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Vanhuysse, Pieter

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Czech Exceptionalism? A Comparative Political Economy Interpretation of Post-Communist Policy Pathways, 1989–2004*

PIETER VANHUYSSE**
School of Political Sciences and Faculty of Education,
University of Haifa

Abstract: This article makes a plea for a more explicitly intentional and political-strategic analysis of post-communist public policy pathways. The author analyses a set of social and labour-market policies implemented in the Czech Republic (pro-active job loss prevention) compared to Hungary and Poland (large-scale non-elderly retirement), and indicates why, far from being fully constrained by structural or external variables or by international pressures, political elites were able to design policy packages that served to reduce anti-reform protests. Once enacted at a formative historical turning point, these early policies fundamentally reshaped the subsequent operational space of post-communist politics throughout the 1990s. They crystallised the distinct pathways of post-communist welfare regimes, and they enabled early, and irreversible, democratic and market reform progress. While seemingly inefficient, and definitely costly in public-finance terms, these policy packages contained a degree of political rationality, as they contributed to the making of the great Czech, Hungarian, and Polish transition success stories, in an otherwise highly heterogeneous population of post-communist transition cases.

Keywords: public policies, political strategy, constrained democratic efficiency, East European welfare regimes, post-communist transformations, path contingency

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** Direct all correspondence to: Pieter Vanhuysse, School of Political Sciences and Faculty of Education, University of Haifa, Mount Carmel 31905, Haifa, Israel, pieterv@construct.haifa.ac.il

> *I consider the transformation of the Central Eastern European region a success story because it established a capitalist economic system within a historically brief timeframe, thereby placing our nations again on the course of development leading towards the main direction of history.*
> János Kornai [2006: 226]

As I write these lines, the Czech Republic has been a full EU member for two-and-a-half years and is fast approaching the twentieth anniversary of the uprisings on Wenceslas Square and the similar popular mobilisations that precipitated the fall of communism. This is a good time to take stock of what we have learned about the public policy pathways taken since 1989. This article proposes a number of theoretical arguments on constrained democratic efficiency, the success (or lack thereof) of post-communist social and economic policy reforms, and, in particular, the political causes and consequences of recent Czech policy pathways as compared to those in Hungary and Poland. In so doing, I present, and further elaborate upon, a number of key arguments set out in my book *Divide and Pacify: Strategic Social Policies and Political Protests in Post-Communist Democracies* [Vanhuysse 2006a]. Consider the following observation, especially in light of the remarkable Hungarian riots of early autumn 2006: Contrary to prior expectations, contrary to earlier democratic and economic reform experiences in the 1970s and 1980s, and notwithstanding a number of high-profile individual cases of mass strikes or protests, the Central European transitions to market democracy have actually been distinctly non-violent and non-disruptive [e.g. Greskovits 1998; Vanhuysse 2004a]. In *Divide and Pacify* I examined the interplay between labour militancy, (neo)corporatist institutions, state policies, and social and labour-market strategies, developing social policy-based explanations for the remarkably limited number of strikes and protests, despite the high social costs of transition. This perspective overlaps with a number of social science research strands, including the Varieties of Capitalism literature, the political economy of democratic transitions and policy reforms, the political sociology of strikes, protests and contention, and the comparative political economy of welfare regimes.[1]

[1] Like much of the Varieties of Capitalism literature [e.g. Kitschelt et al. 1999; Hall and Soskice 2001; Hancké, Rhodes and Thatcher (forthcoming)], *Divide and Pacify* explores different constellations of state policies, labour-market institutions, and unions – but in the novel context of the early post-communist market democracies; which is a hitherto barely explored terrain [see also Pop and Vanhuysse 2004]. The book draws deeply on the political economy of transitions and policy reforms [e.g. Offe 1991, 1993; Rodrik 1996; Greskovits 1998; Vanhuysse 1999; Barr 2005; Hasselmann 2006] and on the comparative politics of contention [e.g. Tarrow 1998; Crowley and Ost 2001; Vanhuysse 2004a, 2006b] and welfare states [for general overviews, see Esping-Andersen 1990, 1999; Pierson 1996, 2001; on pensions, see Myles and Pierson 2001; Vanhuysse 2001, 2004b; on welfare attitudes, see Sabbagh and Vanhuysse 2006a, 2006b; Sabbagh, Powell and Vanhuysse (forthcoming)].

In a nutshell, I argue that social and labour market policies constitute a crucial yet hitherto inadequately explored reason for the comparative success of the Czech, Hungarian, and Polish transitions. To see why, we need to adopt a more explicitly strategic and political lens on post-communist policy design. Emphasising the ways in which welfare state programmes can be manipulated by governments in an attempt to prevent or forestall disruptive mass protests, Vanhuysse [2006a] identified a political strategy that could significantly reduce the capacity of selected groups of job-threatened workers to organise large-scale collective action. As I indicate in this article, over the course of the 1990s, social policy packages consistent with such a thesis have in fact been adopted in Hungary and Poland, though not in the Czech Republic. However, in the Czech case, I discuss a number of ways in which public policies, while seemingly exceptional, have exhibited equivalent elements of strategic manipulation by political leaderships eager to achieve particularly urgent goals — social peace in the polity, as a strong prerequisite for fast progress in reforming former communist dictatorships into liberal democracies and capitalist economies. I conclude by arguing that, when viewed from an integrated political economy perspective, seemingly inefficient policies turn out to have contained a degree of political rationality.

