The Superiority of Eliminating Barriers to Entrepreneurship over Privatization Activism of the State

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During the whole period of transformation, i.e. since the memorable 'Autumn of Nations' in 1989, politicians, analysts and societies in general have concentrated their attention, energy, and resources on privatization, that is the transformation of state ownership into private ownership. Privatization, understood in a manner defined above, has been largely seen as a cornerstone of transition to a capitalist market economy in the longer run (please note that the terms: 'transition', 'transformation' and 'systemic change' are used here interchangeably). Private ownership is best performing within the framework of the institutions of the market. There has been a near consensus on the latter view (a few utopian strands of economic thinking notwithstanding).

Since this essay concerns Poland more than any other post-communist economy in transition – as a case study for ideas developed here – it is worth mentioning that in Poland the term 'ownership changes' has been used at the start as a substitute for privatization (even the ministry that transforms state-owned enterprises into privately-owned ones is called the Ministry of Ownership Changes and not, as is the case with other countries in East-Central Europe, the ministry, or agency, or office of *privatization*).

This has not been a linguistic slip-up but a conscious political economy decision on the side of the team shifting Polish economy onto a path of a capitalist market system. For in Poland the resistance to privatization has been stronger than in the other countries in the region. The main source of this stronger resistance have been the *de facto* collectivistic ideological origins of the 'Solidarity' movement

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under communism and its later activity, consisting of a marriage of a problem elsewhere (Winiecki 1992 and 1993). In every post-communist country there have been socialistic opponents of privatization on the left and nationalistic ones on the right. But the uniqueness of the Polish situation consisted of the fact that they were also over-represented in the systemic change-oriented centre.

Unsurprisingly, stronger resistance to privatization has been translated into a very slow (and fiercely contested) privatization process, as well as meagre privatization effects. Privatization in Poland markedly lags behind that in the Czech Republic, Hungary and a number of other countries in transition, even those that are not noted for their successes in other areas of systemic change.

At the same time, however, Poland is widely regarded as one of the leaders in the shift to a capitalist market economy among the countries of the region. Moreover, the share of the private sector in GDP and employment is in Poland about as large as in the countries regarded as success stories with respect to privatizing their economies. What happened? There is yet another, generally under-appreciated, process. It is the development of the generic private sector, contributing to the growth of the size of the private sector in the national economy. And it is the relative role of the former *vis-à-vis* that of the latter in post-communist transition – and lessons drawn therefrom – that will come under scrutiny in this article. Poland is taken as the case study, but the reader will see that the potential for such success exists, under certain conditions, elsewhere as well.

Insignificant contribution of privatization to the size of the private sector in Poland

Privatization does not consist merely of the ownership changes in state-owned enterprises, that is of the privatization activism of the state, but also of the creation of new private enterprises and expansion of those, which already exist and have been privately-owned from the start. This is what the present writer calls the *generic* private sector. The final objective of privatization is, after all, the creation of an economy with the ownership structure similar to that of Western countries (that is, at a minimum 85-90% of output of the enterprise sector generated by private firms).

This objective can be reached by two complementary routes. One of these routes attracts everybody's attention; this situation hardly changed since 1989. It is the the activism of the state, or the *privatization 'from above'*. Another route may be called, using parallel terminology, the *privatization 'from below'* (for more on this distinction, see Gruszecki and Winiecki 1991).

With over six years of political system transformation already behind us, it is worth taking a calm look at both these routes. One thing which can be said at the outset is that in the whole area of public activity – from political conflicts to the allocation of funds – privatization 'from above' has definitely dominated over privatization 'from below'.

It is hardly surprising, though. At the very beginning of the transformation process, politicians, trade union activists and even analysts in Poland and elsewhere noticed almost exclusively the privatization 'from above'. The public sector – in reality, the *state* sector – dwarfed the private sector, outside agriculture, with respect to its size. Consequently, people tied any hope of a successful radical systemic change with the transformation of state-owned enterprises into privately-owned ones; or, in accordance with the utopian beliefs still common in Poland in 1989-90, transformation into independent enterprises managed by the workers collectivities. It should be noted that in other countries in the region (except Hungary) the generic private sector had at the start even smaller shares than in Poland.

