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THE DYNAMICS OF ECONOMIC AND POLITICAL POWER IN THE FORMER
SOVIET UNION COUNTRIES

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LIST OF ABBREVIATIONS AND ACRONYMS

FSU-former Soviet Union

GDP-gross domestic product

IMP-International Monetary Fund

PPP-purchasing power parity

ABSTRACT

After the collapse of Soviet Union, the former Soviet Union countries entered the 'transitional period.' However, the former Soviet Union reality in terms of political and economic power interactions is something which can be discussed and explored via some models and estimations although some differences of the countries' path. This research takes a dynamic model developed by Daron Acemoglu and discusses it for the former Soviet Union countries taking the assumption that it is relevant for them as well as a hypothesis. Hence, according to this model political institutions and the distribution of resources are the state variables which determine economic and political institutions that, in their turn, determine economic performance and the further distribution of resources. Besides, it makes fixed effect panel estimation in order to find out whether the given framework is appropriate for the former Soviet Union. The estimation seeks correlation among Freedom house democracy index as the measure for the political institution; Gini coefficient index as the measure of distribution of resources and GDP level as the measure of economic performance. The following six FSU countries are examined: Armenia, Belarus, Kirgizstan, Russia, Ukraine, and Moldova. The research comes up with some findings which render that although democracy level is decreasing, but the inequality is still decreasing as well. Thus, using the given framework the research concludes that the further decrease in inequality will lead to democratization either through revolutionary or evolutionary developments. So, as a recommendation, the research calls the government of Republic of Armenia for further decrease in inequality by using both the means of International organizations and internal policies and providing consistent GDP growth.

INTRODUCTION

After the collapse of the Soviet Union, the countries that were the part of it had to find new ways of being adjusted in the new reality. They entered a new phase of development which is called ‘transitional period.’ Thus, they had to make decisions what kind of political or economic path to obtain. Although all the FSU countries initially intended to become democracies, not all of them have succeeded in this. However, the FSU countries had and still have some common features due to their common past in terms of political and economic identification. The commonality is both in the field of economic developments and economic path and in the field of political developments and political path. Moreover, it is obvious that there is an interaction between political and economic power in terms of distribution of resources and how they will be distributed. The ones who obtain political power have also economic power and vice versa. And the FSU reality is not an exception in this context.

Thus, this research is an attempt to discover the interaction between these two powers for the FSU reality. As a vantage point it takes a dynamic model developed by Daron Acemoglu et al. (2005a) and discusses the FSU reality through this framework. This model differentiates two types of variables: political and economic. Political variables are political institutions, de facto and de jure political power. Economic institutions are economic institutions, distribution of resources and economic performance. These two types of variables interact with and determine each other. Hence, in order to explore the FSU reality and discuss it within the theoretical perspective and within the model by Acemoglu, the following discussion is done. Firstly, the research discusses the FSU reality in the context of Acemoglu’s model. This part finds some evidence that renders the same correlations in the FSU as it is discussed in Acemoglu’s framework. Thus, it discusses the transitional period and the political and economic changes that have happened during this period. Besides, it

discusses how some economic policies have affected and begotten political changes and vice versa and how this evidence fits in Acemoglu's context. The second part discusses the economic policies that this or that FSU country carried out. It discusses two ways of reforms; gradualism and shock therapy. Then, this part presents Poland's experience of the shock therapy as the most successful one and Russian case of shock therapy as a failed one. It presents two cases of the countries that have obtained gradualism policy of implementing economic reforms. These two parts of the paper give the overall expression and the environment and path towards which the FSU countries move or have already reached. The paper presents the findings and analysis after this theoretical discussion and historical overview. The first part of the findings is based on the fixed effect panel estimation by Eview, which has been carried out for six FSU countries; Armenia, Russia, Ukraine, Moldova and Kirgizstan. However, in order to explore the dynamics of the given results and the revealed correlation, these results are also discussed in the context of Acemoglu's model and Kuznets curve. Taking all these results into account, some generalizations and concluding remarks are done. These generalizations and conclusions let us make some recommendations either and give some remarks on the policy implementation in Armenia.

Hence, the purpose of this study is firstly, to discuss the post-soviet reality and the environment where economic and political changes happened. Secondly, it provides a pretty general framework, which renders how different institutions and powers interact and determine the overall political-economic structures. In this context, it makes some predictions how implementing this or that economic policy may beget some political changes in the time dimension. Thus, this paper may become an interesting study for further research and discussions which will reveal the FSU politico-economic and social reality and come up with the most effective policies that may improve the current situation.

Thus, for the purposes of this paper the following hypothesis and the research questions are put.

Hypothesis: The modified dynamic structure of economic and political power by Daron Acemoglu is a relevant framework for exploring the former Soviet Union reality.

Research questions:

1. What is the relationship among the main variables in the model for the former Soviet Union countries?
 - a) Democracy score – measure for political institutions
 - b) Inequality – measure for distribution of resources
 - c) GDP – measure for economic performance
2. Which are the economic policies that will foster democratic structures in the former Soviet Union countries?

METHODOLOGY

The chosen methodology is combined one, because it uses both deductive and inductive methodology. As a theoretical framework it takes Daron Acemoglu's (2005a) dynamic model. This framework is enriched by the case studies from the FSU countries.

As a primary data the research conducts fixed effect panel estimation by Eview. The examined countries are Belarus, Armenia, Russia, Ukraine, Moldova, and Kirgizstan. The period of estimation is from 2001 to 2008. The data used is Freedom House democracy index (from 1 to 7, where 1 is perfect democracy and 7 is perfect non-democracy), Gini coefficient

(from 0 to 1, where 0 is perfect equality, 1 is perfect inequality) and GDP (Gross Domestic Product) level adjusted by PPP (purchasing power parity) in real terms.

The findings are discussed in the context of Kuznets curve (1955) and Acemoglu's framework (2005a), which provides the dynamics of the found correlations.

LITERATURE REVIEW

There is a lot of literature that concerns to the political economy and explores some relationships between political and economic variables. One of the popular theories that discusses the relationship between democracy and economic development and some social factor such as education is modernization hypothesis. So, according to this hypothesis (Papaioannou & Gregorios, 2008) economic and educational developments may beget democratization as a result. The point is that industrialize societies are quite complicated contracted which makes it difficult to govern from one centralized body. Second, the ruling elite may benefit from democracy and thus conduct some reforms that will bring to democratization. It may happen in the case when where it is in the interest of the elite to encourage democracy since it fosters human capital accumulation and minimizes the possibility of expropriation. Third, education fosters democracy through socializing and by shaping incentives for certain group. However, democracy creates weak incentives but it has a popular base, meanwhile oligarchy offers much stronger incentives for a very limited part of the population. As educated part of society reduces the costs of political participation it suggests that some significant part of the population will become engaged in the political process, which, in turn, will foster democracy. So, according to the reduced version of the

modernization hypothesis, democracy is more likely to become consolidated in developed and especially educated societies other things being equal.

In order to empirically estimate whether there is a relationship among democracy, economic freedoms and economic growth, Mueller & Peev (2009) have conducted a regression analysis for all FSU countries from 1994 to 2007. They examine the following causal chain among these three variables.

Democracy → Economic Freedom → Economic Growth

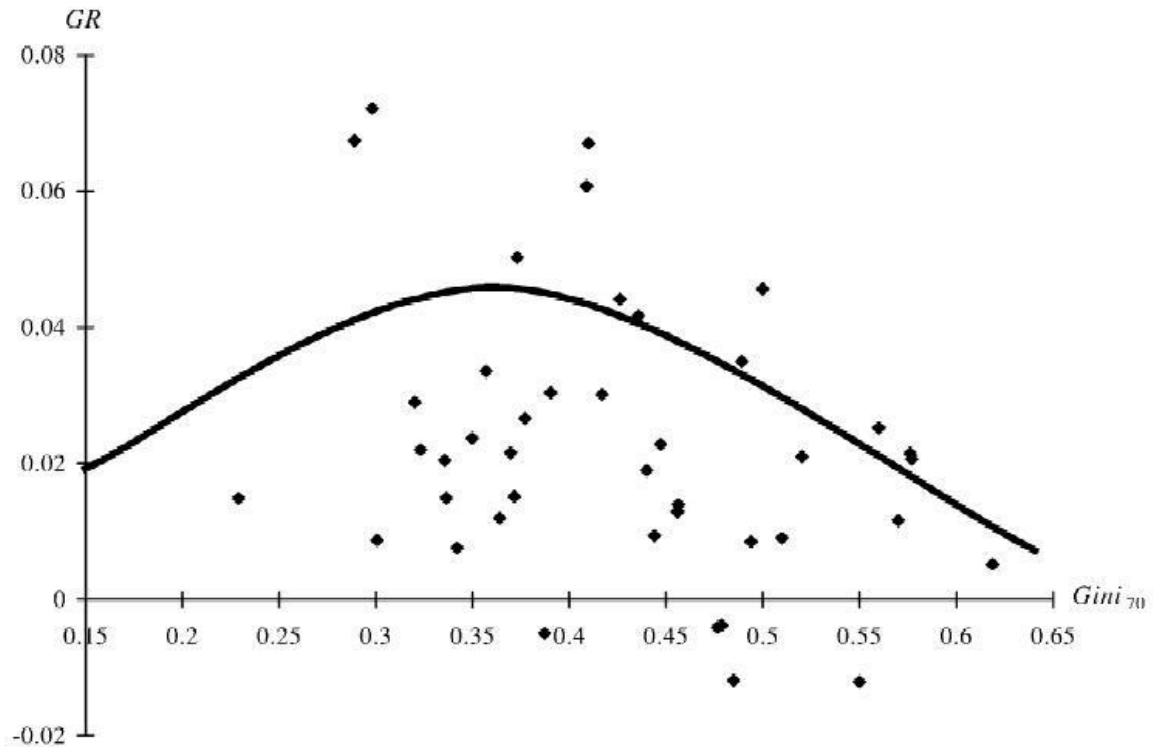
Thus, democracy is the independent variable that determines strong economic freedoms. Having strong economic freedoms, a FSU country obtains a more rapid economic growth. So, the regression analysis renders that there is a positive correlation between the country's democracy and its economic institutions. The FSU countries where strong democratic institutions prevail, economic freedoms are stronger and corruption is weaker. If the democratic institutions are defined and established well enough, voters demand less corruption and greater economic freedoms and politicians have to respond to these demands. This link between democracy and economic freedoms, in its turn, creates a link between economic freedom and economic growth, as liberal markets with competitiveness produce relatively more economic growth.

