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Political and Economic Transition of Formerly Socialist Countries

For many decades, the world was divided into socialist and capitalist countries. The countries east of the Iron Curtain were characterized by a one-party-system and a socialist economic system. The economic system was marked by the absence of markets and a price system; instead allocation was done by the planning administration. As a result, the production structure followed the priorities imposed by the administration. At least on the micro-level, chronic shortages prevailed in many areas and were paired with surpluses in other areas. The so-called soft budget constraint is one of the phenomena in this system: as the state cannot commit to letting firms become insolvent, the firms anticipate that the state will bail them out. This, of course, had negative effects on the firms' efficiency (Roland 2000). In the end, many countries, in particular the Soviet Union, experienced enduring economic stagnation. In order to solve the resulting problems, several attempts at gradual reform were undertaken. However, in 1989 the Berlin Wall fell unexpectedly, and the Soviet Union collapsed in 1991. Since then, the formerly socialist countries have undergone a fundamental transition, both politically and economically. The following article will explore the developments that have occurred since the fall of the Iron Curtain and will describe and compare the current political system as well as the institutional and regulatory environment of the formerly socialist countries. The analysis will be centered around two main indicators – 1) the Polity Score, describing regime authority characteristics and transitions in government, and 2) the Ease of Doing Business indicators, scoring countries on essential components of doing business such as resolving insolvency and starting a business – as measures for the institutional environment that a government has to provide so that markets function properly.

POLITY IV PROJECT

The Polity IV Project, a part of the Integrated Network for Societal Conflict Research, established by the Center for Systemic Peace, is a set of indicators that describe regime authority characteristics and transitions in government. It is an annual and cross-national time series that analyzes data for all independent countries with a population of over 500,000 (167 countries as of 2017).

The project aims to divide all polities into three separate groups, based on their polity score on a scale from -10 to 10: autocracies (-10 to -6), anocracies (-5 to 5) or democracies (6 to 10). This final polity score is calculated by subtracting the autocracy score from the democracy score, both of which aim to display the most general autocratic and democratic tendencies within a polity.

To make comparison possible, both indices include the same general categories reflecting access into and competitiveness of the political system, as well as constraints upon executive powers. While the democracy index (ranging from a score of 0 to 10) displays a citizen's ability to (successfully) conduct oppositional political activities, unhampered from negative consequences, the autocracy index (ranging from a score of 0 to 10) displays the contrary, mainly the limitations upon access into the executive ranks and political activity. For example, if a country is fully democratic, it would have a democracy score of 10 and an autocracy score of 0. The final polity score (democracy-autocracy) would thus be 10, making it a fully democratic country. If a country has a democracy score of 1 and an autocracy score of 8, then its overall polity score would be -7 (democracy-autocracy), making it a country with autocratic characteristics.

The data included in these indices is focused on the socially institutionalized and "real world" implementation of a polity's hierarchical structure and gathered through the analysis of historical accounts and research. To standardize the necessary interpretation and allow for comparability, key determinants for autocratic or democratic regimes are displayed in the form of a checklist. As an example, a point on the checklist regarding competition in the political systems is whether there have been multi- or single-party systems. As a whole, the indicator allows direct comparisons of nations and the levels of freedom that countries have within their governments.

The scores are individually displayed in the following tables for four different country groups, namely: Central Europe and the Baltics, South Eastern Europe, Central Asia, and Eastern Europe and the Caucasus. For the country groupings, we follow the structure used by the European Bank for Reconstruction and Development (EBRD). The scores are offered from the dissolution of the Soviet Union in 1991, until the most recent scores in 2017.

Central Europe and the Baltics

In 1991, there was only one country in Central Europe and the Baltics with a polity score below 0, namely Croatia (-3). Estonia had a score of 6; the Czech Republic, Latvia, and Poland a score of 8; and Hungary, Lithuania, and Slovenia a score of 9. From 1991 until 1998, the scores remained generally consistent, with an average of 7 for all countries in Central Europe. In 1999, the average increased from 7 to 8, rising to 9 in 2000. This change