A legitimate question to ask is the following: to what extent did Polish privatization 'from above' live up to those great expectations? The correct answer, surprising to those who fought – and are still fighting – heroic battles for or against privatization, is that this extent was *very small.* I will support the statement by quoting some numbers. I begin with quoting some independent studies on the subject for one cannot take respective bureaucracies official statements' for granted.

Bobinska (1994) tried to calculate how many state enterprises (SOEs for short) have been privatized and got numbers sharply different from the officials ones. According to official figures of the then latest privatization report of the ministry, 52% of SOEs underwent 'ownership transformation'. However, 'ownership transformation' may mean different things to different people.

A thorough calculation by Bobinska (1994, p. 35) reveals the following: "Out of a total of 8,441 state-owned enterprises in 1990, 1,595 (18.9%) have been transferred to the State Treasury Agricultural Ownership Agency, i.e. a state-owned institution. 263 enterprises (3.1%) were communalized, i.e. taken over by local governments and 2,521 (29.9%) were transformed on the basis on the above-mentioned law [of July 1990]. The remaining enterprises have not undergone *any* transformation". Going below the surface, Bobinska also established that among those enterprises officially described as "having undergone transformation" only 98 (1.2%) have been transformed into joint-stock companies and have had at least 50% of their stock sold, i.e. have actually been privatized; 424 (5%) have been transformed but not privatized; 707 (8.7%) have been liquidated under the terms of Article 37 of the privatization law of 1990, including 85 enterprises (0.5%) that have been sold. In most of the enterprises, the assets are merely leased and therefore true privatization will have occurred only when they have been paid for by over 50%; 172 enterprises (2%) have also been liquidated according to Article 19 of the old law on state-owned enterprises; and there are 1,220 enterprises (13.2%) undergoing transformation. At the same time 4,062 enterprises or *nearly half of the total* (48.2% to be exact), have not undergone *any* sort of transformation.

Bobinska concluded that "over the past four years privatization has been carried out fully and completely in only 1.7% of the enterprises according to the terms of the privatization law [of 1990]". Thus, official statements do not present the real picture of Polish privatization.

Barely 2% of enterprises being really privatized, means surprisingly little but one might ask whether the percentage of the enterprises is not a misleading indicator. For it does not take into account the fact that in a communist (Soviet-type) economy – from which Polish post-communist economy emerged – most state-owned enterprises are large and very large, and consequently 1.7% may account for a much higher share of employment and production.

Helpful in answering this query is a study on the growth of the private sector in Poland (Chmiel and Pawlowska 1996), which estimates the changing shares of the individual types of privatization in the economy as a whole (privatization, referred to by us as privatization 'from above'; reclassification of the cooperative sector from public to private sector, i.e. purely statistical operation; and what we call privatization 'from below').

These changing shares of public and private sector result from two parallel developments. On the one hand public sector employment in various segments of the economy continues to shrink; on the other, private sector employment increases in absolute terms. Both developments take place at different rates, depending on the segment of the economy. Thus, the deepest decline in public sector employment has been registered in construction (–70.7% in 1990-1993), while the biggest increase in private sector employment took place in wholesale and retail trade (+166.9% in 1990-1993). Interestingly, registered growth in private sector employment in construction was only +24%, due to the large 'black economy' employment in this particular segment (a phenomenon not unknown elsewhere).

A very detailed analysis of these authors shows that, quality of the official data notwithstanding, the share of privatization 'from above' as the share of the private sector in terms of GDP and employment is nonetheless very small. It varies from 'imperceptible' (below 1%) to 'perceptible' with the latter term still signifying relatively small shares (that is small relative to the share of privatization 'from below').