Another important issue is the correlation between economic growth and equality. The theory which examines the dynamic correlation between these two is developed by Simon Kuznets (1955). According to his model economic growth and inequality level are both negatively and positively correlated. His argument is the following: initially in the development path of the country, economic growth is positively correlated with inequality. It is the case, because the groups who make some savings and are able to invest are only the upper groups of the society. The proportion of the assets is highly concentrated in the hands of quite limited people. However, they invest their assets and provide economic growth.

Another reason how economic growth may foster inequality is urbanization and industrialization. The people, who initially are engaged in the agriculture, now lose their business providing income due to these industrialization and urbanization processes. The inequality increases, but the economic growth happens as well due to new technologies and new services. However, a stabilization period comes when the rapid industrialization and urbanization rates become more slowly and stabilized. Starting from this point on the inequality starts decreasing, as the government implements some social programmes such as education spreading and so on, since they may be the threat of social tensions. Thus, the decrease in inequality becomes essential to insure economic growth. Thus, Kuznets (1955) discusses an inverse U-shaped relationship between economic growth and inequality.

However, these theoretical assumptions are relevant according to the cross-country regression analysis carried out by Been-Lon Chen (2003) as it is illustrated in the figure 1. According to the results of the regression, the countries with initial small level of inequality may increase it in order to obtain long-run economic growth, while the countries that initially have bigger inequality should decrease it in order to obtain economic growth.

Figure 1: A Fitted Relationship between Initial Gini and Long-run Economic Growth



Source: Chen (2003)

THE DIFFERENT PATHS OF POLITICAL DEVELOPMENTS IN THE FSU REALITY

After the collapse of Soviet Union, each of Former Soviet Union countries adopted its path and policies towards political and economic development. Although it was initially expected that all the Former Soviet Union countries would move towards democracy in political terms and free market in economic terms and that these phenomena were considered inevitable, the history showed that the transitional period didn't necessarily bring to democracy or liberal market relations. Some of the FSU countries moved to democracy and economic liberalism and successfully overcame transitional period, some of them haven't

been able to overcome the transition and their future developments in political and economic sphere is not clear yet, and some of them have become authoritarian political system with concentrated and not-proportionally distributed economic power. Hence, what does transition mean and which are the results after the transition for the FSU countries? Transition in its broad sense means change of one political and economic structure by another. In its special meaning transition means change of authoritarian regimes by development path towards democracy (Carothers, 2002). However, not all the countries that intended to become democratic become so after transition and this was the case for former Soviet Union countries as well. The Ones among the most successful countries which were able to move towards democratic path are Baltic region states-Latvia, Lithuania and Estonia. The ones that failed to become democratic and it is already obvious that they have returned to authoritarian path are Uzbekistan, Kazakhstan, Tajikistan, Turkmenistan and Belarus. However, the development path of the most of the FSU countries is not salient yet. They are states that are neither dictatorial nor democratic. They have entered a political gray zone, as they have more or less developed democratic constitutions, regular elections and independent civil societies or other attributes of democracy, but still they suffer from real non-democratic phenomena such as absence of rule of law, low levels of public trust towards government, its legitimacy and all state institutions and so on (Carothers, 2002).

But which were the conditions and how some countries obtained this or that conditions? For instance, how did the Baltic States become relatively democratic and Central Asian states and Belarus become authoritarian? The new distribution of political power in Baltic states happened via 1989 and 1990 elections (McFaul, 2006). The *ancien regime* was challenged by new anti-communist power-Sajudis in Lithuania, the Latvian Popular Front and Latvian National Independence Movement in Latvia, and Estonian Popular Front in Estonia. All the three republics declared their independence after the elections in 1990. After

obtaining real independence, the societal actors which were committed to democratic values started to impose their will. However, some of the new leaders in these countries tried to impose some anti-liberal rules, but the possibility of integration in Western organizations such as the European Union and NATO, played a crucial role for their further democratic consolidation. Nevertheless, this path of development was not the case Central Asian countries. After the collapse of Soviet Union, these Central Asian countries didn't even declare their independence either in societal or state level. Some liberalization processes didn't occur after the elections in 1989 and 1990. And those who were and still are in power didn't have and don't have intentions of liberalizing the state. Civil society was and is weak in those states. Belarus also became authoritarian after some developments. First, the next leader of post-communist Belarus wasn't a democratic reformer, but a leader from within the last system. During the presidential elections in 1994, Alyaksandr Lukashenka an autocratic leader won the elections. The *ancien regime* leader became consolidated with Lukashenka's system and created an authoritarian regime in Belarus. The third path was adopted by the other FSU countries. These countries were wavering between democracy and dictatorship. These regimes were stuck in a twilight zone and it was seemed that they are stable in this political position. The other countries that have followed this or that development paths were stable and consistent as well. However, some changes occurred in some FSU countries during 2000s. The revolutionary political changes occurred in three FSU countries. Those countries were Georgia in 2003, Ukraine in 2004, and Kyrgyzstan in 2005, where relatively democratic processes occurred after revolutionary changes. Nevertheless, developments towards the opposite direction were in Russia. It moved towards more autocracy and somehow inspired other FSU countries to move towards this direction as well. The democratic changes happened in these three FSU countries had common features. First, the changes occurred through national elections and not through war or other shock events. The

changes were triggered by those who obtained the power and not by those who challenged it. Second, the challengers didn't seek a new political system, but they were trying to insure the real functioning of existing constitutional order. Third, the old ruler and new ones declared themselves as the authority of the same territory. Fourth, all these revolutionary changes occurred without the use of violence by either the state officials or the opposition leaders *ibid*. New situation and then new development path emerged in Russia. After coming to power in the spring of 2000, Vladimir Putin made sure that all factors that somehow may affect and encourage democratic developments became non-existing. He systematically weakened the democratic institutions thus abolishing the possible constraints that might limit Kremlin's power. Putin was successfully able to control some mass media means. He arbitrarily used his administrative power to jail some individuals who may have been potentially threat for him and his autocratic system. However, he was empowered to make this kind of changes due to Russian natural resource-oil, which was under his disposal (McFaul, 2006).

Trying to explore the nature of political transitions Acemoglu & Robinson (2001) consider the role and power of the poor in different political societies such as democracy and non-democracy. While democratic societies are able to impose high taxes on the rich, the poor are excluded from the politics, but they carry a revolutionary threat in non-democratic societies. However, the rich or the elite will try to prevent from the revolution by doing some reforms if the threat of the revolution is ahead. Thus, transition towards democracy is mainly possible by the threat of revolution. Hence, the cause of instability is inequality. If the country is democratic and there is a high degree of inequality, then the elite constantly contest for the power. If the country is non-democratic, then there are a lot of social unrests and revolutions are possible for the redistribution. Thus, the best condition for the democracy to become consolidated is equality.

This framework seems quite feasible in the context of FSU. After the collapse of Soviet Union, almost all newly emerged states practiced similar phenomena such as unsecured property rights, great corruption, inflation and so on (Frye, 2006). Thus, obviously high inequality and distributional gaps emerged in some of these countries. And although all these countries initially intended to become democratic countries, some of them passed away from this path and the democracies didn't become consolidated, because some of the interest groups became so powerful that they impeded the potential democratization on their own sake as it may primarily affect their political and economic power.

