

# Post-Communist Transition as a Critical Juncture: Political Origins of Institutional and Cultural Bifurcation

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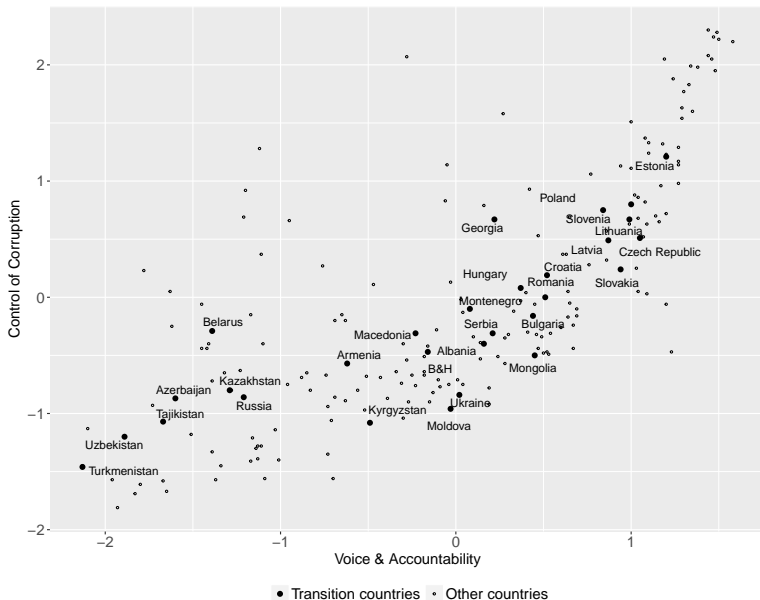
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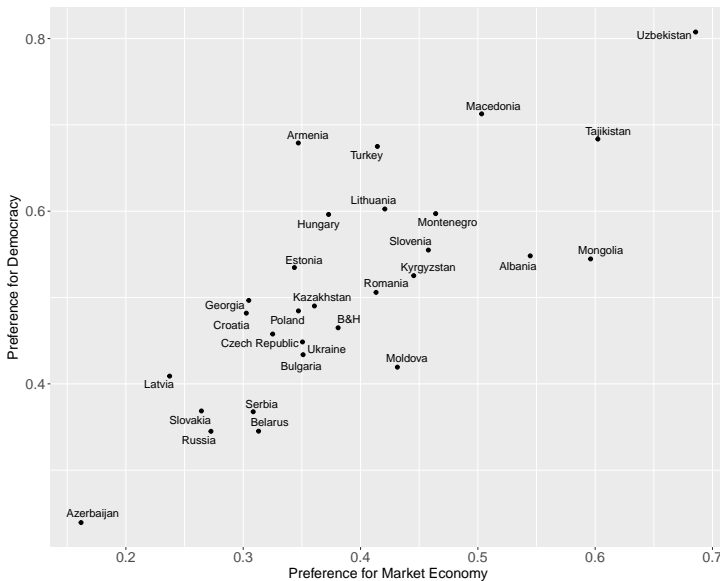
# Institutional Divergence

- Post-communist countries, despite of similarities of their political and economic systems prior to the collapse of the Eastern Bloc, presently exhibit vastly different institutional regimes, ranging from robust market democracies to oppressive autocracies, with disparate social and economic outcomes
- Cultural differences between these countries are similarly startling, especially in terms of modern vs. traditional views, autonomy vs. paternalism, civic culture vs. survival values, and attitude to market and democracy

# Institutional Map of the Transition Region



# Cultural Map of the Transition Region



- History — path dependencies and legacies (pre-communist, communist, and post-communist; Pop-Eleches and Tucker, 2017)
- Geography — proximity to the West (“distance to Dusseldorf”), natural resources (“Resource curse”) and EU membership, or credible prospect thereof (Sachs, 2018)

- At a critical juncture, factors which appear to be temporary and not expected to have long-term consequences, in fact send economic and political institutions in different directions and trigger persistent institutional patterns of either inclusive or extractive type (Acemoglu and Robinson, 2012).
- Economically, inclusive institutions are public production inputs supporting private sector development; politically, they ensure representation of broad societal interests. Extractive institutions, on the contrary, protect economic and political interests of the elites (“oligarchies”) at the expense of the rest of society.

