

Life After Communism

By JEFFREY D. SACHS

Ten years ago today Czechoslovakia began its "Velvet Revolution," which toppled Prague's communists less than three weeks later. Poland, East Germany and Hungary were already on the road to democracy, and the Soviet Union itself would dissolve two years later. A decade after democracy swept Eastern Europe, it's perhaps too early to assess the social transformations in the former Soviet empire. Yet it's important to learn what we can from the drama of the past decade.

There certainly have been surprises. Poland—everybody's "basket case" of 1989—proved the most durable and dynamic reformer. By contrast, the Czech Republic, everybody's favorite for a smooth transition, is mired in recession and controversy. Yugoslavia exploded, and the rest of the Balkans are beset by economic difficulties. Unsurprisingly, the Baltic states, especially Estonia, have done far better than the rest of the former Soviet Union.

Stubbornly Refused

But most of all it is Russia that has perplexed us. It failed to fall into utter chaos, as gloomy Sovietologists predicted it would. But it has also stubbornly refused to become a "normal" country, as reform-minded economists like me hoped it would. Even knowing that the path from communism would be difficult and that Russia would need considerable and timely financial help from the West, I thought the end of communism would bring a quicker social rejuvenation in Russia.

This kaleidoscope of success and failure offers some general lessons:

- *Markets work, but privatization isn't easy.* The end of price controls and the convertibility of exchange rates at the start of economic reforms succeeded in ending chronic shortages and bringing long-absent goods to the market. Quick liberalization unleashed the beneficial forces of supply and demand, as Poland's experience made dramatically evident.

But when privatization was rushed through via mass voucher schemes, as in Czechoslovakia in 1991 and Russia in 1993, the result all too often was corrupt asset grabs, managerial plunder of enterprises and paralysis of firms. The voucher holders often ended up with nothing. Even though the abuses became clear early on and could have been lessened or reversed, many governments were themselves too corrupt to care.

- *Civil society is crucial.* Power corrupts, and while constitutions can provide some modest checks, civil society—with associations of professions, religions and regions—must provide the deeper balance. Stalin kept his grip on power largely by destroying every manifestation of civil society. In Poland, some vestiges of a civil society survived. (Stalin once complained that establishing communism in Poland

was like putting a saddle on a cow.)

- *Initial conditions matter—often in unexpected ways.* The chaos in Poland in the 1980s actually helped create the basis for rapid growth in the 1990s. By the time the reforms began, the Poles had effectively smashed the stultifying hand of central planning. By contrast, central planning was still very much intact in Czechoslovakia until the Velvet Revolution. As a result,

Since 1989, some Eastern European economies have soared, while others crashed. Their experiences provide some sobering lessons for would-be reformers.

was like putting a saddle on a cow.) The Roman Catholic Church and the Solidarity movement deserve much credit for the success of Poland's reforms, even though they opposed many specific policy proposals. Solidarity unionists within the enterprises stopped the managers from committing outright theft. In Russia, where civil society was dead, corrupt government officials and enterprise managers could act with impunity.

- *Geography influences the pace and depth of transformation.* States bordering prosperous Western European countries—states such as Poland, Hungary, the Czech Republic, Slovakia, Slovenia and the Baltic states (a short ferry ride from Scandinavia)—have done much better at attracting foreign direct investment, expanding exports and generally achieving a successful transformation. Just as U.S. firms often go next door to Mexico, German firms head for the immediate neighborhood to the east. Farther away, some of the Balkan states are doing poorly. The non-Baltic former Soviet Union is in worse shape still.

- *History casts a long shadow.* Nineteen eighty-nine was supposed to be a fresh start, the awakening from a nightmare. But 1989 also awakened ancient antipathies that had been repressed in the communist era. Who would have thought that Serbian myths about the 1389 Battle of Kosovo would galvanize a population in the late 20th century behind the murderous leadership of Slobodan Milosevic? History conditions different societies to expect different things of their leaders. In Russia, society expects little of its leaders and gets less. In Poland, much more was expected—and demanded—of the post-1989 leaders, and much more was ob-

tained in good governance.

- *Western actions make a difference but typically fall short of what is needed for true transformation.* There has been a damaging and persistent view in the West that the success or failure of the transition was



none of our business. The glib optimists held that reform would be its own reward; simply introduce markets and all will work out well, they said. The pessimists maintained that no matter what we did, the situation would be terrible for a generation to come, so why waste the money and effort? These rationalizations of inaction proved tragically wrong.

When the West helped—as when it canceled Poland's debts and gave Warsaw a special fund to stabilize its currency—the results repaid the efforts many times over. When the West did nothing—refusing to provide Russia with funds in the beginning

or to cancel its debt—the results were disastrous. (The International Monetary Fund finally gave aid to Russia, but only after the reformers had been thrown out of office.) Similarly the West missed opportunities to help Yugoslavia, as when Belgrade appealed unsuccessfully for a rollover of its foreign debts in 1990.

My own watchwords as an economic adviser to the region were these: Go for quick internal reforms; seek ample international assistance because that is necessary in practice for successful and democratic transformation; pay attention to morality and government ethics; and insist on transparency in the actions of all parties. This formula got a lot right, and in the places where it was actually applied—Poland, Estonia, Slovenia—the results have been salutary. I was overly optimistic about the possibilities of mass privatization, an approach that I now think was flawed, especially when the governments themselves ignored the danger signs of corruption.

In the case of Russia, I repeatedly warned in 1992 and 1993 that Russian reforms were going off the rails. I even resigned from advising Moscow six years ago and issued a strong public warning against Russian corruption and Western inattention. Sadly, that particular forecast has proved correct.

Expanded Infrastructure

And for the future? For the states that are doing well, the crucial next step is admission into the European Union. This will consolidate the democratic and market reforms and will spur urgently needed private investments. For the Balkans, accession to the EU will probably take some years longer. In the meantime, there is a vital need for greatly expanded infrastructure investments by the EU—in highways, fiber-optic networks, power grids—to link the Balkans more closely with Western Europe.

As for Russia, we can only hope that we have not cheated ourselves of a unique historical opportunity to help it find its way to democracy, social stability and a market economy. If the Russian people are wise enough to select a real reformer in next year's presidential election, we should be wise enough this time around not to squander a precious chance to create a more peaceful world.

Mr. Sachs, director of the Center for International Development at Harvard, has worked as an economic adviser to many Eastern European governments.