THE POSSIBLE REASONS OF DEMOCRATIZATION

Acemoglu & Robinson (2006c) make further research and try to find out the economic reasons for democracy and dictatorship in fundamental research. This model is constructed based on three assumptions.

1. It is "economic-based" meaning that it takes into consideration the individuals' preferences and interests.
2. There is a conflict among different groups, because different social groups have opposing interests over political outcomes.
3. The role of political institutions for solving the problem of commitment and thus affecting future distribution of de jure political power is central.

Hence, they (Acemoglu & Robinson, 2006c) construct a model which gives the explanation why the non-democratic elite becomes democratized. They define democracy as the conditions when free and fair elections are held and there are no barriers to entry into politics. Correspondingly, the non-democracy is the situation where a quite limited number of people or even just one person such as the elite, the dictator or so one run the country and

make decisions. From this perspective, it is understandable that democracy is more beneficial and desired by majority of the population, while non-democracy is beneficial to very limited number of people. Thus, the elite are reluctant to democracy, while majority of the population is for democracy and vice versa. But why in some cases do the elite make changes in the political institutions and follow the path of democratization and in some not? The elite make changes in political institutions, because they are threatened to lose their power. Since it is costly for the elite to survive and overcome riots and social unrests, they try to prevent it. Of course, they may go through another way and use repression to stop social unrests but not become democratized. However, repression may be even costlier than coming to the concession. But coming to the concession doesn't still mean that the elite will become democratized. However, the population will require democratization and not concession in many cases. The majority will require democratization, because they care about not only today but also about tomorrow. It is more about the regulation of the political power in future. The citizens should be insured that the changes will be consistent in the future as well. That's why they need change in the underlying institutions. Therefore, democratization is more likely when

a) The possibility of sufficient social unrest is high, and the concessions won't satisfy the citizens. It, in its turn, depends on the strength of civil society, the non-democratic conditions and so on.

b) When the costs of turning from non-democracy to democracy are not pretty high for the elite and the elite don't have a lot to lose from the institutional change.

As determinants of democracy they (Acemoglu & Robinson, 2006c) distinguish several factors. The first is civil society. When the citizens have solved their collective action problem and are well-organized, the threat of revolution is high, thus the future democratization is more possible as well. The second determinants are shocks and crises. As

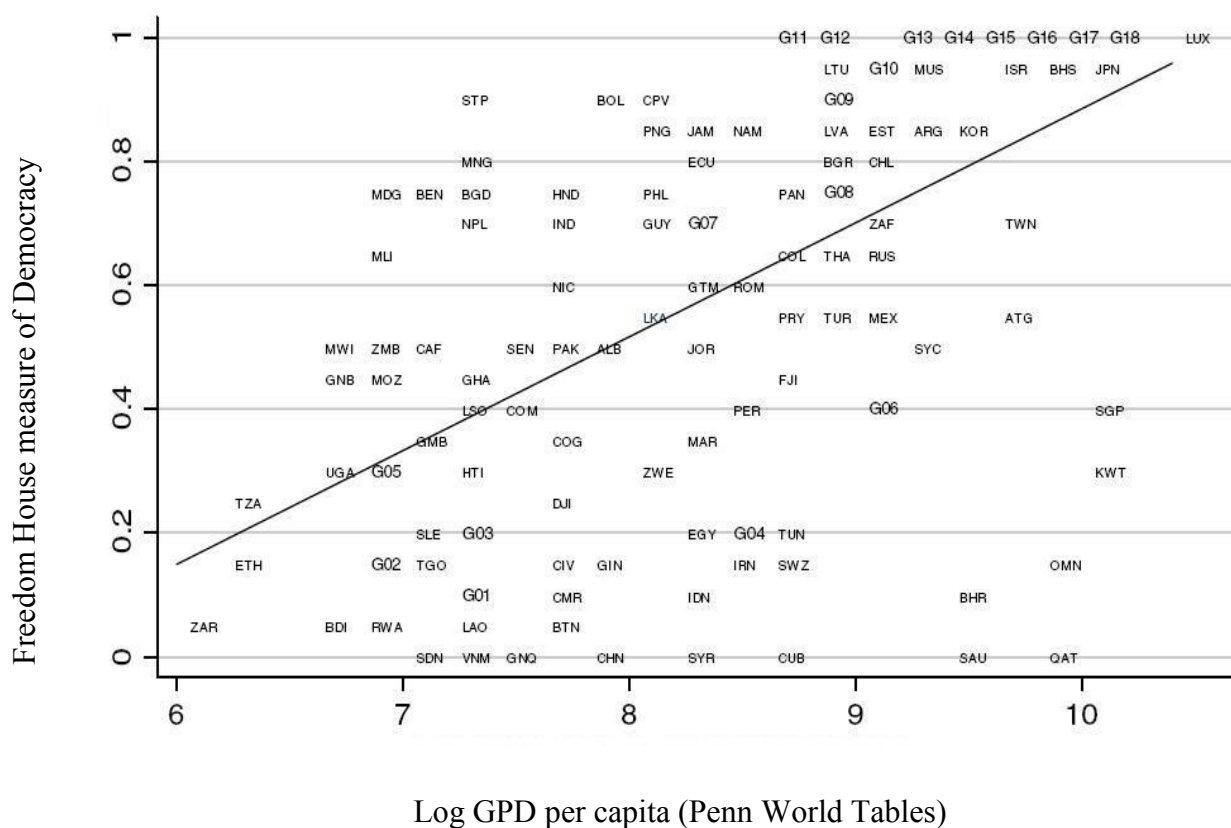
shock and crises may be considered economic depression, wars and so on. During this kind of period, it is easier to coordinate the opponents. Hence, they (Acemoglu & Robinson, 2006c) distinguish three possible development paths. The first path is the one which gradually but necessarily non-democracy turns into democracy. Once the democracy is created it is consolidated and safe. As the best illustration for this kind of development of democracy is Britain. Thus, Britain became democratic because its economy was based mainly on physical and human capital. As such assets are easily destroyable by a conflict; the elite couldn't make recession as it was pretty costly for them. Thus, they found the best solution to become democratized. However, these changes brought undesirable changes for the elite. The second one is when democracy is created, it doesn't become consolidated and collapse. By saying consolidated, they (Acemoglu & Robinson, 2006c) mean the set of institutions that persistent through time. The forces that have enforced democracy try to re-asset themselves, but democracy breaks down again, and the cycle repeats itself. The best illustration for this kind of developments is Argentina during the 20th century. Argentina became democratized because of some riots and revolts caused by economic and financial crisis. However, as Argentina's elite benefited from the boom in the world trade a lot, they value of losing it was much higher. And as the economy wasn't diversified well enough the elite were able to make converse changes in political institutions. The third path is when democracy is either not created at all, or its creation is much delayed. The reasons for such kind of development path are different. The countries don't turn into non-democratic to democratic ones, because the society is more or less egalitarian and people are satisfied by these institutions. Singapore may refer to such development path. In the second case, the opposite situation is there. The societies are so highly unequal and exploitative that the elite are afraid of democracy and institutional changes they try to keep away from such developments by all means. The illustration of this may serve some countries from South

Africa. The states of South Africa don't come to democracy, because the society is rather apartheid about the inequality and thus, it is relatively cheap for the elite to prevent riots and changes. After discussing all these paths of development and considering the underlying reasons for this or that kind of development, they (Acemoglu & Robinson, 2006c) try to do predictions about the future of democracy. Thus, they present several reasons why democracies will become consolidated. The first reason why democracies will become consolidated is that world practices and increasing importance of human capital rather than land or physical capital. The average citizen is relatively more educated nowadays than fifty years ago. So, the middle class will emerge thus facilitating distributional inequalities and stabilized democracies in higher extend. The second reason is globalization. The argument assumes that international economic and financial ties in terms of open markets will help the democracies to become more consolidated. And lastly, as the Cold War is over, the financial and political support that some non-democratic countries received doesn't make sense any more making these countries to become democratic easier. Thus, they (Acemoglu & Robinson, 2006c) come to the conclusion that democracy will become consolidated in the countries where it is not and non-democratic countries will turn to democratic path as well. Hence, this model can explain the political developments and emergence and not-emergence of democracy in FSU countries. As it is rendered by the evidence, the countries like Latvia, Lithuania and Estonia were able to consolidate democracy, because the interests groups and the civil society were quite strong and interested in creating and consolidating democracy. Thus, elite in these countries had to consolidate democracy despite their anti-democratic intentions. As contrast, the countries where the civil society was weak such as Turkmenistan, Uzbekistan and so on, the elite didn't commit to democracy, but became authoritarian. Coming to the question how changes happened, it is important to note that these changes are explainable via this model as well. Changes in Georgia and Ukraine happened because the elite committed to

leaving their offices as the possibility of taking power via social unrest and revolution was high. As contrast, as the civil society wasn't well developed in Russia and the stakes of turning to democracy were too high, because the elite would lose a lot of economic power and political power as well, the political elite on behalf of V. Putin strengthened the authoritarian regime in order to insure the further reproduction of the same elite. As it is seen from this evidence the countries that are relatively rich are not necessarily the pioneers of democracy. For instance, Turkmenistan is relatively rich country among the FSU countries, but it is not only a pioneer of democracy, but also a very authoritarian one. However, the modernization hypothesis tries to find out a causal relationship between income level and democracy.

