

THE EVOLUTION OF POSTCOMMUNIST SYSTEMS: EASTERN EUROPE VERSUS CHINA.

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Abstract: We propose in this article a new interpretation of the evolution of post-communist systems by comparing the evolutions in Central and Eastern Europe and in China. Transition is reinterpreted as the result of a collapse of communist state structures in Central and Eastern Europe and, in China, in contrast, as the result of the will to prevent such an outcome. This reconceptualization helps understand better the emergence of bad institutions and corruption in Eastern Europe under the market economy as well as the absence of political liberalization in China and the strengthening of the power of the Communist Party in recent years.

1. Introduction

It has been nearly 40 years since the beginning of market economic reforms in China and more than 25 years have passed since the historic transition from socialism to capitalism in Central and Eastern Europe. These issues have been studied at least since the late eighties, but it is only now that we are starting to have a minimum of historical perspective on these events and the surprises experienced.

In the first decade of China's reforms, observers criticized the partial and gradual character of Chinese reforms starting reforms only with countryside. There was the hope that radical political change towards democracy in Central and Eastern Europe would lead to better performance following more comprehensive reforms made possible by the elimination of the communist regimes. Surprisingly, this proved wrong at the time. Countries in Central and Eastern Europe all experienced an output fall early in transition and their growth performance ended up being significantly below that of China.

Transition delivered many other surprises than the output fall. The output fall turned out to be much longer and sustained in the Former Soviet Union compared to the New Member States of the European Union (Berglof and Bolton, 2002). Results of privatization turned out to be disappointing in many cases (Estrin et al., 2009). The democratization process turned out to be short-lasting and less deep in most Former Soviet Union countries and is proving shaky even in New Member States (Bruszt et al., 2012). These surprises of transition led to lots of research. One of the conclusions of some of this research is that the differences in the quality of institutions explains a lot of the economic divergence between Central and Eastern Europe (Roland, 2000; Aslund and Djankov, 2014). Accession to the European Union played an important role in anchoring institutions in Central Europe and New Member States (Berglof and Roland, 1997).

In this article, I view the evolution of former socialist economies in China and Eastern Europe in a longer historical perspective. In doing so I do not want to focus on the effects of particular policies but focus instead only on the long run, low frequency processes that have been at work. In doing so, I propose a new interpretation of the evolution of post-communist systems in Central and Eastern Europe and China. Specifically, I want to see transition in Central and Eastern Europe less as a process of reform but more as a process of disintegration of the communist state apparatus. In contrast, I characterize China's evolution as the conscious replacement of central planning by the market economy to keep the communist party's control over political power. I will argue that this reinterpretation yields a better understanding of the evolution of central planning and the forces at work in transition processes. It also provides for a better understanding of the fundamental differences in the evolutions in Central and Eastern Europe on one hand, and in China on the other hand. As we will see, these new interpretations of transition have important implications.

In section 2, I explain the process of erosion of the state apparatus in Eastern Europe before transition. In contrast to most of the transition literature, I start with the socialist economy, not with the political overthrow of communist regimes. In section 3, I explain how transition unraveled in light of the collapse of the communist state. I also propose a new conceptualization of the post-communist state in Central and Eastern Europe. Section 4 turns to the evolution in China since the beginning of the reform process in 1976. Section 5 concludes.

2. The erosion of the communist state apparatus in Eastern Europe.

Most of the literature on transition in Central and Eastern Europe starts with the radical political changes in 1989 in Central Europe and in 1991 in the Former Soviet Union. This perspective is, in my view, too narrow. I argue that by integrating the evolution of central planning, one can better understand the forces at play in transition processes. This is important not only because it allows for a better understanding of what has been going on in transition countries, but knowledge about how central planning worked in practice has quasi-disappeared from the planet¹.

Under socialism, the communist party concentrated all political and economic power in its hands. While this gives the impression of overwhelming leverage and power in the hands of communist leaders, in the long run, this concentration of both political and economic power proved a toxic mix for communist Soviet leadership. To see this better, one needs to understand better some of the mechanisms of central planning.

Scholars who studied the reality of central planning for decades (see e.g. Grossman, 1963; Nove, 1979; Kornai, 1980) emphasized the informational overload facing central planners. In the theoretical debates of the first part of the century on the relative advantages of central planning versus the market, Hayek (1945) had in hindsight predicted that information overload would be the Achilles' heel of the centrally planned economy. Since the market mechanism was outlawed by the communist regime, coordination of economic activity and balancing of supplies and demands was left in practice to the central planning bureau. The main mechanism for this was the system of "material balances" for each good or category of good listing sources of supply in one column and sources of demand in the other column. We know that material balances were in general inconsistent (see e.g. Manove, 1971) as adjustments to the material balance for one particular good were not matched by adjustments to other material balances. For example, suppose that the material balance for glass had to be adjusted so as to increase its supply so as to match the sum of demands for glass. For plans to be consistent, increase in glass output should increase demand for sand and energy. The output plans for sand and energy by producers would often not be adjusted upward, which would create

¹ I was able to devote a chapter to it in my development undergraduate textbook (Roland, 2014).

shortage of sand and energy, making it difficult to meet planned quotas for glass output. Input-output tables, which would avoid these inconsistencies were not used in practice when computing plans, and when input-output tables were introduced, decades after the establishment of central planning, they were used only for very broad product categories, usually not more than 200 whereas the number of different products was around 12 million in the eighties. Since actual plans suffered from inconsistencies and since the market was not used as a coordinating device, it was left to the bureaucrats inside the planning apparatus to do the actual coordination, which involved mostly discretionary actions, changes in plans and reallocation of resources between enterprises and sectors². The burden of managing on a day to day basis an economy with no real balanced plans and without market mechanisms, became heavier as the economy grew more complex (more goods differentiation, more input complexity, more economic links, ...). The growing information overload for those responsible of running the economy resulted gradually in economic stagnation and rigidity (Roland, 1989, 1990). What is important for our purpose is that it also inevitably led to a gradual erosion of the communist power apparatus. Let us see why in more detail.

Central planning necessitated that orders be obeyed, at least not challenged. This was a fundamental need of central planning. Coordination of economics activity was already difficult enough from an informational point of view, but the role of the Center would amount to nothing if its orders were not obeyed. Moreover, since much of the coordination was on a day-to-day basis, it was important that the orders of the Center be obeyed swiftly, and without opposition. The organization of central planning was from that point of view comparable to that of an army where strict obedience and rapid implementation of orders are necessary (though not sufficient) for success. It is not the place here to go into detail into the reasons for the comparison between the organization of central planning and military organization, but there are many similarities, the economics of which has been explained in Weitzman's (1974) classical article. To give some basic intuition, since adjustments between supplies and demands were mainly done by planners (either at the Center or in economic ministries), failure to obey or delays in implementing orders would cause shortages which could spread very fast in the whole economy. This is not just a theoretical proposition, but a hard reality. Once the authority of central planners started eroding, centrally planned economies started to implode.

