



# 1989

- “The transition from socialism to capitalism ... one of the most significant events in ..world economy since industrialization...” (Berglöf & Roland, 2007)
- A brief triumphal moment: for neoclassical economics and thus for Robbins’s focus on how a system handles scarcity (Kirzner, 1991).
- **“The experience from transition provided strong empirical support for this shift in focus from markets and price theory to contracting and the legal, social and political environment of contracting”**,

- Robbins's on market socialism (1934: 153)

- “ There is a certain aesthetic attraction in the contemplation of a project which setting out to eliminate the institutions of a “planless” society...arrives finally at an attempt to reproduce them. Unfortunately, there does not seem reason to suppose the reproduction would be successful. The propounders of such schemes conceive of the problem in altogether too static and *simpliste* a manner. ”
- “ ...conditions of demand and supply are continually changing. Tastes change. Technique changes. The availability of resources and the supply of labour and capital is in process of continual alteration. For competition to be free the *entrepreneur* must be at liberty to withdraw his capital altogether from one line of production, sell his plant and his stocks and go into other lines. ”

Market-- the newest ideology for Eastern Europe?

No, real meaning in conditions of 1989-1992

Moscow, December 1991 [Rostowski]:

Barter, implosion of production, repressed  
very high/hyper inflation

“The Walrasian auctioneer of Russia”

r this shift in focus from markets and price theory to contracting and the legal, social  
are the root cause of economic inefficiency, and that if the Soviet system is ever to

ence from transition provided strong empirical support for this shift in focus  
ng the currently dominant school of Soviet economists now that central plan

## Kanbur (1999) Strange case of the Washington Consensus

- “So the negotiators from Washington always took a more purist stance, a more extreme stance than even their own intellectual framework permitted (they were all surely well schooled in the theory of the second best). "Give them an inch of nuance, and they'll take a mile of status quo", seemed to be the mindset...”

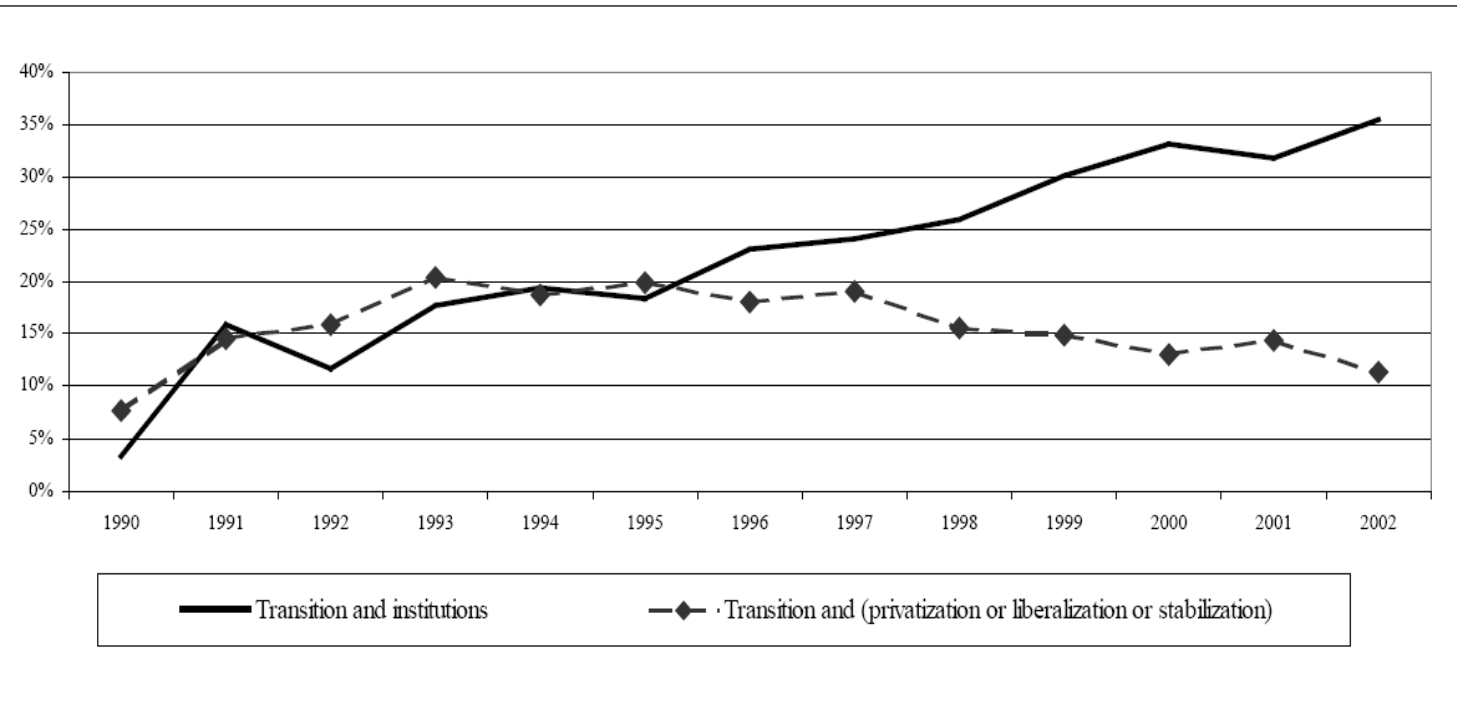
## Who will write the economic history of the Transition?

