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Recovery Growth as a Stage of Post-Socialist Transition?

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Yegor Gaidar

Yegor Gaidar received a Ph.D. in economics from Moscow State University in 1980. When the USSR dissolved in 1991, Mr. Gaidar began a distinguished career in government. He served in a number of positions from 1991 to 1993, including: Deputy Chairman of the Russian Federation, responsible for matters of economic policy; Minister of Economy and Finance; Acting Chairman of the Russian Federation government; Counselor to the President of the Russian Federation; First Deputy Chairman of the Russian Federation government; and Acting Minister of Economy of the Russian Federation. In 1993 and again in 1999 he was elected to the State Duma. In the period 1993-2003 he was active in politics, serving, inter alia, as Chairman of the Democratic Choice of Russia Party. In 2003, he returned to the directorship of the Institute for the Economy in Transition, where he remains today. Yegor Gaidar has published several books and over 100 articles on economic reform and post-communist transition.



Abstract

Unfolding in 3-7 years after the collapse of socialism, economic growth at its first stage has a recovery nature. It appears secured by a new system of market institutions that provide other than under socialism fundamentals allowing for a reorganization of economic relations and boosting volume of output of goods and services that enjoy effective demand. At the recovery growth stage, the post socialist governments' mission should be casting preconditions for the transition from recovery growth stage to investment-based growth, with the latter basing on capital investment and creation of new production capacities. The major challenge today is promotion of reforms to ensure a sustainable long-term growth, and laying down socio-economic fundamentals of the post-industrial society. This determines the core of the ongoing transformation and the main challenge that almost all post-socialist countries will be facing over next decades.

Complexity of post-socialist transition is unprecedented; at the initial stage no one could forecast precisely within what time-limits and to what extent such objectives would be implemented and foresee all the obstacles and dangers on that way.

For instance, when the Solidarity's victory at the 1989 elections had opened up a 'window of opportunities' for Polish reformers, it was impossible to assess the extent of problems which needed to be solved and foresee the difficulties which would arise in the period of adaptation to market conditions. At present, however, the stage of transformational recession, as well as debates on the causes and consequences thereof are mostly left behind. Economies of post-socialist countries are characterized to a great extent by a sustained growth and effective market mechanisms.

Generally, transformational recession can be explained as follows: collapse of the socialist economic structure has revealed a regrettable factor that most economic activities which were carried out under a command economy would never be required in market conditions and democracy. Reallocation of labor resources concentrated in those activities cannot be done overnight. Processes which took place at the stage of post-socialist recession were similar to those defined by J. Schumpeter as 'creative destruction'. However, their scale has been unprecedented for market economies. It is to be realized that both post-socialist recession (adaptive recession) and subsequent recovery are a single process which consists in structural transformation of the economy².

In different countries that process has taken different forms.

Polish reformers who were the pioneers of post-socialist transformation made an emphasis on immediate price liberalization, opening up of the economy, convertibility of a national currency and rapid disinflation through measures of monetary and fiscal policies, wage control and structural reforms aimed first and foremost at privatization (a combination of the above measures was generally called a 'shock therapy'). Other countries, for example Romania, preferred an evolutionary way, while a third group of countries – an intermediary way. For instance, Russia tried to carry out a shock therapy, but under the pressure of populist forces backtracked to gradual reforms seen by some as 'moderate'. With results being different (they are obviously better in the first group of countries and worse in the second group and the third group), the overall picture of economic development has appeared surprisingly similar: at first, deep economic recession (less severe in the first group and more dramatic in the second and third groups) and then a gradual economic recovery (first observed in the first group and then, in the second and third groups). See Fig. 1 and Fig. 2.

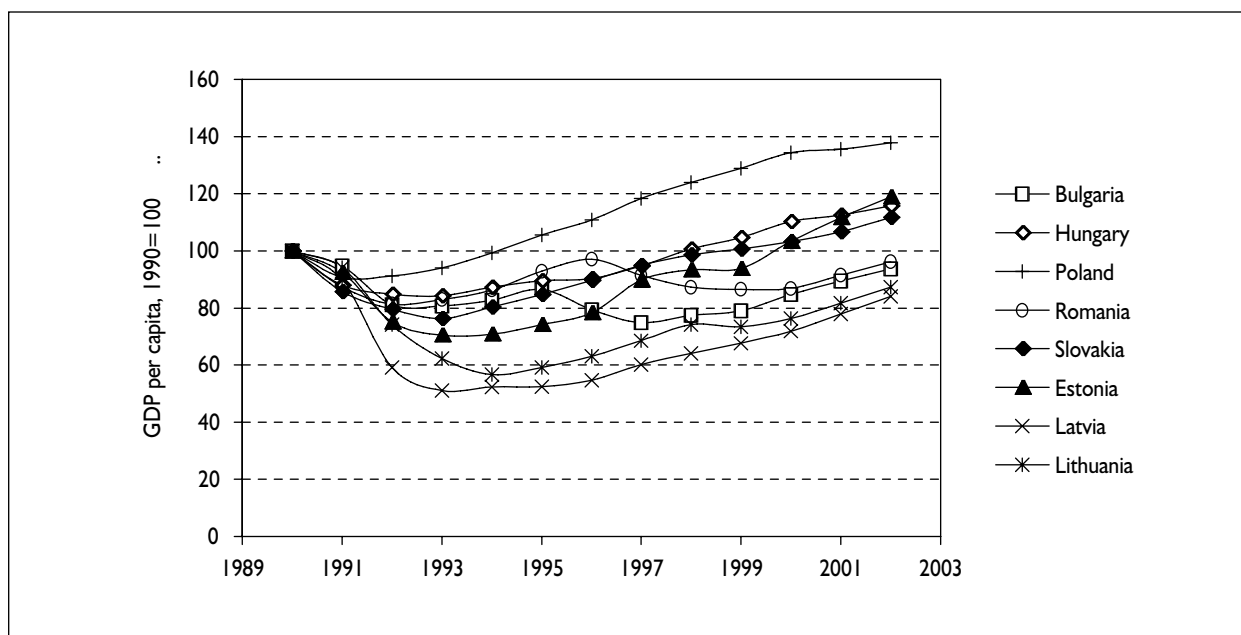
At present, with recession left mostly behind it is expedient to focus on issues related to economic growth. As regards Russia where growth has been observed since 1999, there are two principal points of view on that issue. The first one underlines political stabilization and structural reforms following V. Putin coming to power³.

