The Balkans: Foreign Direct Investment and EU Accession

Transition and Development

Aristidis Bitzenis

THE BALKANS: FOREIGN DIRECT INVESTMENT AND EU ACCESSION

Transition and Development

Series Editor: Professor Ken Morita
Faculty of Economics, Hiroshima University, Japan

The Transition and Development series aims to provide high quality research books that examine transitional and developing societies in a broad sense – including countries that have made a decisive break with central planning as well as those in which governments are introducing elements of a market approach to promote development. Books examining countries moving in the opposite direction will also be included. Titles in the series will encompass a range of social science disciplines. As a whole the series will add up to a truly global academic endeavour to grapple with the questions transitional and developing economies pose.

Also in the series:

Transition and Development in China
Towards Shared Growth
Yun Chen
ISBN 978 0 7546 4834 5

Globalization and the Transformation of Foreign Economic Policy
Pawel Bozyk
ISBN 978 0 7546 4638 9

The Political Economy of Asian Transition from Communism
Sujian Guo
ISBN 978 7546 4735 5

The Periphery of the Euro
Monetary and Exchange Rate Policy in CIS Countries
Edited by Lúcio Vinhas de Souza and Philippe De Lombaerde
ISBN 978 0 7546 4517 7

Transition, Taxation and the State
Gerard Turley
ISBN 978 0 7546 4368 5

The Institutional Economics of Russia's Transformation
Edited by Anton N. Oleinik
ISBN 978 0 7546 4402 6

The Balkans: Foreign Direct Investment and EU Accession

ARISTIDIS BITZENIS
University of Macedonia, Greece

Routledge
Taylor & Francis Group
LONDON AND NEW YORK

First published 2009 by Ashgate Publishing

Published 2016 by Routledge
2 Park Square, Milton Park, Abingdon, Oxon OX14 4RN
711 Third Avenue, New York, NY 10017, USA

Routledge is an imprint of the Taylor & Francis Group, an informa business

British Library Cataloguing in Publication Data
Bitzenis, Aristidis.
The Balkans : foreign direct investment and EU accession.
-- (Transition and development)
1. European Union--Balkan Peninsula. 2. Balkan Peninsula--
Economic conditions--21st century. 3. Investments, European
--Balkan Peninsula. 4. Balkan Peninsula--Foreign economic
relations--European Union countries. 5. European Union
countries--Foreign economic relations--Balkan Peninsula.
6. Balkan Peninsula--Economic integration.
I. Title II. Series
337.1'42'09496-dc22

Library of Congress Cataloging-in-Publication Data
Bitzenis, Aristidis.
The Balkans : foreign direct investment and EU accession / by Aristidis Bitzenis.
p. cm. -- (Transition and development)
Includes bibliographical references and index.
ISBN 978-0-7546-4566-5 1. European Union--
Balkan Peninsula. 2. Investments, Foreign--Balkan Peninsula. 3. Balkan Peninsula--
Politics and government--1989- I. Title.

HC240.25.B28B58 2009
332.67'309496--dc22
2009007624

ISBN 9780754645665 (hbk)

Contents

This page has been left blank intentionally

List of Figures

This page has been left blank intentionally

List of Tables

Acknowledgements

Εγώ ειμί το φως του κόσμου.
Ο ακολουθών εμοί ου μη
περιπατήση εν τη σκοτία
αλλ' έξει το φως της ζωής.
'Ιησούς Χριστός'

This book would have never been completed without the valuable support of my wife. Also, the comments and suggestions from Dr. Marangos were of greatest importance for the finest preparation of this book. I would also like to thank some other people for the help they offered me during the preparation of this book such as Prof. Klaus Meyer, Prof. Gabor Hunya, Prof. Bruno Sergi, and Prof. Paul Hare. I am most grateful to all of them.

Special mention needs to be made to the splendid Ms. Christou Angela, who has spent hundred of hours and a great amount of her precious time checking on my written English, proofreading and editing all the chapters in this book. Her suggestions, comments and corrections were invaluable. Also, I would like to thank Kafteranis Xarisios, who not only supported my efforts, but also encouraged and helped me in every difficulty I faced during the preparation of this book.

I should not forget Dymphna Evans, Brendan George, Carolyn Court, Aimée Feenan and Adrian Shanks from Ashgate for their kindness and full support, as well as Ashgate Publishing for giving me the opportunity to publish this book.

Last but not least, I am especially grateful to my wife Anna – Xenia Lyssikatou, and to my sister Bitzeni Yiouli, for their continuous emotional and economic support and for helping me bring this task to its completion.

I dedicate this book with my deepest love and affection to my son Loukas, my daughter Eftychia and to my whole family.

This page has been left blank intentionally

List of Abbreviations

BGN	Bulgarian Lev
BOP	Balance of Payments
CARDS	Community Assistance for Reconstruction, Democratisation and Stabilization
CEE	Central and Eastern Europe
CEECs	Central and Eastern European Countries
CEFTA	Central European Free Trade Association
CIS	Commonwealth of Independent States
CMEA	Council for Mutual Economic Assistance
COMECON	Council for Mutual Economic Assistance
CPI	Consumer Price Index
DEM	Deutche Mark
EAD	Economic Analysis Division
EBRD	European Bank for Reconstruction and Development
EC	European Community
ECB	European Central Bank
ECE	Economic Commission for Europe
ECSC	European Coal and Steel Community
ECU	European Currency Unit
EDP	Excessive Deficit Procedure
EEC	European Economic Community
EFTA	European Free Trade Association
EIB	European Investment Bank
EIU	Economist Intelligence Unit
EMS	European Monetary System
EMU	Economic and Monetary Union
EU	European Union
FDI or DFI	Foreign Direct Investment
FRY	Federal Republic of Yugoslavia
FYROM	Former Yugoslav Republic of Macedonia
GATT	General Agreement on Tariffs and Trade
GDP	Gross Domestic Product
GDR	German Democratic Republic
GNP	Gross National Product
IBI	International Banking Institute
IBRD	International Bank for Reconstruction and Development
IFC	International Finance Corporation

IIB	International Investment Bank
IMF	International Monetary Fund
IPO	Initial Public Offering
M&As	Mergers and Acquisitions
MEBO	Management and Employee Buyouts
MNC	Multinational Corporation
MNE	Multinational Enterprise
NAFTA	North American Free Trade Agreement
NATO	North Atlantic Treaty Organisation
OECD	Organisation for Economic Co-operation and Development
PETs	Planned Economies in Transition
PHARE	Poland/Hungary: Assistance for Reconstruction of the Economy [Pologne/Hongrie: Assistance a la restructuration economique]
PPP	Purchasing Power Parity
SAAs	Stabilization and Association Agreements
SAP	Stabilization and Association Process
SEA	Single European Act
SEEs	South East European Economies
SEECs	South East European countries
SGP	Stability and Growth Pact
SMEs	Small & Medium Enterprises
SOEs	State-Owned Enterprises
UK	United Kingdom
UN	United Nations
UNCTAD	United Nations on Trade and Development
UNECE	United Nations Economic Commission for Europe
US	United States
USA	United States of America
USD	United States Dollar
USSR	Union of Soviet Socialist Republics
VAT	Value Added Tax
WB	World Bank
WIIW	The Vienna Institute for International Economic Studies [Wiener Institut fur Internationale Wirtschaftsvergleiche]
WTO	World Trade Organisation

Introduction

The fall of communism and the subsequent developments have put a renewed spotlight on the potential of the Balkan economies. Bulgaria, Albania, Serbia & Montenegro, Romania and the Former Yugoslav Republic of Macedonia are countries that have attracted rather low levels of investment, with poor political leadership in the majority of these countries delaying the much needed and anticipated reforms. However, there are now signs of improvement and this timely book aims to fill a significant gap in the literature. This book demonstrates and supports the idea that these countries must engage as fully as possible with the world economy via EU accession and explores the implications of the specific characteristics of these countries which have made the transition process more difficult.

It is well known that FDI plays a potential role in encouraging and supporting a successful transition. FDI in transition economies appears to be an effective tool for several reasons such as transfer of knowledge, increased productivity, upgrading of managerial and labour force skills, improving the state balance, balancing deficits, accelerating privatization of state-owned enterprises and quickly restructuring of them.

Over the last 30 years economists and investors have dealt with countries mainly from Latin America, and Asia such as Argentina, Mexico, Chile, Korea, Malaysia, Hong Kong, Taiwan, Singapore, the Philippines, China, and a few others like the UK, the USA, Spain, Ireland, Portugal and Greece for their inward investment activities. After 1989 and the collapse of communism, Central and Eastern European countries along with the Baltic States and the CIS have been an ‘attractive area’ for business. The interest is always with countries that open their borders; their economies offer great opportunities, incentives and challenges for inward FDI. In the last two decades (1990s–2000s), the interest of foreign investors has focused mainly on the Central and Eastern European Economies and secondly on the South East European Economies.