Table 1-4

Table 1

Central Europe/Baltics	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Croatia	-3	-3	-3	-3	-5	-5	-5	-5	1	8	8	8	8	8	8	9	9	9	9	9	9	9	9	9	9	9	9
Czech Republic	8	8	10	10	10	10	10	10	10	10	10	10	10	10	10	9	9	9	9	9	9	9	9	9	9	9	9
Estonia	6	6	6	6	6	6	6	6	7	9	9	9	9	9	9	9	9	9	9	9	9	9	9	9	9	9	9
Hungary	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10
Latvia	8	8	8	8	8	8	8	8	8	8	8	8	8	8	8	8	8	8	8	8	8	8	8	8	8	8	8
Lithuania	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10
Poland	8	8	8	8	9	9	9	9	9	9	9	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10
Slovakia			7	7	7	7	7	9	9	9	9	9	9	9	9	10	10	10	10	10	10	10	10	10	10	10	10
Slovenia	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10

Table 2

South Eastern Europe	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Albania	1	5	5	5	5	0	5	5	5	5	5	7	7	7	9	9	9	9	9	9	9	9	9	9	9	9	9
Bosnia and Herzegovina		0	0	0																							
Bulgaria	8	8	8	8	8	8	8	8	8	8	9	9	9	9	9	9	9	9	9	9	9	9	9	9	9	9	9
North Macedonia	6	6	6	6	6	6	6	6	6	6	6	9	9	9	9	9	9	9	9	9	9	9	9	9	9	9	9
Kosovo																		8	8	8	8	8	8	8	8	8	8
Montenegro																	9	9	9	9	9	9	9	9	9	9	9
Romania	5	5	5	5	5	8	8	8	8	8	8	8	8	9	9	9	9	9	9	9	9	9	9	9	9	9	9
Serbia																	8	8	8	8	8	8	8	8	8	8	8

Table 3

Eastern Europe and the Caucasus	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Armenia	7	7	7	7	3	-6	-6	5	5	5	5	5	5	5	5	5	5	5	5	5	5	5	5	5	5	5	5
Azerbaijan	-3	1	-3	-3	-6	-6	-6	-7	-7	-7	-7	-7	-7	-7	-7	-7	-7	-7	-7	-7	-7	-7	-7	-7	-7	-7	-7
Belarus	7	7	7	7	0	-7	-7	-7	-7	-7	-7	-7	-7	-7	-7	-7	-7	-7	-7	-7	-7	-7	-7	-7	-7	-7	-7
Georgia	4	4	4	4	5	5	5	5	5	5	5	5	5	7	7	7	6	6	6	6	6	6	6	7	7	7	7
Moldova	5	5	7	7	7	7	7	7	7	7	8	8	8	8	9	9	9	9	9	9	9	9	9	9	9	9	9
Russia		5	3	3	3	3	3	3	3	6	6	6	6	6	6	6	4	4	4	4	4	4	4	4	4	4	4
Ukraine	6	6	5	7	7	7	7	7	7	6	6	6	6	6	6	6	7	7	7	7	6	6	6	6	4	4	4

Table 4

Central Asia	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Kazakhstan	-3	-3	-3	-3	-4	-4	-4	-4	-4	-4	-4	-6	-6	-6	-6	-6	-6	-6	-6	-6	-6	-6	-6	-6	-6	-6	-6
Kyrgyzstan	-3	-3	-3	-3	-3	-3	-3	-3	-3	-3	-3	-3	-3	-3	3	4	3	3	1	4	7	7	7	7	7	7	8
Tajikistan	-2	-6	-6	-6	-6	-6	-5	-1	-1	-1	-1	-1	-3	-3	-3	-3	-3	-3	-3	-3	-3	-3	-3	-3	-3	-3	-3
Turkmenistan	-8	-9	-9	-9	-9	-9	-9	-9	-9	-9	-9	-9	-9	-9	-9	-9	-9	-9	-9	-9	-9	-9	-9	-8	-8	-8	-8
Uzbekistan	-9	-9	-9	-9	-9	-9	-9	-9	-9	-9	-9	-9	-9	-9	-9	-9	-9	-9	-9	-9	-9	-9	-9	-9	-9	-9	-9

Source: The Policy Project (2018).

was driven by the transitions in the Croatian government at that time. After the end of the Croatian War of Independence in 1995, the country was in a state of post-war recovery for several years. After the elections of 2000, the country put in place a new government system that was much more democratic (Freedom House 2008). This change led to a transition from a polity score of -5 in 1998 to a score of 8 in 2000. Croatia is now similar in its level of democracy to other nations in the EU, with a score of 9, a score shared by the Czech Republic and Romania. Hungary, Lithuania, Poland, Slovakia, and Slovenia have the highest score of 10. All countries have held their current scores for the past ten years.