The erosion of the authority of central planners became, however, inevitable. For this authority to be legitimate, managers needed not only to fear the threat of punishment from the Center but they also needed to feel that the planning

² There was a whole literature on the mechanisms by which central planners actually reallocated resources to ensure coordination between supplies and demands (see e.g. Kornai, 1980, Powell, 1977; Birman, 1978; Roland, 1989). Given the absence of consistent plans, economists were trying to understand how an equilibrium between supplies and demands could be achieved in the absence of balanced plans or markets.

bureaucracy was able to solve the many shortage situations occurring. To maintain its authority, the Center had to be perceived as being in control, as having enough coordination capacity. Unfortunately, this was less and less the case as time passed. As stated above, plans were never balanced. In the early years of central planning, what mattered mostly was priority coordination of steel, coal and heavy industry. The Soviet economy was starting to industrialize and the capacity to allocate basic resources made it possible to generate high growth rates despite coordination problems. Campaign-style management, ideological enthusiasm, terror and *Stakhanovism* made things work and compensated for the lack of balanced plans. As the economy became more complex and as time went by, it became more and more difficult to substitute ideological mobilization and selfless but reckless overtime work for efficient coordination. What followed was cynicism with the system. This cynicism was shared by people all across the communist hierarchy, from top leaders to enterprise managers and ordinary workers. People were frustrated with a system that was able to send people into space but unable to produce quality television sets or cars.

In this context of increasing cynicism and erosion of authority of the Center, managers started to realize that their bargaining power was stronger than what they might have initially thought. Threats of punishment, which were very strong in the Stalinist era, stopped being credible after a while. Managers were indeed not responsible for the economic imbalances they were experiencing. Threats might incentivize them, but only to a limit because they could do little about their external circumstances. Punishing managers for not fulfilling plans by firing them or demoting them would backfire since these punishments represented disruptions to plan fulfillment. Indeed, economic ministries also had their plan quota to fulfill, which was the sum of all plans of enterprises under their supervision. Any disruption in an enterprise would not only hurt the manager of that enterprise, but also the economic ministers higher up in the planning hierarchy. Managers realized more and more over time that threats of punishment were less and less credible and that those higher up in the planning hierarchy were dependent on the performance of their enterprise. In other words, as the authority of central planners was gradually eroding, enterprise managers realized that they could be more assertive in bargaining with the Center.

How did this increase in the bargaining power of managers manifest itself? Managers tried first to bargain for lower plans. It is not just that lower plans were easier to fulfill. Too taut plans might be counterproductive for the central planners. There had always been a strong discontinuity in managerial bonuses, and the main financial bonus was the one they received for plan fulfillment. A too taut plan might be impossible to fulfill, and managers would therefore be discouraged from putting in effort. A somewhat less taut plan might have a higher probability of being fulfilled if managers put in the right amount of effort. Indeed, scholars of central planning found that there is an “optimal level of plan tautness” (see e.g. Hunter, 1961). Managers would thus try to convince planners that plans were too taut and that lower plans should be called for. Also, managers tried to bargain for higher supply

plans, because higher supply plans would make it easier to fulfill the plan. They also tried to bargain for more autonomy on wage-setting. Indeed, there was shortage on labor markets just as in other markets and managers complained that they could not hire enough people because wages were set rigidly at the central level, and they needed flexibility in setting wages to attract labor. Managers also tried to bargain for more tolerance towards the shadow economy. The aim was to grease the wheels of the planning system. If planned supplies could not be achieved, managers wanted to have the possibility of purchasing substitute goods in the shadow economy and not be punished.³

The more concessions central planners made to managers the more their authority eroded as they had less and less leverage over managers. Simultaneously, managers realized, as these concessions were made, that they could bargain for more. There was thus a dynamic of increased erosion of the authority of central planners and increased bargaining power of enterprise managers. This dynamic was well known to students of central planning, and it is surprising that the connection with transition processes was not made, as we will do below. One of the reasons is that while these processes were observed, their nature was mostly misinterpreted.

The central authority of planners had been eroding at different speeds in different countries. In countries where it had been eroding faster (this was the case of Hungary, Poland, Yugoslavia as well as the USSR under Gorbachev), this erosion of authority and the greater autonomy of managers was generally interpreted as partial reform towards the market economy, whereas it was in reality an increase in the bargaining power of managers towards the Center. As we will see below, this difference in interpretation matters for how we think about transition.

This variable speed in the erosion of the authority of the Center across countries is not surprising. In Central Europe, the communist regime, and the associated centrally planned economy, lacked legitimacy mostly from the start. This is because communist regimes were established there as the Soviet Army moved to defeat the Nazis and transformed countries of Central and Eastern Europe into satellite states. Popular revolts against the regime broke out in 1953 in East Germany and in 1956 in Hungary and Poland, and local populations generally saw the regime as that of the Russian invader. In the Soviet Union, the erosion of power took place gradually starting from the sixties. Growth started slowing down and complaints about the economic inefficiencies of the system had been piling up in newspapers and specialized journals since the late fifties. The so-called Kosygin reforms in 1965 were already a limited step to increase the autonomy of managers. They were mostly undone under Brezhnev when Kosygin was ousted, but the Brezhnev years (called years of stagnation) were years of disillusionment and loss of legitimacy of

³ This shadow economy was called the “grey economy” in contrast to the “black economy” (see e.g. Katselinboigen, 1978). The “grey economy” consisted in using illegal market transactions to help fulfill the plan, whereas the “black economy” was a completely different economy operating outside the planned economy.

the regime within the elite. Despite the invasion of Czechoslovakia and the sporadic repression against dissidents, there was a lack of appetite of the top Soviet leaders to use terror and threats of punishment to consolidate their power over the central planning apparatus. The result was cynicism and loss of legitimacy of the Center. What is important to note here is that the erosion of the authority of the Center on the planned economy also led to erosion of authority in the political sphere. Weakened economic authority would feed in weaker political authority and vice-versa.

The erosion of the power of the communist state apparatus in the economic sphere and the increase in the bargaining power of enterprise managers can be described in several steps.

The first step was the elimination of mandatory planning and its replacement with some form of non-binding plan. This happened in Yugoslavia in 1965, in Hungary in 1968 and in Poland in the early eighties. This is something that was desired by managers because, as seen above, managerial bonuses depended mostly on plan fulfillment. Ninety nine percent plan fulfillment instead of hundred percent would lead to a loss of bonus. Elimination of the mandatory plan quotas made life much easier for managers and eliminated a lot of the frenzy related to the need to achieve hundred percent plan fulfillment. This is something that bureaucrats in economic ministries could live with, as their own performance was a function of the sum of outputs of enterprises under their authority. Moreover, plan fulfillment bonuses were two-sided. They were a good instrument to coax managers into squeezing some more output when plan fulfillment was within reach, but managers were also indifferent between ninety nine percent plan fulfillment and ninety five percent plan fulfillment whereas the economic ministries were not. Overall, the elimination of mandatory plan quotas was a measure mostly desired by enterprise managers.

