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Transition to Market Economy in Eastern Europe: Interest Groups and Political Institutions in Russia

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The article analyzes the causes of the incoherent reformprogram in Russia in the last decade. It argues that the slow and partial policies can be attributed to a viscous combination of lobbyism and constitutional design. Because the post-communist transitions after 1989 were non-violent "velvet revolutions," the old state monopolies were not removed. State monopolies have small-group advantages in contrast to the large group of private firms, which are numerous and not yet organized. It leads to an asymmetrical pattern of lobbyism in favor of non-transition, which can only be mitigated by establishing dispersed political institutions, that can raise the price on rent-seeking. In Russia the centralized political institutions of the past were not replaced. Hence, Russia inherited both interest groups and political institutions of the late communist era – an unfortunate starting point for carrying out comprehensive economic reforms. Free trade with the West and potential competition may put pressure on the old state monopolies. However, lobbies in the European Union may oppose free trade to maintain their monopoly. JEL codes: B0, D7, P0

The process of transition to market economy in Russia follows a rugged path. Harmful regulation is prevalent and production subsidies still amount to almost 7 percent of GNP – the highest in any post communist country.[1] Especially subsidies to energy and agricultural production continue to be heavy burdens for Russian taxpayers, and the fact that some nec-

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Special thanks to *Norbert Wunner*, *Martin Paldam*, *Frans Van Winden*, *Anders Bornefalk*, *Niclas Berggren* and *Klarita Gerxhani*. Also, we are grateful to *Tor Eriksson*, *Finn Laursen*, *Carsten Daugbjerg*, *Chr. Hjorth-Andersen*, *Erik Strøjer Madsen*, *Ann-Marie Gabel*, *Wally Oates*, *Karen Dunn* and *Mancur Olson*. Needless to say, we alone are responsible for any shortcomings.

1. EBRD (1999:137). Production subsidies are given either as direct budgetary subsidies or as soft governmental loans. The corresponding figures for more coherent reformers as the Czech Republic and Poland are respectively 2.4 and 2.5 percent.

essary steps, e.g. foreign trade liberalization, have been taken, cannot remove the image of a slow and uneven reform process.

But why does Russia find it so hard to capture the gains from a coherent reform program? Unfortunately, this question has not been convincingly answered in the social science literature. One of the main problems is the reliance on narrow disciplinary approaches. In economics, the dominating neoclassical paradigm has proved to be of little relevance. In the full-information world of neoclassical theory, welfare gains can be realized at no costs. Hence, economist have had much to say about optimal policies, but little about why they are not implemented.[2] At the same time, political scientists relying on the traditional behavioralistic approach have found it difficult to account for the existence of slow and incoherent reform policies in Russia. Usually, studies within this reasearch tradition conclude that the country's authoritarian political culture precludes all liberal tendencies in both the political and economic sphere. Needless to say, such explanations are too deterministic.[3]

Instead of relying on narrow approaches, we believe that the study of post communist transitions would benefit from paying attention to some of the studies within the new interdisciplinary research tradition of positive political economy. First, lessons from public choice studies by Mancur Olson, tell us that the ability of interest groups to affect public policy is affected by their ability to act as small groups. Second, lessons from North and Weingast's studies of the economics of institutions tell us that results from such lobbying may be reinforced, or mitigated, by the structure of political institutions.

Our contribution is to combine the insights from these studies and thereby shed new light on the drastic and unanticipated economic slow-down in Russia. By introducing a simple theoretical model, the aim is to explain the dominance of incoherent reform policies and to recommend how these important barriers to economic growth can be eliminated. Essentially, we will argue that policy solutions can be attributed to a viscious combination of interest group formation and political institutions, which both are products of Russia's non-violent 'velvet revolution'.

