European Association of Evolutionary & Political Economy / EAEPE 2001
Thirteenth Annual Conference, Siena, Italy, 8-11 November 2001

POLITICAL CO-ORDINATION AND CORPORATE CONTROL OF ECONOMIC ACTIVITIES BY THE STATE

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Abstract:

In a period when the globalisation of the World is recognised by all, and systemic problems are emerging on a global scale. A search for systemic solutions is on the agenda. This paper offers a critical in depth discussion of the political co-ordination in Central and Eastern Europe before 1989 implemented through the Central Plan, and compares this with other models of regulation of economic activities and administrative intervention. It builds on public administration theory and introduces a model that describes the network of administrative actors in the socialist economies before 1989 that engaged in political and economic decision making and policy implementation at macro level. The concept of 'political co-ordination' of economic activities is introduced, and it is argued that it represents more adequately the co-ordination and control mechanisms within the former Centrally Planned Economies.

A critical examination of the administrative links before 1989 reveals the dynamic system of negotiation and bargaining between firms and government agencies that took place in the past. The uncertainty of outcomes of these former negotiation practices is compared with other practices of public administration and management in developed market economies. The regulation by the state is interpreted as one of the main structuration factors that affects the fundamentals of transactions and institutional relations within a particular socio-economic system. The paper attempts to highlight the role of the institutional factor in co-ordination of economic activities under the Central Plan. Our critical analysis of this experience establishes foundations for the analysis of the public administration practices in developing countries and other social systems facing the challenge of industrialisation and market reform.

I. Introduction

The collapse of the Berlin Wall and the embarkment of the countries in Central and Eastern Europe on the path of transition initiated a wave of publications on the economic reforms implemented in each country, and the efforts of governments in the region to integrate these nations with the global economy. The sudden abandonment of the central planning mechanism, and the liberalisation of economic activities focused the attention of the academic community on the macro-economic transition reforms ignoring to a large extent the fundamentals of these economies, related to embedded co-ordination mechanisms and typical forms of division of labour and organisation of production. Exception from this trend in the literature is the work by Kornai (1992), Chavance (1994), Nove (1995), Poznanski (1995), who attempted to revise the academic view on the governance, co-ordination and political leadership of the socialist economies. Serious analysis of the transformation of public administration from a Central Plan to a regulated market economy is still overdue.

The crises in public administration of the socialist system under the Central Plan transformed into a systemic administrative failure during the transition. There are no doubts about the deep economic recession during the transition, and some of the factors that led to it, such as: the lack of clear criteria to distinguish between the potentially viable enterprises and the rest; the absence of well defined economic policies and national strategies for reconstruction; the operation of conflicting policy goals throughout the transition period; the lack of public experience in democracy (Kornaj, 1992, Chavance, 1994, Dobrinsky, 1996). At the same time, there are a number of assessments of the current systemic problems that are entirely speculative. Statements like the shortage of experienced and capable bureaucrats and enterprise managers, or the lack of proper institutional infrastructure (Frydman & Rapaczynski, 1994; Dobrinsky, 1996) are based primarily on personal observations, rather than on a systematic research. By institutional infrastructure it is meant merely financial institutions and controls. Public authorities are usually treated in the literature as constraints, rather than co-ordinating agencies. The field has failed to a large extent to incorporate the public administration theory, and to take into account that the fundamental change of the system requires a systemic approach to transforming government.

This paper attempts to throw some light on the complexity of embedded co-ordination mechanisms implemented within the socialist economies under the Central Plan, and the transformation of public administration during the transition. Our aim is to make more explicit the role of the institutional environment provided by the Central Plan to facilitate economic transactions, and how this practice of public administration relates to other practices of regulation and co-ordination of economic activities.

We suggest a model of the key institutions designing and implementing the Central Plan, and the administrative agents of the socialist system engaged in strategic and operational decision making (Fig. 1.). The model describes the administrative links between different economic agents in the past, including firms, government agencies, public and political organisations, and other stakeholders involved in the decision making process regarding economic planing at macro and micro level. The past ten years of transition reforms had proven that the business relationships, established within the communist economic model, are robust and difficult to change. The vertical and horizontal linkages between firms, established by the Central Plan, affected considerably the transition strategies. The relationship between various political actors involved in administrative decisions in the past continue to shape resource allocation. Our analysis of the political and economic bargaining between different actors within the central planning mechanism leads to a critical discussion of the barriers to transition towards a developed market economy.

