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The Postsocialist States in Southeast Europe:
Challenges and Dilemmas





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About

Shortly after the end of the Kosovo war, the last of the Yugoslav dissolution wars, the Balkan Reconstruction Observatory was set up jointly by the Hellenic Observatory, the Centre for the Study of Global Governance, both institutes at the London School of Economics (LSE), and the Vienna Institute for International Economic Studies (wiiw). A brainstorming meeting on Reconstruction and Regional Co-operation in the Balkans was held in Vouliagmeni on 8-10 July 1999, covering the issues of security, democratisation, economic reconstruction and the role of civil society. It was attended by academics and policy makers from all the countries in the region, from a number of EU countries, from the European Commission, the USA and Russia. Based on ideas and discussions generated at this meeting, a policy paper on Balkan Reconstruction and European Integration was the product of a collaborative effort by the two LSE institutes and the wiiw. The paper was presented at a follow-up meeting on Reconstruction and Integration in Southeast Europe in Vienna on 12-13 November 1999, which focused on the economic aspects of the process of reconstruction in the Balkans. It is this policy paper that became the very first Working Paper of the wiiw Balkan Observatory Working Papers series. The Working Papers are published online at www.balkan-observatory.net, the internet portal of the wiiw Balkan Observatory. It is a portal for research and communication in relation to economic developments in Southeast Europe maintained by the wiiw since 1999. Since 2000 it also serves as a forum for the Global Development Network Southeast Europe (GDN-SEE) project, which is based on an initiative by The World Bank with financial support from the Austrian Ministry of Finance and the Oesterreichische Nationalbank. The purpose of the GDN-SEE project is the creation of research networks throughout Southeast Europe in order to enhance the economic research capacity in Southeast Europe, to build new research capacities by mobilising young researchers, to promote knowledge transfer into the region, to facilitate networking between researchers within the region, and to assist in securing knowledge transfer from researchers to policy makers. The wiiw Balkan Observatory Working Papers series is one way to achieve these objectives.



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This study has been developed in the framework of research networks initiated and monitored by wiiw under the premises of the GDN–SEE partnership.

The Global Development Network, initiated by The World Bank, is a global network of research and policy institutes working together to address the problems of national and regional development. It promotes the generation of local knowledge in developing and transition countries and aims at building research capacities in the different regions.

The Vienna Institute for International Economic Studies is a GDN Partner Institute and acts as a hub for Southeast Europe. The GDN–wiiw partnership aims to support the enhancement of economic research capacity in Southeast Europe, to promote knowledge transfer to SEE, to facilitate networking among researchers within SEE and to assist in securing knowledge transfer from researchers to policy makers.

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GDN-SEE Project ‘Long-term development in Southeast Europe’
**Subproject: “The Role of the State in Southeast European Economies: Current State and
Future Changes”**

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The postsocialist states in Southeast Europe: challenges and dilemmas

1. Introduction

Typically, all great transformations in modern history were supported by some widespread beliefs, stylised facts and stylised theories on past and future societal organisation, organised in widely upheld models of reality to be rejected and models of reality to be embraced. Postsocialist transformation is no exception to this pattern. With the breakdown of socialist political economy and collapse of socialist institutions, after failures to reform/marketise socialism, the ideal of a modern Europeised liberal-democratic society became central in the new democratic agenda for creating societies of freedom, efficiency, justice and affluence. Liberalisation, marketisation, privatisation, on one hand, democratisation and Europeisation, on the other, became the building blocks of this great social and political design. While some earlier episodes of 20th century social engineering (socialism, fascism) had put their hopes in collective actors (class, nation), the new utopia put its bets on individual actors – if provided with the proper structure of incentives he or she would not fail to perform optimally, given constraints and respecting some fundamental rules of the market and politics. The most important in this was to remove, quickly and radically (as argued by “radicals”), or step-by step (as argued by “gradualists”), all barriers to the workings of the markets. (Murrel, 1992; Roland, 2000). In this, it was particularly important to decisively break the iron grip of politics over the economy and its actors in their actions. This is quite

understandable, taking into account the centrality of the state in the old economic system, where all aspects of the economy, and social life in general, were deeply embedded in politics.

With the beginning of the second decade of transition, it became clear that reality in too many cases simply failed to "perform" as expected. Instead the complexity and versatility of emerging market societies in postsocialist Europe, the numerous failures and associated concerns regarding the future, highlighted the limitations of social engineering approaches, often based on simple textbook economics and politics. Among major failures of early "Washington consensus" was its underestimation of the importance of institutional and political dimensions for successful transformation. (e.g. Murrell, 1992; Stiglitz, 1998 and 2000; Roland, 2000) Both the theoretical fundamentals on which this consensus was based, and the political/ideological preferences of its proponents contributed to this. Theoretically, the role of the state was based on standard market-failure reasoning, while the state itself was not theorised beyond standard government failure reasoning. In addition, major actors of change (national and international) tended to converge around something that might be considered as an optimal neo-liberal worldview, implicating the possibility of choosing an optimal market vs. state mix. The Washington consensus "unspoken premise is that governments are worse than markets. Therefore the smaller the state the better the state" (Stiglitz, 1998). An overly optimistic picture emerged about the task facing transition countries. On the other hand, those who, early on, argued for much more activist role of the state, following late-modernisation policies of "developmental states", particularly inspired by some Asian paradigmatic cases (Amsden et al., 1994; in a way joined latter by Stiglitz, 1998), overestimated the actual capacities of the states in Eastern Europe. They underestimated the consequences of the collapse of the socialist state and its organisational and ideological apparatuses for the functioning of emerging postsocialist states. (Dabrowski et al, 2000)

One of the greatest paradoxes of early "Washington consensus" thinking was its insistence on forceful and radical, irreversible destruction of the socialist state (thus recognizing both its centrality and omnipotence), both in the economic and political sense, and in the naive belief that small, modern, efficient, non-interventionist, market-friendly, but public-good providing, states would, by some miracle, instantly emerge. It is true, some have been much more careful from the start: concerning inherent difficulties of the market&democracy coupling in Eastern Europe and concerning the importance of the legacies of the past (e.g. Offe, 1991; Geddes, 1995). Some institutionalist/evolutionary economists issued their warnings as well, some argued for a more gradual and evolutionary approach (Murrell, 1992; Kornai, 1990). Institutional imitation was

questioned as well. Instead, multiple sources of institutional inefficiencies and failures, influence of path-dependency and the possibility of lock-ins were discussed (North , 1990 and 1997)

It began to become clear not only that the transformational state and politics, institutions and traditions, should take a central place in any analyses, but that this analyses should be able to embrace the emerging complexity and versatility. Instead of convergence towards the liberal-democratic ideal as an end-state, we found ourselves witnessing great variation, and great uncertainty regarding future evolution in all but a handful postsocialist countries. Postsocialist societies are developing across a rich spectre of state-forms (both in general and in particular aspects). Various expressions are used to describe this evolution in reorganising state vs. citizens and state vs. economy relationships. They include "kleptocratic", "predatory", "paternalistic", "clientelistic" states – all of them being particularly present in South East Europe (SEE) and the former Soviet Union.