South Eastern Europe

Table 2 shows the scores of nations categorized as being in south-eastern Europe by the EBRD. This region includes the countries (Bosnia and Herzegovina, North Macedonia, Kosovo, Montenegro, and Serbia) that formerly belonged to SFR Yugoslavia, which started to collapse in 1991 and faced a series of wars on its former territory. This explains why in some of the countries, the reporting starts later. Within this region, there has been a trend towards full democracy, with every country holding a score of 9 in 2017 with the exception of Serbia, which holds an 8. There has been extreme sta-

bility since 2005, since when no country has changed score. In 1989, three nations held scores below 0, namely Albania with a score of -9, Bulgaria with a score of -7, and Romania with a score of -2. However, all three countries quickly reformed their political system, having completed some form of transition by 1990. Bulgaria underwent the most dramatic change, having a score of -7 in 1989 and jumping to a score of 8 in 1990. Albania performed a similar feat over the course of three years, changing from a score of -9 in 1989 to 1 in 1990 to 5 in 1992. However, within four years, Albania had fallen back to a score of 0. By 1997, it had once again transitioned towards democracy and now holds a score of 9. Both Serbia and Montenegro have held constant scores since they were first reported by the Polity Project in 2006, when they formally dissolved their union. Serbia has been scored at 8 and Montenegro has been scored at 9. Bosnia has not been scored since 1995 as it functions with a decentralized government. In the 1990s, there were many transitions and changes in government in this region. However, it has become a very stable region, with the last major transitional period ending in 2005.

Eastern Europe and the Caucasus

In Eastern Europe, there are three countries that were formerly parts of the Soviet Union and now border the new EU member states: Belarus, Moldova, and Ukraine. Belarus saw a drop in its score from 7 in 1994 to -7 in 1996, where it has since remained. Ukraine has also slid back, but to a lesser degree, having dropped from a peak score of 7 in 2009 to 6 until 2014, when it dropped to 4. Moldova, in contrast, is now among the most democratic nations, with a score of 9. Thus, these three countries are quite diverse, covering all three classifications of the polity score: autocracy, anocracy, and democracy, respectively. Russia started off with a score of 5 in 1992 and fell to a score of 2 from 1993 onwards. This increased to a score of 6 from 1994 to 2000, when it dropped to a score of 4, which it has held since then.

The Caucasus region is similarly scattered in terms of development, with its three nations – Armenia, Azerbaijan, and Georgia – also currently holding scores that include all three government types. Azerbaijan, after a one-year spike to a score of 1 in 1992, quickly fell back into autocracy, with its score falling 8 points in six years. It now holds the third-lowest score of all post-Soviet countries, tied with Belarus at -7. At the time of its independence, Armenia held the third-highest score of all post-Soviet nations: 7. However, after 1994, it quickly fell to -6 in 1996, but recovered to a score of 5 in 1998. Since then, Armenia has retained this score of 5, holding just below the threshold for a democracy. Georgia initially held a score of 4, but in two periods, 1994–1995 and 2003–2004, its score rose to 7 before falling again to 6 in 2007. In 2013, it returned to a score of 7, which it holds as of 2017.

CENTRAL ASIA

In Central Asia, the former Soviet Union nations of Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan, and Uzbekistan are almost all autocratic states, with the exception of Kyrgyzstan. After a six-year transition from 2005 to 2011 from a score of -3 to 7, it was the first and only one of these nations to achieve democracy, and now has a score of 8, implying a relatively strong democracy. Tajikistan made progress towards democracy in the late 1990s, progressing from a score of -6 in 1996 to -5 in 1997 up to a peak of -1 in 1998 before dropping to a consistent -3 in 2004. While it is still more autocratic than democratic, among its neighbors it is one of the most democratic-leaning nations. Kazakhstan, Turkmenistan, and Uzbekistan are all autocracies, with scores of -6, -8, and -9 respectively, with Uzbekistan holding near to the lowest possible score.

Overall, the successor states of the former Soviet Union are scattered across the spectrum of democracy and autocracy; the overall trend, however, is towards democracy. Only six nations hold scores below 0, meaning that they have more autocratic tendencies than democratic, while the remaining nine hold scores of at least 4, with five countries holding scores of at least 8. An overview of the development over time of the Former Soviet Union countries can be seen in Figure 1.

