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Economic System and Transition Mode: A Comparative Research on Transition Economies

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Abstract

This passage mainly deals with the problem of why different transition countries have different transition mode and different economic performance. According to this research, it has been found that the economic system of the traditional socialist countries played an important role in their process of reform and transition. The socialist countries with their different economic systems had determined the economic performance, the space, as well as the environment of the transition. All of this jointly formed the initial conditions of the transition, which further determined the different transition mode of the (post) socialist countries. The success or failure of internal reform on planned economies profoundly affected their later transition. On this occasion, it was not the different countries chose the specific transition mode, but was the transition mode had already been determined in the process of institutional change. If we concentrate on the process of the whole institutional change in these (post) socialist countries, the preconceptions of “radicalism” or “gradualism” will not lead the problems to the wrong path. By making the comparative research on different transition countries, an institutional reason was provided in order to better illustrate the China’s catch-up development after her reform and opening compared with other transition economies in their process of system transition and institutional change.

Keywords: economic system, socialist country, transition economy, institutional

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change, transition mode, structural reform, economic performance

1. Different Economic Performance in Transition Countries: Doubts and Biases

As the former communist countries began to find their way to the market economy, the transition economics had become an important researching field worldwide. When economists talked about the different economic performance among China, East European and the former Soviet Union countries, they were used to attributing to the different transition modes: gradual reform or radical change. Some people believed that, because of the gradual reform on the economic system and the strategy of disequilibrium promotion, China had found his way to the rapid economic growth with less transition cost through the induced institutional change (Lin, 1989; Lin, Cai and Li, 1993; Fan, 1993). Comparing the remarkable growth of China's economy after her reform and opening with the serious economic recession in the East European and the CIS countries which happened in 1990s, many people strongly blamed to the "Shock Therapy" and "the Washington Consensus" (Stiglitz, 1996; Nuti, 1997; Poznanski, 1997; Kolodko, 2000). They believed that it was the prevailing trend of neo liberalism had led to the catastrophe in these countries. Although the height of the transition has passed for more than a decade[1], the debate on which is the better mode for system transition of theses countries lasts till now. However, we may ignore the fundamental factor which is concealed by the argument on "Radicalism" and "Gradualism". That is the more basic reason for why theses countries have different transition modes, which then leads to different economic performance.

Compared with the transition mode, there has been an increasing attention to the initial condition of different transition countries relating to the research, such as the difference in economic structure before the transition, the duration and influence degree of planned economy, the distortion of macro economy, geopolitics, social circumstance and historical culture (Yang and Li, 2001; Popov, 2008, 2011a). The

[1] Most of the post socialist countries have finished the transition form central-planned economy to market economy. But in China, the further reform and transition is still in progress. Therefore, many of the world's major economies do not acknowledge China is being as a market economy not only economically but also politically.

most obvious difference in initial conditions, however, is the diverse economic system of traditional socialist countries. The operation mechanism of the economy and the specific transition background originated from the economic system, which played an important role in the economic transition in each country. Unfortunately, many people still believe that China and other post socialist countries shared the same economic system before their transition. They are accustomed to using the word “planned economy” by ignoring the huge difference on the economic system when they generalize the system transition and institutional change of these countries. The habitual ignorance and theoretical misunderstanding might lead to a plausible conclusion that all of the former socialist countries shared the same type of “planned economy”. By believing that all these countries were standing at the same starting point in the aspect of economic transition, the “determinism of transition mode” almost became the most persuasive theory to interpret the issues about the transition. However, the unilateral opinion may lead to misunderstanding since it isolates the process of institutional change by using the non-evolutionary analysis of institutions.

2. Different Types of Planned system in the Traditional Socialist Economies

The similarities of planned economy which established in different transition countries including the public ownership, the government leading in economic administration and operation, as well as the strategies of economic growth in traditional socialist countries, might mislead us to believe that there is no necessity to concentrate on the different types of planned economy at all. However, China’s planned economy was obviously different from the Soviet Union and East European countries during the period of 1958 to 1978. If the planned economy in Soviet Union and East European countries was respectively regarded as a typical one and an improved one, the system in China would be an “atypical” sample.

The typical central-planned economy, which was established in Soviet Union just at the same time of the “Great Recession”, was based on the thought and theory of centralized administration and state regulation in socialist economy. By using the

methodology of modern science, the authorities of socialist country believed that they had found a new approach with scientism and rationalism to manage the economy. By means of the command plan made by the central, the planned economy attempted to eliminate the spontaneity and blindness which commonly existed in the market. The economic calculation was widely used in the process of simulating the optimization of economy in order to realize a more efficiency level for resource allocation than the market economy.