How can we account for this? In what follows I shall not try to give a theory of the state-form evolution in SEE, which would require more substantial and detailed analyses but, instead, I shall make some notes on a couple of issues which in my opinion could be important blocks in building such a theory. I shall be particularly concerned with the so called 'south tier' of transition, that is countries of SEE. Even if not explicitly dealing with them, it will be their experience which will inform this paper greatly. In spite of great differences between them, they clearly exhibit some typical patterns, characteristics and problems. It doesn't only concern the economics of transition (failures to fully transform, restructure and grow along a sustainable high growth path, see: Bicanic, 2000; Dobrinsky, 2000; extended poverty and growth of inequality, Bicanic, 2001a) but the politics of transition as well (failures to truly democratise and fully integrate into worlds of international politics, persistence of considerable democratic and institutional deficits, lack of institutional credibility and weak enforcement of the formal rules, Gligorov, ed, 2000; Mostov, 2001; Tismaneanu, 1999; for Croatia, Franicevic, 1999). There is growing evidence and consensus that these countries are in many respects lagging behind the "north tier" and exhibiting some common properties (see, for example a number of papers in Gligorov (ed) 2000; USAID, 2000 for a compilation of numerous economic, social and political indicators; and Hellman and Schankenman, 2000 for indicators on corruption and state capture). Characteristically, comments Tismaneanu, in interpreting the postsocialist evolution in Europe, the "optimists" are those who insist on the depth of the democratic consolidation and the weakness of nationalist, illiberal movements – Poland is their story. The "pessimists" story is focused primarily on the Southern

case: However, the very fact that failures and pathologies of transition are being vividly debated in these societies is a major sign for hope. (Tismaneanu, 1999) Is it?

It is certainly true that initial economic conditions in most of these countries were quite weak, geography not too convenient, shocks of liberalisation strong, and impact of dramatic disintegration and wars of Yugoslavia profound. Yet, there seems to be much more that should be looked for in search for an explanation of the SEE failures - in that fuller understanding of the state and politics seems to be fundamental .

The SEE states are considered to be too large (but some, due to collapse of old state institutions are too small), too paternalistic (selectively, however), too corrupt. Their fiscal systems are neither efficient nor fair (Gligorov, 2001). Governments in the region “lack the capacity to govern effectively and support reform” (Mostov, 2001), even when large they are “weak”, and “tightly linked to illegal economies...corrupt business practices; uneven and slow economic development...”(Mostov, 2001), they are not growth oriented. (Gligorov, 2001) What matters is not economic policies *per se*, but “the nature of the regime” in SEE countries (Gligorov, 2001: 14)

Mostov is right in stressing the importance of legacies of communism – inefficient bureaucracy and informal ties of favours and connections. Gligorov sees some continuity between failures of modernisation and development, failures of socialism, on one hand, and failures of transition and European/global integration, on the other. While rejecting an explanation based on the persistence and pervasiveness of “Balkan values”, Gligorov points to the importance of the institutional and political set-up, but also sees it as an encouraging sign that the region can be ultimately reformed. (Gligorov, 2001:20) Mostov argues for “institutional capacity building”, based on transparency and accountability of public officials. To achieve that, the SEE states should refocus from issues of territorial control to governance functions. (Mostov, 2001). Both analyses are perceptive and illuminating. In addition, they share methodological position – SEE states are analysed with clear benchmarks in the background – those of liberal democracy. Implicit to their reading is that liberal democracy should be (at least preferred as) the end result of institutional reforms and institutional capacity building. Yet, this may be the most problematic part of the story, both in principle, and, particularly, in the context of challenges faced by SEE in attempts at modernisation, development and globalisation. Are liberal democratic states really in the making in the Balkans? And even if they are, with how many variations?

In what follows I shall first deal with some fundamental dilemmas of the postsocialist state. In the next section market and democracy dilemma will be discussed, in order to show that, both in principle and in particular (concerning SEE) expected benefits of their coupling may not come forward, particularly not in a stylised liberal-democratic form. Section three will discuss major political-economy dilemma of the postsocialist state - one between accumulation and legitimation - in order to show that inability to resolve this dilemma may easily compromise transformational politics of marketisation and democratisation. Particularly, lack of growth may lead societies towards experimentation with, potentially even radical, alternatives, thus questioning both sides of the transition equation, that is market and democracy. Section four will deal with demands for the welfare and for the developmental state and associated challenges to liberal democracy. Finally, in the concluding section, I shall discuss some conditions for consolidation of marketisation and democratisation in postsocialist societies, particularly those of SEE.

2. Market and democracy dilemma

Early liberal democratic pronouncements in postsocialist Europe shared the idea of mutual reinforcement between market and democracy. Not just simultaneity and complementarity, but "additionality" was believed to exist. However, it may not be so simple, the whole package may be controversial, and some difficult "trade-offs" might be inherent. It is true that marketisation in the socialist settings had a double meaning: on one hand it was considered as an avenue towards economic efficiency and affluence; on the other hand it was considered as a necessary part of democratic political reforms. Marketisation, liberalisation, privatisation, and entrepreneurship were seen as fundamental to demonopolise the socialist state and to free the economy from the grip of politics.(e.g., several papers in Njavro and Franicevic, 1990) Even more – it was considered as fundamental to (re)constitute the civil society: its actors and institutions. Demands for Europeisation only reinforced this coupling. However, such a choice, even if sincere and credible, is not without its share of problems and dilemmas. Concerning sincerity, it early on became clear that legacies of the illiberal and non-democratic past play their role, that nationalistic mobilisation is often neither liberal, nor democratic. More interesting is, however, the issue of credibility. Are states and societies of SEE really committed to take the recommended path? And is it in the interest of major actors to follow?

Firstly, let us notice that the very constitution of market society is political per se, and so it is in postsocialism.

Concepts of power and political intervention seem to be central in understanding the emergence and consolidation of institutions of modern market societies (Polanyi, 1944; Schott, 1984; Slatter and Tonkiss, 2001). To understand the workings of market societies requires bringing power, and hence the state to the very centre of postsocialist economic and social reform: "Historically we cannot understand the development and operations of markets without recognizing the extent to which they have been shaped by the fiscal interests of the state and forms of legitimation of state power..."(Friedland and Robertson, 1990: 10-11). Marketisation of postsocialist societies is not simply an outcome of the state backing away from its totalitarian grip over the economy, society and citizens at large – it is an act and process of political will and power, through which not only property is (re)distributed, but social positions and roles, incentives and constraints are profoundly changed. Creation of labour markets was not an end result of simple evolution but also of forceful political interventions into existing property and human rights – this is true not only for early capitalism (as shown by Polanyi, 1944), but it is equally true in postsocialism.