# Political Plurality of Transition as a “Sorting Factor”

- A critical juncture could leave behind an extractive institutional regime if political power at the time when institutions are malleable is narrowly concentrated and devoid of checks and balances. In such case ruling elites form an oligarchy which crafts and thereafter protects extractive economic and political institutions.
- Vice versa, if political power at a critical juncture is distributed broadly and subjected to checks and balances, inclusive economic and political institutions obtain. In both cases institutions “harden” after a critical juncture and are sustained via resp. vicious or virtuous circles.

# The Importance of Being Inclusive

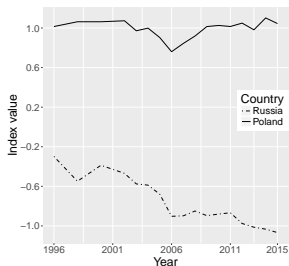
- Post-communist transition in the early 1990s bore all the hallmarks of a critical juncture (see e.g. Gelman, 2015; Gaber et al., 2018), but such role of the transition has not yet been demonstrated empirically
- We show that plurality **in the early years of transition**, measured by the number of political veto players (Tsebelis, 2002) has had long-term consequences for institutional quality, perceptible through the present time.



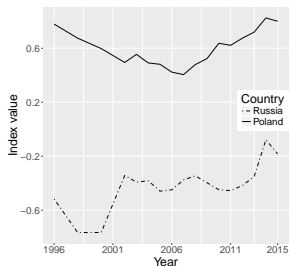
# Roots of Inequality and Cultural Divergence

- The same factor explains cross-country variations of economic inequality in the post-Communist region over the ensuing quarter of century, since high inequality is typical for extractive institutional regimes.
- Finally, we observe strong correlation between transition's plurality and the attitudes to democracy and free market in post-communist nations — countries which had more checks and balances in the early 1990s exhibit stronger social support of the market democracy. We explain this finding by the “institutional learning” as a mechanism shaping views and attitudes in a society (Mishler and Rose, 2007), and provide direct evidence of such process at work by establishing mediating role of institutions in the link between transition plurality and attitudes in society.

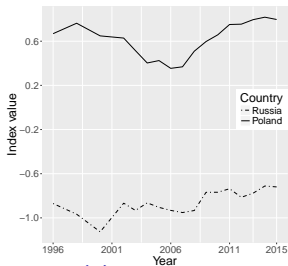
# Russia vs. Poland: Institutional Divergence



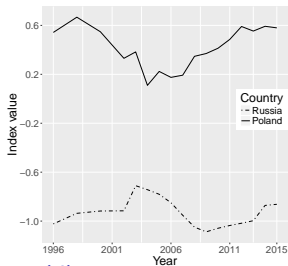
(a) Voice and Accountability



(b) Government Effectiveness

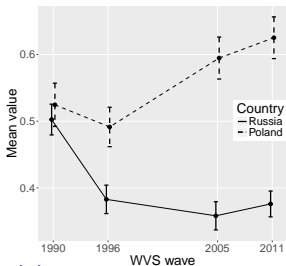


(c) Rule of Law

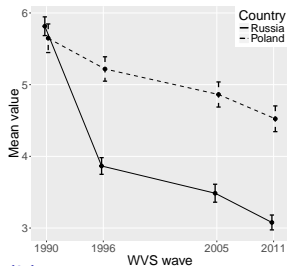


(d) Control of Corruption

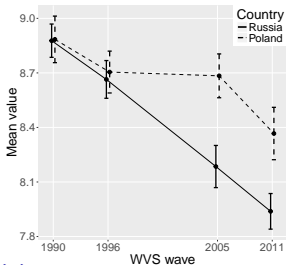
# Russia vs. Poland: Cultural Divergence



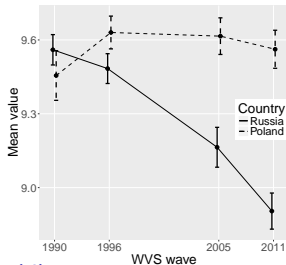
(a) People should have more say



(b) People should be responsible...



