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Economics

Post-Communist Capitalism and the Modern World of Dead Economy

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ABSTRACT. After the collapse of the Communist regimes and their command economies, the countries of the former Soviet Union found themselves with only a very small amount of goods to supply to the global market. There was no way that they *could* have existed in an economy of this type that is nothing more than a corpse or a so-called "necroeconomy." As international experience shows, dead firms do exist and "successfully" function in the most developed of economies as well, with Japan being the most obvious example. These insolvent and, in fact, bankrupt firms which continue to operate despite their "mortality" are commonly referred to as "zombie-firms." *© 2009 Bull. Georg. Natl. Acad. Sci.*

Key words: *Post-Communist Capitalism, necroeconomy, zombie-economy, financial crisis.*

Almost twenty years have passed since the beginning of the period of post-Communist transition to a market economy. Naturally, this has resulted in the accumulation of a rather rich experience overall and one which allows us to make some generalisations. It may be asserted that market economies as such have been established in almost all of the countries of the former Socialist bloc with the period of transition over and the individual newly-independent states having passed through this period with varying degrees of success.

Some of the countries were so successful within their movement towards a market economy that they achieved EU membership [1] whereas others - in fact, all of the post-Soviet nations with the exception of the Baltic states - became "prisoners" of their own product, that is, post-Communist capitalism [2] which is a very special phenomenon of modern times and which includes in itself a wide range of different forms of capitalism [3, 4].

The purpose of this paper is to distinguish the various economic foundations of post-Communist capitalism and to examine the key economic problems of the dead economy.

What is a Necroeconomy?

In order to understand the essence of the economic foundations of post-Communist capitalism, one has to analyse one of the key peculiarities of a command economy; that is, the quality of its material and technical bases.

It is common knowledge that a command economy excludes any possibility for the existence of any forms of competitive relationships either domestically or internationally—inside any distinct economy or between different command economies—owing to its very nature. The majority of command economies used to be integrated into one big common economic space. The former Council of Mutual Economic Assistance, which existed for approximately 40 years and was governed by a co-ordinating organ, is perhaps the best example of this. Economic co-operation with market economies was maintained upon a very limited basis and exclusively at an inter-governmental level.

The absence of competition in command economies quashed the only effective stimulus for economic development. As a result, the quality of products, as a rule, was very low—as were their prices—which were maintained artificially by means of national budgetary subsidies. The key sources of the former Soviet Union's national budget revenues included the sales of alcoholic beverages and the export of raw materials (basically those of oil) which represented the only stable channel for the accumulation of foreign currency reserves.

Based upon the studies and generalisations of key aspects of the economic system of the Communist regime in Poland, Adam Lipowski came to a conclusion that when the whole world was divided between the "developed" and the "developing" countries, those with command economies could not qualify for either of the foregoing and so he invented the term of "misdeveloped" countries specifically for command economies [5: 9]. In such cases of "misdevelopment," Lipowski asserted that:

- the share of industries in GDP was too high because of a low percentage of domestic and foreign trade and services,
- a significant portion of industrial production accounted for manufacturing production as opposed to the comparatively small output of consumer goods,
- the volume of high quality competitive products capable of meeting international standards was very limited,
- the major part of industrial output included goods which were generally useless to customers and
- the share of outdated products in industrial output was too high.

After the collapse of the Communist regimes and their command economies, the countries of the former Soviet Union found themselves with only a very small amount of goods to supply to the global market. With few exceptions, such as some hydro energy outputs, oil and gas extraction and the primary processing of raw materials, the goods they manufactured failed to meet the high international standards as a result of their overall low quality and/or high prices. In fact, no markets existed for these particular products. Moreover, in principle, there was no way that they *could* have existed in an economy of this type that is nothing more than a corpse or a so-called "necroeconomy" [6] or, similarly, a "virtual economy" [7]. The economic theory which deals with this kind of economy is called "necroeconomic theory" or "necroeconomics" [2, 8].

Lipowski uses the term "divesting" (as an antonym to "investing") in order to describe the process of a command economy's being "stripped" [9], which amounts to "liberating" the post-Communist economy from the list of pathologies characterising a "misdeveloped economy" [5: 31-32] which, in our opinion, is the way in which a necroeconomy develops.