1990 as a critical juncture — or, policymakers did make (fateful) policy choices

> *Economic change ... is for the most part a deliberate process shaped by the perceptions of the actors about the consequences of their actions. The perceptions come from the beliefs of the players – the theories they have about the consequences of their actions – beliefs that are typically blended with their preferences.*
>
> Douglass North [2005]

In order to develop satisfactory explanations of post-communist policy reforms, it is necessary to simultaneously acknowledge and circumscribe the causal role of 'structure' and 'history' or 'legacy.' Given the strong and pervasive effects of the communist one-party systems and planned economies on Central European societies for over four decades, it would be unwise to dismiss these concepts entirely (for broader perspectives, see Ekiert and Hanson [2003]; Mahoney and Rueschemeyer [2003]; North [1990, 2005]). But we need to move beyond the highly aggregate concepts predominant in the transition literature, such as the novelty of democracy, the presence of tripartite bargaining institutions or demographic variables, rural density, national tax revenues, indebtedness and welfare spending, poverty or income inequalities, to explain post-communist policy reforms. The role of history and structure can be spelled out and theorised at intermediate levels, and as partly subject to manipulation by governments, rather than inherited or invariant beyond strategic action. Political path-dependence theories can be insightful here. But for such theories to have value-added as an explanatory framework, beyond the vacuous claim that history matters, they need to specify two elements as precisely as possible [Pierson 2000, 2004]. First, what was the initial point at which one path rather than another was taken? Second, what were the causal mechanisms that subsequently locked in that particular path once taken? In Central and Eastern Europe around 1989–1990, the first point is unusually clear. The transition to market democracy was an exceptional instance of large-scale social change; a formative historical turning point. At a time when civil society was not yet a strong countervailing force, the first democratic governments were able to reverse the course these societies had taken for over four decades.

One core policy area where there were particularly significant consequences to result from the early choices made is the welfare state in general and pensions in particular. Set up shortly after Second World War, by 1989–1990 Central European pension systems had reached maturity. Between 1960 and 1980 alone, pension replacement rates (benefits/average wages) had already converged to high levels in Hungary (from 32% to 55%), Poland (from 40% to 46%) and the Czech Republic (from 60% to 54%). System dependency rates (actual pensioners/actual workers-contributors) had also increased significantly, from 24% to 43% in Hungary and from 20% to 35% in the Czech Republic [Müller 1999]. However, despite similar legacies and starting points, in subsequent years pension policy pathways in Hungary and Poland rapidly diverged from those in the Czech Republic. Elsewhere I have documented how post-communist governments in the first two cases, but not in the third, provided the legal and financial incentives and the implicit encouragement for scores of working-age citizens to become non-elderly pensioners. Between 1989 and 1996 alone, the number of old age pensioners increased by a mere 5% in the Czech Republic, but by 20% in Hungary and by 46% in Poland. In the same short period, the number of disability pensioners increased by respectively 11%, 49%, and 22%. These figures indicate radical shifts in the lives of many hundreds of thousands of Hungarians and Poles. Additionally bearing in mind that demographic pressures in these societies were relatively mild at the time, these developments in the latter two countries can be labelled 'the great abnormal pensioner booms' of the post-communist transitions [Vanhuysse 2004b, 2006a: 87–89].

From a public-finance viewpoint, these were distinctly sub-optimal policies. Abnormal retirement was doubly hazardous, as it increased the numerator of the pension system dependency rate while simultaneously decreasing the denominator. The number of pensioners increased by respectively 22% and 35% in Hungary and Poland in these seven years, while the number of workers-contributors decreased by respectively 25% and 14% [Schrooten, Smeeding and Wagner 1999: 281]. Existing theories cannot be automatically applied to account for these events. Public choice and political economy theories concur in their explanations of why welfare programs prove difficult to reform or retrench, even when this would enhance aggregate welfare. Serious impediments can be expected to arise if a) losses are certain or concentrated while benefits are less visible or more diffuse, b) the identity of winners and losers is uncertain ex ante, c) voters are more sensitive to losses than to gains, or d) median voters are elderly or approaching retirement age [e.g. Olson 1965; Quattrone and Tversky 1988; Fernandez and Rodrik 1991; Breyer 1994; Rodrik 1996; Vanhuysse 1999, 2004b]. The 'new politics of the welfare state' literature proposes that politicians face an uphill battle in reducing welfare program generosity while avoiding blame for it [Pierson 1996, 2001]. The political logic behind mature pay-as-you-go pension systems further complicates reforms. When shrinking pools of workers-contributors need to finance large or fast-growing pools of pensioners-beneficiaries under conditions of slow real wage growth, the financial balance of such systems is endangered. However, when switching to fully funded pension arrangements, current workers must simultaneously finance current pensioners and their own future pensions. This transitional double-payment problem presents a strong political barrier to systemic reforms of public pension schemes [Myles and Pierson 2001; Hasselmann 2006].

But while it is one thing to predict that politicians may find it hard to reform or retrench mature pension systems with growing financial imbalances, it is quite another to posit that they will strongly add to the already existing imbalances by *expanding* rather than retrenching the systems — in a period, moreover, of strongly decreasing fiscal revenues [Vanhuysse 2001, 2004b]. However, by allowing hundreds of thousands of working-age individuals to retire within just a few years, the Hungarian and Polish governments did precisely this. They actively *created* a pensions crisis towards the mid-1990s, where there had been none in 1989. A large amount of literature in sociology, social policy, political science, and economic policy has described these developments [e.g. Boeri 1994, 1997a; Boeri, Burda and Köllö 1998; Elster, Offe and Preuss 1998; Macha 1999]. However, this literature heavily underplays the fact that 'the great abnormal pensioner booms' were not a purely exogenous characteristic of the transition. Rather, they involved policy parameters that were still largely at the discretion of governments. Nor do existing accounts explain why pension policies that directly contradicted national financial prudence, international financial pressures, and basic economic common sense, were nevertheless enacted by domestic policymakers [see Hasselmann 2006 for an exception]. For example, Müller [1999: 56] argues that by 1996 the precarious state of external debts and pension finances in Hungary and Poland, but not in the Czech Republic, necessitated systemic pension reforms only in the first two countries. But she provides no convincing causal narrative explaining why finances spiralled out of control *before* 1996 and why they did not in the Czech case. Received wisdom agrees that pension reforms until the mid-1990s 'were slow, piecemeal, and not sweeping enough', and that the ensuing pensions crisis that 'did not stem from population ageing but was transformation-induced.' Others interpret the pensioner booms as essentially unforeseen or unintended consequences of decisions by non-strategic or simply bewildered politicians [e.g. Müller 1999: 71, 150; Schrooten, Smeeding and Wagner 1999: 282; see also Hausner 2001; Spéder 2000; Golinowska 1999].