¹ Schumpeter J.A. Capitalism, Socialism and Democracy. New York: Harper & Brothers Publishers, 1950. P. 81.

² Describing the specifics of transformational recession as compared to normal recessions in market economies, J. Kornai points out the following two specific factors: a need for transfer from the market of the seller to the market of the buyer and introduction of hard budget constraints (see: Kornai J. Transformational Recession: The Main Causes // Journal of Comparative Economics. 1994. Vol. 19. P. 39-63). O. Blanchard defines the key processes of the post-socialist transition as a combination of the two elements: reallocation of resources from the old types of economic activities to the new ones (closing of enterprises and their bankruptcy in combination with establishment of the new ones) and restructuring of the most important companies (innovation, change in the structure of production and new investments) (see: Blanchard O. The Economics of Transition in Eastern Europe. Oxford: Clarendon Press, 1997). On factors behind recession at the early stage of post-socialist transition and their effect on the need for change in the structure of production (to reflect an effective market demand) and imposition of hard budget constraints see: Havrylyshyn O., Izvorski I., Rooden R.V. Recovery and Growth in Transition Economies 1990-1997: A Stylized Regression Analysis // IMF Working Paper. WP 98/141. September 1998. P. 10-13.

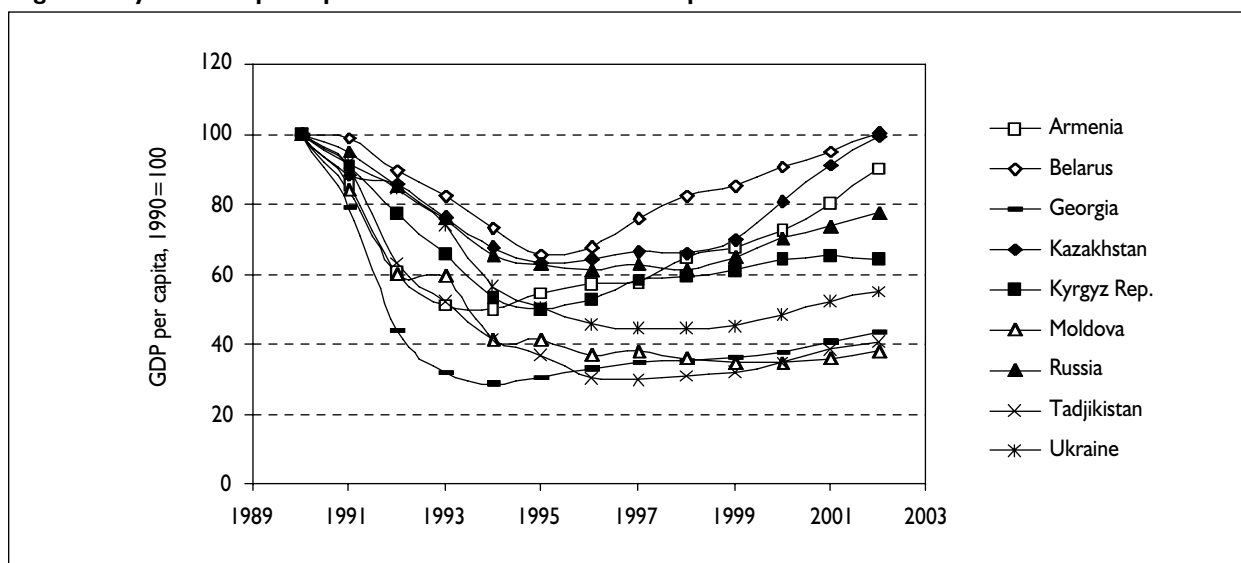
³ See e.g. N. Fedorenko. Russia at the Turn of the Century. Moscow. Ekonomika, 2003. pp. 54-57.

Figure 1. Dynamics of per capita GDP in the Central and Eastern European Countries and Baltic States in the period 1990-2002



Source: International Financial Statistics, IMF 2004.

Figure 2. Dynamics of per capita GDP in the CIS states in the period 1990-2002



Source: International Financial Statistics, IMF 2004.