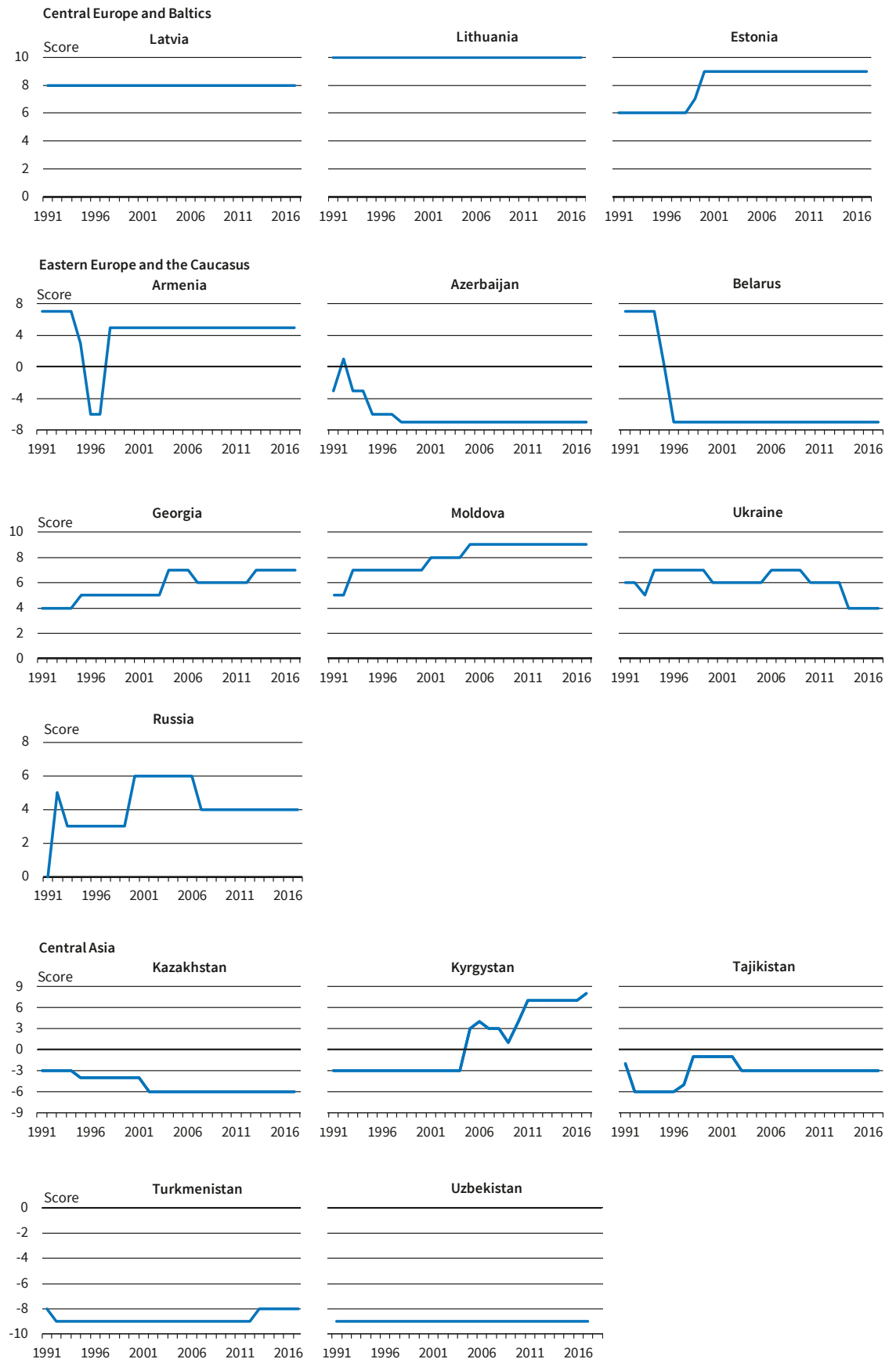
EASE OF DOING BUSINESS INDICATORS

At the same time as the change in political systems commenced the transition from socialist to more market-based economies took place. To measure this development, we have chosen the Ease of Doing Business Index, as it captures the institutions and regulations that govern the operation of firms, which are the core of a market-based economy.