Such explanations are unconvincing because they too heavily view national policymakers as lacking in the ability to make competent and conscious decisions [Vanhuysse 2004b]. After all, new laws were written and approved by parliamentary majorities to create new legal opportunities for workers to retire abnormally, and sometimes to increase the generosity of benefits. A new law in March 1991 created two additional legal opportunities for early retirement in Hungary. The new pension benefit calculation formula implied that beyond 32 working years workers could gain almost nothing from continuing to work Similarly, the Polish Sejm twice passed new laws in 1990 to ensure that pensioners were better protected from hyperinflation. A quarterly indexation mechanism was first introduced in May 1990. Minimum pensions were increased, while indexation was based on average wage growth. Regulations were similarly introduced in 1991 to allow early retirement specifically for workers who were made redundant, without the loss of benefits [Müller 1999: 66–68; Spéder 2000; Inglot 2003: 222; Cain and Surdey 1999: 158; Czepulis-Rutkowska 1999: 152].

The case of the Czech Republic further indicates why post-communist pension policies were not uniformly dictated by external circumstances or international institutions. Unlike their Polish and Hungarian counterparts, and despite being faced with larger, not smaller, pensioner constituencies at the start of transition, Czech legislators moved to retrench rather than expand their pension system (more on this below). In early 1993, all special privileges were abolished. Retiring early was possible only under two sets of circumstances, both of which entailed a significant reduction of the earnings-related component of benefits. Czechs wishing to retire two years early had to have been on the unemployment register for at least 180 days. Their pensions were then reduced by 1% for every 90 days of pension taken prior to official retirement age, although this reduction was lifted upon reaching the official retirement age. Czechs wishing to retire three years early saw their pension benefits reduced by 0.6 percent for every 90 days, and permanently so [Müller 1999: 132, 146fn]. While early exit mechanisms were somewhat relaxed by the senior incumbent party ODS (Civic Democratic Party) to appease unions and the KDU-ČSL (Christian Democratic-Czech People's Party) coalition partner [Večerník 2006a: 7], these mechanisms were less pronounced than in Hungary and Poland.

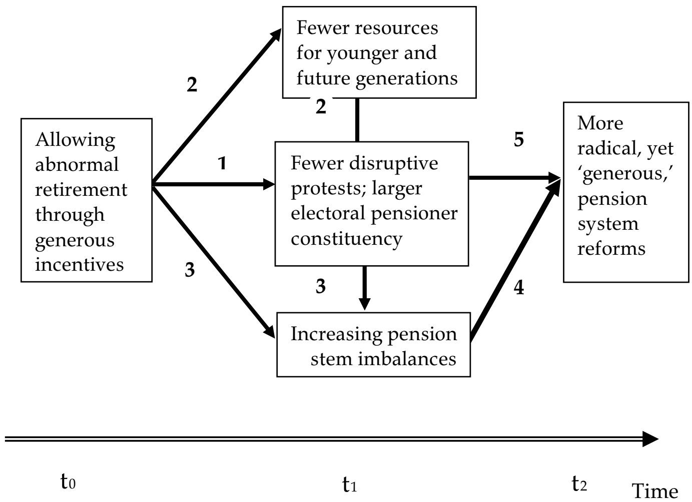
How best to assess these divergent, early policy choices? As Douglass North's recent writings on economic change in history have reminded us, the actions and beliefs of the elite political and economic entrepreneurs who shape policy are crucial for understanding the evolution of societies over time. Indeed, North [2005: 3] emphasises that: "The key to understanding the process of change is the intentionality of the players enacting institutional change and their comprehension of the issues". Discussing path dependency throughout history, North [1990: 98–99] also hammers home the point that: "At every step along the way there [are] choices – political and economic – that provide ... real alternatives. Path dependence is a way to narrow conceptually the choice set and link decision making through time. It is not a story of inevitability in which the past neatly predicts the future". The benchmark assumption of non-intentional or overly constrained policymaking is therefore neither a helpful nor a complete and coherent explanation of the social policy packages adopted during the extraordinary political juncture of the early 1990s. Existing 'non-political' or 'external' accounts are imbalanced, in that they too heavily impute non-intentional behaviour to post-communist policy-makers – a social-science approach that anyway holds little theoretical appeal in general [Elster 1986, 1989, 1993; Alesina 1994; Rodrik 1996].

Conversely, I argue that after 1989 political elites were able to make purposive decisions *within* the parameters set by external, structural, and legacy constraints rather than being eclipsed by them. Developing a more explicitly intentional and strategic-political interpretation of public policy design, I have suggested that transferring core groups of threatened (and unionised) workers onto welfare programs promised large political payoffs for post-communist governments [Vanhuysse 2006a]. By splitting up of well-networked and formally organised groups of workers, sending some of them onto unemployment benefits and many others onto 'abnormal' pensions — early retirement and disability retirement — the capacity of such workers to successfully mobilise for large-scale strikes and protests was reduced. In part, this was due to the reduced sense of agency and to the less heterogeneous social networks among unemployed and retired people [Gallie, Marsch and Vogler 1994; Gallie, Kostova and Kuchar 2001; Gallie and Paugam 2000]. Both groups tend to have fewer weak ties, which makes it harder for them to the unemployed and pensioners to reach out to actors with different political and social-economic positions and resources in order to organise collective action. In part, workers, the unemployed, and abnormal pensioners, who had until recently worked together in the same workplace and had shared very similar material interests, were now locked into a range of mutual distributional conflicts over scarce, and ever scarcer, state resources. Moreover, during a period of declining living standards, the unemployed and the abnormal pensioners had stronger economic incentives to earn informal private sector incomes — a Hirschman-type exit — instead of pursuing public goods through collective protests, i.e. through a political voice [Greskovits 1998; Vanhuysse 2006b]. Divide and pacify policies were one among many policy paths that could have been taken. But the fact that they were taken in Hungary and Poland, and *not* in the Czech Republic, has had significant political and policy consequences.