The second one denies the government's merits and links growth to high oil prices and depreciation of the ruble⁴. However, there is still another point of view on that issue which is most justified, but, unfortunately, not presented at all. Economic growth is a direct consequence of the reforms which have been carried out and a result of new more effective macro-and-microeconomic conditions in which both

⁴ Berglof E., Kunov A., Shvets J., Yudaeva K. *The New Political Economy of Russia*. London: The MIT Press, 2003; Gaddy C.G. *Has Russia Entered a Period of Sustainable Economic Growth?* // Kuchins A.C. (ed.). *Russia After the Fall*. Washington, D.C.: Carnegie Endowment for International Peace; [distributor] Brookings Institution Press, 2002. P. 125-144; Ellman M. *The Russian Economy under El'tsin* // *Europe - Asia Studies*. 2000. Vol. 52(8). P. 1421; A. Aslund. *Building of Capitalism: Market Transformation of the Former Soviet Bloc Countries* / Edited by I. M. Osadchy. p. 37. It is to be noted that a very reference to depreciation of the ruble as a factor behind economic growth suggests that market motivation in the Russian economy has started to work.

Russian and foreign companies operate. Most importantly, participants of those debates ignore, as a rule, experience of nearly thirty countries which, like Russia, try to adapt themselves to conditions of development after the collapse of socialism⁵. It is clear that at present economic growth is observed in all the post-Soviet states (Table 1).

As stated above, recession was observed in all the post-Soviet countries in the period 1991-1994. From 1995, the first indicators of economic growth become evident primarily in those countries (especially, where preceding recession was rather deep) which had been involved in wars or subjected to an economic blockade. Within the next two to three years, unsteady growth spread over to other parts of the post-Soviet territory⁶.

Finally, in 1999 growth stabilized and a year later became widespread⁷.

Among post-Soviet states, there are net exporters and net importers of oil and oil products, as well as countries whose national currency either appreciated or depreciated in the period 1995-2002 (see Table 2). None of those countries have ever started such reforms as were carried out in Russia in the period 2000-2003. However, nearly all of them are regarded as countries with growing economies.

Table 1. GDP growth rates in post-Soviet states in the period 1996-2003, % change

Country	Year	1996	1997	1998	1999	2000	2001	2002	2003
Azerbaijan ¹		1.3	5.8	10.0	7.4	11.1	9.9	10.6	11.2
Armenia ¹		5.9	3.3	7.2	3.3	5.9	9.6	12.9	13.9
Belarus ¹		2.8	11.4	8.3	3.4	5.8	4.7	5.0	6.8
Georgia ¹		11.2	10.5	3.1	2.9	1.8	4.8	5.5	8.6
Kazakhstan ¹		0.5	1.7	-1.9	2.7	9.8	13.5	9.8	9.2
Kyrgyzstan ¹		7.1	9.9	2.1	3.7	5.4	5.3	0.0	6.7
Moldova ¹		-5.9	1.6	-6.5	-3.4	2.1	6.1	7.8	6.3
Russia ¹		-3.6	1.4	-5.3	6.4	10.0	5.1	4.7	7.3
Tadjikistan ¹		-6.7	1.7	5.3	3.7	8.3	10.2	9.5	10.2
Uzbekistan ¹		1.7	5.2	4.4	4.4	3.8	4.5	4.2	...
Ukraine ¹		-10.0	-3.0	-1.9	-0.2	5.9	9.2	4.8	8.5
Latvia ²		3.8	8.3	4.7	3.3	6.9	8.0	6.4	-0.7
Lithuania ²		4.7	7.0	7.3	-1.7	3.9	6.4	6.8	9.0
Estonia ²		4.5	10.5	5.2	-0.1	7.8	6.4	7.2	5.1

Sources: ¹ The International Statistics Board of the CIS macroeconomic indices.

² International Financial Statistics, IMF 2004.

If in the early 1990s production decreased in nearly all the post-Soviet states, while by the end of the decade it started to grow, there are ample reasons to justify the above idea: both recession and subsequent growth are components of a single process which is determined by common historical and economic regularities. It depends only to a small extent on persons and parties which came to power in one or another country in that period.

At the initial stage of post-socialist transformation, more resources (than required by the market) are released from the non-market sector; their volume exceeds actual demand. By the time demand of a

⁵ L. Aron has paid attention to the fact that all the processes of post-socialist transition in most countries of Eastern Europe and in the post-Soviet territory are normally studied in a comparative context against developments which take place in other post-socialist countries, while Russia (because of its vast territory) is often studied individually. (See: Aron L. Structure and Context in the Study of Post-Soviet Russia: Several Empirical Generalizations in Search of a Theory // Russian outlook. January 1. 2001). The same idea is underlined by P. Sutela (See: Sutela P. The Russian Market Economy. Helsinki: Kikimora Publications, 2003. P. 7, 8).

⁶ One can associate GDP growth in CIS in 1993-2003 with growing prices on Russian, Kazakh and Azerbaijani oil, which in turn promoted growth in other CIS countries exporting to oil producers. However, a sustained decrease of the share of Russia and other oil producers in the foreign trade of non-oil-producing CIS countries seriously weakens the above hypothesis (see: Havrylyshyn O. Transformation of Post-Communist Societies: What Happened, Why it Happened and What Next? Unpublished manuscript provided by courtesy of the author).

⁷ Kyrgyzstan, where growth slowed down in 2002, was an exception. A natural disaster brought the largest gold-mining enterprise to a virtual standstill for a few months. In 2003, economic growth resumed.