As the framework of central-planned system basically formed in the Soviet Union, meanwhile, the "Lange Model", which was introduced in the debate on the calculation problem of socialist economy in 1930's, had provided a theoretical basis and practicability for a kind of market way to improve planned economy[1] (Lange, 1935). After the Second World War, with the enlightenment of the "Lange Model", many East European countries were convinced that they had already found an alternative mechanism against the market system in developing socialist economy. Despite the "Market Socialism" in many East European countries was regarded as an improved system compared with the typical planned economy, they still had something in common, that was the centralized administration, the bureaucracy, the emphasis on economic calculation, planning equilibrium, and the technicality of planning process. Based on the main features of these two types of planned systems, the authorities and economists in socialist countries argued that the planned economy would fundamentally solve the market failure, the periodic crisis and other economic problems in capitalist world. Despite the inherent defects of planned economy and the "Lange Model" which had already been pointed out by Mises and Hayek during the debate[2] (Mises,2008; Hayek,1975,1989), these economic systems still established in

[1] By assuming that the market of consumer goods and labor were established, there would be a dual price system in the planned economy. That was, the price of consumer goods and labor was decided by the market, but the price of capital goods was made by central authorities by means of simulating market competition. Lange believed that, with the simulation of market mechanism and the method of "trial and error", the planned economy could ultimately find the equilibrium price instead of the market. (Lange,1935).

[2] Mises emphasized that in the condition of socialist economy, the factor market would not exist in the public ownership of capital goods indeed. The price mechanism also could not regulate and optimize the resource allocation as it functioned in the market system. Therefore, it was impossible to solve the calculation problems of labor and capital goods by means of simulating the market (Mises,2008).Hayek argued that, because of the disregard on the information and incentive mechanism in economic operation, it was impossible for the central authorities to collect and deal with all of the information in the entire economy. What is more, the planning

most of the socialist countries after the Second World War.

Being as a representative model on economic modernization in socialist country, the central-planned economy with its strategies of industrialization and agricultural collectivization were completely transplanted into China in the early of 1950s. Based on the close relationship of Sino Soviet Alliance, as well as the lack of the experience on economic construction, China had no choice but humbly to study from the Soviet Union. With the implementation of central planning and the large amount of economic aid from the Soviet Union, China had basically established her industrial system during the First Five-year Plan (1953-1957). The simulation on "Soviet-style" system, however, ended in 1958 since the increasing divergence between the two communist parties not only politically but also ideologically. Instead of bureaucratic management, planning equilibrium and economic calculation in economic administration and operation, the command plan in China had become more and more aggressive and unpractical. The planned production of steel, crop and other capital goods were continuously exaggerated by the central authorities and local government during the "Great Leap Forward" (1958-1961)[1]. The high political fever and the fanaticism of ideology made China's economic system drift further way from the Soviet's typical planned economy during the mass movement and the personality cult. Although the central planning was remained in economic administration and operation formally, it did not work in terms of the rules and features of typical planned economy which was based on mathematical logic, balanced accounting, and the economic process of optimization. Compared with the former practice on planning, China's economy was sinking into a more primitive form which can be characterized as a kind of "Command Economy[2]" (Hicks,1987). Instead of emphasizing on the logic and

officials had no incentives to perfectly follow the optimal plans without considering their own interests. In addition, the central authorities can not afford the high computational cost in the real economic world. That is to say, only if the human beings handle the information at the speed of the occurrence of the information itself, can the optimization process of the planned economy become practically possible (Hayek,1975;1989).

[1] In order to quickly finished the socialist construction during the Second Five-year Plan and to provide the basis for transiting to communism. The political bureau of CPC discussed and approved "the Resolution on the Second Five-year Plan" on August 1958. According to the indicators of the planning, the total value of farm output would be grown over 2.7 times than that of 1957 in the coming five years. The total grain output would reach 750 million ton, as well as the steal and coal would be reach 80 million and 900 million ton in 1962.

[2] Hicks had researched the formation and evolution of "Command Economy" in the process of analyzing on the relationship between institutional change and economic growth. He argued that the "command economy" also had

rationality of planning process, the economy was managed and controlled by the romantic magisterial volition and personal preference which come from the highest decision-making level. The “supreme directive” or “command” with its strong political implications was totally optional and blind, since it was divorced from reality and had become more and more radical during the social mobilization. It sounded strange and absurd, but it was the true story of the evolution of China’s planned system from the Soviet-style to the “atypical” before her reform and opening.

In fact, after the rupture of Sino Soviet Relationship in the early 1960’s, the Soviet-style planned economy was quickly marginalized by the China’s authorities. Mao firmly believed that the Soviet Union was on his way to revisionism not only politically but also ideologically. He argued that China should get rid of the constraint of the Soviet-style and being controlled by the strong socialist neighbor so as to find her own way to modernization. On this occasion, instead of promoting the economic construction in terms of the way before, class struggle and mass movement became the main stream in socioeconomic life during the “Culture Revolution”. Factories in China were not managed by the experienced planning officials, specialists and technologists, but by people who had political passion and good class origin. The continued chaos, which resulted from the “Culture Revolution”, had led to economy fell into paralysis at the height of the movement. Unlike the Soviet Union, whose production order was coordinated by the command plan within the framework of a hierarchical bureaucracy system, the bureaucracy system which once had been established in China was nearly destroyed by the decentralization to the local and the mass movement. Therefore, instead of the coordination of scientific planning in economic system, the link between the central and the local, as well as the production and the consumption was suspended by a kind of anarchic chaos. In fact, the central government lost the control of the whole economy since both planning and “command” did not work normally. Compared with other socialist economies at the

mobility of factors of production and social division in a certain extent. Instead of being a consequence of the early development of the market, however, it was resulted in the specialization which made by the upper ruler in bureaucratic politics. The direction of institutional change in economy was from “Custom Economy” or “Command Economy” to market economy in the sense of modern commercial civilization (Hicks, 1987).

same time, there was a vacuum on the coordination mechanism in China's economic system: Neither the plan nor the market was functioning in the economic operation, which ultimately led the whole economy to disorder.

