

Transition in the Czech Republic from Institutional Point of View

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Abstract—This paper concentrates on selected aspects and continuities of system changes in Central East Europe. Transition in Central East Europe in 1990-ies was influenced by two distinct processes: societal transformation on the one hand and global modernizing trends on the other. The country in focus is the Czech Republic. As it is argued, system changes in the Czech Republic suffered from many economic-institutional weaknesses that turned out to be largely path-dependent. Comparison of transformation processes in the Czech Republic with other Central East European countries provides us with numerous facts useful for the derivation of economic-institutional evaluation of above mentioned processes. From the western point of view, the post-communist countries seemed to be encapsulated in similar institutional-economic categories just due to the mutually shared past; closer analysis, however, discloses that while from the western, outer point of view, these countries seem to resemble each other, in reality, from inner perspective, they are rather heterogeneous.

Keywords—system changes, Czech Republic, Central East Europe, institutions.

I. INTRODUCTION

Societal transformation in post-communist countries in 1990-ies consisted in the transition from totalitarian to democratic political regime and from centrally planned to the market economy. Moreover, these governmentally directed changes were accompanied by more spontaneous move from extensive forms of development to the intensive ones, which corresponded to the post-fordist modernizing trends in practically all developed countries. From wider societal perspective, we are entitled to speak about return to the modern developmental track. Obviously, such comeback can be very slow and rather painful, which applied also to Czechoslovakia and later, when the country was split, to the Czech Republic and Slovakia [32].

Nowadays it is generally accepted that in the Czech Republic, the socioeconomic transformation was accomplished under the design of shock therapy. From the economic standpoint the attention was focused mainly on macroeconomic questions and spatial-institutional framework remained largely omitted. Insufficient attention was paid to the fact that transformation of any national economy is composed

of particular regional/local transformations. It has been ignored that stability of any entity can be reached only by means of functional interconnectedness of its components.

After the collapse of the state socialist regimes in 1989, policy-makers and researchers faced the problem of designing the transforming country's economic, social, and political strategy. In this, they could not refer to any historical precedents of post-communism. Only an overall direction of the desired change, towards a Western-type democracy and market economy, was clear and generally accepted [24].

The above-mentioned task was furthermore enriched by the general process of the move from fordist paradigm of socioeconomic development towards the post-fordist one. While western economies cope with these modernizing trends two or three decades, transition economies are exposed to the modernization categories in much shorter, compressed period.

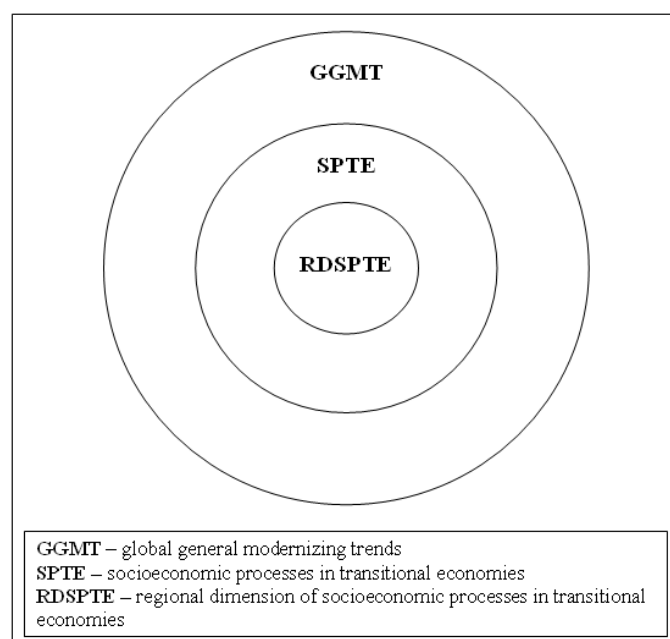


Fig. 1: Rank-spatial differentiation of transition processes

The main objective of this article is to analyze and interpret selected aspects of initial phase of transition in the Czech Republic. This will be facilitated also by the comparison of the transformation in the Czech Republic with other Central East European countries. As it is shown, seeming economic-institutional homogeneity of post-communist countries seen

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from the outer perspective is in reality much more differentiated.

II. FRAMEWORK OF TRANSITION IN CENTRAL EAST EUROPE: TOWARDS MODERNISATION

A. Theory of regulation

Theory of Regulation that was pioneered namely by [1] and [2] grew up in France in the second half of 1970-ies. The basic concept of this theory consists in the idea that society and economy are exposed to crises periods from time to time. These crises are sooner or later surpassed by the adaptation of existing socioeconomic and institutional forms.

[1] argued that both neo-classical economics and Marxian economics had reduced complex social relations to a postulate of homogeneity that were fundamentally untenable. Neo-classical economics reduced all human behaviour to the axiom of rationality and Marxian economics reduced them to general laws that led to the overthrow of capitalism. This form of methodological individualism ignored the asymmetry of information and the role played by externalities. [1] showed that the assumption of a general equilibrium under perfect competition or general laws of history was simply incorrect just due to the asymmetric information and the role of externalities.

In this context, a mode of regulation and a regime of accumulation constitute the principal notions. According to [1] 'A mode of regulation is a set of mediations which ensure that the distortions created by the accumulation of capital are kept within limits which are compatible with social cohesion within each nation.'

Society finds itself in a crisis in case that regime of accumulation is in discordance with the mode of regulation or the economy and the general political-institutional organisation are unbalanced. The formation of a new general dynamic balance is initiated by the changes in the regime of accumulation, i.e. in economic sphere.

Existing paradigm is always given by specific mode of production, including organisation of labour as well as labour relations, specific regime of accumulation delimited by macroeconomic relations between production and consumption and a certain model of social regulation. Some authors distinguish three essential periods of capitalism, which are based on specific regimes of accumulation and systems of social regulation:

- Extensive accumulation based on free economic competition and lasting from the second half of nineteenth century till 1914,
- Intensive accumulation based on Fordist-Keynesian regulation from the end of World War II to 1973,
- 'New' post-fordist accumulation after 1973 (see also [8] or [31])

Nonetheless, proponents of above mentioned approach emphasize that theory of regulation is rather a general framework of thoughts than consistent theory. A great advantage of this theory consists in its applicability to various periods of capitalism. Therefore, the widest theoretical frame of this work is based just on the theory of regulation, whose most frequent application is the transition from fordist towards post-fordist socioeconomic regime (see also [2]).