- “The victors in the theoretical and policy debate will be those who establish the salient facts through the murk of reform,”

Peter Murrell (1995:167-8) *Journal of Economic Literature*, “The Transition According to Cambridge, Massachusetts.”

# Murrell's tale: Econlit on institutions

Figure: Percentage of those documents in the *Econlit* database having transition as a keyword that also use institutions or Washington consensus policies as keywords



Source: Handbook of NIE, 2005, Murrell, Institutions and Firms in Transition Economies

# Institutions: Robbins v Coase

- Although Coase has repeatedly said (for example, 2002) that the new institutional economics will “not replace neoclassical economics but make it infinitely more fruitful,” what he singled out for criticism (in his Nobel address) was the view of “my old chief and wonderful human being, Lionel Robbins” that economic analysis should take institutions as given, reducing microeconomics to price theory.

# Robbins on planning (1935: 125)

Fn 1: The alleged advantage of economic "planning"—namely, that it enables greater certainty with regard to the future—depends upon the assumption that under "planning" the present controlling forces, the choices of individual spenders and savers, are themselves brought under the control of the planners. The paradox therefore arises that either the planner is destitute of the instrument of calculating the ends of the community he intends to serve, or, if he restores the instrument, he removes the *raison d'être* of the "plan". Of course, the dilemma does not arise if he thinks himself capable of interpreting these ends or—what is much more probable—if he has no intention of serving any other ends but those *lie* thinks appropriate. Strange to say this not infrequently happens. Scratch a would-be planner and you usually find a would-be dictator.

## Transition: Post-Washington Consensus view

- “The defining stylised fact of the first 10 years is the massive output fall”

$$Q_{(\text{theories})} > Q_{(\text{theorists})}$$

- Murrell, 2005:

Key, turning point Blanchard and Kremer (1997):  
Disorganisation, and a contract approach

However:

“There is weak empirical support for this model, but **precise testing is difficult**, meaning that the pertinent empirical work is not as convincing as in many other areas.”

# Transition: post Washington continued

- “Macro over micro” a mistake
- Gradual price liberalisation (or controls) not problematic
- Build reform coalitions gradually
- No set window for “extraordinary politics”
- Get privatisation right, not fast
- Make sure institutions are in place before reform
- Example of China (Murrell: at least the style) applicable

# The Output Fall: alternative view

- About half the size recorded.
- Do not need novel factors to explain. Should not have been a surprise.
- Not very large in Poland (10 or 15%, return to growth in 2 years), Russian and other CIS cases different
- Fast reformers grew more swiftly than slow reformers after fall
- Implication: writing off unviable sectors, value-subtracting once valued at international prices
- Russian case: very large rents (eg gas and oil internally 1/10 world market price), opportunities for arbitrage, swiftly raised the benefits to corruption and deflected entrepreneurship
- Not a “novel fact”, was not predicted, but depth was a surprise