Naturally, even if one part of an economy is dead, the rest of it may still be alive which can be referred to as its "vital economy" or "vitaeconomy." Further accordingly, the economic theory which deals with this kind of economy is called "vitaeconomic theory" or "vitaeconomics." By its substance, this is nothing more than economic theory itself—or economics in its common meaning—because economic theory as such is something which deals with the economy as a vital system.

Collectively, all of the aforementioned leads us to the question: What does necroeconomy have in common with vitaeconomy and how do they differ?

In a necroeconomy, like in a vitaeconomy, some goods may be produced which in fact means that *supply* may exist. In contrast to those goods produced in a vitaeconomy, however, those emanating from a necroeconomy are in a situation of no *demand* owing to their low quality and/or high prices. Consequently, a necroeconomy *excludes any reasonable act of sale and purchase and, as a result—equilibrium prices*.

If any segment of an economy is dead, then theoretically there should be no problems within. Common sense tells us that a necroeconomy cannot have any influence over its vital parts. Under the conditions of a market economy, economic theory prescribes that uncompetitive productions must disappear and, at the same time, should not create any significant problems for the rest of economy. This explains the limited focus from the side of economic theory upon the problems of such a post-Communist market economy in which necrocompanies do exist.

Specifically, in the countries which are still undergoing the process of post-Communist transformation—as well as those in which post-Communist capitalism has already been established—*necroeconomy has grown on top of the roots of the command economy's material and technical bases.* We can conclude, therefore, that the necroeconomy is *exactly* that which differentiates the economy of post-Communist capitalism from all other models of capitalism.

The economy of post-Communist capitalism consists of the following groups of necroeconomy and vitaeconomy:

Group 1. Necroeconomy in the public sector
Group 2. Vitaeconomy in the public sector
Group 3. Privatised necroeconomy
Group 4. Privatised vitaeconomy

Group 5. Vitaeconomy developed by means of new private investments.

The majority of the first group, as a rule, consists of large- and medium-size processing industry enterprises which, depending upon the types of goods they produce, are labelled "strategic" ones even though they are dead under the conditions of a market economy owing to their low or lack of competitive powers.

On the other hand, enterprises within the energy sector (first of all, electricity generation and transmission and the extraction and distribution of oil and gas), as well as those of transport and communications constitute a basis for the vitaeconomy in the public sector. When privatised, they move to the fourth group comprising the privatised vitaeconomy which may also include some medium "although mostly small-size industrial enterprises (prior to their privatisation)".

The third group consists of the former first group enterprises following their privatisation. The change in ownership by itself does not automatically entail the restarting of formerly idle enterprises in that a "corpse's" status does not depend upon whether it is owned by the government or a private firm. *Disregarding this fact is the key reason that the process of privatisation has been relatively discredited.* Privatisation, especially during its initial phases—irrespective and taken separately of any investments—has often been believed to be a universal remedy capable of restarting any inoperable enterprise, dead or alive. As we will seek to demonstrate, the institute of private ownership alone is not able to create sufficient conditions for the abolition of necrofirms.

The fifth and last group embraces the "healthiest" segment of the post-Communist economy which is based upon the principles of a market economy maintained by private investments. Some problems, however, may be discovered herein as well which will require to be adequately addressed. In particular, this refers to some foreign investments by means of which post-Communist countries receive relatively old technologies which have become obsolete from the standpoint of modern international standards. In our opinion, these could be labelled as "second-hand investments" with goods manufactured by means of this capital only being competitive in "emerging markets" and only for a limited period of time until the arrival of highly competitive goods which meet all of the international standards.

What is a Zombie-Economy?

We have already stated that necrocompanies are found within the countries of post-Communist capitalism but the question arises of whether or not this is a problem confined to such countries in transition alone or if such enterprises also exist in developed and/or developing economies.

As international experience shows, dead firms do exist and "successfully" function in the most developed of economies as well, with Japan being the most obvious example [10]. These insolvent and, in fact, bankrupt firms which continue to operate despite their "mortality" are commonly referred to as "zombie-firms."

A system of continued lending is the key source of the sustainability of these zombie-firms [11, 12] with their loans granted by so-called "zombie-banks" which extend beneficial credits to the firms (in particular, interest rates for such loans are lower than average rates at the market level) [12, 13]. In full risk of stating the obvious, these unreasonable loans can only lead these banks to direct and inevitable losses [14: 368].