B. From Fordism towards Post-fordism

Immense socioeconomic changes in 1960-ies and 1970-ies are usually depicted as the transformation of advanced countries from fordism towards post-fordism. According to the 'regulation school', fordism was a mode of capital accumulation that originated in 1914 when Henry Ford introduced a five-dollar, eight-hour workday for the assembly line production of cars.

The regime of intensive accumulation was formed already in 1930-ies, but mainly after World War II, when it constituted true bait mainly for Western Europe both physically and mentally destroyed by the war. This societal-economic paradigm called fordism was prevailing in basically all advanced countries until 1970-ies, when oil crisis suffocated practically the whole planet. The typical features of fordism are as follows (see also [8] or [31]):

- The division of labour was based on the rigorous separation of management functions from individual standardised manual performances of workers, which resulted in a greater productivity. However, this division of labour required a higher degree of labour-discipline and subservience to a central directing authority.
- Regime of intensive accumulation enabled the augmentation of investments on the one hand and the growth of employees' purchasing power on the other hand.
- Mass production and mass consumption as principal categories of fordism.
- Mode of regulation was determined mainly by collective bargaining and trade-unionism as well as by intense redistribution processes in the framework of welfare state. The state interventions into the economy were typical phenomenon of the time for the sake of prevailing Keynesian doctrine. Keynesian approach, in a certain sense, represented the application of Fordism at the level of the state.

Welfare state that was created in the fordist era handled very extensive social nets. Strong redistribution processes in the framework of social but also many other policies formed adequate social and economic conditions facilitating the stability of fordist society based mainly on mass production and mass consumption.

Relatively idyllic fordist times were broken by formidable economic problems in 1970-ies. Oil crisis in combination with quickly advancing technological development and the rise of globalisation enfeebled the dominance of fordist paradigm. Fordist way of production appeared to be obsolete in new socioeconomic conditions. It was claimed that fordist industrial production is too rigid, non-flexible and finally leading towards the decline of competitiveness. All of these changes finally stimulated the gradual appearance of a new system of flexible accumulation that was based on new core innovations.

New findings in the sphere of microelectronics and information technologies enabled the transformation of production, which started to utilise flexible computerised and robotic systems. New information and communication technologies speeded up the operations on financial and capital markets as well as transfers of the capital enormously. Finally, the liberalisation of world trade and quick movement of capital together with deregulation measures gave rise to the socioeconomic phenomenon called ‘time-space compression’ (see for instance [8]).

If rigidity in the labour market, owing to trade-unions or cultural impediments, was the main feature of Fordism, extreme flexibility became the central concept in the post-fordist era. Flexible accumulation is based on a couple of fundamental principles:

- Just in time production, which aims at the minimisation of inventory at every stage of production since unused inventory represents unrealised capital.
- Total quality management, when the introduction of quality control circles to check quality of supplies of components inside and outside the factory.
- Teamwork, which consists in the creation of autonomous task oriented work groups.
- Managerial decentralisation, consisting in the replacement of centrally controlled hierarchies with flowing matrices of a federation of organisational styles and practices.
- Flexible labour force lies in the possibility of laying off workers during a lean periods and hiring them back in times of prosperity.
- Functionally flexible workers including task integration and rotation and multiskilled labour force (see [8]).

These transformations in the organisation of the work facilitated the further growth of productivity, which became the necessity vis-à-vis sharpened competition at the global level. Increasing differentiation of the society to the bigger number of social groups and the saturation of the high proportion of society with consumer goods in advanced countries changed the patterns of consumer’s behaviour and heighten the scope of specific needs and wishes. Enterprises

Table 1: Differences between Fordism and Post-Fordism [8] and [33]

FORDISM	POSTFORDISM
ECONOMY AND THE PRODUCTION PROCESS	
Economies of Scale	Economies of Scope
Mass production of homogeneous goods	Small batch production
Mass consumer’s society – less differentiated demand	Differentiation of demand and individualisation of consumer styles
Large stocks and inventory	Minimal stocks (just in time)
Testing quality ex-post (rejects and errors detected late)	Quality control part of production process (immediate detection of errors)
Dominance of industry	Dominance of tertiary sector and rise of quaternary sector – disindustrialisation
Cost reductions through wage control	Learning-by-doing integrated in long-term planning
Payment per rate (based on job design criteria)	Personal payment (detailed bonus system)
Single task performance by worker	Multiple tasks
High degree of job specialisation	Elimination of job demarcation
Vertical labour organisation	More horizontal labour organisation
Trade Unionism	Individualism
SPACE, STATE AND IDEOLOGY	
Welfare state – extensive social security system guaranteed by state	Postwelfare state based - privatisation of social security systems and collective needs
Keynesianism and state interventionism – market regulation	Neoliberalism – deregulations, support of free market functioning
National, central, exogenous regional policy	‘Territorialised‘ endogenous regional policy
Subsidized state/city	‘Entrepreneurial‘ state/city, sharpened interregional/intercity competition
Centralisation – hierarchic top down management	Decentralisation – emphasis on bottom up activities, new public management
Public sector regulates and controls private sector	Public Private Partnership, co-operative behaviour of public sector, which stimulates the activities of private sector.

were forced to respond flexibly and started the production of smaller and special series of products. Obviously, those happenings were detrimental to the mass production based on fordist principles.

The implementation of new information and communication technologies further fortified the strike of post-fordist tendencies. Production became flexible enough in order to be able to respond to the market requirements. Manufacturing capacity that played a relevant role in the course of fordism became less important and impulses emanated by the demand side turned into a decisive factor for management of the production. Very often, the pivotal developmental change is depicted as 'from producer's market towards consumer's market'.

Some authors speak about 'industrial divides' that embody the periods of fordist mass production and post-fordist flexible specialisation. According to them, the first industrial divide took place especially after 1920-ies and complies with fordist societal-economic paradigm. The second industrial divide should be perceived as a consequence of economic pressures in 1970-ies and is based primarily on post-fordist categories ([8] or [31]).

As already mentioned, while western economies coped with post-fordist modernising trends in the course of two or three decades, transitional economies are exposed to the modernisation tendencies in a much shorter, compressed period.