The second step in the increase of the bargaining power of managers was to increase their decision-making autonomy in particular on prices and wages. We already explained that managers wanted decision-making power over wages so as to be able to pay a higher wage to attract more workers in a context of generalized shortages, in particular shortages of labor. Increased autonomy over prices had the advantage of driving up profits, or of compensating for the increases in wages. It is important to note here that higher wages led to increased shortages. Indeed prices were mostly fixed in the planned economy and higher wages led to an increased demand for consumption goods, which, given the total lack of supply elasticity, led to increased shortages of consumer goods. In countries where prices remained sufficiently rigid, this led to goods disappearing from the shelves, such as during perestroika in the late eighties under Gorbachev. In countries where there were sufficiently many prices that were partly liberalized, this led to price inflation, as was the case in Yugoslavia and Hungary. In any case, increased autonomy of managers led to generalized wage increases, which led to the so-called monetary overhang and macro-economic imbalances that had to be dealt with early in the

transition. Note that managers had soft budget constraints in the socialist economy (Kornai, 1980). This means that they did not feel constrained financially when increasing wages. The drive to increase output remained the priority in centrally planned economies, even after mandatory planning had been abolished, which meant that there were no financial constraints to output increases in state-owned enterprises (SOEs).

The third and final step in the erosion of the communist economic apparatus was the privatization of state assets to managers. This happened as communist regimes were on the brink of collapsing or already collapsing. This privatization to managers happened in many different ways: via spontaneous privatization (asset-grabbing by managers), management buy-out schemes or mass privatization programs like in Russia where assets ended up in the hands of managers. There were many academic debates about the most efficient forms of privatization (see e.g. Bolton and Roland, 1992; Boyko et al. 1997; Frydman et al. , 1999), but the reality in most countries was that managers were seizing ownership of the assets that they controlled under central planning. This was clearly not optimal from an economic point of view as managers who had developed skills related to central planning would not necessarily have the skills to run an enterprise under the market economy. This pressure for privatization to managers was already present in the last years of communist regimes whose leaders were too weak to react or sufficiently corrupt to participate in these schemes. Once communist regimes were overthrown, this pressure became even larger, and politicians who were opposed to privatization to managers, be it for reasons of efficiency or equity, were never powerful enough to resist these pressures.

Note finally that outside the economy, under the communist state, there was also a gradual reduction of power of the state apparatus vis-à-vis civil society. There was a lot of bargaining for parts of civil society to gain partial spheres of autonomy, where the Communist Party would not interfere, especially in the artistic domain. Citizens also managed in the last years of communism to set up private enterprises, usually operating under illegal circumstances, but left alone by the communist regime.

3. Transition processes and the nature of the post-communist state.

In Central and Eastern Europe, transition started with political overthrow of the elite in power after a critical threshold of weakness of the communist state had been reached. It started with partially free elections in Poland that ousted the communists, continued with East Germans fleeing to Hungary to cross the unguarded border with Austria, followed by the Fall of the Berlin wall and the velvet revolution in Czechoslovakia. Within a few months at the end of 1989, all satellite regimes of the Soviet Union had been overthrown. After the failed August 1991 putsch in the Soviet Union, the communist party was outlawed and former Soviet Republics became independent, triggering there also radical political change.

Transition thus started in Central and Eastern Europe with the collapse of the existing communist regimes. This stands in stark contrast to the Chinese transition, which started as an economic strategy to strengthen the monopoly power of the Chinese Communist Party (CCP) after the pragmatic realization that central planning was less effective than the market economy.

3.1. Collapse after years of erosion of communist power.

When thinking back about the collapse of communist regimes in Central and Eastern Europe, people often have in mind the East German protests which quickly spread everywhere, eventually leading to the Fall of the Berlin Wall. While these protests obviously played a role in triggering the end of communism, one should not underestimate the role played by the internal erosion of the economic system. The communist leaders in Central and Eastern Europe had come to a point where they completely lacked authority, were not able to get obeyed and were hardly able to continue playing a role in coordinating the economy. Eventually, they just gave up as they felt that they could not continue to manage the system.

The fact that the regime change was mainly due to collapse is important to understand what followed. If the regime change had been due only to push from below, which was present in some countries like Poland, Hungary or Czechoslovakia or the Baltic countries, but much less so in the Former Soviet Union, things might have been different (we discuss below the impact of civil society engagement on governance issues in transition countries). However, internal collapse of the communist regimes from the top created a vacuum. This vacuum opened up space for various networks, within or outside the elite, to grab pieces of power of the defunct communist state and use them for their private benefit. This vacuum thus led to transform the communist state apparatus into what can be called a *kleptocratic* state. Different networks played different strategies to grab pieces of power, but they had one thing in common: steal as much money as possible.

We can identify two main strategies of kleptocratic networks. A first one involves grabbing directly power positions within the state apparatus to enrich oneself either as a politician or as a high level administrator. Power positions were used directly for personal enrichment in a variety of ways: demanding or receiving bribes, predatory behavior towards enterprises or sources of wealth and money, asset-stripping for personal enrichment. The second type of strategy, used mostly by non politicians, involved the use of connections in the state apparatus to grab assets and economic power by influencing privatization laws or deals, obtaining monopoly privileges, influencing procurement allocations or contracts, etc....

Privatization of SOEs was obviously the biggest opportunity to influence the allocation of assets. This was a one-shot, once in a lifetime opportunity, to steal and accumulate wealth in a very fast way. This happened in different ways. A first was to use political influence to establish privatization policies that maximized the rents

for those receiving control over assets (via free distribution of the assets for example). This strategy was used by insiders of the state apparatus as well as by would-be oligarchs with political connections. Apart from directly influencing privatization policies, a second way was to influence the administrative process via corruption to divert outcomes in one's favor. This was sometimes more discreet but not less efficient. Many people got rich very fast through privatization policies. The immense wealth of many Russian oligarchs cannot be explained differently, but similar processes were at play in other countries.

The reciprocal consolidation of economic and political power has been a constant in the creation of the post-communist state. People used the market power received from *privatization policies* or *regulatory capture* or any other influence activity to increase not only one's wealth, but one's influence inside the state apparatus, which made it easier to further enrich oneself.

3.2. Oligarchs and the plunder of state assets.

There are many examples corroborating the nature of the post-communist state as a terrain for kleptocratic strategies of different networks.

Ukraine is the perfect example of this since its independence. The last 25 years, the Ukrainian state has been a battlefield for the various oligarchic networks, each controlling part of the state apparatus. Rinat Akhmetov was a loan shark and was involved in protection rackets already under the Soviet Union. He got rich fast by grabbing control over the Donbas coal mines in Eastern Ukraine and subsequently becoming the most powerful man in the Donetsk area. He was very influential under Yanukovich, but has lost a lot of his influence under Poroshenko. Victor Pinchuk was the son in law of President Leonid Kuchma and became rich via this connection. He has sided with the West, is friend with the Clintons and organizes every year the Yalta European Strategy meeting that takes place in Kyiv since the invasion of Crimea. Since Trump came to power, he is trying to build bridges to Russia. Ihor Kolomoisky started his career in the Dniepropetrovsk area and also became rich under Kuchma. He has, among others, important stakes in the airline business. He supported the Orange Revolution and the Maidan, but came into conflict with President Poroshenko who removed him as governor of Dniepropetrovsk. Dmytro Firtash became quickly very rich in the gas business and acquired important stakes in other sectors. He fled to Austria in 2014 as he faced extradition charges, first to the U.S. and then to Spain, both including corruption charges. Yulya Tymoshenko is mainly a politician. She became prime minister after the Orange Revolution and was jailed when Yanukovich became president. She is still active in politics as head of party Baktyvshchina. She made money with her husband in energy brokerage and was jailed on accusations of corruption in that context. Poroshenko made a career as a corporate raider (see below), and like Tymoshenko was always on the "Western" side in Ukrainian politics.