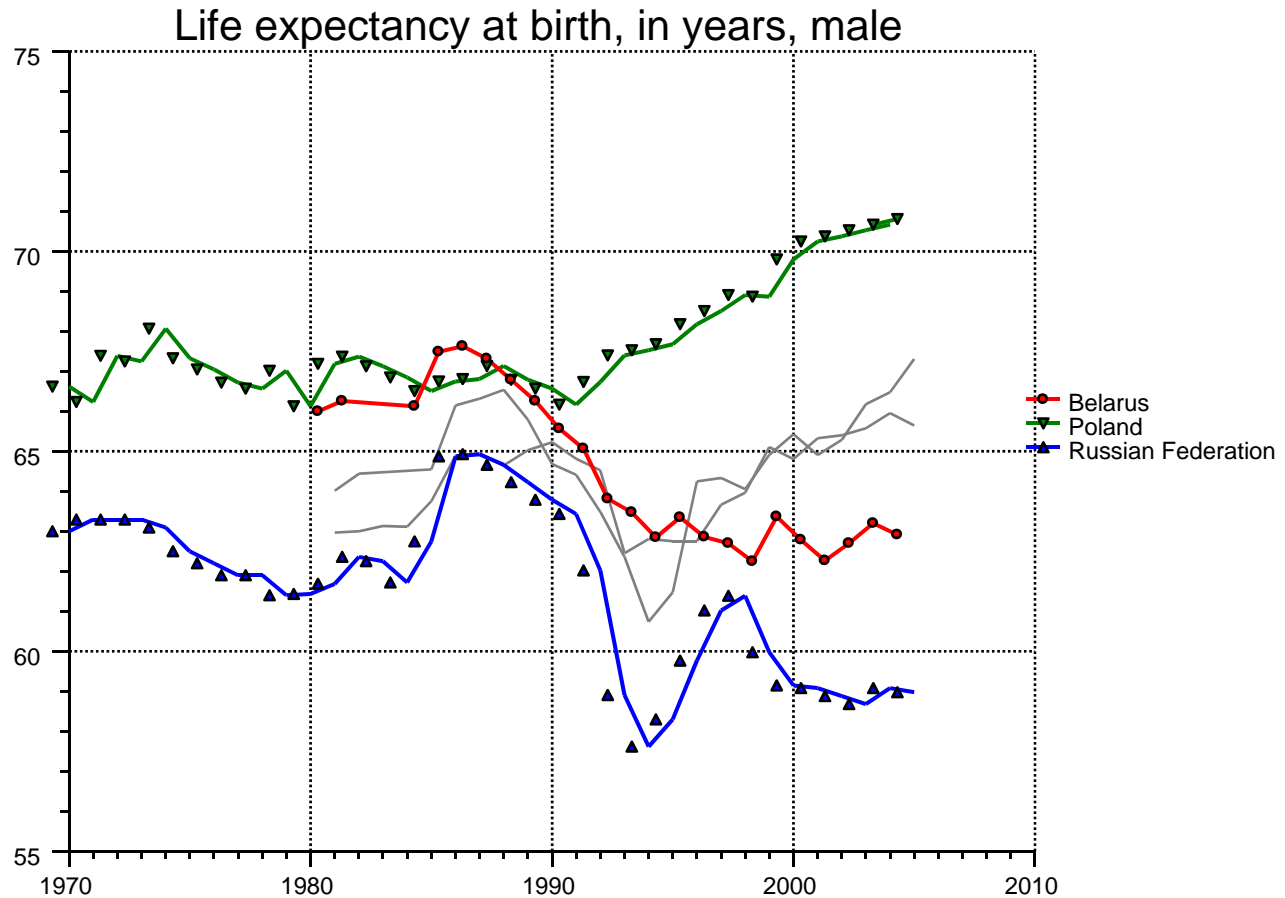
## Wesley C. Mitchell, QJE 1935: Robbins, Great Depression

•Sir Josiah Stamp has said of this book: "No economist can read it without real enjoyment, and provocation to argue back." I have yielded to the provocation; I must testify also to the enjoyment. Professor Robbins is an eminently skillful expositor. He arranges his materials in orderly fashion; he writes clearly; he stands manfully for the viewpoint he has adopted, never dodging an issue. He is frank about his dislikes... Temperamentally Professor Robbins is less a scientific inquirer trying to understand a complicated world than he is a militant apostle preaching an orthodox faith to a disillusioned generation. In that role he is so gallant a figure that one is tempted to say on putting down his book, "Almost thou persuadest me to become an Austrian."