The standard transition economics was, of course, well aware from the very beginning of the legacies of the socialist state and its effects on the economy. Marketisation was seen as de-politicisation of the economy, with the state's role being reduced to dealing with market failures, including protecting and enforcing property rights and contracts, and providing public goods. In this, the state itself - as an institution of power and governance, as an institution with its own "logic" was largely abstracted for. If "government failures" were invoked, it was primarily in order to argue for the "minimal state", or in more subtle analyses for a "transition of government" (Schleifer, 1997). However, in the process it became clear that a separation of the economy from politics (something in principle impossible to achieve) is not the issue, but a redefinition of this relation. What is really at stake is not emptying postsocialist economies of politics but restructuring their relations. The inherent political dimension of market society has to be recognised. Re-creating institutions of market society in postsocialism proved to be a truly political task - open to conflicting political actions, bounded rationality, ignorance, rent-seeking strategic behaviour and actors' ideological interpretations. Far away from an optimal Washington design.

Secondly, markets may well function without true democratic constitution of politics being achieved – "democracy is no precondition for a capitalist market economy" (Bernholz, 1998)

Connection, and mutual reinforcement between market and democracy are far more contingent, both logically and historically, than has been recognised by some postsocialist reformers and their western advisors: " It is not polyarchy as a general phenomenon that is tied to market. It is only polyarchy under liberal constitution auspices...Logically...polyarchy and market are independent ". And: "If we understand that polyarchy is a component of a highly developed form of constitutional liberalism...we would not expect a polyarchy without a market. But we would expect markets without polyarchy... (Lindblom, 1977: 162-169). In addition, while "democracy (in today's developed capitalist countries - v.f.) had to accommodate itself to the soil that had already been prepared by the operation of the competitive, individualistic market society, and by the operation of the liberal state, which served that society through a system of freely competing although not democratic parties" (McPherson, from King, 1986: 89), such a soil was not prepared, with just a couple of exceptions, before a dramatic breakdown of the socialist state and socialist political economy. It had to be created, almost ex nihil. In addition, it had to be created under newly adopted formally democratic constitutions. Yet, in principle, there is nothing that can ensure that actors' interpretation of these constitutions will be liberal and/or democratic, that it will enhance property and/or human rights. If free markets are not generating growth and welfare improvements, if the state is failing to provide public goods and an efficient but fair fiscal systems, and if democratic decision making is discredited by corruption, capture, low accountability and low transparency, then both market and democracy can be challenged on the political terrain – constitutional and non-constitutional. If the credibility of new economic and political constitutions is low, and enforcement weak, then unofficial markets, both economic and political will flourish.

Thirdly, even if the postsocialist choice on capitalism was made democratically, it doesn't change a basic fact that there is an inherent conflict between democracy and capitalism.

(I) There is latent conflict between personal and property rights:

"Liberal democratic capitalism is a contradictory ensemble of institutions in which distinct rights are often conflicting as they are mutually reinforcing....Not socialism, but the full extension of personal rights has been the fundamental threat facing the capitalist order in the liberal context" (Bowles and Gintis, 1986: 32). Constitutional rights and the rule of law are providing a terrain where property rights can legitimately be questioned by those with a stake (of whatever kind) in

the workings of the markets' private actors and organisations.¹ This may be even more relevant in the postsocialist context where the very process of establishing property rights might legitimately be questioned using democratic means. This is particularly important in cases where privatisation (typically for SEE) has been based on non-transparent rules, with a lot of corruption, discretionary decision making, cronyism. A democratic terrain, however, may not only be used to contest emerging (re)distribution of assets and incomes, but emerging social relations too, that is to contest workings of the markets.(as shown in numerous examples of stakeholders activities in Croatian privatisation, Franicevic and Sisek, 2000)

The most important aspect is that it is on the political terrain, through political processes, where rights are being interpreted (in their scale and scope) and legitimised. For the weak modernising and entrepreneurial elites this may simply mean "too much democracy", lack of "governability"². While the capitalist order, historically, was able to avoid "the clash of rights" through "a series of historically specific institutional accommodations" which "constituted a definition of the range of application of personal rights and property rights capable of muting the explosive potential of the clash of these rights" (Bowles and Gintis, 1986: 33), for postsocialist societies it may be much more difficult for a number of reasons that could lead to temporary/permanent suspension of one set/both sets of rights. Both low democratic capacity and low credibility of the rule of law point to that. A paradoxical relation between market and democracy in the East European contexts emerges from the fact that "only a developed market economy produces (by creating actors and interests that are looking for democratic institutions of conflict-resolution - v.f.) the social structural conditions for stable democracy...But the introduction of a market economy in postsocialist societies is a 'political' project, which has prospects of success only if it rests on a strong democratic legitimation. And it is possible that the majority of the population finds neither democracy nor a market economy a desirable perspective" (Offe, 1991: 881). Ten years later, we don't find too much nostalgia for dictators and a strong state. Particularly after the demise in a number of SEE countries of political regimes formed in the 1990s which could hardly be

¹ It is highly recognised in the modern managerial literature (Blair, 1995; Mitchell et al., 1997). But also in deliberations on western "third ways" (see Kelly et al., 1997)

² It was a typical complaint echoed in the wake of neo-liberal revolution – the target was the state based on the "Keynesian accord".

considered as truly democratic ones.³ Yet, precisely because the demand for democracy seems to be strong and persisting, there is a paradox of postsocialist democracies: anti-market sentiments and challenges can be legitimately expressed on a democratic terrain, and actually challenge the emerging capitalist economic order. Both in principle, or in particular form. For new pro-market elites of wealth and power it may produce some difficult dilemmas, particularly if the economy does not deliver early promises.

(II) Democracy may be in conflict with economic growth.

It is in the nature of democratic decision-making that “state activity will be growing in time in democracies”, if not disturbed by wars, crises etc. This is due, it is argued (relying on public choice findings), to the nature of political competition, demands of voters and of special interest groups which arise over time. If this leads towards a higher level of regulations, subsidies, transfers and taxes, but less efficiency, savings and innovation, then negative consequences for economic growth may be expected. (Bernholz, 1998). However, if a crisis arises, while it may be conducive to reforms cutting government expenditures and deregulating the economy (as it can again be shown in terms of public choice), it is not necessary so: crises also provide opportunity for radical reforms leading towards new political-economic regimes. (Bernholz, 1998) In countries with strong legacies of anti-market sentiments, with great demand for paternalistic protection, broad constituencies could be mobilised around ethnic/organic identification. In crises situations they may achieve majority and eventually compromise not only the market but democracy as well. Alternatively, democracy may fall victim to the authoritarian longings of weak entrepreneurial and managerial classes looking for state support against popular demands. Resolving growth crises via the market and democracy, in countries where neither of them have really consolidated, may be a true challenge, and certainly is opened to alternatives.

All these well-known arguments give us a lot of reason to think and to question the naive ideas on an inherently happy marriage between market and democracy in postsocialist Europe. But some more particular reasons should be considered, too.