(c) Taking unjustified benefits is bad



(d) Unacceptable to take a bribe

# Plurality Was Not a Part of Transition Orthodoxy

- In the late 1980s-early 1990s there was a near consensus that successful transition required a strong executive autonomy insulated from societal control, and suspension of checks and balances in the interests of a resolute and radical reform (Haggard and Kaufman, 1995; Rodrik, 1996; Roland, 2000; Roland, 2002).
- Democratic support of reform was not expected ex ante, and hence it was recommended to ease democratic accountability of government to society and implement “reform from above”, insulating the reformers from societal control (Hellman, 1998), on the hope to obtain the necessary endorsement ex post, when reform benefits would fully transpire.

- Bresser Pereira et al. (1993) argued that more inclusive, pluralistic and competitive reform politics would stand better chances to consolidate the new economic and political institutions.
- Hellman (1998) warned against the danger of capture of the new institutions by narrow interests when checks and balances are weakened and the society at large lacks proper political representation. He observed a positive correlation between reform success and executive turnover in transition countries, arguing that political competition and democratic accountability were in fact conducive to successful transition.

- Gelbach and Malesky (2010) related EBRD's reform progress measures and the incidences of reform reversals to the checks and balances proxied by the number of political veto players (Tsebelis, 2002). These authors either average veto players over the 1992-2004 period, or use the current numbers of veto players in panel estimations over the same period, and find a positive association between veto players and successful transition.
- The significance of **contemporaneous** veto players for further reform progress declines at more advanced stages of transition, possibly pointing to a critical juncture effect, which however was not directly tested and confirmed in the above paper.

- We use the number of veto players from the Database of Political Institutions (Beck et al., 2001) to measure the degree to which transition politics was pluralistic and subject to checks and balances. We are interested in these measures in the early 1990s, when a critical juncture is expected to have occurred, and average the veto player numbers over 1991-1993
- Measures of institutional quality are from the Worldwide Governance Indicators project, which include annual scores in the following categories: Voice and Accountability; Political Stability and Lack of Violence; Government Effectiveness; Regulatory Quality; Rule of Law, and Control of Corruption. The period of observation is 1996-2016.
- EBRD's Life in Transition survey data are used to measure preferences for democracy and market economy.

# Institutional Quality and Inequality After Critical Juncture

|                            | Voice & Account      | Political Stability  | Govern Effect        | Regul Quality        | Rule of Law          | Corrupt Control      | GINI Index           |
|----------------------------|----------------------|----------------------|----------------------|----------------------|----------------------|----------------------|----------------------|
| Veto Players               | 0.236***<br>(0.032)  | 0.101***<br>(0.028)  | 0.061***<br>(0.021)  | 0.117***<br>(0.028)  | 0.167***<br>(0.024)  | 0.121***<br>(0.018)  | -0.981***<br>(0.265) |
| GDP per capita             | 0.430***<br>(0.052)  | 0.465***<br>(0.067)  | 0.502***<br>(0.035)  | 0.615***<br>(0.050)  | 0.634***<br>(0.044)  | 0.534***<br>(0.044)  | 2.844***<br>(0.592)  |
| Distance from West         | -0.057<br>(0.035)    | -0.128***<br>(0.045) | -0.058***<br>(0.021) | 0.052*<br>(0.027)    | 0.058**<br>(0.026)   | 0.029<br>(0.026)     | 2.993***<br>(0.386)  |
| Natural Resources          | -0.028***<br>(0.003) | 0.006**<br>(0.003)   | -0.022***<br>(0.002) | -0.033***<br>(0.003) | -0.021***<br>(0.002) | -0.022***<br>(0.002) | -0.279***<br>(0.060) |
| Constant                   | -3.961***<br>(0.620) | -3.509***<br>(0.798) | -4.299***<br>(0.410) | -6.053***<br>(0.560) | -6.664***<br>(0.499) | -5.533***<br>(0.524) | -9.257<br>(7.095)    |
| Year dummies               | Yes                  | Yes                  | Yes                  | Yes                  | Yes                  | Yes                  | Yes                  |
| <i>N</i>                   | 485                  | 479                  | 480                  | 480                  | 485                  | 485                  | 314                  |
| Adj. <i>R</i> <sup>2</sup> | 0.631                | 0.369                | 0.660                | 0.585                | 0.653                | 0.637                | 0.263                |

\* $p < 0.1$ , \*\* $p < 0.05$ , \*\*\* $p < 0.01$ . Robust standard errors in parentheses.