All these people, like oligarchs in Russia and other countries, became immensely wealthy in a matter of a few years. This did not happen via capital accumulation but via direct or indirect power positions in the state apparatus. It is useful to know that out of eleven major privatizations that took place when Kuchma was president, nearly all were rigged towards particular oligarchs (Abrams, 2014).

Many of the changes taking place in the last 15 years in Ukraine have affected power shifts between various groups of oligarchs inside the Ukrainian state apparatus. Thus, after the Orange Revolution, more pro-Western oligarchs seemed to gain the upper hand like Tymoshenko, Kolomoisky and Poroshenko. However, when Yanukovich became president, he favored more oligarchs from Eastern Ukraine such as Akhmetov to the detriment of Tymoshenko. Since the Euromaidan revolution in 2014, there has again been a massive shift of power between different groups of oligarchs, benefiting mostly Poroshenko to the detriment of several of his rivals. Nevertheless, as we will explain below, Ukraine has also become a battleground for the fight against corruption and oligarchic power, and many young people have now been fighting for years against the ambient corruption inside the state apparatus that has hardly changed since the Euromaidan.

Similar stories about the emergence of networks of oligarchs and power shifts between various groups can also be told for other countries. In Russia, massive wealth transfers in favor of oligarchs took place under mass privatization and the “loans for shares” scheme whereby oligarchs agreed to lend money to the Russian government in exchange for shares in state-owned companies at a value largely exceeding the sums lent. The default on Russian bonds allowed these shareholders to sell those shares at a large profit (see Treisman, 2010 on this). Major shifts of power between various networks took place as Putin replaced Yeltsin as president of the Russian Federation. Many oligarchs who thrived under Yeltsin were forced to leave the country (Berezovsky, Gusinsky and others), others lost control over major assets or were even sent to jail, such as Mikhail Khodorkovsky. Putin’s reconstruction of the Russian state apparatus using his network of former KGB agents led to the rise of the so-called “siloviki”, a new group of oligarchs striving under Putin.

Another characteristic of this period is the generalization of corporate raiding, a phenomenon we were reminded of with Russian invasion of Crimea. Corporate raiding is nothing else than the violent takeover of assets by criminal and armed gangs who seize control over industrial assets and valuable property by chasing the owners under the threat of using armed weapons against them.

In the Czech Republic and Slovakia, members of the former Nomenklatura benefited from privatization along with adventurers. The Czech voucher privatization program benefited state-owned banks who ended up owners of their shares and of other privatized assets. Adventurers like Kozeny bought vouchers from Czech citizens to acquire shares that were hundred times more valuable. Corruption in the judiciary and in government administration spread to cover up

various forms of predatory behavior or abuses of power with the purpose of enrichment. In Slovakia, corrupt privatizations took place when Meciar was president. Corporate raising was quite prevalent when Dzurinda (1998-2006) and Fico (2006-2010 and 2012-) were Prime Ministers.

In Poland, one observed the siphoning of bank assets by former Nomenklatura insiders. The so-called Foreign Trade Centers played an important role in the siphoning of assets. Under communism, they served as centers to exchange foreign currency since the zloty was inconvertible. This involved buying goods from SOEs at cheap prices and selling them against hard currency. When transition started, many of those who had control over these centers used them to line money in their own pockets rather than filling state coffers. Other forms of siphoning were the non reimbursement of loans to state-owned banks or forms of “tunneling”, i.e. using positions in SOEs to sell at cheap prices assets and goods to firms one controlled oneself. These techniques were generally prevalent in all transition countries. Corporate raiding was also quite prevalent in Poland.

Overall, one could write books and books on corruption and stealing using positions in the state apparatus in transition economies.

3.3. The nature of the post-communist State.

Competition between different networks (Nomenklatura insiders, outsiders looking for fast enrichment, networks from former secret police, criminal networks taking advantage of collapse of communist state) implies lawlessness, collaboration with organized crime, abuse of power positions within the State (political, judicial, administrative positions, positions in SOEs and state-owned banks), threats and use of violence. Competition leads to conflicts and deal-making in the shadow of the law. So, both the actions of networks as well as the competition between them lead to bad quality institutions.

Predatory institutions are thus directly a consequence of the collapse of the communist state and of competition among former Nomenklatura networks to grab pieces of power within the state apparatus. In this situation, there is no internal incentive to introduce the rule of law. This point was already made many years ago by Sonin (2003).

The implosion of communism thus explains the organization of the post-communist state and its main features: 1) the prevalence of influence networks and clans, 2) generalized corruption and the use of direct or indirect power positions for enrichment and siphoning away of resources. The post-communist state is best characterized as a kleptocratic state where state power is used like an ATM machine. This use of the state like an ATM machine is much more severe than the soft budget constraint phenomenon that Kornai had identified under socialism and in early transition. People with positions in the state apparatus siphon away

millions of dollars that they shore in safe havens while the economy of their country deteriorates.

The competition between networks implies political instability as various networks jockey to improve their position and to fight off rival networks. Since the stakes of this competition are high, lawlessness and criminal actions will obviously characterize this competition. This instability will be stronger when networks are roughly of equal size, and the competition fiercer, but it will be smaller if one network manages to dominate others. Ultimately, this is likely to be the outcome. This could be an interpretation of the situation in Russia where Putin's network has managed to crush most other networks.

The relation between the kleptocratic state and democracy is ambiguous. Repression is generally not in the interest of the oligarchs unless their interests are at stake or threatened. Kleptocracy is incompatible with the rule of law, but may coexist with corrupt and hollowed out forms of democracy that are not necessarily highly repressive. Two variables appear important here. First, if the state's power is fragmented between various networks, there will be less investment in repression, because various groups want to free ride on each other. If one network has consolidated relative monopoly control over the state apparatus, it is more likely to repress if it senses threats to its power. Second, it depends on how active or passive the population is. If civil society is passive, then there is less need for repression as there will be little opposition to generalized corruption, only widespread cynicism and passivity. If on the other hand, civil society is active enough, then repression is more likely. A strong civil society may on the other hand be victorious in its fight against corrupt interests inside the state apparatus.

3.4 Countervailing effects to the kleptocratic state.

We now discuss three possible countervailing effects to the kleptocratic state: 1) the strength of civil society, 2) culture, 3) accession to the European Union.