³ Some of them (e.g. in Serbia, Croatia, Romania, Belarus and Slovakia) were recently analysed as “pariah regimes”, regimes that “normally satisfy the formal criteria of procedural democracy but are deficient in those areas of substantive democracy relevant to international opinion”(Pridham, 2001: 70)

They are part of the history of failed modernisation and Europeisation, of wars and inability to build the foundations for a modern civil society. They belong to cultures and traditions of the SEE countries. But they also belong to new path dependencies and structures of power and interests established through early political and institutional choices made under particular contingencies such as the dissolution of former Yugoslavia, wars, regional insecurity and radical uncertainty. While formally many, but not all, SEE countries adopted some variation of standard prescriptions for economic and political transformation (marketisation and privatisation plus political pluralisation via democratic constitutions), the selection of players, and actors interpretation of new rules and institutions was not always, under specific opportunities that emerged, and constraints they acted under, either liberal or democratic.

Particularly important in this is a role of nationalism.

In spite of its emancipatory and democratic potential, in the postsocialist contexts nationalism often acts (as it often did in the past) as a barrier to democratic development and modernisation. Particularly in SEE countries, “nationalism legitimised itself as traditionalism”, as a tool for the emergence of new elites and their rule (often tending to authoritarianism), and not as a tool for the emancipation of citizens. To adapt national states to the demands of the global liberal democratic order, required is reinterpretation and transformation of the role of nation from “cultural/ethnic” (which does not implicate necessarily either pluralistic constitution or respect for citizens’ rights) into the “political”. Yet, this may be (even if this is a fundamental requirement for Europeisation and EU integration) quite uncertain: national states, as they emerged, particularly but not exclusively in former Yugoslavia, very much reflect vested interests of major parts of new economic, cultural, religious, military and political elites. (more in Švob-Đokic, 2000: 68-87) However, it is important to note (with Massey, Hodson and Sekulic, 2000, based on their research in Croatia) that “nationalism in the Croatian context is not solely of an organic or ethnic variety, nor is ethnic nationalism as broadly supported as is usually supposed”. They find “coterminous with but less strongly embraced than ethnic nationalism, support for economic and political liberalism”. Yet, the future of liberal nationalism and future growth of liberal sentiments will very much depend on the improvement of economic conditions through privatisation and entrepreneurship, and on improved educational access. (Massey et al ., 2000) I believe that this picture is representative for a wider area as well. There is no reason to believe that democratic liberalism has irreversibly triumphed, particularly not in SEE (Tismaneanu, 1999). Where

transition is failing, resurgence to ethnic nationalism, and collapse of pluralism into national homogenisation are a clear option and threat. So, is there reason to believe that liberal democracies might eventually triumph in SEE?

A combination of weak economic performance, lagging growth, inability to catch-up under present conditions – thus belonging to an inferior growth-club (see UNECE, 2000; Bicanic, 2000) - and weak moral economies of transition (Francicevic, 2000), are the central issues for the prospects of liberal democracies in SEE. In addition, these failures are often associated on the political scene with imposition of “neo-liberal” policies of the Washington consensus, leading to demands for more state intervention through use of discretionary macro and micro policies.⁴ To this we turn now.

3. Growth and legitimation

With transition the process of capital accumulation has radically changed - not only on the micro level (privatisation, liberalisation) but on the macro level and, most importantly, on the institutional/regulatory and social level – thus encompassing all relevant areas of social reproduction (the economy proper, education, health, family etc.). Instead of political directives and discretion, the process should dominantly be based on system-built incentives and risk-taking behaviour. Yet, experience shows that this is the hardest part: entrepreneurs and managers, workers and citizens at large are looking to the state to share, to insure against, or to completely socialise inherent risks. A solution to these demands, their accommodation in wider rules of the game, is decisively influencing the state and articulation of the economy vs. politics nexus.

That institutional structure of accumulation (ISA), in general, should be supportive of and conducive to innovation, investment and growth is well recognised: ranging from the Marxian ‘modes of production’, to the American radical economists’ ‘social structures of accumulation’, to

⁴ The Croatian debate, by a major group of economists, with the support of some parties and unions, is typical - government economic policies are dubbed “neo-liberal” and criticised as being pro-recessionary. Instead, anti-recessionary politics are asked for, meaning discretionary fiscal, exchange-rate and monetary policies. (Baletic and Zdunic, 1999)

the French regulationists, to the Northian microeconomic institutionalism pointing to formal vs. informal institutions' (non)correspondence etc. Transition economies are no exception to this. Their success depends on building a sustainable and enforceable structure of institutions and regulations. However the emergence of such structure is not a process of perfectly rational and informed social design, but a process of search through political choices, conflicts, bargaining, coalitions (pragmatic and ideological) and compromises. While new institutional choices are typically influenced by some sort of strong vision and/or ideology it is the interpretation of that vision/ideology by real actors and their "models of reality" (North, 1997) that really counts. This is a source of indeterminism and uncertainty, and may be a cause of possible institutional failure. Such failure may result from special interest strategic behaviour – resulting in capture (see Hellman and Schankerman, 2000), but also from prevalence of non-economic social and political concerns in institution building (security and ethnic concerns, as well as paternalistic preferences first come to mind). Institutional change may not only be relatively autonomous regarding the requirements of capital accumulation and economic growth, it can be also a true barrier to them.⁵ However, a combination of vested interests and general resistance to change, dependency to path, makes it unlikely that inefficient institutions will be easily reformed. Very often, dramatic political-economic deterioration is necessary before forces are mobilised to establish new ISA. (Block, 1990: 300) Yet, there is no guarantee that new choices will be efficient and growth enabling.

One of the most important functions of the state in transition countries has been to provide private-based accumulation with functional ISA and to ensure its complementarity and credibility. Yet, in a context of radical economic and social change, with radical uncertainty prevailing, one of the most important problems facing these states has been to provide nascent modes of accumulation with legitimacy.⁶ Both issues in democratic settings are deeply connected: leading towards politicisation of each aspect of the economic process (everything can be in principle legitimately contested) as well as its scrutinisation through structures of legitimation interface. This interface is not only made of formal constitutions and rules (providing, limiting and interpreting rights), but of moral values and considerations as well. In view of the widespread

⁵ It can be plausibly argued that persistence of soft -budget constraint in transition economies, does not only result in delayed restructuring, including exit, of concerned firms, but acts as a true barrier to potential rival's entry. (Grosfeld, 1998)

⁶ More in Franicevic, 1996

tendency of economists to judge market outcomes in instrumental terms only, rejecting any moral valuation as inappropriate, the question is "not how well the argument stands up to philosophical or social scientific scrutiny, but rather how effective it is likely to be as a legitimation of market outcomes in the sense of actually conditioning perceptions and actions in society at large. And, judged from this standpoint, the chances of success would seem small. Its basic weakness is that the attempted veto on judging market outcomes in moral terms - whatever its philosophical merits - goes directly counter to popular tendencies. A variety of evidence indicates that in society at large, differences in incomes and other rewards are indeed very frequently and readily assessed in terms of their 'fairness' ... Rather, a free-market economy must be regarded as one that is at all events charged with a large potential for generating distributional dissent". (Goldthorpe, 1987: 369-73). Ultimately, in countries where formal institutions are weak, enforcement not credible, the rule of law hardly existent, this *moral economy* interface will certainly be critical in providing or denying the new political economy with legitimation. (more and applied to the Croatian case in Franicevic, 2000)

Why is economic growth so central to finding a sustainable solution to accumulation and legitimation nexus in postsocialist societies? One aspect of this is economic growth as such, the second is insurance, and the third is compensation. As we shall see, all three aspects are not only critical in sustaining market and democracy in them, but are sources of some great pressures on the state. There are pressures on the state to assist entrepreneurship and growth (developmental state), to provide security from market society inherent risks (welfare state), and , finally, pressures to achieve social accord on (intertemporal and intergenerational) compensations (consensual state). As we shall show later, the ability or inability of nascent democracies to accommodate associated demands in the liberal-democratic framework will greatly influence the forms which the states in SEE are eventually going to take.

