

I. (60%) Short Descriptions: 20 of 22 (3% each)

- 1) Ayatollah Khomeini: *the spiritual leader (Imam) of Iran's Shiite community and head of state of Iran's Islamic Republic after the 1978-79 revolution in which the Shah was deposed.*
- 2) Boris Yeltsin: *Russia's president during the transition, after the collapse of the Soviet Union. He was involved in violent conflict with the Congress of People's Deputies and presided over a dramatic economic collapse in spite of efforts to liberalize prices and foreign trade, and privatize state-owned firms.*
- 3) Chaebol: *Large conglomerate firms in South Korea, including Hyundai, Samsung, and LG, that came to dominate manufacturing and exports, due in large part to government policy and supported lending.*
- 4) Central Bank of Russia: *the successor to the Soviet Gosbank, the CBR was run by Gerashchenko, the "world's worst central banker." In 1995 it was made responsible for Ruble stability, and this helped to finally stabilize prices.*
- 5) Cultural Revolution: *The period in China from 1965-76 in which Chairman Mao Zedong organized young people into groups of "Red Guards" to attack any opponent of Mao, real or imagined, and destroy the "four olds." China became extremely conformist, millions were attacked and many killed, schools were shut down, and the economy stagnated until Mao died.*
- 6) Deadwood problem: *the danger of allowing market competition and bankruptcy for large inefficient firms in a socialist economy. Because bankruptcy was not imposed for decades, these firms became very inefficient. Allowing them all to suddenly go bankrupt can cause a severe recession that threatens even viable firms.*
- 7) Deng Xiaoping: *the paramount leader of China between 1978 and 1997, who led the reform effort after Mao. He pushed for reforms that included the Open Door Policy, Special Economic Zones, the Household Responsibility System, and ultimately the Socialist Market Economy.*
- 8) Great Leap Forward: *A movement launched by Chairman Mao to go beyond Soviet methods and push China rapidly into the industrial age, with backyard iron smelters, huge rural communes with communal kitchens, extraction of the agricultural surplus for urban industry, and a belief that rapid change was possible through new ideas and the application of immense amounts of labor. The policies were very misguided, and the leadership was kept misinformed. The result was a catastrophic famine, and Mao stepped back from direct leadership in the early 1960s.*
- 9) Household Responsibility System: *The major rural reform after Deng became China's paramount leader, in which rural areas were effectively decollectivized and land was allocated to families for a fixed quota or rent. Farmers had much more control over what and how they produced and they could sell any surplus at higher market prices. This led to a rapid increase in productivity.*
- 10) Islamic Banking: *a system of banking which gets around the Koranic riba prohibition on interest. The most common systems are mudarabah, a method of profit-sharing, and murabaha markup method.*
- 11) Jawaharlal Nehru: *India's first prime minister through 1964 and leader of the Congress (I) Party. He followed policies promoting political democracy, secular nationalism, self-reliance and import-substitution, indicative planning, and state licensing of private firms to limit monopoly power.*
- 12) Mao Zedong: *the chairman of China's communist party until 1976 and leader of China's 1949 revolution. Under Mao, China switched from a Soviet-style five year plan to the Great Leap Forward and the Cultural Revolution.*
- 13) Market Socialism: *a system in which state ownership is combined with market allocation methods. Lange's model of trial and error pricing was one approach which had many contradictions, while Yugoslavia's labor-managed economy was another approach.*
- 14) Matyas Rakosi: *the leader of the Hungarian Socialist Workers Party, who used "salami tactics" to eliminate his enemies one at a time after the second world war. His opposition to Nagy's reforms helped to create the 1956 Hungarian uprising.*
- 15) Mohammed Mossadeq: *Prime Minister of Iran during the 1950s, who attempted to nationalize foreign oil firms and was overthrown by the CIA. American intervention led to simmering resentment among many Iranians.*
- 16) New Course: *Imre Nagy's first policy of reform prior to the Hungarian revolt, which ended forced collectivization and reduced the Stalinist priority given to producer goods.*

17) Perfection of Control: *Kornai's phrase for the basic type of reform in socialist economies, which involves improvements in planning, changes in planners' preferences, adjustment to state prices, organizational changes, and moving the "spotlight" in the belief that these things can fix its inherent and inevitable contradictions and inefficiencies.*

18) Prague Spring: *the reforms and events of 1968 in Czechoslovakia under Dubcek, which allowed workers to take over their unions and establish workers councils to run firms, allowed free speech and a free press, promoted foreign trade, and led to an invasion by the Warsaw Pact.*

19) Township and Village Enterprises: *Rural firms in China that were at least nominally owned by local governments. In the early 1980s the government would allow them greater freedoms over what and how they produced in an effort to employ some of China's rural surplus labor, and the result would be rapid growth, productivity improvements, investment, and exports.*

20) Two-tier Pricing: *The method China used to "grow out of the plan." First farmers and then state firms were expected to produce their planned quota at the state price, but any production surplus could be sold at higher market or above-quota prices without the quota being ratcheted up. While it offered opportunities for corruption, it also encouraged rapid growth and competition, and when the plan was eventually dismantled it had become largely irrelevant.*

21) Velvet Revolution: *Peaceful demonstrations in Czechoslovakia in the Fall of 1989 that led to the bloodless overthrow of the communist government. This was helped along by Gorbachev ending the Brezhnev Doctrine. Free elections were held, and the dissident Vaclav Havel became its first postsocialist president.*

22) Voucher Method: *An approach to privatizing state-owned firms, used in Russia and Czechoslovakia, in which the rights to purchase ownership is distributed widely among the population. While this sounds good in principle, it leads to a diffuse stock ownership which makes it very difficult to control managerial abuses.*

II. (40%) Short Essays: 4 of 5 (10% each).

- A. What was the significance of China's "Socialist Market Economy," and what policies did it initially entail? How did these policies change over time?

