trade effect for the more successful countries. These countries have seen significant real currency appreciation associated with stabilization processes.

It becomes clear that separation shocks, by affecting the costs of stabilization, affect both the timing and degree of success of stabilization without making stabilization either automatic or impossible.

Long-run Issues

The degree of success at stabilization is only one indicator of the economic viability of the new nations. Since short-run success may not translate into long-run success, and short-run measures may even interfere with long-run prospects, it is worthwhile mentioning some of the major long-run factors:

1. While the immediate crisis of independence and hyperinflation created breathing space, in the long term the structure and style of labor relations will be a major factor affecting macroeconomic stability, economic growth, and social stability. So far, union movements have been weak, since the old unions were generally identified with Communism, and new unions have to begin organizing almost from scratch. There are exceptions: Slovene labor movements played a significant role in the independence struggle, and Ukrainian miners were and remain a potent force.[70]

Union activity has generally not affected stabilization too drastically so far. Even in Russia, where wage demands were often vocally expressed, wage increases followed inflation, rather than causing it.[71] The biggest exception is

Ukraine, where the government has been unable to find common ground with the predominantly Russian work force in the Donbass, and labor unrest has helped generate inflation. Indeed, this is one of the keys to the stabilization delay in Ukraine. As Dabrowski emphasizes, parliament's support of labor's demands figured heavily as well.[72]

The examples of Macedonia, Slovenia, and Estonia suggest a different situation: successful stabilizers may have labor problems once stabilization is achieved. Workers' willingness to make sacrifices can evaporate quickly once victory is proclaimed in the war on inflation. In Macedonia, trade union pressure led to the granting of substantial wage increases in the summer of 1992 and the summer of 1993, seriously threatening stabilization.[73] In Slovenia, trade unions have resisted incomes policy; and a number of specific unions, including teachers and metalworkers, have struck. Stabilization was perhaps slowed down by wage increases in the spring of 1992 and January 1993, but overall wage increases have been kept to a level compatible with monthly inflation in the 1-2 percent range. In Estonia, labor unrest has focused on Russian industrial workers in Narva, but without endangering stabilization as yet. Eventually, all these countries will need to institutionalize labor relations so as to avoid continual conflict.

2. In the successful stabilizers, central banks have achieved a degree of operational independence. This occurred in part under international pressure (it was strongly urged by international financial institutions). But it was also an endogenous result of antiinflation consensus, as Posen argues is generally the case.[74] The converse is true as well, as the Russian example suggests: the failure of the Central Bank of Russia to fight inflation reflected the preferences of the Russian parliament, especially in 1992.

Central bank independence is an important institutional feature that will shape long-term prospects.[75] Greater central bank independence is generally expected to lead to more restrictive policies with a greater focus on inflation as the central economic issue. Furthermore, those countries that have adopted extremely restrictive monetary arrangements, such as currency boards (Estonia and Lithuania) should have lower inflation rates, but they may also have difficulties living with such rigid institutions.

3. Restructuring of ownership relations in the economy should allow significant growth in productivity and facilitate long-term specialization. Ownership restructuring is often reduced to privatization, but it can include the formation of a public sector as well. Rehabilitation and restructuring of the financial system are closely related to real sector restructuring as well.

Here, while greater homogeneity might facilitate the passage of privatization legislation, the larger relative size of key enterprises and interest groups could be a restraining factor. Hence the relationship between independence and privatization/restructuring success remains an open issue.

4. Both the success and the content of initial stabilization efforts can have a strong effect on future developments. Early success in creating macrostability should facilitate restructuring and encourage foreign capital flows. Because of their early stabilization success, countries like Estonia and Slovenia may benefit from first-mover advantages and attract some footloose investment that otherwise might have gone to neighboring countries.

5. Fiscal and industrial policies to stimulate economic growth require both new institutions and new thinking. These may be facilitated by independence, but it should be noted that smaller states may be less able to implement industrial policy and have less fiscal room to manoeuver as well. Also, stabilization programs that require drastic fiscal adjustments can have a negative impact on public investment, with negative long-term effects.[76] And very tight monetary policies can leave a legacy of high interest rates and overvalued currencies that may impede growth.[77]

Conclusion

While many factors contributed to stabilization success among the new transition countries, it seems that where independence movements were strongest, stabilization efforts generally were the most successful. More successful stabilizers also displayed lower levels of regime continuity than less successful stabilizers. Successful stabilizers have been easier to find where external alliances were most favorable as well. Authoritarianism does not aid stabilization, but political freedom is positively correlated with stabilization. Small economies almost universally were stabilizers, while larger economies generally were not. Finally, positive fiscal effects of separation and negative terms-of-trade shocks were usually associated with more success in stabilization.