The index is created by Doing Business, which is part of the World Bank Group. It measures, scores, and ranks countries according to their performance regarding their legislative, regulatory, and institutional environment for private businesses in the following fields: starting a business, dealing with construction permits, getting electricity, registering property, getting credit, protecting minority investors, paying taxes, trading across borders, enforcing contracts, and resolving insolvency. Each of these sub-categories is made up of individual indicators, which are all considered essential components of doing private business (41 individual indicators in total across all sub-categories). To obtain the required data, the World Bank regularly conducts surveys and questionnaires with businesses around the world, supplementing them with expert accounts on the regions. Alternatively, it directly requests the data from local utilities (e.g., electricity or water suppliers), experts (often lawyers), and administrations or registries. The final index score is derived by averaging the countries individual performance in the ten sub-categories. The maximum achievable overall

Figure 1

Polity Scores for Countries of the Former Soviet Union (1991–2017)



Source: The Polity Project (2018).

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Figure 2

Ease of Doing Business Score (2018)



Source: The World Bank (2019).

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score (as well as the maximum score in each sub-category) is 100, and the minimum is 0. A country’s individual performance in each indicator is determined in contrast to a global best and worst performance, which is usually set every five years.

From the indicators, we have chosen to include the overall “Ease of Doing Business” indicator, the “Resolving Insolvency” indicator, and the “Starting a Business” indicator. We included the “Ease of Doing Business” indicator as a way of looking at the overall trends. We chose the sub-categories “Resolving Insolvency” and “Starting a Business” because they are two particularly interesting aspects of doing business: after the end of the socialist system and during the transition from a planned economy to a market economy, alongside the handing over of state-controlled business to private owners, many businesses had to be closed and many more were to be newly started.

Figure 2 shows a map of Central, Eastern, and South Eastern Europe as well as Central Asia along with these regions’ overall scores, showing the large amount of variation.

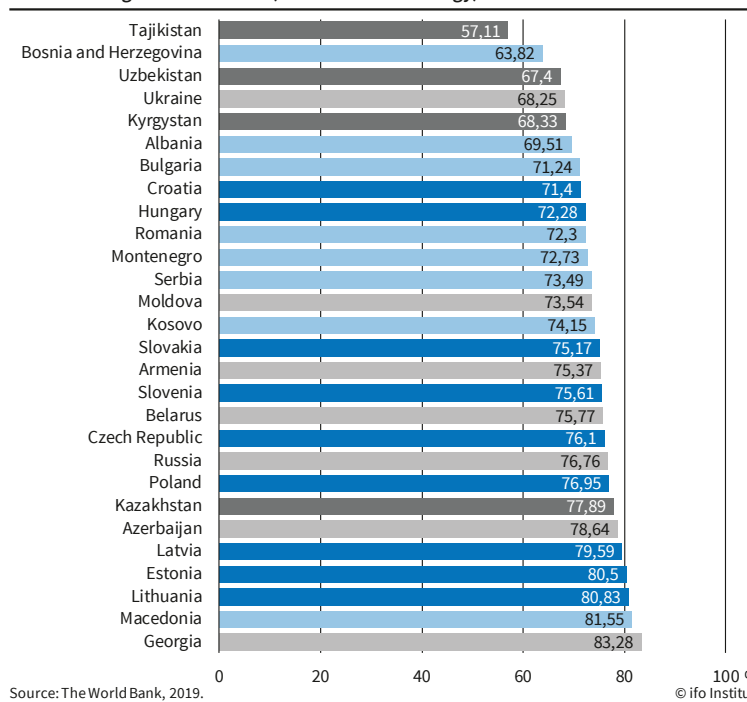
We find that the nations of Eastern Europe and the Caucasus and Central Asia generally achieve a higher score in the “Starting a Business” category than those in Central Europe and the Baltics and South Eastern Europe. This is not the case for “Resolving Insolvency,” a category dominated by countries in Central Europe and the Baltics and South Eastern Europe.

Sub-category: Ease of Doing Business

Figure 3 shows the “Ease of Doing Business” scores for all nations of interest grouped into Central Europe and the Baltics, South Eastern Europe, Eastern Europe and the Caucasus, and Central Asia. Within the countries of interest, the scores range from a minimum score of 57.11 for Tajikistan, yielding a rank of 126 of 190, to 83.28 for Georgia, yielding a rank of 6th. Three of our top five countries, namely Estonia, Latvia, and Lithuania, are in Central Europe and the Baltics. Overall, the countries in this region receive the highest score, with an average of 76.5, followed by Eastern Europe and the

Figure 3

Ease of Doing Business Score (DB17-19 Methodology)



Source: The World Bank, 2019.

