

CONCLUSION

The fundamental attitude of true individualism is one of humility toward the processes by which mankind has achieved things which have not been designed or understood by any individual and are indeed greater than individual minds. The great question at this moment is whether man's mind will be allowed to continue to grow as part of this process or whether human reason is to place itself in chains of its own making.

F. A. Hayek¹

INTRODUCTION

Vera Wollenberger is a proto-typical intellectual in the former communist bloc. She believed in the promise of communism, but was compelled to pursue a dissident path because of the ugliness of the East German regime. Her activism cost her a normal life. She was spied on and harassed by the Stasi (the East German Secret Police), fired from her job and even imprisoned because of her political activities with groups like the Church from Below, a human rights group she helped to organize. But Wollenberger persevered and today she is a Member of Parliament.

Unfortunately, her life in the post-communist world is still irrevocably scarred by the past. She helped shape a law intended to give victims of Stasi abuse a chance at justice. Since 2 January 1992 each victim has been allowed to read the file that the police had collected on them and discover who had betrayed them. Rather than achieving justice, opening the 125 miles of files that the Stasi had collected has shattered lives. The Stasi, it turns out, developed an extensive information network that went far beyond anyone's expect-

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ations and permeated deep into the social fabric of East German society. In addition to secret police agents, the Stasi relied heavily on the reports of friends, neighbors and family members to gather information on those under surveillance. In Wollenberger's case, her husband, Knud, provided the most detailed information on her activities to the Stasi.² It is estimated that the Stasi relied on the testimony of some 500,000 informers.³ Purity from communist collaboration has proven to be a rare commodity.

How are the untainted members of society to pass judgement on the rest? For most of the communist era, dissident activity in Eastern Europe was rare. Tacit consent to communist power was the rule. Citizens had to go along to get along. Communist Party membership in the countries of Eastern Europe represented between 10 to 20 per cent of the population.⁴ The revolutions of 1989 have literally thrust some individuals from prison to power.⁵ Lech Walesa, for example, in the span of a decade rose to prominence as the opposition leader of Solidarity in 1980, was harshly put down by General Jaruzelski's imposition of martial law in 1981, eventually formed a coalition government with Jaruzelski in 1989 and emerged as the President of Poland in 1990.

The Polish government, however, has not sought revenge for past oppression. Most of the government apparatus is populated by the same individuals who were there under Jaruzelski's rule. Some Members of Parliament tried to pass legislation that would ban ex-communist officials from public office for ten years. This legislation has so far been successfully blocked by a strange coalition – former communists and the liberal intellectual leaders of Solidarity, who find the legislation unjust and unnecessary.

The puzzles in Walesa's Poland are not just political. Walesa's moral and political power derives from his base – the Solidarity labor union. But Walesa is the President of a government supposedly introducing capitalism as quickly as possible.⁶ Catering to the demands of labor for higher pay, greater security and decision-making control over production does not accord well with tested notions of efficient capitalist production.

The surreal situation of post-communism was most evident in Czechoslovakia, where a dissident poet and playwright, Vaclav Havel, became the President. Havel and his Charter 77 group were the conscience of Central and Eastern European political dissent under the old regime.⁷ Imprisoned and blacklisted in his work, Havel continued to struggle to stop the abuse of human rights under the communist regime throughout the 1970s and 1980s. After the revolution of 1989, Havel

found himself in charge of a government that had to transform society and prevent the degeneration of Czechoslovakia into civil war.

Havel reports that on the day he assumed the presidency he was given a list of fellow writers who had informed on him. Havel states, however, that on that day he 'lost' that list and completely forgot the names of those on it. Personally, he leaned toward letting sleeping dogs lie, but as president, he could not make that choice for the people. People, whose lives were destroyed by the old regime, would feel that the revolution remained unfinished unless justice was served.⁸

But the delicate balance that must be struck between justice and revenge in creating a civil society is not at all an easy one to achieve. The punish and purge mentality that many reformers believe is necessary to accomplish a 'debolshhevization' of these societies leads to witch hunts and character assassinations. In other words, many of the same vices that the old regime is pronounced guilty of are simultaneously advocated by the new regime as necessary to root out and punish communist collaborators.⁹

The National Assembly of the Czech and Slovak Federal Republic, for example, passed legislation preventing former secret police agents, informers, senior communist officials and other former members of Communist Party organs from holding public jobs for a five-year period. Suspect individuals are not allowed to hold high level administrative posts in government ministries, the military, intelligence offices, police, communication industry and state-owned enterprises involved with foreign trade, rail transportation and banking. The 'lustration' law also precludes impure individuals from obtaining high academic posts, and working within the legal system as judges, prosecutors and investigators. It is estimated that the law could adversely affect over a million people.

The understandable anger that people possess concerning their former life under communism is expressed in the demand for revenge. But at the same time their fear of the future is expressed in the demand for the social stability of subsidized prices and guarantees against unemployment. The psychological trauma of transformation is born of both the despair of realizing how much of life was wasted under communism, and the apprehensiveness of having to take full responsibility for one's choices in the post-communist society.¹⁰ As the former regime breaks up, entrenched ways of life break down. The old sources of prestige are now reasons to be despised, whereas the new paths to success, such as accumulating capital and turning a profit, were considered mortal sins under the old regime.

THE POLITICS AND ECONOMICS OF ERROR

The situation in Russia is more acute than any other transforming country. The Communist Party's rule was much longer and its penetration into the social fabric was much deeper. In January 1990, the Communist Party still claimed a membership of around 19 million.¹¹ And, even though in the year preceding the August coup attempt about 20 per cent (4 million) of the membership quit the Party, its influence continued to permeate Soviet society.¹² Before the election of Boris Yeltsin as President of Russia, for example, Party cells existed in all state-run places of work. Yeltsin's move to dissolve Party cells was a direct and major challenge to the Party's grip on the everyday lives of the people of Russia.

Still, and in spite of the fact that the Party has been officially divested of power, its effective power remains alive. This survival is largely due to the fact that communist apparatus was endowed with a political monopoly, and, therefore, its members alone were able to acquire the administrative skills necessary to govern. Communism has been abolished and the Russian government seems committed to democratic rule, but civil service offices are largely run, and the military command is exclusively run, by former communists.¹³ Moreover, the effect of the Communist monopolistic position in society was not only in limiting administrative experience to those that loyally served the Party, but the entire realm of public life was abdicated by the population.