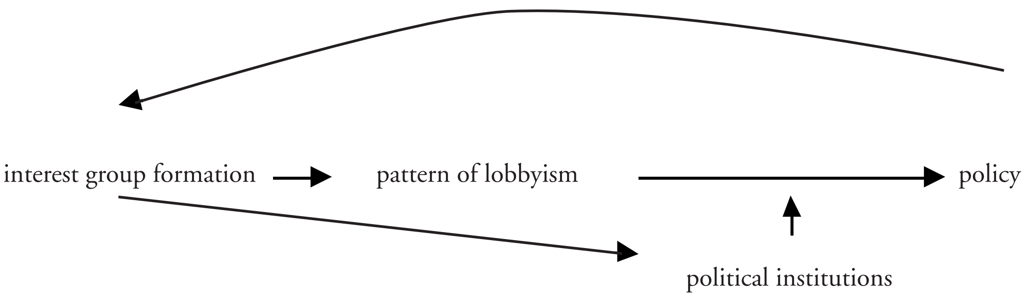
The outline is the following. First, we will introduce the basic assumptions of the research tradition of positive political economy. Second, we will introduce Mancur Olsons theory of interest groups, and develop a hypothesis about interest group behavior when moving from centrally planned to market economy. Third, the theory of political institutions as governance structures is presented, and a hypothesis about the relations between political institutions and lobbying in post communist countries, developed. Fourth, we will analyze the interaction between interests groups, political institutions and policy outcomes in Russia since 1991. Finally, a conclusion will be drawn and policy recommendations and perspectives presented.

Positive Political Economy

Positive political economy is essentially 'the study of rational decisions in the context of political and economic institutions'.[4] Even

2. See Murell (1991) for a discussion of the limits of the neoclassical theory in explaining performance in formerly centrally planned economies.
3. Zimmerman (1995) offers a thoughtful discussion of the problems of determinism in studies of political culture in Russia.
4. Alt and Shepsle (1990:2).

Figure 1.
An integrated positive political economy perspective on interest groups, political institutions and polic



though it rejects the narrow focus of standard neoclassical theory, it is grounded in the rational actor methodology of microeconomics. It assumes that both political and economic actors act optimally towards well specified utility functions, while at the same time being constrained by the institutions established to structure their interaction.

The assumption about human behavior is, as such, harsh and simple: man will pursue private interests and not those of the public or the common interest. While market agents seek to maximize income in monetary terms, politicians will tend to maximize tenure and political influence. Therefore, utility functions may vary according to ones position, but it is assumed that everybody, irrespective of position, acts optimally towards his well-specified preferences.

Even though these basic assumptions are the foundation for every study within the positive political economy discipline, the studies often emphasize different aspects of human interaction. Olson's studies of interest groups mainly focus on how interest groups endowed with different resources may affect policy outcomes, while North and Weingast's study of constitutions, on the contrary, mainly concentrate on how policy outcomes are constrained by political institutions.

These different perspectives are not mutually exclusive. In fact, we believe that it is when the perspectives are combined and integrated, that the positive political economy framework is best suited to analyze policy outcomes. Olson provides an understanding of how rational interest groups endowed with different resources and interests lobby for favorable regulation, while North and Weingast provide an understanding of how their lobbyism is affected by the structure of political institutions. Hence, by combining the two we get a coherent framework for analyzing 'rational' public policy decisions in the context of political institutions. Figure 1 illustrates this logic.

As the model in Figure 1 indicates, the political institutions are themselves designed under the influence of interest groups. This relation is not clear-cut, as interest groups rarely on their own determime the constitutional design. They can influence the design by lobbying for a set of political institutions, but they can still be overridden by a majority of unorganized voters, who on a daily basis are more or less ignorant about politics.[5] Hence, the success of political institutions to mitigate the pressures from narrow interest groups is dependent upon voter's ability to prevent those groups from designing the constitution.[6]

Furthermore, the model includes the distributive consequences of policies, which feedback to the formation of interest groups. It implies a certain inertia and that the political process reproduces itself.

Now, who are the interest groups who will try to influence public policy in Russia, how are their lobby activities constrained by the rules of the political game, and how are policy outcomes affected by these processes? We will start our investigation by introducing some lessons from the public choice theoretical literature on interest group behavior.

Interest groups, lobbyism and transition

In Eastern Europe, the new markets are only added to what is left of the old system of state monopolies. These public enterprises were the dominant interest groups in earlier communist regimes and got their privileges at that time. Because the transition to democracy in 1989 were non-violent "velvet revolutions", the state monopolies were not removed. Rather – as economically rational interest groups – they will now try to preserve the existing redistributional system and block economic growth.