3. Different Operation Mechanism, Structural Reform and Their Performance

Although the differences are huge, we can still find some similarities, such as collectivism, the enforcement mechanism, the preservation of "command-submission" relationship, and political dictatorship among different planned economies which we have just discussed above. However, the divide on the evolutionary of planned system gradually appeared in socialist world. It should be observed that China had gone backwards in the process of institutional change for over 20 years, the terrible system made China become one of the poorest countries in socialist world before 1980s. Meanwhile, other socialist countries managed to improve or reform their planned economy. On the one hand, many East European countries had practiced the "Market Socialism" reform by means of partly fostering market factors under the planned system (Brus and Laski, 1989). On the other hand, the Soviet Union continued to perfect his central planning and optimization by using advanced techniques and methods.

It must be pointed out that the different planned systems with their diverse evolution paths determined their structural reform and economic performance before the transition. Although planned economy had dominated in the socialist countries for a long time and led to the rapid growth within a certain period, the inherent defect of the typical planned economy had been more and more obvious in the early 1970s. The continued weak growth in socialist countries universally indicated the inefficiency and disequilibrium of the planned economy as well as its operation mechanism. The failure of "Market Socialism" in some East European countries demonstrated that the "Lange Model" was merely a theoretical method to realize the planning equilibrium and economic optimization: Without considering the information cost and incentive mechanism, the theory did not make sense in practice. The deep-rooted conflict

between the individualism and collectivism within the planned system was the origin of many problems: shortage economy, soft budget and distorted resource allocation. The huge gap between the ideal and realistic socialism was the planned system could not eliminate the conflict of interest which had objectively existed. Therefore, it inevitably could not eliminate the obstacles which hindered the planned system to be perfectly performed.

3.1 The Aggrandizement of Central-planned System

The inherent defect of planned economy, in consequence, could not result in a sustainable economic growth. As the momentum of growth gradually weakened, the problems which chronically accumulated had forced the economy to be adjusted and reformed. By reviewing the history of the institutional change in socialist countries, it should be recognized that the more developed the planned economy was, the more difficult to make progress in structural reform. The phenomenon called “the lock-in effect” which mainly functioned in the highly developed central-planned economies. The Soviet-style system had gone so far on its way to perfect planning. Therefore it had not enough space to be adjusted, as well as could not gain plenty of bonuses from the internal reform (Jin and Qin, 2012). The bureaucracy system with highly concentrated structure, as well as the elaborately designed of labor division system with specialized network implied that the Soviet-style planned economy with its compact structure, interlinked and ordered relation, was an economic system of planning equilibrium. There was a strictly corresponding relationship on input and output for each kind of capital goods to each product. The precision of the central-planned system demonstrated that if a certain link of production went wrong, the whole process of economy would become disordered. What is more, the economic parameters which had been pre simulated would be reset. In consequence, the overall economic equilibrium would be adjusted and reconstructed. We can better understand this process by setting a simplified central-planned system. Under this circumstance, if the demand of product X, for example, is over its supply, the planning center will

increase the production by using command plan in order to keep the equilibrium. Usually, it would immediately readjust the capital goods $x_i (i = 1,2 \ldots m)$ and $y_j (j = 1,2 \ldots n)$ which are needed in producing X. However, as the capital goods x_i and y_j were pre settled for the former production equilibrium, the adjustment of capital goods will simultaneously change the balance of input and output of other product, as well as the equilibrium of whole system. Furthermore, in view of the dynamic interperiod problems of economy and the intensive mechanism of planning enforcement, the maintenance of planning equilibrium would be more complicated. In order to get rid of this situation, the central authorities more tended to control the demand of commodity by means of rating system. However, the severe disequilibrium between the demand and supply resulted from the control was the main character of shortage economy, which was a common fault in traditional socialist countries[1]. Thus, sectional disequilibrium in any step or link usually led to the overall disequilibrium of planned system. Instead of perfect planning and economic optimization, continued disequilibrium and readjustment are common in the real planned world. On this occasion, by means of command plan to rectify the disequilibrium which had been generated by the planned system itself only would further aggravate the disequilibrium of socialist economy conversely.