3.4.1 First countervailing effect: civil society

Civil society plays a critical role as a countervailing effect to the kleptocratic features of the post-communist state. This happens in two ways.

First of all, levels of civil society engagement affected the very nature of political institutions chosen. In Bruszt et al. (2012), we showed that levels and maturity of dissident activities in the eighties before the collapse of communism affected the types of political institutions that were chosen in transition countries. Countries like Poland, Czechoslovakia and Baltic countries had higher level and stronger maturity of dissident activity, which affected initial political institutions. In effect, dissident movements had been rallying for years against communist regimes. When the latter became close to collapsing, roundtable negotiations were organized with representatives of dissident movements in order to discuss post-communist

political institutions. Those who had fought for democracy for a very long time made sure to shape institutions in the right way: lower concentration of power in the hands of the executive, more separation of powers and more inclusive institutions. In contrast, in most of the Former Soviet Union where the collapse of communism happened after the failed August 1991 putsch against Gorbachev, the fall of the regime did not happen under pressure from the street but from the top's failure to hold power. People were stunned in Russia to discover overnight that the Communist Party that had been in power for more than 70 years, and had exercised ruthless and totalitarian power in a way unprecedented in history, was outlawed overnight. Because civil society was not very prepared for this turn of events, political entrepreneurs from within the former Nomenklatura were able to shape institutions towards strong presidential executive powers and low judicial independence, in a way that would favor them without creating too much accountability towards citizens, and instead creating lots of instruments for predatory behavior.

Second, a low level of civil society leaves the transformation of the post-communist state unchecked, leaving room for unbridled corruption and enrichment of elite networks. The population falls then victim to the exactions of the kleptocratic state, but remains passive and fatalistic. This is unfortunately still the case for most former Soviet republics. There are, however, exceptions.

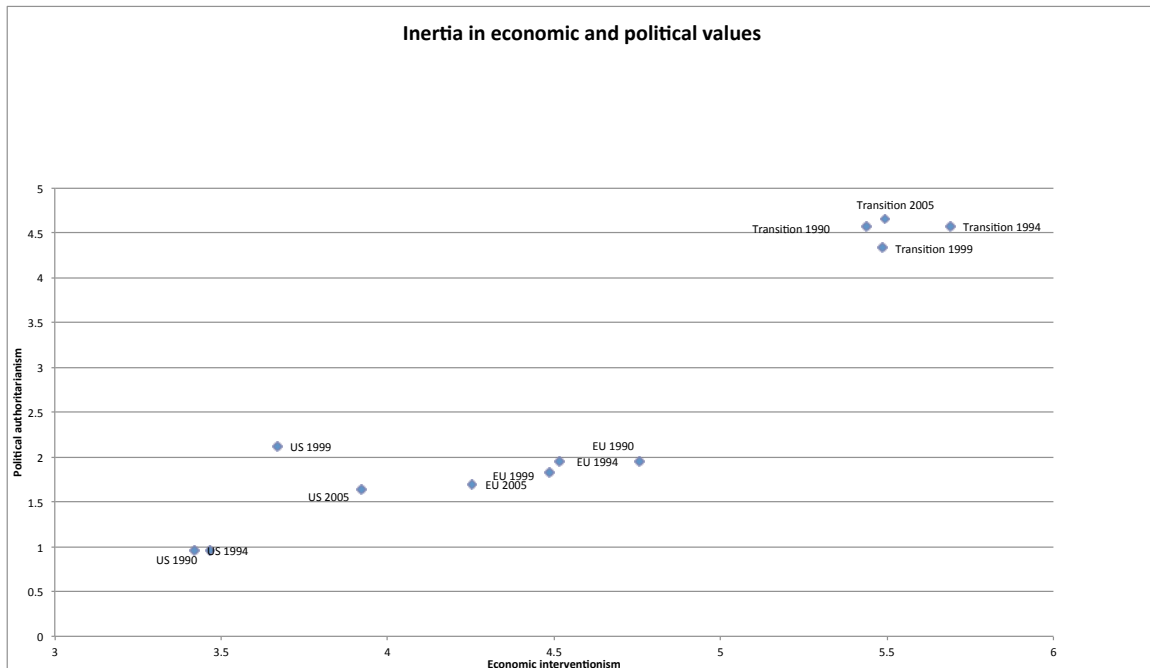
The Rose Revolution in Georgia led to a very radical eradication of corruption in the Georgian state (World Bank, 2014), a country that had developed an unprecedented level of corruption both before and after the collapse of communism, and was ranking together with the most corrupt countries in the world, like Angola, Cameroon, Nigeria and Haiti. President Saakashvili (2008-2013) who led this reform push was ousted from power in 2013, but the reforms he introduced had a staying power.

The Euromaidan revolution of 2014 in Ukraine was motivated in large part by the ambient corruption in Ukraine since its independence in 1991, a strong illustration of the kleptocratic state we are describing in this article. While the Euromaidan has led to important changes in Ukraine, in the economic and political sphere, as well as in the state institutions, corruption has remained mostly unscathed, and proved much more difficult to eradicate than in Georgia. Fortunately, civil society mobilization remains particularly strong, much stronger than after the Orange revolution, and this may bode well for the transformation and modernization of the Ukrainian state. Interestingly, the war instigated by Putin in Eastern Ukraine, whose purpose was to fight the Euromaidan, has had the effect of keeping the mobilization much alive. The frequent burial ceremonies, in Kyiv and elsewhere, for the soldiers killed on the Eastern front constantly remind people that they fought to become a normal European state. This is an unintended consequence that Putin probably did not have in mind.

3.4.2. Second Countervailing effect: Culture

While civil society engagement is an important factor shaping the trajectory of the post-communist state, culture is also very important. When talking about culture, economists usually mean the sets of values and beliefs inside society. Values about society are a potentially strong countervailing force to the kleptocratic state. People will tend to revolt against political institutions that do not correspond to their values. Unfortunately, cultural values in former transition countries, tend to be more authoritarian than in Western European countries or in the US. Values are more nationalistic, favorable to discrimination against women, homosexuals, ethnic minorities and foreigners.

FIGURE 1



Source: Roland (2012)

Figure 1, taken from Roland (2012), puts together several country answers to various questions from the World Values Survey for different years. The horizontal axis measures preference for economic interventionism while the vertical axis measures preferences for political authoritarianism. As one sees, Figure 1 confirms the fact that populations in transition countries have stronger preferences for political authoritarianism and economic interventionism. These values have hardly changed since the beginning of transition, and they are less different between New Member States and Former Soviet Union countries compared to the difference between transition countries and Western European countries. This inertia is very surprising given the major institutional changes that have been taking place in these countries in the last decades.