II. The Theory of Public Administration and the Notion of Co-ordination Mechanisms

The public administration theory has acknowledged that the authoritative allocation of resources is central to human society (Russell & Waste, 1998). A clear distinction is made between allocation by authority and by bureaucracy. Social systems utilise different co-ordination mechanisms in order to govern and regulate the allocation of resources. As co-ordination mechanisms, the following are suggested: (1) bureaucratic co-ordination, (2) market co-ordination, (3) political co-ordination, (4) central planning and strategic allocation of resources, (5) self-governing co-ordination, (6) ethical co-ordination, and (7) family co-ordination (Kornai, 1992; Todeva, 2001). The theoretical analysis of these co-ordination mechanisms crosses over multiple disciplines such as: political economy, political system theory, public administration theory.

Among the many theoretical perspectives, there is a shared view that public administration is simultaneously governance of the society and economy within national boundaries, management of the resource allocation process, and institutionalisation of justice in the public domain, where public administrators are seen as agents carrying out the public interest with their authority (Wamsley, 1990, pp. 21-29). The leading public administration theories that aim to explain the functioning of public organisations, and the relationships that emerge in relation to the definition and fulfilment of public interests, are: the *public choice theory*; the *social contract theory*; the *managerial efficiency theory*; and the *principle-agent theory*.

The public choice theory supports the discussion of innovation vs. bureaucratic authoritative allocation of resources. It is assumed that bureaucratic government is based on command and hierarchy, while the innovation in government implies experimentation and the working of a 'free market' (Russell & Waste, 1998). Critics of this juxtaposition emphasise that "the purpose of public organisation is the reduction of economic, social, and psychic suffering", and the enhancement of life opportunities for all societal members (LaPorte, 1971, p. 32). The choice, therefore between a free market, and administrative allocation of resources is a question of which means are more appropriate to certain chosen ends, and not a question of ideological choices. Central Planning, therefore, as a public choice is merely a form of administrative co-ordination of macro-economic activities, along with its costs and benefits to society.

The social contract theory emphasises the agreement between the public and the government as enacted through democratic elections. Government efficiency in fulfilment of the social contract is measured in terms of democratic accountability (Wilson, 1987). This ignores the fact, that evaluation of both policy objectives, and outcomes is conducted mainly by the elected officials, therefore the public is not capable to exercise an affective control over government regarding the extent of fulfilment of the contract. The fact that the public through general elections could change government, does not mean that the public could evaluate the true outcomes from the work of this government. The theory of social contract does not make clear who is the agency of real control over the policy process. Compliance with government rules and regulations is much wider observed behaviour, rather then effective public control. Public administrators never receive performance measurement (Selde, et.al., 1999), and their true accountability resides within the government hierarchy, and not within the public election system.

An uncontested ground for the social contract theory is the notion of reason and power in administrative action. It is the organisation theory, which looks at the individual, group, and organisational motives for certain behaviour and action. The implementation of the social contract, therefore is subject to the motivations and enactments by different social actors. Within organisation theory the behaviourism appears as complementary to the institutionalism, which focuses on the rules and other institutional constructs that produce social norms and subsequent behaviours (Russell & Waste, 1998). Institutions are necessary to change and maintain certain value preferences. However, the very preferences, motivations and commitments are very often an outcome of the policy process. Therefore, the political authority that shapes individual and organisational behaviour, is the leading agency of change and reform in the society. Simultaneously, humans are more motivated in environments where they have a greater choice and control (Katzell & Thompson, 1990; Rainey, 1993).

Political objectives, institutional constraints, and individual motivations seem to be intertwined into a tight node that drives the continuous policy process. The social contract, therefore, between the Government and the society implicitly requires the support of an appropriate institutional framework, political leadership, and widely spread legitimacy of the administrative agencies. The Central Plan implemented within the socialist economies in the past in this context could be defined as an institution that facilitates the implementation of political and economic objectives under the political leadership of the Communist Party. The evaluation of the efficiency of the Central Plan as a co-ordination mechanism, therefore, should be differentiated from the judgement over the political choice of objectives, established by the leading Party. A centralised planning by a large multinational corporation, for example, manages in some cases larger resources but is implemented in a different way, and pursues different objectives.

Every mission-driven government is established under a political leadership by a Party, and implies a top-down goal orientation and a centralised planning, where the implementation of the policy objectives is based on strict budget control over public finances. The efficiency of government is measured by the extent of achievement of policy objectives, compared to the costs of policy implementation, monitoring and control – whether it is related to market regulation, or to direct intervention in the economy through central planning. The implementation of political objectives involves building coalitions of agencies that bargain and negotiate between themselves certain outcomes, and exercising public influence on the allocation of resources. Even in market economies governments respond to demands by public organisations and free public associations. The negotiation and bargaining in Central Planning systems usually took place between administrators and government officials at different hierarchical levels.