The Soviet Union also made his effort to promote internal reform by limited liberalization. From Khrushchev to Gorbachev, every attempt to structural reform eventually made the economy fall into disorder and chaos. The reason was the reform with their market-oriented policies ultimately resulted in the deviation from the track of central-planned system. Although the incentive of institutional innovation may

[1] There was another interpretation on the structural distortion in traditional planned system by analyzing the relationship between planned economy and industrialization. It was argued that the traditional planned system was an endogenous outcome of the priority development strategy of heavy industry (Lin, Cai and Li, 1994). The development of heavy industry did not coordinate with the resource endowment at that time. The market mechanism obviously could not solve the problem Therefore only by artificially reducing the cost of production could achieve the threshold of developing the industrial capital. On this occasion, a set of macro economic policies which indicated the overall distortion of product and capital goods with lower price eventually formed. Furthermore, in order to ensure the flow direction of these lower-price resources, as well as the surplus accumulation of the economy could make better use for the heavy industry, the enforcement of centralized management and planned allocation to these resources, with the deprivation of autonomy in management of the micro would naturally become the institutional arrangement. Thus, once the priority development of heavy industry was selected, the traditional planned system with these characters would be consequently established.

enhance micro economic performance in the short term, with the destruction of planning equilibrium and labor division system which the central-planned economy highly relied on due to the introduction of market factors, the entire economy would fall into disequilibrium. In order to recover the economic equilibrium, the central authorities had no choice but to improve and perfect the economic planning by using more precise mathematical simulation and optimization method. Thus, the limited liberalization often tended to abort and the economy which to be reformed would go back to the former practice. Actually, this was the institutional reason for the difficulty and dilemma of an essential reform on some traditional socialist economies. With its deep-rooted operation mechanism of central-planned economy, structural reform was much more difficult to be implemented in Soviet Union, Czechoslovakia, as well as East Germany. Obviously, the planned system was highly developed in these socialist countries.

3.2 The Dilemma on the "Market Socialism"

The "Market Socialism" once was regard as a stimulant to the planned economy since it could enhance the efficiency of socialist economy by partly introducing the market mechanism and promoting decentralization instead of maintaining command plan and hierarchical bureaucracy. As a combination of state regulation and market autonomy, the model of "containing a built-in market mechanism within planned economy" (Brus,1972)which developed in East European countries still had not fully clarified the boundary between the plan and market not only in theory but also in practice. The continued conflict between the formal rules of market mechanism and the informal restrains of planned system ultimately resulted in severe institutional exclusion which hindered the structural reform on its further way to the market economy. The weak growth in the long term indeed confirmed that the East European countries were facing difficulties in their later reform: Although the marketization had become an overwhelming trend to these socialist economies since the scope and power of market mechanism developed much further during the reform. The

authorities still restrained the market within the framework of planned system due to their conservative ideology and unspeakable interests.

Undoubtedly, the structural reform of these East European countries also had problems themselves. Despite the shadow price was good for improving the resource allocation to a certain extent by providing a cost benefit analysis to the enterprises, being as a tool of economic calculation, it still could not function as the real market price, which was more sensitive to showing the scarcity and providing incentives to economic activities (Ji,1994). What was more, the deficiency of capital and labor market implied that the interest and wage could not truly reflect the distortion in planned system. When some part of the economy was determined by the market mechanism, the rest which were still operated by mandatory plan or other former ways could not automatically correspond with the new mechanism. In consequence, the function of regulated market within planned system was limited. Thus the disequilibrium of traditional socialist economy still widely existed. The East European countries were actually facing a crossroad in their process of institutional change: Because of the practice of “Market Socialism”, marketization had made a breakthrough against the equilibrium system which was elaborately established by planned economy, however, the development of market power was still insufficient to reconstruct a new one. To further improve the planning equilibrium and the method of optimization towards central-planned system was obviously unrealistic to the economies which had gone so far to the market. Nevertheless, the structural reform was continuously disturbed by the institutional obstacles from the internal system. The traditional ways of state regulation and bureaucracy system with its implantation of ideology had penetrated into all fields of socioeconomic life, thus it had a profound impact on individual’s behavior and expectations to business activities as well as the further reform. After all, to what extent can socialist system can be preserved was indeed a serious issue to be discussed for these East European countries not only economically but also politically.

3.3 A More Extensive Space in China's Transition: Out of "Atypical Planned Economy"

Compared with the Soviet Union and East European countries, the operation mechanism of China's economy before 1978 was actually in a vacuum condition, which was called "no plan and no market". By promoting the highly-accumulated industrialization at the expense of sacrificing the agricultural growth and social consumption, the real economic performance with its serious structural distortion was concealed by the rapid GDP growth. However, China was not affected by the "lock-in" effect[1] which happened in the Soviet Union. In addition, it did not experience the "dilemma on reform" similarly to the East European countries. The vacuum of operation mechanism, however, provided an extensive space for the structural reform on China's economic system. By means of recovering the scientific planning and promoting the market-oriented reform, China's economy benefited both from the plan and market which brought in the "order" and "efficiency" comparing with the continued chaos and low inefficiency before 1978 (Jin and Qin,2012). The disequilibrium of the "atypical planned economy" had been improved by the structural reform, and the achievement was directly reflected in the increasing economic performance after the well-known reform and opening.