China's "Socialist Market Economy" (Shehuizhuyi Shichang Jingji), a new policy announced in 1992, was a major shift in China's stated economic objective. Prior to this reform was seen as a temporary stage on the road to socialism and communism, but suddenly a market economy – with the Chinese Communist Party in charge – was now the long-term goal. Initial policies included an efforts to improve state firm management through limited liability incorporatization and creation of stock markets, tax and fiscal reforms to stabilize the macroeconomy, simplification of exchange rates and adjustment of the Yuan to to match the black market rate, with eventual full convertibility of the current account, and the separation of state banks into commercial banks and policy banks. Initially, state firms were to be the "cornerstone" of the economy, but after Deng died in 1997 the government announced a policy to privatize many SOEs and consolidate the bigger ones.

- B. To what extent was India's economy after independence socialist, and how was it fundamentally and philosophically different from the classical socialist economy? What reforms were implemented after the assassination of Rajiv Gandhi?

Nehru was influenced by British "Fabian socialism" as well as Gandhi's belief in Swaraj, and he was impressed by Soviet planning. But he also favored small-scale appropriate technologies and democratic egalitarianism. The Indian Planning Commission established 5-year plans, but planning was indicative, not directive. Private industries were licensed and the size of private firms was limited by the "license Raj." While the government did create state enterprises and nationalize private firms, SOEs accounted for only a quarter of GDP at their peak, and government's share of the economy was much smaller than in economies like China or the USSR. After Rajiv Gandhi was shot in 1991, the new government applied for IMF loans to address their balance of payments problem, and began to reduce their budget deficit, devalue the Rupiah, reduce trade barriers, allow FDI, deregulate banking, and encourage private firms.

C. Compare and contrast Poland and Hungary in their approach to economic transition, and how their economies responded.

After the Roundtable talks and elections in which Solidarity took virtually every seat, Poland implemented the Balcerowicz Plan in 1990, the most rapid approach to shock therapy in all of eastern Europe. This included price liberalization, rapid privatization through public sales and “mass privatization,” rising FDI, trade with the EU, and macroeconomic stabilization. Poland’s economy declined dramatically, but was the first to recover and by 1995 it was the fastest-growing economy in Europe, though unemployment remained high. Hungary had already experienced several efforts at reform, and in 1988 implemented the Economic Stabilization and Structural Reform Program, a gradual approach to market liberalization, implementing western legal systems, tax and banking reforms, et cetera. After Antall become prime minister, gradual economic reforms continued, budget deficits grew along with unemployment and foreign debt, and privatization slowed. The economy continued to decline. Not until 1994, when Horn led the government, did Hungary launch an aggressive privatization and policies to promote exports and budget austerity did inflation slow, FDI increase, and the economy begin to grow.

D. How is economic transition different from reform, and what are the major components of a transition strategy?

Economic reform is usually an effort to make the socialist economy work better, while economic transition is the path taken when the socialist economy is intentionally abandoned. It usually happens after the collapse of the existing socialist government, providing the context of democratic liberalization and domestic turmoil. It requires price liberalization, privatization and the creation of conditions for the growth of new firms, legal reform, including such things as contract enforcement, tax reform so the government can get revenue without relying on the eroding profits of state firms, social reform, including the replacement of the state firm’s role in providing education, housing, medical care, and retirement, and, perhaps most importantly, macroeconomic stabilization though reduction of the budget deficit. Opening to foreign trade and investment is usually key to doing much of this.

E. Give a brief economic history of the two Koreas after the Korean war.

After the war, South Korea (the Republic of Korea) was one of the poorest countries in the world. The government of Rhee Syngman was corrupt and lacked popular support, but implemented land reform and import substitution policies in an unsuccessful effort to build their own industrial base. After a military coup in 1961, General Park Chung-hee led an authoritarian and interventionist government that promoted exports, reduced budget deficits, stabilized prices, and subsidized the creation of large chaebol conglomerates through preferential access to state-owned banking. The Economic Planning Board had effective control over government budgets and five-year plans, and there was minimal labor protection. South Korea relied on foreign borrowing through the 1980s, but grew enough to repay. After Demonstrations in 1987, the military returned power to an elected civilian government.

In the north, the Democratic People’s Republic of Korea was led by the “Great Leader” Kim Il-sung and the Korean Worker’s Party. Land reform was followed by full agricultural collectivization, nationalization of industry, central planning, bureaucratic management, forced savings, and high rates of investment in heavy industry and military. Kim followed a philosophy of “Juche” which emphasized isolation and self-reliance. North Korea started a little better off and grew fairly rapidly at first, but within a couple of decades it was surpassed by South Korea’s economy. After Gorbachev refused to continue to subsidize it, North Korean growth turned negative, shortages grew chronic, and famine hit. Under the “Dear Leader” Kim Jong-Il, North Korea has made some effort to implement Chinese-style reforms, without dramatic success, at least so far.

III. Bonus: (1% each).

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| 1. China – d | 5. Iran – i | 9. Germany – E |
| 2. Japan – z | 6. Russia – x | 10. Poland – N |
| 3. India – c | 7. France – C | 11. Czech Republic – M |
| 4. Korea – y | 8. Sweden – S | 12. Serbia – H |