# Death of macro too?

- Klammer and Solow
- Data
- Reality is that the questions are not so novel

# Mortality in transition: complex



Source: WHO "Health for All Database,  
<http://www.euro.who.int/hfad>

## Oliver Williamson what NIE doesn't know

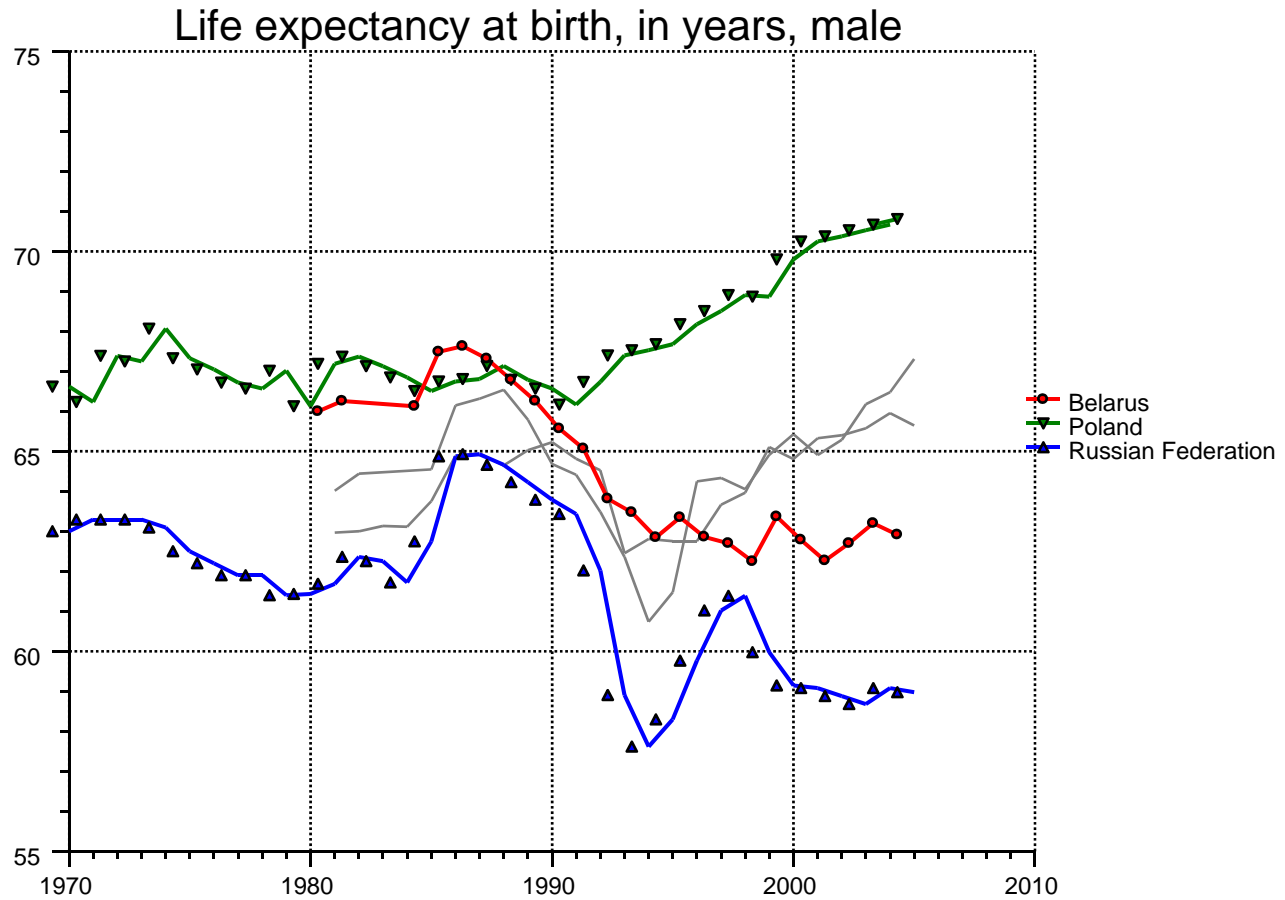
- “Broad reach notwithstanding, the NIE is not and does not pretend to be an all-purpose construction, as the reform of economies of Eastern Europe and the former Soviet Union illustrate.” (JEL 2000)
- + Coase Nobel lecture, “If we knew more about our own economy, we would be in a better position to advise them”.