The use of political terror, right from the founding of the Soviet state by Lenin, subdued the population into compliance and reinforced the monopolistic situation. The Russian people understood, as Richard Pipes has argued, that 'under a regime that felt no hesitation in executing innocents, innocence was no guarantee of survival. The best hope of surviving lay in making oneself as inconspicuous as possible, which meant abandoning any thought of independent public activity, indeed any concern with public affairs, and withdrawing into one's private world. Once society disintegrated into an agglomeration of human atoms, each fearful of being noticed and concerned exclusively with physical survival, then it ceased to matter what society thought, for the government had the entire sphere of public activity to itself.'¹⁴

The former Soviet Union was the exemplar of the modern totalitarian state. Russia has not yet opened the files of the KGB to mass inspection.¹⁵ But, if the East Germans are shattered by the

extent to which the Stasi employed friends, neighbors and family to gather information, then it is probably safe to assume that revelations of the KGB's activities would destroy any hope for civil society in Russia. Betrayal may have simply been the price one paid for getting along. Sometimes, it is better to get on with the future rather than focus on redressing past wrongs. Bygones are bygones and, however unpleasant, nothing can be done to change what has happened. The present and future must not be sacrificed to the past.

This is not to suggest that historical conscience is not fundamental to civil society. On the contrary, I believe that Gorbachev's great contribution was allowing the Russian people the chance to regain their own history – blemishes and all. But the activities of the German Parliament and the Czech and Slovak National Assembly are counter-productive. What happened happened, nothing can be done to change it. If it is understood that the ugliness that occurred was due to institutional failings, then institutions can be established to guard against it ever happening again. The real problem with much of the demand for purification is that it seems to stress the 'bad people' explanation. 'If we guard against bad people, then all will be well.' Unfortunately, that advice achieves nothing on the path to a civil society.

Moreover, focusing on the past and attempting to purify the population simply bogs down the process of transformation. In the political realm, purification rituals involving the 'naming of the namers' requires the new leaders to resort to the same unpleasant tactics that their oppressors relied on before. In addition, on the economic front, resentment on the part of the people against former members of the *nomenklatura* underlies arguments against 'spontaneous privatization' and the capitalization of former Communist Party assets. In Russia, for example, *privatisatsia* (privatization) is commonly referred to as *prikhvatitsia* (piratization).¹⁶ Both the politics and economics of purification undermine any attempt to transform quickly into a market economy with a limited government.

A successful political economy strategy for the transformation requires an understanding of the past, but a focus on the future. A romantic view of the politics of transformation may suggest that enlightened leaders can simultaneously punish and purge those that deserve it without tainting the rest of the civil order. But realism in politics questions that ability.

Political choice, as choice in general, is susceptible to two kinds of errors: (1) errors of omission and (2) errors of commission. In other

words, political choice may entail rejecting a policy that should have been accepted or accepting a policy that should have been rejected. Either way, inefficiency and waste occur. But basic principles of decency demand that the civil order of law be structured in a way that guards against errors of commission even if that biases the system in the direction of committing errors of omission. Letting a guilty party go free, in other words, is strongly preferred to convicting an innocent party. The witch hunts and character assassinations associated with purification drives flaunt that basic principle of civil society.

The most fundamental function of free markets, moreover, is their role in error detection. The social institutions of competitive markets, most notably monetary prices, provide signals to economic actors concerning errors and motivate the learning that leads to the mutual adjustments among market participants to eliminate the previous errors of omission (profit opportunities hitherto unrecognized) and commission (losses suffered as a result of failed projects).

A realist vision of political economy must recognize that errors are omnipresent in social life. The normative focus must be on political and economic institutions that cope well with error and motivate individuals to adjust their actions to eliminate most of the errors that are committed. Communism was a political and economic system that in practice possessed no weapons to eliminate errors of the kind being discussed here. Political and legal institutions of communism were not biased against errors of commission as liberal institutions are supposed to be. And, the economic institutions of communism simply did not provide any signal to economic actors concerning errors of either omission or commission. As a result, the real existing social, political and economic life under communism was one of perpetual error.

What I have tried to demonstrate throughout this book is that the reform efforts under Gorbachev failed to introduce anything that would correct the error-prone situation in the former Soviet Union. The problems of political and economic organization, as well as the issue of credibility, were never addressed by Gorbachev. Moreover, in Chapter 7, I tried to suggest what I thought would be necessary to correct the situation. Those suggestions were introduced without regard to the political feasibility of any proposal I offered. What is considered politically feasible at any point in time changes too quickly to be an issue of concern. Instead, the policy suggestions sought to provide an institutional framework which would be able to tolerate and encourage experimentation and learning among diverse peoples

in a manner which addresses the problems of political economy that I have raised throughout the book. If such a system is coherent, then it may serve as a useful benchmark from which to compare reform efforts.

THE YELTSIN REFORMS

Boris Yeltsin's unlikely ascendancy has brought the promise of a new freedom to Russia. Unlike Gorbachev, Yeltsin rose to political power through the industrial management ranks, rather than strictly through Communist Party activity.¹⁷ A graduate of the Polytechnic Institute of Sverdlovsk, Yeltsin went to work at the Urals Machinery Plant (Uralmash). He only joined the Communist Party at the age of 30, and did so mainly for professional career advancement reasons. Yeltsin became the manager of Uralmash at 32. Later he was named First Secretary of Sverdlovsk in 1976 and was finally brought to Moscow by Gorbachev in 1986. But, in October 1987 he attacked Yegor Ligachev for his efforts in resisting reform and Gorbachev for his timid support of reform against conservative forces. As a result, Yeltsin was purged and ridiculed as uncouth, drunken and mentally incompetent. But unlike previous Communist Party officials who had fallen from grace throughout Soviet history, Yeltsin rose again as a leader of the democratic opposition. In 1991 he became the first democratically elected President in Russian history. His courageous stance in the face of the August 1991 coup attempt solidified his position as the future hope of Russia.