Into the 21st century — the path-contingent evolution of welfare regimes

Path-dependence theories can help to explain the *persistent* differences in the larger work-welfare pathways taken by post-communist societies, as once-contingent early policy choices have strongly shaped subsequent social, economic, and political outcomes. Having spelled out how policy choices in the early 1990s initiated particular pathways, the task now is to distinguish the *self-reinforcing* mechanisms that locked in these initial policies in the late 1990s and into the present century. Mirroring Douglass North's views, Margaret Levi [1997: 28] notes that: "path dependence has to mean, if it is to mean anything, that once a country or region has start-

Figure 1. Post-communist welfare regime pathways: the temporal dynamics of early social policies



Source: Vanhuysse [2006a: 105].

ed down a track, the costs of reversal are very high. There will be other choice points, but the entrenchments of certain institutional arrangements obstruct an easy reversal of the initial choice". After the initial pensioner booms in Hungary and Poland, but not the Czech Republic, how did the work-welfare regimes of these three societies crystallise subsequently? Figure 1 depicts some causal mechanisms indicating how the choice sets of post-communist policy-makers were constrained and narrowed over time.

As Vanhuysse [2006a: Chapters 5 and 6] spells out in much greater detail, over the course of the 1990s the Czech welfare regime has diverged increasingly from those in Hungary and Poland. In the latter two countries, once many at-risk workers had been allowed to retire abnormally (at *t0*), it was impossible for governments to reverse this exit later. The pension system was now more likely than ever to require reforms in later years (at *t2*). But the wider work-welfare set-up of society was now imbalanced. The new abnormal pensioners depended on state benefits rather than working wages, but they represented less of a disruptive threat. Thus the nature of post-communist politics was altered. More powerful pension demands by over-sized pensioner constituencies could be expected at the end of electoral cycles, but fewer protests occurred in the short run (cause 1). Compared to young or middle-aged households, pensioner households depended to a greater extent on the state for their income. Post-communist pensioners had now become a classic example of a powerful and single-minded voting constituency. The real value of their public pensions formed a common interest that was both easily identifiable and of high importance. With already existing cohorts of elderly pensioners newly joined by hundreds of thousands of early and disability pensioners, the pensioner constituency's electoral clout was higher than ever. Even if not all pensioners adhered to a single ideology, or voted as a single bloc, or were even represented in single-issue parties or pressure groups, their sheer size could now pre-emptively influence the policy platforms of politicians.

Since fiscal resources were strongly constrained in the transition, favouring pensioners left fewer resources available for younger or future generations (cause 2 at *t0*). At the same time, the transfer of hundreds of thousands of working-age individuals out of the labour market aggravated pension finances (cause 3 at *t0*). Once the pensioner constituency had been enlarged, it was harder than before to retrench pensions (cause 3 at *t1*). Polish governments stabilised pension replacement rates only after first letting them soar during the first, and socially most costly, years. Successive Hungarian governments were only able to stabilise pension replacement rates and did not otherwise retrench pensions. For instance, the Bokros stabilisation package passed by the Hungarian parliament in May 1995 included such measures as the abolition of universal family allowances, a sharp reduction of child care assistance, and large cuts in civil service jobs, but it never touched pensioners [Vanhuysse 2006a: 82–83, 106–107].

After the great abnormal pensioner booms, systemic pension reform was more urgently necessary than ever before (cause 4). But the way in which this could be done was now more strongly constrained (cause 5). In a process that accelerated from 1996 in Hungary and from 1997 in Poland, both countries took steps to draw up and implement comparatively radical pension-system reforms, including a three-pillar system with a large privatised component [Müller 1999; Müller, Ryll and Wagener 1999; Nelson 2001; Hasselmann 2006]. The mere mention of such systemic reforms had been a political non-starter only seven years earlier. At the same time, the abnormal pensioner booms shifted the dominant distributional politics in these democracies away from the template of 'reform protests' and onto a new political template: *the political economy of gerontocracy,* or the logic of *generational politics*, in which public expenditures for elderly generations are made increasingly at the expense of younger generations. I predict that this logic of distributional conflict between generations will increasingly determine future democratic politics in these societies.[2]

Strongly constrained by the much enlarged electoral clout of pensioners, governments now shifted the reform burdens onto the generations of younger workers and future taxpayers, while continuing to favour current pensioners [see also Goli-

[2] For formal models of the political economy of intergenerational politics, see Browning [1975], Breyer [1994], Sala-i-Martin [1992] and Mulligan and Sala-i-Martin [2003]. For empirical evidence and political explanations, see Myles and Pierson [2001], Campbell [2003], Vanhuysse [2001, 2004b], and Sabbagh and Vanhuysse [2006b]. For an insightful analysis of different political and distributional cleavages within Czech society as seen from a middle-class perspective, see Večerník [2004].

nowska 1999; Simonovits 1999; Nelson 2001; Hasselmann 2006]. Thus the move to the new privatised pillar was made attractive by substantial incentives covered by the general budget. The Hungarian Finance Minister even stated publicly that: "there is no critical threshold in this instance. If there will be more entrants, the budget will cover the whole deficit without any fuss" [quoted in Ferge 1999: 243]. In very recent years, the left-of-centre government has put forward the payment of a thirteenth month of pensions. This has been more than a minor contribution to the worrying rise in Hungarian public deficits, which stood at around 10% of GDP by 2006. As with the pensioner-favouring policies of the 1990s, younger generations will eventually have to pick up the bill.

