



Circles Within Vicious Circles

Redevelopment
in
Eastern Europe

Professors
Craig MacPhee and
John Anderson

Capitalism and its accordant principles is such a part of the American fiber, it is a difficult leap for most of us to realize that what we understand almost by instinct is really the outcome of a jealously protected system of laws and expectations that have taken centuries to develop.

Nearly twenty years after President Reagan demanded, “Mr. Gorbachev, tear down this wall, the states of the former Soviet Union still are victim to gangsters and corruption. There was an optimistic idea that when the people were freed from the shackles of Marxism and tyranny, the entrepreneurial spirit would sour and soon those newly formed countries would be thriving under the precepts of capitalism. The reality is very different; progress is being made, but slowly.

The College of Business Administration at the University of Nebraska–Lincoln has been a crucial part of the long process to redevelop these countries. Operating under grants from USAID, many of our Professors have provided expertise and guidance to governments, business people, and educators. As the map of Eastern Europe continues to shift, more new countries are asking for assistance to redevelop their infrastructures and thought processes, and our professors continue to lend their support.

USAID – United States Agency for International Development is an independent federal government agency that provides foreign assistance and humanitarian aid to advance the political and economic interests of the United States.

Two of our professors of economics were on site to advise the governments of former communist countries. Their experiences are related in the following stories.



Moldova

Privatization & Property Rights

John Anderson, Chair of the Department of Economics and the Baird Family Professor, was in Moldova during 1998-1999 and has returned four times since then for short-term advising. Moldova was ruled by Romania, until taken over by the Soviet Union following World War II. It lies inland from the Black Sea, surrounded by Ukraine to the east and south, and Romania to the west.

“As an educator, the opportunity to lecture the members of Parliament of Moldova on the key elements required for an economic transformation was a great moment in my life.” Anderson worked with Frank Cooksey, former mayor of Austin, Texas, on the Local Government Reform Project, or what they called, “OK, I have been elected mayor, now what do I do?” The target group had little idea as to municipal governing, since the concept of a mayor who was not acting under directions from the central government was so alien.

After researching the existing systems and taking into account the previous experience of the newly elected mayors, Anderson and Cooksey prepared a “Local Government Resource Guide,” beginning with the most basic idea of

privatizing land and capital, then creating property rights and the institutions to protect property rights. The most basic ideas of urban economics had to be described in detail with the implementation plans clearly laid out. The result was better and more cohesive systems used throughout the country. The mindset of the elected and appointed officials changes slowly, and often the official would slip back to the old ways of favoritism, collectivism, and bribery.

A continuing theme of redevelopment in Eastern Europe is property rights and laws. Personal property is a new concept for most of the people. Prior to the advent of Marxism and Communism, these were feudal countries; they have never been open to universal property ownership. Under the feudal system, even the landowners maintained their property at the pleasure of the ruling despot, essentially having no rights by law, only by whim.

With decentralization, the central governments wanted to disburse the property, to give ownership to the people who were living in the apartments, homes, and farms. The questions of who gets the property, how much they have to pay for it, what if they can't pay

*Scenes of Moldova
Photography by Dr. John Anderson*

“...to create a fair and equitable tax base, property laws must be created and enforced equally...that presumes an appropriate legislative and enforcement system which has never existed in Moldova.”

John Anderson



anything, what rights do the new owners have, seemed insurmountable.

According to Anderson, property values since independence are a remarkably accurate indicator of the economic health of an area. From those relatively stable values, a basic local tax base can be created from which revenue can eventually be derived.

A consistent tax collection policy in any of these former Soviet Republics is so difficult, that it caused Anderson to insert a little levity by creating the “Top Ten Ways to Not Collect Taxes in Moldova” to capsule the problems. They run the gamut from granting capricious exemptions, to permitting corruption in collecting, and encouraging smuggling. The Number One way to not collect taxes is “Don’t pay the tax collectors. By not paying them you give them the opportunity to seek bribes. That way you can undermine public confidence in the tax system and assure

that taxpayers have no predictable way to know how the tax system works.”

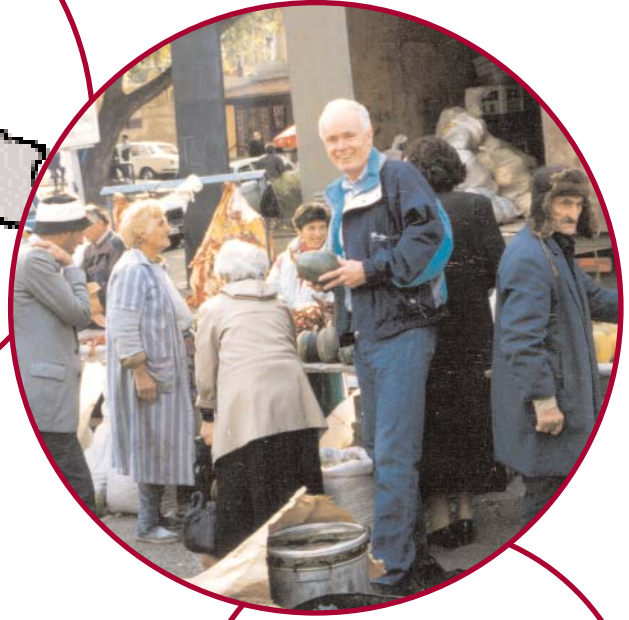
In order to create a fair and equitable tax base, property laws must be created and enforced equally. Judges must have the training to enforce the laws, and the judges must be above reproach. As with the tax collectors, judges are poorly paid and poorly trained, and generally run their courts by demanding bribes for favorable rulings.

Foreign investment is limited because there are few enforceable property laws, making any investments in the country vulnerable to take over by the government or the gangsters.