- With regional fixed effects for the following macroregions: (i) former Soviet republics, with the exception of the Baltic states; (ii) other Asian post-communist nations; (iii) the Baltic states; (iv) other European post-communist nations; estimation results become even sharper — veto players number in the early 1990s are now significant 1% for all six measures of institutional performance, and rise in magnitude by 25-75%.

# Too Many Veto Players, or Decreasing Returns to Checks and Balances

- Excessive veto players could be an obstacle to policy change. Furthermore, inclusive institutions require adequate political centralization (Acemoglu and Robinson 2012).
- When we add to the panel the square of veto players number, the coefficient of this variable is negative for all measures of institutional quality, indicating decreasing returns to checks and balances, but is significant (at the 1% level) only for the voice and accountability and regulatory quality measures. The optimal number of veto players for these measures across our panel is slightly above three.

- Institutional learning is a mechanism shaping views and attitudes in the society to institutions, including free market and democracy, through personal first-hand experience of living under such institutions (Mishler and Rose, 2007).
- Since checks and balances at the critical juncture of post-communist transition have had a strong effect on institutional performance, they can also be, via institutional learning, a sorting factor behind the observed variations in attitudes to market and democracy across the post-communist region. We test this by using the 2006, 2010, and 2016 rounds of the Life in Transition surveys

# Views and Attitudes After Critical Juncture

|                            | Market Econ         | Democracy          |
|----------------------------|---------------------|--------------------|
| Veto Players               | 0.022**<br>(0.011)  | 0.025**<br>(0.010) |
| GDP per capita             | -0.059**<br>(0.022) | -0.038<br>(0.028)  |
| Distance from West         | 0.021<br>(0.014)    | 0.034*<br>(0.018)  |
| Natural Resources          | 0.001<br>(0.002)    | -0.001<br>(0.001)  |
| Constant                   | 0.769***<br>(0.279) | 0.640*<br>(0.335)  |
| Year dummies               | Yes                 | Yes                |
| <i>N</i>                   | 78                  | 78                 |
| Adj. <i>R</i> <sup>2</sup> | 0.189               | 0.102              |

\* $p < 0.1$ , \*\* $p < 0.05$ , \*\*\* $p < 0.01$ .

Robust standard errors in parentheses.

# Direct Evidence of Mediation Effect

- To observe directly a mediation effect (in the sense of Baron and Kenny 1996), we include lagged values of institutional quality back to increasing number of years. Evidence of mediation would be numerical and statistical diminishing of the role of veto players during transition

**Table:** Mediation effect of institutions on views and attitudes

|                | Voice & Accountability | Political Stability | Government Effectiveness | Regulatory Quality | Rule of Law | Control of Corruption |
|----------------|------------------------|---------------------|--------------------------|--------------------|-------------|-----------------------|
| Market Economy | Medium                 | Strong              | Absent                   | Weak               | Medium      | Strong                |
| Democracy      | Absent                 | Weak                | Strong                   | Strong             | Strong      | Strong                |