Being as a transitional form of China's economic transition, the "dual track system" was indeed an institutional innovation according to the real situation at that time. It made the entire economy gain double benefit from the recovery of scientific planning and the introduction of market mechanism during the early structural reform. At the beginning of China's reform and opening, the function of scientific planning particularly played a more important role in recovering the order of production which had been suspended by the political struggle and mass movement for a long time. In fact, before the opening to the outside world and the promotion of a series of market reform, the government firstly stabilized the macro economy by resuming the planned

[1] Actually, the "path dependence" obviously functioned in the process of the institutional change in Soviet Union. The continued aggrandizement of central-planned system eventually resulted in a long existence of terrible institution with its lower efficiency. The operation mechanism in central-planned economy we have already analyzed could provide a direct material and real scene to the "path dependence" and the "lock-in" effect which were mainly introduced in the theory of institutional change (North, 2008).

system in order to lead the economy back to normal. Originally, the recovery made the plan still operate in the entire economy in a large extent. However, since the Soviet-style planned economy did not highly developed in China, the market factors could be more easily introduced into the institutional system. It can be observed that during the early times of China's structural reform, there was an evolutionary process which indicated that the plan was gradually giving place to the market in the aspect of operation mechanism. The "dual track system" divided the whole system into two parts: the internal and the external. The strategy of structural reform was to encourage the external to rapidly grow by the economic stimulant from the market. As the "demonstration effect" of the external began to function, it would further drove the internal to be reformed (Fan, 1993). During this process, more and more capital, labor, and other resources would flow into the external, which made the external become more powerful. The cognition of the market was deepened during the structural reform, and the better performance of the external also made the market to be more acceptable not only by the authorities, but also by the ordinary people. Because of saving a large number of transition costs in the short term, China was enjoying the rich bonus from the operation of "dual track system" during the 1980s[1]. Compared with the situation in Soviet Union and East European countries, being as a category of incremental reform, the early structural reform implied a kind of Pareto improvement to China's economy: From disorder, inefficiency and disequilibrium to a better situation by recovering the plan and developing the market. It was interesting and subtle that because of the negative impact from the "atypical planned economy" before 1978, China had more plasticity and more extensive space in economic reform and transition.

However, there was still questionable that in what conditions could the incremental reform became viable. Zhang (1997) realized that the difference between the China and Soviet Union on gradually promoting the incremental reform. He

[1] In view of the long-term effect of the institutional change and constitutional transition, some economist argued that the "dual track system" played a negative role in economic reform and constitutional transition. Sachs, Woo and Yang believed that the dual track approach to economic transition may generate very high long-term cost of constitutional transition that might well outweigh its short-term benefit of buying out the vested interests (Sachs, Woo and Yang, 2000).

argued that unlike the “dual price system” with strict quota restriction in China, the “dual track system” without quota restriction within the Soviet Union’s reform (1985-1989) resulted in a huge amount of resources flowing into the private sector. On this occasion, there was an increasing shortage and growth bottleneck in state department, since the loss of resource and the production decline was much faster than its growth. Because of the state department was much larger than China, as well as there was not a kind of compensation mechanism to preserve its production during the reform, the incremental reform in the form of “dual price system” in Soviet Union ultimately aborted.

3.4 Economic Performance under the Different Planned System

China’s economy grew faster than the Soviet Union in terms of GNP during the period of 1950-1980. The average of annual growth rate was over 10% in China and it was not more than 7% in the Soviet Union at the same time. This conclusion, however, was quite questionable since GNP did not reflect the real economic performance comprehensively. Based on the disequilibrium on the economic development, the “Late-development Advantage Theory” (Gerchenkron, 1962) was also adequate for interpreting the catch-up development of the agricultural countries to the industrial ones among socialist economies. China simulated the Soviet-style industrialization in her early economic construction. In addition, the effect of technology diffusion played an important role in the socialist camp, which indicated that the backward countries could realize more rapid economic growth with lower cost by simulating the advanced countries not only technologically but also institutionally. On this occasion, it was not surprised to see that being a backward socialist country, China had been at a higher speed in economic growth than the Soviet Union and East European countries. What is more, the violent economic fluctuation in backward socialist countries made the statistics lose its reference value in a certain extent, especially the fluctuation was due to non-economic factors such as politics, war and natural disaster. Take China for an example, the average of annual growth rate in industrial and agricultural production

was about 20.2% during the year of 1950-1952 but it was -31% in 1961 (Table 1). The fragility and abnormality of the growth implied that the backward socialist countries with their terrible systems usually resulted in worse economic performance.

Table 1：The Growth Rate of Total Industrial and Agricultural Output in China (1950-1977)[1]

1950	1951	1952	1953	1954	1955	1956
23.4%	**19%**	**18.3%**	**30.3%**	**9.4%**	**5.6%**	**16.5%**
1957	1958	1959	1960	1961	1962	1963
6%	**32.2%**	**19.5%**	**5.4%**	**-31%**	**-10.1%**	**9.5%**
1964	1965	1966	1967	1968	1969	1970
17.6%	**20.4%**	**17.3%**	**-9.6%**	**-4.2%**	**23.8%**	**25.7%**
1971	1972	1973	1974	1975	1976	1977
12.2%	**4.5%**	**9.2%**	**1.4%**	**11.9%**	**1.7%**	**10.7%**

It was generally believed that the socialist countries were used to forging and cheating in their economic statistics for political and ideological reasons. However, the unconvincing statistics could also reflect the reality. Compared with the disorder and chaos of the “atypical planned system”, the economic performance of the Soviet Union and East European countries were much better than China. Taking the Soviet Union and China for an example, in consideration of the huge gap on the level of economic development in these two countries, we selected the different periods in order to maintain the fairness of the comparison.