Table 2. Index of the real exchange rate of national currencies * to the US Dollar in post-Soviet states as of the year-end. The year 1995 = 100%

Country	1996	1997	1998	1999	2000	2001	2002	2003
Azerbaijan	126.1	134.5	131.5	104.5	98.7	93.1	92.0	...
Armenia	106.6	104.2	105.8	103.9	94.5	93.2	89.1	94.3
Belarus	110.1	88.9	43.9	56.0	39.5	46.2	53.3	59.6
Georgia	130.1	134.0	98.7	107.4	105.4	103.1	105.6	...
Kazakhstan	117.9	131.3	124.9	80.3	84.0	85.2	86.2	96.2
Kyrgyzstan	86.0	99.6	64.1	55.1	59.5	62.7	65.2	68.9
Latvia	110.2	110.8	118.2	116.4	109.9	104.4	113.6	124.9
Lithuania	121.1	128.8	133.3	131.4	128.4	126.5	150.9	174.0
Moldova	113.2	119.7	70.4	72.2	85.8	86.6	85.1	97.2
Russia	119.8	125.3	45.5	63.2	70.8	78.1	84.5	101.3
Ukraine	165.9	187.0	112.8	89.0	106.1	118.3	116.7	120.1
Estonia	110.1	103.2	117.6	102.5	95.4	93.3	112.6	134.3

* USD per unit of national currency.

Source: International Financial Statistics, IMF 2004.

market sector for resources have exceeded supply originated from the non-market sector, transformational recession stops and recovery growth begins⁸.

Total factor productivity⁹ in post-socialist transition starts to grow earlier than the total output. In Russia, it has started to grow since 1995. The 1997-1998 financial crisis brought about only insignificant fluctuations in the dynamics of that index¹⁰. Recovery growth discontinued from time to time, primarily due to financial and economic crises, but there have been fewer instances of that in Eastern Europe (since the mid-1990s) and the Baltic States (since the late 1990s).

The term "recovery growth" was introduced by Russian economist V. Groman in the 1920s¹¹. According to his theory, recovery process uses earlier created production capacities. To launch a mechanism of recovery growth, it is important to stop disorganization of the economy and rebuild economic relations. V. Groman noted that despite destruction and loss of material resources as a result of the civil war economic recession was caused to a greater extent by disruption of economic relations, rather than by the above factors¹². By restoring economic relations, it would be possible to engage production capacities and start the process of recovery growth.

Comparing recovery growth in the 1920s with that of the present day, it is important to pay a particular attention to the following two factors: first, resources of extensive (recovery) growth are almost exhausted and, second, the extent of the role played by finances in recovery of the economy and dynamics of the financial situation.

⁸ The most interesting works dedicated to analysis of post-socialist recession and subsequent growth include: De Melo M., Denizer C., Gelb A. From Plan to Market: Patterns of Transition // Blejer M.I., Skreb M. (eds.). Macroeconomic Stabilization in Transition Economies. Cambridge: Cambridge University Press, 1997. P. 17-72; Berg A., Borensztein E., Sahay R., Zettelmeyer J. The Evolution of Output in Transition Economies: Explaining the Differences // IMF Working Paper. WP 99/73. 1999; Havrylyshyn O., Wolf T. Growth in Transition Countries. 1991-1998. The Main Lessons. Paper Presented at the Conference «A Decade of Transition», International Monetary Fund. Washington, D.C. February 1-3, 1999; A. Aslund. Building of Capitalism: Market Transformation of Countries of the Former Soviet Block / Edited by I.M. Osadchy. Moscow: Logos, 2003.

⁹ Total factor productivity is defined as a ratio of the aggregate output to the aggregate costs. Growth in total factor productivity (or output per unit of costs) is related to growth in efficiency justified by technical progress and better organization of production.

¹⁰ Factors of Economic Growth in Russian Economy: Treatise No. 70 P.M.: IET, 2003. p. 66, 138.

¹¹ V. Groman. On Some Regularities in National Economy Established Through Experiments // Planned Economy 1925. No. 1, 2. The same issue was actively studied by V. Bazarov (see: V. Bazarov. On "Recovery Processes" in General and «Issuing Possibilities», in Particular // Ekonomicheskoe Obozrenie. 1925. No. 1; By the same author: Prospects of Development of the National Economy in 1925/1926). The issues of recovery growth discussed by the above authors are also considered by V. Mau in his work (See: V. Mau. Reforms and Dogmas: 1914-1929. Moscow. Delo, 1993).

¹² See: V. Groman. On Some Regularities in National Economy Established Through Experiments p. 101.

Exhaustion of resources of recovery growth is not identical to the achievements of the pre-crisis level of production. In mid – 1920s, that mistake was made by researchers of "recovery regularities". Market economy (as Russian economy was in 1913) normally has reserve capacities. After the pre-crisis level had been attained, engagement of such capacities in production permitted for some time to maintain high rates of growth. B. Bazarov and V. Groman paid a high price for that mistake; they were charged with willful anti-Soviet activities and an attempt to halt "socialist restructuring"¹³.

A different situation took place in post-communist Russia. The Soviet Union was overloaded with production capacities aimed at meeting artificial demand which was formed by means of centralized state planning. As the national economy was a closed one it was possible to maintain demand on low-quality products. In addition to that, those products were imported by satellite countries against loans advanced by the Soviet Union on a virtually free of charge and irrevocable basis. Some capacities which have survived the collapse of the socialist system could not be used at all. In that situation, completion of recovery growth is to take place long before the 1989 level of the GDP is attained.

It is important to avoid illusions that pre-crisis levels of production and monetization of economy are attained at the same time. Experience has shown that it is unjustified to apply the logic of "recovery commensurability" to the analysis of financial problems.

In the period 1917-1923 of extremely high inflation, the extent of monetization of economy in Soviet Russia had decreased dramatically. V Groman and B. Bazarov supposed that with the beginning of recovery processes the demand for money would promptly grow and it would permit (without a risk of inflation) to increase considerably credit expansion to national economy. The above assumption was used as a basis of calculations of planned targets for the years 1925-1926¹⁴. The hypothesis was never confirmed.