Other seemingly important variables displayed less explanatory power. Political system design, ethnic homogeneity, and income level did not seem to be especially good predictors of stabilization success. Also, while smooth labor relations and/or social compacts were a prerequisite to stabilization, building of new bargaining relationships was not a major contributing factor.

The evidence discussed here also suggests that independence has facilitated stabilization in the countries most eager for independence in the first place. Thus it seems that the exante assessment that independence would be economically beneficial has been affirmed for states such as Slovenia, Estonia, Latvia, and Lithuania. For others, slow or failed stabilization (Belarus, Kazakstan, Uzbekistan, Ukraine, Turkmenistan) or extremely high costs of independence (Macedonia, the Kyrgyz Republic) raise serious questions about the economic rationality of separation. Of course, these assessments may look different from a longer perspective.

This research is only a small part of the evaluation of the economic prospects and performance of the new states. Undoubtedly, the new states will become more diverse as time goes on. It will be most interesting to follow economic trends in these countries to see how long-term economic outcomes can be explained.

Notes

The author would like to acknowledge the helpful comments of Vojmir Franicevic, Ivo Bicanic and Mieke Meurs. They bear no responsibility for any remaining errors.

1. Bicanic argues that the breakup of the multinational states of Yugoslavia, Czechoslovakia, and the Soviet Union must have had some economic rationale. He notes that the debates over separation and independence suggest that political leaders at least thought that they would gain economic advantages from going it on their own. Ivo Bicanic, "The Economic Causes of New State Formation During Transition," *East European Politics and Society* 9, 1 (Winter 1995): 2–21.

2. Milica Uvalic, "Costs and Benefits of Separation: The Case of Yugoslavia," *Communist Economies and Economic Transformation* 5, 3 (September 1993) 273: 293; and Bert von Selm, *The Economics of Soviet Break-up* (Capelle a/d Ijssel, Holland: Labyrint Press, 1995).

3. If I merely asked, "Are the new states better off?" part of the answer would have to be that those experiencing war are certainly worse off. My question is a narrower one: Does the new structure of smaller states facilitate stabilization (and thereby economic growth)? Even that narrower question, we shall see, cannot be answered with an unambigios yes.

I have included Croatia and Moldova in my sample although both their conflicts were over early enough to allow for stabilizationto become a serious issue fairly quicky. In other cases mentioned, war created choas nd prevented stabilization efforts, at least for a significant period of time. Among the countries more deeply affected by war, Federal Yugoslavia (Serbia-Montenegro), Armenia, and Georgia did stabilize inflation, but it seems unwise to include these countries in comparisons based on the speed and success of stabilization.

I have excluded Czechoslovakia, also a multinational Communist state, because stabilization of inflation has not been a major issue since seperation into the Czech and Slovak republics.

4. Among recent works, Stanners disputes the existence of tradeoff; Levine and Revelt and Levine and Zervos argue that the evidence for the tradeoff is not robust; Fischer, De Long, and Summers (1992), Cukierman et al., and Smythe uphold it. See W. Stanners, "Is Low Inflation an Important Condition for High Growth?" *Cambridge Journal of Economics* 17, 1 (March 1993): 79–108; Ross Levine and David Renelt, "A Sensitivity Analysis of Cross-Country Growth Regressions," *American Economic Review* 82 (September 1992) 942–63 Ross Levine and S. Zervos , "Looking at the Facts: What We Know About Policy and Growth from Cross-Country Analysis" in Luigi Pasinetti and Robert Solow, eds., *Economic Growth and the Structure of Long-Term Development*, (New York: St. Martin's Press, 1994), 22–44: Stanley Fischer, "Macroeconomic Development and Growth," *NBER Macroeconomics Annual* (Washington, D.C.: NBER, 1991), 329-64: Stanley Fischer, "Macroeconomic Factors in Growth," *Journal of Monetary Economics* 32, 3 (December 1993): 485–512; J. Bradford DeLong and Lawrence Summers, "Macroeconomic Policy and Long-Run Growth," *Federal Reserve of Kansas City of Economic Review* 77, 4, 4th Quarter, 1992: 5–30; Alex Cukierman et al., "Central Bank Independence, Growth, Investment and Real Rates," *Carnegie-Rochester Conference Series on Public Policy* 39 (December 1993): 95–140; David Smyth, "Inflation and Growth," *Journal of Macroeconomics* 16, 2 (Spring 1994): 261–70.