Therefore, the fall of communism in Central and Eastern European countries raised the interest of economists, entrepreneurs and multinational enterprises (MNEs) in analysing and exploiting the potentials of Central and East European markets and especially the Balkan market. Bulgaria, Albania, Serbia & Montenegro, Romania and FYROM are among the countries that have not been studied yet. In reality, what makes this book interesting is the fact that the Balkans is a relatively neglected region in studies of transition, as well as being one that presents some unusually difficult problems. The economic environment in the region has not proved especially attractive to business, and the poor political leadership in most of these countries has delayed much needed reforms for way too long. However, there are signs of improvement in most countries, and that might make this book quite timely. These countries must simply engage as fully as possible with the world economy (globalization, EU integration), otherwise there is no way they will ever escape their present poverty.

At the same time, the Balkan region displays the following specific characteristics: geographical distance from the Western markets, cultural distance from the West, strong dependence on the former Soviet Union and its subsequent dissolution (Russia and CIS), strong dependence on the CMEA trade organization and its collapse, adverse initial conditions, and political instability and/or inability of the respective governments that hinders the success of the whole transition process.

This book will therefore prove suitable for gaining a greater understanding of the South East Economies as special case studies as well as understanding their prospects to enter to the EU.

The book can be used in modules relating to transition economies, those discussing international business in the Balkan region, and the European business environment as it relates to the South Eastern Europe region. The book includes more than 20 case studies (uniquely from the Balkan region) and topics such as FDI, privatization (entry modes), and prospects for an EU entrance have been presented and analysed. The book is designed to further understanding of the reasons behind the low accumulation of FDI flows in the Balkan region and provides detailed coverage of the difficulties of the Balkan's business environment (mentality, entrepreneurship, banking reform, legal reform, etc.). The book will also assist in comprehending the macro environment of the SEE region.

Chapter 1
Transition Economies vs. Market Economies: Increased FDI Inflows in Transition Economies

1.1 Introduction: Planned vs. Market Economies; The Transition from a Planned to a Market Economy

The breakdown of centralized socialism in the Union of Soviet Socialist Republics (USSR), Central and Eastern Europe and Asia resulted in the adoption of the market process as a means of organizing the economy. The movement from a centralized socialist economy to an economy based on market relations has been termed *transition*, and thus the economies that have adopted this process are named *transitional economies*. In particular, the transition process was associated with an explicit end-state. The transition economies associated this end-state with the establishment of a capitalist economic system. Hence, the transition involved, in essence, the introduction of private ownership as a result of privatization and/or restructuring of state-owned enterprises, and the establishment of market equilibrium as a result of abolishing centrally administered commands. The transition went further to involve liberalization of economic activity, an institutional reform, a change in economic behaviour as a result of economic actors adjusting their behaviour in line with self-interest, and the rules of the exchange market. It also involved the reduction of the state's role as a legislator and facilitator of economic activity.

The term *transition* has been criticized as being inadequate, as it does not capture all the complications involved during the process. The term implies a linear movement from A (centralized socialism and disequilibrium) to B (capitalism and equilibrium). Specifically, as the term *transition* implies an end-state, the achievement of the end-state completes the whole process. It can be argued that the process is already completed as transition economies have adopted a capitalist economic system and most countries of the Central and Eastern Europe have become members of the European Union (EU). Hence, the term *transitional economy* is obsolete.

On the other hand, it can be argued that the 'transition' process is ongoing and equilibrium can never be achieved by using terms such as transformational economies or simply developing economies. In addition, since capitalism comes in many forms, the question arises as to what type of capitalism should be the goal. This further complicates the process (Sergi, 2003; Marangos, 2004a). Even the goal of achieving a capitalist economic system was questioned by some commentators who offered alternatives such as market socialism as the most appropriate economic system, pointing out China and Vietnam as examples (Marangos, 2006a; 2006b).

The economic programme of transition involved the following four factors, but in no particular order. The first was macroeconomic stabilization, in order mainly to reduce inflation and to decrease the debt burden. The second was liberalization of economic activity such as prices, trade, currency convertibility, etc. The third was the reduction of the size of public sector by privatizing and restructuring state-owned enterprises. The last factor required introduction of new laws and regulations. For example, property rights, corporate law, accounting practices, tax regulation, etc. Hence, the decision to move to a market-based economy required a total transformation of the economy as a whole (see also Zloch-Christy, 1994). Meanwhile, as citizens had been protected for so long by the socialist state, they were ill prepared to face the economic adversity and uncertainty that came about as the result of the free market process.

Although all countries in transition had more or less the same final goal, the results of their efforts diverged. This was due to the diverse and/or adverse internal as well as external conditions each country initially faced and to the different strategies, policies, and paths they undertook to ensure smooth and successful transitions (Bitzenis, 2006b; 2007).

A market economy, or a free economy, or a free enterprise economy is an economic system which allocates scarce resources, based on the interaction of market forces of supply and demand. It is an economy that operates by voluntary exchange and it is not planned or controlled by a central authority. It is the conceptual opposite of a command, or central, or planned, or government controlled economy, where all goods and services are produced, priced and distributed under government control. Nowadays, a market economy is associated with a capitalistic economy (see Tables 1.1 and 1.2).

The market is a process in which individuals interact with one another in pursuit of their separate economic objectives. The basic principle under which the market functions is: if you own something which you are entitled to and you wish to exchange it for something else which belongs to someone else and you execute the exchange without violence, theft or deception then you become entitled to what the other person was previously entitled to, and vice-versa. Both parties in an economic transaction in the market benefit from it, provided the transaction is bilaterally voluntary and the parties well-informed. Otherwise, the transaction will not take place. In this way, through the market process, everyone is able to escape coercion at the hands of any buyer or seller by turning to another buyer or seller.

Table 1.1 Planned economies vs. market economies

Planned (centralized or central planned) economy characteristics	Characteristics of an economy during its transition to a market economy
State owned enterprises (SOEs), no private sector	Bribery, lack of transparency, bureaucracy, corruption
No effective allocation of resources (natural + human + capital)	Governmental inability/unwillingness for adequate reforms (political cost)
No unemployment, no or limited inflation	Black economy
Limited quantity, variety and quality of products	Nomenklatura, criminality, mafia
Central plan (the government set the prices, salaries)	Unclear property rights
Central plan (what to produce, in which quantity and quality → secured clients – secured trade partners)	Unemployment and increased poverty
Subsidies → on products for the local/foreign market → on enterprises (bad loans), soft budget constraints	Legacy of communist regime as an adverse initial condition
Manipulation of output, pricing and employment	Economic crises and output decline
Free education – health system (high levels)	Small savings, low GDP per capita
Production of certain products	High inflation, exchange rate devaluations, monetary overhang
Trade with Eastern countries (CMEA – COMECON)	Lack of competitiveness
Exchange of products in special (low) prices	Lack of sound financial institutions, political instability
Over-inflated macroeconomic data	Adverse economic initial conditions
Lack of commercial legislation and market oriented taxation systems, one-tier banking system, no stock exchange	Reductions of trade quotas and tariffs, Elimination of subsidies
State: the guiding force of the market	Unstable legal framework
Geographical and cultural distance from the west, isolation of the country	Lack of experience (managerial skills, reformers, governance, mentality, entrepreneurship)

There is currently no country where all markets within its borders are absolutely free. Rather, a free market economy is one with limited government intervention (otherwise known as laissez-faire). Market based economies require appropriate laws and institutions which include defined property rights that are respected and enforced, as well as procedures to guarantee the execution of contracts. Many states which are said to have a capitalist system do not have the level of market freedom that some would prefer. Even the United States of America (USA), a worldwide representative of capitalism, has placed restrictions upon the freedom of individuals in the economy.

Markets are also characterized by market failure, i.e. an allocation of resources which is not efficient. The market is able neither to produce public goods (defence, law and order, etc.) nor to 'cover' the social cost or benefits of externalities (environmental pollution, education, etc.). Thus, it creates monopolies and oligopolies. Then, the state takes on the responsibility of producing public goods and subsidising positive externalities funded through taxation, while it restricts negative externalities, monopolies and oligopolies.

Table 1.2 Market economy characteristics

Market economy characteristics
Market forces (supply and demand)
State: A role of the legislator and facilitator of the economic activities
Competitive environment
Free prices, trade, interest rates, exchange rates
Private sector
Hard budget constraints, new corporate governance
New laws and institutions
Taxes on private companies (corporate and personal income taxes and VAT)
Black economy, under-reported data
Unemployment
Effective governance, competition
Advanced two-tier banking system (central bank + commercial banks)
Stock market exchange
Financial intermediaries (insurance companies, pension funds etc.)
Limited or even absence of subsidies, trade quotas and tariffs
Reforms at all levels (tax, financial, legal etc.)
Privatization and restructuring, macroeconomic stabilization, liberalization, institutional or structural reform (new laws, new institutions, new mentality)
Open country, FDI flows, open trade, open economy

Finally, Bitzenis and Marangos (2007) argued that the terms 'integration and transition' are more appropriate than just 'transition' of what essentially took place in the Central and east European region and generally in transition economies. They stated that in fact, it is an integration-assisted transition. These terms, integration, assistance and transition, are not substitutes but complements in demonstrating the transition process in the CEE economies. Integration means that a country becomes a part of the globalized world. Integration is the goal of globalization, and integration is achieved by inviting multinationals and entering the EU. Integration is further enhanced by membership of the EMU and the adoption of the single currency. Both the European Union (EU) and the Economic and Monetary Union (EMU) are the best examples of integration and globalization, as membership involves the abolishment of barriers to entry, liberalization policies, and the adoption of the 35 chapters of the acquis (6th EU enlargement policy). All of them determine the legal, political and economic convergence among member countries, and create the fundamentals for stability for the members and a sound business environment to attract FDI and trade flows (Sergi, 2004).