III. CZECH REPUBLIC IN THE CONTEXT OF SYSTEM CHANGES IN CENTRAL EAST EUROPEAN SPACE

A. General features of transition in Central East European countries

With the fall of totalitarian political regime in Central East European economies and its replacement by democratic political system the question of economic transformation has arisen urgently. The transition from centrally planned economy to market economy took place never before and consequently, academicians and practitioners missed both theoretical apparatus and practical verifications of this enormously complex process.

These shortcomings were 'enriched' by deformed or practically non-existing institutions, such as market or private ownership. Fifty years of non-democratic regime combined with central planning negatively influenced or even suppressed also numerous informal institutions connected with gradual development in politically democratic societies with market economies. Nonetheless, practically all of these uncertainties or imperfections were considerably reduced by the enthusiasm and optimistic expectations of the population during the first years of transition.

There exists nothing like general theory of transformation so far. It is mainly for the sake of yet unsettled, running process of transition from centrally planned economy to the market economy and from totalitarian political system to the plural political system. Put succinctly, the process of transformation is not and cannot be of absolute nature as it has strong connections with existing as well as newly created institutions.

At the same time, it is not necessary to emphasize the extraordinary range and complexity of system transformations in post-communist countries and the quantity of antagonist opinions that arised in connection with its intensity, depth and sequence of reformatory measures. From this point of view, the clear delimitation of system changes' goal represents the principal part of its conceptualization. [11] states that generally asserted requirement of market is insufficient. Market cannot be the aim, but only the mediator to the reaching of higher economy's productivity. She emphasizes that 'process of the creation of economic minimum that comprises proprietary, political and other social relations, which will determine the framework of societal development in next decades' is the real goal of transformation.

Economists agree that transformation should be composed from the whole set of changes running either concurrently or consecutively in order to replace the unsuccessful state mechanisms by market mechanism. According to [14], the transformation should be perceived as:

- Macroeconomic stabilization accomplished by means of adequate macroeconomic policy,
- Microeconomic liberalization through abolition of administrative control of prices and production and widening the general economic liberty; this involves the release of price regulations, limitations of foreign trade restrictions, changes in the regime of proprietary rights, possibility to launch private business etc.,
- Fundamental institutional restructuring, which consists in the change of existing institutions (privatization of state enterprises, re-organization of public administration etc.) on the one hand and in the formation of new institutions (such as stock exchange, for instance) on the other hand.

[9], [20] or [23] wisely point out that there are two common denominators of transition in Central East Europe: ideal base of transition was inspired by liberal economics and the whole system change was accomplished by means of imperative method. [9] states that there are basically two approaches to the process of system changes:

- 'Imperative method that consists in forcing through the desired changes using the tools available. In this method, the transformation process is an experiment initiated and directed by central authority. For the experimenter, the participants in the system are the active objects of his policy. The aim is to stimulate, using the available means, the desired changes in the mentality and behavior and to adjust them to the new rules of the game. For the experimenter, these rules are self-evident, given, and exclusively correct. However, the objects of his policy need not understand or accept these rules. If they do, the experimenters's task becomes much easier; if they do not, then in order to

accomplish the task (which is a moral, intellectual, and political imperative), he must weaken the resistance of the participants – objects towards these rules. For the experimenter, the rules taken together constitute a coherent vision of social order whose realization will guarantee some kind of desired state of social equilibrium.

- The opposite approach is based on interactive method, which consists in inducing the desired changes by generating a process of social innovation resulting from social interaction. In this method, the central authority, initiating and directing the changes, takes on the role of participant and treats the other participants as independent agents, whose behavior can only change as a consequence of mutual interaction. The task of the central authority initiating the transformation process does not involve establishing certain new system, forcing the participants to respect them; rather it is to stimulate the process of defining and formulating these rules, thus allowing the participants to satisfy their needs and realize their interests. In this process, the role of the ‘central authority’ is also subject to definition and formation by society.’

In Central East Europe, exclusively imperative method of system changes has been applied. At the very beginning of the transformation, International Monetary Fund and World Bank prepared general package for the scenario of reforms in all Central East European countries. This became to be known as ‘Washington Consensus’ and included the set of advices for former post-communist countries that concerned the process of transformation. The most important advices were as follows: opening the economy to world markets, privatisation, price deregulation, currency devaluation, independence of central banks and lowering the taxes. Unfortunately, this conception did not take into account the specifics of particular countries.

The most widely criticized assumptions of the liberal conception of system changes in Central East Europe are as follows:

- Dichotomous thinking, i.e., viewing, at the theoretical level, various elements of social reality and institutional arrangements as antithetical, e.g. plan versus market, state versus society, public domain versus private domain [20].
- Linear approach, perception of system changes as essentially a transition from one system (command economy) to another (market economy) [20] or [23].
- Uniformization, the assumption that all post-socialist countries should embark on the same programme of system changes.

- Rejections of alternatives, the assumption that there exists only one workable programme, or one single path to the market economy (see for instance [16]).

According to [9], the acceptance of afore-mentioned assumptions and assertions has two practical consequences of cardinal importance:

- The supporters of the liberal conception and those who implement it believe that there exist an unambiguous goal of the system transformation and, moreover, they treat the pursuit of this goal as a moral imperative, and their task as a historic mission (see for instance [23]).
- These groups perceive this goal as a technical-organizational operation, in the course of which there should be introduced, by administrative methods, arrangements that would compel individuals, social groups and society as a whole to act in conformity with the preferred model. Should society resist such arrangements, it is perfectly justifiable to resort to coercive means [20].

Not surprisingly, some phenomena appear to be common to many post-socialist economies. Thus, one can contemplate dynamic development of the ‘grey sector’ in transition countries, which adversely affects the security of business transactions and confidence in the rules. Economic decisions are based predominantly on short-term considerations, both in publicly- and privately-run economic units; moreover, a large proportion of the latter lean towards speculations, which reinforces the tendency to shorten the time-horizon of economic decision (see for instance [9]).

B. Central East European countries from economic perspective

Institutionalists generally ascribe rather great weight to initial conditions that determine the developments of economic and other processes. Institutions are always historically-specific and dependent upon previous developments.

The heritage, with which the post-communist world started the process of transformation can be expressed via Index of Initial Conditions. This index is constructed as a weighted mean of 11 economic indicators (see also [4]).

The indicators range from GDP per capita in 1989 to the institution of market memory measured by the number of years of socialism in the given country or the degree of urbanisation. The higher value of afore mentioned index, the better economic starting position of given country at the beginning of system changes. The following table shows Index of Initial Conditions in Central East European countries before the start of system changes.