Sustained high growth path – if reached – is the strongest legitimacy source and the only source which gives credibility to promises and expectations. This explains, more than ideological manipulation and media pressure, the high popularity of even brutal dictatorships, as long as they were able to deliver growth and growth-based expectations. It is very uncertain whether the SEE economies are able to embark on such a path, simply following standard transitioning policies based on the original or on the revised Washington consensus (which recognizes the importance of “getting institutions right”, yet in the framework of liberal markets and highly constrained state)?

Or will more radical deviations be necessary, possibly questioning key components of the liberal-democratic set-up?

Next comes *insurance*. The introduction of Darwinist selection mechanisms radically increases risks of defaults – business ones and personal ones. Inherent risks and insecurities of markets “have to be managed in order for social legitimacy of the market to be maintained” (Rodrik, 1997: 435) In societies with a great deal of social anomie, institutional gaps and democratic deficits, with serious informational asymmetries, with many investments suddenly becoming sunk (both in physical and human capital, but in social as well) with announced rules of the game being quite different from the real ones, risks of (non)adaptation are dramatically increasing. Yet, there are too many which cannot privately insure against these risks. And this is precisely an area where market failures are inherent. However, for the transitional state this is one of the most difficult issues. It is, namely, necessary but very hard to break with legacies of paternalism, clientelism, lack of personal or business responsibility nurtured during decades, and at the same time to provide a socially reasonable amount of insurance against the unbearable risks of market society. Again, it is important to note how deeply this is connected to the issue of growth.

Finally, there is the issue of *compensation* and its credibility. Are winners in the transition game (most likely a minority for the foreseeable future in SEE) going to be able to compensate losers (most likely a majority for the foreseeable future)? It is important to notice that this well-known efficiency criterion (suggested by Hicks and Kaldor in 1939) does not necessarily imply real compensations, but just the possibility of them. (Johansson, 1991: 22-27) In transition economies, where many are still ready to carry the burden of transition costs, it is important particularly in intergenerational terms. Will children have prospects to live better than parents? However, a credibility of an affirmative answer rests both on economic growth and distribution of opportunities. If there is no credibility to such an expectation, exit may easily become preferred option to voice, with further loss of credibility based on growth-related expectations. With a major loss of highly valued human capital, the vicious circle may easily be formed.

Of course, there is no guarantee that all transition economies of SEE will ever reach the high growth path under liberalised markets and pluralistic politics. They may simply fail due to failures of markets and democracy, locked in deficient and inefficient institutional choices, and unable to find a political path out of this. In addition, they may be on the side of ‘non-lucky’ ones. Whatever the cause, *it is important to note that accumulation and growth, in principle, do not require*

markets, as is important to note that legitimation, in principle, does not need a democratic constitution. Modern history is rich with examples of countries passing through long periods of high growth and political stability in spite of the fact that neither markets nor democracy were dominant attributes of the period. Combinations of authoritarian politics and developmental states, in different settings and arrangements, abound. Some of them were successful for longer periods, and have been suggested as models to follow in transition economies. (Amsden et al, 1994) The social- institutional arrangements of the so-called “Golden Age” period in the most developed countries of the world, can hardly be described as purely liberal and/or democratic. Rather, corporatist arrangements and states were functional to such growth. (on corporatism, King, 1986: 114-150) Even socialist industrialisation (which can be viewed as a particular case of late modernisation) produced periods of high growth under highly non-democratic but hardly contested arrangements.

But the postsocialist situation is very specific. Political choice on markets and democracy came simultaneously, and both had to be “introduced”, in spite of the fact that some countries did have some experience with markets and pluralism during the socialist era and/or before. This makes both accumulation and legitimation issues particular. Namely, economic reforms and institutional change were supposed to simultaneously create new agents of growth and growth itself. On the other hand, political reforms and new democratic constitutions were supposed to simultaneously create new agents of democracy and democracy itself. On both counts, agents themselves, their choice and selection (cronyism, asymmetric information), may all be problematic as may also be institutions (or lack of them), and their coupling. It is not accidental that recent discussions on transition failures particularly point to weak corporate governance and public governance as major sources of these failures. (EBRD, 1999; Roland, 2000) To make things more complicated, neither market nor democracy are simply tools to achieve reform goals. They are public goods of the kind and self-legitimising devices: only performing markets and democracies may thus give credibility to liberal democratic reforms.

In the postsocialist world, it was hoped that by radically altering the ownership rights, through privatisation and liberalisation, on one hand, and quick introduction of the full spectre of market friendly and market-controlling institutions, a fine and growth enhancing match between institutions and actors would emerge. Even if realising that shock was imminent (output fall, disruption of trade), the benefits should have been great enough and come timely enough to enable winners to compensate losers, before commitments to both market and democracy were seriously

being challenged. While it may be true for a number of ‘north tier’ countries, it is not true in general. Unfortunately, there is a pattern: typically in SEE, Russia and NIS, first, the output shock, disruption and destruction proved to be deeper and longer than expected, second, recovery was weak and established a growth path far below popular hopes and the expectations nurtured by new elites. (see Roland, 2000; Kraft, 1999; UNECE, 2000; Dobrinsky, 2000)

If economic growth is lacking/lagging, once actors realise that commitments are not credible, the postsocialist state can hardly avoid being entangled in numerous and overburdening redistributive struggles, including shifting interests and constituencies. Moreover, legitimation itself can easily be questioned, contested and even revoked, leading towards political demands for deep reforms, that is for a “second transition”. In such a process not only are the new rules questioned, but the selection of players, as well as their moral economies. This is what really happened in the Croatian transition and privatisation particularly (see, Bicanic, 2001b; Cengic, 2001; Franicevic, 2000).

Achieving economic growth is vital if a new political and economic order, along liberal and democratic lines, will ever stabilise and progress in the SEE countries. Failure to provide a credible institutional framework conducive to accumulation, conducive to a sustainable high growth path and lasting legitimation is a source of major dilemmas and challenges to infant democracies in SEE. To them we turn now.