# Mediation of Preference for Market Economy by Corruption Prevention

|                            | Preference for Market Economy |                     |                      |                     |                     |                     |                     |                     |                     |
|----------------------------|-------------------------------|---------------------|----------------------|---------------------|---------------------|---------------------|---------------------|---------------------|---------------------|
|                            | (1)                           | (2)                 | (3)                  | (4)                 | (5)                 | (6)                 | (7)                 | (8)                 | (9)                 |
| Veto Players               | 0.022**<br>(0.011)            | 0.022**<br>(0.010)  | 0.020**<br>(0.010)   | 0.020*<br>(0.010)   | 0.020*<br>(0.010)   | 0.016<br>(0.011)    | 0.016<br>(0.011)    | 0.012<br>(0.012)    | 0.011<br>(0.012)    |
| GDP per capita             | -0.059**<br>(0.022)           | -0.058**<br>(0.025) | -0.069***<br>(0.025) | -0.060**<br>(0.025) | -0.060**<br>(0.025) | -0.060**<br>(0.026) | -0.059**<br>(0.026) | -0.062**<br>(0.026) | -0.063**<br>(0.026) |
| Distance from West         | 0.021<br>(0.014)              | 0.021<br>(0.014)    | 0.020<br>(0.014)     | 0.022<br>(0.014)    | 0.022<br>(0.014)    | 0.021<br>(0.015)    | 0.024<br>(0.015)    | 0.020<br>(0.015)    | 0.020<br>(0.016)    |
| Natural Resources          | 0.001<br>(0.002)              | 0.001<br>(0.002)    | 0.001<br>(0.002)     | 0.001<br>(0.002)    | 0.001<br>(0.002)    | 0.001<br>(0.002)    | 0.001<br>(0.002)    | 0.001<br>(0.002)    | 0.001<br>(0.002)    |
| Corruption Control         |                               | -0.000<br>(0.027)   | -0.178<br>(0.112)    | -0.141<br>(0.112)   | -0.139<br>(0.121)   | -0.148<br>(0.125)   | -0.176<br>(0.131)   | -0.160<br>(0.128)   | -0.171<br>(0.132)   |
| Constant                   | 0.769***<br>(0.279)           | 0.768**<br>(0.294)  | 0.882***<br>(0.292)  | 0.791***<br>(0.293) | 0.795***<br>(0.288) | 0.824***<br>(0.305) | 0.800***<br>(0.300) | 0.862***<br>(0.305) | 0.892***<br>(0.318) |
| Lags of Cor. Control       | No                            | No                  | Yes                  | Yes                 | Yes                 | Yes                 | Yes                 | Yes                 | Yes                 |
| Year dummies               | Yes                           | Yes                 | Yes                  | Yes                 | Yes                 | Yes                 | Yes                 | Yes                 | Yes                 |
| <i>N</i>                   | 78                            | 78                  | 78                   | 78                  | 78                  | 78                  | 78                  | 78                  | 77                  |
| Adj. <i>R</i> <sup>2</sup> | 0.189                         | 0.177               | 0.185                | 0.187               | 0.175               | 0.181               | 0.180               | 0.182               | 0.164               |

\* $p < 0.1$ , \*\* $p < 0.05$ , \*\*\* $p < 0.01$ . Robust standard errors in parentheses.

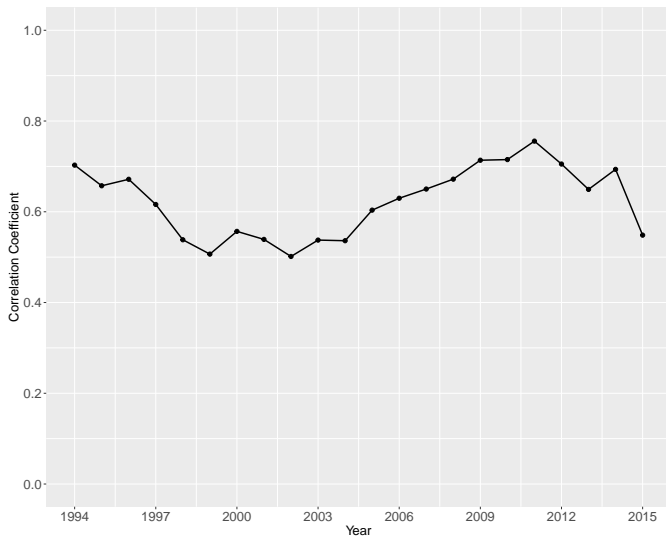
# Mediation of Preference for Democracy by Corruption Prevention