Table 2: Index of Initial Conditions in Central East European countries [12]

Country	Index of Initial Conditions
Hungary	3.3
Slovenia	3.2
Poland	1.9
Czech Republic	3.5
Estonia	-0.4
Latvia	-0.2
Lithuania	-
Slovakia	2.9
Croatia	2.5
Bulgaria	2.1
Romania	1.7
Russia	-1.1
Ukraine	-1.4

So, according to the Index of Initial Conditions, Czech part of Czechoslovak economy had the best starting position for the accomplishment of system changes. In 1989, the economic performance reached 73% of the level of European communities, 71% of German level, 67% of Austrian level and 49% of American level. However neither Index of Initial Conditions nor above-mentioned numbers tell us anything about the structural strengths and weaknesses of Czechoslovak economy in 1989.

There were several favourable circumstances for the transformation of Czechoslovak economy, such as relatively efficient industry, relatively qualified labour, the lowest indebtedness among all socialist countries, low inflation, full employment, efficient agriculture and relatively good households' equipment with consumers' goods (see [19]).

[5] states that public finances during the socialist period were quite sound. The same applied to the 'monetary policy' of the socialist state bank and the extent of the money supply overhang was rather limited. Czechoslovakia, unlike Hungary or Poland, also had relatively low gross foreign debt (15 percent of GDP at the end of 1989).

On the contrary, Council of Mutual Economic Promotion split up in 1991 and Czechoslovakia lost relatively low demanding markets for its production. One has to consider also more profound deformation of sector structure than in other socialist countries, which was the consequence of the preference of heavy industry in communist past. The next unfavourable factor that weakened the economy consisted in absolute liquidation of private sector in socialist era. Moreover, at the beginning, the long-term disputes about the conception of system changes arose, which led rather to the escalation of the pre-transformational tensions than to the general consent about the way of the accomplishment of system changes.

So, in spite of common socialist heritage and certain commonalities, transitional countries were actually economically rather differentiated already at the beginning of

their transformation. And the same holds true for their institutions.

C. Central East European countries and their institutional-economic peculiarities

Although it is seldom stated, one of the deepest manifestations of the socialist regime in former Czechoslovakia can be found in the sphere of institutions, or more precisely, their depletion. Nationalisation of private ownership brought the oppression of owners' and entrepreneurs' classes. At the same time, it stimulated also the disappearance of the institution of private entrepreneurship with regard to its experiences, habits, morality and ethics. The vanishing of formal institutions driving private entrepreneurship and private sector followed.

These facts become much more apparent if we compare them internationally. Poland, for instance, kept the institution of private sector and private entrepreneurship in retailing and agriculture in the course of the whole socialist period. In Hungary, private sector became supported from the end of 1960-ies in the domains of small entrepreneurship, co-operatives or joint-ventures. The same applied to German Democratic Republic that partly maintained the private production. Czechoslovakia had lower share of private sector on the total production than the Union of Soviet Socialist Republics.

So, Poland and Hungary entered the market economy with certain institutional infrastructure of private entrepreneurship and small but existing know-how. German Democratic Republic finally took the whole institution of private entrepreneurship from its 'big brother', i.e. West Germany. All republics of former Yugoslavia benefited from specific heritage of 'market socialism'. Many Central East European countries thus had a certain entrepreneurial community, corresponding legal norms and mainly informal relations and customs, which enabled the reproduction and further augmentation of private activities.

Czechoslovakia that suppressed private sector in the same manner as its Soviet teacher, was forced to build the whole private sector from nearly-zero basis. Paradoxically, from purely economic perspective, the Czech Republic was number one at the beginning of transformation, from the standpoint of market institutions, the country turned out strongly underdeveloped. Market institutions with all their attributes are built and mature in the course of centuries and after 1989, the Czech Republic tried to resurrect them in a couple of months or years.

Several attempts to measure the quality of institutions has been made in the course of the last decade (see for instance [13] or [6]). World Bank constructed the set of indicators called 'governance indicators' that actually embody the general institutional frameworks in particular countries and are suitable for the purposes of our work.

Six aggregate governance indicators show the way, in which authority in a given country is exercised. All six indicators are composite indicators, i.e. constructed by combining available indices, based on both subjective opinion polls and expert judgements, into an aggregate governance indicator through unobserved component model methodology (for more information, see [6]).

These indicators provide us with cross-country comparisons as well as information about changes in countries' relative positions over time. There are only little doubts that institutional framework in Central East European countries has been driven primarily by the pressure from the European Union. At the same time, one has to take into account that European Union pressure might have influenced primarily formal rules, but only to a limited extent the informal ones, not to speak about the way formal rules are enforced. The Czech Republic can serve as a typical example of such development (see also [6]).

[13] describe the contents of above-mentioned indicators. There are two indicators that are related to the area of 'Political Process', i.e. the process, by which governments are selected, monitored and replaced:

- Voice and Accountability, which measures various aspects of political process, civil liberties, political rights and the independence of the media.
- Political Stability and Absence of Violence that expresses the perception of the probability that the government in power will be destabilised or overthrown by unconstitutional or violent means.

Figure 2 shows the indicator 'Voice and Accountability' that acts as the proxy for the quality of democracy. This indicator is not so differentiated from cross-country perspective, however, the distinction between old and new European Union countries is apparent. Unfortunately, Czech Republic worsened its position between 1996 and 2004.

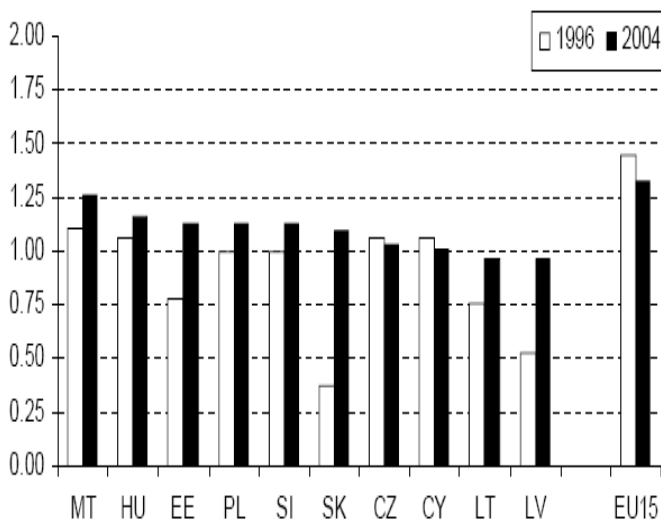


Fig. 2: Voice and Accountability [6]

Political stability and absence of violence turned out to be much more differentiated. Some new member states perform very well, while the position of the Czech Republic, on the contrary, deteriorated again (see Figure 3).