In January 1992, the Yeltsin government began a new stage of radical economic reform in Russia. The reforms go much further toward establishing a market economy than any of the proposed plans introduced during the Gorbachev era.¹⁸ Whereas Gorbachev remained throughout his reign emotionally and intellectually committed to some form of socialist economic planning, Yeltsin has rejected socialism and emotionally, if not intellectually, embraced the necessity of capitalist markets for bringing prosperity to Russia. He has surrounded himself with a team of young economists, such as Yegor Gaidar and Anatoly Chubais, who supposedly possess a strong commitment to reforming the Russian economy and joining the international economic community. But there remain fundamental problems with even Yeltsin's shock therapy.

Gorbachev's piecemeal reforms neither improved the apparatus of central economic administration (the rhetoric of the first stage, 1985-7)

nor introduced market discipline (the rhetoric of the second stage, 1987-91). As a result, the economic situation actually grew worse under Gorbachev. Budget deficits soared as subsidies to both enterprises and consumers continued to accelerate. The deficits, in turn, were covered by printing more roubles. The combined budget deficit for the central and republic governments in 1990 was an estimated 20 per cent of GNP, and by the fall of 1991 the exchange rate on the rouble was over 100 roubles to the dollar. Gorbachev's hesitations and reversals eventually destroyed any credibility the reform efforts possessed with Western financial institutions by the winter of 1990-1.

Yeltsin, therefore, inherited not only an abject economic failure, but an entire social system of production in absolute ruins. On 28 October 1991, Boris Yeltsin announced his economic reform package. The Yeltsin program eschewed gradualism. 'The period of moving in small steps,' Yeltsin stated,

is over. The field for reforms has been cleared of mines. There is a unique opportunity to stabilize the economic situation over several months and to begin the process of improving the situation. Under conditions of political freedom, we must provide economic freedom, lift all barriers to the freedom of enterprises and entrepreneurship, and give people the opportunity to work and to receive as much as they can earn, casting off bureaucratic constraints.¹⁹

Yeltsin's broad program consisted of: (1) macroeconomic stabilization, including the 'unfreezing' of prices, (2) privatization and the creation of a healthy 'mixed economy' with a strong private sector and (3) foreign trade liberalization.

Yeltsin followed up this promise of radical reform with ten presidential decrees and resolutions on 15 November 1991 which placed full economic power in his hands. Russia, he decreed, would take control of all financial agencies in its territory. Russia would also completely control oil, diamond and precious metal output in its territory. In essence, Yeltsin delivered the crushing final blow to the old structures of Union power.²⁰

Then, on 2 January 1992, Yeltsin's government acted unilaterally and freed most consumer-goods and producer-goods prices from administrative regulation. But the Yeltsin economic program has been attacked from all directions.

Conservatives, like Russian Vice-President Aleksandr Rutskoi,

accuse Yeltsin of 'seeking to conduct yet another experiment on the Russian people.' Moreover, much of the opposition that the Yeltsin's reform program faced at the Congress of People's Deputies in April 1992 was due to the fact that many in the Congress still represent the old guard, including state enterprise managers who are unsure of where the reforms will leave them.²²

On the other hand, liberal reformers like Larisa Piyasheva, argue that the Yeltsin program for economic stabilization lacks a foundation in basic free market economics. 'The stabilization of the economy,' she states, 'should begin with the privatization of property, not with setting extortionate taxes and the introduction of inordinately high prices.' Both the 28 per cent value added tax and the implementation of price liberalization without first privatizing make no sense to her. All that will result from these efforts is a discrediting of economic liberalization. Piyasheva concluded that 95 per cent of what the Russian government is implementing represents 'economic exercises devoid of common sense.'²³

Nikolai Petrakov has argued that the Yeltsin price reform has 'nothing in common with market-based setting of prices.'²⁴ And, Mikhail Leontyev criticizes the program in even more biting terms, referring to Yeltsin's price liberalization as the 'Pavlovization' of liberal reform. The price liberalization of January 1992 amounts to nothing more than another administrative price increase. The basic institutions of regulated distribution of goods remain intact. 'Free' prices are not preventing limits from being placed on the quantity of goods that can be sold to individual consumers. Even worse, the government has reinforced the practice of trade restrictions by limiting the ability of individuals to buy low and sell high in the market-place by placing a 25 per cent mark-up ceiling on retail prices.²⁵

The main adversary of the Yeltsin reforms, however, may in fact be Yeltsin's own populist posture. He has already backed away from some of the harsh short-term realities of economic liberalization. Yeltsin has criticized political opponents and the members of the media who have attacked his program for reform as engaging in blasphemous political profiteering. But Yeltsin is not just a critic of political profiteering, he has also expressed outrage at monopolistic profiteering on the part of producers.²⁶ In addition, he has already made some significant concessions to appease segments of the population and privatization has not advanced at a rapid pace.²⁷ But

without rapid privatization, price liberalization will not solicit the supply response desired.

The Gaidar reform team has decided to pursue the public auction method of privatization. Nizhni Novgorod, Russia's third largest city, has been chosen as the testing ground for selling off government-owned shops, which if proven to be a successful model could be copied throughout Russia. Even under these most favorable conditions, though, only three dozen shops have been sold in the first two months. At that rate, it would take 8 years to sell the shops in Nizhni Novgorod alone. The government intended to sell 100,000 shops within a year.²⁸ The auction method does not work quickly enough in privatizing even small shops.

Given the industrial structure of the economy, the most important component of reform is the quick privatization of economic entities. Agricultural reforms are moving quickly along the lines of a 'give away' scheme. At the beginning of 1991, 97 per cent of Russia's farm land was comprised of 26,000 state-owned farms, whereas 3 per cent represented 38 million private plots. Russia, however, has started to eliminate the large state-owned farms by simply giving away the farm land to the farmers. Since January 1992, farmers on state-owned farms have been allowed to vote on whether to remain state-owned, or to be operated under various alternative property arrangements. Only 10 per cent have voted to remain state-owned. 90 per cent have voted to experiment with alternative arrangements. 50 per cent have chosen to divide their giant farms into family farms or private farm associations where farm land is owned and managed privately, but the farm equipment is commonly shared. The other 40 per cent have voted to remain a single unit, but be operated as a privately held cooperative.²⁹ This agricultural reform model should be copied for the industrial sector as well.