|                            | Preference for Democracy |                    |                     |                     |                     |                     |                     |                     |                     |
|----------------------------|--------------------------|--------------------|---------------------|---------------------|---------------------|---------------------|---------------------|---------------------|---------------------|
|                            | (1)                      | (2)                | (3)                 | (4)                 | (5)                 | (6)                 | (7)                 | (8)                 | (9)                 |
| Veto Players               | 0.025**<br>(0.010)       | 0.020*<br>(0.011)  | 0.017<br>(0.011)    | 0.017<br>(0.011)    | 0.017<br>(0.011)    | 0.013<br>(0.011)    | 0.013<br>(0.011)    | 0.010<br>(0.013)    | 0.011<br>(0.013)    |
| GDP per capita             | -0.038<br>(0.028)        | -0.060*<br>(0.030) | -0.078**<br>(0.032) | -0.077**<br>(0.032) | -0.082**<br>(0.032) | -0.082**<br>(0.032) | -0.081**<br>(0.032) | -0.084**<br>(0.033) | -0.083**<br>(0.033) |
| Distance from West         | 0.034*<br>(0.018)        | 0.033*<br>(0.018)  | 0.031*<br>(0.017)   | 0.031*<br>(0.018)   | 0.031*<br>(0.018)   | 0.030<br>(0.019)    | 0.033*<br>(0.019)   | 0.030<br>(0.020)    | 0.031<br>(0.020)    |
| Natural Resources          | -0.001<br>(0.001)        | -0.000<br>(0.002)  | -0.000<br>(0.002)   | -0.000<br>(0.002)   | -0.000<br>(0.002)   | -0.001<br>(0.002)   | -0.001<br>(0.002)   | -0.001<br>(0.002)   | -0.000<br>(0.002)   |
| Corruption Control         |                          | 0.043<br>(0.027)   | -0.269*<br>(0.147)  | -0.267*<br>(0.151)  | -0.242<br>(0.154)   | -0.250<br>(0.153)   | -0.274*<br>(0.163)  | -0.261<br>(0.164)   | -0.243<br>(0.170)   |
| Constant                   | 0.640*<br>(0.335)        | 0.868**<br>(0.370) | 1.068***<br>(0.381) | 1.061***<br>(0.380) | 1.112***<br>(0.378) | 1.139***<br>(0.395) | 1.118***<br>(0.397) | 1.171***<br>(0.411) | 1.141***<br>(0.415) |
| Lags of Cor. Control       | No                       | No                 | Yes                 | Yes                 | Yes                 | Yes                 | Yes                 | Yes                 | Yes                 |
| Year dummies               | Yes                      | Yes                | Yes                 | Yes                 | Yes                 | Yes                 | Yes                 | Yes                 | Yes                 |
| <i>N</i>                   | 78                       | 78                 | 78                  | 78                  | 78                  | 78                  | 78                  | 78                  | 77                  |
| Adj. <i>R</i> <sup>2</sup> | 0.102                    | 0.114              | 0.152               | 0.140               | 0.136               | 0.137               | 0.131               | 0.126               | 0.081               |

\* $p < 0.1$ , \*\* $p < 0.05$ , \*\*\* $p < 0.01$ . Robust standard errors in parentheses.

# Persistence of Plurality

- Correlations of the veto players at the critical juncture and beyond





## Further Evidence of Critical Juncture

- Acemoglu et al. (2008, 2009) find evidence of critical junctures by entering country fixed effects in correlations between democracy and growth, which render such correlations statistically insignificant. We do the same by entering country fixed effects in a panel regression of institutional quality on contemporaneous veto players

|                            | Voice & Account      | Political Stability  | Govern Effect        | Regul Quality        | Rule of Law          | Corrupt Control      | GINI Index         |
|----------------------------|----------------------|----------------------|----------------------|----------------------|----------------------|----------------------|--------------------|
| Veto Players (current)     | 0.011<br>(0.011)     | -0.002<br>(0.014)    | 0.006<br>(0.009)     | 0.032***<br>(0.010)  | 0.018**<br>(0.009)   | 0.014<br>(0.012)     | 0.300*<br>(0.168)  |
| GDP per capita             | -0.280***<br>(0.080) | 0.615***<br>(0.132)  | 0.244***<br>(0.080)  | 0.404***<br>(0.088)  | 0.211***<br>(0.079)  | 0.250***<br>(0.092)  | 1.676<br>(3.232)   |
| Natural Resources          | -0.000<br>(0.002)    | -0.002<br>(0.003)    | -0.005**<br>(0.002)  | 0.003<br>(0.002)     | -0.004*<br>(0.002)   | -0.002<br>(0.002)    | 0.024<br>(0.066)   |
| Constant                   | 2.364***<br>(0.685)  | -5.415***<br>(1.120) | -2.601***<br>(0.688) | -3.681***<br>(0.745) | -2.546***<br>(0.672) | -2.893***<br>(0.783) | 15.639<br>(27.638) |
| Country dummies            | Yes                  | Yes                  | Yes                  | Yes                  | Yes                  | Yes                  | Yes                |
| Year dummies               | Yes                  | Yes                  | Yes                  | Yes                  | Yes                  | Yes                  | Yes                |
| <i>N</i>                   | 491                  | 489                  | 489                  | 489                  | 491                  | 491                  | 295                |
| Adj. <i>R</i> <sup>2</sup> | 0.965                | 0.864                | 0.942                | 0.956                | 0.955                | 0.926                | 0.842              |