In two out of the four branches of the economy which the study examined – transport and trade – the contribution of this type of privatization to total employment stood at significantly less than 1%, and in the two sectors where the authors assessed the share as 'perceptible', i.e. in industry and construction, these shares at the end of 1994 stood at, respectively, 4.4% and 11.3%. The shares in production were not significantly different from the shares in employment. By contrast, the contribution of the generic private sector to total employment stood at 33.2% in industry and 60.7% in construction (shares in aggregate output were respectively over 30% and 73%). The details are shown in Table 1.

Thus, a more detailed analysis confirms the initial assessment that privatization 'from above' does not play any significant role in changing the structure of ownership in the productive sector in Polish transition from socialism to capitalism (furthermore, *nothing at all* happened in what is called in Western Europe the public sector: from physical infrastructure to health and education).

Given the foregoing, it is all the more important to explain why in Poland the share of the private sector in the economy as a whole is not much – if at all – lower than in other countries undergoing the transition process, including those which have had much greater successes in privatization 'from above'. Here I am referring especially to Hungary, which has attracted more of the foreign capital than any other country in the region and the Czech Republic, which has privatized most of the state-owned enterprises through its innovative 'coupon privatization'. The lesson(s) to be learned may be important not only for Poland but also for other transition economies.

TABLE 1

SHARE OF PRIVATE OWNERSHIP IN OUTPUT OF SELECTED SECTORS OF THE POLISH ECONOMY, 1989 AND 1993

Sector / Year	Public sector	Private sector	*of which:* Generic private sector	Reclassified Co-op sector[b]	Privatized sector
Industry					
1989	84.8	15.2	7.5	7.7	0
1994[a]	60.6	39.4	30.6	3.5	5.3
Construction					
1989	67.3	32.7	30.0	2.7	0
1994[a]	13.5	86.5	73.5	0.6	12.4
Transport					
1989	91.0	9.0	6.3	2.7	0
1993	54.8	45.2	44.3	0.8	0.1
Retail trade					
1989	40.5	59.5	4.8	54.7	0
1994	9.2	90.8	81.5	9.3	0

[a] Data calculated according to new, slightly different statistical classification of the European Union.
[b] Under the communist system co-operatives were classified as a part of the 'socialized sector'. After systemic change it was reclassified as a part of the private sector.
Source: Chmiel and Pawlowska 1996.

Crucial role of eliminating barriers to entrepreneurship

At the outset it seems worthwhile to stress what factors, apart from failed privatization 'from above', did *not* decisively contribute to Poland's success.

Thus, the reasons for our success surely do not include a particularly stable macroeconomic framework of the privatization process. Although Poland has been relatively successful in managing its stabilization programme, compared to countries of the former Soviet Union or Romania or Bulgaria, it was far from the iron-willed consistency showed in this area by the government of Vaclav Klaus, first in Czechoslovakia and now in the Czech Republic.

Poland was even less notable for the stability of its political situation. Again, compared to post-communist countries with incomplete political change that – in my opinion – is a prerequisite of economic change (see, *i.a.*, Winiecki 1991), Poland may be regarded almost as a paragon of political stability. However, political stability is also a relative term. To illustrate the point, the first non-communist Hungarian government, headed by the late Prime Minister Antall from 1990 to 1994, dealt with *five* Polish prime ministers.

Therefore, we have to look elsewhere for the reasons of our success. I find the reason, first of all, in a more decisive policy of liberalization and deregulation compared with other countries of the region. Poland has gone farther than nearly all other countries undergoing transformation in creating conditions allowing private companies an almost unrestricted access to all sectors of the economy and areas of activity (such as, e.g., foreign trade).

The elimination of most restrictions to private entrepreneurship actually went into effect as early as the beginning of 1989. One might try to argue, as certain defenders of the pre-1989 era in Poland do, that the foundations for the change of the system were, then, in fact laid down by communist reformers. This, however, would be a perversion of the reality. The communist system was unable to change; it was only able to reform, that is to try (unsuccessfully) to improve the unimprovable (see my earlier writings, especially Winiecki 1986, 1990 and 1991). It was only the political change of 1989, which ensured that the right to unfettered entrepreneurship did not remain only on paper, as it was the case with all the earlier reforms of the socialist economy.