3.4.3. Third Countervailing effect: 3. EU Accession

EU accession provided an external check on the formation of kleptocratic states in transition countries. The incentives to enter the European Union dampened kleptocratic behavior compared to non accession members (see Roland and Verdier, 2003, Berglof and Roland, 1997). Even if the rules of the *acquis communautaire* can be criticized in many ways, the promise of accession created an institutional anchor for accession countries. The adoption of EU legislation took away power from rent-seekers wanting to milk the state for their own benefit. The expectation of accession also proved an anchor on behavioral patterns, indicating that the rewards to rent-seeking would decline to the EU level, encouraging agents to engage in more productive activities instead. A similar incentive effect was present for countries wanting to enter the monetary Union. Countries like Belgium and Italy then made great efforts to reduce their persistent budgetary deficits.

As with European Monetary Union, the accession incentive became much weaker once countries had become members of the EU. The EU commission, which does not have anything like a federal state administration, is mostly a body good at preparing legislation. It needs to rely on member states for enforcement of EU legislation. Punishments for misbehavior of member states are often not credible. Once the New Member states had been admitted to the EU, it became much more difficult to discipline them. With the New Member States, we have seen this in recent years with the autocratic drift in Hungary and Poland being virtually unchecked. This does not mean that the EU is useless in fending off tendencies towards the kleptocratic state. It still provides institutional support. A good recent example is Romania. With the help of the EU, a National Anti-Corruption Bureau (DNA) was set up with Laura Codruta Kövesi as chief Prosecutor. The DNA has been very active, including prosecuting high level politicians. The DNA informed the public early 2017 of the government's plan to decriminalize bribes below a certain amount, leading to days of massive protest in Bucharest and the rest of the country until the measure was withdrawn. The European Commission has played an active role in helping Romania set up its anti-corruption institutions, and this has galvanized people's anti-corruption attitude.

3.5 Some implications of this reconceptualization of transition.

We have proposed a reconceptualization of transition processes in former centrally planned economies. Transition processes are not the result of exogenous regime change, but instead the result of a gradual erosion of the communist state apparatus and a concomitant strengthening of the bargaining power of managers of SOEs towards the center. This process caused by the inefficiencies of central planning led eventually to a collapse of the communist regime and a fight between various networks to grab pieces of power of the former communist state, and to use these positions of power for personal enrichment.

This reconceptualization has various implications. We list below the two most important ones.

A first implication is to shed new light on the nature of the post-communist state and the way in which it emerged. The post-communist state is not simply the result of “not introducing the right institutions”, the current consensus view on why transition led to such bad economic performance in most of the Former Soviet Union. In light of our analysis, these “bad institutions” are the direct consequence of the erosion and collapse of the communist state apparatus, which has been deeply transformed from communist absolute power monopoly to rival kleptocratic turfs of variable stability shared by various networks. This implication yields a better understanding, in my view, of the processes we have observed in transition economies since the fall of the Berlin wall.

A second implication is that reforming the post-communist state with failed institutions is of a different nature than reforming the communist state under democratic and market transition. Transition’s main challenge was to introduce the market economy. The current challenge is ousting corrupt vested interests that have created highly profitable niches within the state apparatus. This requires in my view a deeper and more long term transformation if it is to be successful.

It is in my view not very helpful to explain bad economic performance, corruption, etc.. as a result of “unfinished transition”, the preferred view inside international organizations. If one considers, as I do, that transition is mostly about transitioning away from central planning, then that transition has taken place and was finished by the mid 1990s. The new challenges in the whole region are about how to transform post-communist States from kleptocratic States into “normal democracies”. As stated, countries with a more active civil society, with cultural values that favor citizen rights, transparency and accountability and countries that had to follow the admission process in the European Union are closer to that objective. Nevertheless, since all countries went through the same process of erosion of the communist state, corruption and oligarchic networks tend to be present in all of them. The fight of Ukrainian youth to root out corruption, and similar movements in Russia and Belarus, are key for the future of those countries, and for whether they can become successful economies and polities.

4. The evolution of the Chinese system

How does the evolution of China fit in the picture we outlined in the previous sections? The evolution of central planning in Central and Eastern Europe helps better understand China’s evolution even though it went in very different directions.

4.1. The big Chinese innovation: a market economy under communist government.

In the light of stagnation of the USSR in the seventies and the chaotic (and lunatic) Maoist management of the economy since 1958, Deng Xiaoping thought that the best bet to consolidate the power of the CCP was to introduce the market economy in continental China, following the examples of Taiwan, Hong Kong and Singapore. Deng was pragmatic. He had noticed the economic success of Taiwan, Hong Kong and Singapore (called the Asian tigers at the time) and said that if the Communist Party was not able to deliver growth like in those countries, they would irremediably lose power. This was quite prophetic. In the late seventies, it was not clear at all that the Soviet system would collapse and that communist regimes would disappear in Central and Eastern Europe. Many of Deng's colleagues wished a return to the central planning system of the fifties. This seemed like a safer bet and was advocated by Party elders like Chen Yun, Deng's main opponent when it came to market reforms. The compromise they agreed on was to experiment with decollectivization in the countryside and to incentivize peasants via the "Household responsibility system": Maoist communes (large socialist cooperatives regrouping several villages) were disbanded and households received land for a 15 year lease, were obliged to deliver a fixed quota of grain to the state at a fixed price, but were allowed to freely produce and sell at free prices on markets any additional output. This proved to be phenomenally successful and created momentum for further reform leading to China's growth miracle (on the political economy of reform momentum in China, see Dewatripont and Roland, 2005, Xie and Xie, 2017).

Deng eventually used the power of the CCP to unleash market forces in China relying mainly on two elements: government decentralization and yardstick competition (meritocracy) (see Xu, 2013 for the consensus view among researchers on the reasons behind China's success). Contrary to superficial reports, China's economic success was not due to the State withdrawing from the economy, but was due to the CCP using all possible instruments at its disposal to achieve high rates of economic growth. Not surprisingly, this process eventually reinforced the power of CCP in all spheres (military, education, press,...) instead of decreasing it, which had been Deng's avowed goal all along. Private entrepreneurs can since 2001 become CCP members, which can be seen as a way for the CCP to keep control over the private sector.

The initial thinking on the link between economic and political reform in China was that political reform would sooner or later follow economic reform. After all, the Soviet Union did have a political transition shortly before economic transition. The order in China seemed to be different, but most observers thought that economic reforms would lead to gradual political liberalization. In hindsight, that view was deeply mistaken. If anything, the opposite happened. **The transition to the market economy in China was decided with the goal of preserving and consolidating the power of the CCP.** This is no surprise, as Chinese communist leaders always stated that objective. So far, this has been an unmitigated success! China's economy has been transformed in 40 years beyond recognition, and this has

changed the world economy, and will influence the world's political arena in the twenty first century.

China's current system is one of **CCP power over a market economy**. Growth objectives were pursued using existing CCP institutions. CCP power has not faded with progress of market economy. On the contrary! Thanks to China's economic miracle of the last decades, the CCP has probably become the most powerful organization in all of world history.