5. Stanley Fischer, Ratna Sahay, and Carlos A. Vegh, "Stabilization and Growth in Transition Economies: The Early Expirence," *Journal of Economic Perspectives* 10, 2 (Spring 1996): 45–67. See also William Easterly, "When Is Stabilization Expansionary? Evidence from High Inflation," *Economic Policy: A European Forum* 22 (April 1996): 65–98; and Michael Bruno and William Easterly, "Inflation's Children: Tales of Crises That Beget Reforms," *American Economic Review* 86, 2 (May 1996): 213–17.

6. Uzbekistan's output fall is remarkably small. Agzamov, Anvarov, and Shakirov point to a high share of agriculture in total output, favorable trade shocks thanks to the large weight of cotton and gold in exports, a relatively small military-industrial complex, preservation of managerial talent due to the absence of drastic political change, and successful gradualist policies. The latter two points, however, are debatable. The IMF emphasizes only the homogeneous nature of Uzbekistan's main exports, cotton and natural gas. These can be very easily redirected to world markets, thus cushioning the effect of the collapse of the CMEA. Akhad Agzamov, Alisher Anvarov, and Kahramon Shakirov, "Economic Reform and Investment Priorities in the Republic of Uzbekistan," *Comparative Economic Studies* 37, 3 (Fall 1995): 27–38; International Monetary Fund, "Uzbekistan STF," *IMF Survey*, (February 20), 1995: 60–61.

7. The stabilization techniques employed may also be a factor. Sachs argues that stabilization programs employing fixed exchange rates led to smallet output declines that those using floating exchange rates. Jeffrey Sachs, "Economic Transition and the Exchange-Rate Regime," *American Economic Review* 86, 2 (May 1996): 128–33.

For a detailed discussion of factors behind the drastic output declines in the Baltic states, see Pekka Sutela, Production, Employment and Inflation in the Baltic Countries," *Communist Economies and Economic Transformation* 6, 2 (1994): 157–74; and Ardo Hansson. "Macroeconomic Stabilization in the Baltic States," in *Marcoeconomic Stabilization in Transition Economies*, ed. Mario Blejer and Marko Škreb (Cambridge: Cambridge University Press, 1997) 256–80. All the data are of course, highly suspect because of difficulties involved in measuring output in transition economies with large informal sectors and inexperienced and understaffed government statistical services.

8. Berg makes this argument in connection with Poland's stabilization of 1990–1. Andrew Berg "Does Macroeconomic Reform Cause Structural Adjustment? Lessons from Poland," *Journal of Comparative Economics* 18, 3 (June 1994): 376–409.

9. A strong argument for this position is given in Stanislaw Gomulka, "The IMF-Supported rograms of Poland and Russia, 1990–1994: Principles, Errors, and Results." *Journal of Comparative Economics* 20 (June 1995): 316–46.

10. Alberto Alesina and Allen Drazen, "Why Are Stabilizations Delayed?" *American Economic Review* 81, 5 (December 1991): 1170–88.

11. Guido Tabellini and Alberto Alesina, "Voting on the Budget Deficit," *American Economic Review* 80, 1 (March 1990): 37–49. One problem with their argument is the simple fact that, in most countries, voters do not choose debt, only political parties. Since these parties have stands on a great number of issues, only some of which may influence a voter's choice, there is the possibility that the electorate could "vote for debt" by choosing a party that plans to incur debt because that party has an attractive stand on some other issue. For example, in Croatia

voters might not approve of the Croatian Democratic Union's (HDZ) economic plans, but still vote for the party because of its views on nation-building.