To begin with, the comparison of the unrestricted right of establishment in Poland with the various territorial, sectoral, and other limitations which still exist in other countries, makes it easier to understand the causes for the exceptionally dynamic growth of the generic private sector in our economy. With all the complaints about the bureaucratic slowness (and not inconsiderable corruption), Polish rules for the registration of private companies are incomparably more liberal, even when contrasted with, for instance, the requirement to obtain licenses from district or county government offices existing in the otherwise very liberal Czech Republic (Benacek 1993).

While analyzing the mechanisms of liberalization and deregulation to somewhat greater extent, we note the particular significance of the extension of the liberal rule of establishment to both wholesale trade and foreign trade (see Gomulka 1992). Smaller private wholesalers were much quicker than the state-owned mastodonts in identifying the products for which there is a large and unsatisfied demand and signalling consumers' preferences to producers. This faster identification of changes in the structure of demand by private wholesalers creates *positive stimuli* for producers to changes in the structure of supply. At the same time, the liberalization of foreign trade makes it possible for private wholesalers to import higher quality goods. In addition to the positive stimuli (signaling consumers' preferences) wholesalers therefore convey potential *threats*. The most serious of the latter is obviously the possibility of bankruptcy in the event of not adapting to the new, more exacting requirements.

These twofold adaptive pressures affect not only private producers, but also those among the state-owned producers who have become convinced about need to adapt, first of all because they realized that the emerging market system is there to stay and temporizing means endangering one's prospects of success (or even survival). In this manner, the linkage of private wholesaling with the liberalization of foreign trade becomes a powerful factor contributing to the growth of innovativeness in the whole economy.

From the vantage point of the market process/evolutionary economics perspective the foregoing developments create the necessary conditions for the spontaneous, trial-and-error-type search for efficient outcomes within the framework of the Hayekian 'general rules' of open, competitive economy. In line with Schumpeter the spontaneous developments may be decomposed into 'destruction' (elimination of errors) and 'innovation' (generation of new trials).

In the case of a radically liberalized, deregulated Polish economy of early 1990s elimination of errors manifested itself through the exit of many large state-owned wholesale enterprises and generation of trials by the takeover of markets by smaller but better motivated and generally more efficient private wholesalers. In the case of producers, the trial-and-error searches have been more complex, given the slower emergence of viable competitors of manufacturing SOEs due to higher capital threshold. Therefore, error elimination to a greater

extent consisted of a loss of market share to private Polish producers or to imports rather than exit by manufacturing SOEs, while trial generation was seen through product, technological and/or organizational innovation in SOEs, as well as emergence of successful private competitors. Of course, an often limited adaptation of manufacturing SOEs has largely been the result of the political clout of large industrial firms that both created a climate of indulgence for loss-making (and economic failure in general), as well as effective resistance to exit of loss-makers.

Let us stress again the twofold importance of unrestricted entry of both firms and goods under competitive conditions in an open economy for the industrial sector. It should be noted that in industry (mining, manufacturing, utilities) the share of private sector's employment and output barely reached half of the total by the end 1994, that is after more than five years of Polish transition. By contrast, in those sectors where that threshold is not so high, more and more often almost the only players left in the game, except for some large firms, are private companies as, for example, in construction, commerce, and non-infrastructural services (except for some largest firms).

Lagging privatization 'from above' means that state monopolies, especially in the physical infrastructure sector (energy, railways, telecommunications, etc.) continue to be costly and painful 'humps' on the body of the fast growing Polish private sector-based economy. However, these humps, as well other state-made monopolies and near-monopolies in coal mining, oil refining and distribution, etc., did not, at least for the time being, unduly hinder the rapid expansion of the generic private sector. The period of a *relatively* low-cost existence of completely unprivatized industries is, however, coming slowly to an end (more on this in the last Section of this article).

