

## The Transition from Communism



KENT STATE  
UNIVERSITY

Lectures in Macroeconomics- Charles W. Upton

1989

- Berlin Wall falls in November 1989.
- By Christmas Poland, East Germany, Hungary, Czechoslovakia, Rumania, Bulgaria, and Albania have eliminated Communist Governments.

KENT STATE  
UNIVERSITY

The Transition from  
Communism

1990

- German Unification, October 1990.

KENT STATE  
UNIVERSITY

The Transition from  
Communism

1991

- Soviet Union ends Christmas Day, 1991.

KENT STATE  
UNIVERSITY

The Transition from  
Communism

### The Puzzle

$$Y_t = A_t K_t^\alpha L_t^{1-\alpha}$$

KENT STATE  
UNIVERSITY

The Transition from  
Communism

### The Puzzle

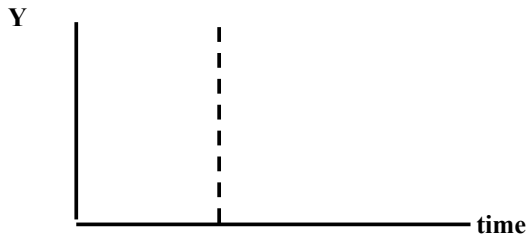
$$Y_t = A_t K_t^\alpha L_t^{1-\alpha}$$

$A_{\text{Marxist Economies}} < A_{\text{Market Economies}}$

KENT STATE  
UNIVERSITY

The Transition from  
Communism

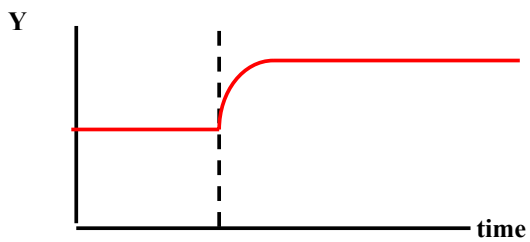
## The Expected Pattern



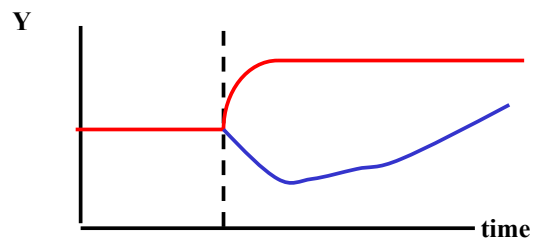
## The Expected Pattern



## The Expected Pattern



## The Actual Pattern



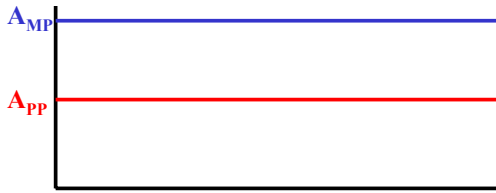
## Issues

- Transition Problems
- Legal Systems
- Safety Net

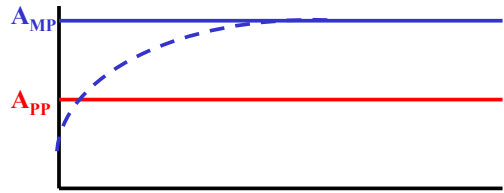
## The People's Pizzeria

- The Peoples Pizzeria to be privatized.
- Shares are transferred to someone
  - Cannot exercise managerial control
  - Whole organization is incompetent and collapses in the light of privatization

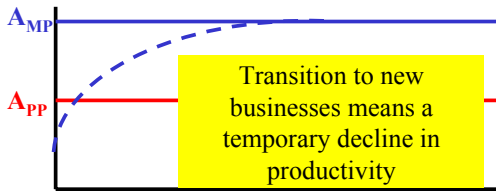
## The People's Pizzeria



## The People's Pizzeria



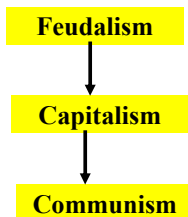
## The People's Pizzeria



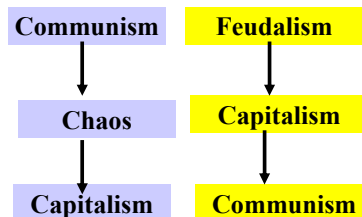
## Managing Miller's Pizzeria

- Limited knowledge of how one works in a market economy
  - Showing up on time
- Limited legal system
  - Cannot enforce contracts
- High level of Corruption

## The Stages of Transition



## The Stages of Transition



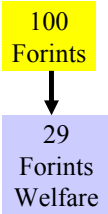
# The Social Welfare System

- Hungary
  - 40% income tax
  - 40% social security tax
  - 24% VAT

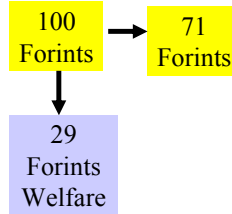
# Effective Taxes

100 Forints

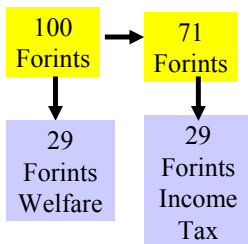
# Effective Taxes



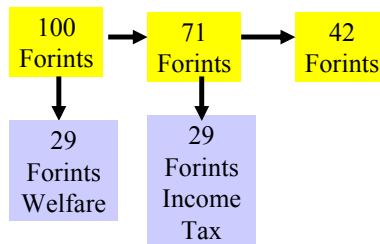
# Effective Taxes



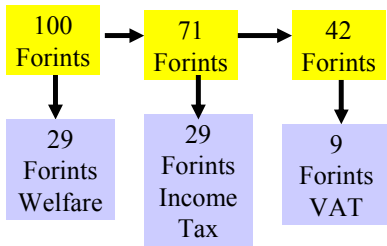
# Effective Taxes



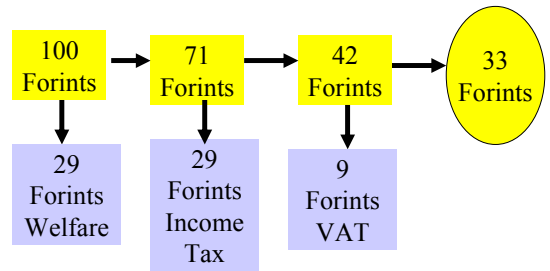
# Effective Taxes



## Effective Taxes



## Effective Taxes



## The Response

- Cheat
  - Work for yourself
  - Deduct everything
- Don't Work Hard
- Corruption

End

©2003 Charles W. Upton.  
All rights reserved