1.2 The Transition Reform Paths to Democracy and/or Market Economy

A successful transition process may be treated as a tool for the economic development of a country. However,

> … (transition) is not only an intermediate goal contributing to economic development. It may also be regarded as an ultimate objective in itself. The market economy, in contrast to central planning, gives, in principle, the individual the right to basic choices over aspects of his or her life: occupation and place of work, where to live, what to consume, what risks to take or avoid, and so on. (EBRD, 1994, 3)

An important factor in studying the transition process is the way in which the initial dismissal of the communist regime occurred. Regimes 'fall' in many different ways. For example,

> the transition of power was smooth and peaceful in Poland and Hungary, which had a tradition of dialogue and negotiations; it was peaceful but painful in East Germany, Czechoslovakia and Bulgaria; and it was painful and violent in Romania which was on the verge of civil war by Christmas 1989. (Berglund et al., 1994, 241)

There is a distinct difference between transition from a planned to a market economy and transition from a communist regime to democracy. In other words, after the Central and East European countries faced the collapse of the communist regime and moved towards democracy, they adopted monetary, income, fiscal stabilization policies and institutional reforms in order to establish all the elements of a functioning market economy in their economic environment. Thus, it is important to present and analyse the transition reform paths and the need to have a 'strict government', which would not sacrifice the successful implementation of its reform policy for the sake of popularity.

Meyer (1998, 209) characterizes the transition from communism to democracy as a: '… decisive precondition for the establishing of new democratic institutions and the restructuring of economic institutions moving away from the planned towards the market economy'. The political transition comprised political liberalization, free elections and general democratization and aimed at replacing the single-party political regime and establishing liberal democracy and a civil society (Sokol, 2001). The transition from communism to democracy in most of the countries was supported by the previous development of a civil society whose characteristics reflected the revolutions themselves: it was anticommunist, anti-ideological, and anti-political (Tismaneanu, 2001). However, certain barriers might arise in the development of the new political system such as the risk the old elite faced to transfer its political power into new forms in the new system, along with the lack of democratic traditions and experience (Mygind, 2000).

Despite the fact that transition countries adopted rapidly multiparty democracy regimes, some reversals of political reforms and many tensions, controlled by the previous regimes arose (EBRD, 1995). There is also a common consensus that the implication of a market-oriented transition might be deemed as a political development because of the robust relationship existing between the political and economic reforms (EBRD, 1995).

We agree with Kolman et al. (2003, 87) who found that in spite of the small geographical distance, there are cultural differences between countries from the Central and East European region and the Western European countries. It was also their belief that, from a managerial perspective, it would be dangerous to treat the Central East European countries as a homogeneous group or cluster.

In an earlier article, Ronen and Shenkar (1985) had attempted to create clusters among different countries and to group them together basically according to their geographical area, their language and religion, their beliefs that arose from certain norms and values and their technological development. Ronen and Shenkar had also argued that geography casually precedes the other variables such as language and religion and that the geographical grouping may contain countries from all five continents as the spread of culture may be attributed to colonization and immigration. They included in the proposed clusters only one country from the Central and East European region, ex-Yugoslavia.

By applying a political economy approach to the transition process, Marangos (2004a) develops alternative models of transition. The alternative models of transition can be distinguished on the basis of what the author defines as the primary elements of each transition model: (1) Economic Analysis; (2) What is a Good Society?; (3) Speed; (4) Political Structure; (5) Ideological Structure; and (6) Initial Conditions. On the basis of the primary elements, Marangos (2004a) distinguished five transition models: The Shock Therapy model of transition; the Neoclassical Gradualist model of transition; the Post-Keynesian model of transition; the Pluralistic Market Socialist model of transition; and the Non-Pluralistic Market Socialist transition model (Chinese model).

In Kolman et al. (2003), Ronen and Shenkar (1985) and Marangos (2004a), the grouping of the countries into clusters is profound and is based on cultural, geographical and transition elements in order to provide a framework for theoreticians and practitioners to study the interaction between companies and a host country (destination country of an FDI project) and to understand the values and attitudes of employees in such a country. To this end, the nine reform models presented in this paper will be our contribution to the categorization of transition countries into clusters, based on their political and transition reform features.

Table 1.3 Nine reform models

Reform models			Countries/Year		
Diplomacy	East Germany (1989)	Bosnia & Herzegovina (1995)	Russia (1991)	Serbia & Montenegro (1995)	Croatia (1995)
Quiet/peaceful/ colour or flower revolutions	Ukraine (Orange Revolution) (2004); Georgia (Rose Revolution) (2003); Kyrgyzstan (Tulip Revolution) (2005)	Czech Republic (Velvet Revolution) (1989)	Slovakia (Velvet Revolution) (1989)	FYROM (1991); Slovenia (1991); Serbia & Montenegro (Peaceful Revolution) (2000)	Estonia (Bloodless – Singing Revolution) (1991)
Disguised	Hungary (1994)	Bulgaria (1990)	FYROM (1992)	Russia (1991); Lithuania (1992)	Albania (2002); Serbia & Montenegro (1990)
Compromised	Bulgaria (1997); Albania (2002)	Hungary (1990)	China (1989)	Poland (1995-)	Estonia (1992); Latvia (2002)
Violent	Romania (1989); Albania (1997)	China (1989)	Serbia & Montenegro (2003)	Lithuania (1991); Russia (1993)	Latvia (1991)
Rebellion	China (1987)	Poland (without revolution) (1989)		Albania (1991)	Bulgaria (1990, 1997)
Belligerent	Serbia & Montenegro (1992)	Bosnia & Herzegovina (1992)		Croatia (1992)	
Transparent	China (1978)	Vietnam (1979)			
Mixed	Bosnia & Herzegovina; FYROM; Albania	Croatia; Serbia & Montenegro	Lithuania; Latvia; Estonia; Russia	China	Poland; Hungary; Bulgaria

Source: Bitzenis, 2007.

Studying the transition models to a market economy and the economic development of transition countries, one recognizes similar and different characteristics among transition procedures of the various countries especially at the beginning of the transition period (1990s), during the collapse of the communist regime. Thus, our introduction of nine general transition reform paths with regard to the way that the reform from communism to democracy and to a market economy was achieved: (1) the Diplomacy Reform; (2) the Quiet Reform; (3) the Disguised Reform; (4) the Compromised Reform; (5) the Violent Reform; (6) the Rebellion Reform; (7) the Belligerent Reform; (8) the Transparent Reform; and finally (9) the Mixed Reform (see Table 1.3).

The Diplomacy Reform model: In the Diplomacy Reform model transition is achieved through political intervention of an external power. This transition path is recognizable in the German Democratic Republic (GDR) where the collapse of the old regime and the subsequent reunion with West Germany was demanded by the East Germans. It is also recognizable in the countries that have been created from the dissolution of the Soviet Union and Yugoslavia (e.g. Russia, FYROM, Croatia, Bosnia & Herzegovina, Estonia, etc.). However, in most cases a Diplomacy Reform was an outcome of a Belligerent Reform (see below).

The Quiet or Peaceful Reform (colour or flower revolutions) model: In the Quiet or Peaceful Reform model the old regime is faced with a peaceful yet determined opposition and through a proclamation of national elections eventually hands over power to the democratic opposition without any resistance. The dissolution of Czechoslovakia (the Czech and the Slovak Republic) and its transition to democracy is such an example. This specific reform is also known as the velvet revolution. In November/December 1989, a peaceful student demonstration in Bratislava and in Prague along with other popular demonstrations and strikes led the communist party to announce at the end of that year the end of its monopoly on political power. This resulted in the first democratic elections since 1946 for Czechoslovakia.

The Quiet Reform with the simultaneous establishment of independence of the country in a peaceful way can also be called the Quiet/Diplomacy Reform. It took place in Slovenia, FYROM, Ukraine, Georgia, Kyrgyzstan, Serbia & Montenegro and Estonia. Both Slovenia and FYROM broke away from Yugoslavia (FRY) in a peaceful manner.

Under the same kind of reform we have the so-called colour revolutions, the rose, tulip and orange revolution. The first of such kind, the Rose Revolution started in Georgia in November 2003. In the parliamentary elections, Saakashvilli, the opposition leader who was supported by independent exit polls, claimed that he had won the elections. However, this result was unacceptable to the leading party and led to a non-violent and anti-governmental demonstration in Tbilisi and other cities of Georgia. The demonstrations of the supporters of Saakashvilli with roses in their hands along with the elite military units' refusal to support the government, forced President Shevardnadze to resign.