Let me now restate the reasons of Poland's success in changing the ownership structure of its economy, in terms of the ongoing economists' debate of the relative merits of 'big bang' versus gradual change. I would submit that Poland's successes are due to those particular features of its transition strategy that have been most strongly criticized by the believers in procrastination as the best strategy of change.

Not a few of them, let it be noted, belong to the 'reformers of the unreformable' (or 'improvers of the unimprovable') from the past. Contrary to all the complaints about 'ruining everything' (meaning the state enterprises ...) and 'excessive openness to imports', it is precisely these features that forced adjustment upon the largely unwilling state-owned producers. To put it in yet another way, the most successful were those developments where economic processes were largely left to the spontaneous market forces.

The view formulated in the preceding paragraph calls for reflection. For wherever the successes depended on the spontaneous market forces, the outcomes were a success. On the other hand, wherever lasting, consistent political involvement *and* administrative efficiency of the state apparatus were required, the effects have been by-and-large unsatisfying. What makes the view even more worth of reflection, this has often been the case also in countries with a somewhat more efficient administration than Polish one (Hungary, the Czech Republic). Considerations of the problem in question are presented in the following Section of this essay.

Transforming state property and organizational capability of the state

As stressed already, the overwhelmingly dominant role of the state sector at the start of the post-communist economy concentrated expectations on the privatization 'from above'. But the reliance on the state went much further than that. The establishment of the institutional framework of a market economy, accomplishment of the macroeconomic stability, to say nothing of a social safety net appropriate to free-market conditions – all these measures were supposed to be designed and, much more importantly, implemented quickly and efficiently by agencies of the state.

By contrast, expectations were much more limited with respect to the privatization 'from below'. Of course, nearly everybody expected generic private firms to emerge and grow, but somehow they were often perceived as a necessary but auxiliary component of the size structure of the firms dominated at the upper end and at the middle by privatized ex-SOEs. At the same time, very little thought, resources and organizational effort have been expended on the creation of the conducive environment for the expansion of the generic private sector.

But in spite of everything, it is the latter that expanded very rapidly, and not only in Poland. Also in countries where privatization

'from above' has been regarded as very successful (Czech Republic) or relatively successful (Hungary). The generic private sector has been performing quite well and its shares in the total output and employment, *vis-à-vis* that of the privatized ex-SOEs, may not necessarily be smaller.

There is, obviously, no such lopsided relationship as in Poland due to greater successes of privatization 'from above', but the shares in question are impressive. In the Czech Republic it is the enterprises with employment up to 25 persons that have been increasing production by leaps and bounds. Since the small business sector has been almost the same as the generic private sector in post-communist world, almost 30% of all employed in the national economy in the small business sector translates into 30% share of the generic private sector. Furthermore, Zemplinerova and Benacek (1995) estimate that adding those employed *only* in the 'grey', or unregistered, economy may increase the total by another ten percentage points to some 40% of the total employment (the term 'only' means that part of the 'grey' economy consists of those already counted who are also working in the registered economy).

The estimates of the relative strength of the generic private sector and privatized ex-SOE sector for Hungary are more difficult for many reasons: unsatisfactory data due to the near-collapse of Hungarian statistical services, relative incomparability of statistical categories concerning small business sector, the unclear ownership structure in many Hungarian quasi-privatized enterprises, etc. Nonetheless, output of small firms employing up to 20 or 25 persons have been for years the only growing part of the national economy. Its share, however, may be smaller than in the Czech Republic. By contrast, though, the share of the unregistered private sector, that by definition is small business sector, is thought to be larger in Hungary than in the Czech Republic.

Great expectations apart, early considerations of the systemic change rarely included more elaborated thoughts about the effectiveness of the state in carrying out the many tasks demanded from the state concerning the transition process. The exceptions are articles, like the one written by Brian Levy (1993), who approached this much under-appreciated question in a systematic manner. Levy's explanations make it easier to analyze the problem being considered in this Section.