Table 2: The Comparison on Economic Performance between the Soviet Union and China[1]

	Period	The Growth of Worker’s Real Income per capita	The Rate of Decline in Agricultural Population
Soviet Union	1921-1940; 1946-1959	390%	32%
China	1952-1984	129.4%	3.3%(1949-1981)

We correspondingly regarded 1921 and 1952 as the different starting point of economic construction in these two socialist countries. According to the 32 years of

[1] The source of the statistics: China National Bureau of Statistics.
[1] The source of statistics: Qin (2003).

economic growth, it was obviously to see that the Soviet Union has a better economic performance than China (Table 2). What is more, the trend of rapid growth in Soviet Union had been sustaining until mid 1970s which is not showed in the table. Meanwhile, China's economy was on his way to collapse. In fact, statistics from 1978 to 1982 of China was also added in the comparison. If we removed this part of statistics which being as a favorable factor to China including the economic growth in the early time of her reform and opening, the comparison would be more convictive that China's economy profoundly suffered from her "atypical command system" for such a long period.

4. China's Catch-up Development: A Comparative Advantage on Initial Condition

Different institution determined different economic performance. China had experienced a worse economic performance compared with most of the socialist economies before the transition. On the contrary, the terrible system provided a more extensive space for her later reform and transition. Because of the "atypical planned system" with its disorder and inefficiency, the structure, organization and institution of China's economy became more reformable. The marginal effect of the reform indicated that China might go further in her process of institutional change not only economically but also politically. Being a critical component of the initial condition, the "atypical planned system" was also a comparative advantage to other socialist economies which led to China's catch up development in her following reform and transition.

As a special aspect of initial conditions, the institutional space and environment of transition jointly modeled the path of institutional change in socialist economies. It also further affected the transition performance of these countries. The reform on economic system in traditional socialist countries had become a critical basis and prerequisite for their later market-oriented transition. It was believed that the more reforms on decentralization and liberalization within the planned system, the economy

would have a more favorable starting position in their later market-oriented transition (Kolodko, 2000). In addition, the management and policy implementation might also be much easier to be promoted at the beginning of the profound transformation. This conclusion was proved by the evidence that, despite both had experienced the serious recession during the 1990s, the recovery and growth of East European economies were universally much better than the CIS ones since the “Market Socialism” had been practiced in some of them before the transition.

4.1 The “Late-development Advantage” in the Evolution of Labor Division System: From an Economic Transition Point of View

China had a more extensive transition space in the aspect of the evolution of labor division system (Yang and Li, 2001). Compared with the highly centralized and specialized labor division system of Soviet Union’s industry, the low-evolved labor division system provided a more favorable condition to the development of township enterprises at the beginning of China’s reform and opening. The central-planned system with its highly concentrated mode of production and organization form was nearly destroyed by the decentralization to the local during Mao’s period. According to a related research, until 1978, China’s rural area was still in a considerable degree of self-sufficiency (Yang, Wang and Wills, 1992). Despite China had stimulated the industrialization mode from the Soviet Union during her First Five-year Plan, which resulted in a relatively high level of labor division in urban. The disequilibrium development between the rural and urban in China, however, made the rural still maintain a very low level of commercialization for a long time, which implied that it was much more easily to develop market mechanism with commercialization under a low-evolved labor division environment. On the contrary, the development of private property and other market factors was more difficult to intensify in a highly specialized network of labor division economy within the central-planned system. Under this circumstance, the small-scaled household production and fragmented individual economy in China began to emerge and develop in the middle of 1970s,

which eventually become an institutional momentum to disintegrate the planned economy. In addition, township enterprise which was mainly originated from the collective economy in China was getting more and more development space under the informal system of “ambiguous property right”. With its booming intensification during 1980s, the new organization had become a critical dynamic of the rapid economic growth in the process of reform and opening. In fact, all of these above had vividly indicated the low-evolved labor division system was good for the formation and the development of new organization and institution in China, despite the whole process was not independently directed and controlled by the outside force. It was argued that the degree on the evolution of labor division determined the transition mode of traditional socialist economies in a certain extent. The highly industrialized labor division network which was coordinated by the central-planned system would be out of order at the same time of the elimination of central planning. Thus, the gradual reform on economic system was more prone to cause a kind of institutional inertia on the central-planned economy.

The completely opposite in the aspect of the evolution of labor division system between the Soviet Union and China had led these two countries to different paths in each process of structural reform. In fact, the reform was more easily to be promoted where the labor division system was not highly evolved, especially in China’s rural area. On the contrary, being as an industrial economy with the high level of labor division, it was more difficult to make progress in promoting the reform in urban, where the industrial economy was constructed by the central-planned system. On this occasion, the relative economic sector, especially the state-owned enterprise would be the main beneficiary of the existing institutional environment. Thus, it was common to see that workers in urban state-owned enterprise were used to being provided with the “iron rice bowl” (an occupation with absolutely guaranteed job security, as well as steady income and much social welfare) by the government. Compared with only 18% of the labor force in non-agricultural organization among China’s state-owned sector before 1978, more than 85% of the labor force was working in stated-owned

industrial enterprise at the same period in Soviet Union (Sachs and Woo, 1999). In view of the risk and uncertainty that resulted from the later reform and transition, the labor benefited from the planned system was more eager to maintain their original living standard and social status. Thus, these people had become a strong resistance against the later reform, which made the central-planned system more difficult to disintegrate, as well as more difficult to promote further market-oriented reform.