In the same direction, in the Ukrainian presidential election at the end of 2004, Yanukovych (President from the end of 2002 until the end of 2004) was declared the winner. However, this outcome was not accepted by the majority since the exit polls proclaimed Yushchenko (Prime Minister from the end of 1999 until the end of April 2001) the winner. Thus, mass demonstrations in Kiev and many other Ukrainian cities took place at the end of 2004. Over half a million protesters, wearing orange ribbons demonstrated and supported Yushchenko (orange was the official colour of the movement and the predominant colour in Yushchenko's election campaign). They peacefully asked for new elections in which Yushchenko finally won in the third round (Orange Revolution). This revolution has sometimes also been called the Chestnut Revolution due to the abundance of chestnut trees in Kiev, the capital city of Ukraine and the centre of this revolution.

In March 2005, there were demonstrations in Kyrgyzstan against President Akayev and his government who were increasingly corrupt and authoritarian. These demonstrations were known as the Tulip Revolution and ended with Akayev's resignation. Another peaceful revolution of the same kind took place in Serbia, in October 2000 with mass demonstrations in Belgrade when Kostunica and his supporters doubted the results of the presidential elections and the demonstrations replaced Milošević's autocratic regime.

Last but not least, another similar revolution took place in Estonia. It was in 1991 when mass demonstrations blocked the Soviet tanks and proclaimed the restoration of the independence of Estonia with the Singing Revolution which lasted four years (1988–1991). The Singing Revolution started in 1988 with various protests, acts of defiance, yet without violence. It ended with demonstrations with thousands of Estonians singing forbidden national songs and finally, winning Estonia's independence.

The Disguised Reform model: In the Disguised Reform model the old regime anticipates the inevitable changes and in an attempt to stay in power, 'disguises' itself as a democratic socialist party. For example, Bulgaria's regime was transformed by a 'Disguised Reform'. The ruling elite in Bulgaria lacked pressure from a strong opposition and moved to the 'political opening' only when the Soviet Union politically intervened. Then the communist party renamed itself the Socialist party, ousted its president, scheduled and won the first elections.

The Compromised Reform model: In the Compromised Reform model under no significant pressures, the communist regime gives in to the demand for change and democratization by joining or co-operating with the democratic party. Together, they proceed to the first free elections (after 50 years of communism) and make the transition reforms. The Compromised Reform can also take place when the communist regime 'allows' the democratic opposition to hold and win the elections in order to proceed to the necessary transition reforms. The Compromised Reform can also be seen as the result of a conscious political decision for a gradual reform to a market economy. The starting point of such reforms goes back to the 1980s or even to the 1970s, during the communist era (e.g. Hungary, China, and Vietnam).

In 1989, the communist regime gave up power voluntarily, and Hungary became a parliamentary democratic Republic. The first free parliamentary elections were held in May 1990 and were won by the populist, centre–right and liberal parties. The Magyar Demokrata Fórum (the Hungarian Democratic Forum, MDF – conservative/Christian democrat party) became the dominant party and won 43% of the votes. Its leader, József Antall, was elected prime minister of the centre-right coalition government. This was a coalition with the Independent Smallholders' Party (FKGP) and the Christian Democratic People's Party (KDNP). They commanded a 60% majority in the Hungarian parliament (Compromised Reform).

In October 1989, the communist party was reformed into the social-democratic Magyar Szocialista Párty (Hungarian Socialist Party, MSzP). The poor performance of the Hungarian Socialist Party in the first free elections (won 24% of the votes) raised the political need for compromise solutions.

In May 1994, the socialists made a comeback by winning a plurality of votes and 54% of the seats in Parliament after an election campaign which had focused largely on economic issues and the substantial decline in living standards since 1990 (the Disguised Reform). However, dissatisfaction with the pace of economic recovery, the rising crime rate, and government corruption convinced people to vote centre-right parties in the Hungarian national elections of May 1998.

The Violent Reform to Democracy model: In the Violent Reform to Democracy model the old regime is overthrown by a violent uprising (violent uprising or violent the way that it was countered – e.g. Romania). Reforms and changes could be proposed by the opposition, or by the reform communists who came into power. It was some days before Christmas in 1989 in Romania, when the Dictator Ceausescu was swept from power in a popular uprising. The Romanian people had begun to rebel in Timisoara on 17 December 1989, when demonstrators stormed the Communist Party headquarters. On 23 December 1989, Romania's 'Revolution' or Romanian coup d'état came to an end with the summary execution of Ceausescu and his wife Elena at the hands of a secret tribunal. The square where Ceausescu faltered was officially renamed Piatza Revolutiei (Revolution Square).

The Rebellion Reform model: The Rebellion Reform model is the result of pressure put upon the communist regime during the communist era (e.g. the worker's union pressures in Poland). It appeared with strikes, demonstrations, social anarchy, and demands for liberty and workers' rights, especially in periods of economic crises and political uncertainty and where corrupted governments existed.

More specific, in Poland in 1978, Lech Walesa along with other activists began to organize free non-communist trade unions. In August 1980, Walesa led the Gdansk shipyard strike which gave rise to a wave of strikes over most of the country with Walesa seen as the leader. The primary demands were for workers' rights.

The authorities were forced to capitulate and to negotiate with Walesa the Gdansk Agreement of 31 August 1980, giving the workers the right to strike and to organize their own independent union. When the Polish communists made this concession, which had been without precedent in the history of the communist world since 1917, the new union was named Solidarnose [Solidarity].

The country's brief enjoyment of relative freedom ended in December 1981, when General Jaruzelski, mainly in fear of a Soviet armed intervention, imposed martial law, suspended Solidarity, arrested many of its leaders, and interned Walesa in a country house in a remote spot in Poland. In November 1982, Walesa was released and reinstated at the Gdansk shipyards. Although kept under surveillance, he managed to maintain contact with Solidarity leaders in the underground. Even though martial law was lifted in July 1983, many of the restrictions in the civil code were kept in practice.

In October 1983, the announcement of Walesa's Nobel prize raised the spirits of the underground movement, but the award was attacked by the government press. It was in 1988 when there was another occupation strike in the Lenin Shipyard in Gdansk, which Walesa joined again. A few months later, in 1989, the Polish communists entered into negotiations with Solidarity at the first Round Table. The Jaruzelski regime became even more unpopular as economic conditions worsened, and it was finally forced to negotiate with Walesa and his Solidarity colleagues. In April 1990, at Solidarity's second national congress, Walesa was elected chairman with 77.5% of the votes. Walesa and his colleagues secured semi-free elections in which Solidarity proceeded to triumph. In August 1990, Poland got its first non-communist prime minister in a non-communist government in more than 50 years. In a general ballot in December, Walesa was elected President of the Republic of Poland. He served until defeated in the election of November 1995 (the Rebellion Reform – a genuine workers' revolution).

The next phase in Walesa's political career is more controversial. Angered by the fact that his former intellectual advisers were running the country in cooperation with the former communists, he declared 'war' on the heads of Solidarity. Thus, it can be argued that in that time period in Poland there was a co-operation of the two oppositions and thus, Poland also followed a Compromised Reform (therefore a Mixed Reform).

The Belligerent Transition Reform Path model (e.g. Serbia & Montenegro, Bosnia & Herzegovina and Croatia): The old regime of Yugoslavia, being the most liberal compared to those of other ex-communist countries during the pre-transition period, remained in power and promised transition reforms. However, it failed to change the situation. Only after 1999, after many years of the totalitarian dictatorship of Milošević, when the country had suffered immensely from the NATO war and its embargo, a democratic regime finally was established in the country, starting from scratch the reforms and the actual transition to a market economy.

In June 1991, Slovenia and Croatia seceded from the federation, followed by FYROM (September 1991) and Bosnia & Herzegovina (March 1992) (the Quiet

Reform was followed by all these countries but only at the early transition years [except for Slovenia]). However, the presence of large Serb minorities in Croatia (580,000) and Bosnia (1.6 million) led to wars (Serbia, Bosnia and Croatia).

Hundreds of people died and nearly 100,000 fled from their homes (the Belligerent Reform). More specifically, on 1 March 1992, 64% of the Bosnian electorate voted in response to a simple question: 'Are you in favor of a sovereign and independent Bosnia-Herzegovina, a state of equal citizens and nations of Muslims, Serbs, Croats and others who live in it?' The overwhelming answer to this question was 'Yes'. In April 1992, an alliance was established between the Croatians and the Bosnians in order to combine their strengths against the Serbian forces. On 1 March 1994, an agreement was reached between Croatian and Bosnian ministers to create a Muslim (Bosniak)-Croat Federation. Presidents Izetbegovic and Tudjman signed this agreement in Washington DC, USA on 18 March 1994 and it was quickly ratified by the Bosnian parliament.

On 21 November 1995, the Dayton Peace Accord was initiated in Dayton, Ohio by the presidents of Bosnia, Croatia, and Serbia, calling for the division of the republic into two 'entities' (the Diplomacy Reform). Thus, as both the quiet and belligerent together with the diplomacy reform models appeared in the cases of Bosnia & Herzegovina and Croatia, it can be argued that a Mixed Reform path again is the appropriate one for both countries.