Levy asserts that among the main determinants of the success or failure of reforms (and, one may add, systemic changes), the one which, in addition to political will, plays a crucial role is organizational intensity of reforms, or the already mentioned capability of the national administration to carry out such organizationally intensive reforms. If this capability is rated as low, then the success of reform depends on the proper mix of institutional measures.

Wherever faced with a low organizational capability of the state, the optimal strategy – as suggested by Levy – should consist of limiting the reform effort (in our case the systemic change effort) to a few areas requiring a high degree of administrative capability that are crucial to the reforms' success. If the need be, these efforts can be undertaken with the assistance of foreign experts. All the remaining measures of the reform 'package' should not overburden the public administration. The author in question refers to these latter efforts as '*stroke-of-a-pen-reforms*'. Easy to implement, these measures may nonetheless also be crucial for the success of the reform (e.g. domestic price liberalization or foreign trade liberalization).

Levy's approach makes it easier to understand the relative success of the privatization 'from below' in comparison with privatization 'from above'. The elimination of barriers to entrepreneurship is markedly easier than privatization of the state property. For the latter requires a rather elaborated legal framework, well designed administrative procedures and a network of public and private institutions partaking in the process in varying roles. It is worth noting that even privatization 'shortcuts', such as the well known and highly appreciated Czech *coupon privatization*, although markedly speed up the privatization process, are organizationally more intensive than the simple removal of barriers to the generic private sector.

Superiority of spontaneous order

However convincing, the preceding considerations are based on certain unstated assumptions. The present writer asserts that the elimination of fundamental barriers to entrepreneurship ('the freedom of enterprise' – to put in economic philosophy terms) is easier than privatizing the state property and links the success of the former

with the dynamic growth of the private sector in Poland. Thus, he assumes that there are reasons why planned actions of thousands of officials yield less satisfactory results than spontaneous developments of the generic private sector.

At this point we need to refer to Friedrich von Hayek and his theory of spontaneous order. Over the past 20-30 years the superiority of spontaneous order, not planned by anybody but created by the process of evolution of the economic, political, and social order, created through the trial-and-error process, was enormously strengthened by the argumentation from the philosophy of science, known as *growth-of-knowledge theory,* that emerged from works of Hayek, but also Michael Polanyi and Thomas Kuhn. In a nutshell, it is based on the well argued thesis that the *possibilities of articulating knowledge are limited.* The knowledge we are able to articulate is only a fraction of the knowledge we possess. However, we are able to *use* the inarticulate part of our knowledge in our own actions.

These seemingly abstract concepts have extremely important consequences for economic theory and policy. For it is precisely the consequences of the existence of the inarticulate, *tacit* knowledge that result in the relatively much worse outcomes of the privatization 'from above' *vis-à-vis* the privatization 'from below'. And such outcome may happen regardless of the competence and diligence of officials involved in the former. In the light of the growth-of-knowledge theory, officials, no matter how knowledgeable, are at a very serious disadvantage due to the very limited ability to use the inarticulate knowledge that other participants in the economy possess. While private producers use both their articulate and inarticulate knowledge in their everyday market endeavors, officials have to depend primarily on the articulate knowledge passed on through bureaucratic channels. If they use inarticulate knowledge, it is only their own and their closest collaborators. In comparison with the inarticulate knowledge encapsulated in market decisions of thousands and often hundreds of thousands of private participants, their decisions of necessity are based on a dramatically smaller pool of knowledge (the point is best explained in Lavoie 1985).

It should be kept in mind, though, that Hayek's theory of the spontaneous order is a *general* explanation, holding true for *every* country and its officials who are condemned, for the above-explained reasons, to the relatively ineffective economic decisions *vis-à-vis* those taken by market participants.

Let me add yet another argument. They not only apply more limited knowledge than dispersed market participants but also undertake decisions for which they bear no financial responsibility. This latter argument from the property rights theory points to the fact that those who bear financial responsibility for their actions not only use knowledge more efficiently but also do it in a more responsible manner, in a sense that they are constrained by a threat of a loss. By contrast, politicians and bureaucrats, whose actions – in case of a loss – shift its costs on the taxpayers of their country, are much more prone to follow their whims or ideological preferences, regardless of the economic sense.