Two other explanations of the apparent paradox that voters accept the idea that budgets should be balanced, but vote for candidates who will fail to balance the budget are provided in the work of Buchanan, and Rogoff and Sibert. Buchanan emphasizes "fiscal illusion": voters do not see the connection between tax revenue and expenditure due to the complexity of government operations, and therefore underestimate the opportunity cost of public goods and services. Rogoff and Sibert, on the other hand, view voters as rational, but argue that imperfect information about candidates can lead to suboptimal choices. James Buchanan, *The Public Finances* (Homewood, Ill.: Irwin, 1970); Kenneth Rogoff and Anne Sibert, "Elections and Macroeconomic Policy Cycles," *Review of Economic Studies* 55 (January 1988): 1–16.

12. This may have special significance in the longer term. Long-term stabilization requires microlevel changes to eliminate the soft-budget phenomenon—above all the commercialization and privatization of enterprises and the restructuring of the financial system. The distributional implications of stabilization pale in comparison with the immediate and transparent distributional impact of privatization. It can be expected that the struggle over privatization will be far more intense and drawn out than the struggle over stabilization.

13 For argument and evidence of the role of comprehensive bargaining in minimizing distributional conflict and enhancing macroeconomic stability, see Phillippe Schmitter, "Still the Century of Corporatism," in *Trends Towards Corporatist Intermediation*, ed. Phillippe Schmitter and L. G. Lehmbruch, (London: Sage Publications, 1979); and Nouriel Roubini and Jeffrey Sachs, "Political and Economic Determinants of Budget Deficits in Industrial Democracies," *European Economic Review* 33, 5 (May 1989): 903–33.

14. I owe this point to Ivo Bicanic, who argues that it has special relevance for Croatia.

15. Homogeneity here need not be ethnic; homogeneity of economic interests and political behavior is the bottom line.

16. Paul Mosley, Jane Harrigan, and John Toye, *Aid and Power* (London: Routledge, 1991), 145–47.

17. Mancur Olson, *The Rise and Decline of Nations: Economic Growth, Stagflation, and Social Rigidities* (New Haven Conn.: Yale University Press, 1982).

18. Of course, some distributional coalitions may exist only within the former republic and may pass untransformed into the new state. The power of Croatian shipbuilders was substantial within Yugoslavia and remained strong in independent Croatia, for example. I owe this observation to Ivo Bicanic.

19. Adam Przeworski, *Democracy and the Market: Political and Economic Reforms in Eastern Europe and Latin America* (Cambridge: Cambridge University Press, 1991), 174.

20. This point is made forcefully by Anders Aslund, *How Russia Became a Market Economy* (Washington, D.C.: Brookings, 1995), 7. For a more detailed discussion of distributional coalitions in ex-Yugoslavia and independent Slovenia, Croatia, and Macedonia, see Evan Kraft, "Stabilizing

Inflation in Slovenia, Croatia, and Macedonia: How Independence Has Affected Macroeconomic Outcomes," *Europe-Asia Studies* 47, 3 (May 1995): 469–92.

21. Alesina and Drazen, "Why Are Stabilizations Delayed?" and Nouriel Roubini and Jeffrey Sachs, "Government Spending and Budget Deficits in the Industrial Countries," *Economic Policy*, 8 (April 1989): 100–32.

22. For classic statement of the advantages of authoritarian regimes see Thomas E. Skidmore, "The Politics of Economic Stabilization in Latin America," ed. *Authoritarianism and Corporatism in Latin America* James M. Malloy (Pittsburgh, PA.: University of Pittsburgh Press, 1977). But see also Luiz Carlos Bresser Pereira, Jose Maria Maravall, and Adam Przeworski, *Economic Reforms in New Democracies: A Social-Democratic Approach* (New York: Cambridge University Press, 1993).

23. Laurence Whitehead, "Democratization and Disinflation: A Comparative Approach," in *Fragile Coalitions: The Politics of Economic Adjustment*, ed. Joan Nelson (Washington, D.C.: Overseas Development Council, 1989): 79–94.

24. Although, as Przeworski rightly points out, many anti-Communists are not democrats. Przeworski, *Democracy and the Markets*: 91–93.

25. Lance Taylor, "The Market Met Its Match: Lessons for the Future from the Transition's Initial Years," *Journal of Comparative Economics* 19, 1 (January 1994): 64–87.

26. Richard Pomfret, "The Collapse of the Ruble Zone," *Development and International Co-operation* 11, 20-21 (June-December 1995): 271–92.