The Transparent Transition Reform path model relates to the move towards a market economy without the abolishment of communism (e.g. China, Vietnam). In this case, the previous communist regime remains in power while monitoring the changes taking place in the Eastern bloc and in the former communist countries. At the same time, it proceeds to transition reforms, liberalizing the economy, opening the borders and 'asking' for FDI inflows in order to become a market economy (e.g. China, Vietnam). As mentioned in Marangos (2004a), the Communist Party is still in power in China and Vietnam – unlike the situation in the other transition countries – and the development of a socialist society is still the official state goal.

A quarter of a century ago, the Communist leadership under Deng Xiaoping initiated a marketization process in China's centrally administered socialist economic system. The start of these reforms is usually identified with the Communist Party Plenum in December 1978. Thus, the period of reform has been at least double of that of other transition countries.

China's reforms differed markedly from those reforms implemented in the transition economies of Eastern Europe and the former Soviet Union. The reforms in China consisted of small step-by-step changes. Neither was the ultimate goal announced, nor was any timetable for the transition mentioned. Some of the changes were initiated spontaneously 'at ground level', and only after they were successful were they ratified by the government and implemented as official policy. The reforms proceeded by trial and error, with frequent mid-course corrections and reversals of policy. Marangos (2004a) concluded that the Chinese economic growth rate is among the highest on record and fairly stable. It has been achieved without sacrificing external equilibrium, and inflation has been kept under control. However, China also followed the Compromised Reform model when the communist regime adopted transition reforms just by following the pressures for changes that existed in other transition economies.

Worthy of mention is the fact that the Transparent Reform in China was backed-up by a failed rebellion (1987) and the Violent Reform (1989). The latter took place with various demonstrations in 1989, and was supported by thousand of students and workers in many major cities. Both students and workers peacefully demanded democratic reforms, asking for equality and protested against government corruption. The Chinese government answered with forceful military action with troops and tanks in Tiananmen Square. Hundreds of civilian deaths resulted from this unsuccessful violent reform.

Marangos (2004a) mentioned that Vietnam's transition was greatly influenced by China's successful experience. The beginning of market reforms dates back to the Sixth plenum of the Fourth Party Congress in September 1979. After a long period of unsuccessful partial and gradual reforms in 1989, the course of transition in Vietnam broke away from the Chinese model and a shock therapy approach was adopted. The pace of reform in Vietnam from 1989 to 1991 was anything but gradual, and the stabilization programme adopted in 1989 was certainly as ambitious as the shock therapy approach in other transition economies.

The Mixed Reform model is evidenced in FYROM, where the transition to democracy was achieved through a combination of the following: the Quiet Reform and the Disguised Reform. The Federal Republic of Yugoslavia (FRY) was on the edge of disintegration. Many political, ethnic and economic problems that had been successfully hidden throughout the communist years had risen to the surface, sparking civil wars with Croatia and Bosnia & Herzegovina and the break down of the Federation.

FYROM was the only country together with Slovenia, which had managed to achieve its independence peacefully in 1991 (the Quiet Reform**)**. After the break-up in January 1990 when the last Congress of the League of Yugoslav Communists was held and the Slovenians and Croatians had left, many changes occurred, including the change of the political system. In November 1990, the first multi-party elections were held in FYROM. In January 1991, Kiro Gligorov was elected as the first president of the country and after a while the first government, 'the experts government', was formed. However, by 1992 three governments had succeeded one another and finally the SDSM (Social Democratic Alliance of Macedonia that originates from the former Communist Party) got the right to form a government by coalition with the PDP (PDP – Albanians Party of Prosperity and Integration). Actually, the SDSM is the successor to the League of Communists in FYROM which renamed itself after the 10th Congress in 1991 (the Disguised Reform).

By analysing the above information we can conclude that the country has followed the Quiet Reform model, but as a result of the SDSM's history in the government it can be said that a Disguised Reform also took place (the communists were again heads of the state). Thus, a Mixed Reform path is appropriate for the case of FYROM.

The Mixed Reform path was taken by the Baltic countries. Estonia held free elections on 18 March 1990. The Popular Front coalition, composed of left and centrist parties and led by former Central Planning Committee official Edgar Savisaar, held a parliamentary majority. Parliament chose nationalist Lennart Meri of the Isamaaliit Party (Fatherland Union) as the president of Estonia in October 1992. Lennart Meri appointed Mart Laar, a free-market supporter, as prime minister, who referred to himself as 'Thatcher's grandson' (the Compromised Reform for the case of Estonia).

Through a strict, non-confrontational policy in pursuing independence, Estonia managed to avoid the violence which Latvia and Lithuania incurred in the bloody January 1991 crackdowns and in the border-customs post guard murders that summer (Violent Reform for the case of Latvia and Lithuania). The central government of the Soviet Union granted independence to Estonia on 20 August 1991 (Brown, 1993; Hoag et al., 1999) (the Quiet Reform for the case of Estonia).

On 6 September 1991, the central government of the Soviet Union granted independence to Lithuania, although the USSR had used economic, political, and military pressure to keep it within the union. Lithuania's independence was achieved through mass demonstrations, violence and bloodshed where a number of Lithuanian protesters died at the hands of Russian soldiers in Vilnius, the capital city of Lithuania at the beginning of 1991 (the Violent Reform).

In reality in 1993, Lithuania became the first of the three Baltic countries to be free of Russian military presence. The last unit of Russian troops left the country on 31 August that year. As in several other former Soviet republics, former Communists in Lithuania staged a political comeback in the post-USSR period (the Disguised Reform for the case of Lithuania).

Although the anti-Soviet, pro-independence coalition (the Lithuanian Movement for Reconstruction) won the country's first open parliamentary elections in February 1990 and successfully led the struggle for Lithuanian independence, the coalition could not maintain political leadership. Its popularity dropped as a result of (a) political infighting in the coalition; (b) the severe economic crisis caused by the disruption of trade ties with the former Soviet Republics; and (c) the deterioration of international relations with neighbouring countries. Consequently, the Democratic Labor Party (DLP; the former Communist Party of Lithuania) won a majority of seats in the Seimas in February 1992. In November 1992, Algirdas Brazauskas, the DLP leader, was elected president with 60% of the vote (the Disguised Reform) (Reardon, 1996). Various governments rose to power throughout the years in Lithuania, which succeeded in bringing about economic recovery and Lithuanian's full membership in the European Union (EU) and NATO. Nonetheless, some scandals or negative events came to the spotlight:

- the major banking scandal with two of Lithuania's largest commercial banks, the Innovation Bank and the Litimpeks Bank in 1995;
- corruption problems in the public sector along with the resignation of Prime Minister Vagnorius in 1999;
- economic problems and inadequate reforms (the resignation of Prime Minister Rolandas Paksas in October 1999 due to a protest of the privatization sell-off of a Lithuanian petroleum refinery to a United States company);
- the financial crisis in Russia in 1998 which led to an economic recession in Lithuania in 1999.

In 1991, Latvia claimed de facto independence. The central government of the Soviet Union granted independence to Latvia on 21 August 1991. The process up to independence was marked by violence and Soviet aggression especially in January 1991 when some people from Latvia were killed in Riga by the Soviets and the subsequent soviet coup failed in Latvia on August 1991 (Violent Reform).

Throughout the political situation in Latvia, it can be argued that several coalition governments came into power and the Compromised Reform path was always adopted. Thus, in the 1993 elections, eight political parties passed the 5% threshold to enter parliament, but the Latvian Popular front (LTF) was outvoted. The liberal Latvijas Celš (Latvia's Way, LC) became the largest party, forming a centre-right coalition with the Latvijas Zemnieku Savienība (Latvian Farmers' Union, LZS). The 1995 elections resulted in a deeply fragmented parliament represented by nine parties**,** with the largest party commanding only 18 of the 100 parliament seats. Attempts to form right-of-centre and leftist governments failed and a broad but fractious coalition government of six of the nine parties was formed under the non-partisan Prime Minister, Andris Skele. In 2000, as a compromised candidate, Andris Berzins became prime minister. His four-party coalition lasted until the elections of 2002 (the Compromised Reform path for the case of Latvia).

The Mixed Transition Reform path to democracy (e.g. Albania): After the collapse of communism, the first liberal elections in Albania took place in March 1991. The results gave the Communists a decisive majority, but a general strike and street demonstrations soon forced the all-Communist cabinet to resign (the Rebellion Reform).

In June 1991, the Communist Labor Party renamed itself as the Socialist Party and renounced its past ideology (the Disguised Reform**)**. However, the opposition Democratic Party won a landslide victory in the 9 April 1992 elections, and Sali Berisha, a former cardiologist, became Albania's first elected president of the transition years.

The political career of Mr. Berisha started with the students' movement of December 1990. He had become well known for his public criticism of the old system and his speeches about the need for the democratization of the country. Despite many reforms that took place, his administration was marked by widespread corruption and abuse. The following year, ex-Communists, including Ramiz Alia and former Prime Minister Fatos Nano, were imprisoned on corruption charges.