4.2 The Household Contract Responsibility System: A Pareto Improvement on China's Rural Economic Institution

A noteworthy problem was the reform on rural economic system in these traditional socialist countries. Most socialist countries (Yugoslavia and Poland was an exception) implemented the agricultural collectivization which was introduced by the Soviet Union in 1950s. Regarded as an important driving force and strong guarantee for realizing the modernization and communism, China also implemented the same policy by establishing "communes" to replace the small-scaled household production. Although both suffering from the distortion of the planned system, the Soviet Union had less pressure on industrial development at the expanse of the rural owing to his more advanced mechanization in agriculture and higher level of urbanization than China. Compared with the collective farms and peasants in Soviet Union, the communes in China were reveling in the idealistic Utopia which designed by the authorities. In 1966, a security wage system guaranteed by the national bank was established in Soviet Union for improving the living standard of the rural, which indicated that the peasants in Soviet Union had almost shared the same level of social welfare (basic wages, medical care, pension insurance and other social securities) as the workers in urban state-owned enterprises (Jin and Qin, 2012). In China, however, the network of social security only covered the urban state-owned sector, which merely accounted for about 20% of the whole population. Over 71% of the labor force in rural which had played an important role in supporting China's industrial development was short of the basic social security during the 1960s-1970s (Yang and

Li, 2001). Compared with the collective farm in Soviet Union or the household farm in Yugoslavia and Poland, the rural economic system before 1978 was an unbalanced institutional arrangement to China's peasants with "less protection or even no protection but more restrictions[1]".

The rural productivity and the enthusiasm on agricultural production in China were undoubtedly restrained by the system for a long time. The egalitarianism of rural economic system not only led to the real unfairness but also resulted in sacrificing the material production. Therefore, people strongly appealed to the authorities to change the institutional arrangement on agriculture production and management. In fact, the establishment of the household contract responsibility system in China was typically an induced institutional change from the bottom up, which profoundly reflected the most urgent requirement from the peasants that to adjust and reform the existing system. There was no denying that the development of the rural and the improvement of living standard were restrained by the planned system for a long time. Compared with other socialist economies, the disequilibrium between the agriculture and the industry, as well as the rural and the urban was more serious in China. On this occasion, the rural economic system had a huge potential to be reformed, which would ultimately release a tremendous productivity for China's rapid growth. Being as an incremental reform, without damaging the benefit of any other social class, the establishment of household contract responsibility system was a Pareto improvement which increased the net income of China's peasants. What is more, the large amount of labor was released by the reform at the same time. The whole economy, especially the non-state-owned sector was benefited from the labor flowing to the export-oriented and labor-intensive industry in the process of the labor redeployment during 1980s.

On the contrary, it spent much cost in reforming the existing rural economic system in Soviet Union and East European countries. Peasants were used to enjoying

[1] Qin argued that owing to the agriculture collectivization, peasants in Soviet Union lost the freedom to individually or separately manage their production. However, they gained relatively higher level of social security from the government as a kind of compensation to their submission to the planned system. Thus, there was an almost balanced rural economic system with equal amount of "protections" and "restrictions" (Qin, 2003).

the benefit or "protection" which was provided by the system. Considering the huge state sector almost covered the whole economy in Soviet Union, it was nearly impossible to promote incremental reform relying on labor redeployment from the agriculture to the non-state-owned sector as China[1]. It was more likely to result in a Pareto improvement on institutional change from a worse system with its lower starting position. Obviously, the success of incremental reform was based on China's special initial conditions, which made the marginal effect of institutional change from the worse to the better more remarkable.

4.3 The Legacy of Planned System: Different Function and Effect

Undoubtedly, the legacy of planned system also played an important role in the process of institutional change. One of the most important factors of China's catch-up development was that it properly maintained and took advantage of the positive side of the legacy of planned system. Although centralized politics and mass movement in the name of class struggle was a painful experience during Mao's period, it destroyed the basis of the bureaucracy and also developed a strong mobilization mechanism at the same time. What is more, the legacy of planned system had provided a favorable institutional environment including a powerful state system, a more efficient government, as well as a large quantity of human resource for China's later economic reform (Popov, 2011b). Therefore, the high degree of central authority and efficient operation of the government guaranteed the rapid economic growth politically (Acemoglu, 2013)[1]. A political system of "neo-authoritarianism" in China was established and evolved during the process of economic reform and transition. Compared with the political environment before 1978, the decision level was more enlightened, open-minded and had more inclusiveness. Therefore, it implied that the market-oriented reform had become more and more acceptable to the authorities.

[1] Sachs and Woo observed the obvious difference on economic structure among traditional socialist countries. They believed that this determined the different performance on structural reform before the transition, as well as the different transition approach to these countries.