The reinforcement of Communist State power has led to a state structure that is very different from that in Eastern Europe, even in the more and more numerous non democratic states. This state structure is unique, and is a combination of China's imperial state of the past and a very modern version of Leninism. The Communist Party stays very united and controls all the power levels. The Leninist principle of democratic centralism keeps the party united, as it forbids the formation of political fractions within the CCP. Fractionism is a major sin for Leninists. CCP members are officially allowed to express their opinion only in their own party unit. They are certainly not allowed to organize meetings outside the CCP's organizational structure. The CCP is present everywhere in Chinese society, not only inside the state apparatus, but also in private enterprises, sports clubs, apartment buildings, etc.. The CCP is very much present, albeit in a more secret form, in Hong Kong and Taiwan that it plans to take over in due time. The power of the CCP thus exceeds any governmental structure that we can think of. The state is also able to impose hard budget constraints on enterprises in a way that was not possible in Eastern Europe. Because the CCP exercises power by being everywhere in society, it is also in my view of a less expansionist nature, since it would be a very costly form of expansionism, requiring the CCP to span its fine network over a whole territory. China is already a continent. Communist leaders have openly stated that they want to take over Taiwan after Hong Kong, but for the foreseeable future that is as far as their expansionism goes.

If the CCP has never been more powerful than it is now, why is there more and more censorship and restriction of freedoms under Xi Jinping? Autocracies function very differently from democracies. In a democracy, freedom of speech and freedom in general do not threaten elected leaders. They can be insulted, jeered and mocked, but this does not threaten their power, as they have been elected in contested elections. The mere fact that they were elected implies that they have a power base. Taking away freedoms from citizens would be a sure way to lose votes and political power. In an autocracy, leaders are not elected by universal suffrage, and they cannot count on such visible and official signs of public support as an election. Power inside an autocracy is usually lost to rivals inside the power structure. Autocratic leaders who are perceived as weak are more likely to be challenged by rivals. Therefore, they need to signal strength to deter potential challengers. An autocratic leader can thus not leave any criticism of his rule unchallenged, even if that criticism does not directly represent a threat to his power. This is why absence

of democratic selection of leaders under autocracy always goes hand in hand with repression, censorship and restriction of freedoms.

4.2. The challenges of the market economy to communist power.

Even though Deng Xiaoping's gamble to introduce a market economy under the leadership of the Communist Party represents a major historical innovation, and even though the market economy proved to be hugely successful in China, this does not mean that communist leadership over a market economy does not create specific challenges.

4.2.1. The challenge of an obsolete ideology

A first challenge is related to ideology. Communist ideology is opposed to the market economy and to capitalism. Communist ideology claims that socialism should replace capitalism and give workers a higher welfare level. The introduction of the market economy creates a huge tension between the economic system established under Deng and communist ideology. Facts show that people are on average much better off under the market economy than under the decades of socialist economy. In a nutshell, the success of the market economy makes communist ideology obsolete. This is even more true given the collapse of central planning in Central and Eastern Europe. Only North Korea can claim to have a socialist economy, and it is one of the poorest countries on the planet, while South Korea has become an advanced market economy. So, how serious is the challenge of defending an obsolete ideology to the Chinese communist leaders?

This might seem to be an enormous challenge. One can, however, come up with arguments showing that this challenge is not that big. A useful paper to understand this is Haifeng Huang's (2015) "Propaganda as Signalling" paper. The main idea of that paper, which is very much rooted in governing styles throughout Chinese history, is that the content of the propaganda may matter less than its role as a way to signal loyalty to leaders.

To illustrate the idea, it is useful to recall a particular episode from the Qin dynasty. He is said to have brought a deer to the Imperial Court and in front of the whole court said: "This is a horse". Some in the court contradicted him, while others said: "Yes, this is a horse". Zhao Gao had the first group executed. The adherence to a blatantly false assertion served as a signal of loyalty. Communist ideology plays a similar role in contemporary China. Most people know it is an obsolete ideology, but those in positions of power keep repeating the ideological slogans of the day to signal their loyalty. Such a form of signaling may appear shocking to Western readers, but it is easy to cite a number of falsehoods other than communist ideology that people adhere to, whether in the religious or the political sphere. The spread of fake news and open lying by President Trump shocks many while cementing ingroup loyalties among his core group of supporters. Wu (2015) showed in the

context of Chinese history how Confucianist etiquette was not only a signal of loyalty, but also was a way of minimizing open challenges to the Emperor.

There is nevertheless a major weakness to the persistence of the use of communist ideology in modern China. Ideology cannot be used by leaders as a way to enhance their legitimacy. This leaves them mostly with exercise of power and terror to not appear weak. In the long run, the use of an obsolete ideology by communist leaders will prove a major weakness.

4.2.2. The challenge of corruption.

A second challenge is that of corruption within the CCP. Some people were surprised by the anti-corruption campaign started by Xi Jinping at the start of his leadership. Corruption has, however, in recent decades made major inroads within the party. It is a major challenge for the CCP as it can strongly erode its legitimacy but also the whole functioning of the state apparatus and law enforcement. The full scale of corruption in China is not clear, but all the casual evidence from Chinese news sources tends to show that it is a major issue forming an existential threat to the power of the CCP.

Corruption in China has increased a lot in recent decades. It has reached the point where officials purchase government and party positions for money, instead of being selected for promotion based on merit. Promotion has usually been seen as the biggest incentive for party cadres and government officials. This is the reward that has been sought for promoting higher growth rates than in other places. Officials who consider that they have lower chances of promotion may be more tempted to take bribes (see Persson and Zhuravskaya (2015) on the incentives of different types of bureaucrats). Corruption has very strong effects in terms of eroding the legitimacy of the CCP. Not only does it erode the legitimacy of the CCP among the population, but it also erodes the power of the Party leaders to give orders and get obeyed. Indeed, once corruption chains form, they are very collusive and threaten the authority of Party leaders because members of a corruption chain will tend to be more loyal to members of that chain. Once a corruption chain is big enough, it can even threaten to overthrow the incumbent leadership.

Another development related to the market economy that threatens the control of the CCP over Chinese society is the development of the private sector. As the private sector gets larger, private wealth accumulates allowing private business networks to act independently from the CCP, potentially even using this wealth as leverage on the party. So far, the answer of the CCP to the challenge of the growth of the private sector has been twofold. A first response has been to strengthen party units inside the private sector. The Party's leading role has no boundaries inside Chinese society so if the party secretary in a private enterprise gives suggestions to the business owner, the latter will see these as orders. This means that in China the boundaries between state sector and private sector are not as clear cut as in other countries. The CCP has thus a direct influence over the private sector. The second

response has been to coopt successful entrepreneurs in the CCP. This means that the party secretary inside a private enterprise is often the business owner. This gives even more control to the CCP inside the private sector. The strategy of coopting the private sector has been developed by Jiang Zemin when he was Party Secretary. Xi Jinping is less favorable to that strategy and wants to set a limit to the size of the private sector by keeping the size of the state sector large enough.