Principle-agent theory advocates that the government is composed of elected officials as ‘principles’, and appointed administrators as ‘agents’. Issues of accountability, communications and interactions between ‘principles’ and ‘agents’, as well as the role of political incentives and information asymmetries in decision making are discussed within this theoretical perspective. Researchers are convinced that the policy choices of the 'principles' are 'framed' by the information provided by appointed and entrusted administrators, alongside with the bureaucratic discretion of the latter (Hill, 1985; Bendor, 1990; Selden, et. al., 1999). Authors conclude that change of policy direction by the 'principles' is constrained by the monitoring and control costs, associated with a particular structure of principle-agent relationships. The real 'brokers' of public interests appear to be the bureaucratic 'agents', rather than the democratically elected 'principles'. The concept of the Central Plan illustrates well the principle-agent relationship, where it is recognised that 'principles' and 'agents' are complementary in managing the economy at macro-level. The notion of regulation is replaced by the notion of direct intervention by the state in the context of total public ownership of assets and collective responsibilities in the decision-making. In comparison, the governance of a market economy is based on the same functioning of principle-agent relationship, but assumes different accountability and control mechanisms, and the protection of private interests above the public ones. This is justified with the belief that the protection of private interests in the long term is in public interest, as it leads to wealth creation and the infinite improvement of the quality of life among other positive outcomes.

The ideological context of free democratic elections prompt the assumption that the public has a true means of control of the entire policy process – from the setting of objectives, to the evaluation of government performance, where information is easily accessible and there is a complete transparency of the working of government. This of course is debatable both for public democracies and for systems based on the constitutional leadership of the Communist Party, such as the socialist system. In the context where one political party assumes total control and responsibility over the policy process, the role of government is defined in a different way. The Chinese Government, for example, identifies five leading roles for itself: 1. promoter of growth, 2. manager of the economy, 3. distributor of income, 4. regulator of industry, and 5. protector of citizen and business (Liou, 1998). This by no means contradicts the present role of government in a market economy. The differences are mainly in the means used by government to perform these roles. The Central Plan in the Chinese context, and in the context of Central and Eastern Europe is seen only as a means to achieve the objective of managing the economy on a macro-scale.

Some of the empirical questions of public administration theory are related to difficulties in identifying clearly the leading institutions that represent the foundations of government, the agencies engaged in decision making and resource allocation within given institutional framework, and the 'customers', or all groups of society that are affected by distributive decisions. There are also normative questions, related to the proper definition of the public interest, and the role prescribed to and played by the public agencies. Both types of questions are important in order to analyse the working of a social system. While the normative questions are related to political choices, the empirical questions derive from the implementation process, and focus on the actual working of government.

Questions regarding decision making in public administration have both empirical and normative value. There is an uncritical acceptance of decisions as morally neutral and empirically self-evident. Organizational analysis employs the essentially technicist idea of decisions being totally divorced from the moral questions of the good. Decision-based analysis is usually trivialized, and questions of power and influence are neglected altogether (Harmon, 1998). Not only generalised political decisions regarding the establishment of fundamental co-ordination mechanisms, but specific administrative decisions on allocation of resources involve substantial negotiation and a subsequent administrative control. Weber (1978) stresses that domination is the probability that certain specific commands will be obeyed by a given group of persons. Domination may be based on the most diverse motives of compliance. Domination may be exercised at both stages of decision-making and decision implementation, or throughout the entire political process. Decisions in public administration can not be divorced from the process, where interests are recognised, motives are enacted, and outcomes are negotiated. By their nature decisions include negotiation and contestability. The legitimacy of the decision-making authority and the administrative capabilities of government officials to enact decisions is of crucial importance. Under the Central Plan the decision making process is much closer to scientific management, than in any other system. The reasoning is supported by rational calculations of resource flows, and justified with political aims. In a market economy regulatory decisions are also justified with political objectives. However they are supported with evaluation of the macro-economic environment assuming wider margins of errors and flexibility within the market to absorb the fluctuations of demand and supply. The implementation of these decisions though is fundamentally different between the two systems. In this paper we continue with a more detailed analysis of the co-ordination of this process within centrally planned economies.

Another string of research in public administration is lead by the historical question of the decline of civilisations and crisis in government. Daley's research (1998) reveals that behind the declines and revivals of the Roman Empire stand the questions of 1. Organizational legitimacy of the leading institutions, 2. Ability of government to resist corruption, 3. Organizational abilities to implement political decisions, and 4. Effective leadership of the policy process. In our analysis of the functioning of the Central Plan we address some of these questions in order to highlight the contradictions that undermine this co-ordination mechanism, and how the tensions within the system grew to a situation of crisis in legitimacy and undermined capabilities of government.

It is clear that administrative reforms, market oriented or otherwise, are not neutral. Changing the rules of the game by governments changes the probable winners and losers in political contests, and pre-determines who would be disenfranchised in this process (Knott & Miller, 1987; Russell & Waste, 1998). Governments are the managers of a reform process, and their political choices pre-select the outcomes from this reform process. Both the decisions and their implementation and negotiation are politically biased, and therefore not rational by their nature. Many social equity outcomes involve the distribution of benefits to those with few assets. Re-distributive decisions are often contested and require negotiation with some social groups. This process takes place in both market and centrally planned economies. Our analysis though reveals how the allocation of resources under the Central Plan fails to achieve its political objectives.