27. Przeworski, *Democracy and the Market*, 174–79.

28. Von Selm uses a gravity model to show that the former Soviet republics' share of trade with each other was unnaturally high and that separation necessarily had to lead to a decrease in trade among them. *Economics of Soviet Break-up*, chap. 4. A similar argument could probably be made for Yugoslavia, although very likely the degree of change would be smaller.

29. Slay shows that Central European trade has declined since 1989, but indicates that the worst may be over. He argues that the chances for increasing regional integration are fairly good. Ben Slay, "The Czech Republic, Slovakia, and Regional Economic Cooperation," paper presented at the 25th National Conference of the American Association for the Advancement of Slavic Studies, Honolulu, Hawaii, November 1993.

30. See Evan Kraft, "Evaluating Regional Policy in Yugoslavia, 1966–90," *Comparative Economic Studies* 34, 3–4 (Fall-Winter 1992): 11–33, for analysis of interregional transfers in Yugoslavia.

31. Currency board approaches can support fixed rates with limited reserves. However, the only country among all the new states employing a modified currency board approach, Estonia, had the luxury of returned gold reserves. The reserves were confiscated when Estonia was annexed by the Soviet Union in 1940 and were returned when Estonia regained independence. See Ardo

Hansson, "Estonia," in *First Steps Towards Economic Independence in Post-Communist States*, ed. Michael L. Wyzan, (New York: Praeger, 1995) 25–49.

32. A very important area of future research is to track the effects of separation on transition issues such as privatization and bank restructuring. Since these are mainly supply-side factors, their effect is felt more in the long-term viability of stabilization than in the short-run outcome of stabilization programs.

33. I chose 1995 rather than 1996 because 1995 was the last year in which numerous countries were still experiencing higher inflation. Thus the differences among inflation rates in 1995 are more revealing than the differences recorded in 1996.

In 1996, there were isolated incidents of higher inflation in several countries. Inflation exceeded 5 percent in one month in 1996 in the Kyrgyz Republic, and it exceeded 5 percent in two months in Belarus. But in neither of these cases did monthly inflation reach beyond 7.5 percent, and overall stability was not in question. On the other hand, Ukraine recorded three months of inflation above 5 percent, and Uzbekistan experienced four months of inflation above 5 percent, including two months of inflation over 10 percent at the end of 1996. Finally, Turkmenistan's inflation rate was above 5 percent in eleven of the twelve months of 1996!

My criterion of stabilization success is intentionally narrow. I am very sympathetic to the criteria suggested by Bresser Pereira et al.: a resumption of growth at stable and moderate inflation under democratic conditions. While it appears that most of the countries classified as successful by my narrow criterion will ultimately satisfy the Bresser Pereira criteria as well, it is probably premature to conclude this. See Bresser Pereira et al, Economic Reforms in New Democracies, 3–4.

34. For a useful survey of the introduction of new currencies in the Baltic states, see Seija Lainela, "Currency Reforms in the Baltic States," *Communist Economies and Economic Transformation* 5, 4 (July 1993): 427–44.

35. See Kraft, "Stabilizing Inflation" and Zoran Anušic, •eljko Rohatinski, and Velimir Šonje, *A Road to Low Inflation* (Zagreb: Government of the Republic of Croatia, 1995), for more details. While Croatia would have had great difficulty stabilizing during the war in 1991, it fairly explicitly postponed stabilization in 1992 and most of 1993.

36. See Michael L. Wyzan, "Monetary Independence and Macroeconomic Stabilisation in Macedonia: An Initial Assessment," *Communist Economies and Economic Transformation*, 5, 3 (September 1993): 351–68; and Michael L. Wyzan, "Macedonia," in *First Steps Toward Economic Independence* ed. Michael L. Wyzan (Praguer, Westport, Conn.: 1995), 193–208.

37. Some have questioned whether stabilization is possible even in thoseountries with low levels of development and little tradition in self-governance. Yavlinsky and Braguinsky, for example, argue that the soft currencies of the former Soviet republics, excluding the Baltics, "cannot be stabilized in principle." The Kyrgyz case is a potential counterexample. Grigory Yavlinsky, Grigory Braguinsky, and Serguey Braguinsky, "The Inefficiency of Laissez-Faire in Russia: Hysteresis Effects and the Need for Policy-Led Transformation," *Journal of Comparative Economics* 19, 1 (August 1994): 88–116. A useful overview of the Kyrgyz reforms is found in Marek Dabrowski et al., "Economic Reforms in Kyrgyzstan," *Communist Economies and Economic Transformation* 7, 3 (May 1995): 269–97.