The main concern of reformers should be to transfer resources as quickly as possible to private hands and establish a rule of law that protects private property and the freedom of entry.³⁰ Once resources are in private hands and property rights are well-defined and strictly enforced, resources will tend to flow in the direction where they are valued most by economic actors. Small shops and large industrial enterprises should simply be transferred to the previous *de facto* owners. As I argued in Chapter 7, the managers of existing enterprises would be in the best position to take over control of the state-owned firms. But, in a fundamental sense it does not matter if ownership is transferred to managers or workers. As long as subsidies

to enterprises are eliminated, freedom of entry is permitted and liquidation of assets is allowed, resources will be channeled in a manner consistent with their effective use. Privatization coupled with comprehensive foreign trade liberalization will demonopolize the industrial system in one step. Normal market forces of profit and loss will guide resource use from that moment on.

In addition, rather than engage in endless debate, perhaps the public/private question could be solved by simply copying a Western model, say the US, with an added proviso.³¹ Services that have traditionally received an economic justification for public provision and/or regulation on market failure grounds could remain as state-run enterprises - public utilities, courts and legal system, schools, national defense and so on. But, all other services need to be turned over to the market. Moreover, even in those areas where it is thought that government provision must remain, responsibility for that provision must be decentralized to the most local level and exclusivity must be denied. Competition from alternative producers, as well as from other local and regional governments, will assure that a public/private mix will emerge that corresponds in a reasonable manner with the desire of the populace.

This type of program, however, is far removed from the IMF-type of reform that the Yeltsin team is following. On 28 February 1992, the Russian government released a memorandum on economic policy reconfirming the commitment to economic reform and their integration into the world economy. This memorandum was sent to the Board of Directors of the IMF to be considered in deliberations on whether Russia would be offered full-membership in the IMF.³² The Russian government, along with most of the other republics of the former Soviet Union, was offered full-membership on 27 April 1992.³³

Unlike the received wisdom, I do not see this as an unequivocally desirable invitation. Certainly, IMF and World Bank membership grants a degree of credibility in the international market-place to the reforming countries. But, how successful has the advice of these institutions been in helping other countries reform their economies? The IMF's standard policy calls for an economic austerity program that is questionable on theoretical and empirical grounds. Even Jeffrey Sachs has admitted that the critics have a point when they argue that 'there are almost no success stories of countries that have pursued IMF austerity measures and World Bank structural adjustments to reestablish creditworthiness and restore economic growth.'³⁴

The basic problem is the IMF's preoccupation with managed macroeconomic stabilization policy which biases analysis in a direction away from the microeconomic structural reform required. A tax system that rewards saving and that encourages investment, abolition of tariffs and other trade restrictions and elimination of burdensome regulations on industry would go a long way toward restructuring the system. Successful monetary reforms, moreover, have traditionally been accomplished by either redeeming the currency for a more credible foreign currency or a precious metal, rather than through the devaluation programs sponsored by the IMF and financed by a monetary stabilization fund.

Foreign loan and credit programs do not lead to the needed structural changes. The 'Grand Bargain' idea is neither grand nor a bargain.³⁵ And while Grigory Yavlinsky's 'Grand Bargain' proposal is no longer on the table, the appeals for Western aid from the Gaidar reform team possess the same implicit logic: provide aid for the peaceful transition or else ugly Russian nationalism and militarism will most likely resurface. But foreign aid will not lead to the fundamental structural changes in the political economy that are necessary. Instead, the funds provided in the name of stabilization will unfortunately send Russia down the same failed path that Latin America and Africa have gone in the past few decades at the urging of international lending institutions. Yeltsin, like Gorbachev before him, will find himself at the helm of an economy descending further and further into an abyss of despair and deprivation.

Prosperity, on the other hand, will come from creating opportunities for investment of capital, both foreign and domestic, to turn a profit. Government (or government agency) to government aid is not the source of economic development. The flow of private financial resources into an economy is the important signal to receive indicating that reforms are moving in the right direction. Stability of law and the ability to repatriate profits will attract business investment from afar and stimulate economic development. The development of a nation's economy is the consequence of an open-ended process of the discovery of opportunities for mutual gain among actors. Not only must the institutional environment generate incentives so economic actors use existing resources in an efficient manner, but the institutional climate must also provide incentives that stimulate the perception of new possibilities among economic actors for effective resource use that had remained unexploited until their discovery. In other words, economic development flourishes whenever an institutional

framework is established within which spontaneous processes of unpredictable mutual discovery of opportunities are encouraged.³⁶ With its rich abundance of natural resources, Russia could develop into the thriving world economy of the twenty-first century under the right institutional conditions.³⁷ Unfortunately, Yeltsin's Russia is still a long way from establishing the requisite market and legal institutions for that development to happen.

THE SPIRIT OF THE AGE

Whatever happens in Russia, the collapse of communism possesses a meaning that goes well beyond the immediate problems of the day – no matter how profound those problems are. Whether Yeltsin fails or succeeds, the political and intellectual world will never be the same. The twentieth century was the age of socialism, and that era is now over.³⁸ In an even more fundamental sense the collapse of communism has signalled the end of modernism and all that entails.³⁹

'The end of Communism,' Vaclav Havel writes, 'is, first and foremost, a message to the human race.' We have not yet fully deciphered its meaning. But, in its deepest sense, 'the end of Communism has brought a major era in human history to an end. It has brought an end not just to the 19th and 20th centuries, but to the modern age as a whole.'⁴⁰ Marxism was the quintessential modernist movement. Through rational design man's emancipation from the oppressive bonds of nature and other men would be accomplished. Lenin was the guardian, and then deliverer of this emancipation project to Russia. Lenin, in addition to Russian Marxism, was influenced by the fanatical rationalist Nikolai Chernyshevsky, and especially his novel, *What is to be Done?*, from which Lenin drew the title, and much of the spirit behind, the basic charter of the Bolshevik movement. 'The result,' Martin Malia points out, 'was a fantasy of Reason-in-Power that mesmerized the entire twentieth century, both East and West.'⁴¹

With the socialist movement the Enlightenment turned against mankind and enslaved him in chains made of his own Reason. The death of the political economy of socialism does not mean the end of ideological dispute nor the rejection of reason. History has not ended, even in the narrow sense that Francis Fukuyama intended.⁴² The substitution of technocratic problem solving for passionate discussion of ideas and values is not the intellectual curse that follows the death

of communism as a legitimating power, but rather the logical consequence of modernistic scientism.