The costs of the public administration process accumulate from: the efforts to negotiate and take political decisions; the monitoring and control of policy implementation; the costs of termination of policies, the costs of institution building and support, and the general costs of administration and management (Frantz, 1997, Greenwood, 1997). For the centrally planned economies the benefits from the Central Planning mechanism could not outweight the costs of monitoring and control and the costs of failure to meet the set of targets, and this lead to accumulation of economic inefficiencies and the subsequent collaps of the system.

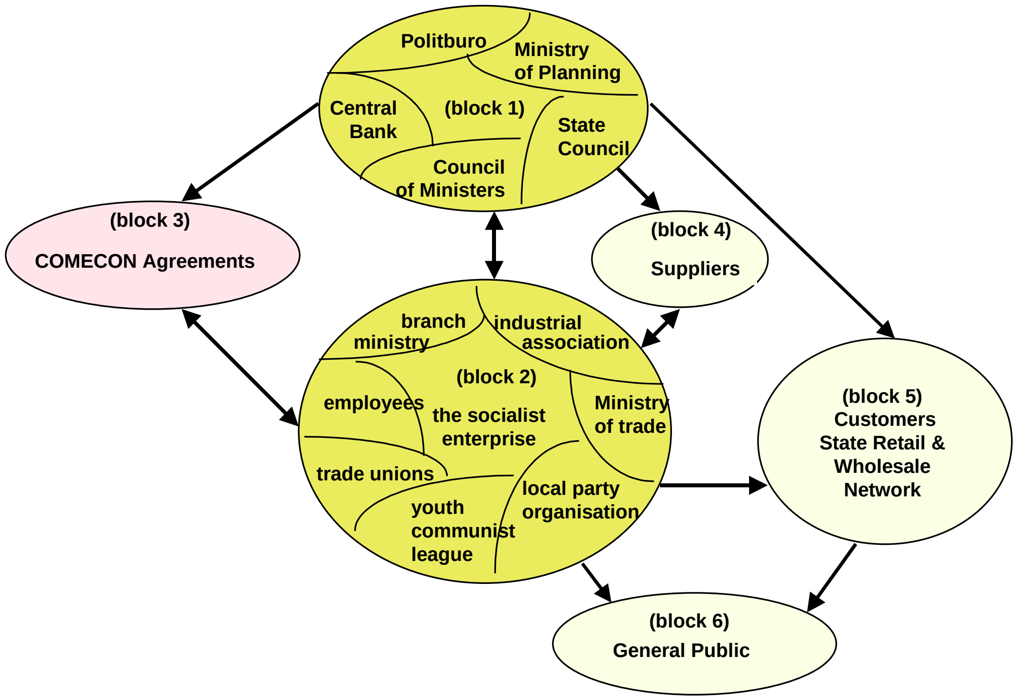
III. Administrative and Political Co-ordination of the Centrally Planned Economies

All institutions and co-ordination mechanisms, used by the socialist system, were embedded in what Marx called the central allocation of socialist labour. Socialism eliminated both private ownership of the means of production and the anarchy of the market, and created a space within the social milieu of an organisation on the scale of the entire national economy. The main tools for co-ordination of activities in this organisation were the Annual and the Five-year Central Plans. The allocation of resources by the Central Plan facilitated division of labour by both economic and social criteria (i.e. types of economic units, distribution of economic activities, labour opportunities, regional participation in production and in distribution of social and economic benefits) (Weber, 1978 on division of labour). The social criteria of division of labour conflicted very often with the technical criteria, i.e. location of inputs (including labour), access to capital, progression of inputs through the value chain, and location of markets. This very fact created enormous economic inefficiencies within the system.

The state institutions controlling the process in most countries were: the State Planning Office (usually Ministry of Planning); the Central Plan itself (endorsed by the Central Committee of the Party); the Central Government (including the State Council and the Council of Ministers), the Politburo (setting aims and giving instructions to all other government agencies), the Parliament (to enact the Plan), the Central Bank (to co-ordinate the monetary transactions and non-monetary payments between firms (see also Jeffries, 1995). The planning methodology was based on a complex set of criteria aiming at an equilibrium both at the aggregate level of the national economy and at the subordinate levels of ministries, industrial associations, and firms. The process of implementation involved a systematic disaggregation, further calculations, and interpretations of the ‘tasks’ set in the Central Plan.