38. Pal Kosto, Andrei Edemsky, and Natalya Klashnikova, "The Dniester Conflict: Between Irredentism and Separatism," *Europe-Asia Studies* 45, 6 (December 1993): 973–1000. Some advances toward peace were made with the announcement of the eventual withdrawal of Russian forces from Transdniester in October 1994, the settlement of the conflict with the Gaugaz minority in August 1995, and Transdniester's acceptance of the leu in the same month.

39. Marshall Goldman argues that the Gaidar reforms did not have the expected effects because of Russia's institutional peculiarities. Lack of market institutions and culture, he believes, prevented significant supply response. See Marshall Goldman, *Lost Opportunity: What Has Made Economic Reform in Russia So Difficult*? (New York: Norton, 1996), chap. 5. While there is considerable merit in this argument, it should also be noted that other former Soviet republics did bring down inflation more rapidly than Russia. It is not clear why Kyrgyzstan or Moldova would have more viable market institutions than Russia. Therefore, at least some of the failure of Russian stabilization has to be attributed to policy reversals rather than the lack of necessary institutions. For a useful account by an influential western advisor, see Aslund, *How Russia Became a Market Economy*, chap. 6. Easterly and Viera de Cunha argue that enterprises ended up flush with resources, creating a situation of "Rich enterprises, poor economy" by their effective lobbying efforts. William Easterly and Paulo Viera de Cunha, "Financing the Storm: Macroeconomic Crisis in Russia," *The Economics of Transition* 2, 4 (December 1994): 443–65.

40. An interesting analysis of the distributional struggle, written from the perspective of the IMF, is found in Ernesto Hernandez-Cata, "Russia and the IMF: The Political Economy of Macrostabilization," in *Policy Experiences and Issues in the Baltics, Russia and Other Countries of the Former Soviet Union* ed. Daniel Citrin and Ashok Lahiri, (Washington, D.C.: International Monetary Fund, 1995), 117–24. For more on the political economy of the government budget, see Peter Kirkow, "Distributional Coalitions, Budgetary Problems, and Fiscal Federalism in Russia," *Communist Economies and Economic Transformation* 8, 3 (September 1996): 277–98. Andrei Illirianov, "Temporary Stabilization in Russia," Paper presented at the 2nd Dubrovnik Conference on Transition Economies, June 1996, describes—somewhat skeptically—the success of stabilization policies in 1995 and early 1996.

41. For example, Kazakstan's willingness to work with the IMF, and the design of its stabilization program, were decisively influenced by the Russian example. Interview with David Hoelscher, IMF Resident Representative, Almaty, July 1997.

42. *IMF Survey*, "Belarus: Standby Credit," 291–2. (September 25, 1995).

43. Richard Pomfret, *The Economies of Central Asia* (Princeton N.J.: Princeton University Press, 1995), 90–95. In Soviet terminology, the Central Asian states were Uzbekistan, Turkmenistan, Tajikistan, and Kyrgyzstan (now the Kyrgyz Republic). The exclusion of Kazakstan seems unnatural, however, so I will follow the practice of Pomfret and others of including Kazakstan in the Central Asian states.

44. See *IMF Survey*, "Belarus: Standby Credit," 291–2. February 20, 1995, and January 8, 1996.

45. Viktor Pynzenyk, "Ukrainian Economic Reforms: Reflections on the Past and the Future," *Economic Policy*, Supplement (December 1994): 197–204; and Daniel Kaufman,

"Diminishing Returns to Administrative Controls and the Emergence of the Unofficial Economy," *ibid.*, 51–70

46. "Ukraine–Hope at Last," *Economist*, September 24, 1994: 32.

47. The success of Kuchma's reforms is touted in "Ukraine: Better Late Than Never, Maybe," *Economist*, July 22, 1995: 17–19, while the near unraveling is discussed in "Ukraine: Slipping Back," *Economist*, November 25, 1995: 38.