In stark contrast, the Czechs avoided abnormal pensioner booms early on, and subsequently steered away from some of the political dynamics described above. As Večerník [2006a: Graph 1] shows, average pension benefits as a share of gross wages increased only marginally, from 51% in 1990 to 55% in 1991, after which they were sharply reduced, reaching 45% by 1996 and 40% by 2004, keeping them well below Hungarian and Polish levels all along. As a result, Czech pension finances did not immediately spiral out of control (cause 3). However, the absolute size of the Czech pensioner constituency, although it grew comparatively much less in the 1990s, had been larger to start with in 1989 [Vanhuysse 2006a: 120]. Hence the political economy of gerontocracy also kicked in here. As argued above, the sheer size of pensioners as an electoral constituency could – and did – influence the policy platforms of all office-seeking parties, right across the ideological spectrum. Consider the 1992 and 1996 elections. Pensioners voted respectively three and two-and-a-half times more numerously (13% respectively 9% of all votes) than average voters for the single-issue 'Pensioners for Security' Party (HDZJ). Nevertheless, this party did not obtain a vote share directly commensurate with the (still much larger) electoral clout of pensioners [Večerník 2006a: Table 1]. My theoretical hypothesis of uniform and *pre-emptive* policy platform adaptation by office-seeking parties goes some way towards accounting for this seemingly paradoxical observation.

Crucially, regarding pensions, no radical and *systemic* reforms were implemented in the Czech Republic (cause 4), despite strong pressures from the IMF and the World Bank to install compulsory private co-insurance. As Večerník's [2006a, 2006b] insightful analyses show, neither trade unions nor political parties (with the exception of the increasingly marginal Freedom Union) even proposed any radical reforms. Instead, the pay-as-you-go system was retrenched *parametrically*, and mildly and gradually at that. In 1995, a new set of laws from the ODS-led centre-right government set in motion an incremental increase in the official retirement age, which was to be incrementally raised from 53–57 to 57–61 for women and from 60 to 62 for men. Pension benefit replacement rates were set to drop gradually, to 38% by 2010 and to 35% by 2015.[3] In the face of now worsening system-dependency rates

[3] See Potůček [2001: 94–95, 2004: 258–260]. In the same vein, Potůček notes that a State Social Support Act was introduced by the conservative government in 1995, replacing universal

and pension system financial balances, the social-democratic ČSSD politicians, who gained power in 1998, still rejected all radical pension reforms [Večerník 2006a: 9]. The next ČSSD-led government, which took office in 2002, only moved to abolish temporarily reduced pension benefits as an early exit template. And it only did so once early retirement had become a truly massive phenomenon, with one in two new pensioners retiring early by 2002–2003 [Večerník 2006a: 10]. Finally, different economic and labour market policies further set the Czech welfare regime on a radically distinct pathway.

Czech economic and labour-market exceptionalism — or, how to be a proactively social, apparent neo-liberal

Czech governments have not adopted any large-scale early exit policies. But they have had to deal with fewer strikes than their Hungarian and Polish counterparts [Vanhuysse 2004a]. However, this does not mean that large-scale protests were therefore less of a headache for Czech politicians. The regime change in Czechoslovakia in late 1989 was spurred to a larger degree by massive popular protests. Unions set up 6000 strike committees in November 1989 and organised a nationwide two-hour strike on November 27, in which around 60% of the workforce participated. Soon afterwards, the Communist Party started to relinquish its power. Czechoslovak unions also implemented a large-scale personnel revolution that saw 80% of the old functionaries replaced by 1990 [Myant and Smith 1999: 26; Garton Ash 1990: 80–84; Orenstein 2001: 65]. Since the new union leadership was not allied with any of the governing parties and inherited the strongest union confederation in the entire region, it was able to credibly threaten to mount protests against contested reforms. The government initially attempted to pre-empt this by means of restrictive strike regulation. But the unions reacted by calling a strike alert throughout November 1990. Together with subsequent threats of a general strike, this made the government back down entirely. Union rights were extended, a liberal strike regulation was legislated, and unions were invited to participate in the tripartite Council of Social Accord [Bruszt 1993: 66–68].

Unemployment rates provide the key to understanding Czech post-communist policy pathways (Table 1). At around 3% right up until 1996, these rates were not just conspicuously below those in other post-communist democracies, they were actually lower than anywhere in Europe, and second-lowest among all OECD countries [Kabaj 1996: 52]. Czech protest pre-emption strategies differed from other Central

child allowances with a (still relatively) generous income-tested method; a policy direction which subsequent social-democratic governments wanted, but could not, reverse. By 2002, state support for young Czech families had eroded significantly, dropping by 27% for families with one or two dependent children, by 35% for families with three children, and by 45% for families with one child, compared to 1989 levels.

Table 1. Official end-of-year unemployment rate (UE, in %), and active employment policy expenditures (AE) as % of total employment policy expenditures, Czech Republic, 1990–2002

Year	*90*	*91*	*92*	*93*	*94*	*95*	*96*	*97*	*98*	*99*	*00*	*01*	*02*
UE	0.7	4.1	2.6	3.5	3.2	2.9	3.5	5.2	7.5	9.4	8.8	8.9	10.3
AE	n.a.	31	55	35	28	26	21	14	18	25	37	43	44

Source: Potůček [2004: Tables 5-4, 262].