# Death of macro caused by end of inflation?

- Low inflation since the 1990s
- Globalisation? Clever central bankers?  
Lessons of 1998?
- Is this the cause of the tilt towards micro?



# Mortality in transition: complex



# 1998

- Unsustainable, very short-term, debt, whilst running a high budget deficit
- Also oil at \$11
- “Contagion “

# Summary I

- **Robbins's scarcity focus** “put finger on key point” for market vs command, probably not accidentally
- But **irony of history**: transition from command economy itself was a challenge for neoclassical economics
- **“Salient facts” of transition**, and their explanation, **all in dispute, but advantage at present to critics**:
  - On magnitude, variance and (especially) cause of output fall
  - Objection to “macro over micro” (Murrell), rapid stabilisation of hyperinflation (Stiglitz), price liberalisation.
  - Assessment of impact of mishandled Russian privatisation
  - Assessment of counterfactual on China's road for Eastern Europe

# Summary II

- Tentatively, concern for institutions is part of a new more diffuse and richer framework.
- Other innovations have already diffused down even to undergraduate level: information asymmetries, agency, uncertainty, game theory, behavioural and experimental economics.
- Institutions lags because it has no clear hard core
- *Was* given a boost by transition, but this would have done little without already existing trend
- Doubtful new package will be as woolly and cuddly as Frank Hahn fearfully forecast (1991)
- Morgan and Rutherford: pluralism to neoclassical. Return trip?
- However, macroeconomics in the doldrums. Low world inflation? Detente between New Keynesians and New Classicals? Fads and fashions? Energy has flowed into growth?
- Macro lessons from the transition not so innovative: vindication of fundamentals on very high inflation, high fiscal deficit

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•Wesley C. Mitchell, "Robbins. the Great Depression" QJE 1935

# Robbins Macro/monetary(1935: 125-126)

- There can be no question that a quite elementary knowledge of the Quantity Theory was of immense prognostic value during the War and the disturbances which followed. If the speculators who bought German marks, after the War, in the confident expectation that the mark would automatically resume its old value, had been aware of as much of the theory of money as was known, say, to Sir William Petty, they would have known that what they were doing was ridiculous.
- Similarly, it becomes more and more clear, for purely analytical reasons, that, once the signs of a major boom in trade have made their appearance, the coming of slump and depression is almost certain; though when it will come and how long it will last are not matters which are predictable, since they depend upon human volitions occurring after the indications in question have appeared. So, too, in the sphere of the labour market, it is quite certain that some types of wage policy must result in unemployment

- Did not ignore institutions, but did theorise them away, either Balcerowicz' "extraordinary politics," need to create demand for them first (Boycko, Shleifer), necessarily take longer (Fischer and Gelb)

# No possible theory of transition?

- Sargent: “In 1989 the problem of 'transition dynamics' forced itself on economists and statesmen. Two generations of work on economic dynamics within parallel traditions in game theory, macroeconomics, and general equilibrium theory have given us theories of dynamics that have their best chance of applying when people are in recurrent situations that they have experienced often before. In Eastern Europe the transition is not like that: people there are confronted with unprecedented opportunities, new and ill-defined rules, and a daily struggle to determine the 'mechanism' that will eventually govern trade and production. Economists who dispense advice about governmental strategies to enable transitions to a market economy can do so with ample help from 'equilibrium theories' describing how to expect a system to operate after it has fully adjusted to a new and coherent set of rules and expectations, but with virtually no theories about the transition itself. We might have prejudices and anecdotes to guide our preferences among transition strategies, but no empirically confirmed formal theories. [1](#)

- No doubt capitalism as we know it, encumbered
- on all sides by interventionism and State-created
- monopoly, and distorted by the vagaries of mismanaged money, is very far short of the accuracy of competitive adjustment. But with all its deficiencies in this respect, it seems a much more flexible mechanism than the collectivist alternatives.

# Gradualism or big bang?

## Robbins's view?

- 1947 Marshall lectures: gradual transition to free prices in postwar Britain
- Hayek too in *Road to Serfdom* (1944), “would discredit” market to do at once
- Contra: Erhard 1948 FRG
- Contra: Corelli Barnett, *The Audit of War*