The post-communist era, if anything, will require that ideological visions of what is good and just be articulated by new spokesmen. Imagination, idealism and the purely abstract goal of a free society must replace the scientific notions of the past era in which the desire to order society in strict accordance to a rational plan ended in political arbitrariness and economic poverty. Just because the ideas that fuel the imagination may not be brand new does not necessarily mean that they are old.⁴³

The liberalism of the nineteenth century failed because of its inability to protect against opportunistic invasion (namely, interest group factions within representative democracy), and the socialism of the twentieth century failed because it was an incoherent utopia (unable to engage in rational economic calculation, and, thus, to progress economically). What is required for the twenty-first century is a vision of a new, but workable, utopia. A post-modern vision of politics and economics if you will. Such a vision of political economy must combine the humility toward the power of reason to control social processes found in the Scottish Enlightenment, with the wealth of theoretical and empirical information that is to be gleaned from the twentieth century experience with economic planning in both East and West.

CONCLUSION

We have the good fortune to live in exciting times. A world that had appeared to settle into a nice equilibrium since the 1970s was suddenly sent spinning in the mid- to late-1980s. New questions concerning international relations, economics, politics, law, ethnic tranquility and nationhood are now up in the air. Most of these questions are far from being answered, and probably will not be in the foreseeable future. And, even if we come to a consensus on some of the issues, each generation must ask them anew. But, universal principles of social interaction do exist for us to discover and those we find must be incorporated into the social wisdom if we are to avoid destroying civilization.

If the Soviet experience can teach us anything, it is that we must, as Richard Ericson has put it, 'abandon the Faustian urge to control, to know in advance, and thus, to allow economic outcomes to arise naturally as the unpredictable consequences of market interaction.'⁴⁴

The processes of market interaction fundamentally lay beyond our control. Rather than attempt to design optimal plans and control social forces, our intellectual efforts must be devoted to asking questions about the institutional framework within which activities beyond our control will take place. Raising and providing useful answers to such questions, however, requires an array of disciplines.

Economics is an important, in fact essential, component in this inquiry. But, economics cannot provide all the answers. Politics, philosophy, history and cultural theory, along with other intellectual disciplines and common sense, must also be employed.

Most importantly, though, moral reasoning must be allowed to regain a legitimate place in scholarly endeavors. Perhaps the most fundamental reason why Sovietologists were so surprised by the events of the late 1980s was the hegemony of a scientific methodology which disregarded evidence from the humanities (such as literature and personal testimony) and dismissed questions of human meaning as metaphysical nonsense. Reasoned debate about such fundamental issues can, and must, take place if we are to think in an effective way about the politics and history of our times.

NOTES

1 INTRODUCTION

- 1 John Stuart Mill, 'The claims of labour' [1845], in *Essays on Economics and Society*, vol. 4, *Collected Works of John Stuart Mill* (Toronto: University of Toronto Press, 1967), p. 370.
- 2 See Stanislav Shatalin, N. Petrakov and G. Yavlinsky, *Transition to the Market* (Moscow: Cultural Initiative Foundation, 1990), republished as *500 Days* (New York: St Martin's Press, 1991). See also '500 Days to Shake the World,' *The Economist* (15 September 1990): 93-4, and David Remnick, 'Gorbachev shifts on economy,' *The Washington Post* (13 September 1990): A30-A31.
- 3 See Ed Hewett, 'The new Soviet plan,' *Foreign Affairs* (Winter 1990/91): 146-67. Hewett argues that the major strength and stumbling block to the 500-Day Plan was the issue of confederation which correctly recognized the collapse of the union, but was a position which Gorbachev simply could not endorse in the fall of 1990. The Ryzhkov Plan, on the other hand, while retaining central power, granted some increased autonomy to the republics. Gorbachev enlisted the services of Abel Aganbegyan to draft a compromise plan of the Shatalin and Ryzhkov Plans, which eventually became the Presidential Plan.
- 4 See the reports by Quentin Peel, 'Reformers despair of 500-day plan as Soviet prices soar,' *Financial Times* (12 October 1990): 20, 'Gorbachev's economic program,' *New York Times* (17 October 1990): A8, Bill Keller, 'Gorbachev offers his plan to remake Soviet economy, but includes no timetable,' *New York Times* (17 October 1990): A1 and A8, 'Soviet plan in the middle,' *New York Times* (18 October 1990): A1 and A14, 'Gorbachev's economic plan approved,' *New York Times* (20 October 1990): A6 and Peter Passell, 'Gorbachev counsels a prudent revolution,' *New York Times* (21 October 1990): E3.
- 5 Boris Pinkser, a leading pro-market Soviet intellectual and the husband of Larissa Popkova-Piyasheva, holds the opinion that Reagan's military build-up was the major contributory factor responsible for the breakdown of the Soviet empire. (Personal conversation with Pinkser on his visit to New York in 1991.) A sample of Pinkser and Piyasheva's views can be found in Lev Timofeyev (ed.) *The Anti-Communist Manifesto*

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banking in formerly communist countries,' *Economic Review of the Federal Reserve Bank of Richmond* (Ma), June 1990: 13-19. As Hetzel points out

A market economy . . . is not established by a one-time reform. It requires a lasting commitment to limiting the role of government in economic activity. The existence of a central bank provides a continuing incentive for politicians under pressure to confuse money creation with wealth creation. The resulting inflation then leads to myriad interventions in the economy in the form of wage, price, interest rate, exchange market, and capital controls. Eliminating the central bank is one way of committing to a limited role for the state (p. 19).