This thought of line follows from Mancur Olson's books, *The Rise and Decline of Nations* (1982) and *Power and Prosperity* (2000). Olson argues that more and more interest groups are assumed to develop over time and by coincidence. Because these organizations tend to persist, older democracies will be filled with a greater number of groups resulting in increasing pressures for redistribution. Consequently, the oldest democracy, Great Britain, experienced economic stagnation after World War II because of the burden of groups, the so-called "British Disease". This in stark contrast to Germany and Japan which experienced economic miracles after World War II, due to the absence of groups at that time. When a totalitarian government, a revolution, or a total defeat in war destroys the institutional fabric of a society, then that society will grow rapidly when a stable legal order is established, if there is no significant redistribution to prevent optimal investments.

Olson argues that this was exactly the case in England/ Great Britain when the country rose to power from the end of the seventeenth century. In 1688-89, the so-called Glorious revolution swept across country and effectively put an end to the long and devastating period of civil war. A revolutionary settlement, which introduced new and more democratic political institutions, was drafted. Because the king had been severely weakened by the long lasting powerstruggles, he had to accept to divide powers with a new elected parliament, which represented wealthy males across the country. As Olson concludes, it was England's 'luck' that it had experienced a violent civil war and revolution. Not only had the country become more democratic, but most important, the special interest groups that previously had been involved in suboptimal redistribution of the national income had

5. Downs (1957) indicates how it is rational for the single voter to stay ignorant about public affairs because his vote is not likely to affect the outcome of a typical election. See also Svendsen (1998a).
6. See Nørgaard (2000) for discussion of this problem.

been severely weakened. Consequently, they were unable to be successful in their traditional lobbying for wealth redistribution. As a result, public spending was increasingly allocated to productive uses. That gave rise to optimal investments and prosperity, which lasted until new groups, hundreds of years later, were able to engage in redistribution and create the 'British disease'.[7]

According to Olson, such redistribution takes place because rational groups will try to steal as much money as possible from e.g. the treasury and redistribute as much as possible from the taxpayers to itself. For example, a farmer lobby or a state monopoly may represent 1% of the national income. It follows that the group will only stop redistributing to its clients when the reduction in national income is a 100 times as great as the amount they win in the redistributional struggle. In contrast, if the interest group tries to change policies for the better, the group will only receive 1% of the benefits, but will bear all the costs.[8] This kind of lobbyism will tend to result in redistribution from the taxpayers to special interest groups.

More precisely, the advantage, A_i that any individual i would get from receiving any amount of the collective good would be the return or "value", V_i, to the individual i minus the total cost of providing the collective good, C, so that $A_i = V_i - C$. If A_i is clearly positive, the group is small and the collective good will be provided; if A_i is approximately zero, the group is intermediate; and if A_i is clearly negative, the group is large.[9] That is to say, the more negative A_i is, the more likely it is that the group will fail. The larger the group is, the less is the extra value to an individual from his individual investment or costs.

The Eastern European version of the "British Disease" can be illustrated by the use of this theory. Let us consider the potential "winners" from (i) transition and (ii) non-transition to market economy. The collective good of transition or non-transition to market economy is provided by lobbyism. The results from this analysis lead to a hypothesis on rational interest group behavior in Eastern Europe and an asymmetrical political pressure against market economy (iii).

i) Economic "winners" from transition to market economy

Say, that 1 million private firms exist in an Eastern European country. These numerous and small firms are not organized yet in a large group but they will all be potential economic "winners" by the collective good provision. In the case of open markets, talented entrepreneurs from the East would conquer market shares from its own state monopolies and from EU firms and farmers.

Assume furthermore, that the individual economic reward in the first year, V_i, is \$1000 from private enterprise. The total costs of providing the good, C, is \$100 million which is used for lobbying politicians to provide the collective good, Q_i, of full transition to market economy.

This case of a large group is shown in Figure 2. The individual demand curve for the

7. Olson (2000: 98).
8. Olson (1991:140). Most redistributions are from unorganized groups to organized groups. When nations subsidize the non-poor, they channel the time and energies of some of their most productive people and assets into less productive pursuits and thereby reduce social efficiency. For example, tax loopholes induce much of the productive capacity of the society to move into tax-favored activities (Olson 1991:146).
9. Olson (1965:23).