“Privatization didn’t really fail. The burdensome tax, in the form of protection, levied by the mafia in these countries caused many of the failures of business.” Anderson tells the story of a successful dairy farm that was opened by a foreign investor in Moldova. After

a few years it was producing well, providing dairy products to the surrounding area at a reasonable cost. Then it caught the eye of the gangsters who eventually forced the foreign ownership out and confiscated the business by demanding greater and greater amounts of money for protection. There was, practically speaking, no recourse for the owners, because the laws governing property are limited and not enforced.

“Development is slow in these countries. Markets presume property rights, but property rights can’t be established because the legislative system is not functional, and even if the appropriate laws were established, they would need enforcement; and since the judges aren’t paid, they make decisions based on bribes rather than enforcing the laws. It is the way business has been transacted there for generations.” ♦



Republic of Georgia

The Stalin Legacy

The following are excerpts from MacPhee's soon to be published book, *Roll Over Joe Stalin: A First-hand Account of the Difficult Transition from Communism to Capitalism*.

One of the most infamous Bolshevik revolutionaries was a Georgian. Stalin left two terrible legacies in Georgia as well as in the rest of the Soviet Union. Through the expropriation of private property, the centralization of control over production, and the ruthless suppression of independent thought, Stalin practically eradicated individual initiative. And through his erratic and arbitrary tyranny over peoples' lives, even to the point of ending the lives of millions, Stalin bred almost universal fear of and disrespect for government. These Stalinist legacies impede the transformation of the Georgian economy, raising more obstacles to reform than early Western advisors ever anticipated.

The World Bank wrote blueprints for reform, the IMF attached long lists of conditions to its loans, and the USAID drafted restructuring plans for Georgia. In the beginning, however, no one in the technical assistance community appreciated the difficulties in actually implementing reforms.

Western advisors initially tried to reform the sick economies of the former Soviet Union by prescribing PILLS: Privatization of the means of production; Investment to replace and expand the antiquated equipment and crumbling structures; Liberalization of prices and trade; Legislation to establish a rule of law; Stabilization of fiscal and monetary policy to reduce inflation and unemployment. The legacy of Stalin and other despots makes PILLS alone inadequate for reform in the former Soviet Union. A long history of foreign rule and especially the last seventy years of bad government left people

When Craig MacPhee traveled to the Republic of Georgia as an USAID consultant to the Georgian Government, he was advised to wear conservative clothing in order to blend in with the people of the country.

with attitudes that sabotage the prescription of PILLS. This is the most important and difficult lesson that I learned trying to help establish the foundations of a modern market system in Georgia.

In the decade since independence, why hasn't the prescription of PILLS brought this corner of the former Soviet Union at least back to the meager communist standard of living? Partly, the failure to cure Georgia's ailments has been a result of failure to follow the prescription. Privatization of large-scale enter-

“Excise taxes on gasoline could help solve Georgia’s fiscal problems, but collecting them in the face of high level corruption proves to be nearly impossible.”

Craig MacPhee

The future of Albania rests on the effective utilization of its rich human capital, especially young business students and entrepreneurs. They are Albania’s future leaders.”

Sang M. Lee

Albania

Perhaps the one reform that has the greatest impact on a re-developing country is the re-development of the education system.

The tiny country of Albania is in south-eastern Europe, bordering the Adriatic Sea and Ionian Sea, between Greece, Macedonia, and Montenegro, and has a landmass slightly smaller than Maryland.

“Jack Goebel* and I left Zurich in May of 1991 and after a flight of about 1 1/2 hours, we arrived in Albania in 1940,” Lee describes his first exposure to Albania. Albania has a history of continuous invasion and occupation, culminated in 1945 when the ruthless communist dictator, Enver Hoxha, claimed control of the country, and Albania became one of the most isolated and poorest countries in Europe. In 1992, new leadership was democratically elected and the country began to show strong signs of economic growth. The growth was short lived, however, cronyism and corruption, the evil twins of the communist system, grew again and brought the government and the

prises that once accounted for the most employment has been agonizingly slow as evidenced by the inactive factories on the streets of Tbilisi. Legislation has not been sufficient to guarantee property rights. Consequently, Georgians have a tendency to hoard what little wealth they have behind the shabby exteriors of their buildings instead of making Investments. Liberalization of trade and prices also has been incomplete, explaining a major part of the difficulties in the mass transit system. Finally, the government has been unable to inspire confidence that it can maintain stabilization of the value of its currency.

I witnessed the sad state of higher education in Georgia when the Georgian Technical University invited me to give a series of economics lectures in 1999. But by then, I had visited and lectured at a dozen universities in the former Communist bloc and most of them were in similar shape. Stalin had left his mark on the academic environment. Some professors clearly feared getting too far out in front of the academic reform movement for fear of retribution. UNL

economists were among the first to receive grants from the United States Information Agency to re-train Russian professors. UNL Professor Bill Walstad, and UNL Ph.D. candidate, Stanley L. Brue, joined MacPhee in Moscow to conduct a three-week seminar .

At a ceremony inaugurating our seminar and the adoption of the textbooks on macro and microeconomics by Campbell R. McConnell of the University of Nebraska and Brue, the glasnost-era dean of the economics college bluntly stated that the historical preoccupation with Marx was a mistake. The McConnell/Brue text, which was originally authored at UNL, was the first western economics book available in the former Soviet Union, and copies are still so scarce that they are copied, shared, and treasured. “We inhaled communism for 70 years. Give us a few years to exhale,” said one of our Georgian colleagues. This is a large and relatively isolated part of the world with academic institutions that will change slowly, but that are surely in an irreversible process of change. ♦