- 48 Abba Hetzel, 'Free enterprise and central banking in the formerly communist countries,' p. 19, fn. 4 (see Note 47).
- 49 See the discussion of free banking theory in White, *Competition and Currency*, and George Selgin, *The Theory of Free Banking* (Totowa, NJ: Rowman and Littlefield, 1988). For an historical discussion of the operation of a free banking system see Lawrence White, *Free Banking in Britain: Theory, Experience and Debate, 1800-1845* (New York: Cambridge University Press, 1984). A key episode in White's discussion is how the banking system handled the Ayr Bank failure of 1772. As White points out, the Ayr Bank, which was in operation from 1769 to 1772, engaged in reckless management and extended a great deal of bad credit through note issue. The bank's failure also led to the failure of eight other private banks, but it did not threaten the financial system as a whole. The note exchange system that emerged in the Scottish system served as an important check against over-issuance by a single bank and provided market incentives to discipline those that attempted to engage in over-issuance of its notes through the law of reflux. White, *Free Banking in Britain*, pp. 30-2, 126-8.
- 50 For a discussion of this problem with central banking see Selgin, *The Theory of Free Banking*, pp. 89-107 (see Note 49).
- 51 However, see the report in *The Economist* (29 February 1992): 78-9 on the surprising rise in the rouble since mid-January 1992. Since the January price liberalization, the rouble rose from 110 to the dollar to 70.
- 52 See, for example, Annelise Anderson, 'Monetary competition and monetary stability in the transition from plan to market,' in James Dorn and Larisa Piyasheva (eds) *From Plan to Market: The Post-Soviet Challenge* (Washington, DC: Cato Institute, forthcoming).
- 53 See Lerner, *The Economics of Control* (New York: Macmillan, 1944), pp. 302-22. Also see Lerner, 'Functional finance and the federal debt,' *Social Research* (February 1943): 38-51, and 'The economic steering wheel,' *The University Review* (June 1941): 2-8. For a criticism from the perspective of the political incentives functional finance engenders see James Buchanan and Richard Wagner, *Democracy in Deficit* (New York: Academic Press, 1977).
- 54 For a discussion of the analytical problems with the notion of public goods see Rothbard, *Man, Economy and State*, pp. 883-90 (see Note 4). Also see

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- Tyler Cowen, 'A public goods definition and their institutional context: a critique of public goods theory,' *Review of Social Economy*, 43 (April 1985): 53-63.
- 55 This argument is developed in Richard McKenzie and Dwight Lee, *Quicksilver Capital* (New York: Free Press, 1991).
 - 56 This idea was directly challenged by Marxists. In the Marxist analysis of capitalism the logic of the system led to increasing monopolization. Since capitalism suffered from internal contradictions, monopoly capitalists would merge with the state to prop up their enterprises. These state monopoly capitalists would then seek to expand their market internationally and the competition between the various imperialistic state monopoly capitalists would breed war. This is how Lenin, for example, sized up the situation of the First World War. Socialism was the only logical leap to take. See Lenin, *Imperialism, The Highest State of Capitalism* (1916), in *Collected Works*, vol. 22 (Moscow: Progress Publishers, 1977), pp. 185-304.
 - 57 Alexander Gray, *The Socialist Tradition* (New York: Harper & Row, 1968), p. 63. For a criticism of utopian reasoning from positions of moral purity see Isaiah Berlin, *The Crooked Timber of Humanity* (New York: Alfred Knopf, 1991). Berlin took the title from a quote of Immanuel Kant which reads: 'Out of timber so crooked as that from which man is made nothing entirely straight can be built.'
 - 58 See Robert Nozick, *Anarchy, State and Utopia* (New York: Basic Books, 1974), pp. 297-334.
 - 59 See the discussion on simultaneity in Janos Kornai, *The Road to a Free Economy* (New York: Norton, 1990), pp. 158-62.
 - 60 This is also true for capitalist economies experiencing depressions. See Rothbard, *America's Great Depression*, 3rd edn (Kansas City: Sheed and Ward, 1975), pp. 25-9.
 - 61 On this distinction see F. A. Hayek, *The Constitution of Liberty* (Chicago: University of Chicago Press, 1960), pp. 103-17.

8 CONCLUSION

- 1 F. A. Hayek, 'Individualism: true and false,' in *Individualism and Economic Order* (Chicago: University of Chicago Press, 1980(1948)), p. 32.
- 2 See Stephen Kinzer, 'East Germans face their accusers,' *New York Times Magazine* (12 April 1992): 24-7, 42, 50-2.
- 3 See 'Eastern Europe's past,' *The Economist* (21 March 1992): 24.
- 4 It was estimated in 1980 that 20 per cent of the Romanians over 18 years of age belong to the Communist Party, 18 per cent of East Germans, 14 per cent of Czechoslovakians, 13 per cent of Bulgarians, 12.5 per cent of Poles and 10 per cent of Hungarians.
- 5 Timothy Garton Ash has perhaps provided the best discussion of the intellectual and political movement behind the revolutions of 1989. See his *The Uses of Adversity* (New York: Vintage Books, 1990) and *The Magic Lantern* (New York: Random House, 1990).
- 6 In February 1992, however, a new blueprint for economic change was

unveiled in Poland. The new plan, announced by Prime Minister Jan Olszewski, intended to maintain some of the austerity measures of the original Balcerowicz program, but restore public confidence in the government's ability to manage the economy effectively. The emphasis in Poland's economic policy would shift from fighting inflation to stimulating the stagnant economy. The proposal met with sharp criticism from several different perspectives. See Stephen Engelberg, 'Polish economic about-face draws criticism,' *New York Times* (21 February 1992): A8. For a report on the attitude of some Polish economists see Barry Newman, 'Poles give lessons on capitalistic ways to ex-Soviet masters,' *Wall Street Journal* (2 April 1992): A1, A10. Mrs Bochniarz, the former minister of industry and now president of Nicom Consulting, argues that Western prescriptions for economic change are fundamentally flawed and led to many problems in Poland, including the loss of political will on the part of the government after the October 1991 elections. Mr Balcerowicz and Mrs Bochniarz lost their jobs after those elections. Mrs Bochniarz now counsels the Russians against following the Polish path exactly. Her most important advice is that reform is too important to be left to the market. Government must guide and manage the process from start to finish. Otherwise, the painful pill of transformation will simply be too hard to swallow.