European democracies mainly in their primary target, which was to avoid large-scale job losses and labour market exits. The Czech equivalent of the Polish Balcerowicz programme, the 'Radical Strategy' blueprint paper, was adopted in April-May 1990. The Balcerowicz plan had no social policy section. By contrast, the social policy section of the Czech paper explicitly spelled out a strategy to avoid the immediate bankruptcy of large enterprises: "There must be sufficient time given for adaptation. Otherwise even viable economic potential will be destroyed, creating mass unemployment. Active structural policy must therefore provide temporary protection to viable enterprises, especially through credit, possibly subsidy, and partly also through customs policy" [Orenstein 2001: 74]. The 'Radical Strategy' document furthermore called for a transitional social policy aimed at standing up to 'the risk of extensive unemployment as well as spiralling inflation and a drop in real wages'. This risk was to be reduced by means of 'structural macro-economic policies, labour-market interventions, and welfare policies designed to preserve a social minimum' [Orenstein 2001: 73–74].

To a greater extent than elsewhere, Czech governments aimed at actively creating employment rather than passively compensating for its loss. This has ensured a higher outflow from unemployment to jobs, as stagnant pools of individuals in danger of rapidly becoming unemployable have been 'churned up' [Boeri, Burda and Köllö: 1998]. Whereas total passive expenditures (transfers) and total active labour-market policies (such as training programs and public works) were equal in scale in Hungary and Poland in 1989, by 1993 passive expenditures were respectively five and nine times larger than active expenditures [UNICEF 1995: 60]. The opposite occurred in the Czech Republic, where the passive/active expenditure ratio decreased from 5 in 1990 to 0.5 in 1993 (compared, for instance, to 0.9 in Sweden and 2.2 in France in 1991). Czech authorities set up a network of 77 regional labour offices as early as 1990, in an effort to provide easy access to a wide range of job services such as labour market information and consultation, professional training and re-qualification, and the creation of job opportunities. Altogether, these active employment offices reached 92% of all unemployed persons. In 1992, they created more than 82 000 new jobs, over 1000 places in protected workshops for disabled people, and 25 000 places for community work, and they completed the re-qualification of 14 600 jobseekers [Potůček 2001: 90]. In 1993, the share of active labour market expenditures in Poland (16%) and Hungary (23%) was significantly lower than the OECD average (33%). But in the Czech Republic (55%), it was higher than in the top-ranking Western country, Sweden (45%) [Kabaj 1996: 33]. As Table 1 shows, after a relative trough in the crisis years 1997 and 1998, this early emphasis on active employment policies was only strengthened once the conservative Klaus-dominated governments were replaced by left-wing governments. By 2002, these policies received as much as 44% of all employment policy expenditures.

The heavier policy emphasis on keeping the employed in work and the unemployed employable translated into better results. Between 1992 and 1996, average inflow rates into unemployment were 1.1 in both Hungary and Poland, but only 0.7 in the Czech Republic. The gap was more striking still for outflow rates from unemployment, at respectively 8.1, 6.3, and 22.[4] And of those who did flow out of unemployment, many more actually found jobs in the Czech Republic, rather than leaving the labour force altogether [Boeri 1994]. By the mid-1990s, the share of long-term unemployment within total unemployment, which was below 40% in Western Europe, hovered around 50% (and rising) in Hungary and Poland. It was above 40% in all post-communist economies – except the Czech Republic, although even there it increased markedly towards the start of the 21st century [Boeri 1994, 1997a, 1997b; Ham, Svejnar and Terrell 1998]. Czech strategies to limit early labour market exit and to emphasise active employment policies led to employment rates of older workers that were significantly higher than in Poland and Hungary, at 84% versus 53% and 44% for men aged 50–59, and at 80% versus 46% and 17% for women aged 50–54 in 1996 [Boeri, Burda and Köllö 1998: 13].

Perhaps the most significant dimension in which Czech governments strayed from market reform orthodoxy was their avoidance of the rapid hardening of budget constraints. A key defining feature of communist economies was the pervasiveness, and persistence, of soft budget constraints, induced through state subsidies to inefficient firms, the lax allocation of bank and trade credits, wage arrears, and so on [Kornai 1993, 1999]. After 1989, Czech governments continued to rely more heavily than other countries on wage controls and continued to allocate consumer subsidies, notably for rent, heat, electricity, and transport [Müller 1999; Elster, Offe and Preuss 1998]. More striking still, they considerably lagged behind in hardening company budget constraints and in implementing the corporate governance regime necessary for this task. Between 1995 and 1997, the proportion of bad loans out of total loans distributed by the banking sector averaged at 7% in Hungary, 17% in Poland, and 29% in the Czech Republic. Between 1993 and 1997, government budget subsidies to firms amounted to respectively 5%, 1%, and 8% of GDP (calculated

[4] Inflow rates are the average annual rates of the number of people flowing into unemployment in a month divided by the number of people employed in a month, multiplied by 100. Outflow rates are the average annual rates of the number of people flowing out of unemployment in a month divided by the number of people unemployed in a month, multiplied by 100 (computed from Ham, Svejnar and Terrell [1998: 1119]).

from EBRD [2000: 156, 172, 196]; see also Kornai [1999]). Similarly, between 1992 and 1996, there was a yearly average of 1895 bankruptcies in Hungary and 1000 in Poland, but only 312 in the Czech Republic [EBRD 1997: 87].

Government policies clearly contributed to these differences. For instance, the Hungarian government enacted a new law back in 1991 requiring all enterprises to switch to Western-style accounting principles. A new bankruptcy act instituted severe penalties for company managers who failed to file for bankruptcy after accountants had sounded the alarm, including a 'harakiri clause' that made managers personally liable in civil courts. As has been extensively documented elsewhere, Czech governments adopted a distinctly softer approach from the very start of the transition until at least the end of the decade [e.g. Kornai 1993, 1999; Večerník 1996; Bruszt and Stark 1997; Orenstein 2001; Horowitz and Petras 2003; Myant 2003; Hasselmann 2006]. In October 1991 the then finance minister Václav Klaus, whose hard-nosed rhetoric on the need to create 'market capitalism without adjectives' earned him the nickname of the Margaret Thatcher of Eastern Europe (at least in the West), managed to get a tough new bankruptcy law through parliament. But despite the rhetoric, the law was never put into practice. By spring 1992, it was suspended for one year, after which it was postponed again. Instead, the Czech government pursued a deliberate anti-bankruptcy policy. This included the creation of the Konsolidační banka (Consolidation Bank) to buy much of the old enterprise debt with privatisation receipts, and repeated interventions by the Ministry of Trade and Industry to prevent dozens of large enterprise bankruptcies. And when bankruptcy legislation was finally released from a two-year deep freeze, it was implemented only selectively [Bruszt and Stark 1997: 155; Orenstein 2001].