Figure 2.
"Winners" from transition: Large group

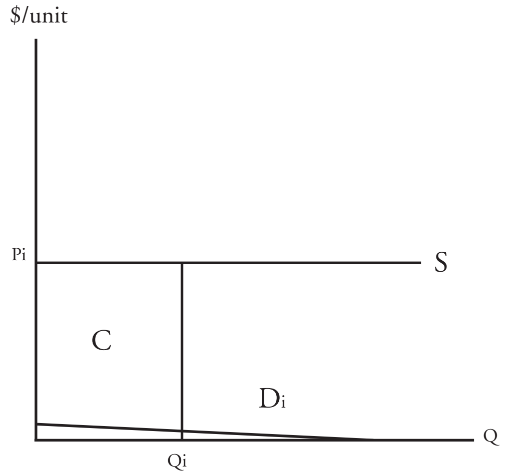
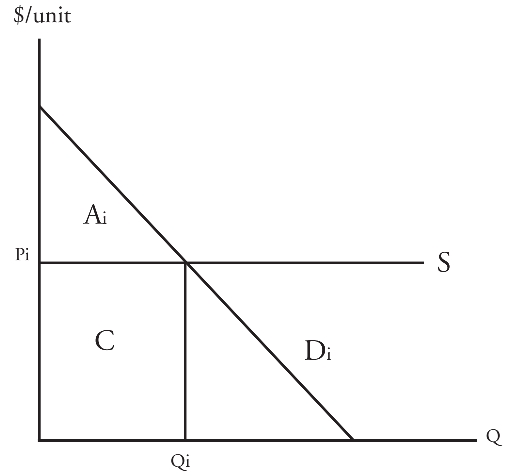


Figure 3.
"Winners" from non-transition: Small group



collective good, Q, is drawn as D_i. The supply curve for producing any amount of Q at the price of P_i, is depicted as S.

In this case of a large group, no single member will provide the good without organization; his advantage or net gain is clearly negative. The total costs, C, is much higher than the individual gain, V_i, below the D_i curve. The net benefit to the individual, A_i, is clearly negative.

ii) Economic "winners" from non-transition to market economy

In contrast, the "winners" from preventing a transition to market economy are few. The ineffective state monopolies would soon be eliminated in competition with private firms.

Assume, that there are 5 state monopolies and that they will lose profits corresponding to the total gain for all the private firms, that is \$1 billion (\$1,000 times 1 million) or a \$200 million gain for each monopoly. Similarly, it will cost the monopolies \$100 million in total to lobby against the market economy and thereby try to preserve their state monopolies.

Figure 3 shows that in this case it is profitable for the individual monopoly to lobby on its own for preventing market economy. One monopoly will on its own earn a net gain A_i (\$100 million) by producing the amount Q_i at the cost C of \$100 million.[10]

iii) Asymmetrical political pressure against market economy

The theory above hypothesizes that an asymmetrical political pressure against the transition to market economy will occur in Eastern Europe. Each of the 5 state monopolies would have a strong economic incentive to provide

10. If the 5 monopolies agree on sharing the lobby costs, each of them must only pay \$20 million. The individual gain, *Vi* can be found in Figure 3 as the sum of *A*i and *C*.

the collective good of non-transition on its own and earn a clear $100 million. Therefore this small group with only a few members will oppose the transition to market economy even in the absence of organization.

In contrast, none of the private firm owners will lobby for transition on their own. Because each of them would gain only $1,000 and would then have to pay all the costs of $100 million for lobbyism. Even though the group as a whole would receive ten times the money invested by collective action ($1 billion in total gain vs. $100 million in total cost), it will not provide the good because this group is not organized. Therefore this large, non-organized group will not promote the transition to market economy.

So, based on Olson, we hypothesize that the few state monopolies are in a strong position to win the economic struggle in the political arena and prevent transition to market economy.