This, therefore, is the maintenance plan for zombie-firms but how, one may ask, do zombie-banks manage to survive under such circumstances? As a rule, such banks are backed by their country's governments [15: 301] which grant them all kinds of guarantees and assure their deposits, amongst other things, which eventually means that zombie-banks exist at the expense of taxpayers [16: 164]. To a certain degree, such a financial system even encourages "healthy" firms to turn into zombies [10: 40].

As a result of the aforementioned relationships between zombie-firms, zombie-banks and their governments, a "zombie-economy," then, develops which becomes a heavy burden for the "healthy" segments of the economy. In particular, zombie-firms, by their mere existence—and which enjoy guaranteed beneficial loans from zombie-banks—block the emergence of new "healthy" firms in the market [10: 33] as they have to borrow at rather higher interest rates [17]. In addition, because of their access to guaranteed beneficial loans, zombie-firms, in their fight for market shares, are at liberty to drop prices [12: 288] and raise the salaries of their employees [10: 33]. The limited market access for "healthy" and, even more so, productive firms eventually leads to the reduced productivity of the whole economy [14: 364].

A zombie-economy takes its roots in times of a financial crisis [14, 17]. Under the conditions of stagnation, the economy becomes characterised by a stoppage of production and trade for a relatively long period of time which, in turn, gives rise to unemployment, a reduction in wages and salaries and the overall decline of the standard of living. During these times, governments, as a rule, are called to help the economy to overcome such difficult conditions through the provision of bailouts and other attempts at keeping the banking sector (to avoid a banking crisis) and the entire economy on the surface.

After the end of a financial crisis, the economy receives its own lifeless portion as a legacy of the difficulties and continues to try to preserve the old system of the government's financial aid which was readily available to it during the crisis. A zombie-economy, therefore, can be viewed as a legacy of a financial crisis.

It must be emphasised that a zombie-economy is a phenomenon peculiar not only to Japan and other developed market economies [18] but also to those countries with developing economies as international experience has shown [16].

Similarities and Differences between a Necroeconomy and a Zombie-Economy

One might have the impression that the terms necroeconomy and zombie-economy refer to one and the same phenomenon; that is, a dead economy which continues to subsist despite its lethal status. In fact, such an impression is both superficial and misleading in that whilst the two "economies" do indeed share one commonality—there is no doubt that they are both dead—there is a wide spectrum of significant differences between them.

First of all, both economies developed in essentially different economic systems. A necroeconomy grew forth from a command economy whilst a zombie-economy is the offspring of a market economy. Further, a necroecoomy, in fact, has nothing to do with a financial crisis whereas a zombie-economy is the immediate end result thereof. It is important to note once again that the existence of zombie-firms depends in the main upon zombie-banks whereas necroeconomic agents subsist by means of immediate and direct subsidies from national budgets or tax exemptions. Moreover, the differences between a necroeconomy and a zombie-economy have also a lot to do with the sectors within which are mostly directly and readily exposed to their influences.

A necroeconomy, therefore, generally expands to large- and medium-size manufacturing industries as opposed to zombie-firms which show no traces of existence therein as evidenced by the situation in Japan's economy [10]. Moreover, the large manufacturing enterprises in a post-Communist capitalist country, have the greater probability of becoming a part of a necroeconomy. On the other hand, as the same Japanese experience demonstrates, most large-size firms, due to their great financial powers, are not zombie-firms but may also often be encountered in those so-called small businesses which are relatively "larger" than others [10].

It is important to note that whilst all international financial institutions, such as the International Monetary Fund (IMF) and the World Bank, insist that the post-Communist capitalist governments eliminate all kinds of national budget subsidies and tax exemptions, all lobbying efforts are mobilised towards pushing those bailout programmes into providing some extensive financial support to the national governments in order to enable them to build up some favourable lending systems under the circumstances of the financial crisis [15: 288, 16: 163].

One may arrive at the conclusion, therefore, that necroeconomies and zombie-economies are related to each other but still differ to a great degree from each other as individual economic phenomena. Unfortunately, however, these differences are not always given due consideration. In some studies, the peculiarities of a necroeconomy are overlooked which means, as a result, that the problems of dead firms in the post-Communist countries (mostly China and Russia) are examined within the context of zombie-economies rather than necroeconomies [15: 300-301, 19: 126, 153, 20: 106-107].