This implementation was based mainly on a downward flow of information, and the Central Plan had obligatory status as a command rather than a recommendation. The process involved a number of institutions engaged in continuous re-negotiations of targets and tasks (see Figure 1.). For example, it would be a practice for influential managers of large firms and industrial associations to negotiate at Ministry level a ‘better deal’ for their firm, altering both input quotas and output targets. This would happen either before the Plan was finalised, or even after its endorsement. The ‘correction’ of the Plan could be enacted through a decision by the State Council and the Council of Ministers (both controlled by Politburo). Here the Politburo is the ‘principle’, while all other government institutions represent appointed ‘agencies’. The ‘principle’ exerts mainly political control in relation to the implementation of political objectives. Efficiency of the rest of the government institutions is assumed. Political objectives are uncontested assuming they are in the public interest. There is no need for a social contract as the relationships between the Government, the political leadership and the public are constitutionally set.

Fig. 1: ***Administrative Network of the Centrally Planed Economies***



Usually the reports of the implementation of the Plan would follow the same vertical line of subordination and, in the process of their aggregation, the accuracy would be traded-off for a demonstration of compliance by all economic actors. The horizontal links of information exchange and negotiations between Branch Ministries and Industrial Associations normally would focus on issues of resources and quantities, rather than strategic investment, improvement and development (Kornai, 1992).

It has to be mentioned, that the decisions related to the Central Plan were affected by and shifted away from economic targets not only because of the operation of the formally responsible institutions, but also because of the patronage relationships and informal political networks of individuals (Willerton, 1992). Figure 1. describes the network of administrative relationships between the key economic actors within the socialist system, including their autonomy and subordination in the decision-making process. Parallel to these formal administrative relationships, powerful political networks of individuals were used for introducing new agenda and for altering strategic investment decisions in regard to international projects within COMECON, or regional development programs. Both sets of relationships executed the governance of the centrally planned economies.

The co-ordination of the economy used to take place at two main levels – the level of leading governing institutions (Fig. 1., block 1), and the agents within the enterprise system (Fig. 1., block 2).

****	Governance Structure (block 1)***

The main aim of the State Plan was to develop 'quantitative macro-economic goals for the economy as a whole', and to break them down to Branch Ministries and to individual firms (Chavance, 1994). The institutions involved in the process of formulation of these macro-economic goals are presented in (Fig. 1., block 1.), and are labelled 'governance structure'. They were empowered to set up economic targets, to design the governance mechanisms and procedures for achievement of these targets, and to establish the necessary institutional framework for monitoring and control of the performance of all economic agents. There were variations in each Eastern European Country of the responsibilities within the governance structure. However, the main principles of the Central Plan remained the same.

The governance structure comprised of five interdependent agencies: 1) *Politburo* and *The Central Committee* of the ruling Party (defining the political aims and objectives for development and supervision of the performance of all other institutions), 2) *Ministry of Planning* (responsible for the design and co-ordination of the Plan), 3) *State Council* (issuing normative documents that facilitate the implementation of the Plan), 4) *Council of Ministers* (responsible for the implementation of the Plan in individual sectors of the economy), and 5) *The Central Bank* (facilitating the financing of economic activity and recording information about the economic transactions between firms). *The Parliament* usually played an insignificant role in endorsement of decisions already made by the other mentioned above actors. The political control and supervision of the entire process was conducted by the Party apparatus, who was empowered to make value judgements and *'recommendations'* in the form of instructions for action.

Neubauer and Demb (1993) quote Kester (1991, p. 10) for his definition of "governance system" which broadly implies the entire set of *incentives*, *safeguards,* and *dispute resolution processes* that are used to control and co-ordinate the actions of various self-interested parties (i.e. stakeholders) interacting in a bilateral and multilateral exchange relationship. All monetary and non-monetary means for co-ordination and control of the economic activities were in the hands of the political elite (Politburo and the Central Committee of the Communist Party) and the state administration (State Council, Council of Ministers, Ministry of Planning, and the Central Bank). Incentives and safeguards were imbedded in the Central Plan indicators, and were subject to implementation by the Branch Ministries and Industrial Associations.

The power for decision making and allocation of resources was concentrated within a vigorously selected elite, formed by political and managerial apparatus. The resolve to retain power by these individuals was determined by the high prestige and the range of material privileges in their hands. The coercion used by the Party organs to maintain Party and state discipline produced a specific pattern of conformity among all administrative actors. In spite of the intensive monitoring of personal conduct, the lack of transparency within the authority relations allowed abuse of power at all levels.

Janos Kornai (1992, 1997) provides one of the most comprehensive analysis of the socialist system, discussing the construction of power relations and the ‘cohesion’ between *political leadership* (through ideology), *administrative governance* (through state apparatus and enterprise management), and the *mass public organisations* employed to support the political leadership. In his work, Kornai shows the ‘interweaving’ between the administrative state and the ruling Party, and the significant impact that this had on the mechanisms for allocation of resources, as well as allocation of economic and political responsibilities. The amalgamation of ideology, power, privileges, and coercion in the past produced a unique decision making pattern applied across the whole system.