Finally, in March 1997, Albania's experiment with the democratic reform and a free-market economy went disastrously wrong when large numbers of its citizens invested in dubious get-rich-quick pyramid schemes. When five of these schemes collapsed in the beginning of the year, depriving Albanians of an estimated $1.2 billion in savings, the citizens' rage turned against the government, which appeared to have sanctioned the nationwide fraud. The country's fragile infrastructure collapsed and gangsters and rebels overran the country; people were killed, a civil war began, buildings were set on fire and half a million rifles and other weapons were stolen when arms depots across the country were raided – plunging the country into virtual anarchy. During this time, Albania's already inadequate and antiquated infrastructure suffered tremendous damage, as people looted public works for building materials (the Violent Reform or Armed Rebellion Reform).

The anarchy of early 1997 alarmed the world and prompted intensive international mediation. A multinational protection force eventually restored order and set up the elections that formally ousted President Sali Berisha. It also led to the victory of a socialist-led coalition of parties. In July of 1997, Berisha was replaced by the socialist Rexhep Meidani. Later, Ilir Meta was elected prime minister in 1999 and rapidly moved forward in his first years to modernize the economy, privatize business, fight crime, and reform the judiciary and tax systems. He resigned in January 2002, frustrated by political infighting. In June 2002, former general Alfred Moisiu (a non-partisan figure) was elected president, endorsed by both the Socialists (headed by Fatos Nano) and the Democrats (led by Sali Berisha) in an effort to end the unproductive political fractiousness that had stalemated the government (Compromised Reform).

Between 1997 and 2002, a series of short-lived governments succeeded one another. Fatos Nano, Chairman of the Socialist Party became prime minister in July 2002. Having in mind the political history of Fatos Nano, it can be argued that in that time period a Disguised Reform model appeared in Albania.

The peaceful transfer of power from Meidani to Moisiu was the result of an agreement between the parties. This 'truce' ushered in a new period of political stability in Albania, making significant progress in democratic and economic reforms and in the rule of law possible and leading to the development of Albania's relations with its neighbours and the USA. Yet, a decade of friction in Albania between the Socialist Party and the Democratic Party has delayed Albania's transition to a market economy and postponed its admission to key European institutions.

Most of the Transition Reform paths appeared in the case of Albania. This can partially be a significant reason for the delay in reforms and economic development in Albania. As the Violent, Rebellion, Disguised and Compromised Reform paths are all valid for the case of Albania, we are led to conclude and argue that Albania together with Serbia & Montenegro are the most complex transition country case studies in the region (the Mixed Reform).

The Mixed Transition Reform path for the case of Bulgaria: Except for the Disguised Reform model for the case of Bulgaria, it can be said that two Rebellion models occurred in Bulgaria. One (with the help of a general strike) took place in late 1990 and replaced the Bulgarian socialist party by a coalition government and the other in 1997 when the Bulgarian people demanded the resignation of the corrupt government which remained in power from December 1994 up to February 1997. In this period, three economic crises took place. After this, a caretaker cabinet was appointed by the Bulgarian president and in April 1997 the united democratic forces' coalition won the elections. Together with the International Monetary Fund, they brought about quick and successful transition reforms (Compromised Reform).

The Mixed Transition Reform path for the case of Russia: After the resignation of Gorbachev in 1991, the USSR was dissolved and Russia as the Russian Federation became its largest successor state, inheriting its permanent seat on the UN Security Council. The 12 June 1990 is celebrated in Russia as its Independence Day. In the first democratic presidential elections in Russia, held on 15 June 1991, Yeltsin captured more than 57% of the vote, defeating Nikolai Ryzhkov and Vladimir Zhirinovsky, amongst other candidates.

Yeltsin was well-known for his harsh criticism of Mikhail Gorbachev and the communist hardliners. In Yeltsin's opinion, Gorbachev should have increased the pace of reforms in the USSR but got tough on the conservatives. However, in July 1990, Yeltsin quit the Communist Party.

Boris Yeltsin's career in the Communist Party administrative apparatus began in 1969, when he became Chief of the Construction Department of the Sverdlovsk Region Committee of the CPSU (Communist Party of the Soviet Union). In 1976, Yeltsin was elected as the First Secretary of Sverdlovsk Region Committee of the CPSU. He was also elected President of Russia by popular vote in 1991 (the Disguised Reform). It was at the end of 1991 when Yeltsin and other presidents of all former Soviet Republics signed the treaty dissolving the USSR (the Diplomacy Reform).

At the beginning of 1992, just after the breakdown of the USSR, Yeltsin and his government started a hard-lined monetary economic policy which became increasingly unpopular. This policy was called 'a shock without therapy', in contrast to the economic reform of 'shock therapy' which took place for example in Poland. However, Schlack (1996) suggests that Russia's parliamentary elections proved that the reformers of the shock therapy received far less support than they had enjoyed three years previous and that this happened after a 'successful' transition. Schlack (1996) added that those who offered advice should have been more sensitive to the question of how ‘success’ might be defined.

In September 1993, President Yeltsin issued a special decree on presidential rule and the use of a referendum to gain approval for his transition and economic reform policies. Publicly opposed by Vice-President Alexander Rutskoi, when Rutskoi refused to submit his resignation at Yeltsin’s request; Yeltsin stripped him of all of his vice-presidential powers. Yeltsin removed Rutskoi as Vice-President on charges of corruption, an action opposed by the parliament. Subsequently, Yeltsin issued a decree dissolving parliament. Although, many deputies obeyed Yeltsin’s order to disband, around 100 deputies and several hundred armed supporters led by Rutskoi occupied the parliament building.

On 4 October, several elite divisions of Russian military forces decided to support Yeltsin. Tanks rolled up to the ‘White House’ (the Russian Parliament building) and firing began. Large crowds of Moscovites ‘attracted’ by the unusual events encircled the parliament building. Many were injured or even killed by stray bullets. A tense stalemate ensued between government and rebel forces that lasted for several days, ending when rebel supporters staged an attack on the city hall in Moscow and Moscow’s main television complex. The government responded by shelling the ‘White House’ and suppressing the rebels. A few days later, under Yeltsin’s pressure, the Head of the Russian Constitutional Court was fired, because he opposed the military and violent solution of the conflict between the presidential and parliamentary side (the Violent Reform).

Thus, Russia followed a Mixed Reform, a Disguised Reform when an ex-communist leader (Yeltsin) was elected president of Russia and remained in power for many years, a Diplomacy Reform after the breakdown of the USSR and finally, a Violent Reform in 1993.

The Mixed Transition Reform path (e.g. the Federal Republic of Yugoslavia (FRY) and Serbia & Montenegro): The historical analysis starts with Milošević who began his professional life as a banker, working for the Beogradska Banka (the Belgrade Bank), at times residing in New York as the bank’s official representative abroad. However, he emerged in April 1987 as a leading figure in Serbian politics. His political views have sometimes been termed as nationalistic, despite the fact that his ideology was strongly marked by socialist and leftist viewpoints. However, after he was elected president of the Belgrade City Committee of the League of Communists, Milošević publicly opposed nationalism.

His mentor and godfather, Ivan Stambolić, was the party leader in the Serbian section of the ruling League of Communists of Yugoslavia. In September 1987, Stambolić became president of Serbia and supported Milošević in the elections for a new leader, to the dismay of the other leaders in the party. Stambolić spent three days advocating Milošević’s election and finally managed to secure him a narrow victory, the tightest ever in the history of the Serbian Communist Party’s internal elections (the Disguised Reform).

In February 1988, Stambolić was officially voted out of power, leaving the path clear for Milošević. Milošević would later be charged with ordering the murder of Stambolić, something that has never been proved. Milošević presided over the transformation of the League of Communists of Serbia into the Socialist Party of Serbia (July 1990) and the adoption of the new Serbian constitution (September 1990) which provided for the direct election of a president with increased powers (the Disguised Reform). Milošević was subsequently re-elected president of the Serbian Republic in the direct elections of December 1990 and December 1992.

Milošević's rejection of claims of a first-round opposition victory in the elections for the Federal presidency in September 2000 led to mass demonstrations in Belgrade on 5 October and the collapse of the regime's authority (the Peaceful Revolution). Opposition-list leader Vojislav Koštunica took office as Yugoslav President on 6 October 2000. Ironically, Milošević lost his grip on power by losing the elections which he had scheduled prematurely (before the end of his mandate).

On 25 January 2001, Zoran Djindjic took over the leading position in the Serbian government. However, the assassination of Djindjic in March 2003 created political instability in the country and a significant delay to the required reforms for Serbia & Montenegro (the Violent Reform).