But the foregoing Hayekian and property rights considerations may be used to explain the variety of state actions around the globe: the superiority of the privatization 'from below' over that 'from above' in post-communist countries in transition, as well as, say, high probability of failure of 'sophisticated' industrial policies in mature Western economies. It says nothing about consequences of the particular weaknesses of a post-communist state.

The generally recognized low organizational capability of the inherited state, its inefficient and corrupt administration, all this should be taken into consideration in the design and implementation of transition programs. The several dozen years of communist centralism has to a large extent extinguished in the people any feeling of responsibility. At the same time, the arbitrariness in the decision-making, as well as the lack of any really observed 'rules of the game' by the ruling stratum, have gravely damaged ethical standards, not only among administrators (see Szymanderski and Winiecki 1996). Under such circumstances political liberalization must have resulted in *increased* corruption. For the fear of the secret police disappeared, while the *bourgeois* ethics, this cornerstone of the capitalist economy, has not been restored (Krasznai and Winiecki 1993 and 1995).

In his excellent essay about the state in the process of transition, Janos Kornai (1992) pointed out numerous weaknesses of the post-communist state. Apart from those already stressed, Kornai enumerated also the lack of political consensus, normally serving as the beacon of orientation, the feeling of uncertainty among the old bureaucracy and resultant servility, as well as the drain of the best people by the business sector. Another important determinant of the weakness of the state is the lack of experience of the judicial system in handling its new duties in the capitalist market economy (weak property rights' enforcement).

Kornai stressed the inconsistency between the weak, overloaded and corrupt state on the one hand and ever growing demands on the state to solve (and solve quickly) all the problems associated with the systemic change. The latter demands are far in excess of the state (meaning: its administration) capacity to fulfill. It was not without some irritation that this author asks all those demanding the state to intervene, whenever they do not like some developments, that regardless of the merits or demerits of the particular case they should be aware that it is precisely "that sort of the state on which they would devolve [all those] functions – and that for quite some time it would remain that sort of the state". In other words, rabid interventionists not only ignore the relative disadvantage of the state in taking decisions concerning economy that have been stressed for some decades by Hayek and other neo-Austrian thinkers and by property rights theorists, they also seem to be unaware that they demand action from the state that is not only disadvantaged in general, but also they demand it from the post-communist state that is at a much more severe disdvantage due to the legacy of communism.

From the foregoing analysis of weaknesses of the post-communist states (and lasting weaknesses at that) stem important conclusions concerning the role of the spontaneous order in transition to the capitalist market economy. The Hayekian approach suggests that economic processes regulated by the market should be given the largest possible extent of freedom in the post-communist transition. The Polish experience, where privatization has been stalled, while at the same time private sector has been growing at impressive rates, gives strong empirical support to the recommendation formulated in the preceding paragraph. The experience of other countries in the forefront of the transition to the capitalist market economy, where privatization 'from above' fared better, is also supportive of this recommendation.

Furthermore, wherever the state cannot renounce its obligations in the design (and sometimes also in implementation) of the exit strategy from the economic scene, its rules should allow the widest room for spontaneous developments *within* the newly established rules, so that decentralized decisions of the private agents, characterized by the superior knowledge base, supersede bureaucratic ones. This is, by the way, the principle followed by the Czech leadership with good results.

One *caveat* is in order here. The greatest possible room for spontaneous economic processes should not be seen as an encouragement for anarchy. The spontaneous economic processes should be given room within the broad, liberal institutional framework (the already mentioned Hayekian 'general rules') that mean a modicum of political stability, relatively stable money and macroeconomic framework, strongly protected property rights, relatively efficient law enforcement, etc.

