

Innovative Fiscal Policy and Economic Development in Transition Economies

Aleksandr V. Gevorkyan



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Innovative Fiscal Policy and Economic Development in Transition Economies

This book explores the problems of fiscal policy as an instrument of economic and social development in the modern environment, primarily focusing on the transition economies of Eastern Europe, Caucasus, and Central Asia. Evaluating the transformational experience in these countries, this work meets a need for a critical analysis, in the aftermath of the 1990s market liberalization reforms, of current trends and outlines the roadmap for future development.

Influenced by market reforms in the immediate post-Soviet era, abrupt fiscal withdrawal from the economy led to a diverse mix of financial, industrial, and social problems. Today, two decades on, the transition economies have grown new structures and established a new, unique development model. This book directly addresses these issues. Combining rigorous analytical discussion with solid statistical examination, the author undertakes a full macroeconomic review of the CIS economies through the present day, including analysis of trade and fiscal balance relations, fiscal policy sustainability, alternative sovereign finance and sovereign debt, aspects of labor market, exchange rate dynamics, a critical evaluation of the current crisis, and the future outlook.

The novelty of this study is in its multifaceted analysis of the global theme of policy for development, pioneering ideas of fiscal net and offering pragmatic post-crisis scenarios and policy solutions with emphasis on fiscal action. Given its rounded approach, the book is of particular use to scholars, students, researchers, and practitioners interested in economic policy and development.

Aleksandr V. Gevorkyan is an Economist at Capco, a global financial consulting firm. Dr. Gevorkyan also teaches a range of financial economics and economic development topics at New York University and St. John's University. He has also taught in the graduate programs at The New School and MBA concentration at Long Island University. He holds a Ph.D. in Economics from The New School for Social Research, New York.

Foreword

The twentieth century was the period of grand transformations on economic, social, and political scales. This multifaceted book builds on the legacy of one of the most profound such transformations of the time: the transition from the socialist society and planned economy to a capitalist market-oriented economy in Central and Eastern Europe and the Former Soviet Union. The imposed shock therapy, at the beginning of the transformation process in the 1990s, led to a large output loss. Then, quite quickly, the transformation process turned out to be more than just an economic transition and evolved into a fundamental shift in the social and economic paradigms of the involved societies, resulting in considerable income and wealth inequality.

This research in particular focuses on the public aspect of the transformation process and offers a novel systematic approach into the examination of all key elements involved in that historic shift. Methodological and theoretical approaches developed in this book are innovative, insightful, and foundational for future research. This study is one of the first of a few to address a number of issues specific to transition under a common heading and with a general focus on the role of policy in development. This has long-ranged implications for developed and developing economies alike.

Addressing transition economies' concerns requires analysis of history, recent economic experience, understanding of the local social content, and vision for the future development trend. This book does that successfully and goes far beyond existing earlier analysis of the difficulties of the transition economies, triggered by the "shock therapy" of the 1990s. It analyzes the current problems of these economies in perspective of the role of the state for future development. In particular, it studies the different impacts of public policy in general and fiscal policy, in particular in resource-based economies and less resource-based types of economies in the region. This has, as the research here shows, turned out to dominantly impact the transition path.

Based on that, the study offers several practical proposals. The book vociferously repositions the role of state in the development, preserving the crucial balance of fiscal involvement in the modern open economy and echoing recent calls for a more active state in the face of the global economic crisis. This is a laudable change of perspective as compared with the usual studies since the 1990s where market dynamics were given the leading role for development, with

the consequence, when implemented, of large welfare losses. There is a lot that can be learned from this new perspective. Studies in fiscal policy and development with strong aspects of social responsibility, especially with factors of inequality and poverty considered, are timely and are welcomed in the contemporary context of global economic transformation.

It should also be noted that some of this book's work has already been recognized in peer-reviewed journal and newspaper publications, presented in multidisciplinary conferences, and has found great attention by an international audience. In addition, some of the book's analytical conclusions have been successfully integrated and applied in courses on macroeconomics, international economics, development, and finance. Overall, this volume is a major contribution to the literature on economic and social development, growth, and the important role of policy for the dynamics of the development of interlinked economies.

Willi Semmler
Professor of Economics, The New School for Social Research, New York, NY

Preface

Economic theories hold a strong sway over the shape and direction of policy making, changing the course of history of entire nations, often within a short time. Perhaps no other countries' experience in recent history serves as a true testimony to the statement as much as the experience of the nations of Central and Eastern Europe (CEE) and of the Former Soviet Union (FSU). The abrupt switch from the socialist system to the capitalist one in the early 1990s was to inspire quick and positive tendencies in terms of economic growth and overall development. This, however, did not occur as had been expected.

In fact, the countries in question, religiously following the policy proposals based on contemporary economic theory, faced long periods of economic decline, social distress, and political uncertainty. The legacy of the more than twenty-year-old reforms is still alive and affects these countries' development prospects. Available evidence points to persistence of initial and post-reform structural problems in the economies of the FSU, while the countries of CEE struggle for closer integration within regional entities, such as the European Union, though far from parity (with exceptions of course).

These problems, and specifically the question of the role of state in the development process, are the true motivation behind this book. The underlying question of this work has been to identify the development path in transition economies and offer pragmatic proposals based on available international experience. The study itself is an outcome of several years of fieldwork and research on diverse topics in economic theory and policy, including open economy macroeconomics, labor migration, sovereign debt, and fiscal policy. The book looks at the great unknowns: economies of the Commonwealth of Independent States (CIS). The book sets fiscal policy as an amalgamation of visionary initiatives and proactive measures aimed at sustainable growth, betterment of social welfare, and development based on evidence and local context.

One advantage of this work—the larger portion of it was completed during and right after the initially worst phases of the late 2000s' global economic crisis—is that it carries a great deal of factual and topical insight. As a novel twist, the book points to the distinction between net exporter and net importer economies in the region. This categorization is integral to understanding the transition dynamics and CIS experience in particular. During initial research and

early drafts of this book, it became obvious that the current crisis impacts, though delayed, were necessarily individual in each country group, based on a unique set of crisis propagation channels.

The systematic analysis emphasized in this book correctly points to the fragile character of the current fiscal policy patterns in both net exporter and net importer economies. This allows for pragmatic policy proposals. The CIS economies, and with them other formerly socialist economies (especially of Southern/Eastern Europe), are uniquely positioned to locally adapt and apply policy measures tried elsewhere. This book calls attention to problems of alternative sovereign finance, fiscal net, exchange rate, international reserves, and issues of labor force and capital flows.

It was a great and insightful journey to work on this research. I would like to express my gratitude to all those people who supported and encouraged my work on this project. Especially I would like to express my sincerest gratitude to my adviser, co-author, and friend, Professor Willi Semmler of The New School. I am thankful for his intellectual support, expertise, wisdom, and mentorship, which inspired and motivated my work on this project. And I am certainly grateful to and would like to extend special appreciation and gratitude to my family. Their love, support, constant patience, devotion, and faith in me have been the foundation for my research work.

Aleksandr V. Gevorkyan
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