The cause of this error could be explained by the very nature of recovery growth. Methods normally used in GDP forecasting in a relatively stable periods are not applicable to analysis of this kind of a growth phenomenon.

In 1920s, the extremely high growth rates at the initial stage of economic recovery were unexpected both by experts and the political elite. None of the experts of the State Planning Committee expected the rates of growth to be that high¹⁵ in the period 1923-1924 after the monetary reform had been carried out and the currency stabilized. It was believed that by 1927, thanks to economic growth alone (with no capital investments made), national income of the Soviet Union would amount to nearly 50 percent of Russia's national income of the last pre-war year¹⁶. But the reality exceeded all those expectations; over that period the Soviet Union caught up with pre-war Russia as regards national income. Though the data of that period is rather controversial (the index in question is estimated within the range of 90 percent to 110 percent of the 1913 GDP level) the overall picture remains unaffected¹⁷.

A similar situation has been observed recently. In 1999, the Russian government believed that in 2000 GDP would increase only slightly (by 0.2 percent) or even fall (by 2.2 percent). The International Monetary

¹³ V. Molotov: "Bazarov admits that real life refutes his theory of "a decaying curve"". J. Stalin: "Really?!" V. Molotov: "Only two years ago Bazarov wrote a book with a great number of tables and diagrams in which he tried to assert quite the opposite. Now, he renounces his "research"" (see: *How the New Economic Policy (NEP) was Liquidated: Records of Plenums of the Central Committee of VKP(b) in 1928-1929* / Edited by A.N. Yakovlev. Vol. 5. Moscow.: *Rossia XX vek; Materik*, 2000. p. 219).

¹⁴ *Planned Targets of the National Economy for the 1925-1926 Period. Report of the Commission on Planned Targets approved by the Presidium of the State Planning Committee of the USSR. Moscow.; L.: Planned Economy, 1925.*

¹⁵ See: V. Groman. *Survey of the National Economy of the USSR in the First Six Months of 1924 and 1925 // Planned Economy, 1925. No. 6.*

¹⁶ Davies R.W, Harrison M., Wheatcroft S.G. (eds.). *The Economic Transformation of the Soviet Union, 1913-1945. Cambridge: Cambridge University Press, 1994.*

¹⁷ On different evaluations of correlation between the GDP of the Soviet Union and that of Russia in the 1913-1928 period, see: L.B. Kafengaus. *Evolution of Industrial Production in Russia (the last thirty years of the 19th century and the first 30 years of the 20th century) Moscow, 1994. Pp. 172-197; The National Economy of the RSFSR in the Past 60 Years. Moscow, 1977. p. 23, 46-48; N. Fedorenko *Russia at the Turn of the Century. Moscow, 2003. p. 121, 122.**

Fund forecasted GDP growth of 1.5 percent. In fact, the Russian GDP increased by 9 percent in 2000, while industrial production rose by 11 percent. In Ukraine where in 2001 the GDP real growth amounted to 9 percent, the IMF forecasted a mere 3.5 percent growth¹⁸.

Recovery growth with its particularly high rates at the initial stage comes unexpectedly and is taken as a gift. Then, less desirable specifics of recovery growth become more apparent: it is of a decaying nature¹⁹. Recovery growth is ensured by existing production capacities²⁰ and trained labor force. But in any country such resources are not unlimited. So, after a dramatic initial take off, the rates of growth tend to decline. Such a situation was observed in the USSR in the 1920s and was repeated in Russia in the period 2001-2002.

The highest rates of recovery growth at its initial stage determined expectations vis a vis the economic policy. In the 1920s, the prime objective consisted in prevention of a slow-down (caused by the logic of recovery processes) in the rates of the growth. In the period 1925-1926 efforts to increase capital investments in order to speed up economic recovery resulted in monetary expansion, price growth and emergence of a trade deficit. However, despite those negative phenomena, reserves of economic recovery were still preserved. The Soviet government tried to overcome inflationary tendencies²¹

In the period 1927-1928, a new effort to speed up economic growth was made in a different situation, where main reserves of recovery processes had been exhausted and rates of growth declined²². The government tried to tackle newly emerged financial imbalances, price growth and an acute trade deficit) through giving up the new economic policy (NEP) mechanisms, confiscation of grain from peasants and forced collectivization²³, rather than by restoring monetary and fiscal equilibrium.

In 2002-2003 period, there were debates in Russia on whether the government was right to rely on a modest four percent GDP growth and give up more ambitious plans. Those who are familiar with the economic history of Russia remember an incident at the meeting of the Politbureau of the VKP(b) in March 1928 where A. Rykov, the Chairman of Sovnarkom (the Council of People's Commissars) tendered his resignation in protest to other party leaders' demands to speed up industrial development of the country²⁴.

¹⁸ World Economic Outlook. Focus on Transition Economies. International Monetary Fund, October 2000.

¹⁹ "What is the rate of growth in the total value of the mass of commodities if it is measured as a percentage of the mass of commodities of the current year to that of the preceding year? In 1922/1923, it amounted to 28 percent, the next year to 25 percent, while in the last year of the period under review to 17 percent. Here is a definite law of a slow-down of rates of growth" (See: V. Groman. On Some Regularities in National Economy Established Through Experiments p. 113).