- 7 See, for example, Vaclav Havel *et al.*, *The Power of the Powerless* (Armonk, NY: M. E. Sharpe, 1985). The papers in this book, written shortly after the formation of Charter 77 and just before the birth of Solidarity, argued that communist power did not derive from totalitarian control of the soul of subjects. The delirium of the Stalinist period was gone. Repression continued, but in a more anonymous way. And, while communist fictions concerning the past, present and future were constantly produced and reproduced by the state apparatus of information, no one believed in the promise any more. Communist power derived, instead, from the passivity, opportunism, cynicism and tacit acceptance of the way of life. Silent disagreement and conformity on the part of citizens assured that communist power was safe. Only with the development of civil society outside of the official state sector – an anti-political politics – can the communist system be defeated.
- 8 See the interview with Vaclav Havel conducted by Adam Michnik and published in *Gazeta Wyborcza* in 'A conversation with President Havel,' *World Press Review* (March 1992): 14–16. Also see Havel's reaction to the 'lustration' law passed by the National Assembly in 'Paradise lost,' *New York Review of Books* (9 April 1992): 6–8. Lustration derives from the Latin and means 'sacrificial purification.'
- 9 See, for example, Jeri Laber, 'Witch hunt in Prague,' *New York Review of Books* (23 April 1992): 5–8.
- 10 See, for example, Vasily Golovanov, 'A deep despair in Yeltsin's Russia,' *Literaturnaya Gazeta*, in *World Press Review* (April 1992): 18–21.
- 11 The exact figure was 18,856,113 members as reported in *The Europa World Year Books*, 1990.
- 12 See Michael Mandelbaum, 'Coup de grace: the end of the Soviet Union,'

- Foreign Affairs*, 71 (1) (1992): 168.
- 13 See Richard Pipes, 'Russia's chance,' *Commentary*, 93 (3) (March 1992): 28–33.
 - 14 Richard Pipes, *The Russian Revolution* (New York: Alfred Knopf, 1990), p. 838.
 - 15 The KGB has actually been abolished, but the AFB (the Agency of Federal Security) has been established to take its place. Also the *Moscow News*, no. 6 (9–16 February 1992): 2, reports that examination of the files has revealed that there were KGB agents among the hierarchy of the Russian Orthodox Church. There is an ongoing investigation of the files by a Parliamentary Commission of the Russian Supreme Soviet. The current commission is the third one to be established, the reports of the first two were suppressed.
 - 16 See 'Behind democracy's façade,' *The Economist* (18 April 1992): 46. But see Oleg Vite and Dimitry Travin, 'Privatization as effected by the nomenklatura,' *Moscow News* (1–8 December 1991): 9. Vite and Travin argue that one must first distinguish between those who rose through the communist ranks as Party functionaries from those who rose as business executives. The business executives and factory managers had not only to master political horse trading required of all those who rose to prominence in the Party hierarchy, but also had to possess an ability to bargain in the bureaucratic market over resources, plan targets and personnel. Vite and Travin argue that those individuals possess the skills that will allow them to adapt to a free market environment quickly – much quicker, they argue, than the small-scale black market entrepreneurs would be able to adapt. The managerial elite is simply seeking to retain their control through privatization of what they have laid claim to as their own property. However unappealing it may be to the romantic, the managerial elite must become an ally of economic reform. The struggle against the managerial elite, they conclude, is not only dangerous to democracy, but economically pointless.
 - 17 See Martin Malia, 'Yeltsin and us,' *Commentary*, 93 (4) (April 1992): 21–8. Also see John Morrison, *Boris Yeltsin: From Bolshevik to Democrat* (New York: Dutton, 1991).
 - 18 An unfortunate consequence of our fascination in the West with the changes in Russia has been the personification in the public mind of reform with particular people. Personalities rather than fundamental ideas have dominated most discussion. This led to a bizarre inversion of the truth. Gorbachev was seen as a democrat even though he was never elected, and Yeltsin was seen as an authoritarian even though he was elected. The West tended to thank Gorbachev for the liberation of East and Central Europe, when in reality power was grasped from him by Solidarity, the Civic Forum, Sajudis and the Democratic Russia Movement. As Anders Aslund has pointed out, Yeltsin's record is much better than Gorbachev's on economics and politics. See Aslund, 'Russia's road from communism,' *Daedalus* (Spring 1992): 77–95.
 - 19 See Boris Yeltsin's speech to the Congress of Russian SFSR People's Deputies, *Izvestia* (28 October 1991), translated in *Current Digest of the Soviet Press*, 43 (43) (27 November 1991): 1. Also see 'Yeltsin outlines

- radical economic reforms,' *Soviet/East European Report*, 9, no. 5 (20 November 1991): 1-2, 4.
- 20 See S. Ruzin, '19 decrees that shook the world,' *Kommunistichaya Pravda* (19 November 1991), translated in *Current Digest of the Soviet Press*, 43 (46) (18 December 1991): 1.
- 21 See Aleksandr Rutskoï, 'In defense of Russia,' *Pravda* (30 January 1992), translated in *Current Digest of the Post-Soviet Press*, 44 (4) (26 February 1992): 1.
- 22 See 'Building the new Russia,' *The Economist* (25 April 1992): 12-13. Also see the conversation with Yegor Gaidar, the architect of the Yeltsin program, *The Economist* (25 April 1992): 17-20.
- 23 See Olga Gerasimenko, 'The country doesn't have a Margaret Thatcher,' *Rossia* (29 January-4 February, 1992), translated in *Current Digest of the Post-Soviet Press*, 44 (5) (4 March 1992): 4.
- 24 Nikolai Petrakov, 'He who doesn't take risks doesn't get to drink champagne,' *Megapolis Express* (6 February 1992), translated in *Current Digest of the Post-Soviet Press*, 44 (7) (18 March 1992): 9.
- 25 See Mikhail Leontyev, 'The Pavlovization of liberal reform,' *Nezavisimaya Gazeta* (15 January 1992), translated in *Current Digest of the Post-Soviet Press*, 44 (3) (19 February 1992): 11-12.
- 26 See Yeltsin's speech to the Russian Federation Supreme Soviet on 16 January 1992, translated in *Current Digest of the Post-Soviet Press*, 44 (2) (12 February 1992): 1-3.
- 27 See 'Mere shock, or therapy too?,' *The Economist* (22 February 1992): 63. This editorial, however, argues against interpreting Yeltsin's raising of pensions and other concessions to ease the difficulties of the transition as a necessary retreat from the long-term stabilization policy. Such an interpretation, it is argued, is both too gloomy and too early. The real threat to the reforms will come, however, if privatization does not proceed quickly to curb the monopolistic situation. In November 1991, a parliamentary committee was empowered to approve any price increase by a monopolistic enterprise. Already 2,000 enterprises accounting for an estimated 70 per cent of industrial production have been named as monopolistic. Wholesale price control, though, could fundamentally destroy the liberalization efforts.
- 28 See *The Economist* (11 April 1992): 72.
- 29 See *The Economist* (11 April 1992): 71-2.
- 30 See the debate on privatization between the Gaidar team and the Piyasheva-Selyunin group in *Current Digest of the Post-Soviet Press*, 44 (9) (1 April 1992): 5-7.
- 31 To reach a Western ratio of public/private the former communist economies would still have to transfer about 50 per cent of GDP from government ownership to private ownership. In her twelve years in power, Margaret Thatcher privatized about 5 per cent.
- 32 See 'Russian government memorandum on economic policy,' *Izvestia* (28 February 1992), translated in *Current Digest of the Post-Soviet Press*, 44 (9) (1 April 1992): 1-4.
- 33 See *New York Times* (27 April 1992): A1, A6.
- 34 Jeffrey Sachs, 'Managing the LDC debt crisis,' *Brookings Papers on*