48. European Bank for Reconstruction and Development, *Transition Report* (London: EBRD, 1996), 178–79.

49. Milan Cvikl, Evan Kraft, and Milan Vodopivec, "Costs and Benefits of Independence: Slovenia," *Communist Economies and Economic Transformation* 5, 3, (September 1993), 295–315.

50. Kraft, "Evaluating Regional Policy in Yugoslavia."

51. Of course, the issue of the role and rights of the Albanian minority has remained crucial and unsettled. For Albanian Macedonians, identification with the Macedonian state is far more ambivalent than for Slavic Macedonians.

52. In many cases, the degree of regime continuity was actually determined before independence, during the 1990 elections. Some new states, such as Ukraine and the Central Asian republics, did not hold parliamentary elections until 1994, so the 1990 parliaments—heavily dominated by Communists—remained in power. In other cases, some regime continuity occurred because of the return of Communists or individual former Communist leaders to power (e.g., Lithuania, Slovenia). Communist politicians were certainly present in Estonia, especially in the Saavisar and Vahi governments that ruled from 1990 to 1992. But the influence of former Communists waned drastically during this time, and the September 1992 elections brought a new group of people to power.

53. Anatol Lieven, *The Baltic Revolution: Estonia, Latvia, and Lithuania and the Path to Independence* (New Haven, Conn.: Yale University Press, 1993), 291.

54. Marko Bojcun, "The Ukrainian Parliamentary Elections of March-April 1994," *Europe-Asia Studies* 47, 2 (March 1995): 229–49.

55. An analysis of the implications of the Lithuanian elections is found in Terry Clark, "The Lithuanian Political Party System: A Case Study of Democratic Consolidation," *East European Politics and Society* 9, 1 (Winter 1995): 41–62.

56. Andrew Wilson and Artur Bilous, "Political Parties in Ukraine," *Europe-Asia Studies* 45, 4 (July 1993): 693–705.

57. Aslund, *How Russia Became a Market Economy*, 191–200.

58. I owe this observation to Mieke Meurs

59. Mohiaddin Mesbahi, ed. *Central Asia and the Caucuses: Domestic and International Dynamics* (Gainesville University of Florida Press, 1994), chaps. 13, 14.

60. Aslund, *How Russia Became a Market Economy*, chap. 4.

61. Another important element in the Baltic stabilizations was the return of monetary gold and government assets confiscated after the incorporation of these states into the Soviet Union; the Baltic states were the only ones among those discussed, along with Russia, to have any international reserves to speak of at the time of independence. The IMF granted Stand-by Agreements to Estonia, Latvia, Lithuania, Moldova, the Kyrgyz Republic, and Kazakstan during their stabilization efforts. Croatia received a Stand-by after its stabilization program had succeeded; Kazakstan received one without implementing a full-fledged stabilization program. Other countries received help through the Systemic Transformation Facility, which required a lower level of agreement with the IMF and signified a lesser degree of IMF support of specific government policy initiatives.

62. The index is found in Adrian Karatnycky, "Democracies on the Rise, Democracies at Risk," *Freedom Review*, January/February 1995: 5–22.

63. A variant of this effect is seen in Croatia, where the ever present danger of renewed war muted social protest, facilitating the stabilization efforts of late 1993. I owe this insight to Vojmir Franicevic.

64. Lainela suggests that ethnic heterogeneity has slowed down privatization in Estonia and Latvia in comparison with Lithuania. Seija Lainela, "Private Sector Development and Liberalisation in the Baltic Countries," *Communist Economies and Economic Transformation* 6, 2 (March 1994): 178.

65. Alexander O. Filonyk, "Kyrgyzstan," in Mesbahi, *Central Asia and the Caucasus*, 149.

66. Kosto et al., "The Dniester Conflict," 974.

67. Data are from Christine Wallich, "What's Right and What's Wrong with World Bank Involvement in Eastern Europe," *Journal of Comparative Economics* 20, 1 (February 1995): 57–94.

68. Pomfret, *The Economies of Central Asia*, 126.

69. Tonci Kuzmanic, "Trade Unions and Slovene Independence," in *Independent Slovenia*, ed. Jill Benderly and Evan Kraft (New York: St. Martins, 1994).

70. Aslund, How Russia Became a Market Economy, 198, 222.