²⁰ Capital investments in the 1924-1925 period (385 million rubles) somewhat exceeded depreciation deductions (277 million rubles) (see: E.I. Kviring and G. Krzhizhanovski. Principal Issues of Planned Targets of the National Economy in 1926-1929. Moscow: Planovoe Khozyastvo, 1929. p. 129).

²¹ See: L. Yurovsky. Monetary Policy of the Soviet Government (1917-1927). Moscow: Nachala-Press, 1996.

²² An increase in production costs in 1925-1926 was an evidence that reserves of recovery growth had been exhausted. It was related to a dramatic growth in wages and salaries and exhaustion of earlier created production and technical reserves (see: A.N. Malafeyev. History of Price Formation in the USSR (1917-1963). Moscow: Mysl, 1964. p. 101).

²³ Earlier classified materials of the Central Committee of the VKP(b) which were published in 2000 illustrate well how preservation of high rates of growth was related to the scale-down of the new economic policy (see: How the New Economic Policy was Liquidated: Records of Plenums of the Central Committee of VKP(b) in 1928-1929 Moscow.: Rossiya XX vek; Materik, 2000. Vol. 1-5). A quotation from the speech of A Rykov, the Chairman of the Sovnarkom: " In this period, the rate of growth in investments in industry may slow down. No fetish is to be made of rates of growth. We need to ensure such a "feeding" of industry as would permit it within the minimum time-limits to occupy leading positions in the entire economy so that our efforts in innovation and restructuring of economy would not be confined by a lack of engines, tractors, chemical fertilizers, experts and skilled workers who could carry out that restructuring" (see: How the New Economic Policy was Liquidated: Records of Plenums of the Central Committee of VKP(b) in 1928-1929// Edited by A.N. Yakovlev. Vol.3 The Plenum of the Central Committee of the VKP(b) held on November 16-24, 1928 Moscow.: MFD, 2000.p.38). A quotation from A. Rykov's speech at the November Plenum of the Central Committee of the VKP(b) in 1928: "At discussing the issue of the rates of growth, we should not think that a constant increase in the rates of growth or even preservation of those rates from year to year is a law of the transition period". A quotation from J. Stalin's speech at the April Plenum of the Central Committee of the VKP(b) in 1929: "The issue of the rates of development of industry and new forms of merger of cities with villages. It is one of the principal issues of our differences. ...the 3 Plan of Comrade Bukharin is a plan for a slow-down of the rates of industrial development and subversion of a merger of cities with villages". (ibid. Vol. 3 pp. 37-38; Vol. 4 pp. 477-480).

That was not an easy decision. Academician S. Strumilin, a renowned Soviet economist, said in those days: "I would rather speak for high rates of growth, than be imprisoned for advocating the low ones"²⁵.

In 2002, it became obvious that resources of economic recovery would soon be exhausted. In the period 1998-2002, the number of the employed in Russian economy rose to 67.3 million from 58.4 million (an increase of 8.9 million people). Lack of skilled workforce resulted in a dramatic growth in real wages and salaries: in the 2000-2002 period they increased by 70 percent. A similar trend was observed in other CIS countries (Table 3).

The above data explicitly shows that in recovery processes growth in real wages and salaries is more rapid than growth in labor efficiency. That factor was noted by V. Groman in his works in the 1920s²⁶.

Table 3. Rates of growth in real wages and salaries in CIS countries in the period 1996-2003, % change

Country	Year	1996	1997	1998	1999	2000	2001	2002	2003
Azerbaijan		19.0	53.0	20.0	20.0	18.0	16.0	18.0	...¾
Armenia		13.0	26.0	22.0	11.0	13.0	5.0	9.9	14.8
Belarus		5.0	14.0	18.0	7.0	12.0	30.0	7.9	3.2
Georgia		53.0	37.0	25.0	2.0	3.0	22.0	...¾	...¾
Kazakhstan		2.0	5.0	4.0	7.0	12.0	13.0	11.0	6.9
Kyrgyzstan		1.0	12.0	12.0	-8.0	-2.0	11.0	13.3	9.9
Moldova		5.0	5.0	5.0	-13.0	2.0	15.0	20.8	15.3
Russia		6.0	5.0	-13.0	-22.0	21.0	20.0	16.2	10.9
Tajikistan		-14.0	-2.0	29.0	0.3	8.0	11.0	25.9	37.1
Ukraine		-5.0	-2.0	-3.0	-6.0	1.0	21.0	20.1	37.1

Source: The Commonwealth of Independent States in 2003: Statistical yearbook. Moscow: The Interstate Statistical Committee of the CIS. 2004.

Market surveys carried out by the IET have shown that evaluations of production capacities (sufficient for meeting the expected demand) changed in the period 1998-2001. Lack of equipment and skilled workers hindered more often growth in production.

A drop in rates of growth (after they have reached their highest values and the most available resources have been engaged in economy) has given rise to economic and political debates on the causes behind a slow-down of growth and the ways of raising it. Since sources of recovery growth have been exhausted, a new issue arises how to ensure economic development beyond the limits of the recovery period through creation of new production capacities, renewal of capital funds²⁷ and employment of new skilled workforce, rather than by engagement of old ones. This goal can be achieved only in case there is efficient market and economic motivation.

This in turn requires strengthening of property rights and carrying out of profound structural reforms. In the period 2000-2001, the Russian government started such complex reforms and there have been breakthroughs in some areas. However, such reforms do not pay off immediately; they just lay a foundation for long-term economic growth.

²⁴ See: *ibid.* Vol. I p.18.

²⁵ V. Mau. Strumilin's Alternative // *Vedomosti*. March 27, 2002.