All those who think that the near-disappearance of the basic functions of the state in some post-communist countries such as Russia augurs the emergence of the much desired limited state and will bring about great economic prosperity as a result (see, e.g., Bell 1996) seriously misunderstand the nature of the problem. The state should be limited in its functions but these functions should be implemented swiftly and efficiently. The efficiency of such a small state is dependent on the existence of certain preconditions such as political acceptance of the system, proper attitudes toward law and law enforcement, a moral order supportive of the free economy. Only then the state can remain small (in terms of the share of resources it takes away from citizens in the form of taxes) and at the same time efficient.

If these preconditions are not fulfilled even to a minimum degree, we see the Hobbesian anarchy that in the particular post-communist context is translated into mafia-like redistributive coalitions that instead of using the Olsonian "logic of collective action" (Olson 1965, 1980) use guns and explosives in their corruptive and extortive activities. The foregoing sharply reduces the incentives for normal citizens to exploit the opportunities given by economic freedom. The potential of the spontaneous order is employed to an extremely limited degree.

Threats to spontaneous processes from incomplete transition: effects of political retrogression

Our considerations have until now been rather optimistic. Regardless of the failure of privatization of state-owned enterprises, of zig-zags in macroeconomic policies, and – no less importantly – of the apparent political instability, the Polish transition to the economy dominated by the private sector has proceeded apace. Poland has been in the lead in terms of economic recovery and rapid growth among post-communist countries. Political retrogression and policies eroding the direction of economic change have turned out to be relatively unimportant.

It is an all important question, however, whether this happy state of affairs may continue indefinitely. As it has been stressed already, spontaneous processes need a conducive environment to succeed. Without it, they begin to degenerate. This is, what – with a time lag, of course – may affect Polish transition. The relative unimportance of harmful state actions is an encouraging feature of Polish transition but only for the time being.

The failed privatization 'from above', coupled with the apparent unwillingness of the successive governments to tackle the problem of labour-dominated state enterprises, may have serious consequences for further expansion of the generic private sector, this real engine of growth of the Polish economy (see recently Mickiewicz 1995). A large majority of state enterprises have not yet been privatized. Many large firms continue to hobble on, without much profit, but pay high wages, while at the same time they do not pay taxes, social security contributions, and do not pay their suppliers and creditors.

The recent law on privatization and commercialization (1996) reveals the design of the ex-communist coalition to maintain a large public sector (a couple of thousands of commercialized state companies!) through the so-called 'commercialization for other purposes than privatization'. These designs are a serious threat for the Polish economy for more than one reason.

Firstly, the existence of a large number of inefficient state firms for an indefinite period is in itself a drag on the national economy. Such firms generate much less value added than alternative uses of resources employed by them would generate. Therefore, the dynamism of the national economy suffers.

Secondly, the maintenance of the large pool of state firms opens widely the window of corruption. Cronyism and political patronage will reduce even further the already relatively low level of efficiency of these firms.

Thirdly, the large public enterprise sector creates a *black hole effect*, in the sense that they swallow resources that would otherwise be made available to more efficient private firms. Under the circumstances, the political clout of large state firms and their managers collusion with public officials, good money are continuously thrown after the bad. And all the more so, since the financial sector is still largely in the state hands and, as such, more amenable to the political rather than economic allocation of financial resources. This reduces the efficiency of the economy as a whole.

Fourthly, aggregate level of subsidies of various sorts flowing to the politically strong public enterprise sector is a constant threat for macroeconomic stability. If these firms cannot survive on their own during the period of high economic growth – and after more than 7 years since the start of transition! – there is a danger that their political clout may become very dangerous for the state budget in adverse economic circumstances.

The present writer believes in the inherent resilience of the private sector and in its ability to shield itself from the worst consequences of governmental policies in spontaneous reactions to state attempts to dominate and control. However, if too much effort is expended on various defensive actions, its fundamental role as the prime generator of wealth will attract less and less attention, while socially inefficient but personally efficient wealth shifting attracts more. We should be aware of the fact that the lessons from both positive and negative aspects of the Polish experience are widely applicable elsewhere in the post-communist world in transition (more on Polish institutional problems under the present circumstances in Winiecki 1996).

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