As previously mentioned, Serbia & Montenegro became involved in a war with the Croats and Bosnians due to the presence of large Serb minorities in Croatia and Bosnia & Herzegovina, and together with the Kosovo war, as well as the war and sanctions with the UN, it can be argued that for a long time period the Serbians followed a Belligerent Reform path. However, at the end of 1995, the Dayton Peace Accord was signed by the presidents of Bosnia, Croatia, and Serbia, calling for the division of the republic into 'entities' (Diplomacy Reform). Serbia & Montenegro suffered greatly during its transition, following a disguised reform path for many years (more than any other transition country) under the Milošević regime, a rebellion reform path when the Serbians ousted this regime together with belligerent and diplomacy reform paths during its war with the Croats and Bosnians, and another war with the Albanians and the United Nations army forces in Kosovo. Lastly, a violent reform model took place with the assassination of Zoran Djindjic in March 2003. Consequently, the Mixed Reform is the appropriate model for Serbia & Montenegro.

It is the author's conviction that there is a close connection between the transition from a planned economy to a market economy with the transition from communism to democracy. Countries which faced a mixed reform and especially the belligerent, violent and disguised reform models, are less advanced countries and weak reformers with limited institutional and transition (macro) reforms. To this end, nine reform paths were explored and analysed in order to describe the chosen democratic and reform paths of the transition countries. It is therefore concluded that the least advanced transition countries followed, or were forced by conditions to follow, problematic reform paths such as the violent, belligerent or disguised models.

These countries have limited economic growth and not only lag behind other transition countries in the region, but are far behind the levels of industrial output they had attained in 1989. To be more specific, according to UNECE (2005), the figures show that Russia's level in 2004/5 was -28.7% of its level in 1989, Bulgaria being -35.6%, Romania -45.6%, FYROM -55.5%, Bosnia & Herzegovina's 84.7%, Albania's -74.2%, and Serbia & Montenegro's at -58.3%. Moreover, the same source claims that these countries are far behind the real GDP levels they had in 1989 (e.g. Bulgaria -8%, FYROM -16.5%, Russia -17.5% and Serbia & Montenegro -46.3%).

We can thus infer that these countries have high unemployment rates, and high corruption rates. Moreover, they lag behind the other transition countries in institutional and transition reforms. Furthermore, they are proved to be countries with low living standards, low GDP per capita even in PPP prices, and low wages. They also rank low in the human development index; have a weak infrastructure, an unfavourable, bureaucratic business environment and an unstable legal framework. Finally, they are the least attractive destinations for FDI inflows in the region. To conclude, we strongly believe that such drawbacks are linked to the above mentioned unfavourable reform models existing in these countries.

1.3 The Transition from a Planned to a Market Economy: The Four Steps Needed for Transition Reform

Given the common goal of the transition countries to move to a market economy and therefore to promote enhanced economic efficiency and high growth rates, there is a widespread agreement that the crucial elements (steps) of the transition process are macroeconomic stabilization, price and trade liberalization, restructuring and privatization and institutional reform (Lipton and Sachs, 1990; Fischer et al., 1996; Fischer et al., 2000; Gomulka, 2000; World Economic Outlook, 2000).

The four dimensions (steps) of the transition reform are interrelated and progress should be made in all of them (sequence and speed of reforms). Otherwise, distortions, negative effects and the risk of a breakdown of the pursued market economy might appear.

When the transition reforms were launched, the inherited imbalances were expected to bring about severe inflation. Therefore, an essential element of the transition towards the market economy was macroeconomic stabilization, which is comprised mainly of money, finance and exchange rate policies (Meyer, 1998). A macroeconomic stabilization programme reduces the inflation and money-overhang followed by severe efforts to decrease the huge debt burden. Kiguel et al., 1991, 85, 90) have argued that: 'The effectiveness of alternative stabilization strategies largely depends on a country's inflationary history … hyperinflation cannot be stopped always and everywhere in the same way'. Macroeconomic stabilization implies implementation of measures and policies related to key macroeconomic variables such as policies for low inflation, higher output performance, improved balance of payments, lower debt, and lower unemployment (EBRD, 1994).

In most countries of the CEE, macroeconomic stabilization was based on the standard IMF heterodox approach, applying an income anchor simultaneously to a tight fiscal and monetary policy, and a fixed exchange rate when feasible. Yet, by considering the credit to government and enterprises, it might be inferred that money was the key nominal anchor, while the exchange rate and income policy had a supportive role (Gomulka, 2000).

After the initial years of transition, there was a tendency in the transition countries to move to more flexible exchange rate regimes, as although inflation declined, it did not fall enough to stop a significant real appreciation. This created balance of payment problems (Jonas and Mishkin, 2003). However, during the transition course it became clear that the choice of the exchange rate regime did not seem to be a critical factor influencing the stabilization results in the transition economies, because a successful anti-inflation policy is primarily determined by pursuing a consistent monetary and fiscal policy (World Economic Outlook, 2000).

The macroeconomic stabilization programme should be initially adopted in order to reduce inflation and money-overhang, and severe efforts to decrease the huge debt burden should follow. There are two determinants for the stabilization process, each of which includes two different stabilization strategies; the orthodox and heterodox approaches combined with money based and exchange rate based stabilization strategies.

The orthodox approach is based on elimination of the budget deficit by using strict fiscal policy (fiscal anchor), simultaneously using a monetary policy (monetary anchor). In the heterodox stabilization approach, income policy is used together with monetary and fiscal policy, as an extra tool for rapid and synchronized cut of inflation. Thus, there is direct intervention in wages and prices (income anchor).

> [The] heterodox approach argues that budget adjustments and tight monetary policy alone are insufficient to stop high inflation … in [the] … contrary … wage and price controls may be superfluous … [The] … price controls may be difficult to enforce beyond a very small group of commodities … controls might be anticipated, controls may be addictive, giving policymakers the idea that inflation can be stopped without any other pain … [Those] … controls can introduce a great deal of rigidity in the relative price structure of the economy … controls may prove hard to phase out. (Jeffrey Sachs, 1993, 754)

In the money based stabilization policy, the central bank chooses the money stock or the net domestic assets as its main policy target. Alternatively, in the exchange rate based stabilization strategy, the exchange rate serves as the main nominal anchor. Therefore, a country has to choose between heterodox and orthodox stabilization policy, setting the option of having the exchange rate as an extra nominal anchor or using the money based stabilization programme. However, if a country chooses the heterodox exchange rate based stabilization programme, but after a short or long time removes the wage and price measures, then the programme becomes an orthodox exchange rate stabilization programme.

Miguel A. Kiguel et al. (1991, 85, 90), argued that ‘The effectiveness of alternative stabilization strategies largely depends on a country’s inflationary history … hyperinflation cannot be stopped always and everywhere in the same way’. It should be pointed out that money based stabilization applies an inadequate solution in the wrong way: because of the unstable demand of monetary targeting is inadequate, applied in the wrong way, designed as a medium-term concept and not as a strategy for short-term macroeconomic fine-tuning (Bofinger, 1996, 665–7).

Most Central and Eastern countries followed the heterodox stabilization programme (Bulgaria, Romania, Czechoslovakia, Poland and Hungary). Only Russia, Ukraine and Kazakhstan, followed the orthodox programme (Bofinger, 1996). Bulgaria and Romania, having limited foreign reserves, chose a money-based approach. However, the other countries mentioned have selected the exchange rate based stabilization programme. The Bulgarian economy suffered from economic and political instability from 1989 until 1997, when on July 1997 the introduction of the currency board finally brought ‘peace’ (see also Zloch-Christy, 2000). The excuse of lack of currency reserves, the inability of each government to draw loans from the western countries or institutions, or the foreign countries’ or institutions’ unwillingness to help, brought about three major economic crises in Bulgaria in the first eight years of the transition period. Those crises weakened the economic position of the Bulgarian people. As a result of which per capita consumption fell drastically, discouraging any significant FDI inflows.

Reaching the main transition goal, sustained economic growth implies that inflation should be kept at a low level, as Fisher et al. (1996) suggests the positive growth in transition economies could be observed within two years of inflation decreasing below 50%. Ghosh (1997) infers that if the inflation level is above 10%, a GDP growth above 2% cannot be attained.

Given the negative impact of inflation on the output level, fighting inflation was a major goal of the macroeconomic stabilization programme at the onset of transition and as stated by Fisher and Sahay (2000, 7): ‘Several checks were introduced in the stabilization programs to contain inflation: tight monetary and credit policies, wage control policies, monetary reforms, and non-inflationary sources of financing the budget deficits’.

By applying either the orthodox or heterodox approach combined with the money- based or exchange rate based stabilization strategy, policy-makers of transition countries can pursue the desired macroeconomic stabilization. The orthodox approach aims to elimine the budget deficit by conducting stringent fiscal policy and by employing a monetary anchor through monetary policy at the same time. The heterodox approach not only implements monetary and fiscal policy, but it also uses income policy, as well as wages and prices controls for fighting inflation.

There were some controversies with regard to the type of stabilization programme to use. Calvo and Vegh (1999) assert that choosing between the exchange rate and money supply as nominal anchors presupposes a trade-off between 'recession now' (related to money-based stabilization) and 'recession later' (indicative of exchange rate based stabilization). It has been pointed out that the exchange-rate anchor is a more easily observable target and if monetary and fiscal policies exhibit discrepancies from the defined exchange rate target, doubt will be cast on the ability of policy makers to conduct the reforms efficiently.