²⁶ V. Groman. On Some Regularities in National Economy Established Through Experiments p. 32.

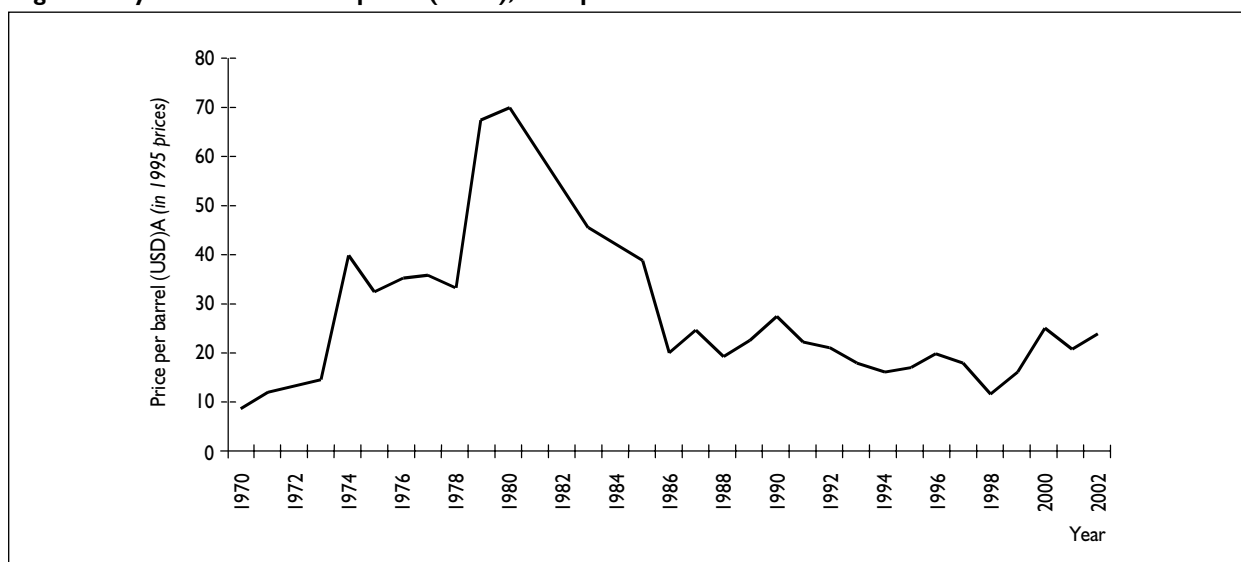
²⁷ On investment limitation in recovery growth in post-socialist transition, see: Wolf H.C. *Transition Strategies: Choices and Outcomes*. New York: Stern Business School, 1997. On specifics of recovery growth where an increase in investments instead of being an engine of growth follows it, see: De Melo M., Denizer C., Gelb A. *From Plan to Market: Patterns of Transition* // Blejer M.I., Skreb M. (eds.). *Macroeconomic Stabilization in Transition Economies*. Cambridge: Cambridge University Press, 1997. P. 17-72; Havrylyshyn O., Wolf T. *Growth in Transition Countries. 1991-1998. The Main Lessons*. Paper Presented at the Conference «A Decade of Transition», International Monetary Fund. Washington, D.C., February 1-3, 1999; A. Aslund. *Building of Capitalism: Market Transformation of the Former Soviet Bloc Countries* / Edited by I. M. Osadchy. Moscow. Logos, 2003.

For example, in the past few years positive changes have been introduced in the Criminal Procedural Code of the Russian Federation. At the same time, the Russian judicial system still has a lot of disadvantages and serious problems related to its functioning will prevail for a long time.

Important measures have been taken in respect to regulation of private ownership of land. One may wonder if the Law on Transfer of Agricultural Lands is good or bad. But the sheer fact that transfer of private lands is regulated and determined by the law undoubtedly promotes long-term growth in Russian economy. The same concerns other measures, for instance, the Labor Code reform and the pension reform. Changes which produce positive short-term results (for example, the income tax reform) are rather rare.

It was mentioned above that high oil prices were an important factor which had an effect on the economic situation in Russia in the early 2000s. In those conditions, the Russian government carried out a prudent fiscal and monetary policy worthy of respect. Quite the contrary was the situation in the period of anomalously high oil prices in the 1970s; in the period 1979-1982 prices on oil in real terms were significantly higher than those of the present day (see fig. 3), but the gained revenues had been senselessly squandered by the then Soviet authorities.

Figure 3. Dynamics of world oil prices (Brent), USD per barrel



Source: International Financial Statistics, IMF 2003.

Structural reforms proceed slowly and promise no miracles, while oil prices remain high. In such a situation, popular decisions are in a greater demand as well as measures which promise immediate pay-offs and "breakthroughs". Calls for a speed-up of the rates of growth and search for "a country which needs to be caught up with and even surpassed" had a serious impact on the economic history of Russia in the 20th century. Suffice to remember N. Khrushchov's efforts to catch up with and even surpass the USA as regards per capita meat production or a situation from the recent past where economic collapse of the USSR started with an attempt to speed up economic growth in the late 80s and the early 90s.

Russia does not have a monopoly on such policy experiments. For example, in Chile the economic policy of the Allende government was also aimed at speeding up the economic growth through abolition of orthodox models, removal of financial limitations and pumping money into the economy. That situation had resulted in a deep political and economic crisis which Chile had to overcome for a decade. But at the initial stage (in 1971), that policy permitted to speed up the rates of economic growth. It is indicative that in Chile macroeconomic manipulation was attempted not in conditions of protracted stagnation of the

economy, but after the period of economic expansion followed by a decline in growth rate and a drop in international copper price (the country's most important export commodity)²⁸.