This inquire is important from Acemoglu's perspective, because it becomes pivotal in constructing his dynamic model of institutions. According to the modernization theory there is a positive causation between democracy and income level. Acemoglu et al. (2008) argue that, first, the causation whether democracy causes economic growth or vice versa is not clear. Second, it is possible that some other variables cause both of them. For exploring whether the association between democracy and income will disappear if a fixed effect like historical variable is introduced Acemoglu et al. (2008) do cross-country correlation while including the historical factor as well. As it is illustrated in the figure 2, when the fixed effects are not taken into consideration, it seems that the regression analysis renders this correlation between democracy and income level. As a measure of democracy the Freedom House democracy index is taken and as a measure for income the logarithm of GPD per capita in PPP terms is taken. The period of estimation is 1990s and the countries of estimation are from all the regions. However, this regression doesn't take into consideration the historical factors.

Figure 2: Democracy and Income, 1990s

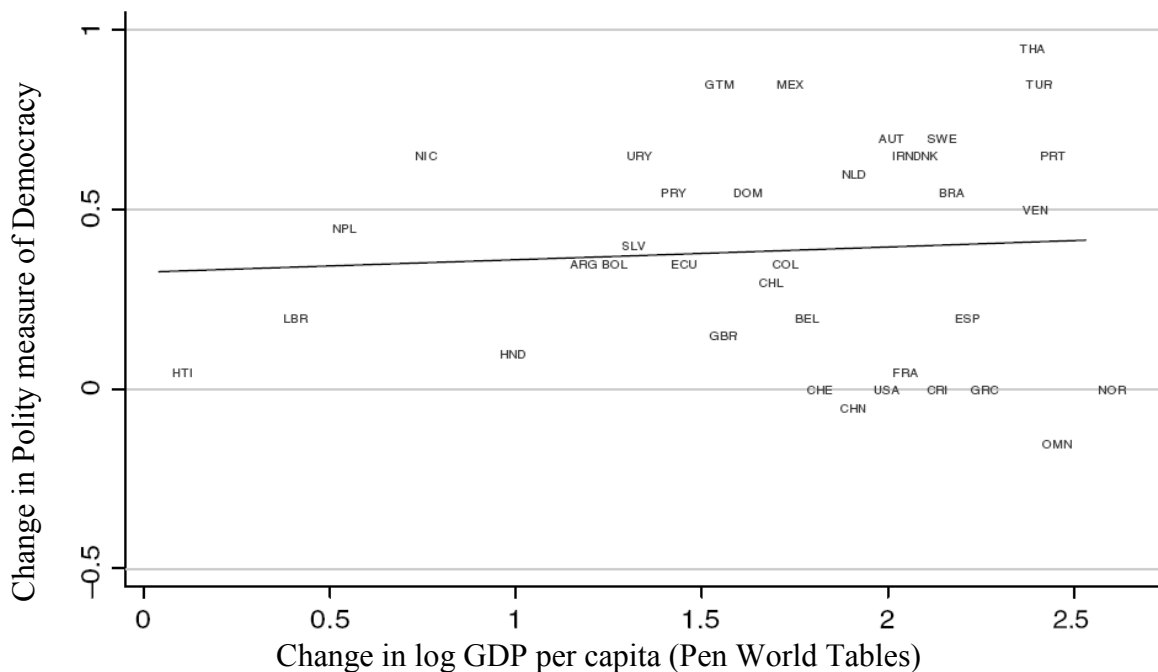


Notes: See Appendix Table A1 for data definitions and sources. Values are averaged by country from 1990 to 1999. GDP per capita is in PPP terms. The regression represented by the fitted line yields a coefficient of 0.181 (standard error 5 0.019), $N = 147$, and $R^2 = 0.35$. The “G” prefix corresponds to the average for groups of countries. G01 is AGO and MRT; G02 is NGA and TCD; G03 is KEN and KHM; G04 is DZA and LBN; G05 is BFA, NER, and YEM; G06 is GAB and MYS; G07 is DOM and SLV; G08 is BRA and VEN; G09 is BWA, DMA, POL, and VCT; G10 is HUN and URY; G11 is CRI and GRD; G12 is BLZ and LCA; G13 is KNA and TTO; G14 is GRC and MLT; G15 is BRB, CYP, ESP, and PRT; G16 is FIN, GBR, IRL, and NZL; G17 is AUS, AUT, BEL, CAN, DEU, DNK, FRA, ISL, ITA, NLD, NOR, and SWE; and G18 is CHE and USA.

Source: Acemoglu et al. (2008)

Thus, after doing the regression, while including historical factor, other results come around. It turns out that after introducing some fixed factors in the correlation, the association between democracy and income level becomes insignificant as it is illustrated in the figure 3.

Figure 3: Change in Democracy and Income, 1970–1995



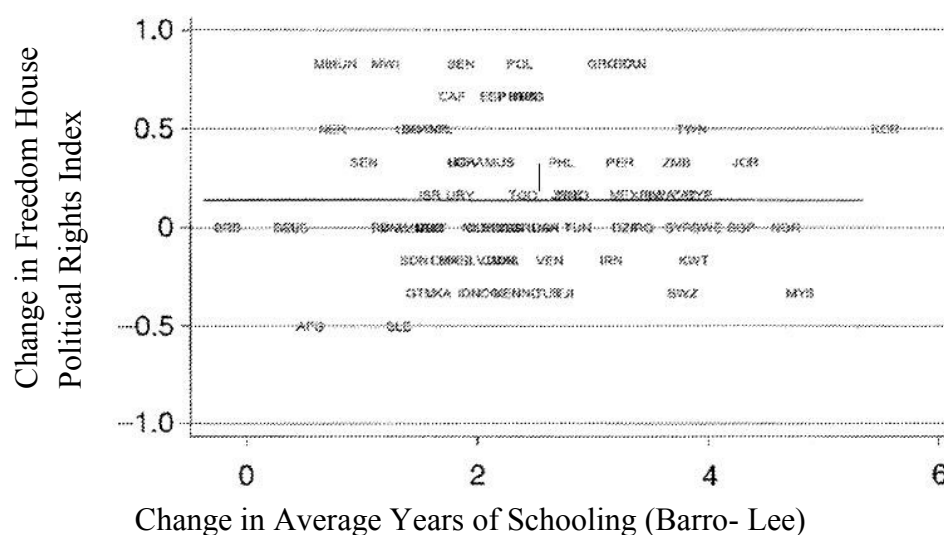
The regression represented by the fitted line yields a coefficient of -0.024 (standard error 5 0.063), $N = 98$, $R^2 = 0.00$. G01 is CHE, CRI, and NZL; G02 is AUS, DNK, and NLD; G03 is BEL, CAN, FIN, GBR, and TUR; G04 is AUT, COL, IND, ISL, ISR, ITA, and USA; G05 is IRL and SYR; G06 is KEN, MAR, and URY; G07 is BOL and MLI; G08 is MWI and PAN; G09 is GRC and LSO; and G10 is BRA and ESP.

Source: Acemoglu et al. (2008)

Hence, the paper (Acemoglu et al., 2009) jumps to the conclusion that there is no evidence of causal relationship between democracy and income level. Thus, developing these ideas, Acemoglu et al. (2009) calls for revaluation of modernization hypothesis putting emphasize on the factor that may determine both of them and that both democracy and income level are endogenous. Moreover, Acemoglu et al. (2005c) argue that education is not a source of democratization and it is not a precondition for as well as economic growth. Again, the modernization hypothesis, which is based on cross-sectional regression, doesn't take into consideration the fixed effect. Acemoglu et al. (2005c) do a cross-sectional regression while including fixed effects. The results render that the correlation is not robust

as it is illustrated in the figure 4. Thus, they again come up with the suggestion that there is something, a third factor, which determines both educational level and democratization.

Figure 4: Democracy Growth and Education growth, 1970-1995



Source: Acemoglu et al. (2005c)

This argument goes in line with the evidence brought from former Soviet Union countries. According to Frye (2006) the causality between democracy and economic growth is not salient in FSU countries. In order to find out how economic growth and democracy are connected he examines the democratic and economic developments of former Soviet Union from 1990 till 2002. Thus, according to evidence, the average level of economic growth in former Soviet Union countries from 1990 to 2002 was a negative 1.88 percent. However, much part of economic decline happened from 1992 to 1994. The growth rate was significantly negative 9.25 percent during this time. However, the trends changed from 1995 to 2002. The average annual growth rate was 3.5 during this period of time. For example, Estonia, Latvia and Lithuania had average annual growth rates after 1994 of 5.0, 4.9, and 4.1 percent, respectively. However, democracy in these countries doesn't vary in and the same respect as the economic growth does. The correlation between the Freedom House scores of political rights and annual rates of economic growth renders that there is no direct

relationship between democracy and income level in former Soviet Union. So, it seems that Acemoglu's perspective finds arguments in former Soviet Union countries.