4. Facing challenges : the welfare and developmental state in SEE?

In many SEE countries to embark on a superior growth path than that followed through the 1990s may mean that the state must actively promote and favour interests of new entrepreneurs, owners and managers (generally weak and perceived as of questionable reputation) in such a way that accumulation may progress, yet without putting too heavy a burden on the rest of society, which is entitled to question distributional outcomes (both in terms of wealth and output). Is this possible? And is it conceivable in societies where many people are facing unemployment, low living standards, great uncertainty about their and their childrens’ futures but still with strong memories of paternalism, egalitarianism, clientelism and a very weak respect for others' ownership and human rights? Is it feasible in societies where legitimacy of entrepreneurship is still weak, and deeply shaken by numerous cases of illegality and dubious morality in privatisation, where the

market is too often associated with 'scheming and dealing'. Is it achievable in societies with serious fiscal problems, growing explicit and implicit deficits (Gligorov, 2001), with pension and health systems on the edge of breakdown, with bureaucracies of low accountability and professionalism, but with a high taste for corruption?

In such settings, typical for SEE, even if we can talk about the social accord on promoting both market and democracy, it is questionable how loyal the parties can be to its terms. In the absence of growth, compensation of losers may not be feasible, while winners gains may prove to be elusive and fiercely contested. Transition losers may not only challenge distributional outcomes but also the new social relations of production. On the other side are those looking to the state for protection of gains and opportunities to enlarge (through further accumulation) these gains. For the state, this means the need to meet and accommodate two demands: one to be fair to and reduce the deep uncertainty that citizens (especially some groups) face due to overall marketisation and privatisation of the economy. The second is to provide a milieu conducive to entrepreneurship, technological and organisational upgrading, accumulation, investment and growth, and at the same time to legitimise and protect emerging property rights. This is not simple if privatisation abounds with corruption, criminal and unethical behaviour and entrepreneurs tend to be engaged in rent-seeking and non-productive entrepreneurship (Francicevic, 2001) It is not only a matter of "trade-offs" implicit in these two demands that is problematic for the transitional state, but the path already taken as well. Can the liberal-democratic state provide a solution and accommodate pressures coming from both accumulation and legitimation?

4.1 Challenges of the welfare state.

There are not many, even among hard-core liberals, who would be so blind to the context as to argue for a minimal ("night watchman") state of the 19th century. And even if they did, in a modern complex society it would just be an "illusion" (Gray, 1997). When "the Western democracies had turned their back on the old traditions of staunch laissez-faire or paternalistic authoritarianism - the welfare state became a key ingredient in the post-war consolidation of universal democracy" (Esping-Andersen, 1994: 714). In addition, the welfare state is considered to be not only "one of the fruits of growth It is also one of the causes of growth.... The welfare state is much more than a safety net; it is justified not simply by any redistributive aims one may (or may not) have, because it does things which private markets for technical reasons either would

not do at all, or would do inefficiently. We need a welfare state of some sort for efficiency reasons, and would continue to do so even if all distributional problems had been solved...The welfare state spending should be optimised not minimised” (Barr, 1999: 27) But social legitimacy is important as well: “...any reform of the state that overlooks the importance of social insurance risks undermining the market-oriented system that is the ultimate objective of the reform”. (Rodrik, 1997: 440). For transition economies, the real dilemma is not *whether*, but *how*.

Among different models of welfare states and social policies (e.g. liberal, Christian Democrat, Social Democrat, socialist-bureaucratic – see MacGregor, 1999), the clear Washington consensus preference is for the first one. It is a model of “residual” welfare state, “distinct in its minimalist approach to welfare guarantees”. It is “market conforming”, encouraging private and philanthropic welfare. In that approach, instead of universalism of the institutional models, social protection should be targeted. (Esping-Andersen, 1994: 715; MacGregor, 1999: 97) With a neo-liberal preference for privatisation and narrowing of public domain, affordability became the central issue: “the affordable welfare state is bound however to decline into the residual welfare state” (MacGregor, 1999: 107) On the other hand, if economic growth is weak, if bottom-up development of new firms is heavily constrained (by market and regulatory failures/barriers) - as is typical in SEE (Bartlett, 2001) - and unable to make up for loss of jobs in privatised and public sectors, if poverty and inequality are on the rise – as they are in SEE (see Bicanic, 2001a) - then we may only witness a growing number of potential "clients" looking towards the state to provide relief, security and opportunity. This is putting a lot of pressure on the fiscally weak states in transition countries. Yet, demands for safety-nets, for the social or welfare state are not only prominent on the postsocialist political scene – their prominence is rising with failures.

Yet, “affordability” is problematic, and so are the politics of welfare reform. (Kornai, 1997; Kornai et al., 2001; Barr, 1999) Of course, the breakdown of the socialist welfare state with its broad universal entitlements provides an opportunity for reform. Even if some were committed to its preservation, this would not be credible. Politically, crises of the old welfare systems in particular, and general threats of the “fiscal crises of the state”, give the state a mandate to look for new solutions. But, this is not so simple for two reasons: one is efficiency of reform, second the politics of reform.

Whatever choices of welfare system (from unemployment and education to health and the pension systems) are made, they most likely mean (a.) reduction of rights and entitlements; (b.) greater

reliance on the market and individual participation in risk insurance; (c.) greater expectations of alternative modes of provision based on civil society initiatives, public and private partnerships, local initiatives and collective organisation. However, even the reformed welfare systems and modes of provision of social security have numerous inherent risks: economic, demographic and political. In addition, private schemes face management and investment risks as well. (Barr, 1999) Lacking developed financial markets may lead towards accumulation of government bonds, lacking private sector capacity may put at risk viability of private funds; lacking government capacity and accountability may lead towards fiscal irresponsibility, macroeconomic destabilisation and increased risk due to regulatory failures. Unfortunately, neither private capacities nor government capacities in the SEE countries look very reliable. If the welfare state reforms fail, that would certainly induce the strongest anti-market sentiments, and face the state with major challenges to radically revise reform choices. Particularly, in countries with strong legacies of paternalism and egalitarianism, on one hand, and on the other with great percentages of population feeling to be on the losing end of transition.

There is no doubt, credibility and sustainability of welfare state reforms along liberal prescriptions, greatly depend on future growth. However, expectations that reforms themselves (particularly private pension funds) will be major engines of growth, that they will be a solution to the growth problem, at least in SEE settings, may be too naive. Private pension funds contribute to growth only by increasing domestic investment. However, if funds face low yield and high risk, they will rather accumulate government bonds and foreign investment – and thus increase fiscal pressure on the state, and/or put growth at risk, opting for contributors’ security (Barr, 1999: 23). Much more is needed (in terms of prerequisites) if the impact of the pension systems reforms on growth will be strongly felt – developed financial markets, stronger private sector capacities, and strong public governance are needed. But, politics may be the hardest part.

Reforms of job security, social security, health, educational and other social systems are inherently long-term, they are lasting processes, asking for actors – both provisioners and clients - to adapt and to learn. On the other hand, each change has a direct, visible and measurable impact on many individuals, families and social groups. This is very different from price liberalisation: where change is quick and sudden, but the impact hard to calculate, and even harder to use as an agenda for collective organisation of those self-recognised as victims. In principle, there is much less of the “pattern” in distribution of gains and losses: usually everybody is on both sides, because there are so many items. Of course, liberalisation as such may be politically exploited, if economies are

failing. But this is not the stuff of daily politics, but rather of crises politics. Welfare reform, on the other hand, being a lasting process, requires “political sustainability....continuing commitment from governmentandcontinuing political support. Reform regarded as a single, once-and-for-all event runs the risk of neglect, discredit and eventual reversal” (Barr, 1999: 21).