At present, Russia needs to learn how to maintain sustained development in conditions of the changing post-industrialist world, avoid any involvement in wars and prevent domestic upheavals. It is important to avoid panic because of short-term fluctuations in rates of growth, to put an end to such practices as are typical of this country where a boost is followed by stagnation and crisis and to use motivation and initiative, rather than instruments of state enforcement. The above task is more complicated than raising the rates of economic growth for a short period of time. Such a task requires hard and consistent efforts which do not produce immediate political dividends. However, such a policy opens up a way to sustained economic growth.

* * *

Let us draw some conclusions.

Economic growth which began three to seven years after a collapse of socialism is of a recovery nature and is ensured by a newly established system of market institutions. The principal objective of governments of post-socialist countries at the stage of recovery growth consists in creation of conditions for moving from recovery growth to investment growth.

L. Walesa was first one to compare post-socialist transition with a task of making an aquarium out of a fish soup. Ten years later, it is to be admitted that that objective was extremely difficult, but feasible. Evidence of that is the sustained economic growth (with rates vary from country to country) observed in recent years over the entire post-socialist territory.

Formation of the market system, reallocation of resources in the market sector and adaptation of management to operation in market conditions are important factors behind starting the stage of post-socialist growth recovery. That process took place in Eastern Europe in the early 1990s and in CIS states in the late 1990s. Specifics of a national macroeconomic situation, dynamics of prices on exports and imports and an exchange rate policy had an impact on this process. The above factors had an effect on a national course of development, but within the framework of the general process of post-socialist recovery growth.

Disruption of economic relations and collapse of former administrative channels of coordination (in conditions where new ones have not yet been established) affect to a great extent industries specializing in production of high-tech products. However, after stabilization of market mechanisms the most dynamic growth is observed in the above industries²⁹.

Russia, like most other post-socialist countries, is already a country with a market economy. That fact is widely recognized internationally³⁰. A historical transition from socialist command economy, under which generations of Russians used to live, to the market economy has succeeded in general.

Needless to say that by a number of important parameters, specifics of post-socialist states, including Russia, differs from those inherent to market economies which did not go through a socialist experiment. However, judging by key indices, countries emerging from socialism are fairly close to market economies of a corresponding level of development. (Table 4).

²⁸ Dornbusch R., Edwards S. *The Macroeconomics of Populism in Latin America*. Chicago; London: The University of Chicago Press, 1991. p. 200.

²⁹ See: *Factors of Economic Growth in Russian Economy: Teatise No.70?*. Moscow. IET, 2003. p. 186, 187, 194, 195.

³⁰ The European Union and the USA recognized Russia as a country with market economy in June 2002 (see: <http://bisnis.doc.gov/bisnis/bulletin/0207bull2.htm> (USA Dept. of Commerce)). A quotation from the speech of B. Marshall, Vice-President of the Russian-American Council on Business Cooperation at the hearings in the US Department of Commerce on March 27, 2002: "To deny official recognition of Russia as a country with market economy is equal to negation of the present-day reality" (see: <http://www.usrbc.org/Transcripts-Summaries-testimonies/2002/Commerce%20Hearing%20march%2027.htm>).

Table 4. Individual parameters of development of Russia and some other countries at the end of the 20th century

Country	Russia	Brazil	Mexico	Spain
Year*	2001	1998	1980	1966
Share of the urban population	72.9	79.9	66.4	62.2
Share of the population engaged in agriculture. %	12.7	23.4	36.3	29.0 (1970)
Share of the population employed in industry. %	30.5**	20.1a	29.1	36.0 (1970)
Share of the population engaged in the service sector. %	56.8	56.5	34.6	35.0 (1970)
Public expenditure on education. % of the GDP	3.2	5.0 (1999)	4.6	1.2 (1966)
Public expenses on health-care. % of the GDP	3.1	¾	¾	2.3 (1970)
Child mortality (at the age of under one year) per 1000 live-born children	18.1	32.0 (2000)	56.0	36.0
Child mortality (at the age of under five years) per 1000 live-born children	21.0	38.0 (2000)	74.0	45.5 (1965)
Number of fixed and mobile phones per 1000 persons	281	165	53 (1988)	94
Number of Internet users per 1000 persons	30	15	¾	¾
Number of cars per 1000 persons	140 (2000)	129	60	33

* corresponds to the level of per capita GDP in the amount of USD 5,437 in Russia, USD 5,459 in Brazil, USD 5,582 in Mexico and USD 5,538 in Spain.

** Employment in industry, including construction.

Sources: 1. Maddison A. Monitoring the World Economy 1820-1992. P.: OECD. 1995.

2. World Development Indicators 2003. World Bank.

3. OECD (healthcare expenditure of all the countries except Russia).

4. UN Common Database.

5. The State Statistics Board of Russia.

6. The Ministry of Finance of the Russian Federation.

7. Mitchell B.R. International Historical Statistics. Europe 1750-1993. London: Macmillan Reference LTD. 1998.

For this reason, a discussion on long-term problems of economic growth should be based on experience cumulated by countries-leaders of present-day economic growth in the past fifty years (taking into account the specifics of the socialist experiment).

It is crucially important to continue reforms, which ensure long-term sustained economic growth and formation of social and economic foundations of post-industrial societies in our countries. The above determines the essence of the current transformation and major challenges to be faced by virtually all the post-socialist countries in the forthcoming decades.