THE DYNAMIC MODEL BY D. ACEMOGLU DISCUSSED FOR THE FSU REALITY

All this research done is somehow connected with the one of Acemoglu's fundamental works is his "Institutions as a fundamental cause of long-run growth" (Acemoglu, et al., 2005a), where they give a framework which generalizes all previously done research. Discussing different approaches and factors such as culture or geographical conditions and also taking into consideration the historical evidence why some countries are richer than the others, Acemoglu et al. (2005a) come up with his own framework. The framework comes up with some conclusions and predictions which may be observed in former Soviet Union countries. Thus, the framework can successfully be used for former Soviet Union countries as well. Hence, let's start discussing the framework and enhancing it by the evidence brought from Former Soviet Union countries.

In order to understand Acemoglu's point, it is important to take into account the main line of the argumentation that he makes in his different works. Discussing different reasons why some countries differ in their economic performance, he (Acemoglu et al., 2005a) renders that whatever reasons are presented they may be explained by other ones, that is, they are not exogenous, but endogenous. The main factor by which the difference may be explained is difference in institutions. He (Acemoglu et al., 2005a, p. 388) defines institutions as the "rules of the game in a society" or formally speaking they are humanly created forms that determine human interactions. The second argument that he uses to construct his

framework is the connection and interaction of political and economic institutions. Hence, taking into account above mentioned considerations, it may be said that his framework hinges on the following arguments.

1. Economic institutions determine economic growth, as they influence key economic actors in terms of investment and organization of the production. Moreover, the given economic institutions also determine the future distribution of resources. Presenting it schematically, this assumption will obtain this form.

$$\text{economic institutions}_t \Rightarrow \begin{cases} \text{economic performance}_t \\ \text{distribution of resources}_{t+1} \end{cases}$$

2. Economic institutions are not given once and forever and determined by the collective choice and decision of the society. Thus, there may be conflicting groups in the society for constructing this or that economic institution, as it determines the distribution of resources. In the case of the conflict groups and interests for establishing or maintaining this or that institution, the group which obtains political power will determine the nature of the economic institutions although sometimes it may also be determined by the efficiency. Schematically it may be presented as follows.

$$\text{political power}_t \Longrightarrow \text{economic institutions}_t$$

3. The naturally rising question why the group who obtains political power doesn't choose the most efficient way of economic institution and then distribute the outcomes according to their preferences. Why do inefficiencies and poverty exist? According to Acemoglu et al. (2005a) it is because of the commitment problems. That is the holders of political power cannot commit not to use their power for their best interest.

4. It is necessary to distinguish between two kinds of political power, de jure and de facto. De jure political power is represented and is begotten from the political institutions such as democracy and dictatorship and so on. Schematically it may be presented as follows.

political institutions_t ==> de jure political power_t

5. However, the political power is much larger than de jure political power determined by the political institutions. Some groups although not obtaining political power by constitution or by other formal means may organize revolutions and impose their wishes. This is de facto political power, which has two sources. The first source is the ability of solving collective action problem. Second, it is determined by the economic resources obtained by this or that group. Hence:

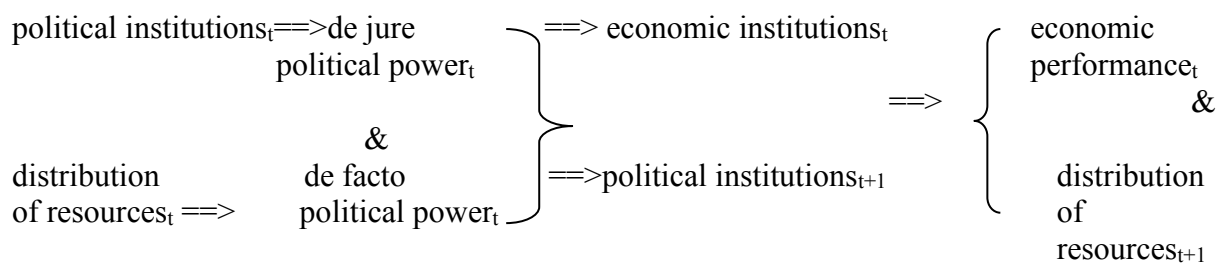
distribution of resources_t ==> de facto political power_t

6. Thus, the distribution of the resources and political power are the state variables in this dynamic system, as they change relatively slowly and they determine institutions and performance. However, the political institutions are endogenous as well. The ones who hold political power will certainly try to maintain it, but de facto political power makes the given institutions be changed. Hence:

political power_t ==> political institutions_{t+1}

As the summarization of all above discussed the following scheme may be drawn.

Figure 5: The dynamic model by Acemoglu et al. (2005a)



If the two variables, political institutions and distribution of resources, are known, then all the other variables will be determined by them. Political institutions and distribution of resources determine economic institutions in the time point t and the political institutions

in the point of $t+1$. Economic performance in the point of t and the distribution of resources for the point of $t+1$ are determined through the economic institutions. However, there are two sources of persistence of the system. First, as the political institutions are pretty durable, a huge change of distribution of resources should happen in order to have changes political institutions. Secondly, if a certain group obtains a large part of the resources, that particular group will obtain much political power and thus being enabled to create political and economic institutions favourable for them. However, the model also accepts the possibility of the change, which may occur via technological changes or some external shocks. These shocks may change the whole chain of the political and economic institutions, changing the balance of (de facto) political power (2005a).

If considering this model in the FSU reality, then it may be said that this framework is pretty much consistent with the evidence from Russian post-Soviet history. According to Robinson (2000), because of forced institutional settlement in 1993, El'tsin was able to use his political power arbitrary and made anti-democratic changes. Thus, he changed political institutions at the point t so changing de jure political power at the point t . After the collapse of Soviet Union, privatization processes took place. During those privatization processes some groups or people were able to obtain main part of Russian economic resources because of inability of the state to create market economy. This created oligarchic structure of Russian economy. Hence, the distribution of resources was pretty unequal. That group of people determined the nature of de facto political power, because they were able lobby, to use their financial resources on the sake of their interests, what they actually did during the presidential elections in 1996. They used some of their resources in order to insure El'tsin's reelection. Thus, after examining the evidence from Russian experience it becomes obvious that distribution of resources decides de facto political power. After El'tsin's reelection, economic institutions were established or were maintained the way that the oligarchs really

benefited them. Of course, the elite also tried to make political institutions which will ensure their further reproduction. As a result, there was created authoritarian regime, which was the best way to ensure the reproduction of the elite in Russia. These developments determined economic performance of Russia, because when there were conflicts between market development and elite's economic interests, the elite took decisions that would empower themselves even if those decisions contradicted economic development. Hence, given that the economic institutions didn't provide market solutions, according to the framework the distribution of resources for the point of $t+1$ is determined. According to the predictions of Acemoglu's et al. (2005a) framework the distribution of resources will continue to be unequal because of given non-market structure. This is the case for Russia, where distribution of resources still continued to be quite unequal till the research Robinson (2000) was done. So, the framework fits quite well in explaining the Former Soviet Union reality.

Another issue, which is discussed by Acemoglu et al. (2005a) and which is also relevant for former Soviet Union countries is the cause of inefficient economic institutions. So, coming to the question why inefficiencies exist in the economic institutions Acemoglu et al. (2005a) distinguishes a several reason. The first reason he names hold-up. This is the situation when a group of people holds unlimited political power. Thus, as they have obtained unlimited political power, they cannot commit not to use that unlimited power on their sake. So, they aren't able to provide efficient economic institutions such as secured property rights and so on. As a consequence, productive investments are made and the economy suffers. The second source of the inefficient economic institutions is the problem of political losers. The ones, who obtain political power, may have rents, gain income by using their political power. Thus, they are reluctant to lose their political power and the change in economic institutions that may somehow affect their political power is not likely to happen. Thus, the political elite may be reluctant even if the change of economic institutions may bring to economic growth.

At the first sight, it seems that political elite should prefer the economic institutions that provide economic growth, because it will provide more returns for them in terms of taxes and assets. Nonetheless, they won't accept the economic institutions that provide economic growth if it also enriches their enemies, as after some point on they may become quite rich and threaten the elite's political power.