However, in societies of low consensus-building abilities, where for systemic reasons (weak private, administrative and political capacities) numerous failures in reform processes are very likely, there are two great risks to face: first, risk of political-business cycle; second, risk of populist mobilisation: “the welfare sector is the subject on which electioneering speakers are most prone to promise the impossible” (as Kornai, 1997: 1186, put it). First risk belongs to the nature of democratic multiparty politics. Welfare reform not only may be (mis)used in daily and election politics (which is unavoidable), it can also be tuned and manipulated in order to improve the election results. It is very unlikely that political parties in SEE countries would ever abide by accord on self-restraint concerning what should and what should not be a matter of daily political exploitation.

The second risk is more contextual. In countries with major illiberal actors and constituencies, it is quite likely that - particularly taking into account all pathologies, weak growth, and even weaker moral economies - populist challenges to the state, accompanied with demands for reversals and full socialisation of risks, will emerge. For would-be liberal-democratic states, supply of paternalistic alternatives and demand for them do not need to mean a full collapse in universal paternalism and full reversal to socialisation of market risks and failures. Yet, it may force them to accommodation, with uncertain influence on both the private sector of the economy, and fiscal sustainability. An accommodation towards corporatist solutions is particularly likely in those countries where design and execution of social policies is strongly influenced by all-encompassing ethnic and/or religion based ideologies and institutions, for example the Catholic church.

On the other hand, due to heavy fiscal constraints, experimentations with the “new paternalism” (MacGregor, 1999) may also ensue: this ‘third way’ includes “decentralisation, local variation, more discretion to bend rules on the local level.... demonstration projects, and better informed governance”. It is particularly targeted to the “socially excluded” – therefore different principles and rewards are operating at different social strata: for “the poor and the deviant, those who cannot or will not assume responsibility for their own well-being, there is the new paternalism” (MacGregor, 1999: 109). No doubt, achieving the legitimacy of economic reforms may be so

costly, and alternatives to them may start looking more rational. Will in this difficult process some new visions of a better society (re)emerge to which practical proposals for social reforms will be linked, will “language of social” be (re)invented (as MacGregor hopes for in arguing for the “fourth way”) is yet to be seen.

4.2 Challenges of the developmental state.

Not less important and acute in failing transition economies are or might become pressures coming from the capital accumulation side. If savings and investment are low, if returns to investment are low, than pressure from entrepreneurs and investors, and from the business community should be expected, in order to improve the “investment climate”, to remove barriers to investment and entrepreneurship. Pressures might also arise for more direct support to capital accumulation: extension of subsidised credit and tax incentives, for socialisation of investment risk, for socialisation of some investment costs (e.g. provisions concerning labour costs and social insurance), as well as for the state to take entrepreneurial roles (e.g. to organise entrepreneurs; to go into particular investments in public enterprises characterised with strong forward linkages or providing key inputs; to directly engage in opening up new industries, technologies and markets; to protect infants and select and support ‘winners’). All this is part of discussions on the “East Asia miracles” (Rodrik, 1997; Amsden et al. 1994; Ha-Joon, 1994). Early on experiences of successful late industrialising models were suggested, against Washington’s “market fundamentalism”, as the path to follow in Eastern Europe (Amsden et al., 1994; Wade, 1996).

With the second transition decade, two important developments should be noted, which might (even radically) influence the (re)consideration of the roles of markets and governments in postsocialist societies.

The first is empirical. Simply, in a number of countries, allegedly relying on the Washington consensus prescriptions, economic growth is weak, microeconomic fundamentals are weak, macroeconomic policies are hardly credible (in terms of their sustainability in the long term). Globalisation only adds to the pressures the new entrepreneurial and managerial groups are facing. In addition, social legitimacy of entrepreneurship and private ownership is undermined by weak moral economies – with an uncertain political impact. The uncertainty under which agents are performing is overwhelming – thus giving rise to a host of coordination and informational problems (Stiglitz, 1997 ; Fu-Lai Yu, 2000; Ha-Joon, 1994) Growth of firms is constrained by both

market and government failures, by numerous regulatory barriers. Corruption and predation are increasingly being felt as barriers to private sector growth. To this we may add that profitability of the private sector is under the pressures of the state and political parties commitments to various social groups, and these groups legitimate demands for resources and protection. From the standpoint of business communities interests', it may necessitate a reevaluation of the path already taken. This may not only lead to a conclusion that there is too much state (as the neo-liberal diagnosis would be) but, paradoxically, in the same time that there is too little and too wrong. The future of capital accumulation and entrepreneurial growth could lead to a stronger demand for a different state, for a different articulation of state vs. market relations.

The second is theoretical and ideological. After two decades of domination - in 1970s and 1980s - both types of developmental states ("Keynesian" with its socialisation of investment function, and late developing ones with states actively undertaking whatever it takes to catch up, see Block, 1994) came into disrepute, while consensus formed in favour of the (neoliberal demand for) the state's pulling back and reducing its role to a minimal one (Washington consensus). However, we are facing a resurgence of interest in state vs. market nexus. The emerging Post-Washington consensus is giving new credibility to a potentially more active and more present state. This is due to two, in addition to arguments for social insurance and safety net provision (as discussed above), interconnected developments: *first*, is the extension of the scope of market failures to coordination and informational problems and asymmetries (Stiglitz, 1997), thus giving legitimacy to numerous macro and micro policy interventions, and development strategies. (Fine, 1999) This is a basis for pro-industrial policies arguments. (Ha-Joon, 1994; Fu-Lai Yu, 2000) Such market failures are considered to be overwhelming in emerging markets. Characteristically, the Washington consensus policies failed to grasp their true importance (Stiglitz, 2000). *Second* development concerns much more subtle reasoning about the government itself: there is "a move away from the tendency to view the government ...as inherently inefficient and, worse yet, as predator" to "more sophisticated institutional approaches". (Rodrik, 1997: 413) In addition, very vague concepts, such as "social capital", "institutional capital", achieved prominence. These notions opened new avenues to legitimise different pro-development policies, as well as the internal reforms of the state in order to achieve greater capacities, professionalism and accountability. More important in this thinking is not *what* the state is doing, but *how* it is doing what is doing, the central question is not the *size* of the government, but its *activities* and *methods*. (Stiglitz, 1998) Complementarities between states and markets are at least as important as possible tradeoffs.

While it would be interesting to review the new developmentalists agenda for its consistency and empirical backing, which is of course a matter of debate (e.g. concerning selective industrial policies), it is here interesting to note that it may help to building proactivist political agendas in postsocialist societies, organising issues, and constraining the public debate domain through credibility attributed to expert diagnoses. Of course, contenders in the political process have their interests to defend. This simple fact can give prominence both to neoliberal ideologies as well as to hardly modernised Keynesian ones. How state vs. market problems will be articulated on the political scene in years to come is uncertain and open to numerous influences and ideological interpretations. How will business interests be argued for, what kinds of political mobilisations, coalitions and ideological interpretations will be on the scene is again uncertain. What is, however, quite certain is that it is through these processes of reinterpretation, that the state versus market domain will ultimately be shaped – not necessarily along the lines which were by liberal democrats taken as an end point in the start of transition.