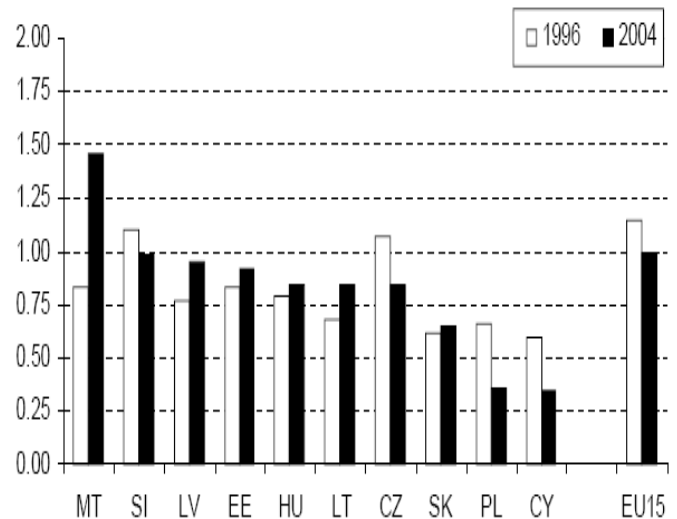


Fig. 3: Political Stability and Absence of Violence [6]

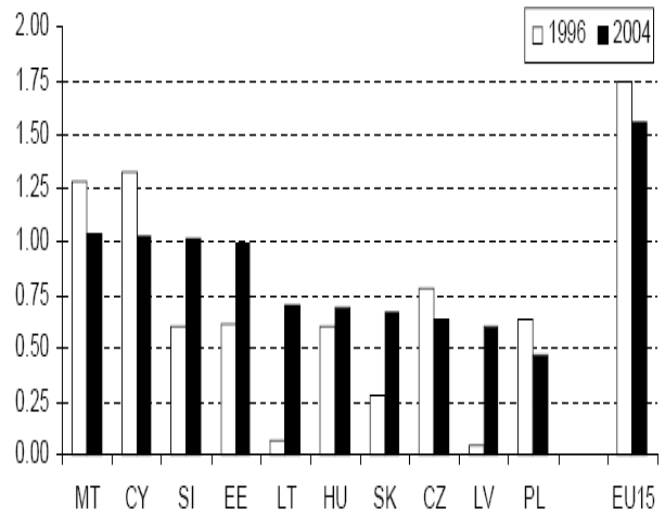


Fig. 4: Government Effectiveness [6]

The next domain called 'Government's Policies' depicts the governmental capacity to formulate and implement sound policies effectively. Again, this area is composed of two indicators:

- Government Effectiveness measures the quality of public service provision, the quality of bureaucracy, the competence of civil servants, the independence of officials on political pressures and

the credibility of the government's commitment to policies.

- Regulatory Quality is on the contrary concentrating upon policies themselves and measures to what extent are the governmental policies market-friendly and what is the perception of the burdens imposed by excessive regulation on private businesses.

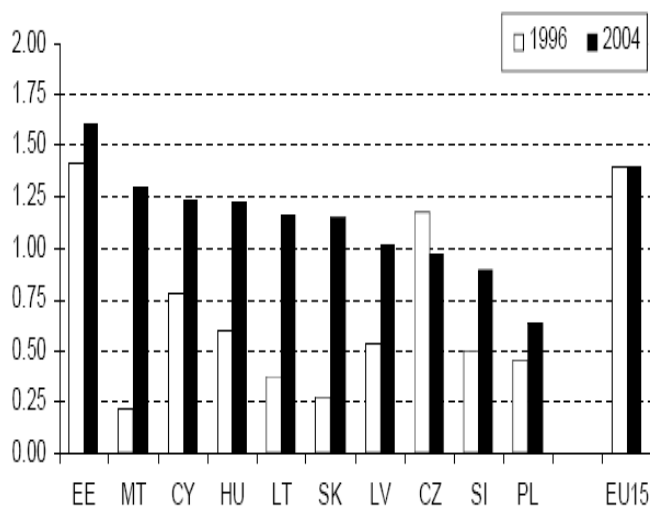


Fig. 5: Regulatory Quality [6]

'Government Effectiveness' indicator shows much lower values in new EU countries. Czech Republic itself belongs among worse countries and moreover, the indicator has an unfavourable tendency in time.

Figure 5 shows that all new EU members improved in terms of 'Regulatory Quality'. The only exception is the Czech Republic, where the indicator declined.

Last but not least, there are two indicators that express 'Respect of Citizens' towards the institutions that govern their interactions. These include:

- Rule of Law representing the degree of confidence individuals have in rules and indicates the perception of the incidence of crime, the effectiveness and predictability of the jurisdiction and the enforceability of contracts.
- Control of Corruption focusing upon the perception of corruption. A great advantage of this indicator is that it ranges from small bribery to big corruption when the private agents corrupt politicians in order to influence the contents of new law and regulations.

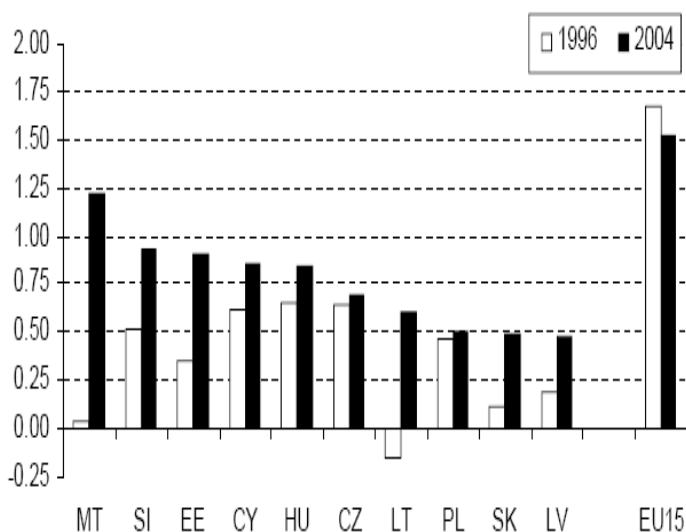


Fig. 6: Rule of Law [6]

As Figure 6 shows, the indicator 'Rule of Law' got much better in practically all new EU member states. At the same time, it has to be underlined that this applies to Czech Republic and Poland only slightly. This just confirms the trend that could be derived from above figures, i.e. qualitatively insufficient institutional environment in the Czech Republic.