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Caucasus (average 75.8), South Eastern Europe (72.3), and Central Asia (67.7).

Sub-category: Resolving Insolvency

The data for the “Resolving Insolvency” category is derived from surveys with local insolvency practitioners and verified through a study of laws and regulations as well as public information on insolvency systems. The insolvency practitioners are presented a hypothetical insolvency case, which is adjusted in terms of size to be comparable across countries. The two indicators for the “Resolving Insolvency Index” are the recovery rate, which is the recovered percentage per dollar invested by an external (secured) creditor after the judicial insolvency process (also taking into account the time and costs during the process), and a separate strength of insolvency framework index, which is in turn the sum of four further separate indices and describes the potential within a country for viable firms to be maintained while non-viable ones are liquidated. Keeping viable businesses operating is among the most important goals of insolvency systems. A good insolvency regime should prevent the premature liquidation of sustainable businesses. A high score implies a high performance in these regards. These indices mainly concern individual participation rights within the formal process of insolvency: for example, by whom and against which standard the liquidation process gets started, whether the debtor retains certain rights to maintain his business and finance dealings, or the extent to which the voting rights are distributed and weighted between the debtor(s) and creditor(s) (Doing Business 2019).

Figure 4 displays the “Resolving Insolvency” scores, with the same categorization as in Figure 3. The highest-ranked nation is Slovenia, with a score of 83.66 and a global rank of 9. The lowest-ranked nation among the sample is Tajikistan, with a rank of 146 and a score of 30.9.

Sub-category: Starting a Business

The “Starting a Business” category consists of four indicators that comprise the steps necessary to legally start a local limited liability company, namely: the number of procedures needed (defined as individual interactions with authorities, notaries, etc.), the time (in calendar days) and overall costs (including fees and taxes, excluding bribes) to complete the whole formal process, as well as the minimum cap-

ital requirements to be eligible for starting said business. The last two indicators are displayed as a percentage of income per capita in the specific country. To obtain internationally comparably data, the Doing Business team sets up two hypothetical cases, which have a starting capital that is adjusted according to the country’s per capita GDP. Based on information from laws, regulations, and other publicly available sources, data on the indicators above is collected. The data is reviewed by experts in the country (Doing Business 2019).

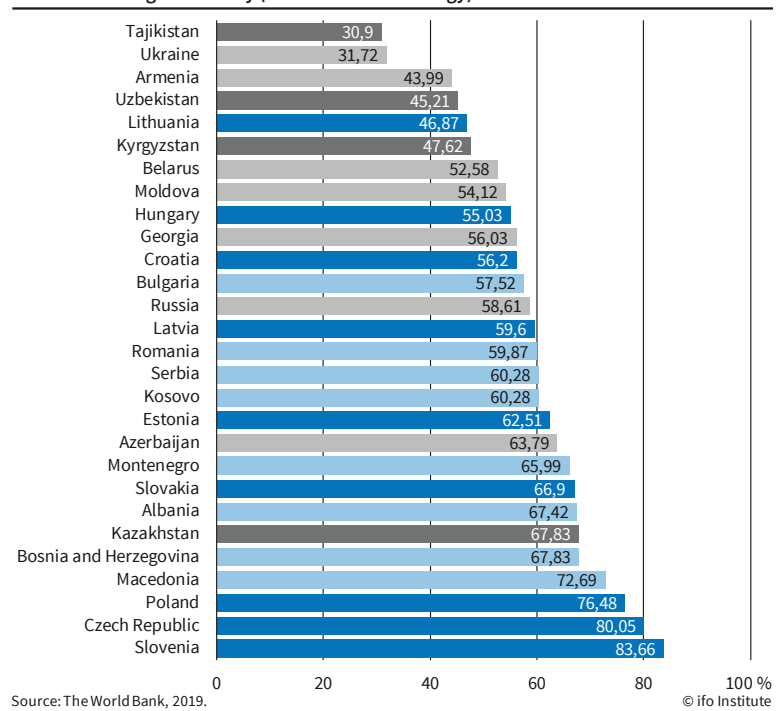
Many Western countries perform relatively badly in this category. For example, Germany and Austria have ranks of 114 and 118, placing them in the bottom 50 percent of nations in the world in this category. Many of these economies tend to be highly bureaucratic and regulated, leading to long periods and high costs in the process of starting a new business. However, in other nations, where these regulations are more relaxed, starting a business can be a very simple.