Routine Mechanisms of a Necroeconomy and a Zombie-Economy

A key question with respect to a necroeconomy and a zombie-economy is what ensures their stable existence.

The answer may be found in an evolutionary theory of economic changes [21] wherein the key tool is the concept of "routine" which implies a certain set of rules and ways of a firm's conduct which regulates the reproduction (of such a conduct) [22].

It is this very routine, which has developed over a period of several decades upon the roots of a command economy, which pushes dead companies in the countries of post-Communist capitalism *to work in the no-longer-existing regime of a command economy.* Without any special governmental support, therefore, the warehouses of these companies become filled with uncompetitive goods for which there is neither demand nor market. Given the fact that as a matter of principle these goods cannot be sold to anyone, the companies find themselves further and further in arrears as regards wages, salaries and debts to national budgets, social funds, energy sector industries and other businesses which eventually creates a network of mutually indebted businesses [23: 244-248, 328-330, 333-334, 24: 132-133].

It was a long-established tradition in command economies that when an enterprise accumulated (often very deliberately) huge debts, its director raised the question before his country's superior governmental institutions (such as Communist Party governing bodies, the Gosplan, the Ministry of Finance, etc.) to write off those debts and, as a rule, such requests were usually granted. Consequently, because of the almost unlimited (or much rather guaranteed) opportunity to have one's own debts removed, enterprise managers did not regard debt accumulation as any kind of danger for their existence. Such a mechanism of off-writing of debts represented a firmly established routine which, however unfortunate it may have been, reappears over and over in the countries of post-Communist capitalism and within various forms such as "tax amnesties" [25, 26].

As for the routine of a zombie-economy, it develops under the conditions of financial crises wherein governments and banks collaborate with each other towards a common purpose of developing and implementing bail-out programmes for insolvent firms and, thereby, avoiding a greater economic decline and a further growth of unemployment. In the case of a relatively long period of stagnation, such collaboration grows into an established order which establishes the rules of a firm's conduct and, in turn, ensures the reproduction of such a conduct. In other words, the activities grow into a routine. Herein one must underline the continued character of stagnation which is a condition precedent for the formation of routine; that is, it must have enough time to develop.

When a financial crisis comes to an end, the routine undertakes the mission to ensure the subsistence of a zombie-economy. The reason is that under all other equal conditions, and irrespective of the crisis, no government would tolerate the growth of unemployment which comes as an inevitable result of the closing down of zombie-firms. Undoubtedly, "healthy" firms are never able to instantaneously react to the disappearance of zombie-firms and quickly address the problem of creating new jobs [17, 19: 235].

ეკონომიკა

პოსტკომუნისტური კაპიტალიზმი და მკვდარი ეკონომიკის თანამედროვე სამყარო

ვ. პაპავა

აკადემიის წევრი, პ. გუგუშვილის ეკონომიკის ინსტიტუტი, თბილისი

კომუნისტური რეჟიმისა და მბრძანებლური ეკონომიკის ნგრევის შემდეგ ყოფილ საბჭოთა ქვეყნებს მსოფლიო ბაზრებზე კონკურენტუნარიანი საქონლის მხოლოდ მცირე ჯგუფის მიწოდება შეეძლოთ. ეს ქვეყნები ნეკროეკონომიკის არსებობის პრობლემის წინაშე დადგნენ.

როგორც საერთაშორისო გამოცდილება ადასტურებს, მკვდარი ფირმები "წარმატებით" ფუნქციონირებენ განვითარებული ეკონომიკის ქვეყნებშიც, და ამის საუკეთესო მაგალითი იაპონიაა. ეს გაკოტრებული ფირმები ქმნიან ზომბი-ეკონომიკის საფუძველს. თუ გასული საუკუნის 90-იან წლებში ზომბირების თემა ძირითადად მხოლოდ იაპონიის ეკონომიკასთან მიმართებაში განიხილებოდა, დღეს ზომბირების პრობლემა უკვე მსოფლიოს სხვა ქვეყნებსაც გადასწვდა.

მკვდარი ეკონომიკის ფუნქციონირება განპირობებულია სათანადო რუტინის არსებობით, რომლის ქვეშ ფირმის ქცევის ჩამოყალიბებული ის წესები და ხერხები იგულისხმება, რომლებიც ამ ფირმის მოქმედების აღწარმოებას არეგულირებს.

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