As it can be seen in the figure 7, level of corruption constitutes one of the biggest problems of transitional economies. Between 1996 and 2004, the development proved to be strongly heterogeneous, since five countries improved their performance and five of them on the contrary deteriorated their control of corruption. Czech Republic belongs to the group of worst countries.

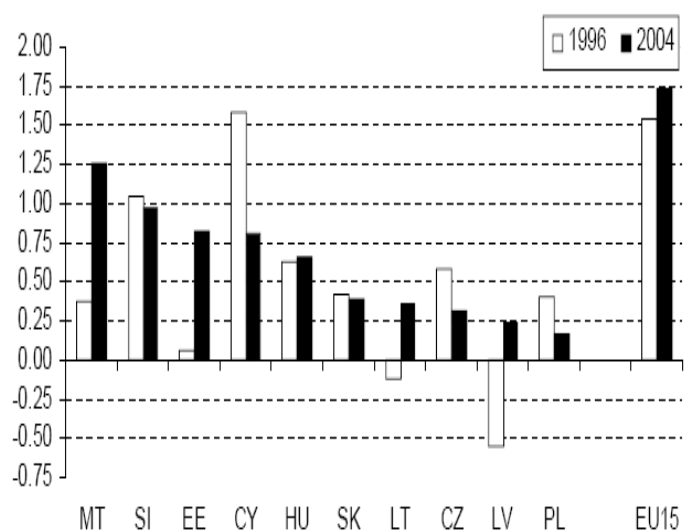


Fig. 7: Control of Corruption [6]

World Value Survey that was conducted between 1981 and 2002 provides us with the value map of the world, sui generis. It represents over 85 percent of the world's population in 81 societies. The results are compressed into the synthetic picture with two dimensions: traditional/secular-rational and survival/self-expression values. The traditional/secular-rational values dimension reflects the contrast between societies in which religion is very important and those in which it is not.

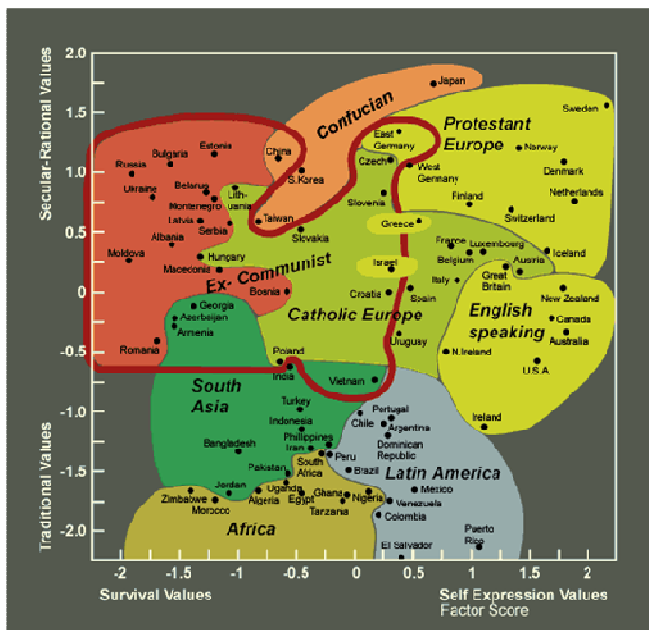


Fig. 8: Inglehart Values Map [36]

It is also apparent that in affluent post-industrial societies priorities have shifted from the stress on economic and physical security towards an increasing emphasis on self-expression and individualization.

In this context it should be reminded that formal institutions can be changed relatively easily; on the contrary, informal institutions that include human behaviour, attitudes, values and habits cannot be changed so quickly and they tend to be more continuous. Their modification is the subject of long-lasting, generational processes.

In other words, informal institutions that evolved in the era of socialism tend to project and reproduce themselves even 20 years after the fall of the Iron Curtain [28]. Undoubtedly, they influenced complex system changes in a profound way (see also figure 8).

IV. COURSE OF TRANSFORMATION IN THE CZECH REPUBLIC FROM A COMPARATIVE PERSPECTIVE

A. General transformation strategies: shock therapy versus gradualism

The debates of the early 1990-ies involved choosing between two essential transformation strategies:

- Shock therapy that preferred shorter transformation path,
- Gradualism giving the precedence to longer, gentle transformation.

The transition in the Czech Republic started at the end of 1990 (see [5], [18] or [24]). Czech Republic can serve as a typical example of the application of 'shock therapy' approach. [5] shows that reform package consisted of quick liberalisation of prices, the sharp devaluation and partial convertibility of the currency, and trade liberalisation. To counter inflationary pressures, the afore-mentioned measures were accompanied by strict fiscal and monetary policy, and a fixed exchange rate. After the period of macroeconomic stabilisation, the process of privatisation was initiated.

According to the supporters of shock therapy, it is first necessary to create private ownership and after that capital market institutions can rise and mature. New owners should be responsible for the restructuring of their enterprises. Price and trade liberalisation in combination with macroeconomic stabilisation should accompany these measures. Quick pace of system changes also causes that people are willing to bear the inevitable costs of transformation. Moreover, speed of reforms should ensure the irreversibility of transformational process.

[17] states that the transition from socialism to capitalism has to be an organic development. According to him, it is a curious amalgam of revolution and evolution. It is a trial and error process that retains or liquidates old institutions and tries out, accepts, or rejects new ones. He prudently underlines that speed of reforms undoubtedly constitutes an important element of transformation in individual countries, however, it cannot be taken as a primary measure of the success. Unfortunately, many actors of post-socialist transformation in the Czech Republic were obsessed with its speed.

[21] notes the main idea of shock therapy consisted in the belief that societal reform from socialistic economy toward capitalist market economy should be accomplished as quickly as possible. The actors of economic life would be thus forced to adapt to new economic circumstances in the short run. Nonetheless, it was entirely omitted that there exist institutions, which substantially form the socio-economic conditions. Actually, neoliberal doctrine that formed the course of transformation in the Czech Republic does not take into consideration the institutions (see for instance [21]).