Political institutions, lobbyism and transition

Under what circumstances do we expect organized interest groups to be successful in their lobbying? According to institutional economists like Douglass North and Barry Weingast, the ability to acquire favorable regulation, is strictly related to the formation of political institutions - understood as 'the rules defining the hierarchical structure of the polity, its basic decision structure and the explicit characteristics of agenda control.'[11]

Their argument is also illustrated with reference to the development in England after the civil war in the seventeenth century. Contrary to Olson, who emphasizes the role of interest groups in his study of British prosperity and decline, North and Weingast attributes the rise of England mainly to the constitutional change following the Glorious revolution in 1688-89. For North and Weingast, the most important feature of the revolution was the way political power was divided. The revolutionary settlement stated that the parliament gained the upper hand in financial matters. Hence, parliament acquired the power to raise new taxes and the rights to monitor and veto spending by the king. On the other hand, only the king could propose an expenditure, which parliament again had to authorize. The outcome was a complex institutional arrangement of checks and balances in which the parliament became the new locus of power, but where the crown still held significant political power.[12]

According to North and Weingast, the new constitutional arrangement had an independent (positive) impact on public policy. First, private property rights became more secure than under the Stuart kings. The rights that the state granted to private agents were now more difficult to renege on, as more actors had to accept such renegation. Second, power sharing and parliamentary supremacy, mitigated rent-seeking activities, by raising the price of favorable regulation. Interest group seeking private benefits now had to deal with both the king and the parliament, which in itself consisted of several actors. Hence, North and Weingast conclude that the institutional arrangement 'significantly limited publicly supplied private benefits'.[13] By establishing rules that increased the number of

11. North (1990:47).
12. North and Weingast (1989:816).
13. North and Weingast (1989:818).

political veto players, England effectively rendered rent-seeking activities more difficult. Not only were private interest groups weakened by violent conflict, as Olson suggests – they also had to pay a higher price for favorable regulation than they previously paid under the centralized political system of the Stuarts.

How does this logic relate to countries undergoing the transition from centrally planned to market economy? The lessons from North and Weingast's study suggest that the political institutions devised during the exit from the old system are crucial for performance afterwards. Likewise, we would expect the design of political institutions to be crucial for economic reforms in Eastern Europe. Harmful lobbyism from the groups surviving the breakdown of state socialism may very well be mitigated if new power sharing arrangements are established. On the contrary, smooth institutional adjustment, where no political veto players are installed, may lower the price of rent seeking.

It is important to note, in this respect, that establishing democracy is not necessarily enough. Even though democracy tends to mitigate pressures from narrow interest groups, democratic constitutions vary in their ability to raise the price on favorable regulation. To illustrate this, think of either a democratic super-presidentialist system or a parliamentary one-party system. In each case the price on special regulation tends to be lower than in a political system in which a multiparty parliament shares political power with a popular elected president.[14]

So, based on North and Weingast, we hypothesize that narrow interest groups will find it easier to influence economic policy when the post communist political institutions are centralized and without a plurality of political veto players.

Russia

In this section we will analyze how our simple integrated model relate to the Russian case. We begin our analysis with an assessment of the formation of interest groups when transition started. First of all: which groups were capable of acting as small groups immediately after the breakdown of the Soviet Union?

Interest group formation

A very robust finding is that the new private firms, established under the period of economic restructuring (perestroika) were not strong lobbies. They were not organized yet, were numerous and small and they couldn't act as a small group in any sector.[15]

With respect to traditional interest groups, Åslund (1995) lists four dominant state monopolies from the Soviet era: The military-industrial complex (VPK), the foreign trade establishment, the agrarian sector and the energy sector.

Even though the foreign trade sector thrived on the subsidized prices in the Soviet Union, it did not itself establish these favorable domestic policies by lobbying as a small group. In fact, the "cross-trading" option itself may be viewed as an unintended result of opening up trade in relation to Western Europe. This hap-

14. See Tsebelis (1995) for a discussion of how to count political vetoplayers.
15. As Åslund (1995:308) laconically puts it, the focus here is on profit seeking rather than rent seeking. It will probably take a significant amount of time before the new, private enterprises overcome the problems of getting organized against the old state monopolies. Favorable circumstances and the right leadership only occur occasionally, see Olson (1982) and Svendsen (1998a). See also Paldam and Svendsen (2000; 2001) concerning entrepreneurship, corruption and the level of social capital in Eastern Europe compared to Western Europe.

pened from about 1970 when the Soviet Union started getting desperate to stop economic decline and to reduce the technology gap with the West.[16] Again, as in the case of the new private firms, the foreign trade sector was not strongly organized and was characterized by numerous small traders. It couldn't, therefore, act as a small group.