Among the countries of interest, the nations of Eastern Europe and the Caucasus are the best performers in the “Starting a Business” category. Georgia, Armenia, and Azerbaijan hold the top three spots in terms of the ranking of our study, with overall ranks of 2, 8, and 9, respectively. Georgia has a score of 99.34 in this category. The range of scores has a minimum score of 59.57, as found in Bosnia and Herzegovina. The individual scores for the countries of interest are displayed in Figure 5.

In Georgia, for example, there is no required paid-in capital and only a single process, which takes two days on average to complete, for starting a busi-

Figure 4

Score: Resolving Insolvency (DB15-19 methodology)



ness. In Germany, however, there are nine processes that must be completed, lasting on average eight days, and requiring minimum paid-in capital of around 30 percent of annual per capita income. The stricter regulations in many more developed countries hinder the ability of individuals to quickly start a business at low cost. While these regulations might, for instance, prevent insolvencies in the future, these factors are not taken into account in the indicators, and so nations that rank lower in other categories rank much higher here and vice versa.

The Doing Business indicators are not necessarily indicative of economic welfare, but rather give an insight into the workings of the government and regulatory agencies of each economy, showing how restrictive or lax they are with respect to businesses. Because of this, there is a large degree of variation within the countries of interest. The overall score and rank is an aggregate score, made up of the scores in the sub-categories, meaning that the overall rank does not necessarily hold strict trends.

CONCLUSION

Our article describes the tremendous changes that have taken place in the formerly socialist countries both politically and economically. With respect to their political systems, many countries, in particular those in Central and South Eastern Europe and the Baltics, are considered democracies by the Polity IV indicator. In the area covered by the former Soviet Union, there are several autocratic countries where we also observe fluctuations and some downgrades over time. Com-

pared to the political system, the patterns for the institutional and regulatory environment as captured by the Doing Business indicators are very different. We focus on the ease of starting a business and resolving insolvency, as the entry and exit of firms is vital for a functioning market-based economy. In these Doing Business indicators, former Soviet Union countries fare particularly well. This demonstrates that political change and institutional and regulatory change are not necessarily closely linked.

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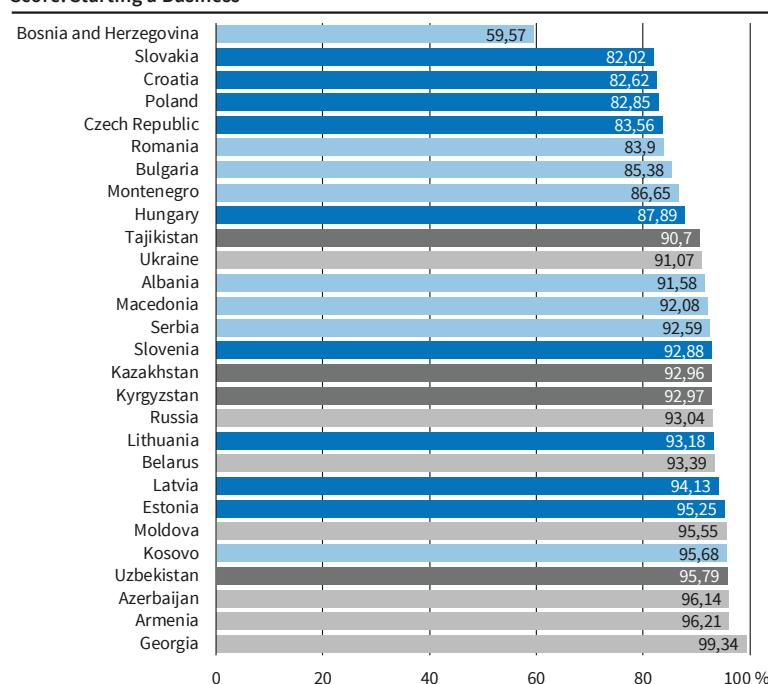
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Figure 5

Score: Starting a Business



Source: The World Bank, 2019.

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