Drabek and Brada (1998) argue that if fiscal policy or other stabilization policies are improper, the decision of choosing exchange rate as a nominal anchor may result in a significant pressure to conduct protectionist trade policies. Christoffersen and Doyle (1998) imply that output losses could be observed due to the employed undervalued pegs, when a rapid disinflation policy involving pegged exchange rate is pursued.

On the other hand, money-based stabilization involves reduction in the growth rate of the money supply. This means a lower level of liquidity. Subsequently interest rates will rise and the economy will be driven into a recession (Calvo and Vegh, 1999). Jonas and Mishkin (2003) contend that in the transition countries the use of monetary aggregates as a nominal anchor is not appropriate because of the instability of money demand and the unstable relationship between the growth of money supply and inflation.

Rusek (2001) investigates the effectiveness of the monetary policy in the transition countries by focusing on the stability of the relationship between the money stock and macroeconomic variables such as output, price level, interest rates, and exchange rates. He infers that active use of monetary policy is difficult in the transition economies because of their significant rigidities, which in turn lead to an unstable relationship between monetary aggregates and macroeconomic variables. The best outcome a monetary policy can provide is to discourage inflation in the long run, by being excessively loose and not impeding growth by being too tight, while the short run application of monetary policy is limited only to maintaining a stable real exchange rate and to providing necessary liquidity.

Klyuev (2002) supports the advantages of the exchange rate anchor in fighting inflation but questions the effectiveness of the exchange rate stabilization in the long run. He argues that the inflation rate does not decline instantly to trading-partner levels that yield a real appreciation of the domestic currency and negative effects on the trade balance and current account balance. The basic inference is that there is a non-linear relationship between the inflation rate and the exchange rate flexibility; an increase in inflation from a low level requires a flexible exchange rate, while the fixed exchange rate regime would be a necessity when a rise in already high inflation appeared.

At the start of transition it was recognized that a crucial part of the macroeconomic stabilization is the change that both state's revenues and expenditures should undergo. However, the need for major fiscal reforms was overlooked and the reforms of state structures and public administration received little attention until a number of fiscal crises appeared in late 1991 and 1992 in transition economies (UNECE, 2000).

Regarding the revenues, the taxation policy should be modified as a new tax system based on general tax rates, value-added tax, income taxes, profit taxes etc., should be adopted. As to expenses, the subsidies to goods and to state enterprises should be eliminated or replaced by credit subsidies. At the same time, many of the government expenditures related to social issues should remain unchanged. Tight wage policy should also be implemented in order to avoid an increase in monetary overhang and to improve the government budget (Meyer, 1998).

Another element (step) of transition is liberalization of economic activity aimed at abolishing the centrally planned system and central regulations by establishing market determined prices, foreign trade liberalization and currency convertibility. Price liberalization is one of the most significant factors for the creation of a market economy because market determined prices are the essence of the market mechanism, reflecting both the consumers' demand and the producers' costs and supply.

An additional decisive condition for the establishment of a market economic system is that trade liberalization should provide for enhanced competition, elimination of trade monopolies and the opening of the economy to foreign investors (Meyer, 1998). Thus, the second step of transition, is liberalization of economic activity (prices, trade, currency convertibility etc.), which should be supported by institutional restructuring. This structural reform provides an efficient system of laws regulating the economic activity and redefining the role of the state. This also includes the restructuring and privatization of the bulk of the state assets, which constitute a large percentage of the total assets of the country.

The sudden exposure to market forces is likely to cause instability in the economy. This, complemented by the trivial experience of people and the mediocre economic legacy of the past, may lead to severe economic crises. In order to avoid these crises, the state needs to establish macroeconomic stabilization policies. The typical symptoms of the 'transition shock' are a drastic increase in inflation, reduction of total output levels, increase in the unemployment rate, increase in prices, a severe social impact, and citizens' negative reactions due to their bad economic condition.

Liberalization of prices is of vital importance for the transition towards a market economy. Prices should be undistorted so as to facilitate enterprise decision-making, as they should be changed significantly and liberalized in order to reflect the required reduction of subsidies needed for the successful macroeconomic stabilization (EBRD, 1995). In the beginning of transition, it was recognized that the expected considerable increase in the prices of basic goods, such as food and energy products should be avoided and either a price ceiling should be placed on them, or the desired price level of the basic goods should be maintained through subsidies (Meyer, 1998).

Since the beginning of transition the relative price adjustments were more divergent among the transition economies. This was because of their greater susceptibility to external shocks such as significant changes in world market prices for commodities, large devaluations of some of the domestic currencies and the various degrees of price control. Although most other product prices were liberalized during the early phases of the reform process, the prices of most formerly state-provided services remained under control, as an element of the social safety net, and their prices increased only gradually. It might be inferred that one of the crucial trade-offs in the transition countries is between achieving macroeconomic stability, and at the same time gradually moving towards market determined prices or instant liberalization of most prices. However, the decision to keep inflation low through price ceilings proved to be counter-productive in the long-run. To this end stable relative price structure is vital for macroeconomic stability and sustained growth (UNECE, 2000). The more intense the price liberalization in the transition countries is, the sharper the initial fall in the level of output will be and the more rapid the contraction of the old enterprise sector will become. On the other hand the creation of new, more profitable enterprises will be encouraged and a favourable environment for higher levels of income in the medium term will also be in place (Herdandez-Cata, 1997).

Herdandez-Cata (1999) analyses the main determinants of the intensity of liberalization reform in the transition countries and concludes that political freedom, proximity to the West, and the level of underground economy are all associated with low resistance to price decontrol. Therefore, they affect positively the intensity of liberalization, while the membership in rouble area and the longer period under central-planning impede liberalization reforms.

However, integration of the transition countries into the world economy requires opening up the domestic economies through an orthodox commercial policy: elimination of the CMEA's regimes, removal of tariffs, establishment of an effective exchange rate reflecting price-based international competition, and entrance into global economic regimes and organizations (Van Brabant, 1994). Many discussions took place regarding the way under which trade liberalization would be conducted. Many studies support the application of a more gradual approach in liberalization of the international trade and the opening of the economies of the transition countries. Van Brabant (1994) maintains that the effectiveness of trade liberalization heavily depends on the credibility of the government policies pursued, pointing out that if liberalization coincides with macroeconomic instability or with an unstable political climate, as in Eastern Europe, there may be a trend toward a lower level of investment. The author suggests that in this case rapid trade liberalization might destroy much of the transition countries' productive capacity. He further argues that the trade regime must be tailored to longer terms, because of the time required for building up production and exporting capacities and capabilities and well functioning capital markets.

These findings are supported by Hare (2001) who asserts that a sudden liberalization may cause a significant adverse shock to domestic enterprises, because they lack the necessary time to adjust to the new environment and external competition will drive them out of the country.

Marangos (2001) offers a set of international trade policies for transition economies, comprised of a fixed exchange rate and protection policies from imports that are expected to result in substantially reducing the transition cost and corruption, thus stimulating a civilized society. He argues that as international trade is an important ingredient of the transition process, it should be introduced gradually, in an organized fashion and by using social benefits as a measure of its effectiveness. He reasons that the total liberalization of foreign trade would damage those industries which were technologically advanced but uncompetitive in the international market.

Designing the proper path for trade and exchange rate liberalization for transition economies means that the initial conditions, political processes and the incomplete nature of domestic markets should be considered. Furthermore, CMEA ties should be maintained at least in the short run, given the substantial volume of idle resources in the transition countries and their considerable absorption capacity (Van Brabant, 1993). Gowan (1995) asserts that after trade liberalization takes place, only a small number of the transition countries (Central European countries) will be able to uphold the considerable market pressures resulting from liberalization and thus be ready to compete in Western markets.

Effective trade liberalization requires re-integration of the formerly centrally planned economies into the global trading system. Almost all countries in transition from central planning have accepted the WTO rules in principle, despite the variations in trade policies and performance. WTO membership is a key factor underpinning the reform process. It provides some protection against imposition of non-tariff barriers and offers dispute mechanisms in case of disagreements between the members. Moreover, in respect of European transition economies aiming at EU membership, WTO membership shows their sincere ambition to create a market economy and to observe international trade law (Pomfret, 2001; Hare, 2001).

Foreign trade liberalization policy is closely linked to the liberalization of the foreign exchange market, particularly with the exchange rate regime, current account convertibility, and capital account liberalization (Hare, 2001).

A third step to transition is the privatization and restructuring of the economy. Privatization and restructuring have a crucial importance for the creation of a market economy, as they are essential determinants for the transition of the decision and motivation structures (EBRD, 1994). Thus, a decisive step in the transformation process is the size reduction of the public sector through quick privatization and restructuring of state-owned enterprises. It is essential that this be supported by the introduction of new corporate governance and property rights. The expected positive outcomes of privatization imply that it should lead to a new private and institutional ownership structure, replacing the old state administered system and together with deregulation and demonopolization, privatization should reform and overcome the inherited industrial structure. It is also anticipated that privatization encompassing all economic areas, including the banking sector, will