\*  $p < 0.1$ , \*\*  $p < 0.05$ , \*\*\*  $p < 0.01$ . Robust standard errors in parentheses

# A Placebo Test

|                                    | Voice & Accountability | Political Stability | Government Effectiveness | Regulatory Quality   | Rule of Law          | Control of Corruption |
|------------------------------------|------------------------|---------------------|--------------------------|----------------------|----------------------|-----------------------|
| A. Transition Economies            |                        |                     |                          |                      |                      |                       |
| Veto Players                       | 0.304***<br>(0.027)    | 0.180***<br>(0.027) | 0.093***<br>(0.019)      | 0.131***<br>(0.025)  | 0.184***<br>(0.021)  | 0.138***<br>(0.019)   |
| Control Variables                  | Yes                    | Yes                 | Yes                      | Yes                  | Yes                  | Yes                   |
| B. Latin America and the Caribbean |                        |                     |                          |                      |                      |                       |
| Veto Players                       | -0.022*<br>(0.013)     | 0.031*<br>(0.018)   | -0.073***<br>(0.014)     | -0.122***<br>(0.013) | -0.087***<br>(0.016) | -0.072***<br>(0.018)  |
| Control Variables                  | Yes                    | Yes                 | Yes                      | Yes                  | Yes                  | Yes                   |

\*  $p < 0.1$ , \*\*  $p < 0.05$ , \*\*\*  $p < 0.01$ . Robust standard errors in parentheses

# Too Few or Too Many Veto Players: It Depends

- In Latin America, a large number of political players was viewed as an obstacle to successful reform (Stein et al., 2008).

|                                    | Voice & Accountability | Political Stability  | Government Effectiveness | Regulatory Quality   | Rule of Law          | Control of Corruption |
|------------------------------------|------------------------|----------------------|--------------------------|----------------------|----------------------|-----------------------|
| A. Transition Economies            |                        |                      |                          |                      |                      |                       |
| Veto Players                       | 0.799***<br>(0.105)    | 0.178*<br>(0.105)    | 0.087<br>(0.076)         | 0.538***<br>(0.103)  | 0.286***<br>(0.087)  | 0.123<br>(0.086)      |
| Veto Players (squared)             | -0.092***<br>(0.016)   | 0.000<br>(0.018)     | 0.001<br>(0.012)         | -0.075***<br>(0.016) | -0.019<br>(0.014)    | 0.003<br>(0.014)      |
| Control Variables                  | Yes                    | Yes                  | Yes                      | Yes                  | Yes                  | Yes                   |
| B. Latin America and the Caribbean |                        |                      |                          |                      |                      |                       |
| Veto Players                       | 0.131*<br>(0.068)      | 0.265**<br>(0.103)   | 0.197***<br>(0.058)      | 0.168***<br>(0.064)  | 0.095<br>(0.076)     | 0.407***<br>(0.078)   |
| Veto Players (squared)             | -0.019***<br>(0.007)   | -0.029***<br>(0.011) | -0.034***<br>(0.006)     | -0.036***<br>(0.008) | -0.023***<br>(0.008) | -0.060***<br>(0.009)  |
| Control Variables                  | Yes                    | Yes                  | Yes                      | Yes                  | Yes                  | Yes                   |

\*  $p < 0.1$ , \*\*  $p < 0.05$ , \*\*\*  $p < 0.01$ . Robust standard errors in parentheses

# A New Instrument?

- Institutional development past a critical juncture is shifted by contingent events which could be a source of exogenous variations (Acemoglu and Robinson, 2012).
- We have tested the number of veto players at the critical juncture as an instrument for institutions in the transition region.
- In a 2SLS estimation of the impact of institutions on economic inequality. Second stage fitted institutional variables are significant at the 1% level, whereas the F-statistics at the first stage is safely above the “rule of thumb” threshold of 10, indicating that the instrument is not weak.
- The proposed instrument was successfully used in (Natkhov and Polishchuk, 2018) to establish the impact of institutions in transition countries on the allocation of talent, measured by the choice of fields of study by university students.

# The End