The State Plan indicators transmitted from the ‘governance structure’ to the ‘enterprise system’ (block 2.) would provide all the instructions for companies (Chavance, 1994; Todeva, 1996). However, the Plan itself does not deliver safeguards, or formalised dispute resolution processes. These mechanisms for corporate governance had to be disembedded and interpreted from the plan indicators by the political and administrative apparatus at the level of the ‘socialist enterprise system’ (Fig. 1., block 2.). The political and economic actors at this level within and outside of the firm had the responsibilities and the authority to make strategic and operational decision, aiming at complete implementation of the Central Plan, and fulfilment of all pre-set targets.

Kornai (1992) points out that fundamental decisions for establishment of a firm, or its liquidation, for appointment, promotion and dismissal of managers, for allocation of products, materials and labour, for price setting and financial regulation, for investment and technical development, for foreign trade and international economic relations - all were made entirely by the bureaucratic apparatus, primarily located outside of the firm – Branch Ministry and Industrial Association. The socialist firm in the middle of block 2., along with its employees, was treated merely as a production unit, interlinked with other production units in the economy.

****	Management of the Enterprise System Under the Central Plan (block 2)***

The aggregate indicators determined by the governance structure included ‘*production sector goals’* and ‘*mandatory targets’* for different sectors of the economy. There were different numbers of intermediaries involved in the process of disaggregation of these State Plan indicators into quantified figures for the operation of the firms. The intermediary institutions, such as Branch Ministries, Industrial Associations, representative departments from the Ministry of Trade, responsible for the supply links of each company (including imports, exports, and realisation of the product on the market), would overlook industrial sectors at national level, and would allocate specific targets and resources to individual firms. In this way, they were in charge of the operation management of all enterprises and, as Chavance described them, they “supervised all aspects of the Production Plan: the supply and turnover of goods, the determination of prices, the wage fund, and relations with financial agencies” (Chavance, 1994, p. 13). The industrial policy under the Central Plan resembled industry management based on administrative and mandatory decisions, very often ill-informed regarding real demand and availability of resources.

The implementation of industrial policies took place at the level of the enterprise, or as Hirschhausen and Hui (1995) defined it, within the 'socialist industrial unit' as networked in a set of economic and political relations driven by political objectives and 'scriptural flows', or 'scriptural money' transfers. Scriptural money, according to Hirschhausen and Hui (1995, p. 422), is "...nothing but an accounting unit for balancing the Plan".

If we look at the individual firm itself, it was intertwined with political organisations that played a variety of roles in the company decision making process. In the model in Fig. 1. they are listed as elements of the socialist enterprise (block 2): the regional and the firm based Communist Party organisations (engaged in direct supervision of economic decisions), the company branch and the regional branch of Youth Communist League (usually involved in career development and promotion), the company branch and the regional branch of the Trade Unions (responsible among others for the implementation of managerial decisions), and the employees with their limited influence mainly through consultations at the level of supervisory management.

It was a common practice of the socialist system for the nomenclature from a 'superior' body to intervene directly in the decision making of an 'inferior' to it structure, without following procedures. This situation of a bureaucratic agent that overrides the formal rules, demonstrates how the bureaucratic structure within the central planning mechanism was undermined by the superior authority, and by the informal practices established among individuals.

The enactment of the Central Plan and the implementation of its targets was supported by a flow of administrative decisions, which framed the relationships between firms. The operational management of firms was highly influenced by group interests within the enterprise and its immediate environment, rather than by economic rationality. The strong personal ties that the enterprise director usually maintained (both internally and externally with suppliers and political organisations) to secure the performance and the position of the firm, were essential ingredients consolidating the system.

IV. Governing Economic and Administrative Relationships within the Centrally Planned Economies

The governance and management of the economy under the Central Plan produced a set of relationships between firms, Industrial Associations, and other government agencies unique, for the system. A thorough analysis of these relationships reveals the complexity of national and international resource links that were administered by the ruling elite. Among the main actors interlinked by the Central Plan, are suppliers, retailers, and customers, foreign partners within the COMECON, and individual citizens as employees and 'owners' of the public assets.

* *Relationships With COMECON[1] Partners (block 3)*

Most of the international trade took place within the framework of the *Council for Mutual Economic Assistance* (COMECON). Contracts were signed in Soviet Rubbles and the same principles of specialisation at macro level and elimination of competition between partner countries were applied. Decisions for business transactions between enterprises were negotiated at Government level (Jeffries, 1993), and strategic decisions for co-operation were made outside of the firm.