Likewise, Åslund (1995) finds that the military lobby wasn't able to act as a small group. On the surface, this is a puzzling finding since the VPK traditionally was perceived as the strongest lobby in the Soviet Union. For example, the VPK consumed one-quarter of GDP in end of the Soviet era.[17] However, Åslund argues that the VPK lobby was weakened severely by internal competition. Already under the old regime, the Ministry of Defense had, quite non-ideologically, insisted on having several producers competing with one another. The goal was to keep up with the West in the arms race. For example, the half-dozen Russian airplane manufacturers had to realize that some would disappear and some survive. Each enterprise on its own competed in design, technology, and quality with several others. Therefore, there was no reason to collaborate and act as a small group.[18]

In contrast, the producers in the energy and the agrian sectors were never competing on the quality of their products. When producing the same products, such as grain and energy, the producers only compete over price. Because the state set all official prices in the Soviet Union, they could not even compete over price. Instead, they could act as small groups and lobby to get as many resources and subsidies as possible.[19]

These findings suggest that an asymmetrical process of lobbyism emerged at the time the Soviet Union fell apart. In any sector new private firms were weakly organized, while especially two of the traditional key industries were capable of promoting non-transition .

The structure of political institutions

Now, what were the political institutional conditions for rent seeking in Russia at that time? To answer this question, we briefly have to consider the circumstances under which Russia left the Soviet Union.

In Russia, the breakdown of the Soviet Union resulted in a very complicated constitutional situation. The main problem was that many Russians never really considered the breakdown before it actually happened in December 1991. The reason was that Russia for seven decades had dominated the Soviet Union. Therefore, even though a large majority of Russians were tired of communism, not everybody disliked the idea of a union they could dominate. Because Russian independence, unlike for instance Baltic independence, was never really an issue prior to the breakdown, no new Russian constitution was seriously considered and no new political institutions devised ex ante.[20]

Because of the lack of a genuine democratic revolt, Russia had to do with the institutions left over by the Soviet Union. Consequently, the constitution from 1977, including amendments, still applied. One important amendment was the introduction of a Russian president who, from November 1991, possessed almost dictatorial powers. The only check and balance in this super-presidential-

16. Aldcroft and Morewood (1995:162-65).
17. Åslund (1995:300).
18. Åslund (1995:302).
19. Åslund (1995:302).
20. Sakwa (1997).

ist system was the weak and not even democratic Congress of Peoples Deputies which had been elected in semi free elections in March 1990 as a part of Gorbachev's democratization of Soviet political life.[21]

Bargaining and policy outcomes

If we recall the lessons from the theoretical literature presented, seventeenth century England prospered due to a virtuous combination of weak interest groups and divided political institutions which had positive consequences for the formulation of economic policy. In many ways, the development in Post-Soviet Russia resembles this logic. The only difference is simply that England represents the positive version of the story, while Russia represents the negative version. This becomes clear when we evaluate the development following the breakdown of the Soviet Union in late 1991.

Initially, Yeltsin started out with an optimistic and liberal economic policy in January 1992. With assistance from well-known economists like Jeffrey Sachs and Anders Åslund, a comprehensive plan was launched on January 2. Prices ceilings were eliminated, foreign trade liberalized and subsidies cut almost over night. Unfortunately, he was an easy prey for the best-organized interest groups that survived the non-violent breakdown of the Soviet Union.

During 1992, massive protests forced him to rethink his strategies. In December, the more conservative industrialist Victor Chernomyrdin replaced the liberal Prime Minister Yegor Gajdar. This very appointment signaled that Yeltsin, as the locus of power, effectively had been captured by the groups, who managed to act like like small groups: Chernomyrdin was chairman of Gazprom, by far the biggest energy company in Russia![22]

Chernomyrdin and his discrete agrarian supporters soon engaged in redistribution on expense of the groups not properly organized. Consequently, the military lobby received only a minimum of state orders and subsidies so that production of military goods fell by 68% from 1991 to 1993. The foreign trade lobby effectively lost its "cross-trading" profits when foreign trade was liberalized in January 1992, and were not able to re-establish their monopoly rents at any time during the Yeltsin-Chernomyrdin reign.[23] In contrast, the energy and agrarian lobbies maintained their privileges. The energy lobby (gas, oil and coal lobbies) remained subsidized and exempted from virtually all taxes. In 1993, coal and gas prices in Russia were as low as 4% of world market prices.[24] Likewise, the agrarian lobby received about half of the subsidized credits and the most of the budget subsidies in 1993.

