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## **Explaining the Diversity of Post-Socialist Transformation Paths: The Evolutionary-Institutional Approach**

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The diversity of regional and national paths is a stylized fact of the past 17 years of post-socialist transformation. Many studies have pointed to the existence of the so-called “Great Divide” between the Central European and Baltic countries, on one side, and the Southeast European (SEE) countries and most of the CIS (Commonwealth of Independent States), on the other. The cross-regional or cross-country differences can be seen not only in the quantitative indicators of socioeconomic performance, but also in the characteristics of the emerging types of post-socialist system. While the Central European and Baltic countries that joined the EU in 2004 (the CEE-8) have made steady progress toward a well-functioning market economy, the post-socialist system in the SEE and the CIS has been marked by persistent insecurity of property rights, the lack of rule of law, and endemic corruption. Furthermore, the recent trends of stronger government involvement in strategic sectors in Putin’s Russia show that the type of socioeconomic system there --- which some authors have rushed to classify as “state capitalism” --- will vary considerably from the ones found in the CEE-8 and in the SEE region.

How can the diversity of post-socialist transformation paths be explained? Initial explanations have focused on economic reform policies, e.g. (1) whether a country implemented the Washington Consensus triad of stabilization, liberalization, and privatization (SLP); and (2) whether SLP reforms were carried out quickly or gradually (the shock therapy or gradualist approaches). Until about 1997, the dominant explanation of transformation failures was insufficient progress in SLP reforms. Since 1997, institutional and political economy explanations have become the mainstream. For example, the World Bank and the European Bank for Reconstruction and Development (EBRD) have often

stressed that institutional reforms such as hardening budget constraints, establishing financial and fiscal discipline, and encouraging the entry of new private firms were a major factor behind the “Great Divide”. The World Bank and the EBRD have also established a system of indicators (“governance” and “transition” indicators, respectively) to measure progress of institutional reforms in individual countries (see <http://www.govindicators.org/> and the EBRD’s annual transition reports).

Although explaining inferior socioeconomic outcomes with weak institutions or ineffective governance has undoubtedly been a step in the right direction, the mainstream approach has, in my view, failed so far to answer the following questions: (1) what are the reasons for weaker institutions in SEE and CIS countries with vicious post-socialist transformation paths? (2) is it possible for them to break away from a lock-in to a “bad equilibrium” by developing better institutions, and if yes, how? In this paper, I apply the evolutionary-institutional approach (Hodgson, 1999; Chavance and Magnin, 2000; Chavance, 2002) to the cases of Bulgaria and Romania to answer the above questions.

The evolutionary-institutional (EI) approach borrows concepts used in evolutionary theories such as path dependence, lock-in, selection, and diversity. However, since evolutionary theories can explain only gradual, incremental institutional change, they need to be complemented with some elements from institutional economics (mainly from the traditions of John Commons and Douglass North). In my view, these elements are path shaping based on anticipations of the future, political selection of institutions, formal and informal institutions, etc. Generally speaking, the aforementioned institutional economic traditions help overcome the limitations of evolutionary theories by bringing back “power” and “conflicts” into the analysis.

In this paper, I use empirical evidence from Bulgaria and Romania (SEE-2) to demonstrate the explanatory power of path dependence and lock-in concepts. In particular, I compare the starting conditions of the post-socialist transformation in the SEE-2 with those of the CEE-8. I also emphasize the role of domestic politics and some small events in the early stage of the transformation that have contributed to the lock-in to a vicious transformation trajectory. Furthermore, I regard economic crises in the latter half of the 1990s and the prospect of EU accession as the main factors that have induced path shaping, i.e. a change (bifurcation) in the post-socialist trajectory of the SEE-2.