At firm level an intensive technical know-how exchange would occur directly between partner companies, linked into international business networks within COMECON. These international partnerships did not expose the inefficiency of individual firms and did not provide incentives for development. They were managed by socialist governments, which made efforts to co-operate and to eliminate competition. The governments tampered internal inefficiencies by using price adjustments and extended investment packages for the operation of strategically significant projects. Firms were encouraged to increase asset specificity in order to match the demand stemming from long-term contracts.

The economic relationships within COMECON gradually built an international network of interlinked firms in targeted sectors throughout the region. Projects were based on national and international supplies. The supplier market both nationally and within COMECON was dominated by administrative and political decisions justified with political objectives.

* *Relationships With Suppliers (block 4)*

The firm relationships with suppliers were pre-determined by the governing structure (block 1), and the intermediary organisations (block 2). In the context of limited resources, frequent disruption of the supply chain, and lack of alternative suppliers, a specific type of protective managerial behaviour evolved - overstocking and hoarding inventory, and establishing informal horizontal relationships with suppliers to secure privileged transactions. This was an ‘alternative’ strategy applied by managers, aiming to protect company performance from supply disruptions and failures of the main co-ordination mechanism – the centralised allocation of resources (see also Chavance, 1992). The suppliers themselves were interlinked with other firms in the economy through the plan indicators. Disruptions and difficulties at supply level had a multiplied negative effect on the economy beyond the individual firms, which was a specific form of administrative failure under the Central Plan.

Both relationships with suppliers and customers were based on projected demand and supply and were directed by the Central Plan. Errors in these projections accumulated throughout the economy and reflected as deficit of certain goods and oversupply of others, which affected all other market relationships.

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[1] Council for Mutual Economic Assistance, established in 1949, with full members – The Soviet Union, Bulgaria, Czechoslovakia, Hungary, Poland, Romania, GDR (1950), Mongolia (1962), Cuba (1972), Vietnam (1978).

****	Relationships With Customers (block 5)***

The link between the firm and its customers in most cases was broken both by the behaviour of the state-owned retailers, and by the lack of market information accessible to the firm. There was no regular information about the extent to which firm's products satisfy real demand, and therefore there was no pressure on firms to improve their products and to extend their product range. Only few large enterprises would have retail outlets of their own, where they would have direct contact with their customers. Most often even in these cases the enterprise management would not collect systematically information from their customers. All quantities, the quality, and the product range would be pre-determined by the Central Plan indicators, and the state retail network would take the output and relocate it throughout the national retail chains to satisfy the 'needs' of abstract customers.

The distribution of final products and services could not satisfy the real demand, and as a result of that the retail sector developed various forms of mis-functional behaviour, such as privileged sales to preferential customers. This was one of the most dissatisfying outcomes from the central planning, that undermined the confidence in the system, and the legitimacy of the institutions involved in its working. The retail sector under the Central Plan was neither able to satisfy the demand for certain goods or services, nor equipped and capable to pass adequate information regarding customer needs, preferences and choices.

****	Relationships with the Public (block 6)***

The general public remained isolated from the process of social control, and therefore could not signal in any way that its needs have not been met, or its interests have been damaged. The system that was designed with the most humanistic values - to serve the interests of its citizens - failed to recognise that the public needs evolve, and can not be framed only as mass consumption.

The contradictions in the system of rules before 1989 derived from different organisations and state administrative departments - all 'sharing' responsibilities for supervision of the firm. While the concepts of the public interests would be heavily used in political discourse to justify decisions about allocation of resources, these public interests were rarely met. There was no institutional framework in which the public could have expressed its opinion. There were no public organisations employed to make government bodies accountable. Effectively there were no institutions empowered to exercise public control over the design and implementation of the Central Plan, and the co-ordination of the social and economic activities. The democratic centralism as a concept of political ideology and public administration facilitated centralised economic decisions by collective bodies who share collective responsibilities.

The existing bodies for public administration comprised of the political elite who were engaged in resource allocation, but were not directly accountable for their decisions. Public organisations such as Trade Unions, that were supposed to represent collective interests, were directly engaged in political control on behalf of the ruling elite.

V. Conclusions

The Central Plan played a fundamental co-ordination role in Central and Eastern Europe, and its sudden abolishment lead to the collapse of a number of economic linkages between firms. Weak governments obstructed the successful replacement of the Plan with a deregulated market. Contradictory and reversal policies and a subsequent information vacuum surrounded enterprise activities after the withdrawal of the state from direct co-ordination. These political choices for the transition were made much more with ideological considerations - to secure irreversibility of the transition processes, rather than in fulfilment of economic objectives.

Some of the main contradictions within the governance structure and its negative impact on the economy under the Central Plan were: de-monetarisation of economic trasactions and de-capitalisation of firms; replacement of economic with political objectives, allowing flexibility of negotiation and bargaining over the economic criteria of performance (soft budget constraints); externalised control and decision making combined with political coercion.