Generally speaking, the pace of private sector reforms was slowed after the appointment of Chernomyrdin. Even though more than 15,000 industrial enterprises were privatized from 1992-94, these were mainly 'pseudo' privatisations, as effective corporate governance was not established. Many privatized firms were brought under control of persons closely affiliated with the energy lobby, and especially Gazprom has converted many unpaid gasbills into direct ownership.[25] From this position, they have been able to extract subsidies from the state, often in

21. White, Rose and McAllister (1997).
22. Sakwa (1997:238).
23. Åslund (1995:300).
24. Åslund (1995:300 and 303).
25. Gustavson (1999: 48).

collusion with local enterprise managers and workers trying to keep their jobs.

The viscous combination of strong asymmetrical lobbying and centralized political institutions was subsequently buttressed by the constitutional development from 1993. In December 1993, Yeltsin, with support from especially the energy lobby, won a constitutional referendum that formalized the super-presidential system. The traditional Russian Duma was reinvented, but only to play a very marginal role in policy formulation. The locus of power continued to be effectively centered around the president, and parliamentary checks and balances did not develop. Hence, the price of rent seeking continued to be very low compared to other post-communist countries, as for instance Poland and the Czech Republic, where more effective and democratic division of powers were established to mitigate the pressures from the state monopolies that survived the breakdown of communism. [26] The chances of these lobbies to be successful in their bid for redistribution have been proportionally higher in Russia.

Conclusion

In this paper we have argued that the slow and uneven process of transition in Russia can be attributed to a combination of strong asymmetrical lobbying and an unfavorable constitutional framework.

New private firms have had severe difficulties in promoting transition due to the inability to act as small groups capable of effective lobbyism. On the contrary, energy and agrarian state monopolies with strong economic incentives to block transition were able to act as small groups. Unfortunately, the centralized political institutions inherited from the past were not able to mitigate their pressure. The presence of only one political veto player made it easy for them to promote redistribution that continues to crumble some of Russia's key industries.

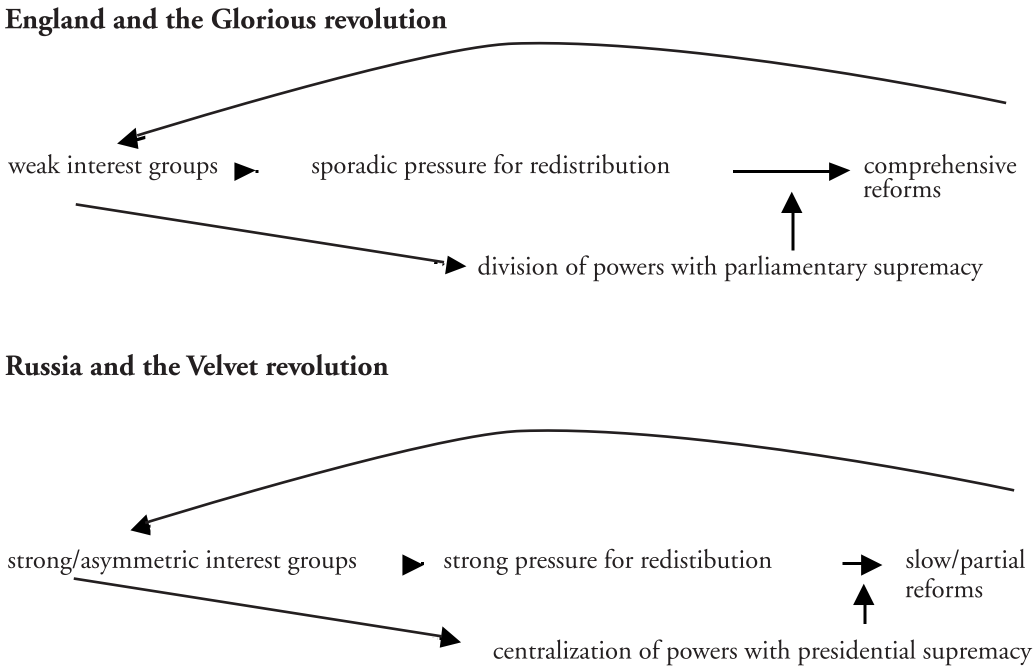
These lobbies have not met sufficient resistance from ordinary citizens who pay for the harmful subsidies. The Russian voters favored the formalization of the very centralized presidential system in 1993. Therefore, the price of rent seeking continues to be too low, which is not conductive to the adoption of more comprehensive reformpolicies. The adoption of more dispersed political institutions, like the institutions of post-revolutionary England, could have been an opportunity to kick-start the battle against the rent seeking of the surviving state monopolies. Unfortunately, it turned out to be another missed opportunity in Russian history.