[25] or [26] claims that nowadays there is wide consensus that shock therapy failed and that countries like Hungary, Slovenia or Poland that underwent gradual privatisation and reconstruction of institutional infrastructure coped with transformational challenges much better than countries that attempted to jump directly into economic laissez-faire. It is worth to remind that in comparison to some of its neighbours, the Czechoslovak government faced relatively favourable conditions for instituting the reforms (see also [5]).

Gradual strategy generally claims that transformation of the economy is long run process by its nature. Its supporters are scared of the costs connected with economic decline caused by shock therapy. In order to prevent the economy from the decay, they strive for the division of transformation into longer

periods. Moreover, they are convinced that transformation should be directed by the state.

Market liberalisation should be accomplished also gradually. The main intention is that economic actors should not be exposed to economic shocks. Therefore, drastic stabilisation measures are not necessary and enterprises are not exposed to them. Private sector accrues gradually, evolutionary, via successive privatisation of state enterprises.

Table 3 shows the cross-country comparison in index of liberalisation. This index is composed of the weighted average of three components:

- liberalisation of domestic market (weight 0.3),
- foreign trade liberalisation (weight 0.3),
- privatisation and banking reform (weight 0.4).

The values of index range from 0 to 1. The higher value of index, the more liberal economy (see also [3]).

Although the Czech Republic (former Czechoslovakia) had economically the best position among other Central East European countries, its economy was the ‘most socialist’. For instance, in contrast to the other former socialist countries, the institution of private entrepreneurship was entirely suppressed. Index of liberalisation confirms that the country actually acted as the most eager and diligent pupil of Soviet system.

In 1997, we get sharply different picture. Czech Republic accomplished the shock therapy intensely and got ahead of all other Central East European countries in terms of liberalisation in a couple of years. There is striking similarity with the previous period and the country can be grasped as the best pupil of Washington consensus.

Table 3: Index of Liberalisation [12]

Country	Index of Liberalisation	
	1989	1997
Hungary	0.34	0.93
Slovenia	0.41	0.89
Poland	0.24	0.89
Czech Republic	0	0.93
Estonia	0.07	0.93
Latvia	0.04	0.89
Lithuania	0.04	0.89
Slovakia	-	0.86
Croatia	0.41	0.85
Bulgaria	0.13	0.79
Romania	-	0.75
Russia	0.04	0.83
Ukraine	0.04	0.65

From the economic standpoint, complex transition process caused that numerous transition countries witnessed more or less profound decline in the first years of transformation. After a certain time, all of them upturned the economic decay and their GDP started to increase again. This is in compliance with economic transformation ‘J-curve’. Diverse attributes and aspects of Czech economy were painstakingly depicted for instance in [7], [27] or [30].

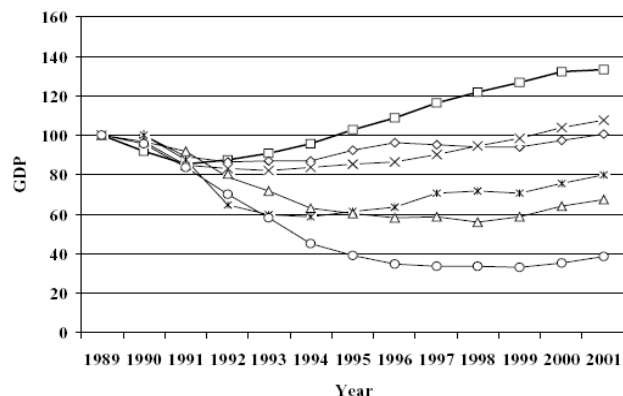


Fig. 9: Real GDP in Chosen Transition Economies (1989=100) [10]

Fig. 9: Real GDP in Chosen Transition Economies (1989=100) [10]

This initial economic ‘tightening the belts’ was facilitated also by afore-mentioned optimistic mood of the population full of positive expectations. It is worth noticing that while the economic situation in transition period in the Czech Republic was not a pink one, it was still good enough in comparison with some countries from Eastern part of Europe.

However, it has to be underlined once again that the measure of economic growth in itself tells us only a little about the institutional aspects of the transition in the analysed country.

B. Privatisation as a basis of transformation

Privatisation can be perceived as one of the most relevant transformational steps. Its course in the Czech Republic was primarily influenced by the fact that since 1990, radical neoliberal reformists had a major impact on the transformation in Czechoslovakia. Privatisation has been regarded by the radical reformers as transformation itself and the process of privatisation had to be implemented with all speed and power.

Since there existed almost complete nationalisation of the economy in former Czechoslovakia, the starting position of the country was worse than the position of Hungary or Poland, where private sector somehow survived. The official efforts to accomplish the privatisation as soon as possible brought the problem of absent owner or inefficient owner (see [21] or [14]).

System, when the primary aim was to find the first but not the final owner in combination with unfavourable legislative and institutional-moral environment could not lead to the formation of real proprietary responsibility of owners. Overmuch speed of system transformation and privatisation in the Czech Republic endangered its institutional quality.

It was argued that fast privatisation is necessary because of state’s inability to manage the enterprises strategically as well as its unwillingness to restructure the individual enterprises.

The architects of economic transformation in the former Czechoslovakia were convinced that successful privatisation would guarantee the irreversibility of the transformation process. At the same time, Czech privatisation bore a couple of specific domestic features. Voucher or coupon scheme as a non-standard method of privatisation is their typical representative (see also [21]).

Moreover, the preparation of privatisation was deeply (and it is questionable to what extent deliberately) underestimated and hectic pace was its typical sign. Table 4 presents the rapid augmentation of percentual share of non-state sphere on the creation of GDP in the Czech Republic.

Table 4: Share of Non-state Sphere on the Creation of GDP (in %) [19]

Year 19xx	91	92	93	94	95	96	97
Percentage Share of Non-state Sector	17	28	45	56	67	75	80

Reformists claimed that economists should be ahead of lawyers and that proper legislation will crystallize after the economic transformation itself. [21] describes this phenomenon as vulgar or uncomprehended neoliberalism and the privatisation is frequently depicted as privatisation under switched-off light.

The following table shows the volume of property that has been privatised until 1996. It is worth noticing that in spite of huge financial amounts and property transferred during the privatization there exist mere rough estimations about the volume of property that was actually privatized.