Czech legislators also avoided bankruptcies by maintaining relaxed and ambiguous standards. As late as 1997, bankruptcy laws only deemed a debtor insolvent if he could not meet his obligations within 'a long period of time' [Kornai 1999]. While the effectiveness of bankruptcy procedures increased over time in all three countries, a smaller share of all filed bankruptcy cases were actually completed successfully in the Czech Republic than in Poland and Hungary throughout the early 1990s [EBRD 1997: 87]. The specific methods used to privatise state-owned enterprises also had important implications for hardening company budget constraints. Hungarian privatisation proceeded by means of sales to individual corporations, which led to clear-cut responsibilities in the subsequent management of privatised firms. In Poland, governments resorted in part to flexible leasing agreements, which allowed companies to pay off the lease with retained earnings. By contrast, as the above-cited literature on Czech reforms spells out in detail, the Czech Republic stood out for the populist character of its privatisation schemes. Public property was privatised through property restitution and free distribution in vouchers, rather than through sales. Given that the vouchers were retained by individuals, they resulted in multiple small owners – hardly ideal conditions for the effective monitoring of management performance [Kornai 1999: 22]. A substantial proportion of voucher assets became concentrated in investment funds run by big banks that were still state-owned. This preserved connections between formally privatised enterprises and the state, which opened up a channel for subsidies or other soft-budget type protection.

Instead of dealing with the expected electoral costs and protest dangers of unemployment, Czech governments thus adopted a range of strategies to try and altogether avoid mass redundancies. As a result, trust in government and support for economic reforms was higher and less erratic than in neighbouring higher-unemployment countries [Orenstein 2001: 80–81]. Václav Klaus was able to maintain high levels of popular support, allowing him to become the longest-tenured prime minister in Central Europe. Klaus used his reform-leader charisma and his hard-nosed neo-liberal rhetoric to mask a range of policies that were, in their detail, politically 'praguematic,' proactively social, and at times economically far from orthodox. In so doing, he successfully banked on the fact that 'the public had reason to expect that precisely an ideological figure like Klaus would be least likely to compromise the overall vision with muddled compromise in the details' [Horowitz and Petras 2003: 255].

But given the political constraints and the policy overload they faced, a strategic muddling through was perhaps the most anyone could expect from post-communist policy-makers. Sure enough, this comparative softness would later come to haunt the Czech Republic. Soon after Klaus won the June 1996 elections, a string of high-profile corruption scandals and costly large-scale bankruptcies in the financial sector as well as finance scandals in Klaus's ODS party exposed the responsibility of his governments for the deep systemic troubles and the lack of regulation of the Czech banking sector. They forced Klaus to resign in November 1997, temporarily ending a remarkable eight-year stint at the top of Czech policy-making, during which Klaus's party had been one of the very few incumbent parties in post-communist Europe to win subsequent general elections. Long hailed as a pre-eminent transition success model, the Czech Republic now started experiencing rapid increases in unemployment (Table 1) and it came to be viewed as an example of economic policy failure [Orenstein 2001; Horowitz and Petras 2003; Myant 2003]. In sum, Czech social strategies differed in their detail from the abnormal retirement approach adopted in Hungary and Poland. What they had in common was government-instigated efforts to reduce large-scale reform protests, and a degree of economic sub-optimality, or muddling through [Lindblom 1959]. But what does this tell us about the efficiency and the reform progress in these three post-communist democracies?

Conclusion: democratic efficiency after all? — or, there may be no free lunch, but buying lunch makes you run faster

In light of the macro-economic developments since 1997, as sketched out above, the academic literature is unclear in its assessment of the Czech transition pathway. Theorists writing before the economic and corporate crisis deemed the country to be a case of inclusive democracy in which institutionalised accountability led to fast reform progress [e.g. Bruszt and Stark 1997]. But subsequent accounts recognised Czech policy reform failures and even attributed these to the long tenure and political dominance of Klaus and his party, which precluded policy learning and the correction of mistakes [e.g. Orenstein 2001; Horowitz and Petras 2003]. At first sight, the policy packages discussed in this article similarly appear to have all the trappings of sheer bad design. The avoidance of stricter budget constraints early on only led to belated macro-financial troubles in the Czech Republic. Sending hundreds of thousands of working-age Hungarians and Poles into abnormal retirement had straightforward consequences for pension finances. Yet it would be unwise to prematurely jump to conclusions about the apparent inefficiency of these policies. At a deeper theoretical level, economists such as Wittman [1989] and Stigler [1992] have built on the Coase Theorem to argue that whatever policies exist (or, at least, persist) in democracies *must be* considered efficient. However, such arguments are flawed at their Coasean core, as they do not incorporate inherent traits of real-life democracies, such as collective action failures, information problems, and principal-agent problems. It is therefore better to use concepts of *constrained* efficiency or *remediable* inefficiency as yardsticks, and to explicitly incorporate the inherently political constraints and motives of democratic policy-makers within any theoretical analysis of their policies [Dixit 1996; Vanhuysse 2002].