[1] Some people realized that a powerful centralized government was needed to ensure the stable production of the state-owned sector during the early period of transition. However, with the authority of the government and communist party seriously decreased in Soviet Union, there was no favorable condition for smooth transition to the market (Murphy, Shleifer and Vishny,1992).

Instead of the class struggle and the fanaticism of ideology, the authorities realized that only by promoting the rapid economic growth in order to continually improve people's living standard, can essentially support the legitimacy of the socialist regime.

It must be pointed out that the economic transition of the most socialist countries was promoted by the government basically. That is to say, government guiding was the driving force of the entire institutional change. The government function represented the state institutional capacity which played an important role in reform and transition (Jing and Huang, 2011). Compared with the immaturity of the newborn democracy and the continual confliction among various kinds of ideologies which happened in the East European and many CIS countries during their first ten year of the transition, China had maintained a more stable political system and social order in the process of promoting her economic reform and transition for over 30 years. It supported China constantly to gain a large amount of reform bonus and to maintain her rapid growth momentum. On the contrary, regarding as a negative and backward factor, most of the East European and CIS countries had completely distanced themselves from the legacy of planned system not only economically but also politically. The market-oriented transition under the "neo-liberalism" had shaken the institutional tradition of "Big Government" in most of the socialist countries. The ignorance of the government function and the state institutional capacity, however, led to their fragile institution basis could not fully support the rapid transition in the short term. It was generally believed that the serious recession which suffered by these countries during the early 1990s was due to this reason. On this occasion, the legacy of planned system, as well as the attitude towards it also affected the different "selection" on transition mode in a certain extent.

4.4 The Institutional Change of Holism: A Weaker Effect on Institutional Exclusion

The constant interaction between the formal rules and informal restrictions in the process of institutional change was interpreted in detail by the new institutional

economics (North, 2008). It was generally believed that the incompatibility between these two aspects would increase the cost of institutional change and would eventually result in a strengthening effect of institutional exclusion. Compared with China, the institutional exclusion had functioned in the East European countries more obviously. Since the parliamentary democracy had been established in many countries before the Second World War, as well as the capitalist economy had developed in a certain degree. The Soviet-style socialist system to these countries, however, was a kind of institutional transplantation which was imposed by their powerful liberator. Highly centralized politics and economy was alien to their traditional culture, as well as the people's cognition of democracy and liberty which had been cherished by the East European society for a long time. The institutional exclusion impelled these countries to break through the framework of the Soviet-style system by promoting various kinds of reform under the anti-Soviet mood and the appeal of national self-determination. All of these were vividly reflected by the tortuous practice on "Market Socialism" in East Europe. On the contrary, the centralized politics and economic control of planned system in socialist China was similar to the characters of traditional system in her feudal society to a certain extent. It had lasted for over two thousand years, which profoundly affected the institution and social culture of China not only in the Mao's period, but also nowadays. On this occasion, the existing system in China was still rooted in the institutional culture, which showed the consistence and the holism of institutional change. Therefore, from a macro and historical point of view, China had a weaker effect on institutional exclusion than most of the East European countries who were suffering from the continual "friction" between different institutions until their unpleasant practice of socialist system ultimately went to the end.

5. A Brief Commentary and Conclusion

We have already made a comparative research on different planned systems with corresponding performance of socialist economies before their transition. According to the different process of institutional change in these countries, we had found the

institutional reason of China's catch-up development in her later reform and transition, which was the comparative advantage on the initial condition. It was ironic that the continued deterioration of economic performance and institutional environment once was regarded as a favorable factor of promoting the transition by the reformists of these socialist countries. Crisis was an opportunity for the reform indeed, which made people realize that the current situation was unsustainable. It seemed that the political implication of "the worse is better" was more significant in the aspect of economic transition. However, it implied that more social cost would be paid for the reform and transition from chaos to order at the same time. Compared with the Soviet Union and East European countries, though suffered from a worse economic performance before reform and opening, the system provided China with a more extensive transition space and a more favorable transition environment instead. Being as the initial condition of institutional change, these factors had become a comparative advantage on China's catch-up development. However, it did not indicate that "the worse is better" had other special implication to backward socialist economies[1]. It should be emphasized that the sensible policy and strategy were important as well to the substantive reform and sustainable development of transition economies.

According to the performance of structural reform in different transition countries, It had been concluded that the more developed the planned system was, the more difficult to promote market-oriented reform gradually. The failure in the structural reform on planned system ultimately led the Soviet Union and East European countries to choose the thoroughgoing change by taking radical reforms. Benefited from the large amount of reform bonus by incremental reform in the form of "dual track system" during 1980s, China was used to the moderate reform and gradual improvement on the economic system. Therefore, it was not different transition economies chose the specific mode, but was the transition mode had already been determined in their each process of institutional change. That was the institutional reason behind the transition.

[1] The potential booming growth of North Korea under her existing system was still uncertain. The country was generally regarded as maintaining one of the worst institutional environments in the world. Perhaps we would not witness the "North Korea's miracle" in our generation, since the sign of essential change was still unable to see.

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