THE ROLE OF INSENTIVES FOR THE POLITICAL AND ECONOMIC CHANGE

After constructing this model, Acemoglu & Robinson (2006a) don't come to the conclusion that changes in political institutions and thus de jure political power may not necessarily change the distribution of de facto political power. Thus, they construct a model which renders this. Verbal explanation of this model may be the assumption that even if the elite which have monopolized de jure political power loses it, it may still maintain de facto political power by increasing the intensity of their collective action. They may use brute force, do bribing etc. and ensure the existence of the previous set of economic institutions. So, the model represents that change in one dimension of political institutions such as the shift from non-democracy to democracy may be not sufficient for changes in economic institutions, because multiple dimension changes are needed. So they (Acemoglu & Robinson, 2006a) argue that persistence of economic institutions happens not because of persistence of political institutions but because of the persistence of the incentives whoever holds the power. The economic institutions are always able to persist even after changes in political institutions, because the incentives of the elite haven't been changed and it still uses the power on the sake of them.

Developing this model they (Acemoglu & Robinson, 2006b) try to explain the reasons of economic backwardness in political perspective. They argue that if everything else equal, the political elite will adopt changes in economic institutions and new technologies, because these will increase the overall output and they will benefit because of more output and additional revenues. However, it is not always the case that political elite prefer changes in economic institutions. The reason is that such change may challenge their political power by enriching other groups and making them powerful enough to fight against the elite. So, there is a trade off to adopt or not to adopt changes, and the elite will prefer not adoption in some cases. The situation is pretty different when there is a political competition. The elite are innovating because there are high chances that they will be replaced. The elite also innovate when it is highly entrenched, because it wouldn't lose its power, anyway. After constructing a model and discussing the outcomes possible Acemoglu & Robinson (2006b) show that adopting the changes is more possible when the elite is either competitive or highly entrenched. In the case, when political competition is limited the elite block the change. The elite are also more likely to block the change when the stakes are higher, that is it enjoys high rents, and the external threats are absent. If the external threats are high the elite is enforced to innovate, because being technologically weak a state becomes pretty vulnerable to be invaded.

THE HISTORICAL OVERVIEW OF ECONOMIC DEVELOPMENT PATHS OF THE FSU COUNTRIES (SHOCK THERAPY VESUS GRADUALISM)

After the collapse of the Soviet Union, new policies and new development path were to be obtained not only in political sphere, but also in economic sphere. Definitely, the

existing command economic system wasn't relevant any more. The transitional process took a lot of debates and it was controversial (Roland, 2001). For instance, it was not clear whether the transition should be implemented rapidly or slowly, how the privatization should take place, what the role of the government is in these processes and so. In economic terms, transition brought some unexpected or not-well defined results. The main results were the huge output fall because of price liberalization, intensive privatization, the emergence of Mafia and oligarchic economic structure instead of market economy. Hence, there were two different economic development paths and two different visions of economic development that the FSU countries should follow. The first view is "Washington consensus" or shock therapy or big bang, while the second may be called "evolutionary-institutionalist" perspective or gradualism. The principal difference between these two visions is the different attitude towards the uncertainty which will emerge because of reforms. According to Washington Consensus perspective, the results of the reforms are surely positive and that it will increase the efficiency of the economy. As opposite to this perspective, the evolutionary-institutionalism perspective emphasizes the uncertainty of the outcomes of the reforms. Thus, the success of the reforms are not necessary beneficial. Hence, the two visions differ in terms how fast the reforms should be implemented and whether they should be reversible or not. According to Washington consensus view the reforms should be undertaken as fast as possible and they should be irreversible. This strategy may be very dangerous from the evolutionary-institutionalism perspective, as it may beget unexpected economic results and because of the irreversibility of the process the given economy may enter an inefficient economic phase. This perspective offers a continuous need and assistance among the society instead of one pot decisions. The Washington Consensus, in its turn, argues that partial reforms may create potential possibilities for rent for some groups, which may oppose the further reforms after then, while the complete and comprehensive reforms don't let such

groups emerge. The issue of what kind of institutions should be introduced finds different answers from different perspectives. If the Washington Consensus emphasized the need of introducing the “best practice” institutions, the second perspective tries to highlight the necessity of flexibility of institutions and it emphasizes the gradual institutional evolvement depending on different political and social conditions. If the first doesn’t take into consideration the need of creation appropriate institutions and only emphasizes the introduction of laws which will secure property rights before the implementation of reforms, then the second argues that lack of appropriate institutions or lack of law enforcement mechanism before reform implementation may beget undesirable and unexpected results. Thus, the first hopes that it is quite possible to get rid of old institutions which are not effective and start introducing reforms with a “clean slate”, while the latter perspective has a great skepticism towards introducing the “best practice” institutions and towards the successful import of institutions. Then, the perspectives also differ upon the issues who should support and become the guarantee of the implementation of the reforms. If the first perspective finds that the supports of the reforms should be the owners of private organization and they should try to persuade the voters, in contrast the second perspectives highlights the need of larger group interest and support for obtaining the reforms. So, it puts emphasis on the middle class. The attitude is different towards the ownership of inefficient state-owned enterprises as well. If the former considers that all state-owned enterprises should be privatized and the non-profitable enterprises should be closed down as soon as possible, then the latter offers gradual downsizing and creating new private sector which will be able to attract workers from public sphere and thus automatically making them closed down. If the former doesn’t accept government intervention in markets at all and calls for “de-politicized” market economy, the latter finds the role of government important for ensuring rules of the market economy and competition, enforcing law and protected security

rights and preventing monopolization. The perspectives also differ in the question of government size. If the former calls for shrinking the size of government, the latter speaks about the change of incentives of government officials in order not to be captured by some interest groups or entrepreneurs with monopolistic intentions (Roland, 2001).

However, these two visions are not dramatically opposing visions, because they both try to introduce market economy. And what the difference is in these two visions is the methods and the policies that this or that country should obtain in order to introduce market economy (Roland, 2001). Hence, the introduction of market economy regardless whether a certain country adopted a shock therapy policy or gradualism, some recession in economy happened in the FSU sooner or later. The recession started in most cases in 1990. It started in 1991 in some FSU countries which were Latvia, Kyrgyzstan, Turkmenistan and Uzbekistan. Some of them, Armenia, Belarus, Estonia, Georgia, Latvia, Lithuania, and Uzbekistan exercised in 1993–1995. Moldova and Ukraine were the last countries where the recession occurred in 1996–1999. Thus, this recession period lasted from 3 to 10 years (Popov, 2007).

Shock therapy

Neither shock therapy, which is the practical implication of Washington consensus, nor gradualism which is practical implication of evolutionary-institutionalist is absolutely successful or failure. Some countries have experienced successful shock therapy; some countries have successfully implemented gradualism policy and there are failure stories in both cases as well. Some Central European countries can be considered as the illustration of successful implementation of shock therapy, and Russia may be considered as the failed story of implementation of shock therapy (Roland, 2001). Thus, let's consider each case separately in more details. The policy implementation of shock therapy started by the following actions

in Poland: “Fiscal and monetary stickiness, a convertible currency, deregulation of prices, demonopolization of the state, the removal of all barriers to international trade, full liberalization of the private sector, the creation of new rules for the regulation of state enterprises, tax reform, institution of unemployment insurance and job retaining schemes, credit allocation to individuals to start small businesses, and privatization. There were also some legislative changes (Murrell, 1993, p.114).” As it becomes obvious, shock therapy is a revolutionary policy which requires changes not only in economic field, but also more fundamental societal changes. The shock therapy started in Poland in 1990. The fiscal policy was tightened, thus producing significant budget surplus. Trade limitations were almost completely abolished. And then massive privatization took place. As a result almost 30 percent drop occurred in industrial production. However, the shock therapy in Poland was implemented by using the existing economic institutions. Thus, the shock therapy was implemented by the political and social structures that had emerged during the communist era and the existing society was using a new policy rather than a new society was being created via new policy. However, the shock therapy begot some unpredictable results, because of which some of the initially planned steps were withdrawn. The most important modifications that happened as compared to initially planned ones were the loosening of fiscal and monetary policies (Murrell, 1993).

However, Russia was also among those that exercised shock therapy. Exercising a lot of economic problems, Russian President B. Yel'tsin announced about his intention of implementing shock therapy in 1991. The real economic reforms began in January 1992. As a result the following steps were undertaken; liberalizing the price system and imports, a complete change of tax system, tightened monetary policy, an ambitious privatization program, preparation for ruble convertibility with other currencies and negotiation with of the trading issues with other former Soviet Union countries. However, as in the case of Poland,

some unpredictable side effects appeared that made the Russian government take some steps. Firstly, the government started to control prices and to use central directives on production. Secondly, the weakened distinction between cash and non-cash money became stricken again in March 1992. Thirdly, because of the threat of bankruptcy, the government had to make a huge amount of money as credit for the enterprises (Murrell, 1993). However, the Russian shock therapy didn't success because the factor of uncertainties wasn't taken into consideration. As the shock therapy wasn't reversible, after finding out that there were a lot of windows of opportunities that can be used by some interest groups. This was the case in Russia. An irreversible reform, mass privatization, happened in Russia. Because the privatization was relatively irreversible, Russia became locked in an ineffective economic situation. The interest groups, who were able to benefit from this mass privatization (oligarchs), have become so powerful and started blocking the further reforms such as tax reform, government reform, stronger law enforcement and security of property rights. As a result, a huge part of Russian population suffered from this transition, because there was a huge concentration of wealth and the privatization process was considered as illegitimate and corrupts (Roland, 2001).