For example, as long as “too much of the state” diagnosis remains prominent on the political agenda, as a credible ‘diagnosis’ of the state of the world, this redefinition of the state vs. market domain may easily result in demands for reduction of citizens and human rights. A recourse to an authoritarian reduction of democratic processes, and implicit separation of the economy from politics may be a preferred option if it is believed that current, however imperfect, democratic set-up, constrains entrepreneurship and investment, costs too much and is associated with government and policy failures to promote and ensure the private capital accumulation.

It is, however, important to note that such a reduction is not compatible with radical economic liberalism only, but with developmentalism (based on close cooperation between government and private business and autonomy of bureaucracies) as well. In addition, domestic business community demands for developmentalist policies, and not for extreme liberalism, are more likely when taking into account the weakness of the private sector in transition countries. Amsden et al. are very well aware of this authoritarian potential. Yet they find it neither desirable nor likely in the more Westernised countries of Eastern Europe. And in any case, in these countries “authoritarianism is not very likely to be efficient or successful” (Amsden et al. 1994: 203) On the other hand, popular demands for material well-being and increased security are not necessarily in line with demands for democracy. It is not so certain that in a number of failing transition countries it is really true that “short of democracy, these societies risk anarchy” (Amsden et al, 1994: 203). Even more: if both markets and democracy would be failing, is it really so inconceivable that this

could result in a collapse of both the liberal and democratic, and end in a resurgence of the totalitarian state providing work and order?

Authoritarian reduction, in order to assist problematic capital accumulation and investment, is much less conceivable in those countries where a democratic set up has consolidated enough to credibly determine and constrain the rules of the state vs. market game. Of course, this forces major political actors and interests to look for a viable consensus, and cooptation of opposing interests (business, workers, citizens, localities and communities) into the growth and development equation to be solved. This consensus is about timing and compensation, about distribution of costs and opportunities. However, through this search the political terrain itself may easily get redefined – be that along corporatist, paternalist, participatory or other arrangements.

5. Conclusion

When the state is choosing which are, supposedly, the most appropriate economic and political institutions, policies and regulatory framework, it is defining itself too - its relation to the economy and society, the articulation of economic and political spheres and degrees of its own 'relative autonomy'. In this process, specific and different state-forms are created. This is where the greatest uncertainties are and where the outcome is least controlled by the actors. However, the contingent nature of these state-forms has not been seriously considered under the dominant transition paradigm. And this is so for a simple reason: the paradigm offered the end state (liberal democracy) as a given - making only means to achieve supposedly uncontroversial ends problematic and controversial.

It is also important to note that the success of a number of transition societies to consolidate parliamentary systems through three or even four cycles of elections may be an impressive sign of how broad is a commitment of major political contestants to democracy. This is certainly very encouraging. But it is definitely not enough to claim that liberal democracies are consolidated in all of them, or that they will ever be consolidated. Rather, very different state-forms may emerge, with a lot of experimentation on one hand, and exposure to dependency on inefficient paths on the other. For all these reasons, the further evolution of postsocialist states is rather an open-ended matter.

Challenges facing the liberal democratic state are particularly pronounced in those postsocialist societies where economic growth is lacking/lagging, where serious democratic and institutional deficits and failures perpetuate, where political economies are contested and moral economies challenged. The South East European tier of transition exhibits some common patterns precisely along these lines. The question facing those acting pro-reform and pro-democratic policies is: are they able to accommodate the above analysed pressures and respond to inherent challenges (of accumulation and legitimation, of security and development) on the liberal and democratic terrain, or its very fundamentals (both market and democracy) will be radically contested. In both cases, the evolution of different state forms, and sub-forms may be expected. What remains uncertain is the following: are these accommodations and political-constitutional choices going to provide these societies with economic growth and well-being.

This general story is and will be unfolding quite differently in different transition countries. It will depend very much on the commitments of political leaders and political parties as well as other collective organisations, including non-governmental ones⁷, to achieve change. It will depend on their ability to command trust from entrepreneurs, owners, managers, workers and citizens at large, that conflicting interests will be protected in such a way that nobody can feel to be on the losing side only. However, only sustained economic growth may give credibility to inter temporal compensations – it is vital for the success of democratisation in postsocialist societies.

Continuation of low growth and perpetuation of unfavourable trends may only destabilise democratic order, and discredit its reliance on market institutions and incentives.

How therefore can a capacity to sustain both accumulation and legitimation in a democratic postsocialist state be achieved and enhanced? What can be done to make simultaneity of democratisation and marketisation irreversible, and commitments of the main actors credible? The answer has three parts. One is *political and strategic*: if all actors realise that it is in their own interest to abide by the social accord on market and democracy then the conflicts will be about dimensions/outcomes, (less) about the rules, and not about the game. But how to achieve this? Coherent vision and strong pro-democratic commitments of all key parties in the process are vital.

⁷ Paradoxically, in a number of SEE countries the explosive growth of NGOs has not led, as hoped for, primarily towards increased civiness (therefore supportive of liberal democratic constitution of society), but just the opposite – grassroots opposition to it. In some states liberal democracy, the rule of law, are opposed on the streets.

Is it possible to get them without mobilising nationalism, without mobilising a sense of national goal? It may be very difficult, particularly in the SEE region. But then new dangers for the liberal-democratic project emerge (Gillwald et al, 1992; Offe, 1991; Švob-Đokic, 2000; Tismaneanu, 1999).

The second part is about *the state as such*. There is little doubt that credibility of procedural democracy is seriously undermined by low accountability, corruption, capture, lack of enforcement, bureaucratic ignorance and absence of the rule of law. Whatever specific path is taken by would-be democratic postsocialist states, it is most important to be capable and credible, well organised, focused and efficient. Simply, governance matters. (Mostov, 2001; Kaufmann et al., 1999; Rose-Ackerman, 1999; Tanzi, 2000) All this is lacking nowadays in postsocialist Europe. In the SEE region particularly. For democratic consolidation, it is particularly harmful.

The third part of the answer is *economic and social*: economic growth must be achieved, before commitments to democracy and/or the market deteriorate, which may be asking for a consensus between actors: (a.) on priorities and sequencing of moves to assure relative primacy of capital-accumulation; (b.) on social insurance and protection; (c.) on dynamic compensation and opportunity structures. That consensus could be necessary is less controversial, than the ability of actors to reach and provide it with credibility. Foreign credit, investment and assistance (economic and technical) may prove to be of critical importance in this difficult undertaking. As may everything be that contributes to regional trade, security and freedom in movement of capital, people and information. Closed, xenophobic states, can hardly survive in a modern world. And if they can – they definitely cannot remain either liberal or democratic.

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