The few positive results are mainly determined by the inability of the foreign trade and military lobbies to act as small groups. Hence, Russia has eliminated both the foreign trade monopoly and a good deal of the military industrial complex. It does not, however, offset the welfare losses caused by the negative elements of the Russian reform program.

The interdisciplinary positive political economy model has proven to be valuable in the search for explanations to why Russia has found it so difficult to capture the gains from a coherent reform program. From this perspective, Russia's rugged transition path and the failure to emulate the English/ British mir-

26. It is not finally settled whether there is a significant correlation between political institutional design and the scope of economic reforms when including all post-communist states. Hellman (1996; 1998) and EBRD (1999) all identify a strong positive relation between division of power and economic reforms, while Nørgaard on the contrary, argues that the correlation disappears when controlled for initial socio-economic conditions (Nørgaard, 2000:141-2).

Figure 4.
England vs. Russia



acle in the seventeenth century can be attributed to an unfortunate interplay between actors and the rules devises for political interaction. Contrary to the Glorious revolution, Russia's 'velvet revolution' eliminated neither interest groups, nor the centralized political institutions of the past. No clean breaks were made, as Russia inherited both the actors and the constitution of the late communist era. Consequently, the processes that supported growth in seventeenth century England, supported rent seeking and slow transformation in Russia. These logics are summarized in figure 4:

Recommendations and perspectives

The results listed above are mainly theoretical suggestions, which can be more carefully operationalized and empirically tested. However, positive political economy sheds a fresh perspective on the process of transition to market economy in Eastern Europe.

To solve the problems of uneven and slow transition is extremely difficult. As mentioned above, the Russian voter's who pay the incomplete reform program, could have reacted when they had the chance to open up the centralized system. Today they can mainly react by replacing the president. Of course that is an option, but no matter who is appointed for the job, he continues to be an easy prey for the groups, which are seeking to block transition.[27] It seems that the Russian voters have to insist on a belated democratic revolution, where the centralized institutions are replaced by a genuine power sharing arrangement. Of course the prospects of such an upheaval look bleak as all the problems of collective action apply.

What can the western world, and especially the EU, do? One obvious solution would be to undercut the old state monopolies by encouraging free trade. The EU must mobilize its consumers and taxpayers and hasten to open its markets to the East, especially the lucrative agricultural markets.

So far, the EU has pursued a cynical and protectionist trade policy towards Eastern Europe, especially with regard to agricultural products.[28] The well-organized farmer lobbies in the EU obviously fear the potential competition from Eastern Europe. Farmer organizations in the EU will oppose free trade to preserve their monopoly. Historically, they have acted as a successful cartel. Extensive lobby efforts have resulted in minimum prices and substantial redistribution to their group from European taxpayers and consumers. Both taxpayers and consumers within the EU would gain from free trade but, being weakly organized large groups, they have easily been overrun by the farmer organizations so far.[29]

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27. Newly elected President Putin seems to be aware of these problems. Thus, he has tried to fight the groups that so effectively captured President Yeltsin. It is doubtful whether he will succeed. Especially the energy lobby, which is strongly represented in mediacorporations, has much to offer a president seeking re-election.
28. Aldcroft and Morewood (1995:219-20) . Other important trade potentials in the EU, such as steel production, are protected too.
29. See Nedergaard (1995) and Daugbjerg (1998) concerning the well-established farmer lobbies, EU protectionism and policy networks.

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