The CCP has a genuine interest in fighting corruption since it threatens its control over society and erodes its legitimacy and authority, as explained above (see Lu and Lorentzen, 2016 on the actual networks of corruption and the patterns of punishment). Nevertheless, the market economy brings strong tensions in a society controlled by the CCP. On one hand, communist leaders at different levels of the hierarchy are asked to promote economic growth. On the other hand, they are required to behave ascetically. In a nutshell, they are asked to behave like communist monks handling a large wealth-making machine. This is not impossible. Parts of the Catholic Church, the Greek Orthodox Church, Muslim or Bhuddist communities behave that way. Nevertheless, the stronger the requirements on ascetism, the stronger will be the temptation to break the rules and to use one's political power for personal enrichment. The emergence of corruption seems difficult to stop if party cadres and government officials are not given sufficient official and legal economic incentive payments. As long as these incentives are legal and transparent, this can reduce the temptation for corruption. So far, the Xi Jinping leadership seems not to have chosen that route, but instead has decided not only to crack down on corruption, but also to take away many of the perks of office of communist leaders (banquets, service cars, size of offices and dwellings, travel facilities, etc..) and impose harsher conditions on their lifestyle, in a way that is a scary reminder of Maoist times. These measures are undoubtedly likely to dull incentives to take initiatives to increase economic growth. The non transparent cracking down on officials is also likely to paralyze decision-making of communist cadres, possibly costing the Chinese economy several percentage points of growth per year.

4.3. The stability of the Chinese Political System.

Despite the tensions inherent to having a market economy develop under the leadership and control of the Communist Party, one should not underestimate the stability of the Chinese political system.

The main tasks of the power structure are not challenged. Finer (1997) lists the following three main problems every type of political system must solve: 1) the *succession problem* of political leaders, i.e. how a leader is chosen to succeed the previous one, 2) the *informational problem*, i.e. how do leaders receive accurate information from their administration when many of their subordinates have an incentive to distort or hide information; 3) generating tax revenues. The Chinese political system had found ways to solve these major systems in a rather efficient way.

The succession problem is a fundamental one in all political regimes. In a democracy, this is solved via elections, but in autocracies every succession can lead to a major political crisis unless there are well accepted rule of succession. In China, one can claim this is the case. The most important rule is the mandatory retirement at age 65 for members of the Central Committee and 68 is the maximum age for nomination to the Standing Committee of the Politburo, the real power center in China. This retirement rule creates automatic turnover. The advantage is that less competent leaders do not stay too long in power. The disadvantage is that very talented leaders have to retire sooner than might be good for the interest of the country. The retirement rule also reduces the number of candidates for a top position in China. Indeed, it is rare to be appointed to the Central Committee before the age of 50. The age interval between 50 and 68 reduced the number of candidates for top jobs. Another rule that has mostly been tacit, is that the current secretary general chooses not his successor, but his successor's successor. Thus, Hu Jintao is said to have been selected by Deng, whereas Jiang Zemin is said to have chosen Xi as Hu's successor, and Hu Chunhua, party secretary of Guangdong province, is said to be the successor of Xi Jinping chosen by Hu Jintao. The big problem in China is: how much commitment is there to the succession rules? There is much speculation that Xi Jinping may use the powers he has concentrated to change it.

The informational problem is an important one in China. Given that it is an autocracy, the party controls means of information, which means that there are hardly any major sources of information generated outside the CCP's propaganda machine. Despite the troubling recent appearance of fake news in advanced democracies, many of which are generated by Russia's autocratic regime, independent media remain a reliable source of information, both for the general public and for political leaders. In China, there are no independent media. Top party leaders have generally always relied mostly on vertical channels of information created and maintained by the Party. Indeed, at all levels of the Party, units constantly send reports above keeping them relatively well-informed. These vertical channels have, however, severely failed at critical times. The best known example is that of the Great Leap Forward, where leaders were afraid to report to Mao the extent of the famine, but were instead sending false reports on output increases to try to win Mao's favors. Communist leaders have learned lessons from these failures and rely also on alternative sources of information: tolerance of local revolts giving information on management decisions of local leaders, voting results (percentage of approval for Party candidates) for local elections, protection of whistleblowers (like in the SARS case), tolerance of partially free speech on social media, etc... One can safely conclude that Chinese Communist leaders are quite well informed.

Taxation and state capacity are not a problem in China's communist regime. Significant state ownership gives direct control over state resources. This makes it possible to support low tax rates, which has good effects both on private sector incentives and on reducing incentives to hide in the informal sector. Moreover, the

CCP has the additional instrument of party mobilization, which can at times mobilize resources and people, be it in case of a natural catastrophe or in case of war. Mobilization and campaigns are a standard instrument of the CCP that can be used in exceptional circumstances. Most democracies do not have that tool.

A final factor that is worth mentioning is that the Leninist organizational form behind the CCP is designed to keep party unity, and thus to prevent the formation of factions and fractional loyalties within the CCP. China's collectivist culture inherited from Confucianism and its millennial imperial institutions, is well suited to existing political institutions.

4.4. Some Implications of this reconceptualization of China's transition

The main idea we put forward is that China's transition to the market economy was a deliberate attempt by the CCP to keep its power. The gamble was that the introduction of the market economy, despite being antithetical to communist ideology, would consolidate the power of the CCP. This is consistent with our reconceptualization of transition in Central and Eastern Europe as an internal collapse of the communist power structure due to the failings of the centrally planned economy. We can draw at least two implications from this.

A first obvious implication of our analysis is that the success of Chinese market reforms happened not despite the power of the CCP, but *because of it*. China's growth objectives were pursued via meritocratic competition. Market reforms have not weakened, but strongly reinforced the power of the CCP over the economy, over personnel decisions within all levels of government and the public sector, over the army and the media. Power is both the instrument and the goal of CCP.

A second, probably equally obvious implication, is that there is currently little hope for gradual political reforms in China in the direction of democratization, sharing or separating powers or accountability to the people. China will either continue being a *sui generis* modern economy under absolutist CCP rule (with delegation from party to government) or be subject to a process of state erosion via corruption reaching ever higher organs of CCP. There could be hope of limited democratization, but it would be quite limited, as it would have to take place within the one party-system and within democratic centralism. It is not impossible. One could imagine for example that the President of the country be elected via approval voting (on approval voting, see e.g. Bouton and Castabheira, 2012), and then become automatically Secretary General of the Party. This would be consistent with these constraints. It would be a huge improvement in a direction opposite to that taken by Xi Jinping, but censorship and fear are currently so widespread in China that it is even impossible to have an open debate on even such a minimalist political reform.

5. Conclusion.

We have argued in this paper that transition outcomes in Central and Eastern Europe are better understood by the dynamics of state erosion rather than by policies. One implication of our analysis is that reforming post-communist kleptocratic states is a very different challenge from transition away from socialism to the market economy. This challenge is nevertheless very important for the future prosperity and welfare of citizens from former transition countries.

In contrast to the erosion and eventual collapse of communist power structures, China made a major institutional innovation under the leadership of the Chinese Communist Party: introduce the market economy under communist rule. This is a major historical innovation, and has not that well been understood so far. China's communist rule faces specific survival challenges in the future, but there are few hopes of major political reform. Overall, it has been successful in terms of its own goals, which is to maintain and reinforce the rule of the CCP over China. The rising role of China in the world raises many important questions for international peace and prosperity, but that is another question.

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