The model in Fig. 1 resembles broadly the system of all stakeholders, or what Neubauer & Demb (1993) describe as: a) the providers of funds and the Government (integrated in an interdependent network of institutions); b) the employees (assimilated within the enterprise system - a process facilitated by the subservient Trade Unions and other political organisations operating in the enterprise); c) customers and suppliers (centrally allocated to enterprises by the governing structure); d) the general public, whose needs were satisfied through a centralised distributive network, and whose behaviour was highly manipulated by the local political organisations.

It is clear that only the political and administrative elite involved in allocation of resources and supervision had any bargaining power under the Central Plan. The rest of the stakeholders - employees, customers, suppliers, and the general public had no say on the management of assets, or to express an opinion on any other more fundamental issue related to the co-ordination and control of economic activities.

The chronic delays of supplies had to be absorbed by the firm and not to show an effect on performance. This made enterprises significantly dependent on their inputs, and restricted further their autonomy on decisions about quality and quantity of output. As their outputs were allocated to distribution networks, firms were isolated from their market. The allocation of resources and outputs, institutionalised through the Central Plan, restricted not only the competition in the economy, but also the choices of firms for access to alternative suppliers.

The model of corporate decision-making, presented in Fig. 1., raises the question of identifying the insiders. There are two groups that possess crucial information about the company - those within the firm with tacit knowledge about the products and the production processes, and those outside the enterprise with detailed information and knowledge about markets, resource suppliers, and buyers. This had a fundamental impact on the privatisation of firms during the transition, which was controlled by the new political and administrative elite mainly from outside the firm.

The problem of information supply is indicated by the links shown on Fig. 1. In the past the enterprise would share information with all institutions closely linked with it - Branch Ministry, Trade Unions, local Party organisation and the rest. However, each of these institutions were able to withhold information to strengthen its position in negotiations with the firm. The information links with suppliers and customers would follow the pattern of predetermined exchanges and therefore would not pass any signals about the changes in demand and the customer response.

Once the communication infrastructure of the Plan was withdrawn after the collapse of the system in 1989-90, all communication links between the individual blocks of the system disappeared. Governments could not honour any longer COMECON agreements. Enterprises lost allocation of suppliers or customers. Firms lost information of the demand for their product, or, due to the economic recession, the demand dropped dramatically for many sectors of the economy. What the socialist countries faced was a bunch of discoordinated government agencies and disoriented firms in an information vacuum. The Central Plan was the main source of market information for state firms that was relevant to business decisions.

The collapse of the central planning mechanism brought an array of new administration and management costs to individual firms that increased the severity of their financial situation. The collapse of both the internal and the COMECON markets restricted the revenue options for the firms. At the same time, the managerial functions performed by the Central Planning authorities in the past had to be reconstructed at the enterprise level independently, which raised the administrative costs. In this context, the abolition of structures and procedures of the central planning system could be interpreted not merely as part of the reform process, but also as a destruction of the economic infrastructure that supported market linkages. The State Plan centralised not only decision making power, but also managerial costs for a number of crucial operational decisions about resources and supplies. The sudden collapse of the Plan created a regulatory vacuum for the enterprises.

The fact that is ignored from the current academic analysis, is that even in an ideal market economy the ‘spontaneous’ business transactions occur in an environment organised by rules, and all players are usually informed about these rules. With the collapse of the State Central Plan in Eastern Europe, the *‘administrative failure’* was associated with the inability of governments to determine the appropriate rules, to communicate them to autonomous businesses in an appropriate way, and to control how these rules are implemented. The speed of the fundamental changes in co-ordination of economic activities also was a barrier to governments to design reform programmes and to acquire the necessary public support.

The neo-liberal economic policies imposed by the World Bank in parallel with loansafter 1989 had a mixed positive and negative effect on the national economies in Central and Eastern Europe, and stretched their administrative capabilities. The privatisation targets shifted attention to ownership rights, rather than to economic restructuring and change of co-ordination mechanisms.

The economic actors and their relationships described in Fig. 1. underwent significant transformation during the transition period. While this paper aimed to describe their role within the system of centrally planed economies, it is important to investigate how these economic and political agents have changed their power position during the transition. Most of the political organisations during the transition period disengaged from the enterprise activities with the exception of alternative trade unions involved in the system of collective bargaining. Most of the intermediary organisations, such as industrial associations, were transformed into autonomous economic agents, which reduced the influence of the central Government.

The failure of the administrative system during the transition is manifested in its inability to provide incentives for restructuring, to exercise control over the dysfunctional behaviour of individual managers, or to obtain adequate feedback about the implications and effectiveness of specific reform policies. The reform of the system of public administration proved to be the most difficult and neglected task of the transition, where further political efforts and research are in need.

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