Gradualism

Some FSU countries chose different path of economic policy than that of Russia. They preferred gradualism, but again some of them were successful in implementing this policy and some of them were not. One of the most successful stories was Uzbekistan. This country adopted gradualist approach for implementing market-oriented reforms. And though the political system was an authoritarian even after the collapse of the Soviet Union, the success of the economic reforms was obvious. As an illustration for the successfully implemented gradual reform the evidence from Uzbekistan may be rendered. Uzbekistan

exercised the slowest fall of gross domestic product rate among all post-Soviet countries (only 18 percent in 1990-1995). The other illustrations were the preservation of industrial output almost at the same level and at the same time the intervention of significant foreign investments. Nevertheless, there is a factor which should be defiantly taken into account before judging whether or not the gradual reforms were successful. This is the fact that Uzbekistan is very rich in natural resources, such as gold, oil, cotton and wheat, which are some fundamental determinants of a country's economic growth. This factor let us think that the economic performance is not because of successful gradual reform, but because of these important resources or at least let us consider the existence of these resources as highly supplementary means for successful economic performance (Papova, 2005).

Another country which exercised gradualist policy was Turkmenistan. However, its implementation was not so successful as in the case of Uzbekistan. Turkmenistan's gradualism brought to significantly different economic outcomes (Pomfret, 2004). It was the least-reforming country among all FSU countries (Pomfret, 2010). However it didn't have positive rates of GDP growth rates from 1990 to 1997. It had 5 percent of GDP growth, a positive GDP growth rate starting only from 1998. It also had quite high inflation rates till 1997 when it dramatically the inflation rate considerably dropped till 84 percent. However, despite the economic decline and increased poverty, Turkmenistan was able to compensate the negative consequences due to energy revenues. However, it is possible to note that the failed economy may be not due to reforming policy held there, but due to some political-economic factor as centralized ruling system, monopolization of the market, great impact and control of the market by the state and so on. Turkmenistan benefited a lot from the natural gas and cotton prices, but because of the personalized political system the revenues were used for the political elite rather than for public good. However, Turkmenistan started economic recovery and rapid growth after 1998 due to high oil prices.

Hence, having all these discussed and understanding the context and overall environment of the FSU countries, it is important to conduct a regression analysis which will estimate the correlation among the main politico-economic variables in the FSU. It is helpful to discuss how the economic growth in terms of GDP, democracy in terms of Freedom House democracy index and inequality in terms of Gini coefficient are correlated. These findings give some useful insights being combined with the discussions made above, can reveal quite important information about the FSU reality for the further discussion. So, let's discuss the findings.

FINDINGS

The findings are mainly connected with the regression analysis. The dependent variable is GDP adjusted by PPP in real terms

GDP_NORM = 6.03 - 21.08*GINI + 1.536*DEMO, where:

Higher democracy corresponds to lower values of DEMO

Higher equality corresponds to lower values of GINI

Table 1: The Results of Regression Analysis

Covariance correlation			
Correlation	GDP_NORM	DEMO	GINI
GDP_NORM	15.01976		
	1.000000		
DEMO	1.078407	0.520956	
	0.385523	1.000000	
GINI	-0.019136	-0.014194	0.003379
	-0.084940	-0.338287	1.000000

The standard errors are significant:

P-value (GINI) = 0.06

P-value (DEMO) = 0.03

The table 1 illustrates three statistically significant correlations. According to the findings, democracy and GDP are negatively correlated. The more democracy rises, the less GDP grows. On the other hand, Gini coefficient rates and GDP are positively correlated. That is, the more inequality decreases, the more GDP grows. However, democracy and inequality are positively correlated. That is, the more democracy increases, the more inequality increases as well. These findings have to be analyzed in order find out the overall FSU environment and reality at least for the period of 2001 till 2009.

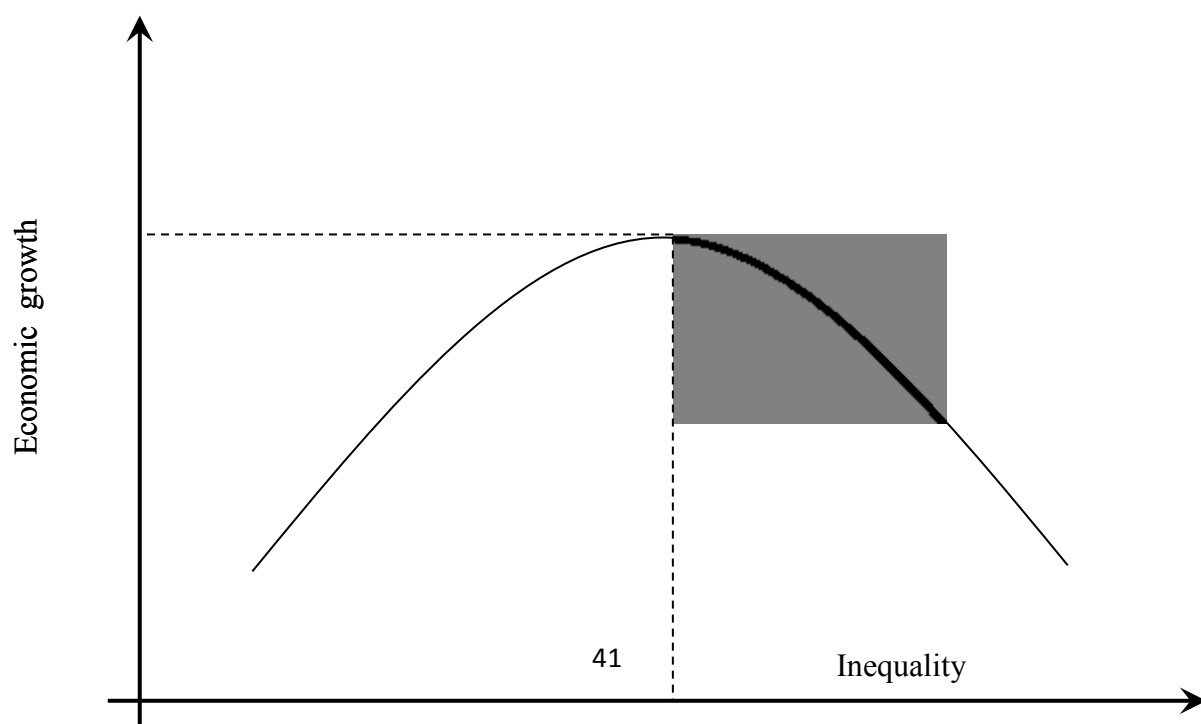
ANALYSIS

The first finding which renders that democracy and GDP growth are negatively correlated let us make some judgments. First, it comes out that the modernization hypothesis isn't supported for the FSU countries. So, the hope that the economic growth will necessarily bring to democratization doesn't justified for the FSU countries. Neither does the increasing educational level bring to democratization. It is also the case for the FSU countries, because historically these countries have had high literacy rates due to the mandatory and free education in the Soviet Union. However, very few of these countries are democratic or tend to democratization. Moreover, the decreasing in democracy causes high GDP. These results, however, don't contradict the model introduced by Acemoglu et al. (2005a). It is possible that the obtainers of non-democratic political power have constructed such economic and political institutions where good economic performance is beneficial for them. In other words, it is possible that given the political and economic power and distribution of resources the elite in these countries benefit quite much from higher GDP, as they increase their wealth and insure

the further reproduction. However, the expectations that these elite will continue to insure economic growth on their own sake are not justified as well. The elite will insure economic growth unless it challenges their both political and economic power. If the economic growth may somehow challenge the elite position the economic growth will be stopped or at least slowed down. Thus, the future of these countries in terms of less democratization and economic growth is not salient. However, one of the most important factors in this relationship is how the benefits of the economic growth will be distributed.

In this context it is important discuss the correlation of inequality and GDP in FSU countries. It turns out that lowering inequality is a determinant for GDP growth. These results are important from the Kuznets curve perspective. Hence, it is obvious that these six countries have passed the phase when inequality rise fosters economic growth. As it is illustrated in the figure 5, the six FSU countries have enter the phase where any further increase in inequality, in this case Gini coefficient rise, will bring to inefficient results from economic growth perspective in this case lowering GDP. Hence, it becomes obvious that in order to have higher GDP, the inequality should be decreased.

Figure 5: The Line of the FSU Countries in Kuznets curve



If discussing these results from Acemoglu et al. (2005a) model perspective, it becomes obvious that the given economic institutions are not efficient any more as they, while being the determinants of economic performance (measured by GDP) and distribution of resources (measured by Gini coefficient), don't provide efficient economic performance in terms of GDP growth. Thus, the given economic institutions are stagnated any more.