As applied to the post-communist policy packages discussed above, enhancing workers' job security or sending at-risk workers into relatively safe retirement, despite its substantial public-financial cost, may also have contributed to policy efficiency by lowering classic hurdles to efficiency-improving reforms stemming from the time-inconsistency of compensation promises [Dixit and Londegran 1995] or from individual-specific uncertainty [Fernandez and Rodrik 1991]. And importantly, we must not lose sight of the fact that successive Czech, Hungarian, and Polish governments, acting in often bewilderingly complex and uncertain policy environments, managed to maintain a high degree of political quiescence in the face of strong grievance levels among the losers in the transition. This in turn provided them with the operational space to quickly entrench the market economy and the formal institutions of democracy, however imperfect these may still be today. I have [Vanhuysse 2006a] therefore proposed the counterfactual argument that without resorting to abnormal retirement policies (Hungary and Poland) or job loss avoidance policies (Czech Republic), post-communist governments could not have implemented initial political and economic reform measures as quickly and as irreversibly as they have done. Buying lunch makes one run faster.[5]

[5] To be sure, a number of other factors also played a role. Obviously, the 'velvet divorce' of the Czech and Slovak lands was one major factor, even though it was a 'short good-bye' [Innes 2001]. Although its role ought not to be overestimated in the early part of the 1990s, the expected accession to the EU has also been both a spur and a straightjacket for policy reforms [Potůček 2004; Barr 2005; Vanhuysse 2006c]. The accelerated reduction of heavy-industry employment, the privatisation of state-owned enterprises and the liberalisation of many domes-

Take economic reforms: countries such as Slovakia, Romania and Belarus considerably lagged behind Hungary, Poland, and the Czech Republic in terms of privatisation and internal and external liberalisation from the early 1990s onward [de Melo, Denizer and Gelb 1997; Vanhuysse 1999]. Moreover, early reform progress led to continued reform leadership. By the end of the last century and into the present one, the Czech Republic, Hungary, and Poland still occupied the top three spots within a sample of eleven post-communist countries with respect to economic and legal transition, economic freedom, and political freedom. And they vied for the top spots together with Slovenia with respect to country risk, press freedom, and corruption perception [Ekiert 2003: 95]. Next, consider political and civic reforms: the Freedom House index, which ranges from 1 (most free) to 7 (least free), indicates that Hungary, Poland and the Czech Republic all experienced significant progress from the mid-1980s to the mid-1990s, going from values of respectively 5, 5 and 6 to 1.5. Countries like Romania (2) and Bulgaria (2.5) had not advanced as much by the mid-1990s, while Belarussians (6) still suffer even now the same lack of political freedom as Czechoslovaks have had over a decade earlier [Freedom House 1997: 6]. Similar results were observed with respect to corruption [Lipset and Lenz 2000].

In sum, seemingly inefficient early social and labour-market policies are likely to have contributed to fast progress in installing procedural democracy and the market economy at a critical historical juncture. Once accomplished, these early successes, if not actually setting in motion a virtuous cycle of further reform progress at least carried these nascent market democracies beyond a certain threshold, below which they would not be able to fall again. In the absence of such early reform progress, a vicious cycle of reform stalling by coalitions of transition losers would have been the more likely scenario. In this light, it is important to remember that today the population of post-communist regimes is extremely diverse. Herbert Kitschelt [2003] notes rightly that there is at present no region or set of countries on earth with a greater diversity of political regimes than the post-communist region. Moreover, the sources of this diversity can be traced precisely to the critical first few years immediately after the fall of communism. The post-communist diversity "came about in the short window of about three years (1990–1993). Since that time, new regime structures have been more or less 'locked in' in almost all polities"

tic economic activities and foreign investment reduced union density levels. Moreover, unions in Hungary and Poland were often in an ambiguous alliance with reforming parties in government, which led them to call for moderation even when it hurt labour interests [e.g. Bruszt 1993]. However, though such alliances were not present in the Czech Republic, union decline was equally pronounced. Czech central union leadership was mainly interested in flexing muscle through calls for national rallies in Prague, but it never got involved in building up local union organisation at the workplace level [Pollert 2001: 20]. More generally, across a wide variety of political-institutional settings, post-communist unions have comprehensively failed to defend material interests of their remaining membership; which is one of the most striking stories of post-communist transformations [Crowley and Ost 2001; Pop and Vanhuysse 2004].

[Kitschelt 2003: 49]. But in the Czech Republic, as in Hungary and Poland, it had become increasingly hard to conceive of major reversals of democracy and the market already by as early as 1996 or 1997. By this yardstick, it could be argued that the free market economy and liberal democracy (at least in its formal and procedural aspects) were fully consolidated extremely early.

With the benefit of seventeen turbulent years of hindsight, such a 'transition complete' message may no longer seem to be all that remarkable today. But it is worth remembering that very few experts were confident about the likelihood of such smooth transition pathways when the Berlin Wall came tumbling down back in autumn 1989. And as Kornai [2006] and I [Vanhuysse 2006a] have emphasised at length, we need to acknowledge the corruption of political and economic elites, the heavy social costs of the transition, and the often alarmingly high levels of popular disappointment and of disillusionment with the institutions of liberal democracy in much of post-communist Central and Eastern Europe. Yet this ought not to make us disregard, let alone forget, the observable empirical fact that the astonishingly fast, complete, and non-violent nature of this latest wave of transitions to democratic capitalism has altogether constituted a great success story – indeed, a historically *unique* move forward for human freedom.

PIETER VANHUYSSE *received his PhD from the London School of Economics and is currently a lecturer at the University of Haifa. His work centres on the politics of social policy, education, human capital, and democratic transitions, and has appeared in journals such as* Political Studies, Europe-Asia Studies, East European Quarterly, Politics, International Journal of Sociology and Social Policy, Social Psychology of Education, Journal of European Public Policy, *and* Journal of Social Policy. *His book on* Central European transitions, Divide and Pacify: Strategic Social Policies and Political Protests in Post-Communist Democracies, *was published by the Central European University Press in 2006.*

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