- Economic Activity*, 2 (1986): 402. Sachs develops an argument for debt relief in this paper similar to the argument used in the law and economics literature to justify court imposed contract renegotiations. Due to the low probability of certain contingencies, contracts are often incomplete. The cost of accounting for every conceivable contingency would be too great. It is sometimes the duty of the judge or the adjudicating party to reduce the costs of renegotiating a contract between parties by offering terms that the parties would have agreed to had they negotiated the restructuring of the contract. Debt relief is in essence a renegotiation of a contract due to unfortunate and unforeseen events occurring to the debtor nation. Debt contracts, Sachs argues, should be renegotiated either when the debtor nation is in such dire economic straits that continued servicing of the debt would threaten the political and social stability of the country, or the ability of the debtor nation to repay the debt would be improved by partial forgiveness.
- 35 On the development of the 'Grand Bargain' idea see Grigory Yavlinsky, Mikhail Zadornov and Aleksei Mikhailov, 'Plus the "Group of Seven": program for an organized return to the world economy,' *Izvestia* (20 May 1991), translated in *Current Digest of the Soviet Press*, 43 (20) (19 June 1991): 1-5. Also see Graham Allison and Grigory Yavlinsky, *Window of Opportunity* (New York: Pantheon, 1991). In addition, see Jeffrey Sachs, 'Helping Russia,' *The Economist* (21 December 1991-3 January 1992): 101-4.
- 36 See Israel Kirzner, 'The entrepreneurial process,' in *Discovery and the Capitalist Process* (Chicago: University of Chicago Press, 1985), pp. 68-92. Also see Alfredo Irigoín, 'Economic development: a market perspective,' PhD thesis, Department of Economics, New York University (1990).
- 37 See Jude Wanniski, 'The future of Russian capitalism,' *Foreign Affairs*, 71 (2) (Spring 1992): 17-25.
- 38 Stephen Howe, 'Hiccup in the long march of history,' *New Statesmen and Society* (6 March 1992): 12-14, argues to the contrary that socialism never amounted to much in Eastern Europe anyway. After the 1930s, communism ceased to be a coherent ideology. The traumas of post-communism have little to do with communism, he argues, because communism was mostly a gigantic ideological façade. However true these sentiments, expressed by Howe and others, are, they fundamentally confuse the issue of the intellectual vision behind the experience of socialism and what that means for us today. The ideological façade and the economic disaster were the unintended consequences of trying to pursue an incoherent and impossible utopian vision of how to organize social relations of production. The failure of this vision had nothing to do with the particular problems of political leadership in East and Central Europe or the former Soviet Union, but was the result of the inherent structural weaknesses of the idea.
- 39 For a discussion of modernism and the ambiguities surrounding post-modernism see Peter Scott, 'The postmodern challenge I-IV,' *Times Higher Education Supplement* (10, 17, 24 and 31 August 1991). Scott, however, argues that post-modernism is too ambiguous to mount much of

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- a challenge to modernism. Moreover, he argues against interpreting modernism strictly as a rationalist philosophy. In the end, though, Scott's essays fail to capture the strength and weaknesses of modernism because he does not distinguish between the French and Scottish Enlightenment. While the French Enlightenment embodied the Age of Reason and Science, the point of the Scottish Enlightenment was, in large part, to employ rational analysis to whittle down the claims of reason. See F. A. Hayek, *The Constitution of Liberty* (Chicago: University of Chicago Press, 1960), pp. 54-70.
- 40 Vaclav Havel, 'The end of the modern era,' *New York Times* (1 March 1992): E15.
- 41 Martin Malia, 'Yeltsin and us,' 24. Also see Z. (Malia), 'To the Stalin mausoleum,' *Daedalus* (Winter 1990): 295-344, and 'Leninist endgame,' *Daedalus* (Spring 1992): 57-75.
- 42 See Fukuyama, 'The end of history?,' *The National Interest* (Summer 1989): 3-18.
- 43 Timothy Garton Ash points out that there are many questions to ask about the new Europe. The most common question raised by commentators is how can the West help the transition of formerly communist countries to liberal democracies. But, Garton Ash thinks that the more interesting question is how might these former communist countries help the West. What, after all those years of hard experience under communism, can they teach us about life and social order? Garton Ash, however, goes too far when he suggests that the new Europeans can offer us no new ideas. 'They can,' he states, 'offer no fundamentally new ideas on the big questions of politics, economics, law or international relations. The ideas whose time has come are old, familiar, well-tested ones. (It is the new ideas whose time has passed.)' See Garton Ash, *The Magic Lantern*, pp. 150, 154 (see Note 5). While true on one level, this assessment misses the great opportunity that the new Europe holds for starting anew, of redefining the basic relationship between the citizen and the state, and what that may mean for the development of social theory.
- 44 See Richard Ericson, 'The classical Soviet-type economy: nature of the system and implications for reform,' *Journal of Economic Perspectives*, 5 (4) (Fall 1991): 26.

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