On the other hand, some interesting results are revealed by the regression analysis according to which while having decrease in democracy (higher Freedom House index) these countries have had lower inequality (decrease in Gini coefficient). However, these results represent only linear correlation and they should be discussed in the dynamic model. How contradictory it wouldn't sound, the further decrease in inequality, however, will bring to democratization. It would happen whether via revolutionary scenario or an evolutionary one depending on the speed of decrease in inequality, the solution of the collective action problem, and commitment problems and so on. Thus, let's discuss each possible scenario separately.

First, if the inequality level in the FSU countries doesn't decrease quite rapidly, it is obvious that this will impede economic growth as it is motivated via Kuznets curve and regression analysis. In this case, the threat of revolution becomes obviously high. However, it is very important how the collective action problem in terms of civil society mobilization in these countries will be solved. If the civil society may become so mobilized that the threat of losing the power for elite becomes salient, then they will necessarily make changes in order to escape this type of developments. Moreover, the changes won't only mean one-day changes but they will necessarily concern to all institutions. It will be the case, because as it is discussed in the figure 4, in order to change economic performance and have changes for the distribution of resources for the next stage a whole chain of changes is necessary. Hence,

the economic institutions should be changed as well. But in order to have changes in economic institutions political institutions both de facto and de jure should be changed either. As soon as these processes start they will inevitably continue providing further and further democratization like the snow-ball effect. Thus, the democratization processes will become inevitable with more or less equally distributed resources with the emergence of “middle class” with its more or less homogeneous interests. And as it is motivated in Acemoglu et al. (2006b) democracy will be the best option for the public and they would prefer it. It will be the case, because given new de facto and de jure political institutions and distribution of resources will determine the whole chain again and will require further and further change in it. However, it depends quite much on whether the collective action problem will be successfully solved or not and how costly it will be for the elite to ensure changes.

Thus, the next possible scenario for these countries may be revolutionary one. Again, it mainly depends on how costly the process of transition for the elite will be and mobilization problem either. In any case the elite in these countries should try to lower inequality otherwise it wouldn't have economic growth and wouldn't be able to carry out some social programmes which would make the threat of social unrest much higher. On the other hand, it should provide economic growth in order to have revenues itself. Nevertheless, if the speed of decrease in inequality is low and the collective action problem is more or less solved, the civil society will become a real challenge for the existing elite. However, if the cost of revolution is lower for the incumbent elite, than the cost of changes, then the solution will be a revolution with its unpredictable results from democratization perspective. The cost of changes in this case for the elite is the loss in political power and distribution of resources and consequently economic power and so on which the elite in these states will have. The cost of revolution is the possibility of the success of the revolution that is, the elite change. Nevertheless, the democratization in the case of revolution is only one option. It is not the

cases that after the revolution the democratization in these states will necessary happen, as the political institutions are persistent and are relatively slow-changeable.

Thus, combining the results of regression and the predictions given from the model the following analysis can be made. First, it turns out that GDP may grow while the democracy may stay in the same level or decrease. On the other hand, in order to insure GDP growth inequality should be diminished. So, for a static point of view it is possible to have low democracy while having GDP growth and inequality decrease. This situation, however, won't be consistent from the dynamic point of view. No matter how GDP growth and inequality decrease are slow processes in these countries, the quantitative changes in them will bring to a qualitatively new political situation either through evolutionary or revolutionary means regardless of the elite's initial intentions. Defiantly, the role of persistence towards political changes and especially changes in political institutions from elite side is pivotal, but it can't last long, because some economic and social policies should be carried out anyway. And each policy, in its turn, will have some feedback. Non-democratic trends may be consistent and ensure the elite reproduction unless they are inefficient from GDP growth and inequality decrease perspective. Speaking from both modernization hypothesis and Kuznets curve and dynamic model perspective, non-democratic political institutions will be efficient for both the elite and the public efficiency perspective until some point. As it is the case for the economic growth and inequality as it described in Kuznets curve, starting from some point on further GDP growth will require democracy. It is possible to speak about that the modernization hypothesis may be modified and viewed as a relationship where income or GDP growth doesn't cause democratic developments till some point after which in order to provide higher economic growth the democratization becomes vital. The relationship between democracy and inequality may be viewed in the same context as well. It may be argued that from some point on the low

democracy can't provide decrease in inequality and in order to have more equality, the democratization processes will happen. And lastly, speaking about the Acemoglu's et al. (2005a) terms starting from some point on the given political and economic changes will become inefficient and changes in the chain will happen which will cause other changes in the chain as well. The six FSU countries are still in the phase, where less democracy provides less inequality and high GDP growth. But it won't be the case for always. Hence, the changes will be ahead. And if the elite will persist the changes and provide inefficient institutions it may happen through revolution, if not through evolution. But the democratization processes in these countries will become inevitable anyway. Hence, some conclusions may be done in the context of these analyses.

CONCLUSION

The FSU countries entered the phase of transition after the collapse of the SU. Some of them have successfully overcome this period and some of them haven't yet. Interestingly enough, while entering the period of transition all countries had the same intension of creating democratic political institutions and liberal market. However, not all the countries succeeded. Some of them like in the case of Baltic States were relatively successful, while some became authoritarian like Turkmenistan and so on. All FSU countries implemented some economic reforms as well. Some of them chose the radical form of economic transformation named shock therapy or Washington consensus, and some of them prefer evolutionary or gradual path of economic reform called gradualism. And again, some of them were relatively successful in these processes, and some weren't no matter which path of economic development they have obtained. However, although the differences of the economic and political directions some of the FSU countries had really similar both political

and economic problems. Many of them exercised socio-economic tensions like poverty, high inflation rates, unemployment, and negative economic growth and so on. Moreover, they exercised quite strong political tensions as well up until revolutions in some cases.

Hence, this research sheds lights how the socio-economic and political developments are connected using some models for exploration. The hypothesis of the research which tries to find out whether there dynamic model by Acemoglu et al. (2005a) may be an appropriate framework for FSU reality, is supported as three statically significant correlation is revealed. The first correlation is the democracy (political institutions) and GDP (economic performance). This correlation supports the assumption of causal relationship of the model by Acemoglu et al. (2005a) according to which political institutions determine political power which determines economic institutions which, in their turn, determines economic performance. The second is the correlation between inequality (distribution of resources) and GDP (economic performance). This correlation supports the assumption of the model that the distribution of resources determines political institutions and these determine economic institutions and performance. After finding out that the given framework is relevant for the FSU reality, the results of the regression are discussed in this framework and other frameworks as well.

It turns out that given the model and the regression analyses results, decrease in inequality may lead to democratization either through revolutionary or evolutionary processes. Moreover, the emergence of revolution in the FSU countries has been evidenced in two countries, Ukraine and Georgia. However, it is not always the case that revolutions will necessary bring to democratization. On the other hand, there is an evolutionary possibility of developments towards democratization.

Nevertheless, the change of political institutions, that is, the democratization processes of elite without pressure from the public side is also a possibility. It will be interesting to explore how democratization processes implemented by a benevolent planer may affect inequality and economic performance for a dynamic model. However, it is beyond of scope of this research.

Moreover, this research has some limitations, which are the short period of panel estimation. Because of short period of estimation from 2001 to 2008, the dynamic of changes is somewhat incomplete and the findings are not based on all the period of the existence of the FSU countries. The second limitation is the sample size. It only includes six FSU countries Armenia, Belarus, Russia, Ukraine, Moldova, and Kirgizstan, while the FSU states are fifteen. Nevertheless, the results are quite important for Armenia as Armenia is included in the sample. Thus, these findings and analyses let us make some recommendations and policy implications for Armenia.

RECOMMENDATIONS

The most important recommendations are connected with decrease in inequality, as this decrease will determine the further processes of democratization as it is discussed in the part of analysis of this research. Moreover, the importance of decrease in inequality becomes pivotal as it will foster economic growth as it is discussed in the context of Kuznets curve. Thus, the government should follow the commitment of consistently decreasing in inequality by using both the assistance of both International organizations and internal resources and means. Hence, the government of Republic of Armenia should cooperate with IMF and other

international organizations that are intended to reduce poverty rates. As internal means of poverty reduction, the government of Republic of Armenia should implement social policies and provide privileged attitude directed towards socially vulnerable groups such as peasants, small and middle businessmen, while strict attitude towards large businesses.

Although the lowered inequality provides better economic performance, however, the Armenian government should follow the commitment of making changes in the economic institutions in the manner that it will consistently provide economic growth and better economic performance.

The most important recommendation, however, is the one directed to Armenian emerging civil society and public and every citizen. They should raise their awareness and be proactive both in political processes and social issues. In other words, Armenian society should become the obtainer of de jure political power that is, the power which is prescribed to the public by the Constitution of Republic of Armenia and other legal means. This is the most effective tool for changes as it has already been discussed.

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