Small-scale privatisation and restitution created the first phase of privatisation. They turned out to be relatively efficient, however, people that had the chance to accumulate the finance and property already during socialistic era, enjoyed much better starting positions. During 1991 and 1992, approximately 1.5 million people became entrepreneurs. Due to the legal hindrances, original owners or their heirs could retrieve their property often rather uneasily.

Table 5: The Volume of Property Privatised until 1996 according to the Method of Privatisation [15]

Method of Privatisation	Volume of Property (in Billiards of CZK)
Restitutions	70-120
Transfer of Property from the State to Municipalities	Over 350
Small-scale Privatisation	23
Large-scale Privatisation	626
Transformation of Co-operatives	200-250
Total Value	1269-1369

On the contrary, large-scale privatisation proved much more controversial. Large-scale privatisation was accomplished partly by means of direct sales. On the one hand, the government succeeded in selling a few large enterprises to foreign investors that were able to raise the competitiveness of these enterprises; on the other hand, Czech owners of large enterprises whose privatisation was financed by Czech bank loans failed to create appropriate corporate governance and restructure their property. Some of the privatised enterprises thus went bankrupt and others could be saved only via huge governmental subsidies.

Voucher privatisation that became one of the most distinctive features of the whole transformation process, finally brought a strong disenchantment. The large portion of shares generated through voucher privatisation was acquired by several influential investment funds. The principal problem consisted in the fact that strongest investment funds were established by largest state-owned banks, namely by so-called 'Big Four' (Komerční banka, Česká spořitelna, Investiční a poštovní banka and Československá obchodní banka). These banks were scared of any bigger enterprise restructuring for the sake of negative impact on their loans. More importantly, asset stripping became common practice performed by managements of big enterprises.

The afore-mentioned state was often rightly referred to as 'banking socialism'. [21] or [14] show that all of these unfavourable phenomena finally led to the creation of so-called cross-ownership that later caused a vicious circle and formidable problems in corporate governance and enterprise restructuring. Typical negative consequences of system changes, such as low enforceability of law, lack of business ethics, overloading of courts with lawsuits, low efficiency of justice, mutual indebtedness of big enterprises, damage of social capital or asset stripping manifested themselves in two essential forms:

- transformation of powerful communist structures to even more powerful post-communist ones on the one hand and
- costs connected with badly performed transformation that reached several hundreds billions of Czech crowns (see also [21]) on the other hand.

C. Underestimation of institutions in transitional Czech Republic

In the light of previous paragraphs, it is not surprising that evaluation of the institutional framework of transition in the Czech Republic is often a gloomy one. It has to be underlined that transition of post-communist countries was a big laboratory experiment that tested what is the level of applicability of mainstream economic theory to the transition process. Washington consensus itself that delimited general features of system changes in all Central East European countries became the target of heavy criticism (see for instance [25]).

Czech experience raises the doubts and embarrassments namely about:

- Conviction that economic reform is more important than the cultivation of legal order and social capital,
- Belief that a fast privatisation is better than a gradualist approach,
- Proposition that privatisation is prior to the solution of the problems of employment and of new workplaces stemming from emphasizing economic stabilisation over economic growth (see also [21]),
- Conviction that geographical dimension of transformation does not matter (see also [22], [29], [31], [34] or [35]).

The transition from ‘socialism to the market’ took place in a legal vacuum and with unfavourable institutional load from the past. The ideology of radical liberalism was intensely combined with nationalistic principle that Czech assets should remain in the Czech hands, which was quickly utilized by the old elites that reproduced their former political power into economic-political influence.

Technocratic concept of economy stressing that economic system can be based merely on self-interest led to the dominance of pragmatism, utilitarianism and opportunism. The neglect of moral dimension in combination with the conviction that economists should be qualitatively ahead of lawyers finally led to the cruel finding that underestimation of institutions is rather costly.

Last but not least, system changes in the Czech Republic were strongly path-dependent on former socioeconomic structures and rules. At the same time, distorted liberal doctrine that delimited the space for the accomplishment of system changes in the Czech Republic actually built the essential stage for current and future socioeconomic structures and activities. Hence, the future socioeconomic development of the country will reflect the playground created during the first years of the transformation and will be path-dependent on the system changes that turned out to be not entirely harmonic.

V. CONCLUSIONS

From western point of view, transitional post-communist countries bore a great resemblance in both economic and institutional terms. However, as it has been shown, the homogeneity that could be perceived from outer point of view turned out to be mere illusion. A thorough analysis disclosed that transitional economies actually create rather peculiar and mutually strongly heterogeneous entities.

The dissimilarities among individual countries applied not only to basic geographical characteristics, such as country's area or its number of inhabitants, but already to the initial pre-transformational economic and institutional conditions. Czech part of common Czechoslovak economy enjoyed practically

the best starting conditions for the accomplishment of system changes.

While from purely economic standpoint Czechoslovakia occupied exclusive position among all transitional countries, its market institutions on the contrary did not practically exist. The country turned out to be most distant from real market conditions in the whole Central East Europe. Non-market and isolated character of Czechoslovak economy was systematically supported by rigid and strictly hierarchized system of central planning that permitted practically no exceptions. Last, but not least, socialist era beset pretty negatively also country's informal institutions.

As for the course of the transformation itself, Czech Republic serves as excellent example of the application of ‘shock therapy’ approach. Moreover, this ‘shock therapy’ has been used (or rather misused) in a rather peculiar way, when economists were always at least one step ahead of lawyers. At the same time, institutional dimension of transition has been disregarded. Hence, unfavourable informal institutions inherited from socialism manifested themselves markedly and insufficiently defined and almost unenforceable formal institutions could only hardly protect the economic-social order.

The realm of problems depicted above was typical for virtually all post-communist countries, however, in contrast to the Czech Republic, these countries largely chose more gradual and prudent way of system changes. It is worth noticing that former Czechoslovakia acted as the most eager and diligent pupil of Soviet socialist system and applied it so strictly, that market institutions and consciousness almost disappeared. On the other hand, striking similarity with socialist period could be contemplated also in the course of transformation, when Czech Republic applied the most liberal and hasty approach to the transition, for which almost total omission of transformational institutional framework became symptomatic. Formidable costs of transformation and reproduction of old economic-political elites into renewed, post-socialist ones became symbols of Czech transition, sui generis. Extreme changes, which are typical also for the whole Czech history, thus became also the typical sign of country's recent economic development.

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